

Company Flash

4 February 2008 | 6 pages

ACC (ACC.BO)

Sell: ACC Underperforms in 4QCY07 Due to Costs

- 4Q below expectations** — ACC's derived adj net profit for 4Q07 (it reported CY07 results) was Rs2.99bn, -11% yoy and 15% below our forecasts. 4Q sales grew 11% yoy, on higher selling prices (+8% yoy), but EBITDA fell 10% yoy, affected by higher costs. Adj PAT for CY07 was Rs12.9bn and sales grew 21% yoy to Rs70bn. CY07 volumes grew 6% and realizations grew 14% yoy.
- Muted volume growth** — Like many of the cement majors, ACC has capacity constraints and volumes grew only 2% yoy in 4QCY07, marginally higher than expectations. Realizations grew only 8% yoy, lower than the other majors, which reported 10% yoy growth during the quarter.
- Costs continue to have an impact** — As in the past three quarters, 4Q PAT was also affected by higher costs. The increase in 4Q was mainly due to higher raw material costs (+29% yoy per tonne of cement sold) and other expenses (+23% yoy). After a surge in 3Q, per tonne power and fuel costs were lower on a qoq basis due to some benefits kicking in from captive power capacity.
- Expansion plans, new plant announced** — ACC has already about 2m tpa of capacity in CY07. Of the ongoing capex, ACC expects to complete 2.5m tpa of capacity by end-CY08 and 3m tpa by mid-CY09. It has announced a 3m tpa cement plant (with 25MW power) costing Rs14.5bn in Maharashtra to be completed by 2010.
- Reiterate Sell (3M)** — We expect a steady stream of new capacities in CY08/CY09, which is expected to disrupt pricing. Maintain Sell (3M).

Sell/Medium Risk	3M
Price (01 Feb 08)	Rs753.50
Target price	Rs790.00
Expected share price return	4.8%
Expected dividend yield	2.3%
Expected total return	7.1%
Market Cap	Rs141,378M US\$3,599M

Price Performance (RIC: ACC.BO, BB: ACC IN)



Figure 1. ACC – Statistical Abstract

		Revenue (Rs m)	PAT (Rs m)	EBITDA (Rs m)	EPS (Rs)	EPS growth* (%)	P/E* (x)	EV/EBITDA* (x)	EV/tonne* (US\$)
FY05	31-Mar	38,874	3,520	6,186	19.6	151%	38.5	24.2	216
CY05 (9 m)	31-Dec	31,775	2,838	5,357	15.3	4%	37.0	20.8	143
CY06	31-Dec	57,170	10,645	16,232	56.7	178%	13.3	8.6	171
CY07E	31-Dec	70,535	14,601	21,813	77.5	37%	9.7	6.1	139
CY08E	31-Dec	75,904	12,536	18,924	66.6	-14%	11.3	7.2	133
CY09E	31-Dec	76,994	8,256	13,499	43.9	-34%	17.2	10.0	117

Source: Company Reports, Citi Investment Research. *Annualised. Price as on 1 February 2008. Rs/US\$ rate at 40. Forecasts shown for CY07, as ACC has yet to report detailed CY07 financials.

See Appendix A-1 for Analyst Certification and important disclosures.

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Quarterly and Annual Results

Figure 2. ACC – 4QCY07 and CY07 Results

(Rs m)	CY07E	CY06	% chg	4Q CY07	4Q CY06	% chg
Sales	70,072	58,035	21%	17,856	16,145	11%
Expenditure	50,898	41,803	22%	13,683	11,514	19%
EBITDA	19,174	16,232	18%	4,173	4,631	-10%
EBITDA per tonne	960	861	12%	832	942	-12%
% margin	27.4%	28.0%		23.4%	28.7%	
Other income—recurring	1,164	1,194	-2%	313	514	-39%
Other income-non recurring	124	223	-44%	124	223	-44%
Interest	239	520	-54%	231	41	462%
Depreciation	2,668	2,543	5%	706	771	-8%
Extraordinary items	2,131	1,609		1893	51	
PBT	19,686	16,195	22%	5,565	4,606	21%
Tax	4,917	3,877	27%	871	1,022	-15%
% tax rate	25%	24%		16	22	
PAT as reported	14,769	12,318	20%	4,695	3,584	31%
PBT (excl non recurring/extraordinaries)	17,431	14,363	21%	3,549	4,333	-18%
Tax on extraord/non-rec	4,539	3,424	33%	555	962	-42%
Adjusted PAT	12,892	10,939	18%	2,994	3,371	-11%
Total cement sales (m tonnes)	19.97	18.86	6%	5.02	4.92	2%
Net selling price per tonne (Rs)	3,380	2,966	14%	3,457	3,206	8%

Source: Company Reports, Citi Investment Research. Note – In the table above, we have excluded Rs382.9m of additional depreciation in CY07 provided due to a change in depreciation calculation method for some grinding units.

ACC

Company description

ACC is India's largest cement company with a capacity of 20m tpa and a market share of about 13% in FY06. This will be increased to around 27m tpa by CY09E. ACC is located in all the major markets but hardly exports any cement. Holcim holds a 43% stake in ACC (through its 78% subsidiary company Ambuja Cement India). Adding on the market presence of Holcim's other group company in India (Ambuja Cements) gives Holcim a total capacity of 36m tpa in India and a significant presence in several key markets. In the past few years, ACC has focused on cost-cutting, selling unviable cement capacity and exiting non-cement businesses. ACC has been a pioneer of blended cement and has the highest proportion of blended cement sales (83%) among the domestic cement majors.

Investment strategy

We rate ACC as Sell/Medium Risk (3M), with a target price of Rs790. Our rating is predicated on the lack of visibility on cement pricing upside, created partly by the uncertainties following the government measures in CY07. Although cement capacities have been delayed, we expect a steady stream of new supply in India in CY08E - making it difficult for producers to raise or maintain prices. Although imports of cement have commenced (from Pakistan), we do not expect a surge in the near future.

Valuation

We rate ACC on EV/EBITDA, a common metric used to value cement companies. Our target multiple is based on a 15% discount to the average EV/EBITDA of 9x of the past seven years, which we round down to 7.5x for CY08E - the lower end of its trading band over the past two years and equates to an EV/tonne valuation of US\$139. We use a discount to reflect our fear that profitability of cement companies will be impacted going forward on increased new cement capacities and cost pressures.

Risks

We rate ACC as Medium Risk based on our quantitative risk-rating system, which tracks 260-day historical share price volatility. The rating reflects the higher relative valuations of cement companies compared with both past cycles as well as regional peers. The main upside risks to our target price include: (1) further delays in industry capacity; (2) higher-than-expected domestic demand growth; and (3) changes in the duty/tax regime in favor of the producers.

Appendix A-1

Analyst Certification

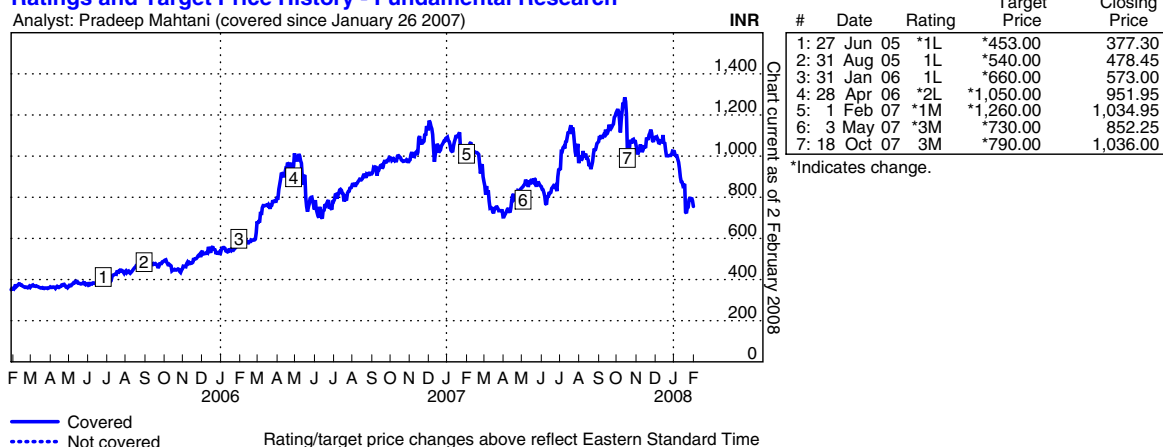
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Analyst: Pradeep Mahtani (covered since January 26 2007)



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