Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

UltraTech Cement Ltd

One-off Q3; Outlook upbeat

Cement	Sharekhan code: ULTRACEMCO
Reco/View: Buy ↔	CMP: Rs. 7,868 / Price Target: Rs. 9,200 ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING Updated Oct 08, 2021	34.10

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

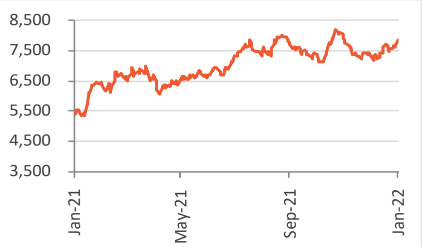
Company details

Market cap:	Rs. 227,119 cr
52-week high/low:	Rs. 8267/5262
NSE volume: (No of shares)	5.9 lakh
BSE code:	532538
NSE code:	ULTRACEMCO
Free float: (No of shares)	11.6 cr

Shareholding (%)

Promoters	60.0
FII	15.7
DII	15.3
Others	9.0

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.8	6.4	7.6	45.9
Relative to Sensex	0.0	7.1	-9.1	19.7

Sharekhan Research, Bloomberg

Summary

- We maintain Buy on UltraTech Cement (UltraTech) with a revised PT of Rs. 9,200, factoring sustained healthy demand environment over FY2022-FY2024.
- In Q3FY2022, UltraTech reported broadly in-line performance as marginally lower-than-expected volumes were offset by higher realisation. Consolidated net debt reduced sequentially by Rs. 189 crore.
- Management expects Q4FY2022 to see y-o-y volume growth, as demand rebounds post one-off weak November. Management expects FY2023 to witness healthy demand, led by infrastructure, rural housing, and urban housing.
- The company announced almost doubling of white cement capacity. Balance grey cement capacity expansion of 16.3mtpa remains on track and is expected to come onstream in FY2023.

UltraTech Cement (UltraTech) reported broadly in-line operational performance, with marginally lower-than-expected volumes getting compensated by higher realisation. The company's standalone revenue rose by 5.4% y-o-y to Rs. 12,471 crore, led by 11.4% y-o-y rise in blended realisation, while volumes declined by 5.4% y-o-y. The company reported blended EBITDA/tonne of Rs. 1,029 (-20.3% y-o-y), marginally lower than our estimate of Rs. 1,075. Adjusting for Rs. 535 crore reversal of tax, adjusted net profit declined by 29.3% y-o-y to Rs. 1,096 crore, which was marginally lower than our estimate.

Key positives

- Blended realisation increased by 11.4% y-o-y at Rs. 5,776/tonne.Interest expense declined by 45% y-o-y. Consolidated net debt reduced by Rs. 189 crore q-o-q.
- Announcement of almost doubling of white cement capacity to 12.5 lakh tonne per annum by 2026.

Key negatives

- Cement volume declined by 5.4% y-o-y due to weak November, affected by NCR construction ban, extended monsoons in South, sand availability issues in East as well as parts of U.P., and the festive season.
- Cost of production increased by 21.9% y-o-y with rise seen across the cost structure.

Management Commentary

- Management expects to achieve volume growth on a y-o-y basis in Q4FY2022 despite high base as demand has rebounded in December 2021 and January till date.
- Management expects healthy demand growth for FY2023, given general elections in 2024. Declining pet coke prices to start reflecting from Q1FY2023.
- Capacity expansion plans of 16.3 million tonne per annum (mtpa) post addition of 3.2mtpa during H2FY2022 till date remain on track.

Revision in estimates – We have revised our net profit estimates for FY2022, factoring higher cost structure, while largely maintaining FY2023-FY2024 estimates.

Our Call

Valuation – Maintain Buy with a revised PT of Rs. 9,200: UltraTech is expected to benefit from expected healthy cement demand over the long term, driven by its timely capacity expansion plans. The demand environment is expected to be strong from segments such as infrastructure, rural housing, and urban housing. Easing of power and fuel costs along with expectation of price hikes is likely to maintain healthy operational profitability. We believe the company's capacity expansion coupled with de-leveraging of balance sheet over the next three years is expected to drive earnings over FY2022-FY2024. We continue to maintain our Buy rating on the stock with a revised price target (PT) of Rs. 9,200.

Key Risks

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

Valuation (Standalone) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	43,188	51,568	57,916	66,134
OPM (%)	27.2%	23.8%	24.5%	24.7%
Adjusted PAT	5,457	6,058	7,416	8,873
% YoY growth	49.4%	11.0%	22.4%	19.6%
Adjusted EPS (Rs.)	189.1	209.9	257.0	307.4
P/E (x)	41.6	37.5	30.6	25.6
P/B (x)	5.2	4.6	4.0	3.5
EV/EBITDA (x)	20.5	19.1	16.0	13.1
RoNW (%)	13.4%	13.1%	14.1%	14.7%
RoCE (%)	10.8%	11.0%	12.6%	13.6%

Source: Company; Sharekhan estimates

Broadly in-line performance

UltraTech reported standalone net revenue growth of 5.4% y-o-y at Rs. 12,471 crore, which was largely in-line with our estimates. Cement volumes declined by 5.4% y-o-y (+7.4% q-o-q) to 21.6 million tonne, while blended realisation increased by 11.4% y-o-y (+0.6% q-o-q) at Rs. 5,776/tonne. The company's blended standalone EBITDA/tonne at Rs. 1,029 (-20.3% y-o-y, -20.4% q-o-q) was marginally below our estimate of Rs. 1,075/ tonne. Power and fuel costs stood at Rs. 1,344/tonne (+40.6% y-o-y, +19.4% q-o-q), freights cost stood at Rs. 1,326/tonne (+7.5% y-o-y, +1.1% q-o-q), and other expense stood at Rs. 766/tonne (+23.6% y-o-y, -2.7% q-o-q). Further, the decline in operating profit was partially offset by lower interest expense (-45.1% y-o-y), which led to adjusted standalone net profit (excluding reversal of Rs. 535 crore provision of tax) decline by 29.3% y-o-y (-15.7% q-o-q) to Rs. 1,096 crore (marginally below our estimate). The company's consolidated net debt declined by Rs. 189 crore q-o-q to Rs. 6,147 crore (net debt/EBITDA of 0.49x).

Healthy outlook post weak November

The cement industry is said to have suffered from a weak November 2021, which was affected by multiple factors such as NCR construction ban, extended monsoons in South, sand availability issues in East as well as parts of U.P., and the festive season. However, the company saw demand bouncing back from December 2021, with capacity utilisation increasing to 85% from the trough of below 70% in November 2021. The company expects Q4FY2022 to see y-o-y volume growth despite high base, while FY2023 is slated to see healthy demand with traction seen in demand from infrastructure, rural housing, and urban housing. On the cost front, the decline in pet coke prices post a high in November 2021 would reflect from Q1FY2023, which along with expected price hikes should lead to better operating margins. The company also announced almost doubling of its white cement capacity to 12.5 lakh tonne per annum, while its balance 16.3mtpa capacity expansion plan remains on track and is scheduled to get completed during FY2023.

Key Conference takeaways:

- **Q3FY2022 performance:** The quarter saw unexpected decline in demand in November with the eastern region witnessing the highest slump. North was relatively strong, performing better than other markets. Unexpected rains, construction ban in NCR, labour availability, and sand shortages affected demand in November. However, demand picked up from December, with the company's capacity utilisation at 84% compared to 75% in Q3FY2022 and below 70% trough in November.
- **Cement prices:** The company expects price hikes to take place going ahead. Cement prices in Q3FY2022 were flat q-o-q. Prices in East, some parts of Maharashtra, and Kerala have increased.
- **Outlook:** The company expects to achieve volume growth in Q4FY2022 despite higher base. The company expects FY2023 to see good growth given general elections in 2024.
- **Expansion plan:** The company commissioned 3.2mtpa new cement capacity, taking total capacity in India to 114.55mtpa. The balance 16.3mtpa capacity would be commissioned in FY2023.
- **White cement expansion:** The board approved capacity expansion of white cement capacity from 6.5ltpa to 12.5ltpa, which is expected to fully commission by 2026 due to delay in land acquisitions. The current putty capacity is 8.2ltpa, and it is in midst of completing 4.4ltpa Greenfield expansion with the project to go on schedule in Q2FY2023.
- **Construction chemical business:** The company expects the business to achieve Rs. 500 crore by the end of the year. Three years down the line, the company expects Rs. 2,500 crore from the business.
- **Debt:** The company prepaid loans of Rs. 3,549 crore from treasury.
- **Costs:** Costs are expected to remain at elevated levels during Q4FY2022. In Q3FY2022, pet coke consumption was 25% and higher share of high calorific value of imported coal.

- **Green energy:** The WHRS capacity stands at 156 MW and solar capacity is at 221 MW, currently at 16% green energy capacity. It expects to achieve 34% share of green energy by 2024 end.
- **Asset Sale:** The fibre glass asset sale is expected to be closed in Q4FY2022 for Euros 90 million.
- **Capex:** The company spent close to Rs. 4,000 crore during 9MFY2022 and expects to make capex of Rs. 5,000 crore in FY2022. In FY2023, it expects Rs. 4,000 crore capex, including maintenance capex (Rs. 1,000 crore-1,500 crore).
- **Other highlights:** The trade mix was 64%.

Results (Standalone) Rs cr

Particulars	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)
Net Sales	**12,470.6**	**11,830.6**	**5.4%**	**11,548.4**	**8.0%**
Operating Profit	**2,221.5**	**2,944.5**	**-24.6%**	**2,600.0**	**-14.6%**
Other Income	108.8	261.6	-58.4%	141.8	-23.3%
EBITDA	2,330.3	3,206.1	-27.3%	2,741.8	-15.0%
Interest	165.0	300.7	-45.1%	182.8	-9.7%
Depreciation	608.9	602.2	1.1%	612.7	-0.6%
PBT	**1,556.4**	**2,303.3**	**-32.4%**	**1,946.3**	**-20.0%**
Tax	460.1	753.0	-38.9%	646.2	-28.8%
Adj.PAT	**1,096.3**	**1,550.3**	**-29.3%**	**1,300.1**	**-15.7%**
Margins			**Bps**		**Bps**
OPM	17.8%	24.9%	-708	22.5%	-470
PATM	8.8%	13.1%	-431	11.3%	-247
Tax Rate	29.6%	32.7%	-313	33.2%	-364

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Improving demand brightens outlook

The cement industry has seen sustained improvement in demand in the past 15 years, barring a couple of years, while regional cement prices have been on a rising trajectory over the trailing five years. Amidst COVID-19 led disruption, the cement industry continued to witness healthy demand from the rural sector, while infrastructure demand has started to pick up. The sector's long-term growth triggers in terms of low per capita consumption and demand pegged at 1.2x GDP remain intact. Evidently, the government's Rs. 111 lakh crore infrastructure investment plan from FY2020 to FY2025 would lead to a healthy demand environment going ahead.

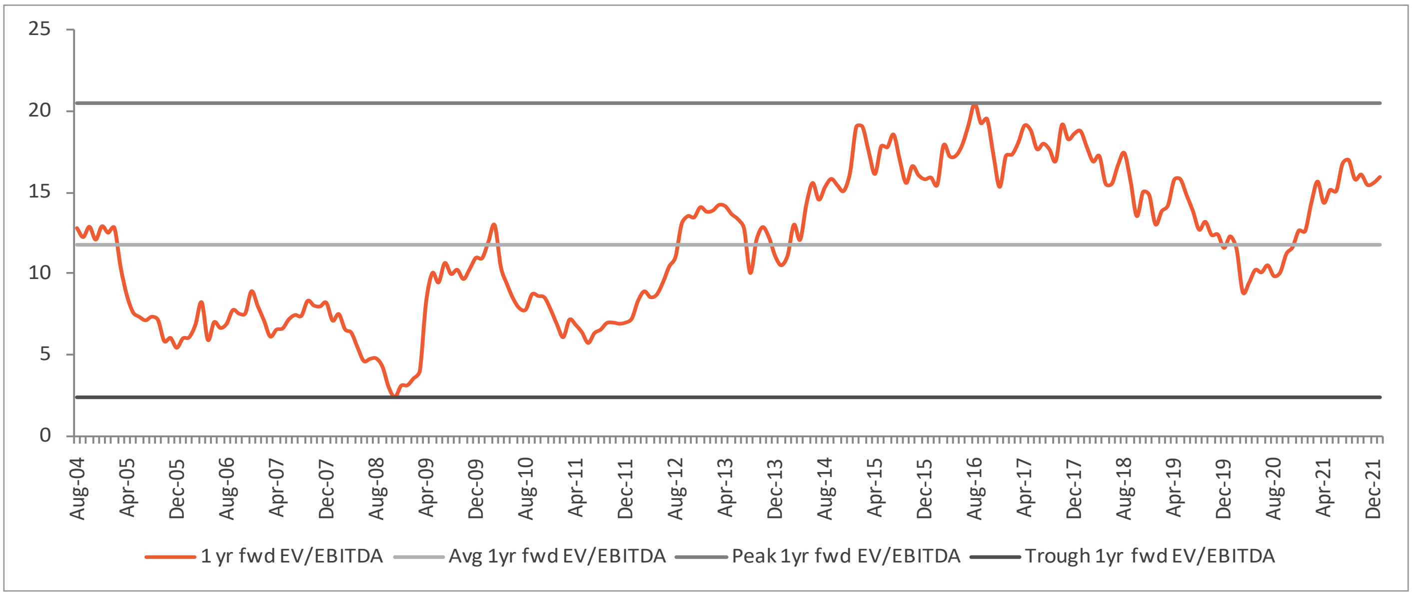
■ Company outlook - Healthy cement demand, profitability, and balance sheet health to remain favourable

UltraTech is expected to see sustained demand emanating from the rural sector and infrastructure sector. Further, demand from the real estate segment in the urban sector has started to witness strong traction with favourable government policies and lower interest rate regime. Management is optimistic of a sustainable demand environment for the cement sector over a longer period, barring the near-term impact of the second wave. The company's capacity expansion plans for adding 19.5 mtpa at a cost of Rs. 6,527 crore is on track and expected to be completed by FY2023 end. Further, the company targets to achieve 25% RoE by FY2025 from 15% currently. The company is well placed to benefit from rising cement demand over the next four to five years. Overall, the company's outlook in terms of cement demand, profitability, and balance sheet is expected to remain favourable.

■ Valuation - Maintain Buy with an unchanged PT of Rs. 9,200

UltraTech is expected to benefit from expected healthy cement demand over the long term, driven by its timely capacity expansion plans. The demand environment is expected to be strong from segments such as infrastructure, rural housing, and urban housing. Easing of power and fuel costs along with expectation of price hikes is likely to maintain healthy operational profitability. We believe the company's capacity expansion coupled with de-leveraging of balance sheet over the next three years is expected to drive earnings over FY2022-FY2024. We continue to maintain our Buy rating on the stock with a revised PT of Rs. 9,200.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer Comparison

Company	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
UltraTech Cement	30.6	25.6	16.0	13.1	4.0	3.5	14.1	14.7
Shree Cement	31.8	27.4	17.0	14.3	4.9	4.2	16.5	16.6
The Ramco Cement	26.3	23.7	15.8	14.3	3.2	2.9	13.0	12.9
Dalmia Bharat	35.9	28.1	12.2	10.2	2.6	2.4	7.6	8.9

Source: Company, Sharekhan estimates

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. With a consolidated grey cement capacity of 116.75 mtpa, it is the third largest cement producer in the world, excluding China, and the only one globally (outside China) to have 100+ mtpa of cement manufacturing capacity in a single country. The company's business operations span UAE, Bahrain, Sri Lanka, and India.

Investment theme

UltraTech is India's largest cement company. We expect UltraTech to report industry-leading volume growth on account of timely capacity expansion (inorganic and organic expansions) and a revival in demand (demand pick up in infrastructure, urban housing along with continued demand emanating from the rural housing segment). 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 and CFO
Mr. Sanjeeb K Chatterjee	Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Grasim Industries Ltd.	57.28
2	Life Insurance Corp. of India	3.35
3	Standard Life Aberdeen PLC	1.90
4	SBI Funds Management Pvt. Ltd.	1.41
5	The Vanguard Group Inc.	1.40
6	Kotak Mahindra Asset Mgmt	1.29
7	Pilani Investment & Industries Corp. Ltd.	1.21
8	Franklin Resources Inc.	1.17
9	BlackRock Inc.	1.07
10	ICICI Prudential Life Insurance Co.	0.90

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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