Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Grasim Industries Ltd

Operational profitability recovers sequentially; retain Buy

Diversified	Sharekhan code: GRASIM

Reco/View: Buy	↔	CMP: Rs. 1,831	Price Target: Rs. 2,150	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 42.75

Updated Aug 08, 2023

Severe Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

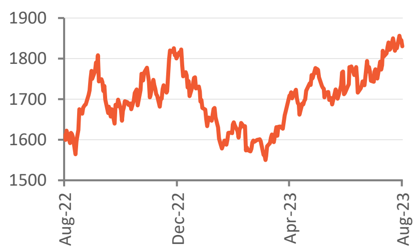
Company details

Market cap:	Rs. 1,20,526 cr
52-week high/low:	Rs. 1,867 / 1,528
NSE volume: (No of shares)	27.8 lakh
BSE code:	500300
NSE code:	GRASIM
Free float: (No of shares)	37.7 cr

Shareholding (%)

Promoters	42.8
FII	16.2
DII	17.1
Others	23.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.0	3.2	11.9	13.6
Relative to Sensex	4.5	-2.9	3.6	2.0

Sharekhan Research, Bloomberg

Summary

- Grasim Industries Limited (Grasim) reported a better-than-expected standalone operational performance for Q1FY2024 led by a sharp q-o-q recovery in Viscose OPMs while Chemical lagged.
- Viscose division to hold margins while Chemical might slide in the near term as Q1 exit prices tread lower compared to average Q1. Domestic slowdown in China remains a hangover on global prices.
- Paints operations are on track to commence from Q4FY2024. B2B e-commerce business launched across three states. Net Debt to inch up with high capex spends over the next two years.
- We retain Buy on Grasim with a revised PT of Rs. 2,150, as we pencil in upwardly revised UltraTech valuation and increased Aditya Birla Capital valuation.

Grasim Industries Limited (Grasim) reported a better-than-expected standalone operational performance for Q1FY2024, led by a sharp q-o-q recovery in Viscose margins while Chemical performance lagged. Standalone revenue (down 14% y-o-y at Rs. 6,238 crores) was marginally below our estimate, with lower realisations affecting both Viscose (revenues down 17% y-o-y) and chemical (down 22% y-o-y) divisions. Overall, Sluggish demand led marginal 5% y-o-y volume growth in chemicals while Viscose reported a 5% y-o-y dip. Standalone OPM surprised positively at 10.8% (down 741 bps y-o-y) owing to a sharp sequential recovery in Viscose margins (up 706 bps q-o-q) while chemical division margins lagged (up 133 bps q-o-q). Overall, standalone operating profit/adjusted net profit was down 49%/56% y-o-y at Rs. 673 crore/Rs. 355 crore, although higher than our estimates. Grasim remains on track to commercially launch the paints business beginning Q4FY2024 in phases. The B2B e-commerce business was found this month, catering markets across Maharashtra, M.P. and Delhi. FY2024 is expected to see high capex spends of Rs. 5791 crore (including Rs. 4283 capex towards paints), majorly funded through debt.

Key positives

- Viscose reported marquee improvement in operational profitability with EBITDA growth of 171% q-o-q to Rs. 390 crore, led by over 700 bps q-o-q margin improvement.
- B2B e-commerce business gets launched this month. It remains on track to start commercial operations in Paints from Q4FY2024 with 630 million litres capacity.

Key negatives

- The chemical division performance surprised negatively, led by a sustained dip in caustic prices. EBITDA margins were lower, almost 1300 bps y-o-y at 16.7%.
- Net Debt rise by Rs. 1735 crore q-o-q to Rs. 3515 crore, led by a capital infusion of Rs. 1000 crore in Aditya Birla Capital and Rs. 1000 crore capex incurred in Paints.

Management Commentary

- Viscose margins are seen bottoming out. Viscose prices reduced since June end, as have raw material prices. Chemical margins may tread lower in Q2 as exit caustic prices were lower than average Q1.
- FY2024 is expected to be a year with high capex spend. Incremental capex requirements would be met through debt. Hence, peak gross debt could be Rs. 8000-10000 crore, although net debt would be lower due to cash balance of Rs. 3000 crores.
- The commercial operations is on track to commence from Q4FY2024. Out of the six plants, two plants would be operational this year. Paints capacity is expected to be 630 million litres by FY2024 end out of the total capacity plan of 1.3 billion.

Revision in estimates – We have marginally lowered our forecasts for FY2024-FY2025.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 2,150: Grasim's standalone businesses are expected to face near-term muted demand and pressure on OPMs, especially in the chemical business. However, its efforts to increase asset productivity and focus on increasing value-added products are expected to yield results as the demand environment recovers. The company's expedited paints expansion will likely provide it with the next leg of growth. Further, the outlook for its key subsidiary UltraTech remains healthy. We maintain Buy on the stock with a revised price target (PT) of Rs. 2,150, as we pencil in the upwardly revised valuation of UltraTech (as per report dated July 3, 2023) and an increased valuation of Aditya Birla Capital.

Key Risks

The funding requirement of its group companies and weakness in standalone business are key risks.

Valuation (Standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
Revenue	20,857	26,840	26,428	29,615
OPM (%)	15.4%	11.8%	12.4%	13.8%
Adjusted PAT	2,348	2,212	1,947	2,360
% YoY growth	163.4	(5.8)	(12.0)	21.2
Adjusted EPS (Rs.)	35.7	33.6	29.6	35.9
P/E (x)	51.3	54.5	61.9	51.1
P/B (x)	2.5	2.6	2.5	2.4
EV/EBITDA (x)	27.4	29.5	29.2	23.6
RoNW (%)	4.8	4.7	4.0	4.7
RoCE (%)	4.5	4.1	3.5	4.0

Source: Company; Sharekhan estimates

A sharp recovery in Viscose margins q-o-q leads to better-than-expected operational performance

Grasim reported a better-than-expected operational performance in its standalone net earnings, led by better-than-expected operational performance in the VSF division. In contrast, chemical and textiles reported subdued performance. Standalone revenue (down 14% y-o-y at Rs. 6,238 crore) was marginally lower than estimated with revenues in Viscose and Chemicals division reporting de-growth of 17% y-o-y and 22% y-o-y. Both divisions were affected by dip in Viscose and Caustic prices led by a volatile global macro environment and lower Chinese domestic demand. Standalone OPM surprised positively at 10.8% (down 741 bps y-o-y), owing to a sharp q-o-q expansion in Viscose OPM (up 706 bps q-o-q to 10.9%). However, chemical OPMs came in lower than estimated at 16.7% (down 1281 bps y-o-y, up 133 bps q-o-q). Overall, standalone operating profit/adjusted net profit declined 49%/56% y-o-y at Rs. 673 crore/Rs. 355 crore, but were higher than our estimates.

Key Conference Call Takeaways

- **Q1FY24 performance:** Consolidated revenues were up 11% y-o-y at Rs. 31065 crore, led by 17% y-o-y and 26% y-o-y revenue growth in Ultratech and Aditya Birla Capital, while standalone revenues declined by 14% y-o-y. Consolidated EBITDA declined by 5% y-o-y at Rs. 4981 crore due to the decline in EBITDA in Standalone business and Ultratech. Standalone revenues declined by 14% y-o-y at Rs. 6238 crore, while EBITDA declined by 42% y-o-y at Rs. 789 core due to high base (high Viscose and Caustic soda realisations last year). Strong sequential recovery in VSF was offset by subdued chemical and textile performance. It generated Rs. 256 crore free cash flows.
- **Net Debt:** Its net debt increased to Rs. 3515 crore. It invested Rs. 1000 crore in Aditya Birla Capital via preferential allotment.
- **Capex:** The budgeted capex for FY2024 is Rs. 5791 crore of which Rs. 4283 crore is towards paints. It incurred Rs. 1380 crore capex in Q1FY2024. FY2024 is expected to be a year with high capex spend. Incremental capex requirements would be met through debt. Hence, peak gross debt could be Rs. 8000-10000 crore, although net debt would be lower due to cash balance of Rs. 3000 crores.
- **Paints:** The commercial operations is on track to commence from Q4FY2024. Out of the six plants, two plants would be operational this year. Paints capacity is expected to be 630 million litres by FY2024 end out of the total capacity plan of 1.3 billion.
- **B2B business:** It launched an e-commerce website this month catering to markets across Maharashtra, M.P. and Delhi. It has onboarded 130 brands.
- **Viscose performance:** Revenues declined by 17% y-o-y at Rs. 3584 crore. EBITDA declined by 22% y-o-y at Rs. 390 crore. It operated at 90% capacity utilisation due to one-month plant shutdown caused by fire. Cotton prices declined by 41% y-o-y and 4% q-o-q for Q1FY2024. Pulp, caustic and coal prices saw correction both y-o-y and q-o-q while realisations fell too. International VSF prices have reduced since June end, while raw material prices have also declined. VSF margins are expected to be bottoming out. It is expected to maintain its 95% market share in VSF.
- **Chemical performance:** Caustic prices declined to $395 from $769 a year ago. It reported volume growth of 5% y-o-y while overall revenues declined by 22% y-o-y at Rs. 2146 crore. Exit caustic prices are lower than average Q1FY2024 prices. Chemical margins are expected to be lower compared to the average Q1.
- **Textile division:** The segment saw an 11% y-o-y decline in revenues at Rs. 549 crore. India's exports of textiles dipped 10% y-o-y and 9% q-o-q for Q1FY2024. Domestic demand for apparel remained sluggish.

Results (Standalone) Rs cr

Particulars	Q1FY24	Q1FY23	Y-o-Y %	Q4FY23	Q-o-Q %
Net sales	**6,237.6**	**7,253.0**	**(14.0)**	**6,645.8**	**(6.1)**
Total expenditure	5,564.2	5,932.8	(6.2)	6,219.8	(10.5)
Operating profit	**673.4**	**1,320.2**	**(49.0)**	**426.0**	**58.1**
Other Income	115.9	43.7	165.1	116.4	(0.5)
EBIDTA	789.2	1,363.9	(42.1)	542.5	45.5
Interest	105.7	86.7	21.9	106.7	(1.0)
PBDT	683.5	1,277.3	(46.5)	435.7	56.9
Depreciation	287.8	255.1	12.8	300.5	(4.2)
Extraordinary item	-	-	-	-	-
PBT	**395.8**	**1,022.1**	**(61.3)**	**135.3**	**192.6**
Tax	40.5	213.6	(81.0)	41.8	(3.0)
Reported PAT	**355.3**	**808.6**	**(56.1)**	**93.5**	**279.9**
Extraordinary item	-	-	-	-	-
Adjusted PAT	**355.3**	**808.6**	**(56.1)**	**93.5**	**279.9**
EPS (Rs.)	5.4	12.3	(56.1)	1.4	279.9
Margin (%)			**BPS**		**BPS**
Operating margin	10.8%	18.2%	-741	6.4%	438
Net Margin	5.7%	11.1%	-545	1.4%	429
Tax rate	10.2%	20.9%	-1066	30.9%	-2064

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Standalone business faces near-term challenges

Grasim is facing a subdued demand environment in its standalone businesses, led by global oversupply and volatility in the pricing environment. However, the viscose demand environment is expected to remain stable with gradual improvement in OPM. The chemical division's performance would be determined by global demand and pricing environment. The outlook for its key subsidiary, UltraTech, remains healthy, with expected demand from government-led infrastructure investments and sustained market from rural and individual home builders.

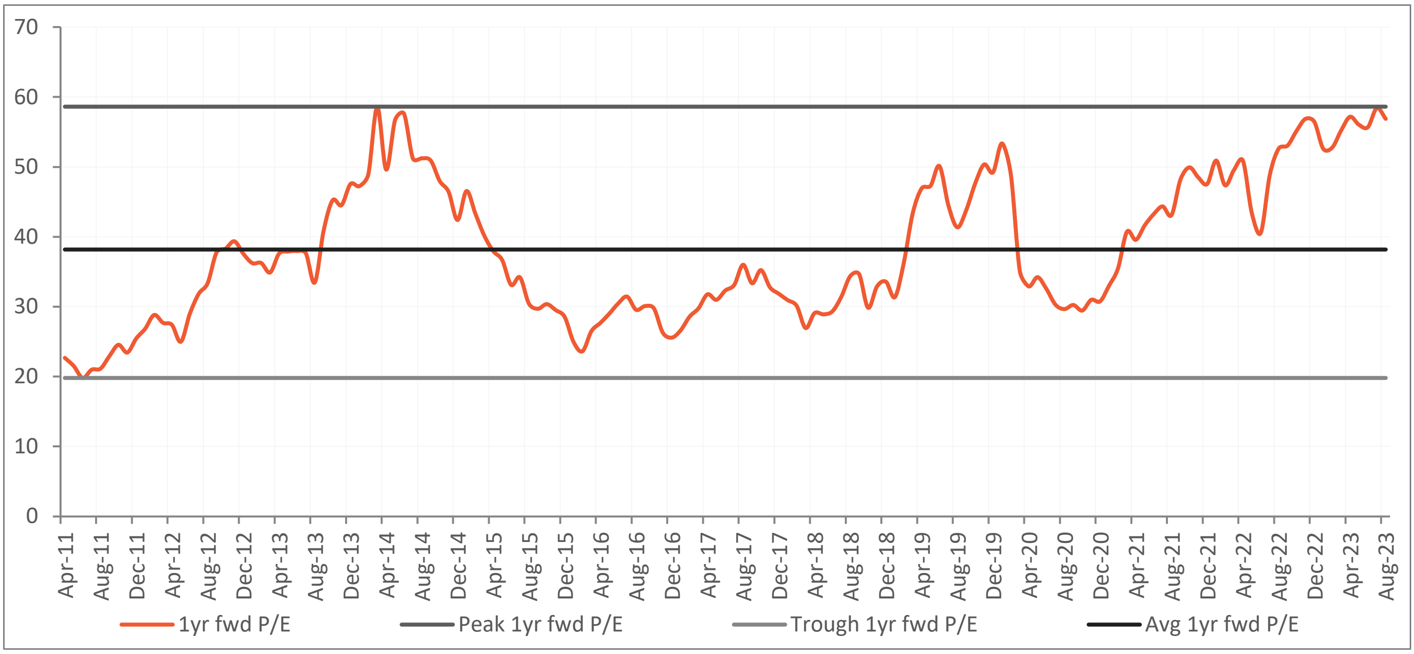
■ Company Outlook – Healthy outlook for key subsidiary and paints venture

Grasim is benefiting from the healthy growth outlook in its key subsidiary, UltraTech, while its standalone businesses are expected to face near-term subdued demand and volatility in OPMs. The company would focus on increasing asset productivity and the share of value-added products to improve operating margins in the viscose and chemical divisions. The company's venture into the paints business will provide scale and growth and reduce the cyclicality of the standalone business. Grasim is venturing into the decorative paints business with an investment of Rs. 10,000 crore by FY2025. Hence, a healthy growth outlook in UltraTech and a venture into paints are expected to drive valuation.

■ Valuation – Retain Buy with a revised PT of Rs. 2,150

Grasim's standalone businesses is expected to face near-term muted demand and pressure on OPMs, especially in the chemical business. However, its efforts to increase asset productivity and focus on increasing value-added products are expected to yield results as the demand environment recovers. The company's expedited paints expansion will likely provide it with the next leg of growth. Further, the outlook for its key subsidiary UltraTech remains healthy. We maintain Buy on the stock with a revised price target (PT) of Rs. 2,150, as we pencil in the upwardly revised valuation of UltraTech (as per report dated July 3, 2023) and an increased valuation of Aditya Birla Capital.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Grasim is the flagship company of Aditya Birla Group. The company started as a textiles manufacturer in India in 1947. The cement business was started in 1985 with a capacity of 0.5 MTPA. Aditya Birla Nuvo Limited, an Aditya Birla Group Company, was merged with Grasim w.e.f. July 1, 2017. Subsequently, the financial services business was demerged from the merged entity and was listed on the bourses as Aditya Birla Capital Limited (ABCL) on September 1, 2017. Currently, the company is a leading global player in VSF and is India's largest chemicals chemical (Chlor-Alkalis), cement, and diversified financial services (NBFC, Asset Management, and Life Insurance) player.

Investment theme

Grasim benefits from an improved domestic demand environment for its key standalone businesses, led by a pickup in demand from end-user industries. The same has led to increased capex expenditure and expansion in both verticals. Further, management's clarity on capital allocation, with priority to the standalone business and nil future investment for listed telecom investment, removes a key hangover on the stock. The company's venture into the paints business will provide scale and growth and reduce the cyclicality of the standalone business. Further, UltraTech's growth outlook remains buoyant, which comprises over 70% of Grasim's SOTP valuation.

Key Risks

- Funding requirements of its other listed entities.
- Pressure on VSF and chemical division's demand and/or realisations negatively affects profitability.
- Higher holding company discounts for any of its other businesses such as telecom, cement, and financial services.

Additional Data

Key management personnel

Kumar Mangalam Birla	Chairman
H K Agarwal	Managing Director
Pavan K Jain	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Birla Group Holdings Pvt Ltd	18.99
2	Life Insurance Corp of India	9.35
3	IGH Holdings Pvt Ltd	6.45
4	Hindalco Industries Ltd	4.29
5	Umang Commercial Co Ltd	4.06
6	Pilani Investment & Industries Cor	3.75
7	Vanguard Group Inc/The	2.23
8	GOVERNMENT PENSI	1.93
9	Norges Bank	1.92
10	SHAMYAK INVESTMENT PRIVA	1.40

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

DISCLAIMER

This information/document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This information/ document is subject to changes without prior notice.

Recommendation in reports based on technical and derivatives analysis is based on studying charts of a stock's price movement, trading volume, outstanding positions, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals. However, this would only apply for information/document focused on technical and derivatives research and shall not apply to reports/documents/information focused on fundamental research.

This information/document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this information/report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved) and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other recommendations/ reports that are inconsistent with and reach different conclusions from the information presented in this recommendations/report.

This information/recommendation/report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst might have dealt or traded directly or indirectly in securities of the company and that all the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst and SHAREKHAN further certifies that either he or his relatives or Sharekhan associates might have direct or indirect financial interest or might have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report. The analyst and SHAREKHAN encourages independence in research report/ material preparation and strives to minimize conflict in preparation of research report. The analyst and SHAREKHAN does not have any material conflict of interest or has not served as officer, director or employee or engaged in market making activity of the company. The analyst and SHAREKHAN has not been a part of the team which has managed or co-managed the public offerings of the company, and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Ltd or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Forward-looking statements (if any) are provided to allow potential investors the opportunity to understand management's beliefs and opinions in respect of the future so that they may use such beliefs and opinions as one factor in evaluating an investment. These statements are not a guarantee of future performance and undue reliance should not be placed on them. Such forward-looking statements necessarily involve known and unknown risks and uncertainties, which may cause actual performance and financial results in future periods to differ materially from any projections of future performance or result expressed or implied by such forward-looking statements. Sharekhan/its affiliates undertakes no obligation to update forward-looking statements if circumstances or management's estimates or opinions should change except as required by applicable securities laws. The reader/investors are cautioned not to place undue reliance on forward-looking statements and use their independent judgement before taking any investment decision.

Investment in securities market are subject to market risks, read all the related documents carefully before investing. The securities quoted are for illustration only and are not recommendatory. Registration granted by SEBI, and certification from NISM in no way guarantee performance of the intermediary or provide any assurance of returns to investors.

Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on www.sharekhan.com

---

Registration and Contact Details: Name of Research Analyst - Sharekhan Limited, Research Analyst Regn No.: INH000006183. CIN): - U99999MH1995PLC087498. Registered Office: The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA. Tel: 022-6115000.

Correspondence/Administrative Office: Gigaplex IT Park, Unit No 1001, 10th Floor, Building No.9, TTC Industrial Area, Digha, Airoli-West, Navi Mumbai – 400 708. Tel: 022 61169000 / 61150000, Fax No. 61169699.

Other registrations of Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/ CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669.

Compliance Officer: Ms. Binkle Oza; Tel: 022-62263303; email id: complianceofficer@sharekhan.com

For any complaints/grievance, email us at igc@sharekhan.com or you may even call Customer Service desk on - 022- 41523200/022 - 33054600