

Cost pressures add to pricing risks

Bank of America
Merrill Lynch

Reena Verma Bhasin, CFA >> +91 22 6632 8667
Research Analyst
DSP Merrill Lynch (India)
reena.verma@baml.com

3Q FY11 results largely in line; mgt. flags cost pressures

UltraTech reported 3Q FY11 net profit of Rs3.2bn, down 36% YoY, but up 176% QoQ. Overall, EBITDA per ton was ~Rs725/t, down 28% YoY, due to higher costs, but up 62% QoQ owing to improved cement prices. In 3Q, domestic cement prices were flat YoY and up 11% QoQ. Volumes recovered seasonally, but stayed flat YoY. In its result statement, UltraTech pointed to a potential margin squeeze from rising energy costs, along with a greater reliance on fuel imports.

Earnings cut due to rising costs and volume disappointment

We have cut our FY11-12E earnings by 13-19%, led primarily by higher operating costs and lower volumes. Nearly 60-65% of UltraTech's fuel requirements are sourced from the open market, where prices are on a sharp uptrend.

Cement prices to fall; rational pricing difficult to sustain

Despite rising industry capacity, average cement prices across India are nearly flat vs. FY10 levels. Based on earlier cycles, we believe cement prices could fall about 5-7%. Recently, there have been reports of cement price hikes, likely led by the industry's rational pricing efforts. We think such hikes are not sustainable.

Demand worries add to supply woes

We forecast the industry's capacity utilization at 74% in FY12 vs. 78% in FY11, assuming demand recovery in FY12. Our outlook has downside, given the inverse relationship between inflation vs. cement demand, and potential slippages in infra-spend

Stock appears vulnerable; maintain Underperform

Among cement majors, UltraTech has relatively high volume exposure to the oversupplied markets of south and west India. Between Grasim and UltraTech, we prefer Grasim (GRSJF, Rs2368, Neutral) for its steep valuation discount.

Estimates (Mar)

(Rs)	2009A	2010A	2011E	2012E	2013E
Net Income (Adjusted - mn)	9,770	10,933	14,145	12,548	15,053
EPS	78.48	87.82	51.63	45.80	54.94
EPS Change (YoY)	-3.0%	11.9%	-41.2%	-11.3%	20.0%
Dividend / Share	5.14	6.00	6.00	6.00	7.20
Free Cash Flow / Share	43.25	93.20	(23.60)	23.06	22.14

Valuation (Mar)

	2009A	2010A	2011E	2012E	2013E
P/E	13.04x	11.65x	19.82x	22.34x	18.62x
Dividend Yield	0.502%	0.586%	0.586%	0.586%	0.704%
EV / EBITDA*	17.99x	14.69x	10.01x	10.51x	9.23x
Free Cash Flow Yield*	1.92%	4.14%	-2.31%	2.25%	2.16%

* For full definitions of *iQmethod*SM measures, see page 7.

Stock Data

Price	Rs1,023
Price Objective	Rs750.00
Date Established	19-Nov-2010
Investment Opinion	C-3-7
Volatility Risk	HIGH
52-Week Range	Rs820.00-Rs1,189
Mrkt Val / Shares Out (mn)	US\$6,135 / 274.0
Average Daily Volume	108,548
BofAML Ticker / Exchange	XDJNF / BSE
Bloomberg / Reuters	UTCEM IN / ULTC.BO
ROE (2011E)	13.2%
Net Dbt to Eqty (Mar-2010A)	-3.2%
Est. 5-Yr EPS / DPS Growth	10.0% / 10.0%
Free Float	36.0%

Key Changes

(Rs)	Previous	Current
2011E EPS	63.90	51.63
2012E EPS	52.50	45.80
2013E EPS	65.79	54.94
2011E EBITDA (m)	37,712.3	32,515.9
2012E EBITDA (m)	34,513.2	30,973.8
2013E EBITDA (m)	41,462.9	35,285.2

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Refer to important disclosures on page 8 to 10. Analyst Certification on Page 5. Price Objective Basis/Risk on page 5. Link to Definitions on page 5. 11012744

25 January 2011

iQprofileSM UltraTech Cement Ltd.

Key Income Statement Data (Mar)	2009A	2010A	2011E	2012E	2013E
(Rs Millions)					
Sales	63,831	70,496	152,508	164,134	182,823
Gross Profit	17,064	19,710	29,762	28,474	32,210
Sell General & Admin Expense	NA	NA	NA	NA	NA
Operating Profit	13,834	17,056	21,049	19,360	22,669
Net Interest & Other Income	(219)	(1,174)	(514)	(1,131)	(801)
Associates	NA	NA	NA	NA	NA
Pretax Income	13,614	15,882	20,535	18,229	21,868
Tax (expense) / Benefit	(3,844)	(4,949)	(6,366)	(5,651)	(6,779)
Net Income (Adjusted)	9,770	10,933	14,145	12,548	15,053
Average Fully Diluted Shares Outstanding	124	124	274	274	274

Key Cash Flow Statement Data

Net Income	9,770	10,933	14,145	12,548	15,053
Depreciation & Amortization	3,230	3,881	8,713	9,115	9,541
Change in Working Capital	(898)	(752)	(6)	86	139
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	1,806	301	0	0	0
Cash Flow from Operations	13,908	14,364	22,853	21,749	24,733
Capital Expenditure	(8,524)	(2,762)	(29,320)	(15,430)	(18,667)
(Acquisition) / Disposal of Investments	(11)	453	(8,100)	0	0
Other Cash Inflow / (Outflow)	9	760	0	0	0
Cash Flow from Investing	(8,525)	(1,549)	(37,420)	(15,430)	(18,667)
Shares Issue / (Repurchase)	0	0	0	0	0
Cost of Dividends Paid	(728)	(851)	(1,874)	(1,874)	(2,248)
Cash Flow from Financing	3,283	(6,222)	2,116	477	(66)
Free Cash Flow	5,385	11,602	(6,467)	6,319	6,066
Net Debt	10,477	(1,488)	27,756	23,311	19,494
Change in Net Debt	(4,655)	(11,964)	29,244	(4,445)	(3,818)

Key Balance Sheet Data

Property, Plant & Equipment	53,130	52,011	141,863	148,178	157,304
Other Non-Current Assets	453	0	11,458	11,458	11,458
Trade Receivables	1,862	2,158	4,551	4,897	5,455
Cash & Equivalents	10,940	17,533	17,707	24,503	30,502
Other Current Assets	10,709	11,728	24,743	26,625	29,657
Total Assets	77,094	83,430	200,321	215,661	234,376
Long-Term Debt	12,193	6,822	42,836	45,187	47,369
Other Non-Current Liabilities	7,229	8,307	17,487	17,487	17,487
Short-Term Debt	9,223	9,223	2,628	2,628	2,628
Other Current Liabilities	12,427	12,991	30,426	32,740	36,469
Total Liabilities	41,073	37,343	93,377	98,042	103,953
Total Equity	36,021	46,087	106,945	117,619	130,423
Total Equity & Liabilities	77,094	83,430	200,321	215,661	234,377

iQmethodSM - Bus Performance*

Return On Capital Employed	19.2%	18.6%	10.5%	9.3%	10.2%
Return On Equity	31.0%	26.6%	13.2%	11.2%	12.1%
Operating Margin	21.7%	24.2%	13.8%	11.8%	12.4%
EBITDA Margin	28.4%	31.4%	21.3%	18.9%	19.3%

iQmethodSM - Quality of Earnings*

Cash Realization Ratio	1.4x	1.3x	1.6x	1.7x	1.6x
Asset Replacement Ratio	2.6x	0.7x	3.4x	1.7x	2.0x
Tax Rate (Reported)	28.2%	31.2%	31.0%	31.0%	31.0%
Net Debt-to-Equity Ratio	29.1%	-3.2%	26.0%	19.8%	14.9%
Interest Cover	8.7x	15.6x	4.4x	3.9x	4.0x

Key Metrics

* For full definitions of iQmethodSM measures, see page 7.

Company Description

Ultratech is the largest cement company in India with an annual cement capacity of 49mn tons in India and 3mn tons overseas. It has cement plants across India but geographical exposure is highest to south-west India at around 52% of overall volumes. Historically, Ultratech ranks among India's largest exporters of cement and clinker. Ultratech is a 60% subsidiary of Grasim, a flagship company of the Aditya Birla group.

Investment Thesis

We rate UltraTech as Underperform for 3 key reasons: 1) cement prices across the industry have downside risk, 2) we forecast UltraTech's earnings to decline over FY11-12E, and 3) stock valuations are above replacement cost despite falling RoE.

Stock Data

Price to Book Value 2.6x

Table 1: UltraTech - 3Q FY11 results summary

Yr to 31 Mar	3Q FY10A*	2Q FY11A	3Q FY11A	YoY	QoQ
Total volumes (mn tons)	9.76	9.10	9.76	0%	7%
Rs mn					
Net turnover	36,818	32147	37152	1%	16%
Operating costs	26,930	28069	30074	12%	7%
EBDIT	9,888	4078	7078	-28%	74%
EBDIT margin	26.9%	13%	19%		
Reported net profit	4,990	1158	3190	-36%	176%

*Pro forma merged financials of Ultratech & Samruddhi; Source: Company

Table 2: Supply-demand outlook for Indian cement industry

As on 31 March (mn tpa)	FY08	FY09	FY10	FY11E	FY12E	FY13E
Reported cement capacity	189	216	256	305	328	353
Effective cement capacity	173	202	234	274	315	340
Effective clinker capacity	139	167	197	236	276	300
Capacity growth	11%	20%	18%	20%	17%	8%
Cement demand	168	181	200	214	233	259
Demand growth	8%	8%	10%	7%	9%	11%
Domestic consumption	164	178	197	211	231	256
Growth in domestic consumption	10%	8%	11%	7%	9%	11%
Cement exports	3.7	3.2	2.2	2.4	2.4	2.4
Export growth	-35%	-12%	-31%	8%	0%	0%
Cement capacity utilisation	97%	90%	85%	78%	74%	76%
Cement/Clinker Ratio	1.36	1.37	1.36	1.36	1.36	1.36
Blended cement as % of total production	75%	75%	75%	75%	75%	75%
Clinker capacity utilisation (incl. exports)	91%	81%	76%	68%	63%	64%
Clinker capacity utilisation (excl. exports)	89%	79%	74%	67%	62%	63%

Source: CMA, BofA Merrill Lynch Global Research estimates

Table 3: Valuation comparison of Indian cement majors

	Share Price	Market Cap (US\$ mn)	BofAML Rating
ACC	1023	4195	C-3-7/UNDERPERFORM
Grasim	2365	4745	C-2-7/NEUTRAL
Ambuja Cements	129	4285	C-3-7/UNDERPERFORM
Ultratech Cement	1,024	6139	C-3-7/UNDERPERFORM
Shree Cement	1727	1316	C-2-7/NEUTRAL
India Cements	99	664	C-3-7/UNDERPERFORM
BSE30	18970		
Yr to 31 March/Dec	2009/FY10	2010E/FY11E	2011E/FY12E
EV/Capacity (US\$/ton)			
ACC	172	169	133
Grasim	98	95	90
Ambuja Cements	185	157	150
Ultratech Cement	138	131	134
Shree Cement	104	84	67
India Cements	67	68	71
Replacement cost benchmark-India (US\$/ton)	120-125	120-125	120-125
RoE (%)			
ACC	29	19	13
Grasim	23	16	14
Ambuja Cements	20	19	16
Ultratech Cement	27	14	11
Shree Cement	43	15	15
India Cements	10	4	2
Local Market RoE	16	18	19
P/E (x)			
ACC	12.3	16.6	21.3
Grasim	7.9	10.3	10.3
Ambuja Cements	16.2	14.9	16.1
Ultratech Cement	11.1	19.8	22.4
Shree Cement	7.7	18.7	16.1
India Cements	8.9	21.5	31.9
Local Market PE	23.6	18.3	15.0
EV/EBITDA (x)			
ACC	7.3	9.8	11.0
Grasim	4.7	7.1	7.0
Ambuja Cements	10.0	8.8	8.8
Ultratech Cement	6.6	10.1	10.8
Shree Cement	4.1	6.4	5.4
India Cements	6.0	10.5	11.6
Local Market EV/EBITDA	12.7	10.3	8.6

Source: BofA Merrill Lynch Global Research estimates

Price objective basis & risk UltraTech Cemen (XDJNF)

We have a price objective of Rs750/sh for UltraTech. We value the company at an EV/capacity of around US\$95-\$100/ton, based on a 20-25% discount to the industry's replacement cost of US\$125/ton. The trough discount vs. replacement cost was steeper, at 40-45%, in the previous cycle, but improved RoEs and a significantly healthier balance sheet may warrant a lower discount in the current cycle. A 20-25% discount is in line with the average (rather than trough) discount witnessed through the previous downturn (1997-2002). An unforeseen rise in energy prices would be an added negative for our outlook. Upside risk to our outlook would stem from strong and sustained rational pricing behaviour from cement producers across the industry. A sharp easing in energy prices would also present upside to our view.

Link to Definitions Industrials

Click [here](#) for definitions of commonly used terms.

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SEBI Regn no. : BSE - INB/INF 011348134 NSE – INB/INF 231348138
Address – Mafatlal Centre, 8th Floor, Nariman Point, Mumbai, India. 400021
Tel : +91 22 6632 8000

25 January 2011

India - General Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Aditya Birla Nu	ADYAF	ABNL IN	Reena Verma Bhasin, CFA
	Anant Raj Industries Ltd	XNRJF	ARCP IN	Gagan Agarwal
	Brigade Enterprises	XBDGF	BRGD IN	Gagan Agarwal
	Chambal Fertilisers & Chemicals	CHBZF	CHMB IN	Prasad Deshmukh
	Cummins India	CUIDF	KKC IN	Sanjaya Satapathy
	DLF Limited	XVDUF	DLFU IN	Gagan Agarwal
	Exide Indus Ltd	XEDRF	EXID IN	Sanjaya Satapathy
	Fortis Healthcare Limited	XFFTF	FORH IN	Prasad Deshmukh
	Havells	HVLIF	HAVL IN	Sanjaya Satapathy
	Housing Development and Infrastructure	XGHSF	HDIL IN	Gagan Agarwal
	Indiabulls Real Estate Ltd	IBELF	IBREL IN	Gagan Agarwal
	Jaypee Infratech	XJAYF	JPIN IN	Gagan Agarwal
	Jet Airways	JTAIF	JETIN IN	Anand Kumar
	Motherson Sumi	XMSUF	MSS IN	Sanjaya Satapathy
	Puravankara Projects Ltd	XPJVF	PVKP IN	Gagan Agarwal
	Renuka Sugars	SRNKF	SHRS IN	Sanjaya Satapathy
	SINTEX INDUSTRIES LTD	SIXDF	SINT IN	Prasad Deshmukh
	Sobha Developers	SBDRF	SOBHA IN	Gagan Agarwal
	SpiceJet Ltd	MDLFF	SJET IN	Anand Kumar
	Voltas	VTSJF	VOLT IN	Sanjaya Satapathy
NEUTRAL				
	Grasim	GRSJF	GRASIM IN	Reena Verma Bhasin, CFA
	Grasim -G	GRSJY	GRAS LX	Reena Verma Bhasin, CFA
	Jain Irrigation Systems Ltd	JNIDF	JI IN	Prasad Deshmukh
	Shree Cements	SREEF	SRCM IN	Reena Verma Bhasin, CFA
	Unitech Ltd	UTKIF	UT IN	Gagan Agarwal
UNDERPERFORM				
	Ambuja Cements	AMBUF	ACEM IN	Reena Verma Bhasin, CFA
	APIL	ANSFF	APIL IN	Gagan Agarwal
	Assoc. Cement	ADCLF	ACC IN	Reena Verma Bhasin, CFA
	Bajaj Hindusthan	BJJHF	BJH IN	Sanjaya Satapathy
	Balrampur Chini	BMPRF	BRCM IN	Sanjaya Satapathy
	Container Corp	CIDFF	CCRI IN	Sanjaya Satapathy
	India Cements	INIAF	ICEM IN	Reena Verma Bhasin, CFA
	India Cements -G	IAMUY	ICEM LX	Reena Verma Bhasin, CFA
	Jindal Saw	SWPFF	JSAW IN	Sanjaya Satapathy
	Nagarjuna Fertilizers & Chemicals Ltd	NFACF	NFCL IN	Prasad Deshmukh
	Omaxe Limited	XOMXF	OAXE IN	Gagan Agarwal
	Tata Chemicals Ltd	TTCXF	TTCH IN	Prasad Deshmukh
	Triveni Engg	TVIEF	TRE IN	Sanjaya Satapathy
	UltraTech Cemen	XDJNF	UTCEN IN	Reena Verma Bhasin, CFA
	Welspun Corp Ltd	XUQRF	WLCO IN	Sanjaya Satapathy

25 January 2011

iQmethodSM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales} + \text{Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

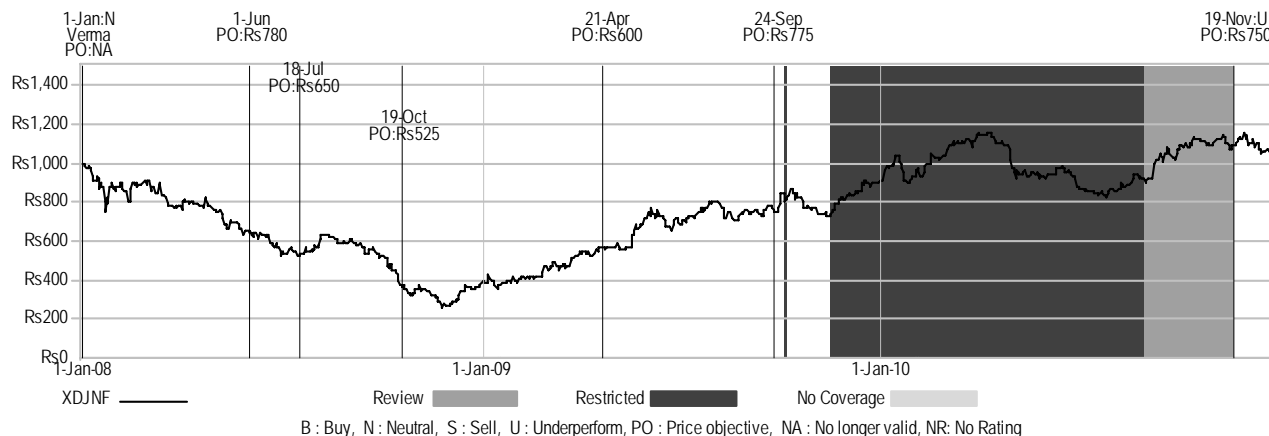
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XDJNF Price Chart



Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of December 31, 2010 or such later date as indicated.

Investment Rating Distribution: Building Group (as of 01 Jan 2011)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	50	47.17%	Buy	21	43.75%
Neutral	31	29.25%	Neutral	8	29.63%
Sell	25	23.58%	Sell	10	41.67%

Investment Rating Distribution: Global Group (as of 01 Jan 2011)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	2011	53.86%	Buy	874	48.31%
Neutral	925	24.77%	Neutral	444	52.30%
Sell	798	21.37%	Sell	276	36.75%

* Companies in respect of which BofA Merrill Lynch or one of its affiliates has received compensation for investment banking services within the past 12 months. For purposes of this distribution, a stock rated Underperform is included as a Sell.

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Neutral	≥ 0%	≤ 30%
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25 January 2011

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