ANANDRATHI

CEMENT

Anand Rathi Research

research@rathi.com
+91 22 6637 7000

Bloomberg Code:	UTCEM@IN
Reuters Code:	ULTC.BO
BSE Code:	532538

Expected Share Price Return (%):	13.9
Expected Dividend Yield (%):	1.2

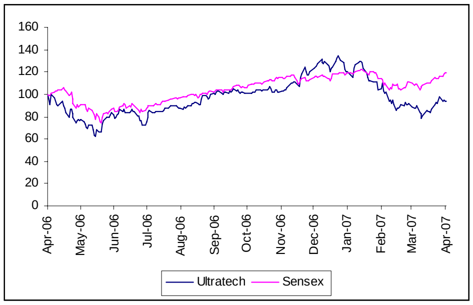
Market Data

Sensex:	14,229
CMP:	808
52-Week Range (H/L):	1,205 / 501
Market Cap ($ mn):	100,588
Shares O/S (mn):	124.5
Free Float (mn):	58.5
3m Avg. Volume:	41,888
Face Value:	10

Price Performance: (%)

	3m	6m	12m
Absolute	-22	-7	-6
Relative	-21	-19	-25

Relative Price Movement



Marketperformer | Ultra Tech Cement.

We initiate coverage on Ultra Tech with **'Market-performer'** rating; Target - **Rs 920**.

Investment Argument

- **Consolidating its presence in the southern region:** Consumption in South has witnessed the maximum growth in the last two years and is expected to continue going forward. With limited capacity additions in the next 15 months, utilization levels are expected to fall only from H2 FY09 onwards leading to firm prices. Ultratech's capacity expansion in AP will give it a good volume growth and enable it increase its market share in the lucrative southern region.
- **Captive power to reduce the power expenses:** Commissioning of captive power plants (188MW) would make Ultratech self sufficient for its total power requirements. The average power cost is expected to go down from Rs.4 per unit currently to Rs.2-2.5 per unit. The savings accruing from this is estimated to be ~Rs.1.4bn from FY09 onwards.
- **Strong internal accruals to support the capex:** The capex program of Rs 27bn involving enhancement of cement capacity to 21.5 mn ton and installation of power plant would be funded equally through internal accruals and debt.
- **Incremental volume growth to come at a lower cost:** Lower freight cost on the new cement capacity and higher sales of blended cement will add to the company's bottomline going forward.

Risks

Drop in industry utilisation rates due to poor demand leading to low cement prices is the key risk to our rating. A potential ban on exports or reduction in cement prices due to the threat of imports will also affect the estimated earnings.

Valuations

We initiate coverage on Ultra Tech with 'Market-performer' rating and a target price of Rs 920. The target price implies a P/E of 12x FY09E, EV/EBIDTA of 6.7x and EV/ton of US$ 142.

Y/E March (Rs mn)	FY06	FY07	FY08E	FY09E
Net Sales	32,995	49,108	52,343	58,338
% Chg	28%	49%	7%	11%
Net Profit	2,298	7,823	8,714	9,702
% Chg	7%	240%	11%	11%
EPS	18.5	62.8	70.0	77.9
Operating Margins (%)	16.8	28.9	30.0	31.5
P/E (x)	43.8	12.9	11.5	10.4
EV/EBIDTA (x)	19.1	7.6	6.9	5.9
EV/Ton (US$)	162	160	134	126

Industry Outlook

Govt interventions will be a deterrent for new entrants and fresh capacities announcements.

The recent government interventions will be a deterrent for any new entrant in the industry and at the same time slow the pace of new capacity announcements. This will help in restricting the extent of price fall. The cement consumption is estimated to grow at a CAGR of 10-11% over the coming years on the back of sustained demand from housing and infrastructure sectors. Any positive surprises on the demand side would provide a further boost in keeping the prices firm.

Financials

We expect Ultra Tech to report a CAGR of 9% in net sales over a period of FY07-FY09. The top line would be largely driven by volume growth which would be on the back of 4.5mn ton expansions program undertaken by the company.

EBIDTA is estimated to rise by a CAGR growth of 14% for the similar period supported by savings accruing on account of commissioning of captive power plant (FY09 onwards) and modernization of cement plants. PAT for FY09 would be subdued owing to higher depreciation and interest outgo. We expect the company to report an EPS of Rs.70 and 77.9 for FY08 and FY09 respectively translating into earnings growth of 11% CAGR over FY07-09.

Quarterly Performance

.

Rs mn	Q4FY07	Q3FY07	Q2FY07	Q1FY07	Q4FY06
Net Sales	14,655	12,605	10,045	11,803	10,604
Operating Profit	4,085	3,802	2,545	3,746	2,146
OPM%	*27.9%*	*30.2%*	*25.3%*	*31.7%*	*20.2%*
PAT	2,315	2,125	1,274	2,108	1,321
Sales Volumes (mn ton)	5.04	4.49	3.68	4.46	4.63
Net Realisations (Rs/ton)	2,908	2,807	2,729	2,649	2,290
EBIDTA (Rs/ton)	811	847	691	841	464

Assumptions

	FY06	FY07	FY08E	FY09E
Aggregate Sales (mn ton)	15.7	17.7	18.1	20.5
Net Realisation / ton (Rs)	2,106	2,779	2,968	2,918
EBIDTA / ton (Rs)	354	802	866	895

Valuations

At the CMP of Rs. 808, for FY08E and FY09E Ultratech trades at:

- P/E of 11.5x and 10.4x respectively.
- EV/EBITDA of 6.9x and 5.9x respectively.
- EV/Ton of $134 and $126 respectively.

We believe that going ahead Ultra Tech would continue to post good performance despite a cap on cement prices. The improvement in the operational efficiency combined with volume growth will drive the earnings growth going forward.

We rate the stock a Market performer with a 12 months price objective of Rs.920. The target price implies a P/E of 12x FY09E, EV/EBIDTA of 6.9x and EV/ton of $142.

Investment Risks

Aggressive capacity additions

Commissioning of planned capacities either on target or within a narrow timeframe would result in a drop in utilisation rates faster than expected leading to a correction in cement prices.

Ban on exports

Export ban, bunching of capacity additions and recent duty waivers could spoil the party for the industry

In the event of implementation of ban on exports, Ultratech would be the worst hit as export (cement+clinker) contributes 20% (FY07) to its total sales. A sharp drop in export realisations would also pose a threat to the company's profitability.

Ban on import duty, CVD & other levies

The recent exemption in import duty, CVD and SAD on import of cement has reduced the difference between domestic prices and landed cost to a great extent. Though this does not have an immediate impact due to various infrastructure and quality issues, it could pose a threat going forward by when various bottlenecks may be removed.
Ultratech's exposure to institutional clients at 25% puts in a precarious position as the institutional clients can import cement without having to pay VAT which makes import price cheaper than prevailing domestic prices. However this would be applicable only for cement usage at locations closer to the port.

Income Statement (Rs mn)

Y/E Mar	Mar-05	Mar-06	Mar-07	ARG Est. Mar-08	ARG Est. Mar-09
Net sales	25,861	32,995	49,108	52,343	58,338
- Operating expenses	22,354	27,452	34,930	36,640	39,987
Operating profit	3,507	5,543	14,178	15,703	18,350
+ Other income	212	370	615	700	700
- Depreciation	2,218	2,160	2,263	2,780	3,500
- Interest	1,069	896	868	859	1,354
- Tax	(365)	558	3,839	4,050	4,495
PAT	797	2,298	7,823	8,714	9,702
+ (Associates-Minorities)	-	-	-	-	-
Consolidated PAT	797	2,298	7,823	8,714	9,702

Balance Sheet Statement (Rs mn)

Y/E Mar	Mar-05	Mar-06	ARG Estimates Mar-07	ARG Estimates Mar-08	ARG Estimates Mar-09
Networth	16,488	16,152	23,240	30,880	38,926
Debt	15,314	14,518	16,559	24,309	20,159
Minority interests	-	-	-	-	-
Capital employed	31,802	30,671	39,799	55,190	59,085
Fixed Assets	25,971	26,782	32,068	46,396	46,807
Investments	1,848	1,724	3,500	5,000	7,000
Working capital	3,421	1,549	1,891	2,041	2,791
Cash	563	616	2,341	1,753	2,488
Capital deployed	31,802	30,671	39,799	55,190	59,085

Key Ratios

Y/E Mar	Mar-05	Mar-06	ARG Estimates Mar-07	ARG Estimates Mar-08	ARG Estimates Mar-09
Topline growth (%)	14.9	27.6	48.8	6.6	11.5
Bottomline growth (%)	105.2	188.3	240.5	11.4	11.3
Operating margins (%)	13.6	16.8	28.9	30.0	31.5
FDEPS (Rs/share)	6.4	18.5	62.8	70.0	77.9
CEPS (Rs/share)	18.8	35.4	79.7	90.7	104.4
DPS (Rs/share)	0.8	1.8	4.0	6.0	10.0
BV (Rs/share)	132.5	129.7	186.7	248.1	312.7
PER (x)	124.6	43.2	12.9	11.5	10.4
P/C (x)	42.5	22.5	10.1	8.9	7.7
Dividend yield (%)	0.1	0.2	0.5	0.7	1.2
P/B (x)	6.0	6.2	4.3	3.3	2.6
EV/Sales (x)	4.3	3.4	2.3	2.2	1.9
EV/ EBITDA (x)	30.0	18.9	7.6	6.9	5.9
Debt/Equity (x)	0.9	0.9	0.7	0.8	0.5
EV per ton (US$)	163	162	160	134	126
Dividend payout (%)	13.4	10.8	7.3	10.0	15.0

Cash Flow Statement (Rs mn)

Y/E Mar	Mar-05	Mar-06	ARG Estimates Mar-07	ARG Estimates Mar-08	ARG Estimates Mar-09
Consolidated PAT	797	2,298	7,823	8,714	9,702
+ Non-cash items	1,538	2,113	2,096	2,580	3,300
Cash profit	2,335	4,410	9,918	11,294	13,002
- Inc. in working capital	287	(1,872)	342	150	750
Operating cash flow	2,048	6,283	9,577	11,144	12,252
- Capital expenditure	669	2,972	7,549	17,108	3,911
Free cash flow	1,379	3,311	2,028	(5,964)	8,341
- Dividends	107	249	568	874	1,457
+ Equity raised	(1,542)	(2,338)	-	-	-
+ Debt raised	(1,043)	(796)	2,041	7,750	(4,150)
+ Inc. in minority interests	-	-	-	-	-
- Investments	(533)	(124)	1,776	1,500	2,000
- Miscellaneous items	(924)	-	-	-	-
Net cash flow	144	53	1,725	(588)	734
+ Opening cash	418	563	616	2,341	1,753
Closing cash balance	563	616	2,341	1,753	2,488

Dupont Analysis

Y/E Mar	Mar-05	Mar-06	ARG Estimates Mar-07	ARG Estimates Mar-08	ARG Estimates Mar-09
EBIT margins (%)	5.8	11.4	25.5	26.0	26.7
Capital turn (x)	0.8	1.1	1.4	1.1	1.0
RoCE (%)	4.6	12.0	35.6	28.7	27.2
Leveraging factor (x)	1.9	1.9	1.8	1.8	1.6
Interest impact (x)	0.3	0.8	0.9	0.9	0.9
Tax break (x)	1.8	0.8	0.7	0.7	0.7
Consolidation factor (x)	1.0	1.0	1.0	1.0	1.0
RoE (%)	4.7	14.1	39.7	32.2	27.8

Quarterly Results (Rs mn)

Calendar year format	2QCY06	3QCY06	4QCY06	1QCY07	ARG Est. 2QCY07
Net sales	11,803	10,045	12,605	14,655	13,503
Growth - YoY (%)	48.8	57.0	59.8	38.2	14.4
Growth - QoQ (%)	11.3	(14.9)	25.5	16.3	(7.9)
Operating profit	3,746	2,545	3,802	4,085	3,875
Operating margins (%)	31.7	25.3	30.2	27.9	28.7
Consolidated PAT	2,108	1,274	2,125	2,315	2,128
Growth - YoY (%)	251.3	159K	790.1	75.3	0.9
Growth - QoQ (%)	59.6	(39.6)	66.7	9.0	(8.1)

Recommendation Guide

Buy – >30% • **Outperformer** – 20 to 30% • **Market Performer** – 10 to20% • **Underperformer** – 0 to 10% I Sell – <0%

Anand Rathi Securities Limited Member, The Stock Exchange, Mumbai

Navaratan Capital & Securities Private Limited Member, National Stock Exchange of India

Victoria House, 3rd Floor, Kamala Mills Compound, Pandurang Budhkar Marg, Lower Parel, Mumbai - 400 013. Tel.: +91 22 6637 7000 Fax: +91 22 6626 6700