## Result Update

May 7, 2010

UTCL reported Q4FY10 revenues of Rs.1,909.4 cr up by 2.6% Y-o-Y. Its Operating Profit fell by 23.8% to Rs.415.8 cr Y-o-Y. The Net Profit too fell by 26.1% to Rs.228.5 cr, while NPM saw a dip of 460 bps to 12% in Q4FY10.

**Quarterly Financials – Standalone** Rs.Cr.

| Particulars | Q4FY10 | Q4FY09 | % Chg | Q3FY10 | % Chg | FY10 | FY09 | % Chg |
|---|---|---|---|---|---|---|---|---|
| Net Sales | 1909.4 | 1860.1 | 2.6% | 1651.8 | 15.6% | 7049.7 | 6383.1 | 10.4% |
| Other operating income | 13.2 | 15.0 | -12.1% | 17.5 | -24.6% | 63.9 | 54.3 | 17.7% |
| Total Operating Income | 1922.5 | 1875.1 | 2.5% | 1669.3 | 15.2% | 7113.5 | 6437.4 | 10.5% |
| **Expenditure** | | | | | | | | |
| Increase/Decrease in stock | 73.9 | 59.3 | 24.6% | -7.8 | -1048.5% | 2.3 | -88.8 | -102.6% |
| Raw Materials | 258.3 | 185.2 | 39.5% | 261.7 | -1.3% | 960.6 | 685.0 | 40.2% |
| Purchase of Traded Goods | 29.2 | 11.4 | 156.0% | 11.0 | 165.1% | 63.7 | 19.5 | 226.9% |
| Employees Cost | 66.0 | 56.6 | 16.6% | 62.3 | 5.9% | 250.6 | 217.7 | 15.1% |
| Power & Fuel | 365.1 | 409.2 | -10.8% | 356.4 | 2.4% | 1430.9 | 1727.0 | -17.1% |
| Freight & Handling Expenses | 348.5 | 306.7 | 13.6% | 293.0 | 19.0% | 1228.8 | 1058.3 | 16.1% |
| Other Expenditure | 365.7 | 300.9 | 21.5% | 291.7 | 25.4% | 1141.7 | 1060.3 | 7.7% |
| Total Operating Expenditure | 1506.7 | 1329.4 | 13.3% | 1268.2 | 18.8% | 5076.4 | 4767.7 | 6.5% |
| **Operating Profit** | **415.8** | **545.8** | -23.8% | **401.1** | 3.7% | **2037.2** | **1669.6** | 22.0% |
| *OPM %* | *21.8%* | *29.3%* | | *24.3%* | | *28.9%* | *26.2%* | |
| Other Income | 12.7 | 16.0 | -21.0% | 12.5 | 1.5% | 58.9 | 51.6 | 14.1% |
| Interest Expenses | 28.5 | 34.0 | -16.3% | 26.2 | 8.5% | 117.5 | 125.5 | -6.4% |
| Depreciation | 99.3 | 90.6 | 9.6% | 98.5 | 0.8% | 388.1 | 323.0 | 20.1% |
| PBT | 300.7 | 437.2 | -31.2% | 288.8 | 4.1% | 1590.4 | 1272.7 | 25.0% |
| *PBTM %* | *15.7%* | *23.5%* | | *17.5%* | | *22.6%* | *19.9%* | |
| Tax | 72.1 | 127.7 | -43.5% | 92.8 | -22.3% | 494.9 | 384.4 | 28.7% |
| *Effective Tax Rate %* | *24.0%* | *29.2%* | | *32.1%* | | *31.1%* | *30.2%* | |
| **Net Profit** | **228.5** | **309.5** | -26.1% | **196.0** | 16.6% | **1095.5** | **888.3** | 23.3% |
| *NPM %* | *12.0%* | *16.6%* | | *11.9%* | | *15.5%* | *13.9%* | |
| Equity Capital | 124.5 | 124.5 | 0.0% | 124.5 | 0.0% | 124.5 | 124.5 | 0.0% |
| **EPS (Rs.)** | **18.4** | **24.9** | -26.1% | **15.7** | 16.6% | **88.0** | **71.4** | 23.3% |
| Domestic Sales (mn tones) | 4.93 | 4.49 | 9.8% | 4.34 | 13.6% | 17.26 | 15.42 | 11.9% |
| Cement Exports (mn tones) | 0.15 | 0.12 | 25.0% | 0.16 | -6.3% | 0.51 | 0.48 | 6.3% |
| Clinker Sales (mn tones) | 0.62 | 0.74 | -16.2% | 0.55 | 12.7% | 2.44 | 2.27 | 7.5% |
| Total Volumes (mn tones) | 5.70 | 5.35 | 6.5% | 5.05 | 12.9% | 20.21 | 18.17 | 11.2% |
| Blended Realisation (Rs. per tonne) | 3349.7 | 3476.9 | -3.7% | 3270.9 | 2.4% | 3488.2 | 3513.0 | -0.7% |

(Source: Company Press Release)

**Some of the key highlights of the results are as follows:**

- UTCL's revenues in Q4FY10 were almost flat y-o-y at Rs.1,909.4 cr and blended realisations per tonne saw a degrowth of 3.7% y-o-y to Rs.3,349.7. On a q-o-q basis realizations improved marginally by 2.4%. Clinker sales (incl. exports) in Q4FY10 fell by 16.2% y-o-y to ~6.2 lakh tonnes, while cement exports witnessed a growth of 25% y-o-y to 1.5 lakh tonnes.

- Domestic cement volumes stood at 4.9 mn tonnes in Q4FY10 vis-à-vis 4.5 mn tonnes in Q4FY09. Domestic and export realizations were lower y-o-y. Post December 2009, there has been some price increase all over the country, with some regions reporting sharper hikes.

- OPMs have fallen y-o-y by 750 bps to 21.8% in Q4FY10. This has been mainly on account of higher per tonne cost of raw materials, other expenditure and lower realisations. Raw materials as a percentage of sales expanded by 350 bps y-o-y to 13.5%. the rise in raw material cost was on the back of increase in limestone royalty rates. A rise was also witnessed in imported coal cost during the quarter. Other Expenditure rose by 200 bps as a percentage of sales y-o-y and by 150 bps q-o-q. Higher packaging cost, repair and maintenance expenses and rise in advertisement cost and clinker freight all led to other expenditure increasing by 14.1% y-o-y and 11.1% q-o-q to Rs.641.6/ton. Power and fuel cost per tonne fell in Q4FY10 by 16.3% y-o-y and 9.2% q-o-q to Rs.640.5/tonne on account of benefits accruing from stabilization of the captive thermal power plants commissioned in CY09. Lower realisations and higher expenses led to EBIDTA per tonne dropping by 28.5% y-o-y to Rs.729.5/tonne in Q4FY10.

| Cost per tonne analysis | Q4FY10 | Q4FY09 | % Chg | Q3FY10 | % Chg | FY10 | FY09 | % Chg |
|---|---|---|---|---|---|---|---|---|
| Raw Materials | 453.2 | 346.2 | 30.9% | 518.1 | -12.5% | 475.3 | 377.0 | 26.1% |
| Employees Cost | 115.8 | 105.8 | 9.5% | 123.4 | -6.1% | 124.0 | 119.8 | 3.5% |
| Power & Fuel | 640.5 | 764.9 | -16.3% | 705.6 | -9.2% | 708.0 | 950.5 | -25.5% |
| Freight & Handling Expenses | 611.5 | 573.3 | 6.7% | 580.2 | 5.4% | 608.0 | 582.4 | 4.4% |
| Other Expenditure | 641.6 | 562.5 | 14.1% | 577.6 | 11.1% | 564.9 | 583.6 | -3.2% |
| Total Cost | 2643.4 | 2484.8 | 6.4% | 2511.3 | 5.3% | 2511.8 | 2623.9 | -4.3% |
| EBIDTA | **729.5** | **1020.1** | -28.5% | **759.6** | -4.0% | **1008.0** | **918.9** | 9.7% |

(Source: Company)

- Other income fell by 21% y-o-y to Rs.12.7 cr. Depreciation cost rose by 9.6% y-o-y to Rs.99.3 cr on the back of commissioning of expanded capacities and captive thermal power plants. Lower other income and higher depreciation cost led to net profit margins dipping by 460 bps from 16.6% in Q4FY09 to 12% in Q4FY10.

- As of December 2009, UTCL has planned a capex of Rs.2,000 cr over FY10-12 for setting up a 25MW Thermal Power Plant at its unit in Awarpur, Maharashtra; additional grinding and evacuation facility at its unit in Gujarat and waste heat recovery systems across units for generating power out of waste gases. The funding of the same will be done through internal accruals. The current 256MW captive thermal power plant caters currently to ~80% of the power required by UTCL. About Rs.800 cr of the total capex is assumed to have been spent in FY10, Rs.1,000 cr would be spent in FY11 and the balance would be utilized by FY12.

- The current cement capacity stands at 23.1 mtpa. The 4.9 mtpa capacity Tadpatri plant commissioned in Q4FY10 could help in boosting volumes in FY11 and FY12. However, given the additional capacities coming in the industry, this could result in cement prices softening and thereby leading to lower overall realisations on y-o-y basis in FY11.

- UTCL plans to minimise the impact of lower realisations and softening of prices by strengthening their logistics infrastructure and keeping power and fuel cost under control.

- The Board of Directors at its meeting held on April 29, 2010 have approved the acquisition of ETA Star Cement Co. LL, Dubai. At an enterprise value of Rs.1,700 cr, which translates into an EV/Ton of ~US$126. It has cement operations UAE, Bahrain and Bangladesh. The acqusition will be carried out by capitalizing 'UltraTech Cement Middle East Investment Ltd, UTCL's wholly owned subsidiary. The deal will be funded through a mix of debt and internal accruals. ETA Star has a market share of 10% and 20% in Abu Dhabi and Bahrain, respectively. ETA Star's manufacturing facilities include a 2.3 million tonne clinker plant and a 2.1 million tonne grinding plant, both in the United Arab Emirates, a 0.4 million-tonne grinding plant in Bahrain and a 0.5 million tonne grinding plant in Bangladesh. This acquisition alongwith the amalgamation of Samruddhi Cement will increase UTCL's total capacity to ~52 MTPA.

- As per the management, the transaction would be completed by end of Q1FY11, and would be accretive to its earnings per share. The acquisition is in line with UTCL's long-term strategy of expanding its global presence across businesses. The acquisition would give UTCL the advantage of size. Apart from adding value to its capacity, it will benefit UTCL as Abu Dhabi and Bahrain's real estate markets are not as depressed as Dubai. The economies of both Abu Dhabi and Bahrain are largely driven by oil, which, given the recent rise in crude prices, could soon revive construction activity and boost demand for cement.

- The Board of Directors at its meeting held on November 15, 2009 approved the amalgamation of Samruddhi Cement Ltd with UTCL in terms of a Scheme of Amalgamation under sections 391 to 394 of the Companies Act, 1956 ("the Scheme"). The appointed date of the amalgamation is 1st July, 2010. The Board has also approved the share exchange ratio of 4 (four) equity shares of the Company of face value Rs. 10/- each for every 7 (Seven) equity shares of Samruddhi of face value Rs. 5/- each. The Cement Business of Grasim Industries Limited ("Grasim"), the holding company, is currently under demerger to Samruddhi and the Scheme will take effect only upon completion of the demerger and issuance of shares of Samruddhi to the shareholders of Grasim pursuant to the demerger. On the completion of this scheme, UltraTech is expected to emerge as the largest Cement and RMC entity in the country, and 10th largest in the world in cement capacity.

- Grasim, announced demerger of its cement business into its wholly owned subsidiary Samruddhi Cements Ltd, which will ultimately be merged with UTCL to make it the largest pure cement player in the country. The board of UTCL has approved the restructuring. The first leg of the restructuring process i.e. demerger of Samruddhi from Grasim has been sanctioned at the High Court of Indore on March 31, 2010 but is yet to be sanctioned by the High Court of Gujarat. The second leg of restructuring is expected to be completed by July/August 2010.

- Going forward, UTCL has indicated that the industry demand for cement could grow by 10% due to initiatives being taken by the Government on the infrastructure front. However, it is expected that the industry will witness a surplus scenario in FY11 with the management expecting addition of 30 MTPA during the year and this could result in pressure on margins. Capacity utilization rate is expected to be ~80% and this too could put pressure on margins. The management has indicated that it will focus on higher growth together with cost efficiency that could partially offset the pressure on its margins it could face due to the oversupply scenario.

## Concerns

- Additional capacities coming on stream across the country could result in capacity utilization rates coming down thereby adding pressure on margins.

- Softening of cement prices could lead to lower realisations.

- Increase in prices of coal could lead to higher costs and pressure on margins.

## Conclusion

UTCL's FY10 results were almost in line with our estimates except that its PBIDT margins were lower by 90 bps than our estimates. UTCL reported EPS of Rs.89.4 vis-à-vis our estimate of Rs.88.

Cement prices have started correcting recently on a seasonally weak demand. We expect cement prices to remain under mild pressure for most of FY11 on oversupply concerns.

We are cautious on the acquisition of Dubai-based ETA Star Cement given the lull in demand in the Middle East. However, the management suggests that through this acquisition it could enter the markets of Bahrain and Bangladesh as well where ETA has its plants and these regions do not currently face the problem of poor demand.

Cement prices after falling sharply across the country in Q3FY10 have moved up in Q4FY10. Total cement capacity in India stood at around 225 MTPA as of FY09 and additionally ~29 MTPA capacity was added in FY10. UTCL management expects another 30 MTPA to be added in FY11. Once these additional capacities are fully ramped up they could put pressure on the operating rates and margins. South India where UTCL majorly operates is currently facing a lull in demand and also additional capacities of ~ 5-8 mn tonnes have been commissioned as of FY10 in the region and this could add to the pressure on margins and also likely result in softening of cement prices.

So far we have witnessed the impact, of a largish fall in realisations in Andhra Pradesh and Karnataka and smaller fall in other areas, on revenues and margins due to new capacities coming on stream. Once this scenario extends to other areas/states, the negative impact could get magnified unless this is offset by an increase in demand from infrastructure and real estate sectors. Although the management has suggested that the situation in the South is stabilizing slowly now, we remain cautious.

In our last update dated January 21, 2010, we had stated that UTCL could find it difficult to cross and stay above Rs.1,059 (the recent high) in the near term, while greater recognition of the impact of falling realisations could take the stock down to Rs.894 (10x FY10E EPS) over the next 1-2 quarters. Post the issue of the report, the stock touched a high of Rs.1,072.2 on April 9, 2010 and touched a low of Rs.882 on January 27, 2010.

We are maintaining our FY11 estimates of Rs.74.1 EPS. At the CMP of Rs.926.6, the stock is trading at 13.2x its FY11E EPS and $125.3 FY11E EV/tonne. We expect the stock to stay in the Rs.870 -1,030 band for the next quarter.

| Particulars (Rs.Cr.) | FY08 | FY09 | FY10 (E)* | FY10 (A)* | FY11 (E)* |
|---|---|---|---|---|---|
| Sales | 5623.8 | 5623.8 | 7051.5 | 7049.7 | 7065.7 |
| Operating Profit | 1689.2 | 1740.4 | 2103.2 | 2037.2 | 1703.7 |
| OPM % | 30.0% | 30.9% | 29.8% | 28.9% | 24.1% |
| PAT | 927.3 | 983.3 | 1112.9 | 1095.5 | 922.2 |
| PATM % | 16.5% | 17.5% | 15.8% | 15.5% | 13.1% |
| EPS (Rs) | 79.1 | 78.6 | 89.4 | 88.0 | 74.1 |
| P/E | 12.0 | 12.1 | 10.6 | 10.8 | 13.2 |

* E = Estimates, OE = Original Estimates, RE = Revised Estimates (Source: Company, HDFC Sec Estimates)

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