

Rationale for Gravita India Limited's IPO Grading

Gravita India Limited	IPO Grading: BWR IPO Grade 3 (Average Fundamentals)
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Brickwork Ratings (BWR) has assigned BWR IPO Grade 3 to the proposed IPO of Gravita India Limited (GIL). Brickwork Ratings' BWR IPO Grade 3 indicates average fundamentals for the issue in relation to its peers. BWR assigns IPO grading on a scale of IPO Grade 5 to IPO Grade 1, with Grade 5 signifying strong fundamentals and Grade 1 signifies poor fundamentals of the issue in relation to its peers.

The grading factors GIL's position in the Indian lead industry, good growth in sales over past five years, diversity in products, domestic and international expansion plans and management's 17 years experience in lead industry. However, the grading is constrained by highly competitive nature of lead industry, volatility in the lead prices, environment and health hazardous associated with lead industry. The project is not appraised by any Term lending institution and is fully funded by IPO proceeds and internal accruals.

Company Profile

Gravita India Limited is the flagship company of the Gravita group. Established by first generation entrepreneur in 1992 with unit at Jaipur, GIL manufactures lead alloy, lead oxides (lead sub-oxide, red lead, and litharge) and lead products (lead sheets, lead pipes etc.) by recycling & smelting. GIL has access to raw material through its global presence, which they import and purify it to 99.97% pure lead for export and domestic sales. The Company's finished products are used mainly in the battery industry apart from the glass, ceramic, pharmaceutical, paint and chemical industry.

The Group owns eight lead manufacturing units in operations presently, out of which two are in Asia and five are in African continent. Apart from lead processing, the Gravita Group is engaged in merchant trade of lead scrap, lead ore, lead concentrates, lead battery scrap and lead products. The Gravita Group also provides technical consultancy and engineering services for setting up of lead smelting & recycling projects / supply of plant & machinery on turnkey basis.

Management

GIL is promoted by entrepreneurs and technocrats Mr. Rajat Agarwal (aged 42 years) and Mr. Rajeev Surana (aged 41 years). Both the promoters have BE-Mechanical engineering degree. Dr. M.P. Agarwal, father of Mr Rajat Agarwal is also associated with the company and is the Honorary Chairman. Dr. Agarwal (aged 75 years) has MBBS and MD degrees in General Medicines.

Mr Rajat Agarwal has more than 15 years industrial management experience in India and abroad. He has travelled widely and attended various conferences, seminars & exhibitions in the field of lead metal & lead recycling. He has established various projects related to lead metal globally. Mr. Rajeev Surana oversees the activities related to setting up project from inception to

commissioning. He has good operational understanding and experience exceeding 14 years in the industry.

Mr. D.K.Govil is an independent director on the board. As a professional Banker, he has 35 years exposure in banking industry. Mr. Govil has served BOB Housing Finance Ltd., Jaipur in the capacity of Managing Director. He holds a bachelor degree in Engineer. Mr. Govil joined GIL's board on June 30, 2009. Mr. Arun Kumar Gupta is an independent director on the board. He has experience of working in various positions with Government of Rajasthan. Mr. Gupta is an engineering graduate from BITS, Pilani and joined GIL's board on August 11, 2009. Mr. Rajesh Patni is an independent director on the board. He has more than 30 years experience in construction industry. Mr. Patni is a commerce graduate and joined GIL's board on August 11, 2009.

Objective of the Issue

GIL is raising equity funds to expand manufacturing facilities at Jaipur and setting up new manufacturing facility at Wada, Maharashtra. The company is planning to expand its operations in Australia, Belarus, Chile and Mexico. GIL will be investing in overseas ventures in Sri Lanka, Senegal and Honduras. Table 1 gives the details of the total cost of the projects and its investment plans.

Table 1: Breakup of total project cost

Particulars	Amount (in ₹ Crore)	Total Amount (in ₹ Crore)
Set up additional manufacturing facilities at		
-Jaipur	7.23	
-Maharashtra	5.79	13.02
Invest in overseas ventures at		
- Sri Lanka- Navam Lanka Limited	1.50	
- Senegal - Pagrik Senegal SA	2.00	5.85
- Honduras - Gravita Honduras SA	2.35	
Invest in setting up manufacturing facilities at Australia, Belarus, Chile and Mexico		18.6
Margin money for working capital requirement		10
General corporate purposes		[·]
Expenses of the issue		[·]
Total		47.47

- Expansion at Jaipur plant will produce diversified lead products like lead wool, lead wire, lead sheets, and lead powder. The company feels there is a growing demand for these products.
- Wada plant has a strategic advantage due to its proximity to Mumbai sea-port. Wada unit will reduce transportation cost and result in 5% saving in its operating costs. The total capacity of the plant will be 8000 MT. This unit will cater to exports and lucrative South India lead market.

- Overseas expansion will help GIL to strengthen its business providing access to low cost raw material.
- Investment in Navam Lanka Ltd. (NLL), Sri Lanka, will help GIL increase its equity stake in the NLL. After the proposed investment the total holding of GIL in NLL would be 52% of the total issued capital and NLL will become GIL's subsidiary. This investment would enable the company to have strategic control over NLL.
- Part of the issue proceeds will be used as margin money for working capital needs. As per company estimates the Working Capital Gap for FY-2011 is ₹ 45.74 Crore which is financed by
 - Bank limits - ₹ 30.00 Crore
 - Internal Accruals – ₹ 5.74 Crore
 - Public Issue - ₹ 10.00 Crore

The implementation of the project is in an initial stage. GIL is yet to identify land for Wada unit. It proposes to acquire land for Jaipur unit from Group Company for ₹ 2.25 Crore. The agreement is not yet firmed up. Orders for the machineries and other equipments as a part of the expansion/new facilities at Jaipur and Maharashtra have not been placed as yet.

The company is in the process of exploring overseas location for set up of new project. This process is also in concept stage with the company having identified potential countries only. These projects will also need regulatory approvals.

Project Funding

To meet the funding requirements, GIL plans to issue 36, 00,000 Equity Shares of ₹ 10/- each at a premium to be decided later and internal accrual. The promoters are not participating in the public issue. Table 2 gives the shareholding pattern for GIL.

Table 2: Shareholding Pattern

	Pre-Issue (%)	Post-Issue (%)
Dr. M.P. Agarwal	27.29	-
Mr. Rajat Agrawal	48.63	-
Mr. Rajeev Surana	0.06	-
Mrs. Shashi Agarwal	7.34	-
Mrs. Anchal Agarwal	16.59	-
Mrs. Kavita Surana	0.03	-
Total Promoter and Promoter Group	99.94	73.52
Public Holding	0.06	26.48
Grand Total	100	100

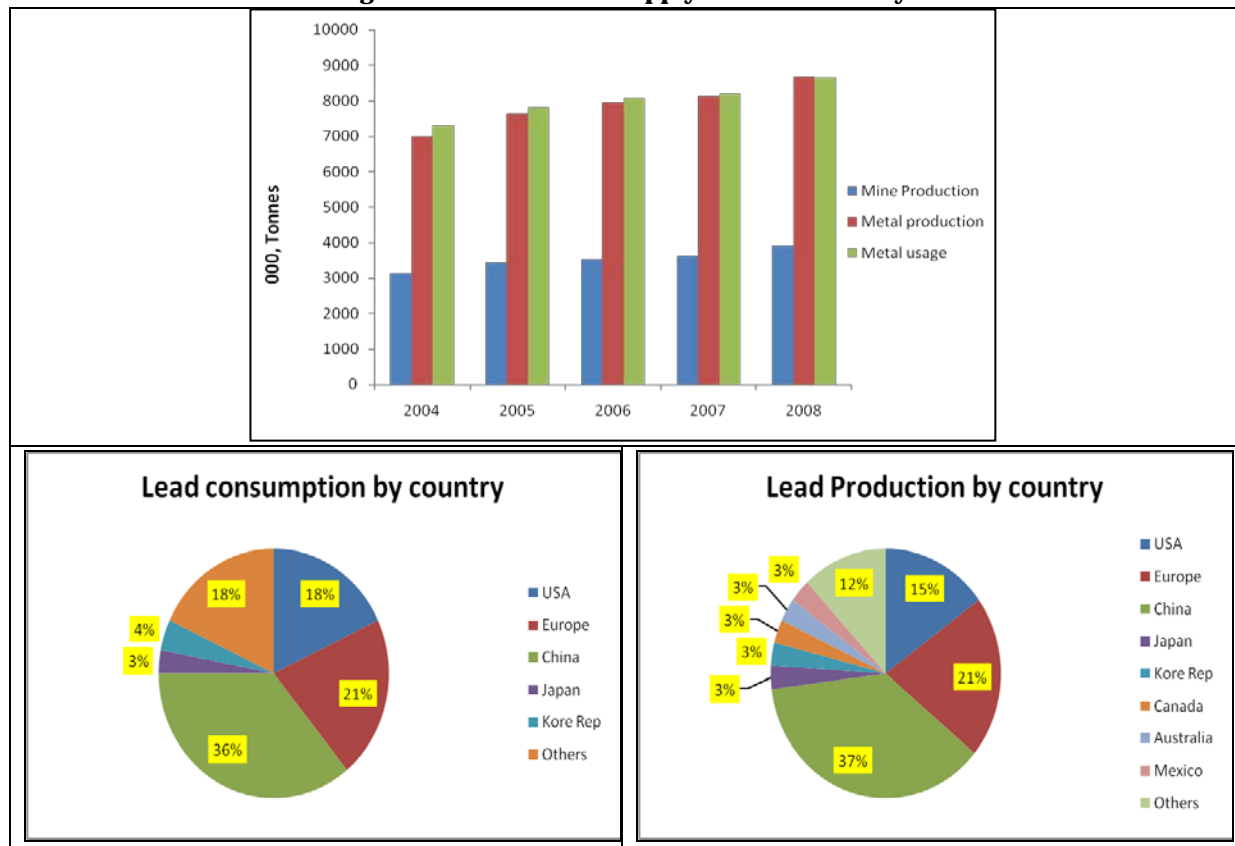
The funds requirement for the project is neither appraised nor tied-up with any term lending / financial institution. In absence of participation by term lending / financial institution the utilization of issue proceeds will be by the company.

The equity holding of promoters and their associates will be 73.52 percent of the issued capital at an average price of ₹ 6.66 per share on face value of ₹ 10 per share post issue.

Industry

Lead is one of man's most valuable commodities. The metal is mined and processed in some 60 countries. The usage worldwide increased from 4 million tonnes per annum in 1960's to 6 million tonnes in the 1990's to around 9 million tonnes per annum currently. Secondary production or recycling is the main source of lead vis-à-vis mining and accounts for almost around 70% of usage worldwide. Figure 1 gives the demand and supply of lead industry globally.

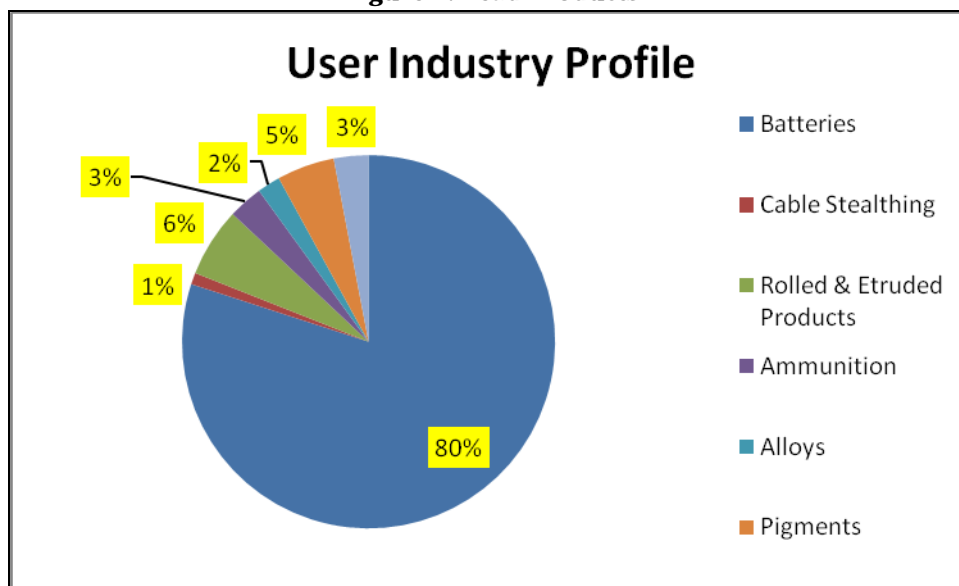
Figure 1: Demand and Supply of Lead Industry



Approximately 80 percent demand in lead is from batteries industry, mainly automobile batteries. Pigment industry is the next largest consumer of the lead, which consumes 5% of total production. Figure 2 gives the breakup of lead products and its demand.

The demand of lead is expected to increase in coming years due to growth in auto sector. It is expected that hybrid cars will be more in demand and usage in future and the hybrid car requirement for batteries is higher, adding to the demand for lead.

Figure 2: Lead Products



The estimated demand of lead in India is 500,000 tones. The demand is expected to grow at a rate of 6% which is being driven due to demand for automobile batteries and invertors and UPS applications. On the supply side Hindustan Zinc of the Vendanta Group contributes to 16% of the total supply in the country while the secondary smelters contribute 22% of lead supply, approximately 30% of supply is contributed by the unorganized sector and the balance is met by imports. In 2009, India produced 127,000 tonnes of lead concentrate of which Hindustan Zinc produced 65,000 tonnes. Due to the economic slowdown, lead production growth was restricted to 1.1%

Business Risk

GIL Jaipur unit is engaged in the manufacture lead metal and other lead products by recycling and smelting process. GIL is specialized in producing high quality pure lead ingots with minimum purity level of 99.97% by weight. The presence of GIL in global markets gives the Company access to raw materials in local markets at competitive costs. This, however, also exposes GIL to business risk as operation of subsidiaries in an efficient manner is a challenge. To mitigate this challenge Gravita exercises control over the operation activities by using MIS system at their corporate office.

Lead industry in India is highly competitive in nature, dominated by Hindustan Zinc as a primary smelter and unorganized sector as secondary smelter. GIL holds 2% of the total market share in India. The low market share in domestic market is a concern as there is growing demand of lead products in India and unorganized sector has an advantage to cater to local demands.

Lead is hazardous in nature and can cause serious damage to the environment. Ministry of Environment and Forests (MoEF) has framed Batteries (Management and Handling) Rules, 2001. These rules specify that only those who possess environmentally sound management systems and are registered with the MoEF / Central Pollution Control Board (CPCB) will be

allowed to carry out battery recycling. GIL being a CPCB certified company produces lead in environmental friendly conditions has an advantage over unorganized sector.

GIL's 52% revenue comes from export of lead which exposes GIL to foreign exchange risk. High volatility in lead prices brings commodity risk. In FY-09 GIL entered into derivate contracts for hedging commodity risk and foreign exchange risk, which shows GIL's ability to mitigate these risks.

GIL's capacity utilization for refined / alloy lead for FY10 was 39.50% up from 28.81% in FY2007 while that for unrefined/remelted lead increased to 19.39% from 2.7% during the same period. Capacity utilization of lead oxides (grey oxide, red lead, and litharge) has varied from 0.21% to 5.79% during FY10. It may be noted that the capacity utilization for grey oxide has significantly declined during the year due to limited demand as a result the company has taken conscious decision to limit their production against confirmed orders with guaranteed payments.

The proposed expansion at Jaipur plant will produce diversified lead products like lead wool, lead wire, lead sheets, and lead powder. The company feels there is a growing demand for these products particularly in aviation sector. Currently there are very few players in global market catering to the demand of the above mentioned products. Table 3 gives the details of the capacity utilization of the existing units of GIL Plant at Jaipur.

Table 3: Capacity Utilization

Particulars	FY 2007	FY 2008	FY 2009	FY2010
Unrefined / Remelted lead				
Installed cap (MTPA)	6000	6000	6000	6000
Utilization%	2.7	0.6	6.49	19.39
Refined / lead alloy				
Installed cap (MTPA)	12600	12600	12600	12600
Utilization%	28.81	30.58	40.99	39.50
Grey Oxide				
Installed cap (MTPA)	1800	1800	1800	1800
Utilization%	10.68	17.68	31.6	0.21
Red Lead				
Installed cap (MTPA)	1800	1800	1800	1800
Utilization%	0.52	1.83	0.36	0.60
Litharge				
Installed cap (MTPA)	1800	1800	1800	1800
Utilization%	4.24	6.77	1.97	5.79

Financial Performance

During FY10, on a consolidated basis, GIL saw an increase of revenue by 53%. Revenue for FY09 was ₹ 109.00 Crore and it increased to ₹ 166.97 Crore in FY10. This growth in revenue has been mainly due to increase in sales of products manufactured. Growth in sales of products manufactured by the company during FY10 was 61% while growth in revenue from products

traded was 21%. There was significant increase in sales from products traded by the company in FY09 (₹ 47.28 Crore as compared to ₹ 3.11 Crore in FY08) due to consolidation of Gravita Exim Ltd. which was made its subsidiary in FY09. Gravita Exim Ltd on a standalone basis contributed ₹ 15.21 Crore as revenue from products being traded. GIL has registered a good growth in revenues and net profits during the last 3 years. Table 4 gives the consolidated profit & loss of GIL.

Table 4: Abridged Profit and Loss (Consolidated) (Amount in ₹ Crore)

	2010	2009	2008	2007	2006
Sales:					
of Products manufactured by the company	105.62	66.69	46.70	18.92	2.07
of Products traded in by the company	58.79	47.28	3.11	3.59	0.45
Total	166.97	109.00	49.17	21.96	3.94
Total Expenditure:	148.36	99.40	44.75	19.33	2.56
EBDIT	18.61	9.58	4.42	2.63	1.37
Less: Depreciation	0.84	0.68	0.26	0.13	0.08
Less : Interest	1.12	1.67	0.41	0.19	0.01
Net Profit before tax	16.64	7.23	3.76	2.31	1.28
Net Profit	13.22	5.42	2.62	2.23	1.14

Table 5 gives the comparison of key financial ratios of GIL with other industry peers on standalone basis. It should be noted that High Net worth of peers is due to presence of Hindustan Zinc Ltd. among its peers. As the Hindustan Zinc Ltd. is a large producer of primary lead and Gravita India Ltd. is a producer of secondary lead, the key financial ratios may not be comparable.

Table 5: Key Financial Ratios (Standalone Figures as of March 10)

Company Name	Gravita India Ltd.	Peers Average
PBDITA/Total income	8.6%	18.3%
PAT/Total income	5.1%	10.9%
ROCE	40%	19.9%
Net worth (₹ Crore)	16.75	1741.1
Current ratio	6.46	1.7
Debt equity ratio	1.17	0.7
Interest cover	10.9	22.1
Inventory/Assets	29.6%	18.1%

Other factors

Due to change in the Exim Policy in the year 2002, the demand for Lead Oxides, primary product for the company, declined and the unit was out of production for a period of four years from 2001-02 to 2004-05. GIL has since diversified its product mix.

Changes in the accounting policy

In FY-09 the company has changed its accounting policy of providing depreciation from Written Down Value method to Straight Line Method. As per this change Depreciation on the Fixed Assets charged is ₹ 26.47 lakhs for the FY 09 as against ₹ 19.04 lakhs for the FY 08.

Compliance and Litigation

Litigations with government bodies:

- Litigation filed by DRI against Gravita India Ltd, the amount involved is ₹ 10.50 Lakhs.
- Litigation filed by DRI against a subsidiary Penta Exim, amount involved is ₹ 0.001 Lakh
- Litigation against Gravita Exim Ltd filed by Income Tax Department, amount involved is ₹ 32 Lakhs.

Litigations with business associates:

- Four labor cases against GIL including its subsidiaries for an amount of ₹ 10.1 Lakhs

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