Grasim Industries Limited’s (Grasim) stock has risen by ~10% over the fortnight, led by two key developments in the telecom sector affecting VIL (Grasim holds 11.6%). Firstly, the government provided benefit of Rs. 23,920 crore to VIL through deferment of spectrum payment for FY2021-FY2022. However, the Committee of Secretaries (CoS) set up to suggest relief measures for the telecom sector has been disbanded, which has put expectations of further relief in abeyance as of now. Secondly, the three major players in telecom have decided upon tariff hike from December 2019, which is seen as a sign of bottoming out of ARPUs for the industry. We believe the recent developments in the telecom sector is likely to bring sanity in the sector and is positive over a long term for VIL. However, the other concerns related to reduction of 8% adjusted gross revenue (AGR) as license fees and payment of AGR dues in less than three months (SC ruling) have not been addressed. Hence, we continue to believe VIL’s funding requirement to remain a key hangover on Grasim. We have introduced FY2022E standalone estimates in this note. We continue to maintain Hold on the stock with a revised price target (PT) of Rs. 850 (factoring revised valuation of VIL, Aditya Birla Capital and rolling forward standalone estimate valuation to FY2022E).

### Positive developments in the telecom sector:

Over less than a fortnight, the two key developments in the telecom sector have led to almost 3x increase in market capitalisation of VIL. Firstly, the government provided deferment of payment of spectrum for FY2021-FY2022 (estimated benefit of Rs. 23,920 crore). Secondly, the three major operators decided upon tariff hikes from December, which is seen as bottoming out on pressure on ARPUs. VIL announced tariff hikes for its prepaid plans up to 42%, which would come in effect on December 3, 2019. The key developments highlighted above although are expected to bring sanity in the sector and are positive over a long term. The same are not expected to ease liquidity pressure for VIL, in turn remaining a key hangover for Grasim.

### Our Call

**Valuation – Maintain Hold with a revised PT of Rs. 850:** Grasim has risen by ~10% over less than a fortnight with two developments in the telecom sector and an increase in Aditya Birla Capital’s market capitalisation (up ~34%, Grasim holds ~56% stake). We see the developments in the telecom sector to bring sanity for the sector and are positive over a long term for VIL; however, reduction of licensee fees and payment of AGR-related dues in less than three months have remained unaddressed. Hence, we continue to believe VIL’s funding requirements to remain a key hangover on Grasim. We have introduced FY2022E standalone estimates in this note. We continue to maintain Hold on the stock with a revised PT of Rs. 850 (factoring revised valuation of VIL, Aditya Birla Capital and rolling forward standalone estimate valuation to FY2022E).

### Key Risks

Funding requirement of its investment in Vodafone Idea is a key hangover.
**Government gives two-year moratorium to telecom companies**

The Finance Minister on November 20, 2019, announced that the government has decided to defer receipt of spectrum auction installment due from Telecom Service Providers (TSPs) for FY2021 and FY2022, considering the current financial stress faced by major TSPs and pursuant to recommendations made by CoS. The deferred amounts of spectrum fees will be equally spread over the remaining installments without any increase in the existing time period specified for making the installment payments. The interest as stipulated while auctioning of the concerned spectrum will, however, be charged so that NPV of the payable amount is protected. The move is likely to yield benefit of Rs. 23,920 crore to VIL. Besides the spectrum payments on which VIL got relief, Vodafone Idea also needs to pay Rs 44,150 crore (out of which it made provision of Rs. 25,680 crore in Q2FY2020) in licence fees, spectrum usage charge, penalties and interest to the government after a recent Supreme Court ruling expanded the definition of AGR. The AGR dues have to be paid in less than three months and the government has not signaled any changes to this.

**VIL raises tariff rates – lower cash burn in near term but need for more relief measures**

VIL yesterday announced new tariffs/plans for its prepaid products and services, which will be effective from December 3, 2019. The company hiked prices of its prepaid plans by up to 42% while also charging 6 paise per minute for every outgoing call to a rival network. The deferment of spectrum fees along with increased tariff rates is expected to slow down the cash burn for VIL in the short term. However, the company would require favourable outcome from the adjusted gross revenue dispute with the government.
Financials in charts

**Viscose volume trend**

Source: Company, Sharekhan Research

**Viscose realisation trend**

Source: Company, Sharekhan Research

**Viscose EBITDA/kg trend**

Source: Company, Sharekhan Research

**Chemical volume trend**

Source: Company, Sharekhan Research

**Chemical EBITDA margin trend**

Source: Company, Sharekhan Research

**Standalone debt**

Source: Company, Sharekhan Research
Outlook

Near-term outlook challenging for the standalone business: Lower exit prices for VSF and caustic soda are expected to put pressure on OPM in Grasim’s VSF and chemical divisions in the near term. However, lower pulp prices are expected to provide some respite to the VSF division in the coming quarters on account of lag effect of sourcing pulp from overseas. The caustic division may remain under pressure for a year due to incremental capacity additions and weak demand. Management is going ahead with capacity expansion plans for the VSF and chemical divisions, which would commence operations from H1FY2021. The company is taking initiatives to increase contribution from value-added products to wither near-term headwinds.

Valuation

Valuation – Maintain Hold with a revised PT of Rs. 850: Grasim has risen by ~10% over less than a fortnight with two developments in the telecom sector and an increase in Aditya Birla Capital’s market capitalisation (up ~34%, Grasim holds ~56% stake). We see the developments in the telecom sector to bring sanity for the sector and are positive over a long term for VIL; however, reduction of licensee fees and payment of AGR-related dues in less than three months have remained unaddressed. Hence, we continue to believe VIL’s funding requirements to remain a key hangover on Grasim. We have introduced FY2022E standalone estimates in this note. We continue to maintain Hold on the stock with a revised PT of Rs. 850 (factoring revised valuation of VIL, Aditya Birla Capital and rolling forward standalone estimate valuation to FY2022E).

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 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, it is a leading global player in VSF, and is the largest chemicals (Chlor-Alkalis), biggest cement producer and diversified financial services (NBFC, Asset Management and Life Insurance) player in India.

Investment theme
Grasim has been underperforming due to its exposure in Vodafone Idea with 11.55% stake. Vodafone Idea’s highly leveraged balance sheet, weak telecom outlook and delay in monetisation of assets may lead to further capital infusion by FY2021 from its stakeholders, including Grasim, to retain its stake. This is expected to lead to erosion in liquid investments or higher leverage at Grasim standalone. Further, weak macro environment is expected to lead to underperformance of ABCL (56% Grasim stake) in the near term. Hence, UltraTech remains a safe bet, which comprises major value of Grasim’s SOTP. We believe investors can directly have exposure in UltraTech, which has no overhangs and a better earnings growth outlook over the next two years. Hence, we have a Hold rating on Grasim.

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

Additional Data

Key management personnel
Mr. Kumar Mangalam Birla Chairman
Mr. Dilip Gaur Managing Director
Mr. Ashish Adukia Chief Financial Officer
Mrs. Hutokshi R Wadia Company Secretary
Source: Company Website

Top 10 shareholders
<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Holder Name</th>
<th>Holding (%)</th>
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<tr>
<td>1</td>
<td>Birla Group Holdings Pvt Ltd</td>
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<td>Life Insurance Corp of India</td>
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<td>IGH Holdings Pvt Ltd</td>
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Source: Bloomberg

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