UltraTech Cement (ULTCEM)

CMP: ₹ 7,250 | Target: ₹ 8,950 (23%) | Target Period: 12 months | **BUY**

October 19, 2021

Result Update

Weak Q2; price hikes on cards to mitigate cost pressure

About the stock: UltraTech is the **largest cement manufacturer** in India with a domestic capacity of 111.4 MT (23% of total market) with a leadership position in most regions (excluding East). It has grown through organic and inorganic routes and added around ~30 MT of capacity in the last three years.

- It has shown its capability to successfully integrate the acquired assets and ramped up its utilisation in a profitable manner
- The company is now **focusing on fast growing market of eastern India**, which accounts for 10.2MT of its total 19.6 MT planned expansion over FY21-23E

Q2FY22 Results: UltraTech's results were weak on the margin front due to sharp cost escalations on the power, fuel and freight front.

- The company clocked revenue of ₹ 11,548 crore, up 15.3% YoY, flat QoQ. Domestic sales volume was at 20.4 MT (up 6.4% YoY). Demand in East, Central remained muted due to heavy monsoons
- EBITDA margin was down 512 bps QoQ to 22.5%, still better than last five year's average EBITDA margin of 20%
- PAT was at ₹ 1,300 crore, down 22.7% QoQ (our estimate: ₹ 1267 crore)

What should investors do? Market leadership, strong brand with highest retail presence and robust balance sheet justifies UltraTech's premium valuations.

- With a target to become net debt free by FY23E and expected RoCE of 18%+, we remain positive on company. Hence, we maintain **BUY** rating

Target Price and Valuation: Valued at ₹ 8,950 i.e. 17.5x FY23E EV/EBITDA

Key triggers for future price performance:

- Expect its capacity to increase at CAGR of ~7.4% to 131 MT by FY23E against Industry average capacity CAGR of 5.6% during the same period
- The new organic capacities are being added at lower capital cost (US$60/t). This will help boost return ratios (to generate 16-18% IRR)
- Despite capex plans, the company also aims **to become net debt-free by FY23E** supported by strong operating cash flows (from existing and acquired assets) and through efficient w/cap management.

Alternate Stock Idea: Apart from UltraTech, in our cement sector coverage we also like ACC.

- It has a strong balance sheet with debt frees status. The company is focusing on cost reduction and also adding new capacities via internal accruals
- BUY with a target price of ₹ 2,800/share

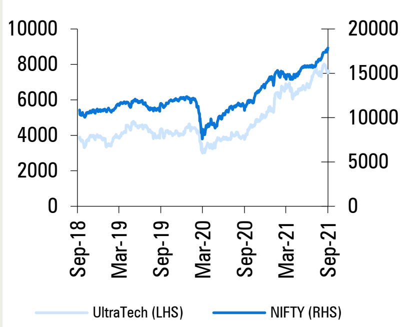
Particulars

Particulars	Amount
Mcap	₹ 209215 crore
Debt (FY21)	₹ 14915 crore
Cash & Invest (FY21)	₹ 1881 crore
EV	₹ 222248 crore
52 week H/L	₹ 7543/₹ 3736
Equity cap	₹ 288.2 crore
Face value	₹ 10

Shareholding pattern

(in %)	Dec-20	Mar-21	Jun-21	Sep-21
Promoter	60.0	60.0	60.0	60.0
FII	16.8	17.3	16.6	16.5
DII	14.2	13.8	14.4	14.6
Others	9.1	8.9	9.0	9.0

Price Chart



Key risks

- Any delay in commissioning of new capacity may impact return ratios
- Volatility in prices of imported coal/petcoke may impact margins

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ICICI Securities – Retail Equity Research

Key Financial Summary

Key Financials	FY18	FY19	FY20	FY21	3 Year CAGR (%)	FY22E	FY23E	2 Year CAGR (%)
Net Sales (₹ crore)	29526	39933	40634	43188	13.5	53092	58888	16.8
EBITDA (₹ crore)	5826	7076	8652	10964	23.5	12792	14676	15.7
EBITDA (%)	19.7	17.7	21.3	25.4		24.1	24.9	
Adjusted PAT (₹ crore)	2458	2530	3550	5506	30.9	6698	8099	21.3
EPS (₹)	89.6	87.7	123.0	190.8		232.1	280.7	
EV/EBITDA	36.4	31.5	25.6	19.7		16.6	14.2	
EV/t ($)	357.9	281	279	276		265	227	
RoNW (%)	9.5	7.6	9.3	12.7		13.7	14.5	
RoCE (%)	10.0	9.0	11.4	14.7		16.3	18.1	

Source: Company, ICICI Direct Research

Key performance highlights

- Domestic blended sales volumes were at 20.4 MT (flat QoQ) while blended realisations were up marginally 1.1% QoQ to ₹ 5,653/tonne, up 8.4% YoY
- Demand in the east and central region remained weak due to heavy monsoon in east and de-growth in infra demand in the central region
- Cost of production was up 8.3% QoQ to ₹ 4380/t due to sharp increase in diesel/petcoke/coal prices. Employee costs were also up 16.3% QoQ to ₹ 308/t due to an impact of increments/bonuses
- As a result, EBITDA/t declined 4.2% YoY (down 17.6% QoQ) to ₹ 1,273/t (vs. I-direct estimate: ₹ 1242/t)

Key conference call highlights

- **Demand**: Strong infra pipeline of government across roads, metros and irrigation segment and upcoming state and general elections to keep demand momentum strong till FY24E. Pick-up in urban housing, commercial real estate to fuel demand further. Trade mix was at 67%
- **Cost of production**: Rise in petcoke & coal prices is expected to keep production costs higher. However, long term fuel sourcing arrangements due to large scale volume would restrict its impact, to some extent. We expect fuel cost to inch up by ~₹ 200/t in Q3 against an increase of ₹ 450-500/t considering the spot rate of petcoke/coal prices. Bicharpur coal block is expected to start coal mining operations from Q3 and will be used in the power plant
- It will focus on improving fuel blending and increasing WHRS capacity. The company has commissioned 12 MW WHRS and 21 MW solar capacity during Q2. UltraTech has set a target to achieve green energy mix target of 34% by 2024 and 100% renewable energy by 2050 from 15% at present
- **Cement Prices**: Cement prices are now back to pre-Covid levels. Price hike of 10% is required to achieve EBITDA level of Q1FY21 (highest ever reported). Companies are now in a better position to pass on the cost pressure on to consumers
- **Expansion:** The company is on track to reach 130.9 MT by FY23E. Commissioned 1.2 MT in East Bara grinding unit 2 MT will be commissioned by Q4FY22. Balance capacities of 16.3 MT are expected to get commissioned in FY23E. The company spent ₹ 2300 crore as of Q2, Estimated capex for FY22 is ₹ 4-5000 crore to be funded via internal accruals
- **B/S strength:** UltraTech has negative working capital of 8-9 days. Quarterly operating cash flow was ~₹ 1750 crore, large part being used for capex. Retired ₹ 5200 crore of long term debt in Q2. Reduction in net debt is expected to pick-up pace further with improved operating cash flows further

Exhibit 1: Variance Analysis

	Q2FY22	Q2FY22E	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	Comments
Net Sales	11,548	11,308	10,019	15.3	11,477	0.6	Capacity utilsation stood at 73% vs 69% in Q2FY21.
EBITDA	2,600	2,558	2,552	1.9	3,172	-18.0	Spike in petcoke/coal prices led to contraction in the margins
EBITDA Margin (%)	22.5	22.6	25.5	-296 bps	27.6	-512 bps	
PAT	1,300	1,267	1,209	7.6	1,681	-22.7	
Key Metrics							
Blended volume (MT)	20.4	20.6	19.2	6.4	20.5	-0.5	
Realisation (₹)	5,653	5,489	5,215	8.4	5,590	1.1	
EBITDA per Tonne (₹)	1,273	1,242	1,329	-4.2	1,545	-17.6	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

	FY22E			FY23E			Comments
(₹ Crore)	Old	New	% Change	Old	New	% Change	
Revenue	50,044.9	53,091.9	6.1	55,410.0	58,887.6	6.3	Volume growth to remain healthy in FY22E & FY23E
EBITDA	12,843.6	12,791.8	-0.4	14,557.5	14,676.4	0.8	Operating leverage to keep margins healthy going ahead
EBITDA Margin (%)	25.7	24.1	-157 bps	26.3	24.9	-135 bps	
PAT	6,864.6	6,698.3	-2.4	8,037.4	8,099.3	0.8	
EPS (₹)	237.9	232.1	-2.4	278.5	280.7	0.8	

Source: Company, ICICI Direct Research

Key triggers for future price performance

Target total capacity of 160 MT by FY30E; to reach 131 MT by FY23E

The target of reaching 160 MT by FY30E from 111.4 MT, indicates capacity CAGR growth of 3.7% during FY20-30E. The newly announced cement capacity expansion of 12.8 MT (9.1 MT clinker capacity) along with ongoing capex of 6.7 MT would take its total capacity to 130.9 MT by end of FY23E. Region wise, major capacities are being added in the eastern and central region (73% of 19.5 MT), which has lowest road and power density per capita representing higher growth potential while rural population share remains one of the higher, offering stability in prices. The balance 27% of new capacities are being added in the north region. Furthermore, as these new organic capacities are being added at lower capital costs (US$60/t), it will help in boosting return ratios (new capacity to generate 15%+ IRR

Efficiency measures to help sustain margins; b/s to stay firm

While there remains uncertainty in cost inflation with respect to price fluctuations in petcoke and diesel prices, the management's focus on consolidating the acquired assets, driving synergies, especially on the logistics front, improving premium segment share (to increase from 10% to 15% in two years) and containing fixed overheads on sustainable basis provides cushion against risk of margin erosion going forward. On the leverage front, net debt/EBITDA is now at 0.5x vs. 1.72x last year.

Valuation & Outlook

UltraTech has successfully integrated acquired assets while protecting its b/s. Given the positive outlook, the new capex targeting central and east region would address the issue of capacity constraint post FY24E. With a target to become net debt free by FY23E and with RoCE of 18%+, we remain positive on company and maintain **BUY** rating with a revised target price of ₹ 8950/share (i.e. 17.5x FY23E EV/EBITDA). (earlier TP ₹ 8,700/share).

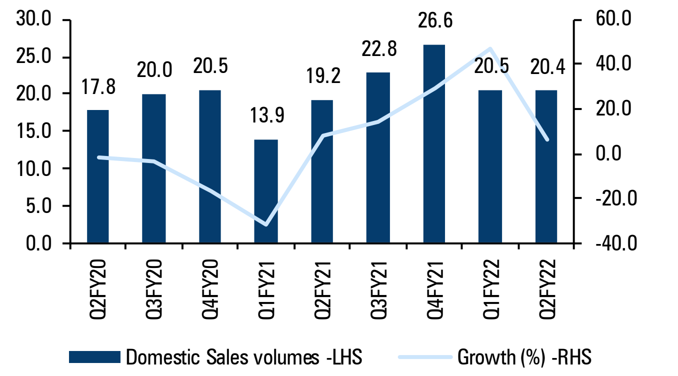
Exhibit 3: Valuation matrix

	Sales (₹ cr)	Gr (%)	EPS (₹)	Gr (%)	PE (x)	EV/Tonne ($)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY19	39933.3	4.7	87.7	12.8	86.6	281	31.5	7.3	9.0
FY20	40634.2	1.8	123.0	40.3	38.3	279	25.6	9.3	11.0
FY21	43188.4	6.3	190.8	55.1	39.2	276	19.7	12.7	14.6
FY22E	53091.9	22.9	232.1	21.7	31.2	265	16.6	13.7	16.7
FY23E	58887.6	10.9	280.7	20.9	25.8	227	14.2	14.5	18.1

Source: Company, ICICI Direct Research

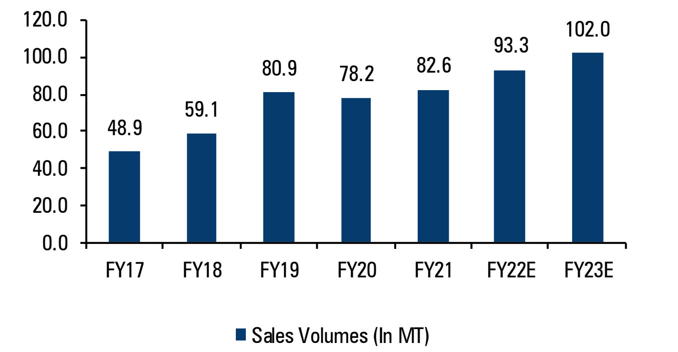
Financial story in charts

Exhibit 4: Sales volumes up 6.4% YoY to 20.4 MT



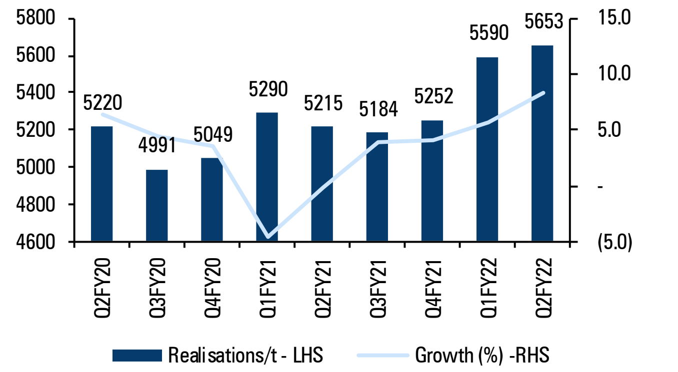
Source: Company, ICICI Direct Research

Exhibit 5: Volumes expected to cross ~100 MT by FY23E



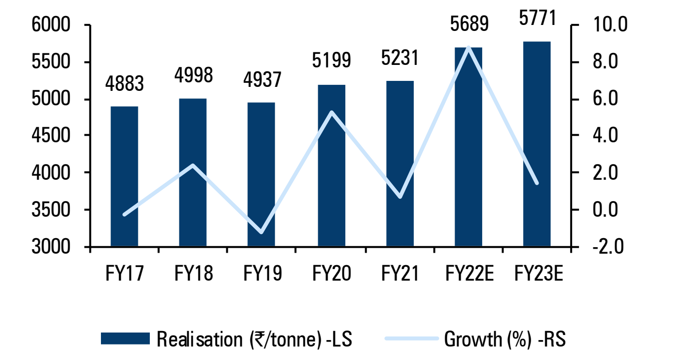
Source: Company, ICICI Direct Research

Exhibit 6: Realisations up 8.4% on YoY basis



Source: Company, ICICI Direct Research

Exhibit 7: Realisations growth to moderate with volume pick-up



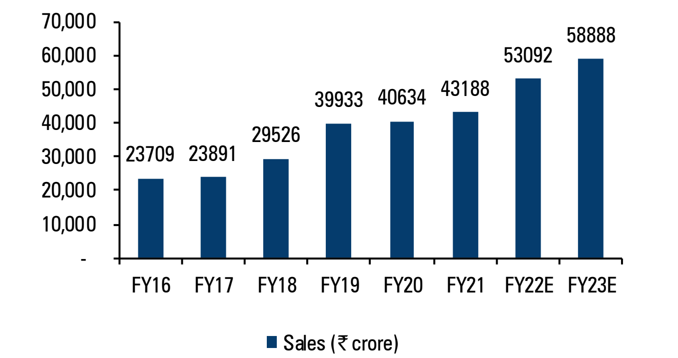
Source: Company, ICICI Direct Research

Exhibit 8: Domestic capacity to reach ~131 MT by FY23E

Zone (in mt)	Capacity	Capacity additions	Total
North	23.8	5.2	29.0
Central	23.3	4.2	27.5
East	16.1	10.1	26.2
West	27.7		27.7
South	20.5		20.5
Domestic Total	**111.4**	**19.5**	**130.9**
Overseas	5.4		5.4
Total	**116.8**		**136.3**

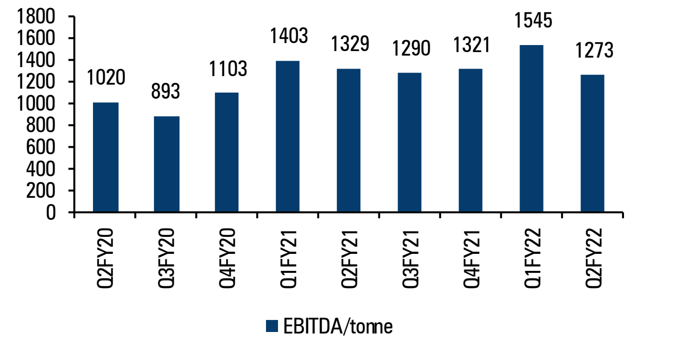
Source: Company, ICICI Direct Research

Exhibit 9: Standalone revenues to grow at 16.8% CAGR in FY21-23E



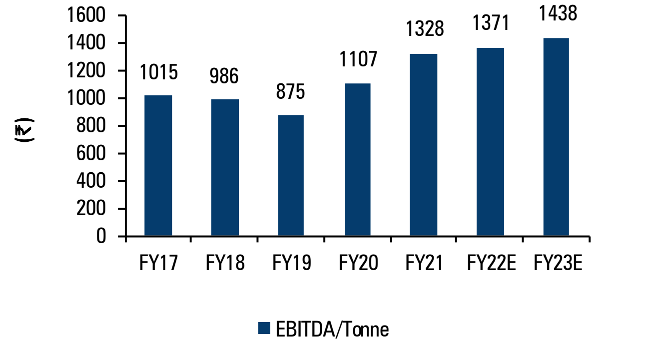
Source: Company, ICICI Direct Research

Exhibit 10: EBITDA/t down 17.6% QoQ due to rise in cost pressure



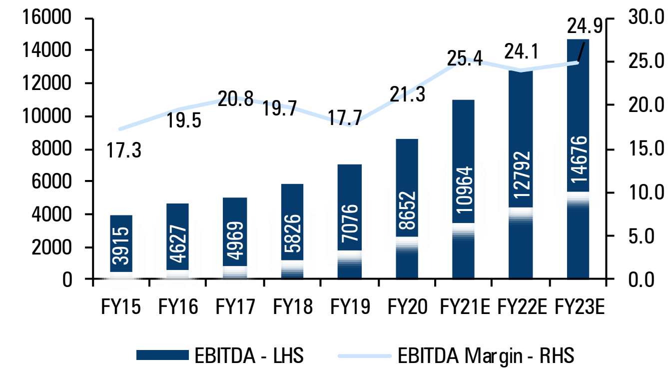
Source: Company, ICICI Direct Research

Exhibit 11: EBITDA/t trajectory to remain healthy due to cost pass through on firm demand outlook



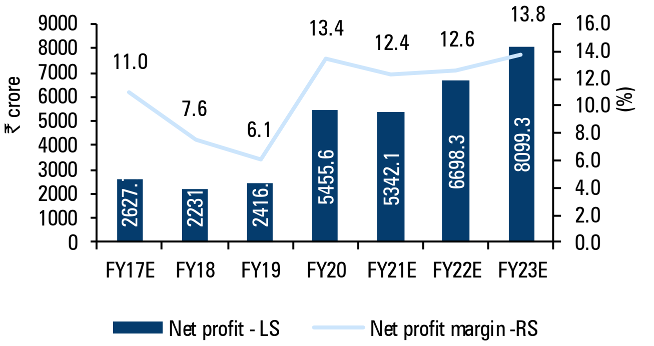
Source: Company, ICICI Direct Research

Exhibit 12: EBITDA growth to trend



Source: Company, ICICI Direct Research

Exhibit 13: PAT margin to reach close to 14% by FY23E led by healthy realisations, efficiency measures



Source: Company, ICICI Direct Research

Financial Summary

Exhibit 14: Profit & Loss Account

(Year-end March)	FY20	FY21	FY22E	FY23E
Total operating Income	**40,634**	**43,188**	**53,092**	**58,888**
Growth (%)	1.8	6.3	22.9	10.9
Raw material cost	6,907	7,539	7,973	9,745
Power & Fuel cost	7,703	7,552	11,263	12,041
Freight cost	9,570	9,940	12,364	13,265
Employees cost	2,336	2,182	2,384	2,527
Others	5,465	5,012	6,316	6,633
Total Operating Exp.	31,982	32,224	40,300	44,211
EBITDA	**8,652**	**10,964**	**12,792**	**14,676**
Growth (%)	22.3	26.7	16.7	14.7
Depreciation	2,455	2,434	2,568	3,026
Interest	1,704	1,259	1,017	712
Other Income	727	789	642	800
PBT	5,220	8,059	9,848	11,738
Total Tax	-236	2,553	3,150	3,639
PAT	**5,456**	**5,506**	**6,698**	**8,099**
Growth (%)	115.6	0.9	21.7	20.9
Adj. EPS (₹)	**123**	**191**	**232**	**281**

Source: Company, ICICI Direct Research

Exhibit 15: Cash flow statement

(Year-end March)	FY20	FY21	FY22E	FY23E
Profit after Tax	5,456	5,342	6,698	8,099
Add: Depreciation	2,455	2,434	2,568	3,026
(Inc)/dec in Current Assets	-435	261	-2,721	986
Inc/(dec) in CL and Provisions	-815	6,620	1,314	-1,638
CF from operating activities	**6,660**	**14,658**	**7,860**	**10,474**
(Inc)/dec in Investments	-288	-920	0	0
(Inc)/dec in Fixed Assets	-1,100	-3,062	-4,500	-4,300
Others	-1,138	1,142	0	0
CF from investing activities	**-2,526**	**-2,839**	**-4,500**	**-4,300**
Issue/(Buy back) of Equity	14	0	0	0
Inc/(dec) in loan funds	-1,565	-3,185	-2,500	-4,500
Dividend paid & dividend tax	-452	-1,288	-1,218	-1,218
Inc/(dec) in Sec. premium	0	0	0	0
Others	16	1,002	0	0
CF from financing activities	**-1,987**	**-3,471**	**-3,718**	**-5,718**
Net Cash flow	-346	1,571	141	455
Opening Cash	656	310	1,881	2,023
Closing Cash	**310**	**1,881**	**2,023**	**2,478**

Source: Company, ICICI Direct Research

Exhibit 16: Balance Sheet summary

(Year-end March)	FY20	FY21	FY22E	FY23E
Liabilities				
Equity Capital	289	289	289	289
Reserve and Surplus	38,008	43,064	48,544	55,425
Total Shareholders funds	38,296	43,353	48,833	55,714
Total Debt	18,100	14,915	12,415	7,915
Deferred Tax Liability	4,077	5,219	5,219	5,219
Total Liabilities	**60,473**	**63,487**	**66,467**	**68,848**
Assets				
Gross Block	64,923	67,569	72,091	76,791
Less: Acc Depreciation	19,668	22,102	24,670	27,696
Net Block	45,255	45,467	47,421	49,095
Capital WIP	1,106	1,522	1,500	1,100
Total Fixed Assets	46,361	46,989	48,921	50,195
Investments	13,090	20,786	20,286	20,286
Inventory	3,834	3,722	4,424	4,611
Debtors	1,848	2,286	2,660	2,503
Loans and Advances	2,300	1,353	1,832	1,701
Other Current Assets	3,039	3,399	4,565	3,679
Cash	310	1,881	2,023	2,478
Total Current Assets	11,331	12,641	15,504	14,973
Creditors	3,250	6,334	6,757	6,150
Provisions	7,059	10,595	11,486	10,455
Total Current Liabilities	10,309	16,929	18,243	16,605
Net Current Assets	1,022	-4,288	-2,740	-1,632
Others Assets	0	0	0	0
Application of Funds	**60,473**	**63,486**	**66,467**	**68,848**

Source: Company, ICICI Direct Research

Exhibit 17: Ratio sheet

(Year-end March)	FY20	FY21	FY22E	FY23E
Per share data (₹)				
Adj. EPS (₹)	123.0	190.8	232.1	280.7
Cash EPS	274.1	269.5	321.1	385.5
BV	1,327.1	1,502.3	1,692.2	1,930.7
DPS	13.0	37.0	35.0	35.0
Cash Per Share	10.7	65.2	70.1	85.9
Operating Ratios (%)				
EBITDA Margin	21.3	25.4	24.1	24.9
PBT / Total Operating income	12.8	18.3	18.5	19.9
PAT Margin	13.4	12.4	12.6	13.8
Inventory days	34.2	31.9	28.0	28.0
Debtor days	18.9	17.5	17.0	16.0
Creditor days	28.0	40.5	45.0	40.0
Return Ratios (%)				
RoE	9.3	12.7	13.7	14.5
RoCE	11.4	14.7	16.3	18.1
RoIC	11.6	16.0	18.2	19.9
Valuation Ratios (x)				
P/E	39.1	40.0	31.9	26.4
EV / EBITDA	26.1	20.0	17.0	14.5
EV / Net Sales	5.5	5.1	4.1	3.6
Market Cap / Sales	5.3	4.9	4.0	3.6
Price to Book Value	5.6	4.9	4.4	3.8
Solvency Ratios				
Debt/EBITDA	2.1	1.4	1.0	0.5
Debt / Equity	0.5	0.3	0.3	0.1
Current Ratio	1.1	0.7	0.8	0.9
Quick Ratio	1.1	0.6	0.7	0.8

Source: Company, ICICI Direct Research

Exhibit 18: ICICI Direct coverage universe (Cement)

Company	CMP		EPS(₹)			EV/EBITDA (x)			EV/Tonne ($)			RoCE (%)			RoE (%)		
	(₹)	Rating	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
ACC*	2,273	BUY	85	105	126	16.5	12.2	10.1	140	136	136	14.5	17.8	19.0	12.6	13.7	14.5
Ambuja Cem*	404	BUY	9	11	14	21.0	16.3	14.3	247	222	220	17.6	19.4	20.6	20.3	22.0	22.9
UltraTech Cem	7,250	BUY	191	232	281	19.7	16.6	14.2	276	265	227	14.7	16.3	18.1	12.7	13.7	14.5
Shree Cement	28,146	BUY	641	682	847	24.4	22.0	18.4	285	281	275	18.2	18.2	19.5	15.2	14.1	15.2
Heidelberg Cem	255	HOLD	14	15	17	12.0	10.0	8.3	131	127	121	20.1	23.5	27.2	21.1	20.6	20.8
JK Cement	3,415	HOLD	100	118	138	17.5	15.5	12.9	207	210	209	18.6	18.5	20.0	20.6	20.1	19.4
JK Lakshmi Cen	650	BUY	34	37	41	10.5	9.2	8.4	89	89	91	21.1	22.1	21.3	19.0	19.5	18.5
Star Cement	109	BUY	6	7	8	10.8	8.4	7.2	90	86	83	13.3	16.4	17.1	12.6	14.2	13.6
Ramco Cement	1,012	BUY	32	35	45	17.9	16.2	13.0	201	204	190	8.6	8.8	10.1	13.5	12.9	14.2
Sagar Cement	312	BUY	79	81	138	10.5	9.7	6.4	104	76	72	15.3	15.2	22.0	15.4	13.7	19.1

*Source: Company, ICICI Direct Research, *ACC and Ambuja FY20=CY19, FY21E=CY20E, FY22E=CY21E*

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%

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