Sharekhan by BNP PARIBAS

UltraTech Cement

Outperformance amidst unprecedented times

Sector: Cement
Result Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 4,136**	
Price Target: **Rs. 5,000**	↑

↑ Upgrade ↔ No change ↓ Downgrade

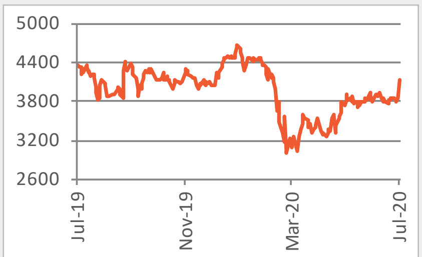
Company details

Market cap:	Rs. 119,367 cr
52-week high/low:	Rs. 4,753/2,913
NSE volume: (No of shares)	5.3 lakh
BSE code:	532538
NSE code:	ULTRACEMCO
Sharekhan code:	ULTRACEMCO
Free float: (No of shares)	11.5 cr

Shareholding (%)

Promoters	60.0
FII	16.4
DII	14.4
Others	9.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	8.6	20.4	-9.5	-5.3
Relative to Sensex	-1.5	2.8	-2.9	-7.5

Sharekhan Research, Bloomberg

UltraTech Cement (UltraTech) reported strong operational performance during Q1FY2021, much ahead of our as well as street's estimates. The company's standalone revenue declined by 33% y-o-y to Rs. 7,374 crore, owing to a 32% y-o-y decline in volume (including Century's assets), while blended realisations dipped by 1.8% y-o-y (although up 4.8% q-o-q). COVID-19 led nationwide lockdown during April affected volumes, which were broadly in line with estimates. The company witnessed strong demand from the rural sector (~35% of overall cement demand), which led to higher trade sales during the quarter (78% share). The company reported strong EBITDA/tonne of Rs. 1,403, which was led by the decline in key input costs per tonne viz. power and fuel (down 15% y-o-y), freight (down 9% y-o-y), and other expense (down 10% y-o-y). Operating profit declined by 30% y-o-y to Rs. 1,955 crore (much higher than estimate). Strong operational performance along with higher other income, lower interest expense, lower depreciation, and lower effective tax rate led to higher-than-expected adjusted net profit of Rs. 914 crore (adjusting for Rs. 108 crore exceptional expense). The company expects rural demand to sustain, led by good monsoon, while non-trade demand is expected to pick up post Diwali, as labourers return to project sites and the government fast tracks infrastructure investments. However, the company is also witnessing an increase in diesel prices and pet coke prices, the impact of which may get reflected over the coming quarters. The company has kick started its capex plan with an increase of Rs. 500 crore to Rs. 1,500 crore for FY2021, which highlights management's confidence in recovery of cement demand going ahead. The company has also reduced net debt by Rs. 2,209 crore during Q1, aided by reduction in working capital (~Rs. 600 crore excluding one-time provisions). We have increased our earnings estimates for FY2021E-FY2022E, factoring better OPM in light of lower fixed cost expense. We have also increased our valuation multiple marginally, factoring early cycle recovery. Hence, we have maintained our Buy rating on the stock with a revised price target (PT) of Rs. 5,000.

Key positives

- Strong beat on EBITDA/tonne,led by major cost savings in key input costs.
- Consolidated net debt reduction of Rs. 2,209 crore in Q1FY2021, reducing net debt/EBITDA to 1.44x from 1.55x in FY2020.
- Capex plan for FY2021 increased by Rs. 500 crore to Rs. 1,500 crore.

Key negatives

- Cement offtake in the non-trade segment remained weak affected by COVID-19 pandemic.
- Yet to find buyers for Dubai and Europe units.

Our Call

Valuation –Maintain Buy with a revised PT of Rs. 5,000: UltraTech has shown strong operational outperformance during Q1FY2021. Going ahead, the company is expected to benefit from sustained rural demand, led by good monsoon, return of labourers at project sites post Diwali, and kick start of government infrastructure investments from Q3FY2021. However, rise in pet coke and diesel prices would be key monitorables going ahead. Further, the company has been able to grow inorganically, improving profitability of the acquired assets and at the same time improving balance sheet quality. We have increased our earnings estimates for FY2021E-FY2022E, factoring better OPM in light of lower fixed cost expense. We have also increased our valuation multiple marginally, factoring early cycle recovery. Hence, we have maintained our Buy rating on the stock with a revised PT of Rs. 5,000.

Key Risks

Weak macro environment leading to lower cement demand and pressure on cement prices negatively affects profitability.

Valuation (Standalone) Rs cr

Particulars	FY19	FY20	FY21E	FY22E
Revenue	39,999	40,649	37,493	43,289
OPM (%)	18.9%	23.1%	24.1%	24.2%
Adjusted PAT	2,526	3,652	3,331	4,331
% YoY growth	6.2%	44.6%	-8.8%	30.0%
Adjusted EPS (Rs.)	87.5	126.5	115.4	150.1
P/E (x)	47.2	32.7	35.8	27.6
P/B (x)	3.6	3.1	2.9	2.6
EV/EBITDA (x)	18.7	14.7	15.0	12.6
RoNW (%)	8.5%	10.2%	8.4%	10.0%
RoCE (%)	7.6%	8.8%	7.7%	8.9%

Source: Company; Sharekhan estimates

Higher realisations and contained costs limit impact of weak offtake: UltraTech reported restated financials with effect from May 20, 2018, to include cement business financials of Century.During Q1FY2021, UltraTech's standalone net sales declined by 33.2% y-o-y to Rs. 7,374 crore owing to a 32% y-o-y decline in sales volume (affected by COVID-19 led nationwide lockdown during April 2020). Blended realisationdeclined by 1.8% y-o-y (although up 4.8% q-o-q). The company operated on an average 46% capacity utilisation during the quarter in which it operated at 60%+ capacity utilisation during May-June 2020. Further, during July 2020, its capacity utilisation is estimated at 60-65%. The company surprised on operational profitability with blended EBITDA/tonne of Rs. 1,403, which came in much higher than our estimate. The company reported a steep decline in key input costs on per tonne basis, viz. power and fuel cost (down 15% y-o-y), freight cost (down 9% y-o-y), and other expense (down 10% y-o-y). During Q1, Century reported EBITDA/tonne of Rs. 900+ (as against Rs. 575 during Q4FY2020). Overall, standalone operating profit declined by 29.9% y-o-y to Rs. 1,955 crore, which was much higher than our estimate. Further, higher other income (up 88.4% y-o-y), lower interest expense (down 22.8% y-o-y), lower depreciation (down 6% y-o-y), and lower effective tax rate (31.3% versus 33% in Q1FY2020) led to decline in adjusted net profit at Rs. 914 crore (adjusting for Rs. 157 crore exceptional expense).

Reviving capacity expansion plans: The company increased capital expenditure target for FY2021 by Rs. 500 crore to Rs. 1,500 crore. The two Brownfield projects (0.6MT each in Bihar and West Bengal) are expected to be completed by early next fiscal year. The 2.3mtpa Dalla Super unit, U.P. (Rs. 120 crore capex left), would be coming up in next fiscal year. The work on Pali, Rajasthan, is expected to start next fiscal year and is expected to commence in October to December 2022 quarter. UltraTech will also be working on one Greenfield project (2.2MT in Odisha). The company would also be doing capex on Bicharpur coal block (~Rs. 120 crore) apart from incurring maintenance capex during FY2021 (~Rs. 600 crore).

Key Conference takeaways

- **Capacity utilisation:** The company operated at an average capacity utilisation of 46% during Q1FY2021, where during the last two months, it had operated at 60%+ capacity utilisation. During July 2020, the company's assets are operating at 60-65% capacity utilisation.
- **Demand-driven by the rural sector:** Cement demand during Q1FY2021 was driven by the rural sector (IHB, which accounts for ~35% of the demand), which led to increased retail share in total volumes to 78%. The company expects non-trade demand from November (post Diwali), as labourers return and the government fast tracks infrastructure investments.
- **China asset sale:** The company expects sale proceeds of Rs. 700 crore from its stake sale in Chinese arm in August 2020, which will be further utilised in reducing leverage.
- **Capex:** The company increased its capital expenditure for FY2021 to Rs. 1,500 crore from Rs. 1,000 crore earlier. The two Brownfield projects (0.6MT each in Bihar and West Bengal) are expected to be completed by early next fiscal year. The 2.3mtpa Dalla Super unit, U.P., would be coming up in next fiscal year. The work on Pali, Rajasthan, is expected to start next fiscal year and is expected to commence in October to December 2022 quarter.
- **Non-core asset sale:** The company has not found any buyers for its Dubai unit and down selling of loans outstanding in its fibre glass unit in Europe. If the company does not find any buyer for its Dubai unit, it may look to operate it.
- **Net debt reduction:** The company was able to reduce its net debt by Rs. 2,209 crore during the quarter. The company reduced working capital by Rs. 600 crore (excluding one-time provisions) during the quarter.
- **Key input cost may rise:** Diesel prices have risen by 15% in June versus April, while pet coke prices are currently at $75 as against the low of $60 in April 2020. Hence, the company expects the impact of rising key costs in the coming quarters.

Financials (Standalone) Rs cr

Particulars	Q1FY2021	Q1FY2020	% yoy	Q4FY2020	% qoq
Net Sales	**7,373.6**	**11,036.9**	**-33.2%**	**10,359.4**	**-28.8%**
Operating Profit	**1,955.2**	**2,790.9**	**-29.9%**	**2,262.3**	**-13.6%**
Other Income	296.1	157.2	88.4%	223.9	32.2%
EBITDA	2,251.3	2,948.1	-23.6%	2,486.2	-9.4%
Interest	333.4	432.1	-22.8%	432.4	-22.9%
Depreciation	588.7	626.0	-6.0%	609.0	-3.3%
PBT	**1,329.2**	**1,890.0**	**-29.7%**	**1,444.8**	**-8.0%**
Tax	415.6	623.1	-33.3%	341.8	21.6%
Adj.PAT	**913.6**	**1,266.9**	**-27.9%**	**1,103.0**	**-17.2%**
Margins			**Bps**		**Bps**
OPM	26.5%	25.3%	123	21.8%	468
PATM	12.4%	11.5%	91	10.6%	174
Tax Rate	31.3%	33.0%	-170	23.7%	761

Source: Company; Sharekhan Research

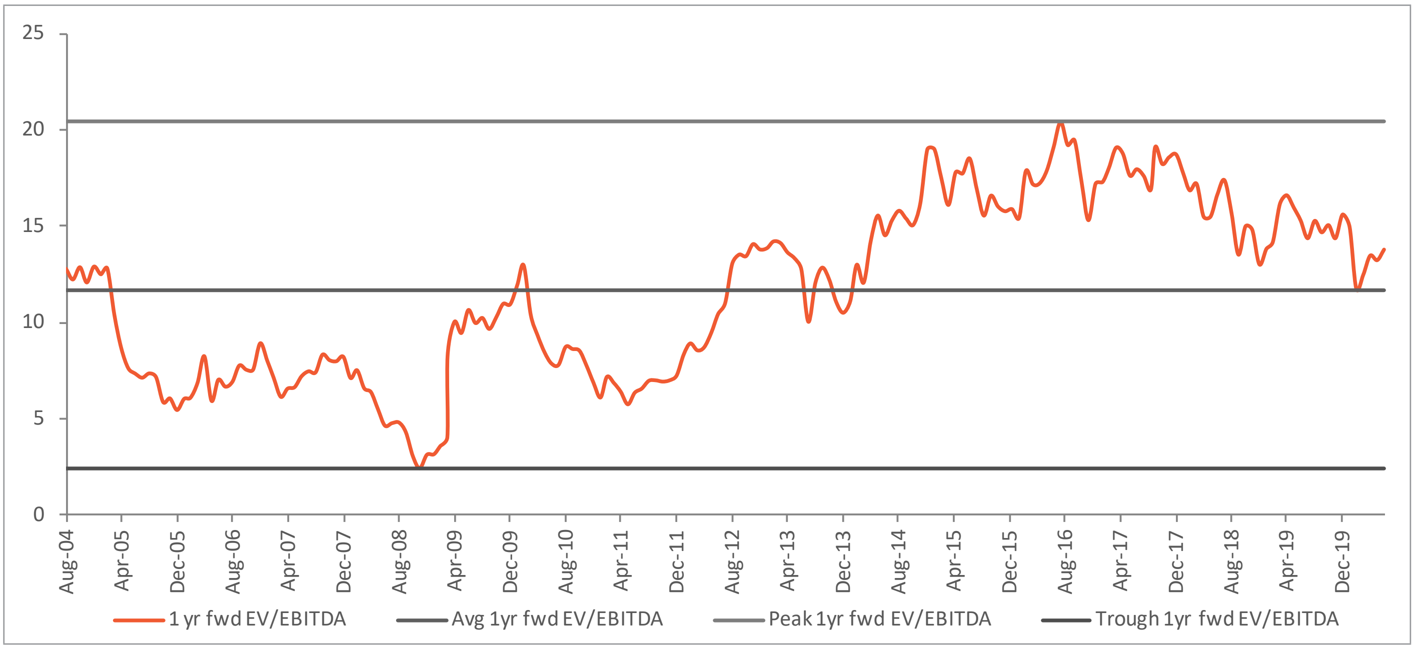
Outlook

Expect demand to improve going ahead: COVID-19 pandemic has affected cement volume offtake since mid-March 2020, whileUltraTech had commenced operations from the third week of April 2020,which had affected volume during Q1FY2021. The company sees rural demand to sustain going ahead because of good monsoon and higher MSPs. The non-trade segment is expected to pick up from H2FY2020 as labourers return to project sites, while the government kick starts infrastructure investments. Going ahead, we expect cement demand to gradually improve with cement demand bouncing back in FY2022. In the interim, as cement players defer capacity expansion plans for atleast a year, it would aid in maintaining healthy pricing discipline in the industry,thereby supporting overall profitability.

Valuation

Maintain Buy with a revised PT of Rs. 5,000: UltraTech has shown strong operational outperformance during Q1FY2021. Going ahead, it is expected to benefit from sustained rural demand led by good monsoon, return of labourers at project sites post Diwali, and kick start of government infrastructure investments from Q3FY2021. However, rise in pet coke and diesel prices would be key monitorables going ahead. Further, the company has been able to grow inorganically, improving profitability of the acquired assets, and at the same time improving balance sheet quality. We have increased our earnings estimates for FY2021E-FY2022E, factoring better OPM in light of lower fixed cost expense. We have also increased our valuation multiple marginally, factoring early cycle recovery. Hence, we have maintained our Buy rating on the stock with a revised PT of Rs. 5,000.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer valuation

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
UltraTech Cement	35.8	27.6	15.0	12.6	2.9	2.6	8.4	10.0
Shree Cement	58.7	42.7	21.1	17.0	5.6	5.1	10.0	12.5
The Ramco Cement	32.6	24.0	18.0	14.1	3.1	2.8	10.1	12.4
JK Lakshmi Cement	16.9	12.5	6.1	5.1	1.7	1.5	10.8	13.1

Source: Sharekhan Research

About company

UltraTech's parent company, Aditya Birla Group, is in the league of Fortune 500 companies.UltraTech is the largest manufacturer of grey cement, ready mix concrete (RMC), and white cement in India. The companyis also one of the leading cement producers globally.The company has a consolidated capacity of 117.4mtpaof grey cement. UltraTech has 20 integrated plants, 1 clinkerisation plant, 26 grinding units, and 7 bulk terminals.

Investment theme

UltraTech is India's largest cement company. We expect UltraTech to report industry-leading volume growth on account of timely capacity expansion (acquisition of Jaypee Group's cement assets, Century's assets, and Binani Cement's assets) and likely revival in demand (with the start of affordable housing projects and enhanced spending on infrastructure development).We expect the company to be the biggest beneficiary of multi-year industry upcycle, being a market leader and its timely scaling up of capacities and profitability in the shortest possible time.

Key Risks

- Slowdown in government spending on infrastructure and increased key input costs led by pet coke and diesel prices.
- Slowdown in the housing sector, especially affordable housing projects.
- Inability to improve capacity utilisation and profitability of acquired units.

Additional Data

Key management personnel

Mr. Kumar Mangalam Birla	Non Independent Director-Chairman
Mr. KK Maheshwari	Managing Director
Mr. Atul Daga	Executive Director & CFO
Mr. Sanjeeb K Chatterjee	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Grasim Industries Ltd	57.29
2	Life Insurance Corp of India	3.87
3	Pilani Investment & Industries Cor	1.6
4	Standard Life Aberdeen PLC	1.47
5	Franklin Resources Inc	1.39
6	Vanguard Group Inc/The	1.36
7	JPMorgan Chase & Co	1.36
8	BlackRock Inc	1.21
9	ICICI Prudential Life Insurance Co	1.11
10	SBI Funds Management Pvt Ltd	0.96

Source: Bloomberg

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