

### Jaiprakash Associates (JAL)

### VISIT NOTE

**Sensex: 13,928**

**CMP: Rs. 588**

**April 24, 2007**

We met the management of Jaiprakash Associates to gain insight about their business model and future growth drivers. The following are the key takeaways from the meeting:

#### Growth Drivers

JAL is a diversified company with business interests in cement, civil engineering and construction, real estate and hospitality industry. It also has a presence in the business of hydro power generation through its Build-Own-Operate (BOO) subsidiaries, Jaiprakash Hydro-Power, Jaiprakash Power Ventures & Jaypee Karcham Wangtoo Hydro Corporation. Increased investments in the hydropower construction, robust cement demand outlook and mega real estate ventures all augur well for the company going forward.

- Expansion in cement capacity from 7 mn tons to 22 mn tons across major regions to enable volume growth and lower geographical risk going forward.
- JAL's current order book of Rs 73 bn (3.7x FY06 revenues) coupled with its experience in successful execution of large scale projects in the past puts it in a strong position to capture a large portion of the potential market.
- The real estate development and sale of JAL's two projects (Taj Expressway and Jaypee Greens) in the coming years would ensure diversification of business risk. Our analysis suggests that the combined fair value could be over Rs 45 bn.

We have a positive view on the company based on the preliminary analysis derived from the meeting with the management. The key risks to growth would be project allotment delays & execution risk, major drop in cement prices and slowdown in the real estate sector.

Bloomberg Code	:	JPA@IN
Reuters Code	:	JAIA.BO
BSE Code	:	532532
NSE Code	:	JPASSOCIAT
52-Week Range (H/L)	:	753 / 280
Market Cap (Rs mn)	:	128,913
Share O/S (mn)	:	219.2
Free float (mn)	:	114.7
3m Avg. Volume	:	211,364
Face Value	:	10

#### Price Performance (%)

	3m	6m	12m
Absolute	(22.4)	15.2	17.4
Relative	(17.2)	10.1	(1.7)

Rs. Mn. (Standalone)	FY05	FY06	FY07E*	FY08E*	FY09E*
<b>Net Sales</b>	<b>27,420</b>	<b>31,410</b>	<b>35,217</b>	<b>39,819</b>	<b>51,381</b>
Operating Profit	5,260	6,120	8,870	10,243	11,932
OPM %	19.2	19.5	25.2	25.7	23.2
Other Income	1,490	1,830	1,430	1,400	1,500
Interest	2,130	2,400	2,610	3,000	2,400
Depreciation	1,330	1,510	1,630	1,793	1,972
<b>PBT</b>	<b>3,290</b>	<b>4,040</b>	<b>6,060</b>	<b>6,850</b>	<b>9,060</b>
Tax	1,220	1,250	2,110	2,310	3,010
<b>PAT</b>	<b>2,070</b>	<b>2,790</b>	<b>3,950</b>	<b>4,540</b>	<b>6,050</b>
NPM %	7.5	8.9	11.2	11.4	11.8
Extraordinary Income	-	3,610	-	-	-
<b>Net Profit</b>	<b>2,070</b>	<b>6,400</b>	<b>3,950</b>	<b>4,540</b>	<b>6,050</b>
Equity Paid Up	1,762	2,150	2,355	2,355	2,355
<b>Adjusted EPS- (Rs)</b>	<b>11.8</b>	<b>13.3</b>	<b>16.8</b>	<b>19.3</b>	<b>25.7</b>
PE (x)	50.1	45.3	32.6	28.4	21.3

\* Quick Estimates

## CEMENT

JAL with a capacity of 7 mn ton is the fourth largest player in India. Its manufacturing facilities are at MP (5.4 mn ton) and UP (1.6 mn ton). The company has lined up aggressive expansion plans in order to become the third largest cement group by 2009.

### Cement expansion plans

#### ➤ **UP Cement (2.5 mn ton)**

The company acquired assets of UP Cement from UP State Cement Corp. in Jan'06 at a cost of Rs 4.6 bn. The assets include two clinkerisation units at Churk and Dalla and a grinding unit at Chunar, all in Mirzapur district. The two units at Churk and Dalla are the only clinker units in UP as it has the last known available limestone reserves in the state.

The company would spend another Rs 3.9 bn towards installation of a new kiln and thermal power plant of 60MW. Post commissioning (Q3/Q4FY08), the facility will have a cumulative clinker capacity of ~2 mn ton and cement capacity of 2.5-3 mn ton (conversion ratio of other units in UP is ~1.4-1.5).

The facilities will enable the company cater to key markets in UP and nearby states and enjoy a lead distance advantage of ~150kms. The company will enjoy certain exemptions for ten years like sales tax, royalty on limestone and electricity duty on power plant.

#### ➤ **HP Cement (4.5 mn ton)**

The company is putting up a greenfield cement project of cumulative capacity of ~4.5 mn ton at Solan (HP) with a split grinding unit at Panipat (Haryana). The plant is expected to be commissioned by Q3/Q4-FY08 and will serve the key states in the Northern region viz. HP, Haryana, J&K, Punjab, Uttranchal and Delhi. The Panipat grinding unit offers the advantages of proximity to fly ash and key cement markets in North including Delhi. The plant will be supported by a proposed captive power plant of 30MW with the additional requirement to be bought from the grid. Capex on the entire project will be ~ Rs 11.5 bn.

#### ➤ **Sidhi Cement, MP (1.5 mn ton)**

The company is putting up a greenfield project of 1.5 mn ton at Sidhi (MP) and is expected to be commissioned by Q3FY09. The capex on the entire project will be ~ Rs 6 bn including a 38MW captive power plant. Post commissioning, the company will have a capacity of 11 mn tons in Central India which is likely to have a capacity of ~30 mn tons by Mar'09.

#### ➤ **Gujarat Anjan Cement (1.2 mn ton)**

JAL, through its subsidiary Jaypee Cement acquired Gujarat Anjan last year which is implementing a 1.2 mn ton cement plant in Kutch. This will enable the company establish presence in the western region and tap the cement export markets of Middle East.

The plant is expected to be commissioned by Q3FY09. The project cost including captive power plant of 22MW is ~Rs 6 bn.

#### ➤ **SAIL Bhilai & Satna Cement (2.5 mn ton)**

JAL plans to put up slag based cement plants through JV with SAIL at its plants in Bhilai (Chattisgarh) and Satna (MP) with a cumulative capacity of 2.5 mn ton. The company will have 74% stake in the project while SAIL will have 26%. The project will have a higher blending ratio and therefore better margins as it will utilize slag, the by product of steel manufacturing. The plant is expected to be commissioned by Q4FY10 at a project cost of ~Rs 6.1 bn.

#### ➤ **Other projects**

The projects under the conceptualisation stage are Chamba Cement in HP and Dungsam Cement in Bhutan (JV with Royal Govt. of Bhutan). These projects will have a cement capacity of 2 mn ton and 1 mn ton respectively and will get commissioned in FY10.

### Funding

The funding of the planned capex (~Rs 36 bn) on the cement expansion will be through FCCB (\$300 mn), ECB (\$250 mn), debt and internal accruals.

### Industry Outlook

The company expects the demand for cement to grow at the rate of 10-12% going forward on the back of 8-9% GDP growth. It expects the cement prices to be stable in the near term and does not expect constant government interventions impacting the sector in a significant way.

The company is confident of registering a significant volume growth from FY09 onwards on the back of planned capacity expansions and robust cement demand. Its cement dispatches over FY05-07 have registered a CAGR growth of 15% compared to industry growth rate of 10%.

### **Key Positives**

Post commissioning of all the planned projects (FY10), the company will have a cement capacity of 22 mn ton spread across all regions of India barring South. This will ensure a sustainable volume growth over the coming years and reduce the geographical risk as well.

### **Concerns**

North is expected to witness a drop in cement prices in FY09 due to a reduction in utilisation rates as the incremental capacities of Grasim, JAL, Shree and Binani are expected to get stabilized. Prices in other regions also would dip going forward as supply catches up with demand.

## Construction

JAL has been in the business of civil hydro power construction for the last four decades. It has been awarded 54% of all new hydropower contracts (14,393MW) during the 10th plan period. Emphasis on hydro power is expected to continue going forward, with a planned capacity addition of 70,000MW over the next ten years.

The company has been assigned "CR 1" grade by ICRA Ltd indicating Very Strong Contract Execution Capacity with best prospects of timely completion of projects without cost overruns, etc. for hydropower EPC contracts of value greater than Rs.2500 Crores.

### EPC Contracts

JAL is executing three out of the five hydropower projects awarded (till Mar'06) on EPC basis. The first project, Chamera II (MP) of 300MW was commissioned in FY04. The other two projects, Baghalihar (J&K) and Omkareshwar (MP) of 900MW and 520MW capacity respectively will be commissioned during FY08/09.

### BOO Projects

The company has commissioned two projects on BOO basis so far; 300MW Baspa II project in HP in FY04 and 400MW Vishnuprayag project in Uttranchal in FY07 through its subsidiaries Jaiprakash Hydropower and Jaiprakash Power Ventures. The third project, 1000MW Karcham Wangtoo in HP is expected to be completed by 2011. The company expects ramp up in construction from Q1FY08.

JAL has also signed MoA for 2,100MW of hydro electric projects in Arunachal Pradesh in which the state government has an equity participation of 11%.

The current order book as on Mar'07 is Rs 73bn over 11 contracts and is 3.7x FY06 revenues. The company expects the operating margins to be sustained around 20-22% going forward. The overall performance of the division is expected to be steady in the near term and accelerate from Q3FY08 onwards due to revenue bookings from Karcham Wangtoo and AP Irrigation projects.

### Key Positives

The government's focus on increasing the hydro power capacity in India (14,393 MW allocations in 10<sup>th</sup> plan v/s 4,538 in 9<sup>th</sup> plan) augurs well for the industry. JAL's experience in successful execution of large scale projects in the past puts it in a strong position to capture a large portion of the potential market.

### Concerns

A delay in project allocations, dip in operating margins, and project execution risk would be the main concerns associated with the sector.

## Real Estate & Taj Expressway

### Jaypee Greens

JAL is developing India's first 'golf centric' real estate project in Greater Noida. The project stretching over 452 acres will encompass development of residences, resort, spa, convention centre, integrated sports complex, nature reserve lakes and landscaped parks for mixed use of residential, commercial, recreational and institutional areas.

Jaypee Greens is envisioned as a development of international standard and excellence with tie ups with the best designers, planners & international consultants for each area of the project. The 18 hole Greg Norman golf course spread over 192 acres is already operational. The proposed real estate development is ~8mn sq ft; the company has sold 1.5 mn sq ft so far and expects to sell the balance over the next five years. The acquisition cost of the entire land for the project is ~Rs 3 bn.

### Taj Expressway

JAL is implementing the 160 kms long 6 lane access controlled expressway connecting Noida to Agra. In addition to the construction and operation of expressway, a ribbon development of 6,250 acres of land at five or more locations along the expressway for commercial, industrial, institutional and residential purposes will be undertaken.

The expressway will be completed over the next four years whereas the real estate development is expected to be phased out over the next fifteen years. The company is already in possession of 600 acres of land in Noida for which its acquisition cost is ~Rs 1.3 bn. The project includes real estate development of ~30 mn sq ft over the coming years and will be launched by Sept/Oct'07. The company expects the second parcel of land in Noida of another 600 acres to be allotted by Q1FY08.

The company expects the real estate business to contribute to the overall revenue and profitability from FY08 onwards. It expects the operating margins to be higher than the industry average due to the low cost of acquisition of land.

### Key Positives

Our analysis suggests that the combined value of Taj Expressway project and Jaypee Greens would be over Rs 45 bn. The real estate development and sale of these two projects in the coming years would ensure diversification of business risk as it will add an allied business stream to the current business.

### Concerns

A slowdown in the demand for housing due to increasing interest rates and a resultant fall in realty prices will be a dampener. Any delay in allocation or approval/clearance hindrances for the residual portion of land along the proposed Taj Expressway will impact the project.

## FINANCIALS

Segment Revenue	YTD FY07	YTD FY06	Var %	FY06
- Cement	13,300	8,680	53%	12,710
- Construction	13,320	14,970	-11%	19,980
- Hospitality & Golf Course	230	180	28%	240
- Unallocated	370	4,130*	-91%	4,310
<b>Total</b>	<b>27,220</b>	<b>27,960</b>	<b>-3%</b>	<b>37,240</b>
Less: Inter Segment Rev.	590	270		390
<b>Total Operating Income</b>	<b>26,630</b>	<b>27,690</b>	<b>-4%</b>	<b>36,850</b>
<b>PBIT</b>				
- Cement	3,590	1,110	223%	1,910
<i>% of Gross sales</i>	<i>27.0</i>	<i>12.8</i>		<i>15.0</i>
- Construction	3,000	3,780	-21%	4,760
<i>% of Gross sales</i>	<i>22.5</i>	<i>25.3</i>		<i>23.8</i>
- Hospitality & Golf Course	30	30	0%	40
<i>% of Gross sales</i>	<i>13.0</i>	<i>16.7</i>		<i>16.7</i>
- Unallocated	-	3,600*		3,610
<b>Total</b>	<b>6,620</b>	<b>8,520</b>	<b>-22%</b>	<b>10,320</b>

\* Includes Rs 3.6 bn of profit on sale of Jaiprakash Hydropower shares

## VALUATIONS

At the CMP of Rs 588, JAL trades at PER of 28.4x FY08E and 21.3x FY09E on its standalone earnings. Adjusting for estimated value of Jaypee greens and Taj Expressway, it quotes at PER of 18.5 FY08E and 13.9 FY09E.