



Shree Cement

STOCK INFO.	BLOOMBERG
BSE SENSEX: 12,353	SRCM IN
S&P CNX: 3,559	REUTERS CODE
	SHCM.BO

11 October 2006

Buy

Previous Recommendation: Buy

Rs1,122

		YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
		END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
Equity Shares (m)	34.8	03/06A	6,677	303	8.7	5.9	129.0	11.1	10.3	9.2	6.4	19.6
52-Week Range	1,187/352	03/07E	13,010	3,284	94.3	983.8	11.9	6.9	76.1	52.2	3.3	7.2
1,6,12 Rel. Perf. (%)	12/0/96	03/08E	17,352	4,279	122.8	30.3	9.1	4.2	57.5	46.3	2.3	5.1
M.Cap. (Rs b)	39.1											
M.Cap. (US\$ b)	0.8											

- Shree Cement's 2QFY07 results were better than we had expected, with PAT growing 108% YoY against our estimate of 67% growth.
- Revenues grew 103% YoY to Rs3.2b, driven by volume growth of 44% to 1.11m ton (v/s our estimate of 1.07m ton) and realization growth of 41% to Rs2,849/ton (v/s our estimate of Rs2,614/ton). Shree Cement benefited from floods in Rajasthan, which impacted other cement manufacturers, but not its plant, resulting in higher volumes and realizations.
- Significant improvement in realization translated into EBITDA margin expansion of 11.6pp to 45.2% (up 80bp QoQ). EBITDA per ton almost doubled YoY to 1,287/ton (v/s Rs678/ton in 2QFY06). Margin expansion would have been higher but for cost inflation (up 17% YoY), led by RM cost (up 40%) and power & fuel cost (up 22%).
- Higher depreciation (up 176% YoY) due to new capacity and write-off of pre-operative expenses and higher tax provisioning (at 29.6% of PBT v/s zero tax in 2QFY06) restricted PAT growth to 108%. The company recorded a PAT of Rs778m for the quarter.
- We are upgrading our EPS estimate for FY07 by 10% to Rs94.3, to factor in better than expected 2QFY07 realizations. We maintain our FY08E EPS at Rs122.8. Better market mix (North) and timely capacity expansion would result in continued pricing pressure, with strong volume growth. The stock currently trades at 11.9x FY07E and 9.1x FY08E EPS and at US\$99/ton (on expanded capacity of 7.5m ton). We maintain **Buy**.

QUARTERLY PERFORMANCE

(Rs Million)

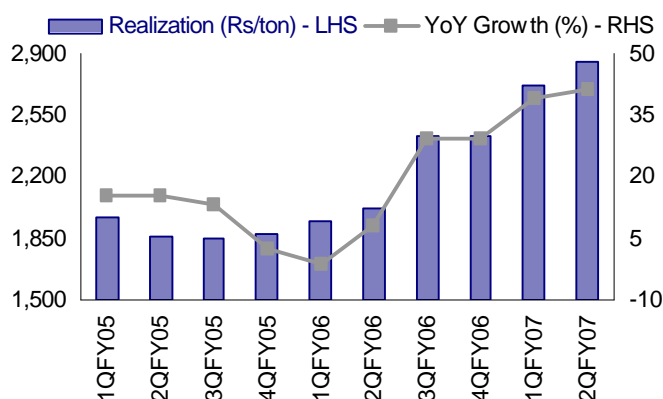
Y/E MARCH	FY06				FY07				FY06	FY07E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Sales Dispatches (m ton)	0.73	0.77	0.72	0.93	1.14	1.11	1.12	1.13	3.15	4.50
YoY Change (%)	1.0	2.1	-0.9	6.9	56.2	44.0	56.0	21.7	2.5	43.0
Realization (Rs/ton)	1,952	2,018	2,010	2,427	2,714	2,849	2,950	3,052	2,122	2,891
YoY Change (%)	-1.1	8.3	8.4	29.1	39.0	41.2	46.8	25.7	11.9	36.3
QoQ Change (%)	3.9	3.4	-0.4	20.8	11.8	5.0	3.5	3.5	0.6	-12.1
Net Sales	1,425	1,554	1,443	2,255	3,094	3,160	3,304	3,452	6,677	13,010
YoY Change (%)	-0.1	10.6	7.4	38.0	117.1	103.3	129.0	53.1	14.7	94.8
EBITDA	443	522	549	836	1,375	1,427	1,545	1,684	2,217	6,031
Margins (%)	31.1	33.6	38.0	37.1	44.4	45.2	46.8	48.8	0.3	0.5
Depreciation	123	123	123	207	263	338	316	326	1,852	1,244
Interest	39	33	33	23	54	27	75	82	128	238
Other Income	3	8	7	17	30	43	35	34	35	143
PBT	284	374	400	624	1,088	1,104	1,189	1,310	271	4,692
Tax	24	0	3	-3	184	326	422	240	29	1,173
Deferred Tax	0	0	0	0	0	0	0	235	59	235
Rate (%)	8.4	0.0	0.8	-0.5	16.9	29.6	35.5	36.2	32.2	30.0
Reported PAT	260	374	397	628	904	778	767	835	184	3,284
Adj PAT	260	374	397	607	904	778	767	835	184	3,284
YoY Change (%)	0.3	119.8	140.6	112.4	247.6	108.2	93.4	37.6	-48.0	1,684.5
Margins (%)	18.2	24.0	27.5	26.9	29.2	24.6	23.2	24.2	2.8	25.2

E:MOSt Estimates; Quarterly results do not add up with full year results as it provides addl. depreciation and deferred tax at the end of the year

Revenue growth driven by firm cement prices and new capacity

Revenues grew by 103% to Rs3.2b, driven by volume growth of 44% to 1.11m ton (v/s estimate of 1.07m ton) and realization growth of 41% to Rs2,849/ton (v/s estimate of Rs2,614/ton).

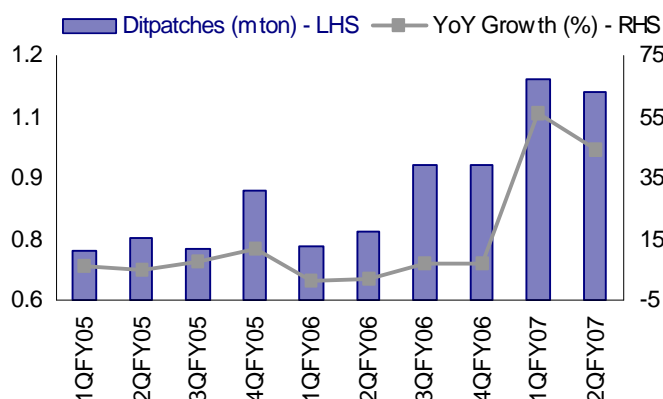
TREND IN REALIZATIONS



Source: Company/Motilal Oswal Securities

Volume growth was supported by commissioning of new capacity, whereas realizations also improved sequentially (up by Rs135/ton) despite monsoon. Shree Cement benefited out of floods in Rajasthan, which impacted other cement manufacturers, but not its plant, resulting in higher volumes and realizations.

TREND IN DISPATCHES



Source: Company/Motilal Oswal Securities

Margins boosted by strong growth in realization

Significant improvement in realization translated into EBITDA margin expansion of 11.6pp to 45.2% (up 80bp QoQ). EBITDA per ton almost doubled YoY to 1,287/ton (v/s Rs678/ton in 2QFY06). EBITDA grew by 173% YoY and 4% QoQ to Rs1.4b. Margin expansion would have been higher but for cost inflation (up 17% YoY) led by RM cost (up 40%) due to higher fly-ash blending and power & fuel cost (up 22%) due to 20% increase in pet coke prices. However, the company managed to reduce its freight cost on QoQ basis (down by 8%) by higher rail usage due to availability of wagons due to lean season.

PER TON ANALYSIS (RS/TON)

	2QFY07	2QFY06	YOY (%)	1QFY07	QOQ(%)
Net Realization	2,849	2,018	41.2	2,714	5.0
Raw Material Cost	335	240	39.8	359	-6.5
Staff Cost	106	97	8.6	100	5.9
Power & Fuel	482	395	21.9	414	16.5
Freight & Selling Exp	350	346	1.0	380	-8.0
Other Exp	290	261	10.9	255	13.5
Total Exp	1,563	1,340	16.6	1,508	3.6
EBITDA	1,287	678	89.8	1,206	6.7
EBITDA Margin (%)	45.2	33.6		44.4	

Source: Company/ Motilal Oswal Securities

Higher depreciation (up 176% YoY) due to new capacity and write-off of pre-operative expenses and higher tax provisioning (at 29.6% of PBT v/s zero tax in 2QFY06) restricted PAT growth to 108%. The company registered PAT of Rs778m for the quarter. Going forward, we expect interest cost to be higher, as during the quarter the company benefited out of interest rate derivative. Also, tax rate is expected to be higher, with full year tax rate of around 30% (including deferred tax).

Expansion plan to increase capacity to 9.1m ton

The company is undertaking major capacity expansion, which will increase its capacity from current 4.5m ton to 9m ton by the end of FY08, thereby enabling it to significantly grow volumes. Shree Cement would be incurring capex of Rs7b for these capacity additions and a 38 MW captive power plant.

Upgrading EPS to factor in higher than expected 2QFY07 realizations

We are upgrading our FY07E EPS by 10% to Rs94.3, to factor in better than expected 2QFY07 realizations. We have raised our realization estimates for 3QFY07 by Rs16.8/bag (which is higher by Rs5/bag QoQ) and by Rs6.8/bag for 4QFY07 (higher by Rs5/bag QoQ). However, we maintain our FY08E EPS at Rs122.8.

REVISED FORECAST (RS M)

	FY07E		
	REV	OLD	CHG (%)
Net Sales	13,010	12,093	7.6
Net Profit	3,284	2,976	10.4
EPS (Rs)	94.3	85.4	10.4

Source: Motilal Oswal Securities

Valuation and view

The Northern and Central regions are going through cyclical upturn and witnessing short-term deficits. Shree Cement, with its 86% of its sales coming from North India, is suitably placed to benefit from the upturn in the cement cycle. Its operating cost is one of the lowest in the industry, and higher volumes and realizations would have a multiplier effect on its earnings. Better market mix (North) and timely capacity expansion would result in continued pricing pressure with strong volume growth. The stock currently quotes at 11.9x FY07E and 9.1x FY08E EPS and at asset valuation of US\$99/ton (on expanded capacity of 9m ton). We have raised our target price to Rs1,350 (~11x FY08E EPS) in line with our earnings upgrade. We maintain **Buy**.

Shree Cement: an investment profile

Company description

Shree Cements the largest single-location integrated cement plant in Northern India with an installed capacity of 4.5 ton. It is strategically located in central Rajasthan from where it can cater to the entire Rajasthan market as well as Delhi and Haryana with economic logistics cost. It is a significant player in Rajasthan (28.3% of volumes), Haryana (22.6% of volumes), Delhi (21.9% of volumes) and Punjab (12.6% of volumes). Over the years, it has established a reputation as one of the world's most efficient cement manufacturers.

Key investment arguments

- ✍ One of the most cost efficient cement producers in the country.
- ✍ Highest volume growth for next three years.
- ✍ Best positioned geographically (86% volumes from North and 14% from Central India) to benefit from current tightening of demand-supply and consequent upturn in cement prices.

Key investment risks

- ✍ Being a single location plant, it is heavily dependent on the Northern region; any downturn in prices in the Northern market would adversely impact its profitability.
- ✍ Increase in pet coke prices would impact profitability, as it uses pet coke as feedstock for captive power plant as well as to fire kiln.

Valuation and view

- ✍ The stock quotes at 9.1 x FY08E EPS and 6.1x EV/EBITDA FY08E, and US\$99/ton (on expanded capacity of 9m ton in FY08E) on asset valuation basis.
- ✍ We maintain **Buy** with a target price of Rs1,350 (~11x FY08E EPS).

Sector view

- ✍ Volume expected to grow by 8% driven by continuous momentum in housing and infrastructure projects.
- ✍ Improved demand supply dynamics due to limited capacity addition in previous years. However Greenfield capacity addition can disturb the tight demand supply scenario envisaged by us.

COMPARATIVE VALUATIONS

		SHREE CEMENT	BIRLA CORP.	CEMCO
P/E (x)	FY07E	11.9	10.2	14.2
	FY08E	9.1	9.5	13.0
P/BV (x)	FY07E	6.9	4.3	6.3
	FY08E	4.2	3.2	4.4
EV/Sales (x)	FY07E	3.3	1.8	2.6
	FY08E	2.3	1.7	2.4
EV/EBITDA (x)	FY07E	7.2	6.1	8.1
	FY08E	5.1	5.4	7.4

SHAREHOLDING PATTERN (%)

	JUN.06	MAR.06	JUN.05
Promoter	63.7	63.7	63.7
Domestic Inst	9.4	9.6	9.9
Foreign	15.0	15.3	15.1
Others	11.9	11.4	11.3

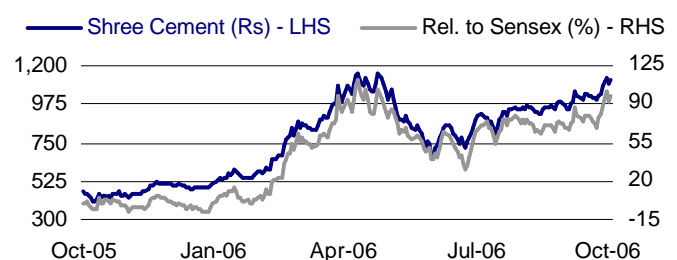
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY07	94.3	84.9	11.1
FY08	122.8	94.0	30.6

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
1,122	1,350	20.3	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT						RATIOS					
(Rs Million)											
Y/E MARCH	2005	2006	2007E	2008E	2009E	Y/E MARCH	2005	2006E	2007E	2008E	2009E
Gross Sales	7,026	7,961	14,846	19,800	23,250	Basic (Rs)					
Less: Excise Duty	1,205	1,284	1,836	2,448	3,060	EPS	8.2	8.7	94.3	122.8	125.7
Net Sales	5,821	6,677	13,010	17,352	20,190	Cash EPS	43.5	55.8	130.0	164.3	170.6
Change (%)	23.0	14.7	94.8	33.4	16.4	BV/Share	101.3	100.8	162.8	264.2	367.9
Total Expenditure	4,127	4,497	6,979	9,567	12,228	DPS	4.0	5.0	5.0	0.0	0.0
% of Sales	70.9	67.3	53.6	55.1	60.6	Payout (%)	54.7	107.9	17.5	17.5	17.5
EBITDA	1,694	2,180	6,031	7,785	7,962	Valuation (x)					
Margin (%)	29.1	32.7	46.4	44.9	39.4	P/E		129.0	11.9	9.1	8.9
Depreciation	1,230	1,640	1,244	1,444	1,562	Cash P/E		20.1	8.6	6.8	6.6
EBIT	464	540	4,787	6,341	6,400	P/BV		11.1	6.9	4.2	3.1
Int. and Finance Charges	198	128	238	454	549	EV/Sales		6.4	3.3	2.3	1.7
Other Income - Rec.	41	35	143	225	405	EV/EBITDA		19.6	7.2	5.1	4.4
PBT before EO Expense	307	447	4,692	6,112	6,256	EV/ton (US\$-Cap)		238	161	99	103
Extra Ordinary Expense/(Incom	-5	175	0	0	0	Dividend Yield (%)		0.4	0.4	0.0	0.0
PBT after EO Expense	311	271	4,692	6,112	6,256	Return Ratios (%)					
Tax	24	29	1,408	1,834	1,877	RoE	10.6	10.3	76.1	57.5	39.8
Tax Rate (%)	6.6	32.2	30.0	30.0	30.0	RoCE	8.5	9.2	52.2	46.3	37.9
Reported PAT	291	184	3,284	4,279	4,380	Working Capital Ratios					
PAT Adj for EO items	286	303	3,284	4,279	4,380	Asset Turnover (x)	0.8	0.8	1.0	1.0	0.9
Change (%)	-3.6	5.9	983.8	30.3	2.4	Debtor (Days)	12	8	7	9	11
Net Profit	286	303	3,284	4,279	4,380	Inventory (Days)	46	62	55	55	55
						Working Capital Turnover (Day	49	35	114	185	256
BALANCE SHEET	(Rs Million)										
Y/E MARCH	2005	2006E	2007E	2008E	2009E	Leverage Ratio (x)					
Equity Share Capital	348	348	348	348	348	Debt/Equity	1.0	1.3	1.2	0.8	0.5
Total Reserves	3,181	3,162	5,871	9,401	13,014	CASH FLOW STATEMENT	(Rs Million)				
Net Worth	3,529	3,510	6,219	9,749	13,362	Y/E MARCH	2005	2006E	2007E	2008E	2009E
Deferred Liabilities	631	690	924	1,230	1,543	Oper. Profit/(Loss) before Tax	1,694	2,180	6,031	7,785	7,962
Total Loans	2,971	3,727	6,540	6,980	6,900	Interest/Dividends Recd.	41	35	143	225	405
Capital Employed	7,131	7,927	13,684	17,959	21,805	Direct Taxes Paid	-21	-87	-1,408	-1,834	-1,877
Gross Block	9,875	12,932	15,500	17,500	18,000	(Inc)/Dec in WC	541	189	-1,315	-629	-443
Less: Accum. Deprn.	5,043	6,632	7,876	9,319	10,881	CF from Operations	2,255	2,317	3,451	5,547	6,048
Net Fixed Assets	4,832	6,300	7,624	8,181	7,119	(inc)/dec in FA	-1,322	-2,739	-3,591	-1,000	0
Capital WIP	1,522	978	2,000	1,000	500	CF from investments	-1,314	-2,739	-3,591	-1,000	0
Curr. Assets	1,517	2,182	5,588	10,925	16,721	(Inc)/Dec in Debt	-527	815	3,047	746	233
Inventory	726	1,129	1,960	2,615	3,042	Interest Paid	-198	-128	-238	-454	-549
Account Receivables	239	183	273	508	678	Dividend Paid	-159	-199	-575	-749	-766
Cash and Bank Balance	130	191	2,286	6,376	11,341	CF from Fin. Activity	-886	483	2,235	-457	-1,083
Others	421	679	1,069	1,426	1,659	Inc/Dec of Cash	54	60	2,095	4,090	4,965
Curr. Liability & Prov.	739	1,532	1,529	2,147	2,535	Add: Beginning Balance	76	130	191	2,286	6,376
Account Payables	502	1,273	953	1,396	1,767	Closing Balance	130	191	2,286	6,376	11,341
Provisions	237	260	576	750	768						
Net Current Assets	778	649	4,059	8,778	14,186						
Appl. of Funds	7,131	7,927	13,684	17,959	21,805						

E: MOST Estimates

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1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No

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