

Rationale for CRISIL IPO Grading

(One time assessment)



Sejal Architectural Glass Ltd.

CRISIL IPO Grade 1.0/5.0

Bid/Offer Opens: *
Bid/Offer Closes: *
Shares Offered: 9,703,580
As % of post issue Equity: 34.66 per cent
Shares Outstanding (Post issue): 28,000,000

Lead Managers

Saffron Capital Advisors Private Limited

Registrar to the Issue

Intime Spectrum Registry Limited

Background: Sejal Architectural Glass Ltd (SAGL) was incorporated as a private limited company in 1998; its constitution was changed to a public limited company in March 1999. Promoted by members of the Gada family, SAGL is in the business of processing glass and is now setting up a float glass manufacturing plant that is expected to commence commercial operations in April 2009.

Highlights

Business prospects

- SAGL has garnered a moderate market share of about 15 per cent in the architectural glass processing business over the past 8 years
- The glass processing market in India is restricted to the relatively low-value architectural glass processing business. Competition is expected to intensify following the entry of more players into the market, especially large float glass manufacturers
- SAGL is likely to face stiff competition in the float glass business from incumbent well-established MNCs, as prices could go down post 2009
- Highly leveraged investment in float glass manufacturing could constrain the ability of the company to sustain price-competitiveness

Financial performance

- SAGL's revenues have grown by about 27 per cent over the past 3 years. It reported operating margins of 17.8 per cent and net margins of 6.9 per cent in 2006-07. The company's return on capital employed (RoCE) and return on equity (RoE) was 12.1 per cent and 12.2 per cent, respectively, during the same period.

Management capability

- Management has good understanding of business dynamics in glass trading and processing
- Management has not displayed the ability to generate adequate returns to justify the investments made in the glass processing business. The same gets reflected in an asset turnover of 1.1 and return on equity of 12.2 per cent in 2006-07.

Corporate governance

- Weak corporate governance structure and limited understanding of business operations by independent directors restricts their ability to effectively exercise management supervision
- The Board has ten directors, of which five are independent

Sejal Architectural Glass Ltd aims to raise Rs 1.0-1.2 billion by this proposed public issue of 9,703,580 equity shares

Detailed Rationale

SAGL: Shareholding pattern

Particulars	Pre-Issue		Post-Issue	
	No. of equity shares	%	No. of equity shares	%
Promoters	7,076,000	38.67%	7,076,000	25.27%
Promoter group	7,513,750	41.07%	7,513,750	26.83%
Others	3,706,670	20.26%	3,706,670	13.24%
Public	-	0.00%	9,703,580	34.66%
Total	18,296,420	100.00%	28,000,000	100.00%

Source: Company prospectus

SAGL: Past Financial performance

Particulars	unit	2005-06	2006-07
Operating income	Rs Million	301.2	393.5
Operating margins	Per cent	14.6	17.8
Net profits	Rs Million	20.9	27.1
Net margins	Per cent	6.9	6.9
ROCE	Per cent	16.8	12.1
Return on Equity	Per cent	25.4	12.2
No. of equity shares	Million	0.3	10.3
Net worth	Rs Million	84.4	360.1
Basic Earnings per share	Rs	69.7	2.6
Diluted Earnings per share	Rs	69.7	2.6
Book value	Rs per share	281.2	34.8
Gearing	Times	2.3	0.8

In order to arrive at the overall grade, CRISIL has considered the following broad parameters:

- Business prospects and financial performance
- Management capability
- Corporate governance

CRISIL has assigned a CRISIL IPO Grade '1/5' (pronounced 'one on five') to the proposed Initial Public Offering of Sejal Architectural Glass Ltd (SAGL). This grade indicates that the fundamentals of the issue are poor relative to 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, the graded instrument's future market price or its suitability for a particular investor.

In CRISIL's opinion, the grading reflects the challenges SAGL is likely to face as a glass processor in setting up a largely debt-funded float glass project (Float glass project cost is about Rs 4.8 billion with debt funding of about Rs 3.2 billion). The float glass industry, apart from being capital-intensive, is dominated by a few large global players and is characterised by profit cyclicality. SAGL has done well to become one of the five largest glass-processing companies in India over the last few years. However, its ability to stabilise and operate a float glass plant and also sell about six times its current volume of glass, remains to be seen. The grading also

reflects the below average corporate governance structure at SAGL.

Rising competitive intensity in glass processing

In a market characterised by low entry barriers and high competition, the company has created a moderate position for itself with a market share of about 15 per cent in architectural glass processing. This places it among the top five architectural glass processing companies in the country. However, in overall glass processing, that includes automotive and architectural glass, its share is less than 5 per cent in value terms.

Over the last 2-3 years, there have been increased efforts by float glass manufacturers such as Asahi India Glass Ltd, Saint Gobain etc, to augment their presence in the architectural glass processing space. With growth in commercial construction investments expected to remain buoyant over the medium term, we expect more number of processing players and float glass manufacturers to enter the architectural glass-processing segment, thereby resulting in intensified competition.

Likely to face stiff competition in float glass business from incumbent well-established MNCs and new entrants, where SAGL's debt burden will be a handicap

The market is currently dominated both domestically and internationally by a few well-established MNCs. Therefore, we believe SAGL's attempt to foray into the float glass segment is an audacious step, given the current size and the nature of its business operations. Additionally, with players like HNG Float Glass Ltd also venturing into this segment and likely to start commercial operations in 2009, competition is only expected to stiffen. Moreover, the fact that significant capacity will come on-stream during the time SAGL will commission its plant will put pressure on glass prices post 2009.

SAGL's float manufacturing business is highly debt-funded (Debt-equity of 2:1), thereby entailing high fixed capital charges. If price competition in the industry continues, the company's ability to sustain itself profitably would be suspect. This is because the MNC players are much better placed given the financial and technological support they receive from their parent companies.

Returns from past investments not encouraging

SAGL has grown at about 27 per cent in the past 3 years – revenues have grown from Rs 244 million in 2004-05 to Rs 394 million in 2006-07. However, its profitability has declined significantly over the same period, with net margins falling from 11.5 per cent to 6.9 per cent. The company has also not been able to generate adequate returns to justify the investments made in the glass processing business, as reflected in the declining asset turnover and declining return on net-worth and capital employed ratios.

In the future, while the company will show growth in its topline, its profitability will remain under pressure due to increased competition in both the glass processing and float glass business. SAGL's highly debt-funded capital investment in float glass manufacturing business will keep the returns depressed and exert pressure on its fund flows.

Limited management capability

The float glass project is expected to be completed on time, given that L&T is the EPC contractor for the same. However, there are concerns regarding the company's ability to operate a float glass manufacturing plant and execute business 10 times its current size, besides having

to compete with globally renowned MNCs. In addition, inadequate marketing strategy and dependency on the skills and experience of select professionals, who have been with the company for a relatively short period of time, do not inspire confidence in its ability to make a success of its future plans. Also, there is significant dependence on the promoters, especially Mr. Amrut Gada, for business direction and continuity.

Weak corporate governance structure limits the independent directors to exercise management control

The company's board of directors comprises five whole-time directors and five independent directors. Even though some independent directors have adequate professional experience, their awareness about the company's businesses is low. Given that the decision to set up a float plant was already made by the promoters before their appointments, they were not aware of the reason for venturing into float glass manufacturing or the manner in which the same was funded. They were also unaware of the presence of other promoter-owned entities in similar lines of business (which could potentially lead to conflict of interests). Additionally, they were uninformed of the share allotments that had been made at face value during August-October 2007; the proceeds from the same had been received in 2006-07. Therefore, CRISIL expects management supervision by independent directors to be limited.

Business profile

Sejal Architectural Glass Ltd (SAGL) was incorporated as a private limited company in 1998 and its constitution was changed to a public limited company in March 1999. Promoted by members of the Gada family, SAGL is in the business of processing glass and is now setting up a float glass manufacturing plant that is expected to begin commercial operations in April 2009.

SAGL started its commercial operations in 2000-01 by setting up a processing facility for insulating glass at Silvassa. Thereafter, in 2001, the company expanded its processing facility by setting up another facility for processing toughened glass. In both the processes the company has established brands such as "Kool Glass" and "Solid glass" that

together constituted over 70 per cent of the total share in revenues from the processing business in 2006-07. The company has added an automated lamination line for processing laminated glass since 2007 and has marketed its laminated glass products with brands such as “Armour glass” and “Fort glass”, which contributed over 15 per cent in revenue terms in its first year of operations (2006-07).

Float glass (clear and tinted) is the key raw material that the company procures from all key float glass manufacturers. Given the high bargaining power of float glass suppliers, availability of the right quality of float glass at the right time is of serious concern to standalone glass processors like SAGL.

SAGL proposes to enter into manufacture of float glass and has already acquired 150 acres of land from Gujarat Industrial Development Corporation (GIDC) at Jhagadia Industrial Estate at Dist. Bharuch, Gujarat. The project implementation has commenced from April 2007 and is expected to get completed by March 2009. The project cost has been estimated at Rs 4.8 billion, funded at a Debt/Equity ratio of 2:1. Hence, the company has raised debt to the tune of 3.2 billion from a consortium of banks, at 10 per cent per annum, with monthly rests to be linked to the PLR of the lead bank. The plant construction is being executed by L&T, which is its EPC contractor, and its installed capacity is envisaged at 2,00,750 MT per annum.

Financial profile

SAGL’s revenues have grown by about 27 per cent over the past 3 years, with operating margins rising to 17.8 per cent in 2006-07 from 14.6 per cent in 2005-06. The net margins of the company, however, remained close to 7 per cent in both the years. The debtors’ position has worsened significantly from about 80 days during 2004-05 to 132 days during 2006-07. The company’s RoCE and RoE was 12.1 per cent and 12.2 per cent, respectively, in 2006-07.

Profile of Management and Board

SAGL is headed by its founder promoter Mr Amrut S. Gada who started out with a glass trading retail shop in 1991 and has been the key driving force behind the company’s business growth in general. He is supported by executive directors - Mr. Dhiraj S Gada, Mr. Mitesh Gada, Dr. R Subramanian and Mr. Ashish D. Karia.

The company’s board of directors comprises five whole-time directors and five independent directors. All independent directors on board - Mr. Atul S. Bharani, Mr. Praful N. Satra, Ms. Vimla M. Shah, Mr. Hasmukh N. Shah and Mr. Mitil R. Chokshi joined the board since October 2007.

Board of Directors

Name	Designation	Age	Date of Joining	Qualification / Experience	Other Directorships
Amrut S Gada	Managing Director	37	Apr-99	Has been in glass business for over 15 years.	Sejal Glass Craft Pvt. Ltd., Sejal International Ltd., Sejal Insurance Broking Ltd., Sejal Float Glass Limited, Sejal Finance Ltd.
Dhiraj S Gada	Joint Managing Director	34	Sep-05	F-MBA (NMIMS, Mumbai) ¹ .	Sejal Glass Craft Pvt. Ltd., Sejal International Ltd., Sejal Insurance Broking Ltd., Sejal Float Glass Limited, Sejal Finance Ltd.
Mitesh K Gada	Whole Time Director	29	Oct-07	F-MBA (NMIMS, Mumbai) ¹	Sejal Glass Craft Pvt. Ltd., Sejal International Ltd., Sejal Float Glass Limited
R Subramanian	Whole Time Director	54	Sep-06	B-Tech IIT- Madras.	None
Ashish D Karia	Whole Time Director	29	Sep-07	Has been associated with paper industry for the past 13 years	Hero Multipap Pvt. Ltd., Sejal Float Glass Ltd.
Atul S Bharani	Independent Director	51	Sep-07	He is into the real estate business and is a promoter of the Sunshine group. Chairman of Progressive Co operative Bank Limited.	Private Ltd. Companies: Jayanti Agency, Sunshine Housing Development, Navketan Premises, Saumya Leasing, Mayurpankh Fine Builders, Mayurpankh Properties, Aarts Module International, Sunshine Projects, Panchratna Realtors, Sun-N- shine Entertainers, Sunshine Tracon, Sunshine Housing, Sunrise Housecon
Praful N Satra	Independent Director	43	Oct-07	He is the CMD of Satra Properties.	Satra Properties (India) Ltd, Satra Properties Developers Pvt. Ltd, Savla Realtors and Developers Pvt Ltd, Shravan Developers Pvt Ltd, Prime Multi Tiles Trading Pvt Ltd, Satra Infrastructure Development Pvt Ltd, Satra Land Development Pvt Ltd, BKC Developers Pvt Ltd, Anupam Stock Broking Pvt Ltd, Satra Novelities Pvt Ltd, Satra Retail Pvt Ltd, Satra Reality and Builders Ltd, Satra Redevelopment Company Limited, Satra Property Development Pvt Limited, Sangam Capital Services Ltd
Vimla M Shah	Independent Director	42	Oct-07	LLB (Mumbai University).	None
Hasmukh N Shah	Independent Director	43	Oct-07	CA, CS, LLB, CPA.	None
Mitil R Chokshi	Independent Director	37	Oct-07	CA, ICWA.	Steve Cragg Advertising Private Limited, Ravin Cables Limited, Citco India Services Private

Note: ¹F-MBA (Family Management Business Administration)

Source: Company prospectus

Disclaimer

A CRISIL IPO grading is a one-time assessment and reflects CRISIL's current opinion on the fundamentals of the graded equity issue in relation to other listed equity securities in India. A CRISIL IPO grading is neither an audit of the issuer by CRISIL nor is it a credit rating. Every CRISIL IPO grading is based on the information provided by the issuer or obtained by CRISIL from sources it considers reliable. CRISIL does not guarantee the completeness or accuracy of the information on which the grading is based. A CRISIL IPO grading is not a recommendation to buy / sell or hold the graded instrument; it does not comment on the issue price, future market price or suitability for a particular investor.

CRISIL is not responsible for any errors and especially states that it has no financial liability whatsoever to the subscribers / users / transmitters / distributors of CRISIL IPO gradings. For information on any IPO grading assigned by CRISIL, please contact 'Client Servicing' at +91-22-66913561, or via email: clientservicing@crisil.com.

For more information on CRISIL IPO Gradings, please visit <http://www.crisil.com/ipo-gradings>