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YEARS

Initiating Coverage

Grindwell Norton Ltd.

09-April-2021





Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Engineering	Rs 925	Buy on dips to Rs 905-910 band and add further in Rs 820-825 band	Rs 993	Rs 1054	2 quarters

HDFC Scrip Code	GRINOR
BSE Code	506076
NSE Code	GRINDWELL
Bloomberg	GWN IN
CMP Apr 08, 2021 (Rs)	925.5
Equity Capital (cr)	55.4
Face Value (Rs)	5
Eq. Share O/S (cr)	11.1
Market Cap (Rs cr)	10246.6
Book Value (Rs)	107.2
Avg.52 Wk Volume	50,000
52 Week High (Rs)	980.0
52 Week Low (Rs)	441.4

Share holding Pattern % (Dec, 2020)	
Promoters	58.33
Institutions	20.18
Non Institutions	21.50
Total	100.0

Fundamental Research Analyst

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Our Take:

Grindwell Norton Ltd. (GNL) is a part of the High Performance Materials division, which is a part of the Innovative Materials Sector of the Saint-Gobain Group. GNL holds ~25% of the abrasives marketshare in India and derives 58% of its total revenue from the abrasives segment. GNL provides its expertise in the areas of innovation and co-development through a wide range of high-performance materials for demanding applications in diverse segments such as the automotive, health, defense, security and even the food & beverage industries. GNL enjoys the benefit of high quality R&D facilities of its parent Saint Gobain helping it with newer and better products to gain share in the highly competitive market. It is a cash rich company with no leverage and robust operating cash flows. In Abrasives, it is part of a duopoly market, being the No.2 player after Carborandum Universal. Capacity utilization of its facilities are ~60% on an average and there is enough headroom to accommodate growth over the next 3-4 years. GNL sees strategic relevance of exports for incremental growth, which contributes ~15% to topline. GNL aims to focus on exports of niche high value products in some cases to replace Chinese products and penetrate neighbouring countries of US, South East Asia markets and enter newer market to drive for stronger growth.

Valuations & Recommendation:

Revival in automotive, engineering and industrial activities would be key for the growth of the company. Changing product mix and high margin new initiatives of the company in performance plastics should aid in margin expansion. Going forward, GNL with its strong parentage and leadership in the domestic market with a proven track record and superior balance sheet provides comfort. We expect segment-wise 6.6%, 9.4% and 17.4% CAGR in abrasives, ceramics and new initiatives of the company over FY20E-FY23E resulting in EBITDA margin expansion of 200bps and RoE improvement to 17.6% from 16% in FY20. We believe GNL is well placed to further gain from gradual economic revival in key segments. Investors can buy the stock on dips to Rs 905-910 (37.5x FY23E EPS) and add further in Rs 820-825 (34x FY23E EPS) band for a base case fair value of Rs 993 (41x FY23E EPS) and bull case fair value is Rs 1054 (43.5x FY23E EPS) in the next two quarters.

Financial Summary

Particulars (Rs cr)	Q3FY21	Q3FY20	YoY-%	Q2FY21	QoQ-%	FY20	FY21E	FY22E	FY23E
Operating Income	457.7	410.0	11.6	439	4.2	1,579.6	1,582.4	1,755.0	1,992.6
EBITDA	98.0	69.1	41.8	94	4.7	264.5	295.9	326.4	372.6
APAT	65.9	46.3	42.5	64	2.6	182.5	207.0	229.1	268.1
Diluted EPS (Rs)	6.0	4.2	42.5	6	2.6	16.5	18.7	20.7	24.2
RoE (%)						16.0	16.6	16.6	17.6
P/E (x)						56.1	49.5	44.7	38.2
EV/EBITDA (x)						37.1	32.9	29.4	25.4

(Source: Company, HDFC sec)

Recent Triggers

Q3FY21 financials

GNL posted strong numbers for Q3FY21 driven by a revival in key end user industries like automobile, engineering and construction. Consolidated revenues witnessed a growth of 11.6% yoy to Rs 458cr aided by robust growth in ceramics and plastics segment. Revenues from abrasives segment grew 12% to Rs 265cr while ceramics and plastic segment witnessed a 18% yoy growth to Rs 155cr. Revenue share of abrasives, ceramics & plastics and new initiatives were at ~58%, ~34% & ~9%, respectively. Led by strong pricing power, gross margin jumped 174bps YoY (254bps QoQ) to 56.9%, the highest over the past ten quarters. GNL maintained its EBITDA margin sequentially at 21.4% (up 460bps YoY), the highest ever. EBITDA grew by 41.8% to Rs 98cr and EBITDA margins expanded ~460bps yoy to 21.4% mainly on account of lower raw material and power expenses. PAT grew 40.3% yoy to Rs 66cr despite lower other income.

Long term Triggers

Increasing share of higher margin Ceramics and Plastics segment

The Ceramics and Plastics segment of the company comprises of performance ceramics and refractories (PCR), manufacturing of silicon carbide, ADFORS (glass fiber technical fabrics) and performance plastics business. PCR business caters to specialized refractory and ceramic product applications that straddle across industry segments like primary and secondary metal (ferrous / non-ferrous) production, Heat Treatment, Waste to Energy Conversion, Insulators, Abrasives, Porcelain and Sanitary-ware. Specialized ceramic product based solutions are also used for Armour application (protection of human and vehicular bodies) and applications that require resistance to wear. Due to

its specialized nature the margins in this segment are higher and increasing share of this segment bodes well for the company. Over FY16-20, this segment had been a key driving force for GNL. It grew at CAGR 10.8% v/s overall GNL revenue growth of CAGR 6.8% for the same period while the revenue contribution of PCR grew from 27% in FY16 to 34% as on 9MFY21.

Capex cycle recovery to provide growth in abrasives business

Saint-Gobain is a major player worldwide in Abrasives. It has a strong product portfolio, a strong R&D set-up with projects in both basic and applied areas and global reach, with plants and marketing/sales organizations all over the world. GNL benefits from being a part of such an organization. GNL's Abrasives business markets and manufactures a full range of Bonded Abrasives, Coated Abrasives (including Non-woven Abrasives), Thin Wheels and Super-abrasives at its plants near Mumbai, Bangalore, Nagpur and Himachal Pradesh. Abrasives are consumable in nature and need to be replaced in the span on ~3 months (except for super abrasives). This replacement demand assures that even in a moderate investment environment, robust sales will continue from this segment. In 2018, Saint-Gobain's High Performance Solutions sector entered the Adhesives & Sealants business by acquiring Tekbond, a leading Adhesives & Sealants brand in Brazil. It has also entered the industrial market for Adhesives & Sealants in India by creating a new business vertical within GNL.

Diversified business model

GNL caters to diversified set of industries which protects its revenues from slowdown in any one of the industries. Its revenues are likely to be impacted only when there is an overall economic slowdown. In the abrasives segment, the company caters to industries like automobile, construction, housing, metal fabrication, etc while in ceramics & plastics, it caters to power plants, coal washeries, cement, glass and steel industries. The dependence on any single industry segment is less than 15%. GNL's largest customer accounts for less than 3% of total sales and its largest dealer accounts for less than 3% of its sales.

Strong support from parent

Abrasives have been used over a very long period of time and technological changes in terms of applications are gradual. GNL Abrasives is well positioned to anticipate and take advantage of these technological changes as Saint-Gobain is a World Leader in Abrasives with a very strong R&D Centre in the USA with regional R&D centers located elsewhere (including a new Centre in India). Both basic and applied research takes place at these R&D centers. GNL has full access to all the research and technology developments.

Cash rich company with clean balance sheet

GNL has been virtually debt free over a long period of time with good free cash flows and growing cash reserves. Even after meeting its maintenance capex over the years, company has managed to maintain a cash balance of around Rs 210-240cr. This abundant cash helps company grab any opportunity to available in the market to differentiate further in its products or to develop new facilities to supply newer and better products.

What could go wrong

Slowdown in end user industry

The resurgence of Covid pandemic could lead to a slowdown in industrial production which would impact sales of abrasives. Also, auto sector growth has slowed down as compared to recent past which might impact growth in performance plastics.

Technology obsolescence

Abrasives have been used over a very long period of time and technological changes in terms of applications are gradual.

Increasing competition

The Abrasives Market has clearly been evolving from two major players to multi-players. The competitive landscape has become much more dynamic.

GNL is dependent on raw material sourcing through imports being dependent on China for import of key raw materials like high grade alumina, bauxite, silicon carbide, etc. An increase in duty structure or other factors could impact the earnings estimates.

GNL leverages on the latest technology from its parent for which it pays royalty, license and trademark fees of 2.5% of sales. Any increase in the same could pose a risk.

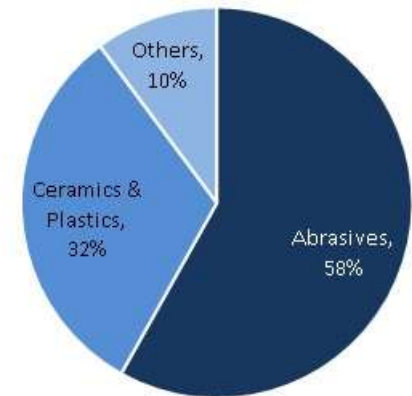
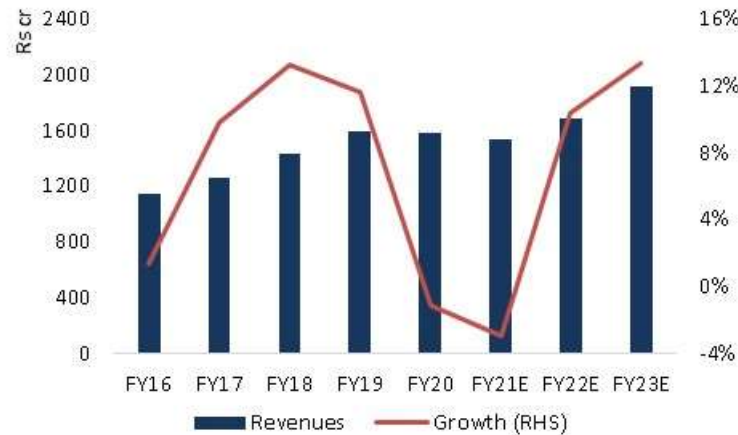
About the company

Grindwell Norton (GNL) was established in its current state in 1967 by a technical collaboration between the India based Grindwell Company and the US based Norton Company, which ultimately resulted in a financial collaboration in 1971. In 1990, Saint Gobain acquired Norton Company, and later increased its stake in GNL in 1996 thereby making GNL its first majority-owned subsidiary in India. The

businesses of GNL include Abrasives, Ceramic Materials Businesses (Silicon Carbide and Performance Ceramics & Refractories), Performance Plastics and ADFORS. The products of the company find application in automobiles, steel, bearings, and construction & fabrication industries. It has seven manufacturing facilities with six located in India and one in Bhutan.

The Saint-Gobain Delegation (Country Head) office, and INDEC (the captive India IT Development Centre for the Saint-Gobain Group globally) are also part of GNL. With a turnover of over €40.8 billion, SaintGobain operates in 67 countries and has more than 175,000 employees. Saint Gobain, globally produces more than 250,000 types of grinding wheels in the bonded abrasives segment (diameters range from few millimeters to nearly 2 meters almost 6.5 feet). In India, GNL offers ~14,000 products in this division, though accounts for mere 5% of the global portfolio. The Group currently holds 51.66% of the equity capital of GNL. Indian promoters including the MD's family, Narang and Bharucha families hold the 7.57% stake taking the total promoter stake to 58.9%.

Revenue trend and breakup (FY20)



(Source: Company, HDFCsec)

Financials – Consolidated

Income Statement

(Rs cr)	FY19	FY20	FY21E	FY22E	FY23E
Net Revenues	1598.1	1579.6	1582.4	1755.0	1992.6
Growth (%)	11.7	-1.2	0.2	10.9	13.5
Operating Expenses	1326.2	1315.1	1286.5	1428.5	1620.0
EBITDA	271.8	264.5	295.9	326.4	372.6
Growth (%)	10.1	-2.7	11.9	10.3	14.2
EBITDA Margin (%)	17.0	16.7	18.7	18.6	18.7
Depreciation	45.2	57.8	56.3	63.1	67.7
Other Income	35.4	40.4	42.7	49.1	59.8
EBIT	262.0	247.1	282.3	312.5	364.7
Interest expenses	1.5	4.5	3.5	4.0	4.0
PBT	260.5	242.6	278.8	308.5	360.7
Tax	91.7	58.8	70.3	77.7	90.9
PAT	168.7	183.9	208.6	230.8	269.8
Exceptional item	-1.5	-1.4	-1.6	-1.7	-1.7
Adj. PAT	167.2	182.5	207.0	229.1	268.1
Growth (%)	11.7	9.1	13.4	10.7	17.1
EPS	15.1	16.5	18.7	20.7	24.2

Balance Sheet

As at March (Rs cr)	FY19	FY20	FY21E	FY22E	FY23E
SOURCE OF FUNDS					
Share Capital	55.4	55.4	55.4	55.4	55.4
Reserves	1042.6	1132.0	1255.9	1390.8	1548.3
Shareholders' Funds	1097.9	1187.3	1311.3	1446.2	1603.6
Minority Interest	13.9	13.6	15.2	16.9	18.6
Borrowings	0.0	0.0	0.0	0.0	0.0
Net Deferred Taxes	23.2	12.0	12.0	12.0	12.0
Total Source of Funds	1135.0	1212.9	1338.4	1475.0	1634.1
APPLICATION OF FUNDS					
Net Block & Goodwill	345.1	384.6	382.9	372.1	353.0
CWIP	43.0	29.1	14.6	7.3	3.6
Investments	182.7	582.7	607.7	657.7	707.7
Other Non-Curr. Assets	27.6	20.4	25.2	27.0	29.3
Total Non Current Assets	598.3	1016.8	1030.3	1064.0	1093.7
Inventories	328.6	303.3	310.0	347.2	389.1
Trade Receivables	205.6	205.0	201.6	225.7	256.3
Cash & Equivalents	234.1	14.7	86.1	149.2	250.9
Other Current Assets	78.7	51.9	63.7	71.6	75.6
Total Current Assets	847.0	575.0	661.3	793.7	971.9
Trade Payables	180.7	226.3	208.1	221.2	245.7
Other Current Liab & Provisions	129.6	152.6	145.1	161.4	185.8
Total Current Liabilities	310.3	378.9	353.2	382.6	431.4
Net Current Assets	536.7	196.1	308.1	411.0	540.4
Total Application of Funds	1135.0	1212.9	1338.4	1475.0	1634.2

Cash Flow Statement

(Rs cr)	FY19	FY20	FY21E	FY22E	FY23E
EBIT	260.5	242.6	278.8	308.5	360.7
Non-operating & EO items	-14.3	-22.5	-5.8	-0.4	-0.5
Interest Expenses	0.6	3.8	3.5	4.0	4.0
Depreciation	44.6	57.8	56.3	63.1	67.7
Working Capital Change	-113.5	106.0	-39.6	-41.2	-29.6
Tax Paid	-93.4	-70.1	-70.3	-77.7	-90.9
OPERATING CASH FLOW (a)	84.6	317.6	222.9	256.2	311.4
Capex	-66.9	-49.9	-40.0	-45.0	-45.0
Free Cash Flow	17.6	267.6	182.9	211.2	266.4
Investments	12.2	-381.6	-25.0	-50.0	-50.0
Non-operating income	0.0	-10.5	0.0	0.0	0.0
INVESTING CASH FLOW (b)	-54.7	-442.1	-65.0	-95.0	-95.0
Debt Issuance / (Repaid)	0.0	0.0	0.0	0.0	0.0
Interest Expenses	-1.5	-4.5	-3.5	-4.0	-4.0
FCFE	28.3	-129.0	154.4	157.2	212.4
Share Capital Issuance	0.0	0.0	0.0	0.0	0.0
Dividend	-55.4	-68.1	-83.0	-94.1	-110.7
FINANCING CASH FLOW (c)	-56.9	-72.6	-86.5	-98.1	-114.7
NET CASH FLOW (a+b+c)	-27.0	-197.0	71.4	63.1	101.7

Key Ratios

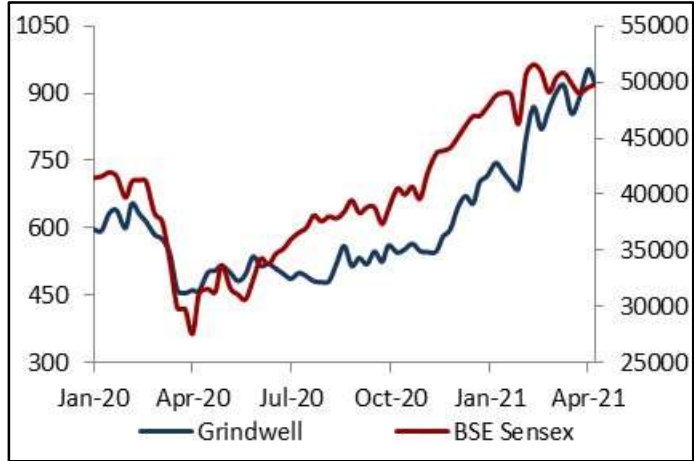
	FY19	FY20	FY21E	FY22E	FY23E
Profitability Ratios (%)					
EBITDA Margin	17.0	16.7	18.7	18.6	18.7
EBIT Margin	16.4	15.6	17.8	17.8	18.3
APAT Margin	10.5	11.6	13.1	13.1	13.5
RoE	16.0	16.0	16.6	16.6	17.6
RoCE	25.1	21.6	22.6	22.7	23.9
Solvency Ratio (x)					
Net Debt/EBITDA	-0.2	0.0	-0.1	-0.1	-0.2
Net D/E	-0.9	-0.1	-0.3	-0.5	-0.7
PER SHARE DATA (Rs)					
EPS	15.1	16.5	18.7	20.7	24.2
CEPS	19.2	21.7	23.8	26.4	30.3
BV	99.2	107.2	118.4	130.6	144.8
Dividend	6.0	7.5	7.5	8.5	10.0
Turnover Ratios (days)					
Inventory days	44.1	47.8	47.3	44.8	44.5
Debtor days	69.2	73.6	71.3	68.9	68.0
Creditors days	43.3	47.4	50.5	45.0	43.1
VALUATION (x)					
P/E	61.3	56.1	49.5	44.7	38.2
P/BV	9.3	8.6	7.8	7.1	6.4
EV/EBITDA	36.8	37.1	32.9	29.4	25.4
EV/Revenues	6.3	6.2	6.1	5.5	4.7
Dividend Yield (%)	0.6	0.8	0.8	0.9	1.1

(Source: Company, HDFC sec Research)

Grindwell Norton Ltd.



Price Chart



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