

October 25, 2013

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Rating	Accumulate
Price	Rs54
Target Price	Rs60
Implied Upside	11.1%
Sensex	20,684
Nifty	6,145

(Prices as on October 25, 2013)

Trading data

Market Cap. (Rs bn)	21.3
Shares o/s (m)	398.5
3M Avg. Daily value (Rs m)	29.4

Major shareholders

Promoters	37.84%
Foreign	14.14%
Domestic Inst.	24.99%
Public & Other	23.03%

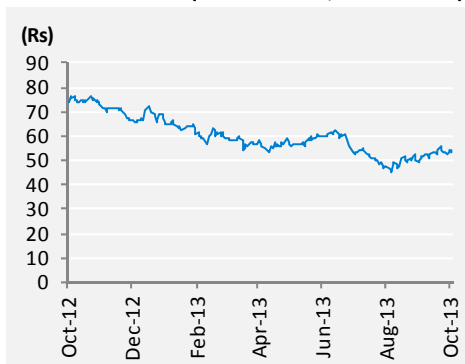
Stock Performance

(%)	1M	6M	12M
Absolute	4.5	(6.1)	(30.0)
Relative	0.3	(12.6)	(40.3)

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2014	11.2	11.1	0.8
2015	13.1	13.8	-5.7

Price Performance (RIC: GSFC.BO, BB: GSFC IN)



Source: Bloomberg

GSFC's Q2FY14 results stood above PLe/consensus estimates driven by higher top-line and higher other income; adjusted PAT came at Rs1.3bn, -14% YoY above estimates of Rs947m. Though valuations are compelling, lack of any positive trigger is likely to keep stock under pressure in the near term. Caprolactam-benzene spreads have recovered from their lows; however, Q2 spreads still remained weak at US\$1,068/mt. Moderate improvement of 6-8% is expected in the near term due to correction in benzene prices. Ammonium sulphate subsidy issue is under litigation and remains a major overhang on the stock. We have downgraded our earnings by 8%/10% to factor in continuous pressure on spreads. At CMP of Rs54, stock is trading at 4.8x/4.1x FY14E/15E earnings and 50% discount to book value. We maintain 'Accumulate' with target price of Rs60.

■ **Q2FY14 results were above estimates driven by higher top-line and other income:** GSFC reported revenues of Rs14.2bn, flat YoY higher than estimates of Rs12.2bn due to higher fertilizer revenues. Adjusted EBITDA for the quarter stood at Rs1.8bn, -11% YoY higher than estimate of Rs1.6bn. EBITDA margins came at 12.8% against an estimate of 13.4%. EBITDA has been adjusted for Rs285m of FX losses included in other expenses. Adjusted PAT came at Rs1.3bn, -14% YoY. For H1FY14, company has done EPS of Rs4.7

■ **Chemicals margins improved 490bps QoQ to 16.1%:** Chemicals revenues stood at Rs5.7bn, 15.6% YoY in line with estimates. Margins improved to 16.1% (+490bps QoQ). Reported chemicals margins stood at 13.6%. However, we have adjusted for Rs143m of FX losses (other expense included Rs285m of FX losses equally split between fertiliser and chemicals segment). On a YoY basis, chemicals margins are lower by 1050bps due to lower capro-benzene spreads this year.

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Key financials (Y/e March)	2012	2013	2014E	2015E
Revenues (Rs m)	53,018	61,967	54,957	58,220
Growth (%)	12.6	16.9	(11.3)	5.9
EBITDA (Rs m)	11,291	7,813	7,023	8,091
PAT (Rs m)	7,664	5,187	4,455	5,206
EPS (Rs)	19.2	13.0	11.2	13.1
Growth (%)	7.5	(32.3)	(14.1)	16.8
Net DPS (Rs)	1.5	2.0	2.0	2.0

Profitability & Valuation	2012	2013	2014E	2015E
EBITDA margin (%)	21.3	12.6	12.8	13.9
RoE (%)	24.2	13.9	10.8	11.5
RoCE (%)	21.1	11.3	8.7	10.0
EV / sales (x)	0.3	0.6	0.5	0.4
EV / EBITDA (x)	1.6	4.4	4.1	3.2
PE (x)	2.8	4.1	4.8	4.1
P / BV (x)	0.6	0.5	0.5	0.5
Net dividend yield (%)	2.8	3.7	3.7	3.7

Source: Company Data; PL Research

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- Fertiliser segment performance was in line:** Fertiliser revenues stood at Rs8.5bn, -8% YoY higher than estimates of Rs6.5bn driven by higher volumes. GSFC sold 282,000mt of complex fertilisers (estimate of 200,000mt) during the quarter. Reported fertilizer margins stood at 5.5%. However, adjusting for FX loss of Rs143m (other expense included Rs285m of FX losses equally split between fertiliser and chemicals segment), fertilizer margins stood at 7.2%.
- Maintain 'Accumulate', with target price of Rs60:** Lack of any positive trigger is likely to keep stock under pressure in the near term. In the chemicals segment, capro-benzene spreads remain weak. Fertiliser industry outlook is also not very encouraging in the near term. Further, ammonium sulphate subsidy issue remains a major overhang on stock. However, valuations look attractive from a medium-to-long term point of view. Company holds more than ~50% of the current market cap in cash and investments.

Exhibit 1: Revision in earnings

	FY14E			FY15E		
	Old Estimates	New Estimates	% Change	Old Estimates	New Estimates	% Change
Net sales (Rs m)	57,202	54,957	-3.9%	60,800	58,220	-4.2%
EBITDA (Rs m)	7,984	7,023	-12.0%	8,901	8,091	-9.1%
<i>Margin</i>	<i>14.0%</i>	<i>12.8%</i>	<i>-118</i>	<i>14.6%</i>	<i>13.9%</i>	<i>-74</i>
PAT (Rs m)	4,869	4,455	-8.5%	5,809	5,206	-10.4%
EPS (Rs)	12.2	11.2	-8.4%	14.6	13.1	-10.5%

Source: Company Data, PL Research

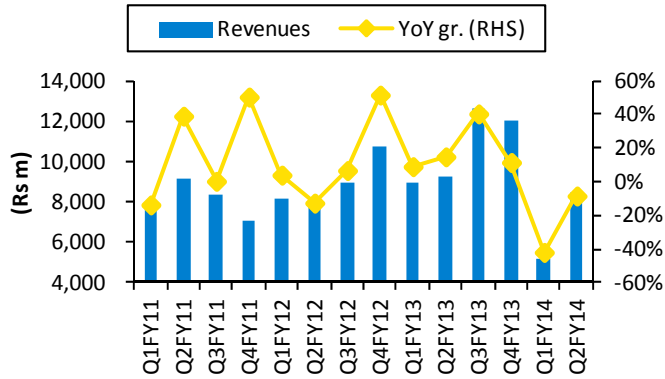
Exhibit 2: Q2FY14 Result Overview (Rs m)

Y/e March	Q2FY14	Q2FY13	YoY gr (%)	Q1FY14	H1FY14	H1FY13	YoY gr (%)
Net Sales	14,180	14,160	0.1	10,180	24,360	28,279	(13.9)
Expenditure							
Raw Materials	8,533	8,616	(1.0)	6,312	14,846	17,485	(15.1)
<i>% of Net sales</i>	<i>60.2</i>	<i>60.8</i>		<i>62.0</i>	<i>60.9</i>	<i>61.8</i>	
Personnel	998	893	11.7	983	1,980	1,866	6.1
<i>% of Net sales</i>	<i>7.0</i>	<i>6.3</i>		<i>9.7</i>	<i>8.1</i>	<i>6.6</i>	
Other Expenditure	2,841	2,624	8.3	2,172	5,013	4,528	10.7
<i>% of Net sales</i>	<i>20.0</i>	<i>18.5</i>		<i>21.3</i>	<i>20.6</i>	<i>16.0</i>	
Total Expenditure	12,372	12,133	2.0	9,467	21,838	23,879	(8.5)
EBITDA	1,809	2,028	(10.8)	713	2,522	4,400	(42.7)
<i>Margin (%)</i>	<i>12.8</i>	<i>14.3</i>		<i>7.0</i>	<i>10.4</i>	<i>15.6</i>	
Depreciation	362	340	6.4	333	695	632	9.9
EBIT	1,447	1,688	(14.3)	380	1,827	3,768	(51.5)
Interest	123	32	280.6	140	264	128	106.7
Other Income	413	460	(10.3)	140	552	1,007	(45.2)
PBT	1,736	2,115	(17.9)	379	2,116	4,647	(54.5)
Tax	438	611	(28.2)	24	462	1,416	(67.3)
<i>Tax Rate (%)</i>	<i>25.2</i>	<i>28.9</i>		<i>6.3</i>	<i>21.9</i>	<i>30.5</i>	
Adjusted PAT	1,298	1,505	(13.7)	595	1,893	3,232	(41.4)
Extraordinary Income	(285)	-	NA	(539)	(824)	-	NA
Reported PAT	1,013	1,505	(32.6)	55	1,069	3,232	(66.9)
Adjusted EPS	3.3	3.8	(13.7)	1.5	4.7	8.1	(41.4)

Source: Company Data, PL Research

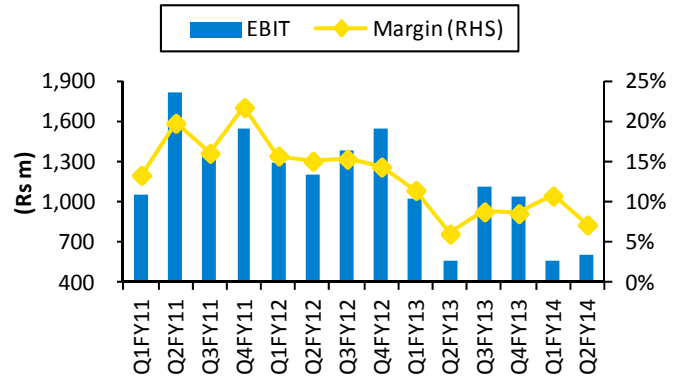
Segmental performance

Exhibit 3: Fertiliser revenues & growth % YoY



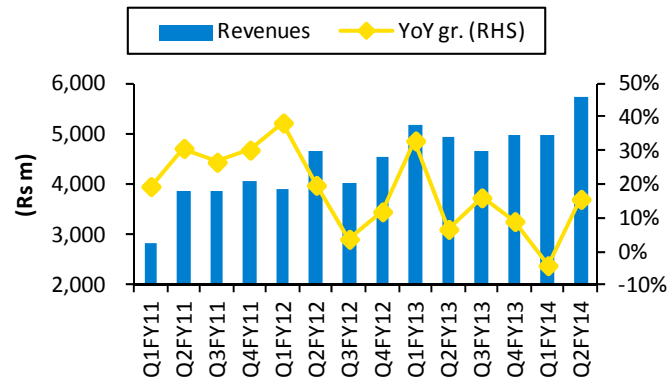
Source: Company Data, PL Research

Exhibit 4: Fertiliser EBIT & Margins



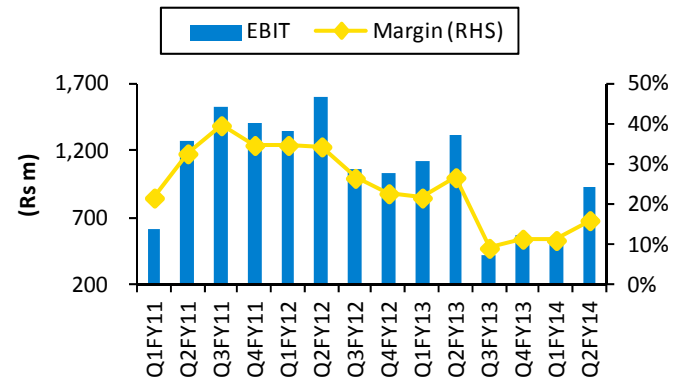
Source: Company Data, PL Research

Exhibit 5: Chemicals revenues & growth % YoY



Source: Company Data, PL Research

Exhibit 6: Chemicals EBIT & Margins



Source: Company Data, PL Research

Key takeaways from conference call

- **Rabi expected to be robust:** H2FY14 is expected to be good for the industry on the back of good water levels in reservoirs, higher moisture content in soil, increase in rabi MSPs etc.
- **Fertiliser profitability impacted in Q2 due to multiple headwinds:** Q2 adjusted fertiliser margins stood at 7.2%. Though monsoons were good, fertiliser business faced multiple headwinds in the form of reduction in farmgate prices, huge inventory in system etc. Hence, fertiliser margins turned out to be lower. However, margins are expected to improve from current levels due to reduction in raw material prices and old inventory getting exhausted in the system.
- **Q2FY14 average capro-benzene spreads stood at US\$1,068/mt; expect improvement of 6-8% in the near term:** Though capro-benzene spreads have improved from their lows of US\$763/mt few months back, they are hovering around US\$1,050-\$1,100/mt. Capro-benze spreads have been pressurised by high benzene prices. For Q2, spreads stood at US\$1,068/mt. However, improvement of 6-8% is expected in the near term due to correction in benzene prices.
- **Fertiliser market still plagued with excess inventory in certain regions; expect normalization during rabi season:** Though complex fertiliser inventory in system has reduced, still excess inventory is to the tune of 2.5m mt (5m mt earlier). Inventory is higher in Northern region, Tamil Nadu where the main season is rabi rather than kharif season. Management expects inventory to normalize in rabi season.
- **Current subsidy receivable stands at Rs11bn.**
- **Going forward, management expects to achieve EBITDA margin of Rs2,000-2,500/mt in fertilisers segment**
- **Ammonium sulphate subsidy issue to be heard again in Jan'14:** GSFC had approached the High Court for the ammonium sulphate subsidy issue and court has put a stay on govt.'s order of recovering subsidy on ammonium sulphate. GSFC continues to sell ammonium sulphate in the market. Next hearing is scheduled in January 14 and management is hopeful that the outcome will be in its favour.

Income Statement (Rs m)

Y/e March	2012	2013	2014E	2015E
Net Revenue	53,018	61,967	54,957	58,220
Raw Material Expenses	29,514	40,515	34,494	37,476
Gross Profit	23,504	21,452	20,463	20,744
Employee Cost	3,936	3,951	4,274	4,701
Other Expenses	8,278	9,688	9,167	7,952
EBITDA	11,291	7,813	7,023	8,091
Depr. & Amortization	1,292	1,321	1,415	1,440
Net Interest	(1,221)	(1,018)	(489)	(480)
Other Income	1,366	1,381	952	880
Profit before Tax	11,220	7,511	6,097	7,131
Total Tax	3,731	2,304	1,641	1,925
Profit after Tax	7,488	5,207	4,455	5,206
Ex-Od items / Min. Int.	—	(21)	—	—
Adj. PAT	7,664	5,187	4,455	5,206
Avg. Shares O/S (m)	398.5	398.5	398.5	398.5
EPS (Rs.)	19.2	13.0	11.2	13.1

Cash Flow Abstract (Rs m)

Y/e March	2012	2013	2014E	2015E
C/F from Operations	5,405	(8,405)	12,093	9,590
C/F from Investing	(3,958)	(6,532)	(5,000)	(5,000)
C/F from Financing	1,402	7,592	(4,890)	(4,826)
Inc. / Dec. in Cash	2,849	(7,344)	2,203	(236)
Opening Cash	6,127	8,976	1,631	3,835
Closing Cash	8,976	1,631	3,835	3,599
FCFF	1,723	(12,894)	9,629	7,190
FCFE	3,970	(4,013)	6,129	3,690

Key Financial Metrics

Y/e March	2012	2013	2014E	2015E
Growth				
Revenue (%)	12.6	16.9	(11.3)	5.9
EBITDA (%)	0.3	(30.8)	(10.1)	15.2
PAT (%)	7.5	(32.3)	(14.1)	16.8
EPS (%)	7.5	(32.3)	(14.1)	16.8
Profitability				
EBITDA Margin (%)	21.3	12.6	12.8	13.9
PAT Margin (%)	14.5	8.4	8.1	8.9
RoCE (%)	21.1	11.3	8.7	10.0
RoE (%)	24.2	13.9	10.8	11.5
Balance Sheet				
Net Debt : Equity	(0.1)	0.3	0.2	0.1
Net Wrkng Cap. (days)	117	185	162	131
Valuation				
PER (x)	2.8	4.1	4.8	4.1
P / B (x)	0.6	0.5	0.5	0.5
EV / EBITDA (x)	1.6	4.4	4.1	3.2
EV / Sales (x)	0.3	0.6	0.5	0.4
Earnings Quality				
Eff. Tax Rate	33.3	30.7	26.9	27.0
Other Inc / PBT	12.2	18.4	15.6	12.3
Eff. Depr. Rate (%)	3.4	3.1	3.2	3.1
FCFE / PAT	51.8	(77.4)	137.6	70.9

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2012	2013	2014E	2015E
Shareholder's Funds	35,168	39,416	42,945	47,225
Total Debt	6,170	15,051	11,551	8,051
Other Liabilities	2,474	2,392	2,392	2,392
Total Liabilities	43,811	56,859	56,888	57,667
Net Fixed Assets	18,114	20,842	24,428	27,988
Goodwill	—	—	—	—
Investments	4,327	6,724	6,724	6,724
Net Current Assets	21,370	29,292	25,736	22,956
<i>Cash & Equivalents</i>	<i>8,976</i>	<i>1,631</i>	<i>3,835</i>	<i>3,599</i>
<i>Other Current Assets</i>	<i>24,247</i>	<i>39,978</i>	<i>34,111</i>	<i>31,082</i>
<i>Current Liabilities</i>	<i>11,853</i>	<i>12,318</i>	<i>12,210</i>	<i>11,725</i>
Other Assets	—	—	—	—
Total Assets	43,811	56,858	56,888	57,667

Quarterly Financials (Rs m)

Y/e March	Q3FY13	Q4FY13	Q1FY14	Q2FY14
Net Revenue	16,728	16,960	10,180	14,180
EBITDA	1,742	1,671	1,193	1,809
<i>% of revenue</i>	<i>10.4</i>	<i>9.9</i>	<i>11.7</i>	<i>12.8</i>
Depr. & Amortization	348	340	333	362
Net Interest	(85)	(53)	1	(289)
Other Income	194	180	140	413
Profit before Tax	1,479	1,384	859	1,736
Total Tax	488	400	24	438
Profit after Tax	1,370	584	55	1,013
Adj. PAT	991	984	602	1,298

Key Operating Metrics

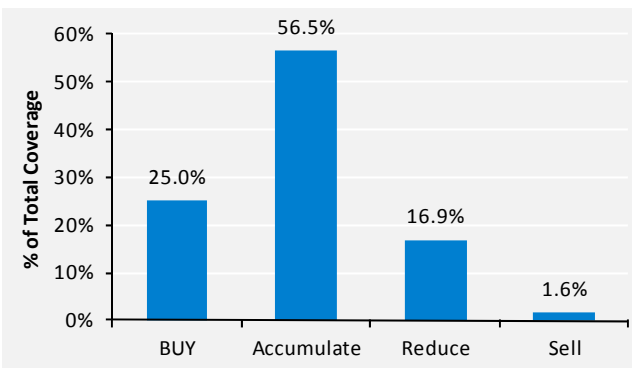
Y/e March	2012	2013	2014E	2015E
Revenues (Rs m)				
Fertiliser	35,919	42,791	33,197	34,284
Chemicals	17,099	19,752	21,760	23,936
EBIT Margin (%)				
Fertiliser	15.1	8.7	8.2	8.0
Chemicals	29.5	17.5	15.7	18.0

Source: Company Data, PL Research.



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BUY	: Over 15% Outperformance to Sensex over 12-months	Accumulate	: Outperformance to Sensex over 12-months
Reduce	: Underperformance to Sensex over 12-months	Sell	: Over 15% underperformance to Sensex over 12-months
Trading Buy	: Over 10% absolute upside in 1-month	Trading Sell	: Over 10% absolute decline in 1-month
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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