Stock Update

Company Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Grasim Industries Ltd

Rights issue to balance leverage and growth

Diversified	Sharekhan code: GRASIM
Reco/View: Buy ⇔	CMP: Rs. 2,079
	Price Target: Rs. 2,300 ⇔

↑ 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		⇔	

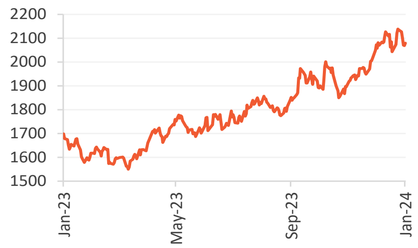
Company details

Market cap:	Rs. 1,36,898 cr
52-week high/low:	Rs. 2176/1528
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	16.1
DII	17.3
Others	23.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	0.3	10.0	16.9	22.4
Relative to Sensex	-3.6	0.3	6.8	3.1

Sharekhan Research, Bloomberg

Summary

- We retain Buy on Grasim with an unchanged PT of Rs. 2,300, considering a healthy growth outlook for its key subsidiaries and standalone businesses.
- The company announced terms for Rs. 4,000 crore rights issue at an issue price of Rs. 1,812 per share, entailing 3.4% equity dilution in-line with street's expectations.
- Repayment of debt from the rights issue along with funding balance capex for paints of over Rs. 5,200 crore via a mix of D/E would keep standalone leverage under check and under management's stated guidance.
- It remains on track to set up six units with an aggregate capacity of 1332 MLPA by Q4FY2025 with three units to commence operations from Q4FY2024. We expect the paints business to be earnings accretive from FY2026.

Grasim's board has announced the terms for its upcoming ~Rs. 4,000 crore rights issue at an issue price of Rs. 1,812 per rights equity share, which is at ~12% discount (LTP as of January 4, 2024), which would entail 3.4% equity dilution. The rights entitlement ratio is 6 rights equity shares for every 179 fully paid-up equity shares. The repayment of ~Rs. 3,000 crore debt from the rights issue along with the balance capex left for paints of ~Rs. 5,231 crore till Q4FY2025 (likely to be done through a mix of D/E) would keep its standalone leverage under check and in line with management's upper cap of net debt to EBITDA of 3.5x post FY2025. Further, it remains on track to commission six plants in phases with an aggregate capacity of 1332 MLPA by Q4FY2025, with three plants slated to commence operations in Q4FY2024. We expect the paints business to be earnings accretive from FY2026.

- **Rights issue terms finalised:** On January 4, 2024, the company's board announced the terms for its 2.2 crore rights issue aggregating ~Rs. 4,000 crore at an issue price of Rs. 1,812 (~12% discount to LTP on January 4, 2024). The equity dilution at 3.4% is in line with market expectations with an entitlement ratio of 6 rights shares against 179 fully paid-up equity shares. The record date is January 10, 2024, and investors will have to pay in four installments (including on application) on or prior to March 2026. The promoters remain committed with subscription to the full extent of their Rights Entitlements and additional rights equity shares, if any, which may remain unsubscribed in the issue. Out of the net proceeds, Rs. 3,000 crore is earmarked for repayment/prepayment of borrowings.
- **Rights issue to keep leverage under check:** Grasim has frontloaded its capex, especially for paints in which it has incurred Rs. 4,908 crore capex till Q2FY2024 out of the ~Rs. 10,139 crore earmarked for the business. The same has led to increased net debt to TTM EBITDA (including other income), which stood at 1.39x as of Q2FY2024 compared with 0.41x as of FY2023-end. The repayment of ~Rs. 3,000 crore debt from the rights issue along with the balance capex of ~Rs. 5,231 crore till Q4FY2025 (likely to be done through a mix of D/E) would keep its standalone leverage under check and in line with management's upper cap of net debt to EBITDA of 3.5x post FY2025.
- **Paints to be earnings accretive from FY2026:** Grasim remains on track to complete six plants with an aggregate capacity of 1332 MLPA, which will be commissioned in a phased manner from Q4FY2024 under the brand 'Birla Opus.' It has received the consent to operate its paints manufacturing plants at 1) Panipat, Haryana, 2) Ludhiana, Punjab, and 3) Cheyyar, Tamil Nadu, and their operations are expected to commence in Q4FY2024. We expect the paints business to be earnings accretive from FY2026.

Our Call

Valuation – Retain Buy with an unchanged PT of Rs. 2,300: Grasim's standalone businesses are expected to face muted demand in the near term and pressure on OPMs, especially in the chemicals business. However, its efforts to increase asset productivity and focus on increasing value-added products are expected to yield results as demand recovers. The company's expedited paints expansion along with strong traction being witnessed in the B2B e-commerce business are likely to provide it with the next leg of growth. Further, the outlook for its key subsidiary, UltraTech, remains healthy. We maintain our Buy rating with an unchanged price target (PT) of Rs. 2,300.

Key Risks

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

Valuation (Standalone) Rs cr

Particulars	FY23	FY24E	FY25E	FY26E
Revenue	26,840	24,552	27,180	29,451
OPM (%)	11.8%	11.6%	13.8%	13.9%
Adjusted PAT	2,212	1,770	2,096	2,187
YoY growth (%)	(5.8)	(20.0)	18.4	4.4
Adjusted EPS (Rs.)	33.6	26.9	31.9	33.2
P/E (x)	61.9	77.3	65.3	62.6
P/B (x)	2.9	2.8	2.8	2.7
EV/EBITDA (x)	34.6	39.5	30.3	28.0
RoNW (%)	4.7	3.7	4.2	4.3
RoCE (%)	4.1	3.2	3.6	3.6

Source: Company; Sharekhan estimates

Terms of ~Rs. 4,000 crore rights issue finalised

The company's board approved the terms of the rights issue in its meeting on January 4, 2024. The company intends to issue up to 2,20,73,935 partly paid-up equity shares (rights equity shares) of face value of Rs. 2 each for cash at a price of Rs. 1,812 per rights equity share (including a premium of Rs. 1,810 per rights equity share) aggregating up to Rs. 3,999.80 crore on a rights basis to the eligible equity shareholders of the company in the ratio of 6 rights equity shares for every 179 fully paid-up equity share held by the eligible equity shareholders on the record date, that is on Wednesday, January 10, 2024 (record date). Opening and closing dates of the rights issue are Wednesday, January 17, 2024, and Monday, January 29, 2024, respectively. The on-market renunciation period is Tuesday, January 23, 2024. Assuming full subscription to the rights issue, the outstanding equity shares post the issue aggregates to 68,06,13,006 equity shares, which is a dilution of 3.35%.

The Promoters and Promoter Group will subscribe to the full extent of their Rights Entitlements and subscribe to additional rights equity shares, if any, which may remain unsubscribed in the issue.

The issue price is Rs. 1,812 per rights equity share. Investors will have to pay Rs. 453 per rights equity share (25% of Issue Price) on application and the balance Rs. 1,359 per rights equity share (75% of the issue price) in up to three additional calls, to be completed on or before March 2026.

Terms of payment

Due Date	Face Value (Rs.)	Premium (Rs.)	Total (Rs.)
On Application	0.5	452.50	453.00
Up to three additional calls, with terms and conditions such as the number of calls and the timing and quantum of each call as may be decided by its board/rights issue committee from time to time, to be completed on or before March 2026	1.5	1357.50	1359.00
Total	**2.0**	**1810.00**	**1812.00**

Source: Company's LOI

Issue Schedule

Last Date for the credit of rights entitlements	Tuesday, January 16, 2024
Issue opening date	Wednesday, January 17, 2024
Last date for on-market renunciation of rights entitlements	Tuesday, January 23, 2024
Issue closing date	Monday, January 29, 2024
Finalisation of basis of allotment (on or about)	Wednesday, February 7, 2024
Date of allotment (on or about)	Thursday, February 8, 2024
Date of credit (on or about)	Friday, February 9, 2024
Date of listing (on or about)	Monday, February 12, 2024

Source: Company's LOI

Objects of the issue

Particulars	Estimated amount (Rs. crore)
Repayment or prepayment, in full or in part, of certain borrowings availed by the company	3,000.00
General corporate purposes	977.65
Total Net Proceeds	**3,977.65**

Source: Company's LOI

Outlook and Valuation

■ Sector view - Standalone business faces near-term challenges

Grasim is facing subdued demand 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.

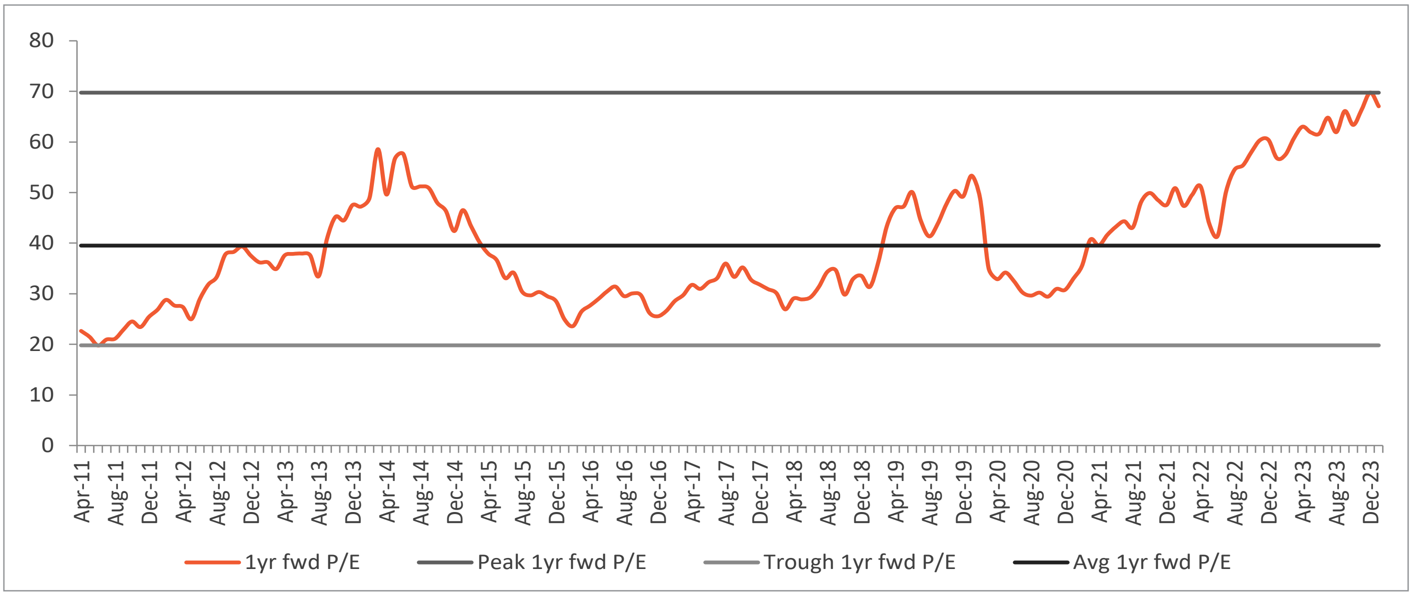
■ Company outlook - Healthy times ahead for key subsidiary and paints venture

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 OPM 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 an unchanged PT of Rs. 2,300

Grasim's standalone businesses are expected to face muted demand in the near term and pressure on OPMs, especially in the chemicals business. However, its efforts to increase asset productivity and focus on increasing value-added products are expected to yield results as demand recovers. The company's expedited paints expansion along with strong traction being witnessed in the B2B e-commerce business are likely to provide it with the next leg of growth. Further, the outlook for its key subsidiary, UltraTech, remains healthy. We maintain our Buy rating with an unchanged PT of Rs. 2,300.

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 (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 affect 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

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	The Vanguard Group Inc.	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

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