Q4FY12 Result Update

May 10, 2012

GIL recently reported its Q4FY12 results, which were below street estimates. Given below are some of the key highlights, which we came across while reviewing the results.

Key highlights of Q4FY12 results:

During Q4FY12, GIL's revenue rose by 12.6% y-o-y to Rs.7,206 cr. Operating Profit declined by 2.8% on account of higher costs. Net profit for the quarter fell by 8% y-o-y to Rs.808.8 cr in Q4FY12, on the back of higher cost and higher tax outflow, despite higher other income.

Quarterly Financials - Consolidated:

(Rs. in Cr)

Particulars	Q3FY12	Q3FY11	% Chg	Q2FY12	% Chg	Remarks
Net Sales	7205.8	6397.7	12.6%	6261.0	15.1%	Higher cement and chemical volumes led to higher sales on a y-o-y basis
Other operating income	83.4	84.5	-1.4%	30.6	172.4%	
Total Operating Income	7289.2	6482.3	12.4%	6291.6	15.9%	
Expenditure						
Decrease/(Increase) in stock in trade and work-in-progress	174.7	47.6	266.8%	-83.2	-310.0%	
Raw Materials	1410.6	1325.9	6.4%	1379.8	2.2%	
Purchase of Finished Goods	72.5	49.8	45.6%	67.2	8.0%	
Employees Cost	368.6	327.9	12.4%	361.7	1.9%	
Power & Fuel	1505.7	1214.6	24.0%	1413.6	6.5%	
Freight, Handling & Other Expenses	1136.7	1045.1	8.8%	977.6	16.3%	
Other Expenditure	1010.8	815.1	24.0%	850.9	18.8%	
Total Opex	5679.7	4826.0	17.7%	4967.5	14.3%	
Operating Profit	**1609.5**	**1656.2**	-2.8%	**1324.2**	21.5%	
OPM %	*22.3%*	*25.9%*		*21.1%*		Margins expanded y-o-y on account of improved realisations
Other Income	273.4	123.5	121.5%	230.1	18.8%	
Interest Expenses	79.9	109.1	-26.7%	50.1	59.6%	
Depreciation	300.5	299.3	0.4%	288.7	4.1%	
Profit before tax	1502.5	1371.3	9.6%	1215.4	23.6%	
PBTM %	*20.9%*	*21.4%*		*19.4%*		
Tax	380.7	223.3	70.5%	330.2	15.3%	
Effective Tax Rate %	*25.3%*	*16.3%*		*27.2%*		
PAT	1121.9	1148.1	-2.3%	885.2	26.7%	
Minority Interest	347.6	281.6	23.4%	234.8	48.0%	
Share in Profit/(Loss) of Associates	34.5	12.4	177.9%	18.6	85.0%	
Net Profit	**808.8**	**878.8**	-8.0%	**669.1**	20.9%	Lower interest cost, depreciation expenses and tax rate helped in Net Profit growing faster than Operating Profit. Also other income, which doubled aided in this jump.
NPM %	*11.2%*	*13.7%*		*10.7%*		
Equity Capital	91.7	91.7	0.0%	91.7	0.0%	
EPS	**88.2**	**95.8**	-8.0%	**72.9**	20.9%	

(Source: Company, HDFC Sec)

Quarterly Financials:

Standalone

(Rs. in Cr)

Particulars	Q4FY12	Q4FY11	% Chg	Q3FY12	% Chg
Net Sales	1388.5	1425.6	-2.6%	1242.9	11.7%
Other operating income	23.8	32.8	-27.6%	23.4	1.5%
Total Operating Income	1412.2	1458.4	-3.2%	1266.3	11.5%
Expenditure					
Decrease/(Increase) in stock in trade and work-in-progress	120.0	29.5	306.5%	-57.6	-308.6%
Raw Materials	629.8	593.1	6.2%	651.3	-3.3%
Purchase of Finished Goods	7.6	0.0	#DIV/0!	4.0	91.9%
Employees Cost	93.7	65.5	43.1%	83.8	11.9%
Power & Fuel	181.0	139.2	30.0%	180.3	0.4%
Freight, Handling & Other Expenses	23.0	16.0	43.8%	17.2	33.7%
Other Expenditure	116.6	117.8	-1.0%	78.6	48.4%
Total Opex	1171.7	961.1	21.9%	957.4	22.4%
Operating Profit	**240.6**	**497.3**	-51.6%	**308.8**	-22.1%
OPM %	*17.3%*	*34.9%*		*24.8%*	
Other Income	126.5	85.1	48.7%	85.9	47.3%
Interest Expenses	7.4	13.3	-44.7%	7.2	3.1%
Depreciation	36.9	42.3	-12.6%	36.6	1.0%
PBT	322.8	526.8	-38.7%	351.0	-8.0%
PBTM %	*22.9%*	*36.1%*		*27.7%*	
Tax	79.2	131.3	-39.6%	76.5	3.6%
Effective Tax Rate %	*24.5%*	*24.9%*		*21.8%*	
Net Profit	**243.6**	**395.5**	-38.4%	**274.5**	-11.3%
NPM %	*17.5%*	*27.7%*		*22.1%*	
Equity Capital	91.7	91.7	0.0%	91.7	0.0%
EPS	**26.6**	**43.1**	-38.4%	**29.9**	-11.3%

Segmental - Consolidated

(Rs. in Cr)

Particulars	Q4FY12	Q4FY11	% Chg	Q3FY12	% Chg
Segment Revenue					
- VSF	1369.3	1530.4	-10.5%	1246.3	9.9%
- Cement - Grey, White and Allied Products	5659.1	4745.9	19.2%	4792.8	18.1%
- Chemicals	219.7	155.7	41.2%	210.0	4.6%
- Others	118.0	104.5	12.9%	116.2	1.6%
Total	7366.0	6536.4	12.7%	6365.3	15.7%
Less: Inter Segment Revenue	76.9	54.1	42.0%	73.7	4.4%
Total Operating Income	**7289.2**	**6482.3**	12.4%	**6291.6**	15.9%
Segment Results					
- VSF	213.3	532.1	-59.9%	270.4	-21.1%
- Cement - Grey, White and Allied Products	1079.9	862.1	25.3%	818.6	31.9%
- Chemicals	23.4	21.1	10.6%	38.2	-38.8%
- Others	6.7	4.8	37.9%	5.2	28.3%
Total	1323.2	1420.1	-6.8%	1132.4	16.9%
Less: Interest	79.9	109.1	-26.7%	50.1	59.6%
Add: Net Unalloacble Income/(Expenditure)	259.2	60.3	329.7%	133.2	94.7%
Profit before Extra Ordinary Items and Tax Expense	**1502.5**	**1371.3**	9.6%	**1215.4**	23.6%
Capital Employed					
- Viscose Staple Fibre & Pulp	3723.0	2633.5	41.4%	3338.1	11.5%
- Cement - Grey, White and Allied Products	19322.1	16558.6	16.7%	18898.7	2.2%
- Chemicals	558.8	428.4	30.4%	516.4	8.2%
- Others	229.5	206.3	11.2%	220.5	4.1%
- Unallocated Corporate Capital Employed	7483.5	7842.2	-4.6%	7731.9	-3.2%
Total Capital Employed	**31316.8**	**27669.0**	13.2%	**30705.5**	2.0%

(Source: Company, HDFC Sec)

The Financial Results for the current period are not strictly comparable with the corresponding period due to :
a. Consolidation of Results of subsidiaries of UltraTech Cement Middle East Investments Limited (Star Cement Co. LLC., UAE and its associate companies) from 1st October, 2010 when acquisition was completed.
b. Consolidation of pro-rata Results of Aditya Group AB, Sweden (AGS) and its subsidiaries including Domsjo Fabriker AB, Sweden as an ‘Associate’ of the Company from the date of acquisition of 1/3 equity interest by the Company in June 2011.

Performance of business divisions:

Viscose Staple Fibre (VSF)

Particulars	Q4FY12	Q4FY11	% Chg	Q3FY12	% Chg	Remarks
Capacity (TPA)	333,975	333,975	0.0%	333,975	0.0%	
Production (MT)	83,349	82,932	0.5%	84,233	-1.0%	
Sales Volume (MT)	94,904	85,650	10.8%	78,215	21.3%	Higher exports led to higher volumes
Net Sales (Rs.Cr.)	1,227.9	1,326.0	-7.4%	1,085.1	13.2%	
Realisation (Rs/MT)	121,293	144,962	-16.3%	128,499	-5.6%	Realisations were impacted on account of lower VSF prices globally
PBIDT (Rs.Cr.)	232.0	513.7	-54.8%	277.7	-16.5%	
PBIDT Margin (%)	18.9%	38.7%		25.6%		Margin impacted due to increase in input costs and higher base effect
JV - Net Sales (Rs.Cr.)	211.7	239.4	-11.6%	232.5	-8.9%	
JV - EBIDTA (Rs.Cr.)	15.8	51.0	-69.0%	25.5	-38.0%	
Consolidated PBIDT (Rs.Cr.)	252.2	567.3	-55.5%	306.6	-17.7%	
Consolidated PBIDT Margin (%)	17.5%	36.2%		23.3%		

(Source: Company, HDFC Sec)

- Q4FY12 ended on a weak note affected by slowdown in Eurozone and China, which in turn affected VSF prices globally. VSF prices globally remained suppressed due to higher cotton crop and new capacity set up in China.
- Lower realisations in the international market and peak prices in Q4FY11 due to cotton shortage led to average realisation declining by 16.3% y-o-y. However sales volumes was higher by 10.8% aided by higher exports.
- Input costs continued to rise in Q4FY12. Higher fixed cost, caustic and energy cost coupled with lower realisations led to PBIDT margin dropping sharply by 1980 bps y-o-y to 18.9%. Profit of JVs was affected due to higher input cost. Consolidated PBIDT for VSF Business was lower by 55%. Domsjo performance improved q-o-q despite fall in pulp realization due to higher volumes and write back of forex losses during the quarter.
- In the present macro economic conditions, demand could remain volatile. Profitability in such scenario could be governed by the prices of competing fibres, input and energy costs. New capacities coming up in China could also put pressure on the markets while stability in Eurozone could influence demand.
- The management has indicated continued focus on specialty fibres and R&D initiatives on the back of high quality pulp assured with Domsjo acquisition and also the Vilayat capacity to come up on stream in FY13 would produce specialty fibres.
- Nagda plant is expected to operate uninterrupted during summer with adequate water storage and hence Q1FY13 results from this unit could be better on a y-o-y basis.
- GIL could emerge stronger from the present challenging times with high level of integration and continued focus on cost and operating efficiency improvement.
- Expansions are progressing as per schedule.

Location	Present Capacity (KTPA)	Expanded Capacity (KTPA)	Commissioning Date
Vilayat, Gujarat	-	120	Q4FY12-13
Harihar, Karnataka	51	87	In phases: Q2 & Q4FY12-13
Domsjo, Sweden	210	255	Q1FY12-13

(Source: Company Presentation)

- The additional capacity including Vilayat could increase volumes in FY13-14. Also GIL plans to set up a Greenfield project of 180K TPA in Turkey in JV with group companies. It is in the process of acquiring land and necessary approvals.

Chemicals

Particulars	Q4FY12	Q4FY11	% Chg	Q3FY12	% Chg	Remarks
Caustic Sales Volume (MT)	72,839	68,253	6.7%	71,232	2.3%	
Net Sales (Rs.Cr.)	219.7	155.7	41.1%	209.1	5.1%	Better volumes and good market conditions continue to aid faster growth in the chemical division
ECU Realisation (Rs/MT)	24,612	18,882	30.3%	24,385	0.9%	
PBIDT (Rs.Cr.)	32.3	29.4	9.9%	47.2	-31.6%	
PBIDT Margin (%)	14.7%	18.9%		22.6%		

(Source: Company, HDFC Sec)

- Caustic prices continued the uptrend in Q4FY12 as chlorine prices declined to abnormal levels on account of lower chlorine demand. This in turn aided ECU realisations in moving up by 30.3% y-o-y.

- During the quarter, GIL witnessed high energy and salt costs and one time remambring expenses. The demand outlook for caustic soda is positive with improved sentiment in the international market.

- Caustic capacity expansion at Vilayat (182,500 TPA) is progressing as per schedule and is expected to be completed by Q4FY13.

Cement

Particulars	Q4FY12	Q4FY11	% Chg	Q3FY12	% Chg	Remarks
Cement Sales Volume (Mn Ton)	12.1	11.1	8.7%	12.1	11.1	Recovery in demand since November 2011 led to higher volumes in Q4FY12
Clinker Sales Volumes (Mn Ton)	0.3	0.4	-25.6%	0.3	0.4	
White Cement Sales Volume (MT)	163,000	147,000	10.9%	163,000	147,000	
Total sales Volume (Mn Ton)	12.5	11.5	8.5%	12.5	11.5	
Net Sales (Rs.Cr.)	5,659.1	4,745.7	19.2%	4,864.8	16.3%	
PBIDT (Rs.Cr.)	1,490.1	1,139.9	30.7%	1,124.2	32.5%	
PBIDT Margin (%)	26.3%	24.0%		23.1%		

(Source: Company, HDFC Sec)

- The cement industry recovered since November 2011 and witnessed growth of 8.8% in Q4FY12 on account of strong growth in Northern and Western parts of India. However, the excess capacity situation still persists and continues to worry the industry. 15 mn MT of new capacity was added in FY12 taking the total capacity to 319 mn MT. Cost pressures continue to haunt the industry. Post the Railway Budget 2012-13, railway freight charges rose by 22% in March 2012. Also increase in excise duty structure in the Union Budget led to cement manufacturers increasing the prices. Inflationary pressures are also taking a toll on coal cost/ton.

- GIL witnessed cement volume growth of 8.7% on the back of recovery in demand. Realisations were higher in spite of its presence in the southern markets, where cement prices during the quarter were not as robust as in the northern region.

- Higher energy costs continued to hurt the company through higher cost of production. Despite cost overruns, GIL managed to improve its PBIDT margins as it could pass on the same to its consumers. Consolidated PBIDT rose by 31% supported by higher volume, improved margins and higher treasury income.

- Star Cement achieved breakeven this quarter through cost control measures.

- As per the management, cement demand is expected to grow in line with GDP growth at 8%+. The surplus scenario could subside gradually in next 2-3 years with expected growth in demand. The management has indicated likely addition of 66mn MT in capacity by FY15.

- Energy and freight cost could be a cause of concern and could create pressure on margins.

- The company's initiative towards setting up additional clinkerisation plants at Chhattisgarh and Karnataka together with grinding units, bulk packaging terminals and ready mix concrete plants is progressing on schedule and are expected to be operational from early fiscal 2014. As a result, the company's cement capacity is expected to be enhanced by 10.2 mtpa.

- The Board of Directors has recommended a dividend of Rs. 22.50 per share (vs Rs.20 for FY11).

Capex Plans:

- UTCL has a capital outlay of Rs.10,384 cr to be spent over the next two years. The capex pertains to a number of projects including clinkerisation plants through brownfield expansion at Chhattisgarh (4.8 mn MT) and Karnataka (4.4mn MT), additional grinding units, installing waste-heat recovery systems; instituting bulk packaging terminals and setting up of ready-mix concrete plants. Orders have been placed for major equipment for setting up of the projects. These expansions are expected to be operational by Q1FY14 and will enhance UTCL's cement capacity by 10.2 mtpa. These projects will be funded through a judicious mix of internal accruals and borrowings. Of the Rs.10,384 cr capex, UTCL has spent Rs.3,232 cr in FY12.

Concerns

- In the next 18-24 months, new cement capacities could be commissioned across various regions and this could put pressure on prices and margins. However, fresh capacity additions for GIL are also coming on stream and that will cater to high growth North and Central regions.

- Lower demand offtake for VSF and cement could be a threat.

- Sustained rise in input costs like pulp, coal, energy, fuel etc could pose a threat. Rupee depreciation could impact cost of imported coal. The new price mechanism adopted by Coal India could hurt margins of cement companies like UTCL.

- Delay in execution of GIL's proposed capacity expansions.

- The Competition Commission of India (CCI) could soon give a negative ruling in the matter of cartelisation by cement manufacturers. The CCI conducted a detailed investigation and has reportedly found many companies including leading players like ACC, Ambuja Cement and Ultratech guilty of cutting production to raise cement price. As per reports, the companies involved in cartelisation are expected to be slapped with penalties of about 7% of total revenue (last three year's average), for each year of the investigation as per reports. This amount of penalty equals 5-6% of the market capitalisation.

Conclusion & Recommendation

GIL's Q4FY12 operating results were below street estimates on account of lower VSF volumes and margins. However, cement business performed well. The fibre business was impacted due to global conditions, while cement performed well due to improved demand. Prices of GIL's VSF, which is one of the main raw materials for making garments, fell 16% in FY12, mainly due to higher capacities in China. This also led to a sharp decline in the operating profit margin of the fibre business.

Going forward, in its cement division and the broader sector, demand is expected to weaken with the monsoon expected to set in over the next few weeks. Cement prices typically weaken during the monsoon season. This comes at a time when input costs are still at elevated levels.

For GIL, input costs still remain high in its VSF division. Apart from that, with no signs of easing in the Eurozone problems and its impact on a key user industry for the VSF division-the global textile industry, the outlook for this division remains hazy in the near-term.

The chemical division is expected to do well going ahead given the increased off take from the aluminium industry.

Being the largest player with total capacity of 51MT (existing capacity) under control and highest organic growth visibility, GIL could be biggest beneficiary of any further increase in cement demand and prices.

In our Q3FY12 result update dated February 8, 2012, we had stated that the stock could trade in the Rs.2,569-Rs.3,010 band for the next quarter. Post the issue of the report, the stock made a low of Rs.2,321.5 on May 7, 2012 and made a high of Rs.2,924.45 on February 21, 2012.

GIL is better placed among the large cement players due to its strong balance sheet, comfortable debt-equity ratio (0.4x FY12), attractive valuation and diversified business. But it suffers from holding company discount due to its holding in Ultratech Cements.

GIL overachieved our FY12 estimates on the top and bottomline front. We are maintaining our FY13 estimates for the time being and will review it later. At the CMP, the stock is trading at 8.4x FY13E EPS of Rs.293.6. However, it could continue to get poor valuations in the face of uncertain commodity price scenario, apart from holding company discount. Improved cement scenario could however take the stock towards its all time high.

We feel that the stock could trade in the Rs.2,202 to Rs.2,716 (7.5x to 9.25x FY13E EPS) for the next quarter.

Financial Estimates:

Particulars (Rs in Crs)	FY09	FY10	FY11	FY12 (E)*	FY12 (A)*	FY13 (E)*
Operating income	18602.9	19933.4	21585.2	23500.0	25244.3	25894.2
PBIDT	4528.6	6048.9	4999.4	5287.5	5574.9	6111.0
PBIDTM (%)	24.3%	30.3%	23.2%	22.5%	22.1%	23.6%
Profit after Tax	2186.7	3095.7	2264.8	2397.0	2647.5	2693.0
PATM (%)	11.8%	15.5%	10.5%	10.2%	10.5%	10.4%
EPS	238.5	337.6	247.0	261.3	288.6	293.6
P/E (x)	10.3	7.3	10.0	9.4	8.5	8.4

* - Quick Estimates, A - Actuals, OE - Original Estimates, RE- Revised Estimates (**Source:** Annual Report, HDFC Sec Estimates)

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