Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

UltraTech Cement Ltd

Strong Q1; long-term demand trend intact

Cement	Sharekhan code: ULTRACEMCO		
Reco/View: Buy	↔	CMP: Rs. 6,455	Price Target: Rs. 7,300 ↑

↑ 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 35.92

Updated July 01, 2022

High Risk

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

Source: Morningstar

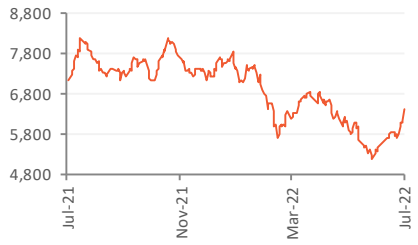
Company details

Market cap:	Rs. 1,86,323 cr
52-week high/low:	Rs. 8,267/5,158
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	13.1
DII	18.3
Others	8.6

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	19.3	-2.1	-9.8	-9.7
Relative to Sensex	12.1	-1.2	-7.4	-1.7

Sharekhan Research, Bloomberg

Summary

- We maintain Buy on UltraTech with a revised PT of Rs. 7,300, considering its long term growth potential and reasonable valuation.
- Q1FY2023 numbers were better than expected led by higher than anticipated volumes, realizations and EBITDA/tonne.
- Management indicated reaching a 200-mtpa cement capacity by FY2030 post completion of its targeted domestic capacity of 153.85 mtpa by FY2026.
- The company expects high demand tailwinds in the run-up to general elections but energy costs are expected to rise for the next 2-3 quarters.

UltraTech Cement (UltraTech) reported better than expected performance for Q1FY2023. Standalone revenues grew 28.2% y-o-y to Rs. 14,715.5 crore led by both higher volumes (up 15.6% y-o-y) and blended realisations (up 10.9% y-o-y). The blended EBITDA/tone at Rs. 1234 (down 20.1% y-o-y) was better than our estimate of Rs. 1187/tonne. Rise in cost of production majorly led by power & fuel costs (up 43.6% y-o-y on per tonne basis) affected operating profit (down 7.6% y-o-y) and net profit (down 7.6% y-o-y). The power & fuel costs are expected to rise for the next 2-3 quarters. The company's consolidated results were impacted by disruption in Sri Lanka. Its capacity expansion plan to reach 131.25mtpa domestic capacity by FY2023 remain on track. It would be adding another 22.6 mtpa cement capacity by FY2026 to reach 153.85mtpa while it has hinted on further expansion to achieve 200 mtpa domestic cement capacity by FY2030.

Key positives

- Standalone business volumes and blended realisation rose by 15.6% y-o-y and 10.9% y-o-y respectively.
- Blended EBITDA/tonne at Rs. 1234 was higher than our estimate.

Key negatives

- Disruption in Sri Lanka affected exports and operations in that region.
- Standalone and consolidated net debt increased by Rs. 900 crore and Rs. 1600 crore q-o-q.

Management Commentary

- The company expects to generate an EBITDA/tonne of Rs. 1400-1500 for Rs. 12,866 crore phase II expansion delivering an IRR of over 15% post FY2026. It would be adding 50-60MW WHRS capacity apart from addition of solar capacities during phase II expansion.
- Urban housing has picked up in the last 2-3 quarters. Large infra projects are leading to cement growth. Going ahead new demand would continue to outpace capacity additions. It expects high demand tailwinds during the next twenty months to the 2024 general elections.
- June exit prices were 3-5% lower than average Q1FY2023. The power & fuel costs would be on rising trend over next 2-3 quarters.

Revision in estimates – We have downwardly revised our net profit estimates for FY2023-FY2024, factoring higher fuel costs.

Our Call

Valuation – Maintain Buy with a revised PT of Rs. 7,300: UltraTech is expected to benefit from healthy cement demand over the long term, driven by timely capacity expansion. Demand is expected to be strong from segments such as infrastructure, rural housing and urban housing. However, elevated energy costs remain a key challenge in the 2-3 quarters. Although, a sustained strong demand environment and expected easing of energy costs remain key growth tailwinds for the company. We introduce our FY2025E estimates in this note. We continue to maintain our Buy rating on the stock with a revised price target (PT) of Rs. 7,300, considering its long term growth potential and reasonable valuation.

Key Risks

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

Valuation (Standalone) Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
Revenue	50,663	60,325	67,000	74,539
OPM (%)	22.8%	20.7%	20.5%	20.7%
Adjusted PAT	5,549	6,132	6,960	8,014
% YoY growth	1.7%	10.5%	13.5%	15.1%
Adjusted EPS (Rs.)	192.2	212.5	241.2	277.7
P/E (x)	31.9	28.9	25.4	22.1
P/B (x)	3.6	3.2	2.9	2.6
EV/EBITDA (x)	16.0	14.6	12.9	11.3
RoNW (%)	12.0%	11.8%	11.9%	12.2%
RoCE (%)	10.2%	10.9%	11.3%	11.8%

Source: Company; Sharekhan estimates

Better than expected Q1

Ultratech reported standalone net revenues growth of 28.2% y-o-y at Rs. 14,715.5 crore which was 5% ahead of our estimate. Cement volumes were up 15.6% y-o-y (-9.3% q-o-q) at 23.73 MT while blended realizations were up 10.9% y-o-y (up 6.9% q-o-q) at Rs. 6201/tonne. Blended standalone EBITDA/tonne at Rs. 1234 (-20.1% y-o-y, up 9.7% q-o-q) was higher than our estimate of Rs. 1187/tonne. The power & fuel costs stood at Rs. 1534/tonne (up 43.6% y-o-y, up 11.6% q-o-q), freights costs at Rs. 1370/tonne (up 7.2% y-o-y, up 4.2% q-o-q) and other expense at Rs. 734/tonne (up 13.2% y-o-y, up 10.9% q-o-q). Standalone operating profit declined by 7.6% y-o-y (-0.5% q-o-q) at Rs. 2929 crore, which was 6% higher than our estimate. Further, lower interest expense (-27.6% y-o-y) was offset by lower other income (-23.2% y-o-y) and higher depreciation (up 5.1% y-o-y). The standalone net profit declined by 7.6% y-o-y (up 5.7% q-o-q) at Rs. 1554 crore (6% higher than our estimate).

Expansion plans remain on track

The company's phase I cement capacity addition plan of 19.9mtpa is expected to complete by FY2023 end taking its domestic cement capacity to 131.25 mtpa. Further, its phase II expansion plan of 22.6mtpa cement capacity would increase its domestic cement capacity to 153.85mtpa by FY2026. In phase II, region-wise, it would adding cement capacity as follows North – 4.4mtpa, Central – 7.3mtpa, East – 5.2mtpa and South – 5.7 mtpa. Further, it would be undertaking next leg of expansion to reach 200mtpa domestic cement capacity by FY2030 through both organic and inorganic routes.

Key Conference call takeaways

- **Capacity expansion plan:** The company would be undertaking next leg of capacity expansion after reaching 153 mtpa in FY2026 to 200mtpa through organic and inorganic routes. The 22.6mtpa phase II expansion is backed by clinker capacities.
- **Phase II expansion:** The company expects to generate EBITDA/tonne of Rs. 1400-1500 for Rs. 12,866 crore phase II expansion delivering an IRR of over 15% post FY2026. It would be adding 50-60MW WHRS capacity apart from addition of solar capacities during phase II expansion.
- **Demand outlook:** Urban housing demand has picked up over last 2-3 quarters. Large infrastructure projects are leading to cement growth. Going ahead new demand would continue to outpace capacity addition. It expects huge amount of demand tailwinds during twenty months to election.
- **Pricing:** Prices in the North and Central regions witnessed double digit growth. West and East had 5-6% rise while South remained flat during Q1FY2023. June exit prices were 3-5% lower than average Q1FY2023.
- **Energy costs:** Power & fuel costs would be on rising trend over next 2-3 quarters. The fuel mix during Q1FY2023 was 52% petcoke, 37% imported coal, 5% domestic coal and balance green fuel.
- **Net Debt:** The consolidated net debt increased by Rs. 1600 crore to Rs. 5561 crore. The standalone net debt increased by Rs. 900 crore to Rs. 4670 crore.
- **Capex:** The company would be left out with Rs. 2000-3000 crore capex pending for FY2023.
- **Consolidated operating profit impact:** The consolidated operational performance was impacted due to its operations in Sri Lanka. It provided Rs. 38 crores towards currency fluctuation. The company's export volumes were dismal during Q1FY2023 as it only supplied 1 lakh tonne to Sri Lanka.
- **Trade and non-trade pricing:** The difference between trade and non-trade has narrowed down to just Rs. 15-20 per bag from over Rs. 20 per bag earlier.
- **Trade and blending mix:** The trade mix was 67% and blending ratio at 70% for Q1FY2023.

- **Replacement cost:** The replacement cost at current prices is $110-120 per tonne.
- **Inventory:** The inventory stood at over 50 days at the end of June.
- **Lead distance:** The lead distance for Q1FY2023 was 429 km.
- **UBS stores:** The UBS stores are B2C stores. There are 3000 stores which sell 15% of cement volumes of the company.

Results (Standalone) **Rs cr**

Particulars	Q1FY2023	Q1FY2022	% yoy	Q4FY2022	% qoq
Net Sales	**14715.5**	**11477.0**	**28.2%**	**15167.5**	**-3.0%**
Operating Profit	**2929.4**	**3172.0**	**-7.6%**	**2942.9**	**-0.5%**
Other Income	166.1	216.4	-23.2%	144.8	14.7%
EBITDA	3095.5	3388.4	-8.6%	3087.7	0.3%
Interest	199.7	275.9	-27.6%	174.7	14.3%
Depreciation	628.2	597.7	5.1%	637.7	-1.5%
PBT	**2267.7**	**2514.8**	**-9.8%**	**2275.3**	**-0.3%**
Tax	713.6	833.7	-14.4%	804.7	-11.3%
Reported PAT	**1554.0**	**1681.1**	**-7.6%**	**2453.6**	**-36.7%**
Exceptional items	0.0	0.0		983.0	
Adj.PAT	**1554.0**	**1681.1**	**-7.6%**	**1470.6**	**5.7%**
Margins			**Bps**		**Bps**
OPM	19.9%	27.6%	-773	19.4%	50
PATM	10.6%	14.6%	-409	9.7%	86
Tax Rate	31.5%	33.2%	-168	35.4%	-390

Source: Company, Sharekhan Research

Outlook and Valuation

Sector View – Improving demand brightens outlook

The cement industry has seen a sustained improvement in demand in the past 15 years, barring a couple of years, while regional cement prices have been rising in the past 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.

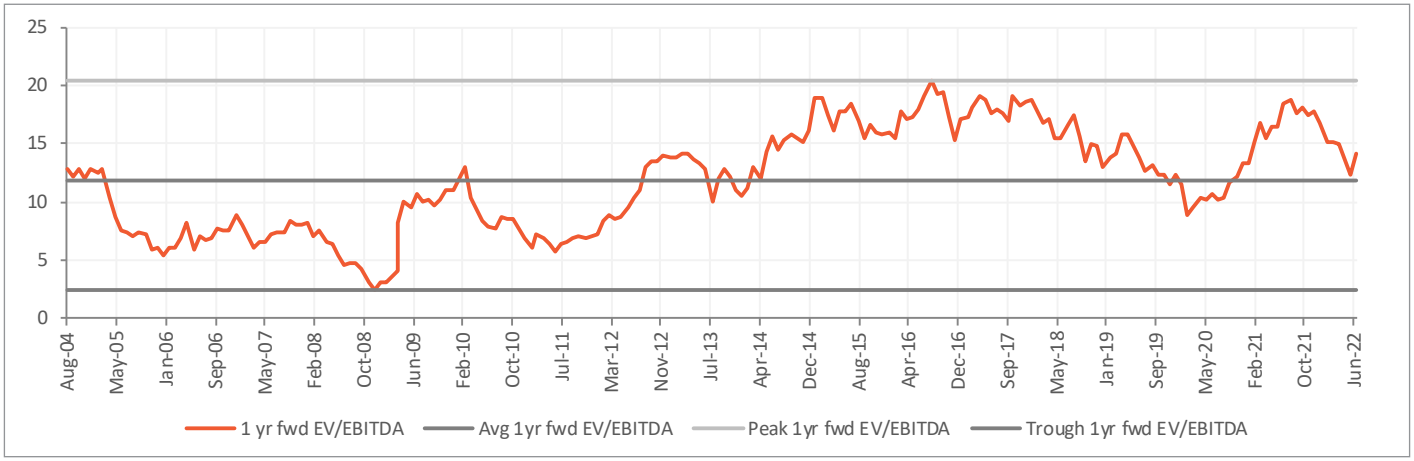
Company Outlook – Healthy cement demand, profitability, and balance sheet health to remain favourable

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 market has started to witness strong traction with favourable government policies and lower interest rate regime. Management is optimistic about a sustainable demand environment for the cement sector over a longer period, barring the near-term impact of the second wave of COVID-19. The company's capacity expansion plans for adding 19.9 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 a revised PT of Rs. 7,300

UltraTech is expected to benefit from healthy cement demand over the long term, driven by timely capacity expansion. Demand is expected to be strong from segments such as infrastructure, rural housing and urban housing. However, elevated energy costs remain a key challenge in the 2-3 quarters. Although, a sustained strong demand environment and expected easing of energy costs remain key growth tailwinds for the company. We introduce our FY2025E estimates in this note. We continue to maintain our Buy rating on the stock with a revised price target (PT) of Rs. 7,300, considering its long term growth potential and reasonable valuation.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer Comparison

Companies	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
UltraTech Cement	28.9	25.4	14.6	12.9	3.2	2.9	11.8	11.9
Shree Cement	30.6	25.9	15.7	13.3	3.9	3.4	13.4	14.0
The Ramco Cement	21.9	18.1	13.0	11.2	2.3	2.1	11.0	12.0
Dalmia Bharat	40.6	33.2	11.3	9.9	1.8	1.7	4.5	5.3

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 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 across 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 revival in demand (demand pick-up in infrastructure and 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 Website

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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