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Company update and
earnings revision

Capital Goods

Target price Rs1,287

Earnings revision

(%)	FY22E	FY23E
Sales	↓ 0.0	↑ 0.6
EBITDA	↑ 1.8	↑ 6.0
EPS	↑ 1.9	↑ 6.1

Target price revision

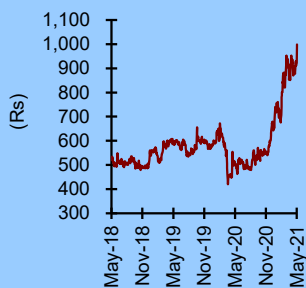
Rs1,287 from Rs1,220

Shareholding pattern

	Sep '20	Dec '20	Mar '21
Promoters	58.3	58.3	58.3
Institutional investors	20.1	20.2	20.4
MFs and others	16.1	16.1	15.9
Insurance Cos.	-	-	-
FII's	4.1	4.1	4.5
Others	21.6	21.5	21.3

Source: BSE

Price chart



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INDIA

ICICI Securities

Grindwell Norton

BUY

Maintain

Rs1,113

Moving towards a new orbit

Grindwell Norton (GWN) during the annual analyst interaction shared its future growth strategies and growth drivers. Despite a challenging FY21, the company was able to gain 100bps market share in domestic abrasives with strong margins. It witnessed strong growth in the performance plastics segment driven by life sciences, pharma, chemicals and F&B. Exports grew by a strong 14% YoY and the management foresees good potential in the same supported by the parent, eyeing India as a global sourcing hub. Factoring-in the higher margins and growth outlook, we raise FY22E and FY23E earnings by 1.9% and 6.1% respectively. Maintain BUY with a revised SoTP-based target price of Rs1,287 (earlier: Rs1,220).

- **Strong margins and cashflows aided by solutions approach:** Leveraging the support of the parent's research and global portfolio, GWN will be able to penetrate lucrative areas under performance plastics (PPL), performance ceramics, and refractories (PCR). Margins under ceramics & plastics increased to 24% in FY21 vs 14% in FY20, given the solutions-based approach and the strong growth in performance plastics. Margins are likely to sustain at these elevated levels. Management is confident about doubling the revenues from PPL in 3-4 years.
- **PCR and PPL – the twin growth engines:** For the past five years, C&P segment growth was at a CAGR of 11% vs 3% for abrasives, resulting in 6% overall revenue CAGR. Going forward, we believe, PPL and PCR will increasingly take the mantle of growth. GWN has plans to introduce various unique solutions in oil & gas, chemicals, pharma and other process industries. PCR caters to high-end refractory requirements, a niche market with better margins.
- **Gradually tapping export markets:** GWN's exports have been largely towards the global subsidiaries of Saint-Gobain and this trend is likely to continue going forward. The parent has plans to make India a global sourcing hub for 2-3 product segments in future and this can further boost the overall prospects from export markets.
- **Stable growth, healthy cashflow to support premium valuation:** GWN has witnessed positive free cashflow consistently for the past 12 years irrespective of the macro environment. This has resulted in a strong balance sheet with net cash of Rs6.4bn and consistent overall RoCE of 16% and core RoCE of 29% for FY21. Given the varying growth profile and return profiles of various segments, we value them separately. Taking into account the company's domestic leadership, technology edge and stable growth profile, we value the abrasive business at 40x FY23E earnings, ceramic & plastic at 50x and 'others' at 30x. Given the revival in domestic industrial activity and benefit to C&P from newer applications, we maintain our **BUY** rating on the stock with a revised SoTP-based target price of Rs1,287 vs Rs1,220 earlier.

Market Cap	Rs123bn/US\$1.7bn	Year to Mar	FY20	FY21	FY22E	FY23E
Reuters/Bloomberg	GRNN.BO/GWN IN	Revenue (Rs mn)	15,524	16,329	18,978	22,335
Shares Outstanding (mn)	110.7	EBITDA(Rs mn)	2,521	3,238	3,559	4,409
52-week Range (Rs)	1142/451	Net Income (Rs mn)	1,830	2,421	2,618	3,271
Free Float (%)	41.7	EPS (Rs)	16.5	21.9	23.6	29.5
FII (%)	4.5	P/E (x)	67.4	50.9	47.1	37.7
Daily Volume (US\$'000)	874	CEPS (Rs)	21.5	26.6	28.9	35.1
Absolute Return 3m (%)	32.8	EV/E (x)	47.2	36.1	32.4	25.9
Absolute Return 12m (%)	122.3	Dividend Yield	0.5	0.9	1.1	1.2
Sensex Return 3m (%)	(3.4)	RoCE (%)	16.2	19.0	18.3	20.7
Sensex Return 12m (%)	58.2	RoE (%)	16.2	19.1	18.4	20.7

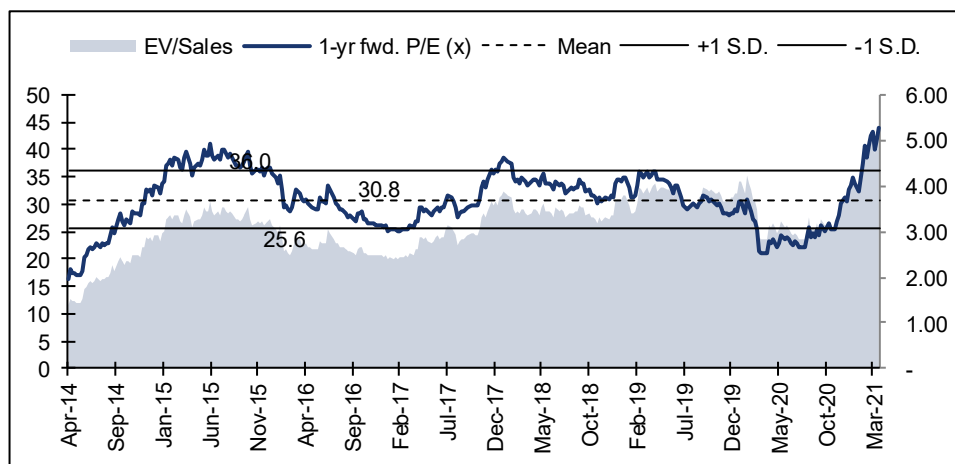
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Outlook and valuations

The pick-up in domestic industrial activity benefits the abrasive business, while C&P will continue to gain from increasing demand from pharma, healthcare and chemicals. Hence, we estimate revenue / EBITDA / PAT CAGRs (FY21-FY23E) of ~17% / 16.7% / 16.2% respectively for GWN.

Given the varying growth profile and return profiles of various segments, we value them separately. We adopt the SoTP methodology for GWN, wherein we assign P/E multiples to FY23E core PAT of various business segments and subsidiaries, and add back cash to the final valuation.

Chart 1: One-year forward P/E chart



Source: Bloomberg, I-Sec research

We value: 1) the abrasive business at 40x FY23E core earnings (better utilisation with industrial growth boosting volumes across industries); 2) ceramic and plastic business at 50x FY23E core earnings (fast-growing, high-margin PCR and PPL businesses, promising growth prospects with limited investments); and 3) 'others' at 30x FY23E core earnings (stable and high RoCE in the IT services business) – and then we add back cash of Rs9.2bn to arrive at an SoTP-based target price of Rs1,287 per share.

Given the healthy recovery expectations in auto and industrial activity and accelerated growth in PPL and PCR segments, we maintain our **BUY** rating. The stock is currently trading at 47.1x FY22 P/E and 37.7x FY23E earnings and our target price implies a core P/E multiple of 43.8x.

Table 1: SoTP valuation

	FY23E Core PAT	Multiple (x)	Value (Rs bn)	Value per Share
Abrasives	1,228	40	49.5	447
Ceramics & Plastics	1,461	50	73.1	660
Others	356	30	10.8	97
Cash and investments			9.2	83
Total			142.5	1,287

Source: Company data, I-Sec research

Table 2: Earnings revision

Rs mn	FY22E			FY23E		
	Earlier	Revised	YoY (%)	Earlier	Revised	YoY (%)
Revenue	18,978	18,978	0.0	22,207	22,335	0.6
EBIDTA	3,495	3,559	1.8	4,158	4,409	6.0
PAT	2,570	2,618	1.9	3,083	3,271	6.1

Source: Company data, I-Sec research

Concall highlights

Revenue & growth outlook

- In FY21, exports grew 14% YoY to Rs3.5bn while domestic sales grew 3.7%.
- Abrasive growth was better than GDP due to its presence in fast-growing areas of application.
- Strong growth in life sciences, exports, auto components and metals drove growth in the ceramics and performance plastics segments.
- The overall size of the domestic abrasive market is in the range of Rs30bn. Grindwell has likely increased its market share by 100bps to 27% in FY21 while its domestic abrasive market share declined by ~5%.
- ~40% of the GNO abrasive is thin wheels, coated etc. 12% is in construction, 12% is consumer facing, 29% is auto and auto-related, while the rest is exports
- C&P has a potential to grow at a faster pace. India government has declared glass, ceramics and plastics as priority sectors, and the company sees potential to double contribution from the same segments in 3-4 years.
- Performance plastics (PPLs) growth outlook: These businesses are application, innovation intensive and track the pharma market globally. Single-use manifold, bags, moulded products, etc. are some of the performance plastic solutions the company is looking at. Company is confident of reaching Rs5bn-6bn sales in PPLs in 4-5 years.
- Tech bond: In sealants and adhesives, under sealants, the company has a unique positioning as these products are related to glass and construction, hence the company's first focus is on sealants and then will gradually enter adhesive segment.
- Price increase in abrasives: GNW is ahead of the curve on the price increase, and is moving into solutions. hence can't distill down to per unit price increase etc. In crude terms, the price increase is 2.5-3%.
- ~25-30% of the sales of FY21 are from products introduced in the past five years.
- GNW can be the global export base for a couple of categories as manufacturing which will be in abrasives, plastics and ceramics.
- Potential long-term growth opportunities will come from 5G, EVs and batteries.

Margins and costing

- Company believes it can maintain the margins under ceramics & plastics in a zone; some of the fixed costs are semi-variable. Covid second wave is impacting the overall trajectory in the near term.
- The sale of silicon carbide from Bhutan factory was impacted due to covid. Given the relatively low margins in the same, this also supported the overall margin expansion under ceramics and plastics segment.
- Pricing was an important reason for increase in profitability. Company focused on solutions-based approach rather than product-based, and this also led to improving the overall margins to some extent.
- ~60% of margin expansion in FY21 was due to lifesciences and the rest 40% from 'others'. Solutions-based approach has been a major driver for margin expansion.
- Company had anticipated the spring back effect on some of the commodities; the price increase already considers this. However, the second wave will result in some uncertainty.
- Long-term policy on the royalty and related-party transaction: 2.5% of net sales (sales minus the products bought) is royalty. Research work carried out in India by the parent is high. There is no change in this policy framework.
- Implemented ERP and integrated with the parent: 22 sites and six legal entities were connected using SAP. In Dec'20, the company shut sales and other processes for 10-12 days. It has completed industry 4.0 in most plants. GNW currently has the most advanced plants. It has invested in digital twins for the industrial furnaces.
- The management expects sustainable level of abrasive segment margins to be at 14-15% levels.

Others

- During lockdown, the distribution was strengthened in the tier II/III/IV cities. Company also supported distribution and retail partners with credit and did not face any NPA due to this. This has strengthened the relationships.
- Private sector investment is coming back in the economy post a dramatic slowdown and there is an increasing confidence on own business resilience.
- Bhutan: Exporting low sulphur coke to Bhutan was a challenge that has now been ironed out. Currently Bhutan is locked out and will likely to be so in FY22. Hence, the company has enhanced production capability in the AP plant for SiC in Tirupathi.
- Company has earmarked Rs1bn-1.1bn towards capex for FY22; deployment will be depend on the progress of second wave of covid.
- Capital allocation is as 50% of cash for dividend, 50% towards organic investments towards product-oriented segments.
- Company is open to explore inorganic opportunities too.

Table 3: Financial assumptions

<i>Rs mn</i>	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E
Abrasives	9,038	9,071	9,752	9,243	9,328	10,914	12,770
Ceramics & Plastics	3,296	3,943	4,522	4,853	5,447	6,427	7,841
Others	1,118.0	1,389.9	1,469.5	1,520.5	1,663.6	1,747	1,834
Total	13,369	14,282	15,668	15,524	16,329	18,978	22,335
EBIT							
Abrasives	1,121	1,250	1,345	1,067	1,120	1,310	1,660
Ceramics & Plastics	294	544	679	719	1,320	1,478	1,960
Others	223	252	345	375	456	437	477
Total	1,638	2,046	2,368	2,161	2,896	3,225	4,097
EBIT Margin (%)							
Abrasives	12.4	13.8	13.8	11.5	12.0	12.0	13.0
Ceramics & Plastics	8.9	13.8	15.0	14.8	24.2	23.0	25.0
Others	20.0	18.2	23.5	24.7	27.4	25.0	26.0
Total	12.2	14.3	15.1	13.9	17.7	17.0	18.3

Source: Company data, I-Sec research

Financial summary

Table 4: Profit & Loss statement

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Total Income	15,524	16,329	18,978	22,335
Operating Expenses	13,002	13,091	15,419	17,927
EBITDA	2,521	3,238	3,559	4,409
% margins	16.2	19.8	18.8	19.7
Depreciation & Amortisation	547	519	587	617
EBIT	1,975	2,719	2,972	3,792
Gross Interest	43	32	34	36
Other Income	462	510	553	606
PBT before exceptional	2,394	3,196	3,491	4,362
Add: Extraordinary	-	-	-	-
/Exceptionals	-	-	-	-
Add: Share in associates	-	-	-	-
PBT	2,394	3,196	3,491	4,362
Less: Taxes	564	776	873	1,090
Less: Minority Interests	-	-	-	-
Net Income (Reported)	1,830	2,421	2,618	3,271
Adjusted Net Income	1,830	2,421	2,618	3,271

Source: Company data, I-Sec research

Table 5: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Assets				
Total Current Assets	9,694	12,293	14,597	17,353
of which cash & cash eqv.	4,208	6,435	7,789	9,176
Total Current Liabilities & Provisions	3,760	4,662	5,416	6,269
Net Current Assets	5,934	7,631	9,182	11,084
Investments	1,891	2,124	2,336	2,570
Other Non-Current Assets	698	553	564	576
Net Fixed Assets	3,391	3,371	2,886	2,569
Goodwill	5	86	86	86
Total Assets	11,920	13,764	15,053	16,885
Liabilities				
Borrowings	-	-	-	-
Deferred Tax Liability	153	193	193	193
Minority Interest	-	-	-	-
Equity Share Capital	554	554	554	554
Face Value per share (Rs)	5.00	5.00	5.00	5.00
Reserves & Surplus	11,213	13,017	14,306	16,138
Net Worth	11,767	13,571	14,860	16,692
Total Liabilities	11,920	13,764	15,053	16,885

Source: Company data, I-Sec research

Table 6: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Operating Cashflow	2,376	2,940	3,205	3,888
Working Capital Changes	1,044	566	(216)	(543)
Capital Commitments	(598)	(449)	(101)	(300)
Free Cashflow	2,822	3,057	2,887	3,045
Cashflow from Investing Activities	227	(1,806)	329	354
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	-	-	-	-
Interest paid	(43)	(32)	(34)	(36)
Dividend paid	(801)	(1,052)	(1,329)	(1,439)
Extraordinary Items/Others	(418)	2,060	(500)	(536)
Chg. in Cash & Bank balance	1,786	2,227	1,354	1,388

Source: Company data, I-Sec research

Table 7: Key ratios

(Year ending March 31)

	FY20	FY21	FY22E	FY23E
Per Share Data (in Rs.)				
Diluted adjusted EPS	16.5	21.9	23.6	29.5
Recurring Cash EPS	21.5	26.6	28.9	35.1
Dividend per share (DPS)	6.0	9.5	12.0	13.0
Book Value per share (BV)	106.3	122.6	134.2	150.8
Growth Ratios (%)				
Operating Income	(0.9)	5.2	16.2	17.7
EBITDA	(2.7)	28.4	9.9	23.9
Recurring Net Income	11.7	32.3	8.1	24.9
Diluted adjusted EPS	11.7	32.3	8.1	24.9
Diluted Recurring CEPS	15.3	23.7	9.0	21.3
Valuation Ratios				
P/E	67.4	50.9	47.1	37.7
P/CEPS	51.9	41.9	38.5	31.7
P/BV	10.5	9.1	8.3	7.4
EV / EBITDA	47.2	36.1	32.4	25.9
EV / Operating Income	7.7	7.2	6.1	5.1
EV / Op. FCF (pre-capex)	34.8	33.3	38.6	34.1
Operating Ratios				
Raw Material/Sales (%)	47.0	44.9	44.9	44.9
SG&A/Sales (%)	23.7	22.7	24.4	24.2
Other Income / PBT (%)	19.3	15.9	15.8	13.9
Effective Tax Rate (%)	23.6	24.3	25.0	25.0
NWC / Total Assets (%)	18.6	11.9	12.3	14.2
Inventory Turnover (days)	69.0	70.3	70.3	73.0
Receivables (days)	47.2	44.7	44.7	44.7
Payables (days)	63.9	87.1	87.1	87.1
Net D/E Ratio (x)	(0.4)	(0.5)	(0.5)	(0.5)
Return/Profitability Ratios (%)				
Recurring Net Income Margins	11.8	14.8	13.8	14.6
RoCE	16.2	19.0	18.3	20.7
RoNW	16.2	19.1	18.4	20.7
Dividend Payout Ratio	36.3	43.5	50.8	44.0
Dividend Yield (%)	0.5	0.9	1.1	1.2
EBITDA Margins	16.2	19.8	18.8	19.7

Source: Company data, I-Sec research

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