MSFL Research

Result Update - Q2FY12

Birla Corporation Ltd.

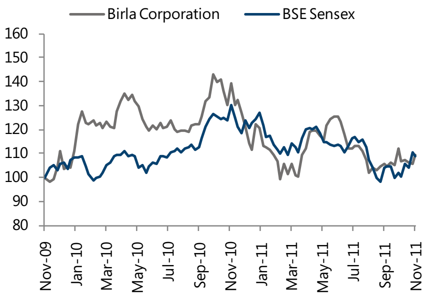
Rising costs knock margins

BUY

Reco	Maintained
CMP	₹ 315
Target Price	₹ 387
Upside Potential	23%

Price Performance

52 wk Hi/Lo	435/278
All time Hi/Lo	448/10
6 mnth Average Vol	15674
Stock Beta	0.37



Valuation

	FY11	FY12P	FY13P
P/E (x)	8.3	7.4	6.1
P/BV (x)	1.3	1.0	0.9
RONW (%)	16.6	14.9	15.9
ROCE (%)	13.7	11.5	11.8

Peer Valuation (FY13 – CY12)

	ACC	UltraTech
PE	17.0	17.3
P/BV	2.9	2.4

Equity Data

Market Cap. (₹ bln)	24
Face value (₹)	10
No of shares o/s (mln)	77

	Sep'10	Sep'11	Δ%
Promoters	62.90	62.90	0.00
DFI's	12.52	14.18	13.26
FII's	7.90	6.88	-12.91
Public	16.68	16.04	-3.84

Birla Corporation delivered lower than expected Q2 numbers where sheer increase in costs coupled with lower realisations has impacted margins and earnings growth. Despite 5% y-o-y top line growth, company ended up reporting 62% decline in net profits primarily due to y-o-y higher costs including foreign exchange fluctuation loss incurred during the quarter.

Top line grew 5.5% on the back of higher contribution from Jute, power segments.

Birla Corp has reported moderate growth of 5.5% in top line. Company saw y-o-y higher gross revenue contribution from Jute and Power segment which grew by 19% and 33% respectively. Cement revenue contributed 88% to total revenue and were up 5% y-o-y on the back of 2% and 3% y-o-y increase in cement volumes and realisation respectively.

EBITDA declined 59% on the back of higher costs on all fronts

59% decline in Q2 EBITDA was more than anticipated and was mainly contributed by increased input costs due to higher clinker purchase on the back of disruption of operations in Chanderia plant followed by High Court order to stop mining and blasting operations near Chitorgarh Fort and also due to higher cost of power, coal and other expenses. Company also incurred a foreign exchange fluctuation loss of ₹ 139mln, impacting Jute segment performance, against foreign exchange gain reported for Q2FY11.EBITDA margin contracted by ~1000bps y-o-y at 6.7% (Q2FY11 – 17.1%) . Excluding this loss, Q2 EBITDA margins stands at ~9% quarter.

Reported PAT declined by 62% on the back of y-o-y higher depreciation, lower other income

Company witnessed y-o-y higher depreciation as a result of commissioning of new capacities during last year. Also due to y-o-y lower other income Birla Corp's Net profit declined by 62% y-o-y at ₹ 262mln as against ₹ 689 for Q2FY11. Company posted EPS of ₹ 3.4 (₹ 8.9 – Q2FY11) against our expectations of ₹ 9.01. Birla Corp declared Interim Dividend of ₹ 2.5 per share.

Outlook and Valuation

We expect Birla Corp to face continued headwinds in terms of higher clinker costs in the light of pending court case on mining issue in Rajasthan. We expect gradual recovery in demand and also sequential improvement in realisations considering the recent rounds of price hikes. Birla Corp has strong presence into Central, Northern and Eastern regions and hence is likely to benefit more from the recent price and demand recovery witnessed in these regions. Due to favourable regional mix and upcoming capacity we continue to like Birla Corp which is currently trading at very attractive valuations. At ₹ 315, stock trades at 4.6 x EV/EBITDA of FY13P. Maintain BUY with target price of ₹ 387 at 5.5 x EV / EBITDA of FY13P.

Summary Financials

₹ in Mln	FY10	FY11	FY12P	FY13P
Net Sales	21984	21622	24854	29384
OPBDIT	7466	4531	4762	5915
Net Profit	5572	3199	3260	3970
EPS	72.4	41.5	42.3	51.6
Net Worth	17912	20579	23301	26734
Debt	7092	10158	13256	16127
Fixed Assets	10265	14644	20343	25842
Net Current Assets	4118	5527	7147	8952

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Exhibit 1: Quarterly Financials (Amount in ₹ mln)

Period Ending	Q2FY12	Q2FY11	Y-o-Y	Q1FY12	Q-o-Q
Sales	**5189**	**4920**	**5.5%**	**5664**	**-8.4%**
Expenditure	4840	4077	18.7%	4103	18.0%
EBIDTA	**349**	**843**	**-59%**	**1561**	**-78%**
% margin	6.7%	17.1%	-1040bps	27.6%	2080bps
Interest	117	119	-1%	120	-2%
Depreciation	178	157	13%	175	1%
Other Income	125	62	102%	11	1053%
PBT	**295.5**	**860.9**	**-66%**	**1538.4**	**-81%**
Tax	14	-17	-179%	109	-88%
PAT	**261.5**	**689.7**	**-62%**	**1118.8**	**-77%**
% Margin	5.0%	14.0%	-900bps	19.8%	-1470bps
EPS	**3.40**	**8.96**	**-62%**	**14.53**	**-77%**

Actual Vs MSFL Estimates

₹ (Mln)	Actual	Estimated	Difference
Net Sales	5189	5248	-1.1%
EBITDA	349	1021	-65.8%
EBITDA Margin	6.7%	19.5%	-200bps
PAT	261.5	693.5	-62.3%

Key Result highlights

Birla Corporations Q2 results were lower than expected. Higher costs in terms of raw material, coal, and other expenses have taken a toll on company's margin and profitability. After a weak Q1, Jute segment reported positive EBIT, however cement and power segment continued to witness margin pressure given rising costs with moderate growth in volumes and realisations.

- Birla Corp's net operating income grew by 5.5% y-o-y at ₹ 5189mln against ₹ 4920mln for the year ago period.
- Cement revenue of ₹ 4540mln contributed 88% to the total sales which increased by 5% y-o-y. Cement volumes improved by 2% y-o-y at 1.41mt (Q2FY11 - 1.39mt) and Cement realisation for the quarter improved by 3% y-o-y at ₹ 3329 against 3119 for the year ago period.
- Jute revenue witnessed strong 19% growth y-o-y and 66% growth q-o-q at ₹ 590mln against ₹ 497mln for Q2FY11 as a result of higher volumes Other operating income was lower on account of foreign exchange loss to the tune of ₹ 138mln against gain for the year ago period.
- EBITDA margins declined by more than 1000bps on the back of y-o-y higher costs on all fronts. Against our expectation of 19% margins Birla Corporation has delivered EBITDA margins at 6.7% (against 173% for Q2FY11 and 27.6% for Q1FY12).
- During the quarter Company's Chanderia plant's operations were impacted on account of High Court's order banning mining and blasting operations within 10km radius of the Chittorgarh Fort. Company operated the plant using clinker from Satna plant and also from outsourced clinker. This in turn has increased raw material costs significantly. Other costs like coal, power, freight and other expenditure also increased y-o-y which put together have impacted EBITDA margins on y-o-y as well as sequential basis.

- Cement EBIT declined significantly by 95% at ₹ 26mln against at ₹ 529mln mainly due to higher cost and lower than expected realisations. Cement EBIT margins stood at 0.6% (Q2FY11 – 12.2%). Jute segment EBIT margin witness ~900bps y-o-y decline at 0.9% from 9.4% for year ago period. Mainly on account of foreign exchange fluctuation loss witnessed during the quarter.
- Company booked y-o-y higher depreciation due to commissioning of brown field expansions during the last year. Reported PAT dropped by 62% y-o-y to ₹ 262mln which also was down sequentially by 77% ₹ 1119mln in Q1FY12.
- Basic EPS for the quarter stood at ₹ 3.4 (Q2FY11 – ₹ 8.9) which was way below our expectation of ₹ 9.01 for the quarter.
- Birla Corp Board declared an Interim Dividend of ₹ 2.5 per share.

Segmental break up

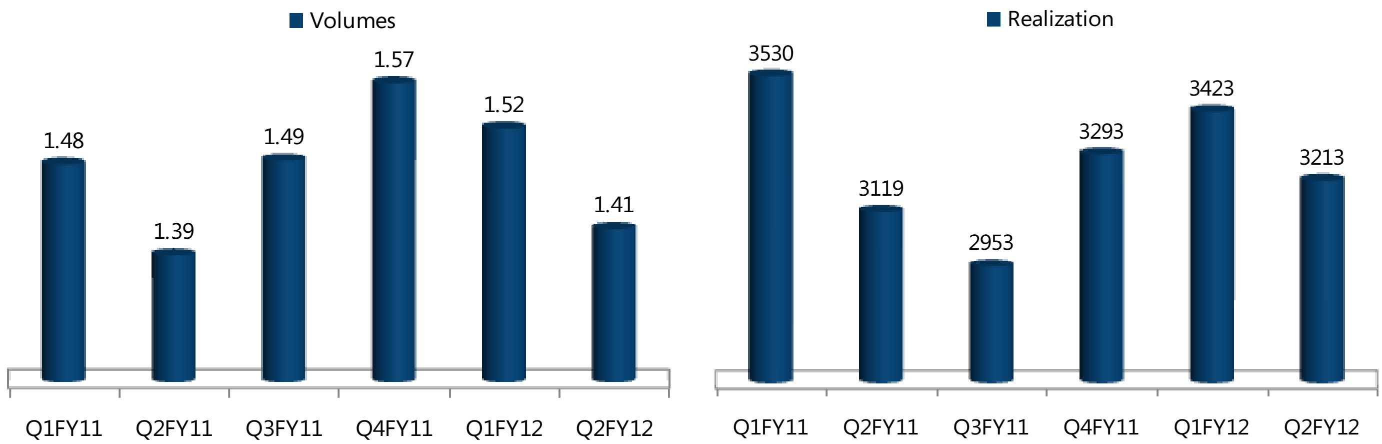
Key data (₹ mln)	Q2FY12	Q2FY11	Y-o-Y	Q1FY12	Q-o-Q
Cement Revenue	4539.9	4319.8	5.1%	5202.2	-12.7%
Jute Revenue	589.9	496.6	18.8%	355.0	66.2%
Power Revenue	538.90	405.90	32.8%	521.10	3.4%
Others	30.00	28.40	5.6%	32.40	-7.4%
Total	**5698.7**	**5250.7**	8.5%	**6110.7**	-6.7%
Less: Inter Segment Rev	-543.40	-407.70	33.3%	-525.40	3.4%
Add: other op. income	33.40	76.50	-56.3%	78.20	-57.3%
Net Revenue	**5188.70**	**4919.50**	5.5%	**5663.50**	-8.4%
EBIT & % to sales					
Cement EBIT	25.8	528.5	-95.1%	1197.3	-97.8%
Cement EBIT%	0.6%	12.2%	-1170bps	23.0%	-2240bps
Jute EBIT	5.3	46.6	-88.6%	-12.5	-142.4%
Jute EBIT%	0.9%	9.4%	-850bps	-3.5%	440bps%
Power EBIT	216	177.6	21.6%	256.3	-15.7%
Power EBIT%	40.1%	43.8%	-370bps	49.2%	-910bps
Others	-8.3	-8	3.8%	-4.1	102.4%

Source: Company, MSFL Research

Cement operational performance impacted by higher costs with lower than expected realisation

Company, like others faced acute cost side pressure where it incurred higher input, transportation, and other expenditure. Cost and availably of coal is a continued concern. Also higher clinker purchase has added further pressure on cement margins. Cement EBIT margins have seen a decline of ~11% points y-o-y at 0.6 %from 12.2% for Q2FY11. Volume growth of 2% is lower than its peers and also on realisation front; company reported a moderate growth of 3% at ₹ 3213.

Exhibit 2: Cement Volume/ Realisation Trend

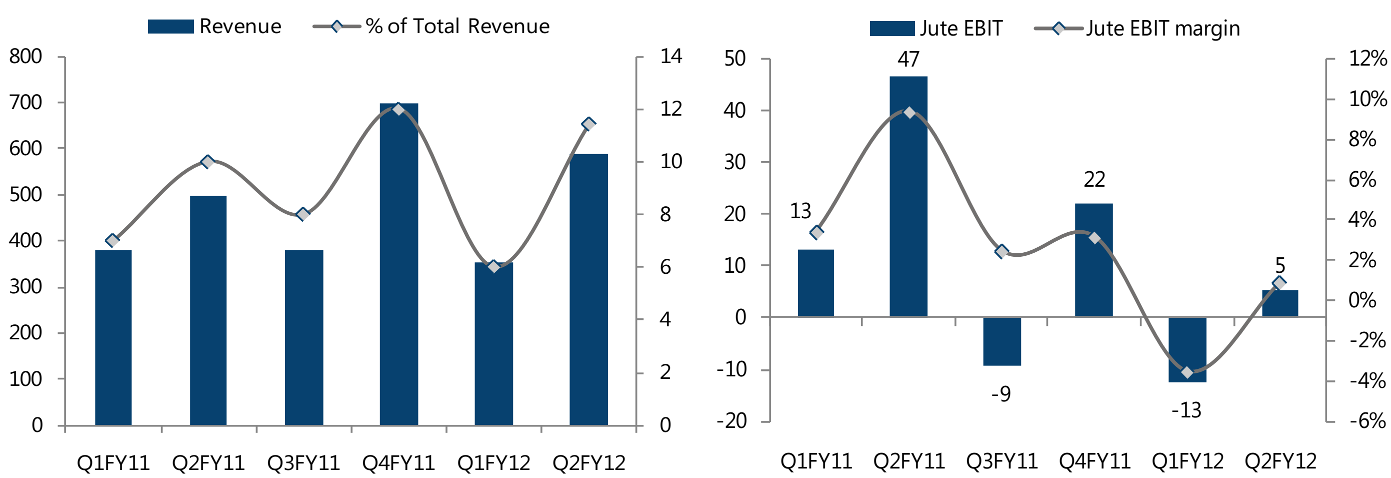


Source: CMA, MSFL Research

Jute business reported sequential improvement

Birla Corporation's Jute division has reported 19% y-o-y and 66% sequential growth for the quarter at ₹ 589mln on the back of higher realisations. Jute segment contributed around 11% to the total revenue. Jute EBIT was seen at ₹ 5.3mln against ₹ 47mln for Q2FY11. And EBIT margins stood at 0.9% against 9.4% for the year ago period. Operating performance of the Jute division was suffered mainly on account of foreign exchange fluctuation loss. With the proposed upgrading of machinery through modernisation programme, performance of Jute division is expected to improve subsequently going ahead.

Exhibit 3: Jute business trend



Source: Company, MSFL Research

Expansion update

- Work on 1.2mt brown field expansion at Chanderia and 0.6mt grinding unit at Durgapur is progressing well. These projects will be completed by the end of this fiscal and will take company capacity to 9.3mt post completion.
- Company has applied to Ministry of Environment and Forest, New Delhi for further capacity expansion of 1.5mt at Chanderia and the process for all necessary approvals is underway.

Outlook and Valuation

We expect weakness in sector sentiment to continue for next couple of quarters in terms of slow pace of demand recovery, unchanged status on infra and realty projects and resultant volatile pricing scenario on account of which margins of players are expected to be under continued pressure. Additional mining tax, rise in rail freight surcharge and continued concern on cost and availability of coal are likely to add further pressure on operating performance of players. Potential threat of CCI investigation and subsequent action looms large on the industry which is an added concern and negative for sector sentiment.

We expect Birla Corp to face continued headwinds in terms of higher clinker costs in the light of pending court case on mining issue in Rajasthan. We expect gradual recovery in demand and also sequential improvement in realisations considering the recent rounds of price hikes. Birla Corp has strong presence into Central, Northern and Eastern regions and hence is likely to benefit more from the recent price and demand recovery witnessed in these regions. Due to favourable regional mix and upcoming capacity we continue to like Birla Corp which is currently trading at very attractive valuations.

We have lowered our EPS estimates for FY12P and FY13P to ₹ 42.3 and ₹ 51.6 respectively to factor in high cost impact. At ₹ 315 the stock trades attractively at 4.6 x EV / EBITDA of FY13P. We have shifted our valuation base from FY12P to FY13P and also have revised rupee dollar assumption upwards to 47. Maintain BUY with target price of ₹ 387 valuing it at 5.5 x EV/EBITDA of FY13P.

Financial Summary

Profit & Loss

Particulars (₹ in mln)	2009	2010	2011	2012P	2013P
Sales	**17907**	**21984**	**21622**	**24854**	**29384**
Total Expenditure	13647	14518	17091	20092	23469
EBIDTA	**4259**	**7466**	**4531**	**4762**	**5915**
EBIDTA Margin (%)	23.8	34.0	21.0	19.2	20.1
Depreciation	434	556	648	801	1001
EBIT	3825	6910	3882	3962	4915
Interest cost	220	270	526	597	726
Operating Profit	3604	6640	3356	3365	4189
Other Income	760	968	1020	1100	1250
PBT	**4365**	**7608**	**4377**	**4465**	**5439**
Current Tax	1010	2013	847	1206	1468
PAT	**3235**	**5572**	**3199**	**3260**	**3970**
PAT Margin (%)	18.1	25.3	14.8	13.1	13.5
EPS	42.0	72.4	41.5	42.3	51.6
Sales Growth (%)	3.8%	22.8%	-1.7%	15.0%	18.2%
EBITDA Growth (%)	-26.2%	75.3%	-39.3%	5.1%	24.2%
PAT Growth (%)	-18%	72%	-43%	2%	22%

Key Assumptions

Particulars (₹ in mln)	2009	2010	2011	2012P	2013P
Volume	5.3	5.6	5.9	6.5	7.3
Realization /tonne	3524	3982	3237	3335	3536
Raw Material (Limestone)	238	218	248	257	265
Raw Material (Gypsum)	1410	1566	1663	1796	1886
Raw Material (Fly ash)	411	443	461	480	494

Balance Sheet

Particulars (₹ in mln)	2009	2010	2011	2012P	2013P
Sources of Funds					
Share Capital	770	770	770	770	770
Reserves & Surplus	12107	17142	19809	22531	25964
Networth	**12877**	**17912**	**20579**	**23301**	**26734**
Secured Loans	2194	5182	7706	10156	12197
Unsecured Loans	570	1910	2452	3100	3930
Total Loans	**2764**	**7092**	**10158**	**13256**	**16127**
Deferred Tax Liability	772	795	1125	1125	1125
TOTAL	**16414**	**25799**	**31862**	**37682**	**43986**
Application of Funds					
Net Fixed Assets	8019	10265	14644	**20343**	**25842**
Investment	5523	11417	11692	10192	9192
Current Assets	6837	8418	10559	12525	14741
Current Liabilities	3965	4299	5032	5378	5789
Net Current Assets	**2872**	**4118**	**5527**	**7147**	**8952**
TOTAL	**16414**	**25799**	**31862**	**37682**	**43986**

Cash Flows

Particulars (₹ in mln)	2009	2010	2011	2012P	2013P
Internal Accruals	3669	6128	3847	4060	4971
Inc./ (Dec) in Net Current Assets	-835	1051	1090	1349	1492
Cash flow from Operations	**4504**	**5077**	**2757**	**2712**	**3479**
Inc. in debt	42	4327	3066	3098	2871
Inc. in equity	0	0	0	0	0
Dividend and others	405	540	538	538	538
Cash flow from financing	**-364**	**3788**	**2528**	**2560**	**2333**
Fixed asset formation	1960	2617	4825	6500	6500
Inc. in Investments	-817	5894	276	-1500	-1000
Cash flow from Investment	**1142**	**8511**	**5100**	**5000**	**5500**
Net Change in cash	**2998**	**354**	**185**	272	312

Ratios

Valuation Ratio	2009	2010	2011	2012P	2013P
P/E	4.2	5.5	8.3	7.4	6.1
P/BV	1.1	1.7	1.3	1.0	0.9
EV/EBIDTA	1.8	3.1	4.7	4.9	4.6
EV/Sales	0.4	1.0	1.0	0.9	0.9
Dividend Yield (%)	2.5	1.5	1.7	1.9	1.9
EPS	42.0	72.2	41.6	42.3	51.6
DPS	4.5	6.0	6.0	6.0	6.0
Book Value	167	233	267	303	347
RONW	28%	36%	17%	15%	16%
ROCE	24%	29%	13%	11%	12%
Solvency Ratio (x)					
Debt/Equity	0.2	0.4	0.5	0.6	0.6
Debt/EBIDTA	0.6	0.9	2.2	2.8	2.7
Turnover Ratio (x)					
Asset Turnover	2.5	2.4	1.7	1.4	1.3
Current Ratio	1.7	2.0	2.1	2.3	2.5
Inventory (days)	40	40	54	63	71
Debtors (days)	5	3	6	6	4

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Key ratings:

Rating	Expected Return
Buy	> 15%
Accumulate	5 to 15%
Hold	-5 to 5%
Sell	< -5%
Not Rated	-

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