

Bajaj Corp Limited

CRISIL IPO Grade 4/5 (Above average)

June 28, 2010

Grading summary

CRISIL Equities has assigned a CRISIL IPO grade of '4/5' (pronounced "four on five") to the proposed IPO of Bajaj Corp Limited (Bajaj Corp). This grade indicates that the fundamentals of the IPO are above average relative to the other listed equity securities in India. However, this grade is not an opinion on whether the issue price is appropriate in relation to the issue fundamentals. The offer price for the issue may be higher or lower than the level justified by its fundamentals. The grade is not a recommendation to buy, sell or hold the graded instrument, its future market price or suitability for a particular investor. To arrive at the overall grade, amongst various other parameters, CRISIL has considered the company's business prospects, financial performance, management capabilities and corporate governance practices.

The IPO grade assigned to Bajaj Corp reflects its dominant position (~50% market share in value terms) in the light hair oil segment, which constitutes ~14% of the total hair oil market. Light hair oil is positioned as a premium product in the hair oil market. The light hair oil segment grew at a 24% CAGR through CY06-09 as against ~18% growth registered by the overall hair oil industry. Higher growth in the light hair oil segment has been driven by: (a) shift in consumption from unbranded and coconut/heavy hair oils to light hair oil; (b) higher urbanisation (68% of the light hair oil market); and (c) increase in disposable income in the rural markets. The grade also reflects Bajaj Almond Drops' - the flagship brand of Bajaj Corp - ability to consistently increase market share of 46.8% in CY09 (in volume terms), far ahead of its nearest competitor with a 21.5% market share.

The grade factors in the advantages the company enjoys due to the location of its manufacturing facilities in tax-free zones. Notably, the existing capacities at these facilities are sufficient to service the expected growth over the next three-five years.

The grade takes into account Bajaj Corp's strong distribution network, which is comparable to its larger peers. The established distribution network will provide the required strength for future growth in existing as well as new products. The grade is supported by the strong brand recall of 'Bajaj' both in the rural and urban markets. The grade has also factored in the strong management, its experience in the FMCG industry and strong promoter background.

The company is expected to have a strong balance sheet post the IPO, which lends the company enough strength to grow its operations. The company plans to use the IPO proceeds to launch four new products in the personal care segment. It also plans to use part of the IPO proceeds for inorganic growth within the personal care segment. CRISIL Equities believes that the new products will diversify and increase revenues.

The grade is moderated by Bajaj Corp's high dependence on Bajaj Almond Drops (92% of 9MFY10 revenues). It also factors in the risk of higher competition to Bajaj Corp now than in the past. It also takes into account the adverse impact on EBITDA and PAT margins over the next three years due to aggressive advertisement and promotion expenditure for the launch of new products.

Since Bajaj Corp was carved out in April 2008, the company financials are available only from FY09. In 9MFY10, the company's net revenues were ~Rs 2,080 mn, EBITDA margin was 30.9% and PAT margin was 27.2%.

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About the company

Bajaj Corp is the second largest company in the Shishir Bajaj Group of companies. The history of Bajaj Corp dates back to 1953 when Mr Kamalnayan Bajaj established Bajaj Sevashram to market and sell hair oils and other beauty products. Bajaj Sevashram used to manufacture and sell products until December 2000. In January 2001, pursuant to a scheme of demerger of the erstwhile Bajaj Group, it transferred its operating business and assigned the trademarks for all the brands to its subsidiary Bajaj Consumer Care Ltd (BCCL). In April 2008, pursuant to the execution of the Trademark Licence Agreement between BCCL and Bajaj Corp, BCCL assigned the trademarks for the products in favour of Bajaj Corp.

Bajaj Corp manufactures and markets five major brands. The flagship brand, Bajaj Almond Drops, is the market leader in the light hair oil segment with ~50% market share in CY09. Bajaj Almond Drops accounted for ~92% of Bajaj Corps' net sales in the nine-month period ended December 31, 2009. In addition, it markets hair oil under the brand names Bajaj Brahmi Amla, Bajaj Amla Shikakai and Bajaj Jasmine Hair Oil. It also markets oral care products under the brand name Bajaj Kala Dant Manjan.

2

Issue details

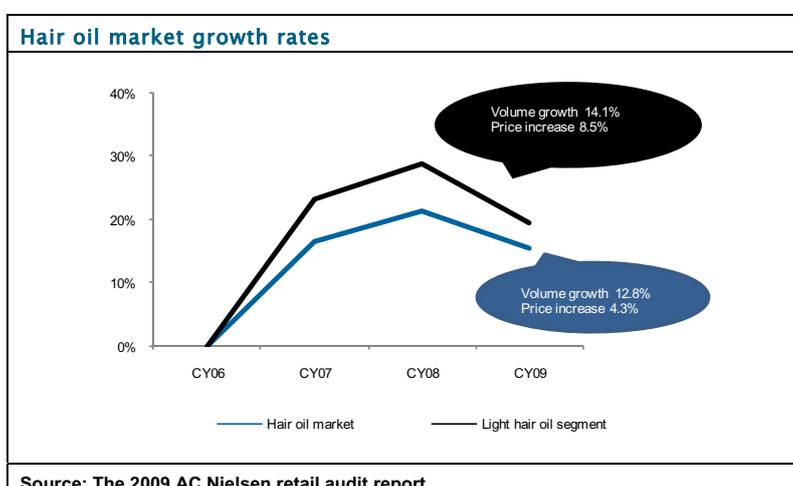
Shares offered to public	4.5 mn
As per cent of post issue equity	15.25%
Object of the Issue	<ul style="list-style-type: none"> • Promote future products – Rs 2,200 mn • Acquisitions and other strategic initiatives – Rs 500 mn • General corporate purposes – not mentioned
Amount proposed to be raised	Not available at the time of grading
Price band	Not available at the time of grading
Lead managers	Kotak Mahindra Capital Company Limited

Detailed Grading Rationale

A. Business Prospects

- Light hair oil segment to continue to grow strong*

The light hair oil segment comprises the premium segment of the hair oil market and constitutes ~14% (in value terms) of the total hair oil market. In the past three years, as per the 2009 AC Nielsen retail audit report, the light hair oil segment has grown at a CAGR of 23.8% on the back of volume growth of 14.1% and price increase of 8.5%. In comparison, the hair oil segment has grown at a CAGR of 17.7%, driven by a volume growth of 12.8% and price increase of 4.3%.



Currently, the light hair oil market is concentrated in the urban market, which constitutes 68% of the segment. With increased focus of vendors, in this segment, on the rural market, the mix is likely to change going forward. On the back of continued urbanisation and higher disposable income in rural markets, the light hair oil segment is expected to continue to grow over the next three-five years. Further, over the past few years, demand for light hair oil has been high despite continuous price hikes, showing acceptance of the product. In light of the above, CRISIL Equities believes the following two factors are the primary drivers for growth in the segment:

- Shift from unbranded hair oils to branded light hair oils.
- Shift from coconut and heavy hair oils to light hair oils.

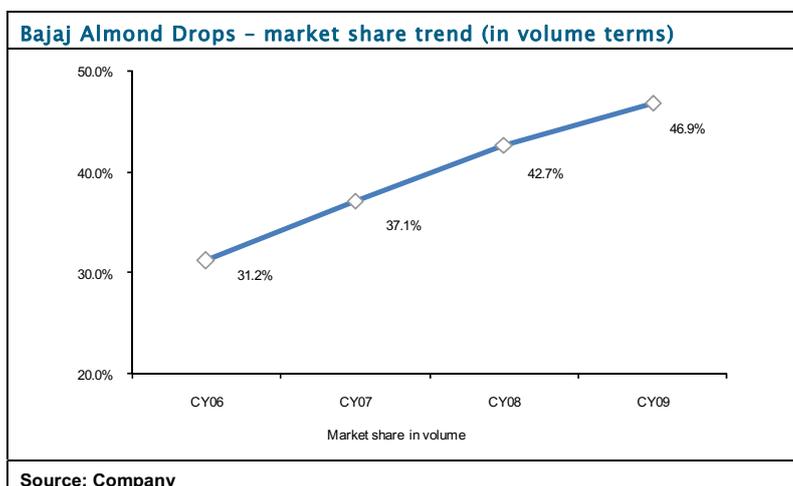
- 'Bajaj' – a strong household brand in India*

The 'Bajaj' brand has more than five decades of history and has been associated with product categories like two-wheelers, FMCG, financial services and other consumer products. It enjoys a strong brand recall both in the rural and urban markets. The demerger of the Bajaj Group continues to allow all the involved parties to use the 'Bajaj' brand. We believe that a strong brand will continue to grow the existing product and also provide leverage while launching new products.

- Focused strategy has helped Bajaj Almond Drops emerge as the market leader***

The Bajaj Group established the hair oil business in 1953 in the heavy hair oil category with its brand Bajaj Brahmi Amla. Following the demerger of the Bajaj Group and subsequent formation of Bajaj Corp, the company made a conscious move of not getting into aggressive competition with Dabur and decided to focus on a niche segment of the light hair oil market. Also, post the demerger of the erstwhile Bajaj Group, Bajaj Corp has become the second largest company in the Shishir Bajaj Group. This has also led to the group focusing more on the company, which has been reflected in the company's performance.

This segment is dominated by three brands including Bajaj Almond Drops, which together account for approximately 83.5% of sales volume.



Over the past three years, Bajaj Almond Drops, the flagship brand of the company, has consistently increased its market share to 47% in CY09 (in volume terms) from 31% in CY06. Notably, its market share is much higher than the second- and third-largest players in the light hair oil segment with a market share of 21.5% and 15.2% respectively in CY09. Bajaj Almond Drops also commands premium pricing than its peers and has 49.5% market share in value terms as of CY09. Though in the past the company has been able to grow amidst competition, it may face higher competition going forward. This remains a key monitorable.

- Adequate sales and distribution network to drive future growth***

Bajaj Corp markets its products through a channel of distributors / stockists and retail outlets. The current distribution channel of the company is comparable to that of much larger peers like Dabur. However, the same has not been fully utilised largely due to a single-product driven revenue model. This is evident from low revenue per distributor or retail outlet. The company is geared to benefit from its established distribution network. This will entail existing brands and new products planned to be launched this year.

Distribution network details – FY09

	Distributors	Revenue per distributor in Rs ('000)
Bajaj Corp	4,300*	538
Dabur	5,000	5,697
HUL	10,000	22,194
* Details as of December 2009.		

	Retail outlets (mn)	Revenue per retail outlet (Rs)
Bajaj Corp	1.5*	1,630
GCPL	3.0	3,780
Marico	3.3	8,540
Dabur	2.8	8,630
HUL	6.3	35,230

Source: Company and DRHP

- New launches to diversify revenue, albeit success remains a key monitorable***

Currently, the company faces high revenue concentration as Bajaj Almond Drops contributes over 90% of its revenue. To leverage the 'Bajaj' brand and its established distribution channel, the company plans to launch four new products in the personal care segment over the next year. New product launches will enable the company to diversify its revenue base both within the hair oil segment and also in the personal care segment. We believe that the company can leverage its strong management and experience in the FMCG industry for the new launches. The performance of the new products is a key monitorable going forward.
- Strong balance sheet could boost revenue growth***

Post the IPO, Bajaj Corp will continue to have zero debt and a strong balance sheet. Further, it is expected to continue to generate adequate cash every year. Surplus cash coupled with approximately Rs 500 mn identified by the company out of the net IPO proceeds would be utilised for acquisitions. We believe deployment of cash to expand both organically as well as inorganically will boost the company's revenues.
- Manufacturing facilities at locations with tax benefits***

The company's manufacturing facilities are located in tax-free zones. The company is exempt from paying excise duties for a period of 10 years from fiscal year ended March 31, 2009 and income tax for a period of five years from fiscal year ended March 31, 2009. After the income tax-free period, the company will be taxed at a concessional rate for the following five years. Importantly, the capacity utilisation at these facilities is less than 30% and is more than sufficient to service the expected growth over the next three-five years.
- EBITDA and PAT margins to decline in the near term***

Over the next three years, the company plans to spend heavily on advertisements and promotions for the new products, benefits of which will accrue only over the long term. This is likely to almost double the selling and distribution expenses spend (Rs 746 mn in 9MFY20) in FY11. In such cases, profitability generally takes a hit in the near term. There is likely to be pressure on Bajaj Corp's EBITDA and PAT margins over the next three years. Further, minimal profitability of the newly launched products may also impact the company's overall margins.
- Volatility in raw material prices***

Raw material cost is ~40% of the net revenue which is almost equally distributed amongst core raw material and packaging costs. Light liquid paraffin (LLP) forms the largest component of the core raw materials, the others are vegetable oil, perfumes and almond extracts. LLP is a derivative of crude oil and is subject to price volatility. While in past the company has been able to pass on the increase in raw material cost through price hikes, volatility in raw material prices remains a key monitorable.

B. Financial Performance

Since Bajaj Corp was carved out in April 2008, the financials for the company are available only from FY09.

The company reported net revenues of Rs 2,197 mn in FY09; Bajaj Almond Drops contributed ~92% of the revenues and Bajaj Brahmi Amla contributed ~5%. EBITDA margin was 23.6% and PAT margin was 21.4% in FY09.

In 9MFY10, the company's net revenues were Rs 2,080 mn, EBITDA margin was 30.9% and PAT margin was 27.2%. As of 9MFY10, the company had net cash of Rs 328 mn on its balance sheet.

Financial performance snapshot

		FY09 Actual 12 months	9MFY10 Actual 9 months
Operating income	Rs mn	2197	2080
Operating margins	%	23.6	30.9
Net profits	Rs mn	470	565
Net margins	%	21.4	27.2
ROCE	%	199.3	163.9
RONW	%	183.2	145.4
Basic EPS	Rs	47	22.6
Diluted EPS	Rs	47	22.6
No. of equity shares	Mn	10.0	25.0
Net worth	Rs mn	516	261
Book value (FV Rs 10)	Rs	51.6	10.5
Current ratio	Times	3	1.3

* Note: Numbers have been re-classified as per CRISIL standards

Source: DRHP

C. Management Capabilities and Corporate Governance

Bajaj Corp has a strong professional management team. The senior management comprises people who are experienced in the FMCG business. The chairman and two whole-time directors have been long associated with the Shishir Bajaj Group of companies - drawing synergies as well as focus.

Bajaj Corp has a strong and experienced second line in place. Majority of them have been associated with the group for a long period of time and have rich experience in the FMCG industry. The operational heads have requisite domain expertise and are well aware of the business opportunities, their strengths and weaknesses vis-à-vis peers. We feel the management is capable and has been given considerable freedom to take independent decisions.

Independent directors have a fair understanding of the overall business of the company. The board includes Mr Gaurav Dalmia and Mr Haigreve Khaitan, who belong to reputed business families and hold directorial positions in various other prestigious organisations. We believe the board is well-equipped to provide guidance and exercise oversight over the management.

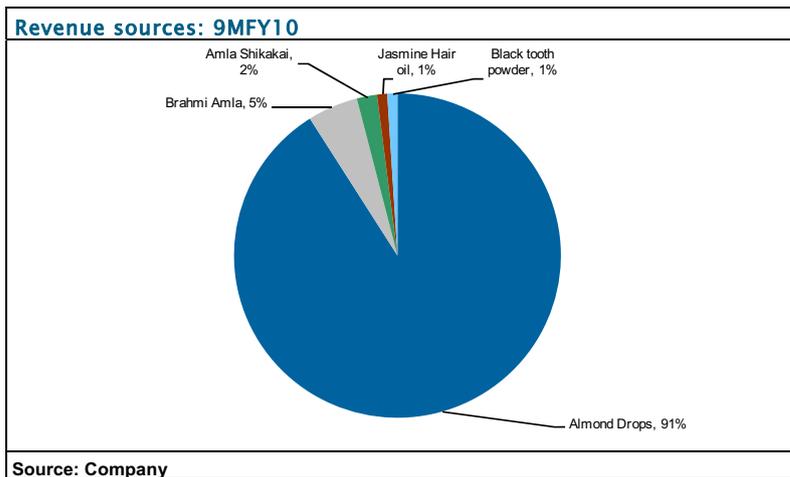
According to our discussions, we believe that the company has good corporate governance processes in place.

Annexure I Business Profile

Bajaj Corp primarily operates in only one business line - hair oils. Oral care forms a very small part of the overall business. The oldest brand is Bajaj Brahmi Amla, in existence since 1953. The other brands include Bajaj Amla Shikakai, Bajaj Jasmine Hair Oil and Bajaj Kala Dant Manjan. Bajaj Corp is the third largest producer of hair oils and the largest producer of light hair oils.

Bajaj Corp derives majority of its revenues from a single product, Bajaj Almond Drops. It is a value-added light hair oil and commands a premium. Bajaj Almond Drops is the market leader in the light hair oil segment with a 50% market share.

Bajaj Corp reported operating revenues of Rs 2,080 mn in 9MFY10.



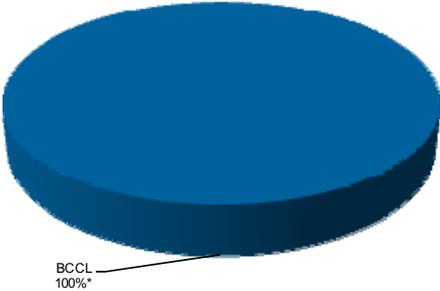
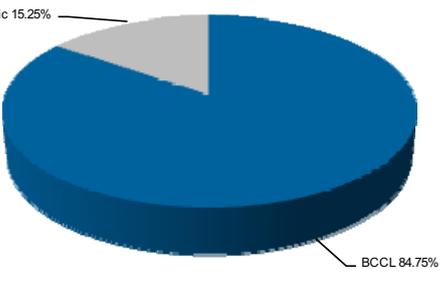
Management and Board Profile

The company has a strong management in place. Mr Kushagra Bajaj, Non-executive Chairman, is the son of Mr Shishir Bajaj and represents the Bajaj family in the company. He is also on the board of Bajaj Hindusthan Limited and BCCL.

The senior management includes Mr Roshan Hinger with over 45 years of experience in companies, which include BCCL and other Bajaj Group companies; and Mr Sumit Malhotra with over 23 years of experience in the FMCG industry - he is responsible for leading sales and marketing initiatives. The key management personnel have more than 20 years of experience. Bajaj Corp has a strong and experienced second line of management in place. Majority of them have been associated with the group for more than six years and have rich experience in the FMCG industry. The operational heads have requisite domain expertise and are well aware of the business opportunities, their strengths and weaknesses vis-à-vis peers. We feel the management is capable and has been given adequate freedom to take independent decisions for execution of tasks.

The company's board comprises seven directors which include four independent directors. The board includes Mr Haigreve Khaitan with more than 15 years of experience in the legal field. Chambers & Partners and Legal 500 have recommended him for his mergers and acquisitions expertise. Mr Gaurav Dalmia is a member of the Dalmia family and was selected as the Global Leader for Tomorrow for the year 2000 by the World Economic Forum. Mr Dilip Cherian has a long standing career in journalism and management consulting. Given the diverse and vast experience, the board is well-equipped to provide guidance and exercise oversight over the management.

Shareholding Pattern

Pre-IPO	Post-IPO
 <p>BCCL 100%*</p>	 <p>Public 15.25%</p> <p>BCCL 84.75%</p>
<p>Source: DRHP *Public shareholding is for 35 shares of the total 25 mn shares for which BCCL is the beneficial owner.</p>	<p>Source: DRHP *Public shareholding is for 35 shares of the total 25 mn shares for which BCCL is the beneficial owner.</p>

Annexure II: Profile of the Directors

Name of Directors	Designation	Age	Qualifications	Experience (years)	Previous Employment	Directorships / partnership in other entities
Mr Kushagra Bajaj	Non-executive Chairperson	33	B.Sc (in Economics, Political Philosophy & Finance), Carnegie Mellon University, USA Masters degree in science in marketing and finance from the Northwestern-University, Chicago	10+		Bajaj Hindusthan Limited. Bajaj Hindusthan Sugar & Industries Limited. Bajaj Capital Ventures Private Limited Bajaj Eco-Tec Products Limited Bajaj Trustee Company Private Limited Bajaj Consumer Care Limited
Mr Roshan Hinger	Vice Chairman and Whole time Director	69	B.Sc, University of Udaipur	45+		Bajaj Consumer Care Limited Bajaj ebiz Private Limited Esugar Clearing Corporation Limited Bajaj Infrastructure Development Company Limited
Mr Sumit Malhotra	Whole time Director	48	Bachelors In Pharmacy, Honours from Institute Of technology, Benaras Hindu University, Varanasi	23+	President, Sales & Marketing, BCCL	
Mr Haigreave Khaitan	Independent Non-Executive Director	39	Bachelors Degree in Law from Calcutta University. Member of Indian Law Institute, Indian council of Arbitration			Ceat Limited Dhunseri Tea & Industries Limited Harrisons Malyalam Limited Hindustan Composites Limited Inox Leisure Limited Jindal Steel & Power Limited Rama NewsPrint & Papers Limited Sterlite Technologies Limited The Madras Aluminium Company Limited The Oudh Sugar Mills Limited Bennett, Coleman & Company Limited BTS Investment Advisors Private Limited Great Eastern Energy Consumption Limited I.G.E (India) Limited Khaitan Consultants Limited Vinar Systems Private Limited
Mr Gaurav Dalmia	Independent Non-Executive Director	43	Bachelors in Computer Science, Salford University, UK Masters in Business Administration with Beta Gamma Sigma honors, Colombia University, USA			Debikay Systems Limited Dalmia Agencies Private Limited Artech Infosystems Private Limited First Capital India Limited Parag Parikh Financial Advisory Services Limited Infinity Technology Investments Private Limited Infinity Technology Trustee Private Limited Landmark Landholdings Private Limited Skylark Consultants Private Limited Artech Steel Industries Private Limited

					India Value Fund Advisors Private Limited Astir Properties Private Limited New Line Buildtech Private Limited Sukhm Infrastructure Private Limited Plus One Realtors Private Limited New Line Developers Private Limited IVF Advisors Private Limited
Mr Dilip Cherian	Independent Non-Executive Director	53	Bachelors in Economics, Presidency College Calcutta University Masters in Economics, Delhi School of Economics, Delhi	Worked as an Economic Consultant in Bureau of Industrial costs in the Ministry of Industry, GOI	Perfect Relations Limited Image Public Relations Private Limited Imprimis Life PR Private Limited Perfect PR Communications Services Private Limited College Hill Perfect Financial Relations Private Limited Accord Public Relations Private Limited Spring Sport and Sustainability Private Limited Webgyor.com Private Limited Mathew Easow Research Securities Limited Muzaffar Ali Communications Arts Private Limited Radio MID Day West Limited The Advertising Standard Council of India Nisco Ventures Private Limited
Mr Aditya Somani	Independent Non-Executive Director	36	Masters Degree in Commerce, Sydenham College, Mumbai PG Diploma in Business Management, S.P. Jain Institute of Management and Research, Mumbai Masters in Business Administration, Pittsburgh, USA		Everest Finvest Private Limited Falak Investments Private Limited Salaam Bombay Foundation White Knight Construction Private Limited Everest Industries Limited

Source: DRHP

Disclaimer

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