ULTRATECH CEMENT

ANNUAL REPORT ANALYSIS FY2019

Cement Industry Overview

The Indian cement industry witnessed another good year of favourable demand. During FY19, industry achieved a double digit volume growth, of 13%, last witnessed in FY10. Demand from infrastructure is witnessing growth backed by Government's thrust on infrastructure development viz. construction of roads, metro rail projects, airports renovation, etc. Capacity utilisation for the industry improved to 71%, about 5% higher over FY18. This is expected to improve further on likely sustained demand growth.

Acquisition of BCL adds greatly to capacity, large investments planned

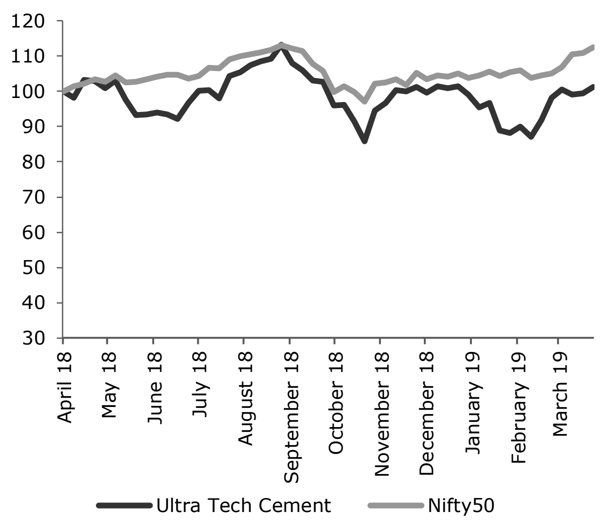
ULTRACEMCO acquired Binani Cement Limited (BCL) and renamed it to UltraTech Nathdwara Cement Limited. Plants of BCL are ready to operate in line with the existing plants of the Company after a successful consolidation. The Company seems to be on track to gain market share from competition after its consolidation. This should provide the Company with increased pricing power, which in turn is expected to boost its margins.
Further, the Company plans to spend Rs. 20 billion in FY20 related to remaining work at Bara, WHRS projects, development of the coal block at Bicharpur, packaging terminal at Mumbai, wall-care putty projects and other normal maintenance CapEx.

Strong top-line growth, but realizations yet to catch-up

Top-line grew by 22% from Rs. 293.6 billion in FY18 to Rs. 357 billion in FY19. EBITDA has grown by approximately 11% during the period, to reach Rs. 65.2 billion. The Company achieved a PBT of Rs. 35.6 billion, which grew by more than 7% as compared to the previous year. Finance cost has increased by 19% to Rs. 14.2 billion, reflecting a full year impact of the acquisition and additional debt taken during the year for the acquisition of BCL. CapEx was Rs. 15.3 billion, owing mainly to the several expansion and modernisation schemes undertaken by the management. Pushed by a rise in energy cost, company is taking initiatives to curb the impact by increasing the usage of renewable energy, procuring solar power, etc. Increase in diesel prices led to an increase in logistics cost but was partially negated with optimisation of lead distance.
Valuations are not cheap and what remains to be seen is whether the Company is able to perform as per the expectations riding on it for a successful consoldation and deriving of synergies from the acquisition. The risks faced include steadily rising debt levels that would need to be trimmed down to boost return ratios. Investors should accumulate this scrip on every dip.

ULTRATECH CEMENT LTD.	
BSE CODE	532538
NSE CODE	ULTRACEMCO
CMP as on 17 Oct 2019 (Rs.)	4284.3
Face value (Rs.)	10.0
Mkt. cap (Rs. billion)	447.1
52-week H (Rs.)	4,903.9
52-week L (Rs.)	3,263.7
Target	
% Upside	

ULTRACEMCO Relative to NIFTY



What's New

Acquisitions:

Binani Cement Limited (BCL) became a wholly-owned subsidiary w.e.f. 20 November, 2018. The name was subsequently changed to Ultratech Nathdwara Cement Limited (UNCL). The acquisition provides the company access to large reserves of high quality limestone and is generating incremental earnings, which are growing exponentially each month.

Demergers:

The BOD has approved a Scheme of Demerger amongst Century Textiles and Industries Limited, Ultratech and their respective shareholders and creditors. This Scheme has received the approval from the stock exchanges, the Competition Commission of India and the shareholders, and is now awaiting approval of the NCLT. Century will demerge its cement business into the company. Upon completion of the acquisition of Century's cement assets, the total capacity will reach 113.35 MTPA.

Environmental Initiatives:

Various initiatives have been taken to protect the environment –

- The company is trying to reduce the consumption of fossil fuels by substituting it with the wastes of other industries.
- It is increasing the use of renewable energy as a part of its energy mix.
- The company is exploring further opportunities for the purchase of green power as well as investment in solar and wind generation.
- It has set a target to reduce its CO_2 intensity by 25% in FY21, as compared to FY06.

Capacity Timeline

FY16

Greenfield capacity of 4.5 MTPA and commissioning of cement grinding plants at Jhajjar in Haryana and Dankuni in West Bengal.

FY17

1.6 MTPA capacity added following the commissioning of the grinding unit Patliputra, Bihar.

FY18

Acquisition of the cement plants of JAL and JCCL, having a cement capacity of 21.2 MTPA, including a 4 MTPA capacity plant which was under installation.

FY19

Commissioning of a greenfield cement capacity of 3.50 MTPA in Manavar, Madhya Pradesh.

Key Takeaways from the MD&A

INDUSTRY OVERVIEW:

- Cement industry achieved a double-digit volume growth, last witnessed in FY10.
- Volume growth of 13% achieved this year is in continuation of the 9% growth in FY18.
- New Capacity Addition – 12 MTPA
  Capacity Utilization – 71% (5% higher than FY18)

PRODUCTION & CAPACITY UTILIZATION:

- Total capacity at the end of FY18 – 85 MTPA
- Commissioned a greenfield cement capacity at Manavar, Madhya Pradesh - 3.5 MTPA
- Capacity of BCL acquired – 6.25 MTPA Capacity of subsidiary Star Cement – 4 MTPA
- Total capacity at the end of FY19 – 98.8 MTPA
- Cement production increased by 17% from 57.2 million tonnes to 67.2 million tonnes
- Capacity Utilization – 76% (5% higher than the industry)

DIVIDENDS & EMPLOYEE STOCK OPTION SCHEMES:

- The Board recommended a dividend of Rs. 11.5 per share as against Rs. 10.5 per share in FY18, resulting in a cash outgo of Rs. 3.8 billion as against Rs. 3.5 billion in FY18.
- The Board based on the recommendation of the NRC Committee, approved formulation of a new scheme viz. 'UltraTech Cement Limited Employee Stock Option Scheme as per SEBI Regulations, 2014. The NRC Committee formulated ESOS–2018 on 18th December, 2018 and granted 158,304 Stock Options at an exercise price of Rs. 4009.30 per Stock Option exercisable into the same number of equity shares of Rs. 10 each and 43,718 RSUs at an exercise price of Rs. 10 each.

RESEARCH & DEVELOPMENT:

- The R&D team has developed new products like low clinker composite cement, red mud-based cement, crack resisting cement, water repelling cement, masonry cement, a series of ultra-lightweight concrete as per ISO standards, a series of high impact resistance concrete for special applications and a series of cement grinding aids and concrete admixtures.
- It has also developed and patented the following products: water positive cement, fire resisting cement and concrete, rapid hardening 3D printable mortar and concrete and red mud-based cementitious material.

HUMAN RESOURCES & SAFETY:

- Number of employees in FY19 were 19,557 as against 19,681 employees in FY18.
- In addition to the existing 7 safety sub-committees, 2 more project safety and mines safety sub-committees have been constituted and regular review is conducted to track progress of defined key performance indicators of these sub-committees.
- Theme-based safety campaigns have been introduced across the organization to further improve awareness amongst all employees about various elements of safety.

Key Takeaways from the MD&A

KEY BUSINESS RISKS IDENTIFIED:

- Economic Environment and Market Demand – Economic slowdown and subdued infrastructural development might lead to low cement demand in the country.
- Inflation and Cost of Production – Company faces the risk of inflationary nature and market-driven cost of coal, pet coke, power and other fuel.
- Accounting Risks - Changing laws, rules, regulations and standards relating to accounting, corporate governance, public disclosure and listing regulations are generating newer and unforeseen risks for the company.
- Environment and Sustainability - The risks associated with environmental pollution through the discharge of waste causing damages to the fragile surrounding environment is a legal offence.
- Talent Management – The risks in talent management are mitigated by following a policy of being an employer of choice and inculcating a sense of belonging.

SIGNIFICANT & MATERIAL ORDERS PASSED BY REGULATORS

- Upon the NCLAT disallowing its appeal against the CCI order dated 31st August, 2016, the Hon'ble Supreme Court has, by its order dated 5th October, 2018, granted a stay against the NCLAT order. Consequently, the Company has deposited an amount equivalent to 10% of the penalty amount.

AWARDS & RECOGNITIONS:

Some of the prestigious awards and recognition conferred on the Company during the year comprise of:

- Golden Peacock National Quality Award: Aditya Cement Works;
- Gold Medal for 'National Awards for Manufacturing Competitiveness (NAMC) 2015-16' in Building Material & Cement Sector: Aditya Cement Works;
- National Energy Conservation Awards-2017 (TPP - Certificate of Merit): Andhra Pradesh Cement Works;
- 14th National Award for Excellence in Energy Management Conducted by Confederation of Indian Industry: Dalla Cement Works;
- National Energy Conservation Award (Thermal Power Plant): Kotputli Cement Works.

SUSTAINABILITY:

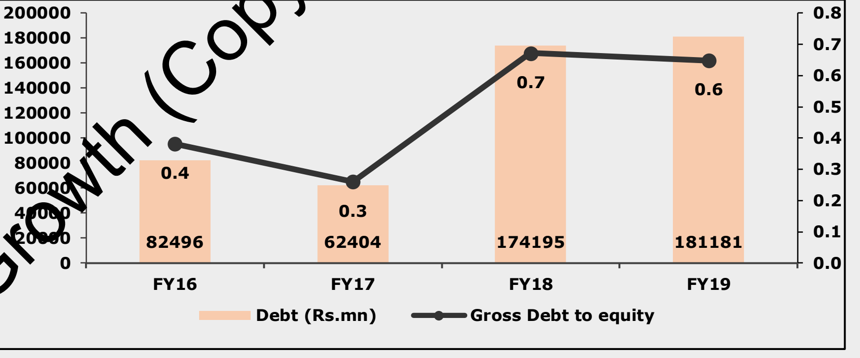
- In order to enhance its environment conservation measures, Ultratech continues to be sensitive towards societal wellbeing and has been consistently adopting new technologies that are cleaner and greener.
- Its plants and processes are constantly driven to become more energy efficient. With its thrust on the use of alternative fuels, the company has been relentlessly striving to reduce consumption of fossil fuels by substituting these with wastes from other industries.
- These efforts have resulted in around 3% of the company's fuel requirements being met through the use of alternative fuels.
- It is currently exploring further opportunities for purchase of green power as well as investment in solar and wind generation.
- During this year, Ultratech cut its CO_2 intensity by 18.65% compared to FY06. In energy efficiency, it has overachieved the target set by the Government of India for the first Perform, Achieve and Trade ("PAT") cycle.

Financial Analysis

Borrowings

During the year, ULTRACEMCO raised Rs. 53.6 million for the refinancing of loans availed/transferred for the acquisition of Jaiprakash Associates Limited and Jaypee Cement Corporation Limited's cement capacity. It also raised Rs. 15 billion, which is placed with UltraTech Nathdwara Cement Limited ("UNCL") as intercorporate deposits for repayment of financial and operational creditors. ULTRACEMCO availed Rs. 2.45 billion as interest free loan under an incentive scheme of a State government and repaid the existing long-term borrowings of Rs. 8.84 billion in line with the agreed repayment schedule. Total debt stands at Rs. 181.18 billion.

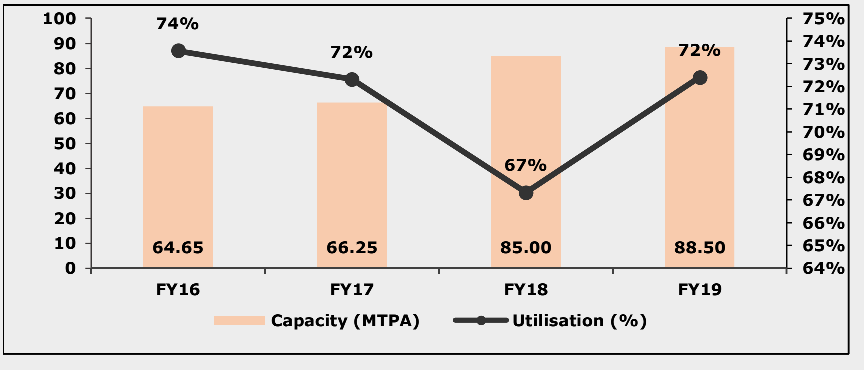
The Debt to Equity Ratio has improved by more than 16% from 0.7 to 0.6.



Source: Company, Leveraged Growth

Increases in Capacity & Utilisation

The total capacity increased from 85.00 MTPA to 88.50 MTPA due to the commissioning of a greenfield cement capacity of 3.50 MTPA at Manavar, Madhya Pradesh. Capacity utilisation improved by 5% on a Y-o-Y basis to 72% on an expanded capacity base. Acquisition of UNCL, was successfully completed, having an installed capacity of 6.25 MTPA in India. Total cement capacity has enhanced to 94.75 MTPA in India and along with its other subsidiary Star Cement, the total capacity of the Company stands at 98.75 MTPA.

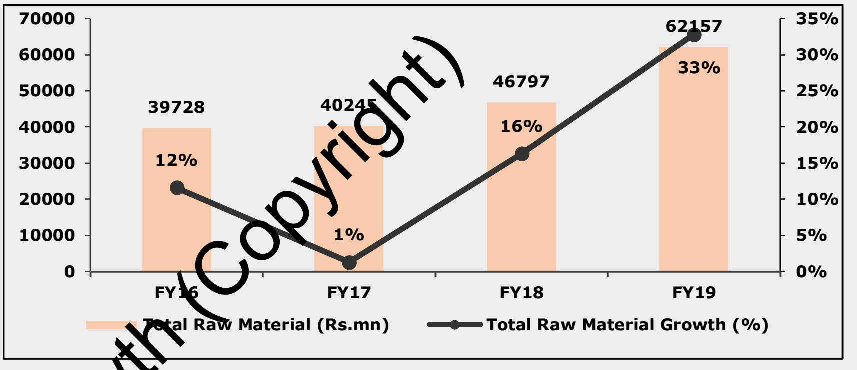


Source: Company, Leveraged Growth

Financial Analysis

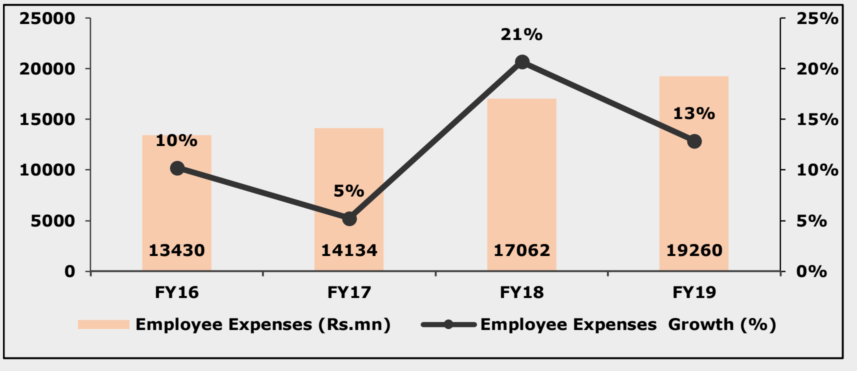
Expenses

Total raw material cost increased by 33% on a Y-o-Y basis due to an increase in slag, iron ore, aluminous clay and fly-ash prices and additional limestone on the transfer of lime stone mines in ULTRACEMCO's name.



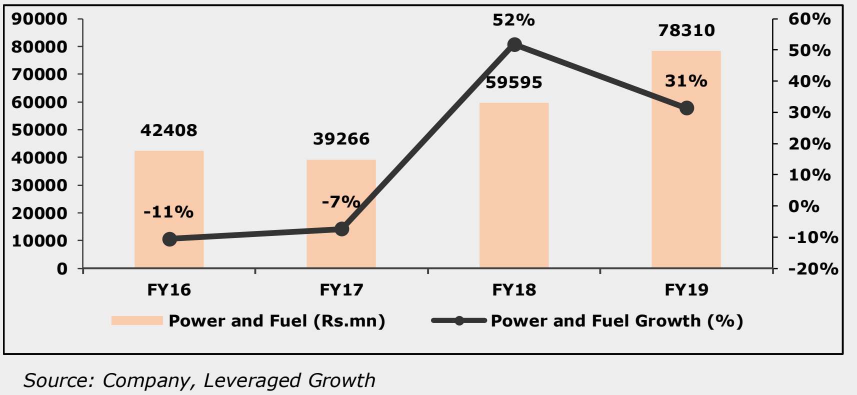
Source: Company, Leveraged Growth

Employee benefit expenses increased by 13% on a Y-o-Y basis due to annual increments, commissioning of new plants and a full year impact of the cost of employees from the acquisition in June, 2017.



Source: Company, Leveraged Growth

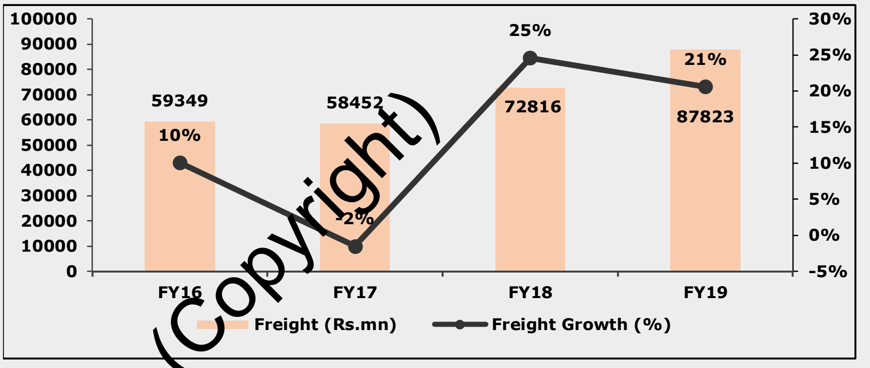
Power and fuel costs increased by 31% on a Y-o-Y basis due to an increase in energy costs by 14%, attributable to an increase in pet coke and coal prices. Imported pet coke prices rose 6% from USD 96 per tonne to USD 102 per tonne coupled with the impact of a currency depreciation of 8% over the previous year and a full year impact of a hike in import duty on pet coke from 2.5% to 10%, w.e.f. December, 2017.



Source: Company, Leveraged Growth

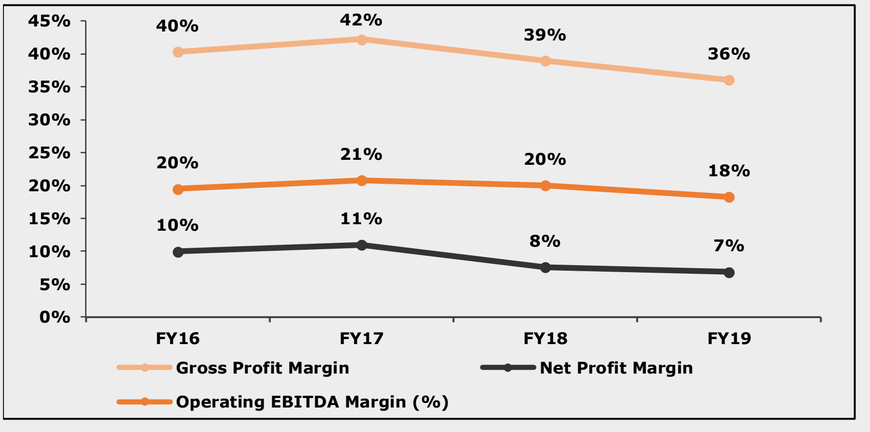
Financial Analysis

Freight and forward expenses increased by 21% on a Y-o-Y basis due to an increase in diesel prices.



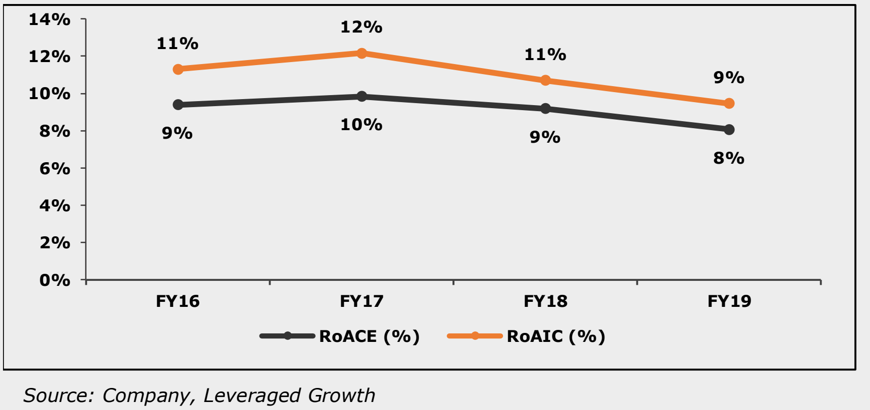
Source: Company, Leveraged Growth

Margins
Net Profit Margin declined slightly by 1%. Operating EBITDA Margin declined to 18% from 20% in FY18. Gross Profit Margin declined by 3% on a Y-o-Y basis.



Source: Company, Leveraged Growth

Return Metrics
ROE declined slightly by 60 bps to 9% in FY19. RoACE declined from 9% to 8% in FY19. RoAIC declined by 200 bps to 9% in FY19.

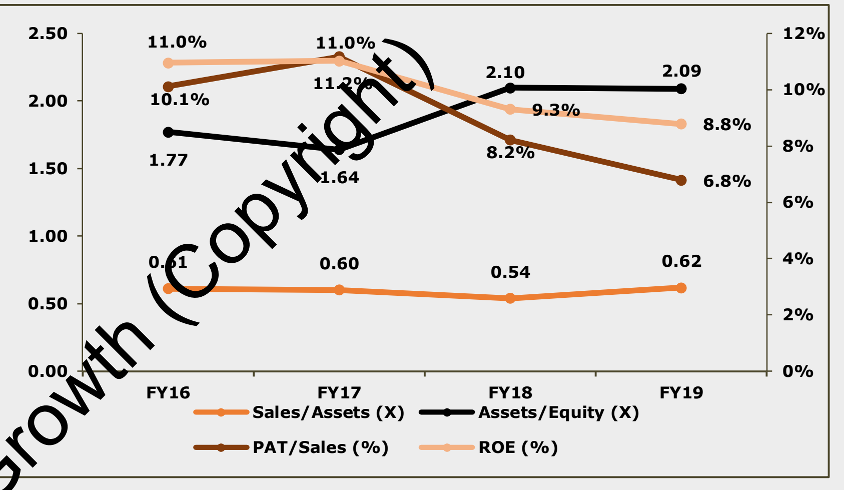


Source: Company, Leveraged Growth

Financial Analysis

DuPont Analysis

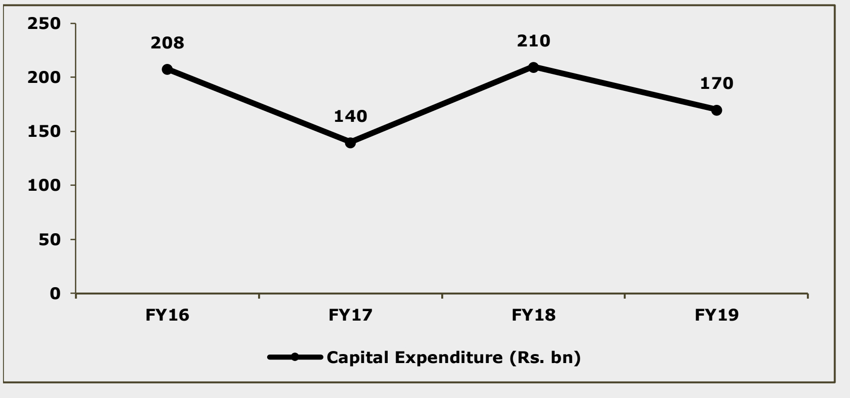
DuPont gave a more insightful analysis for declining RoE. The major source of the drag-down on the ratio was the Net Profit Margin as Asset Turnover and Financial Leverage was largely stable.



Source: Company, Leveraged Growth

Capital Expenditure

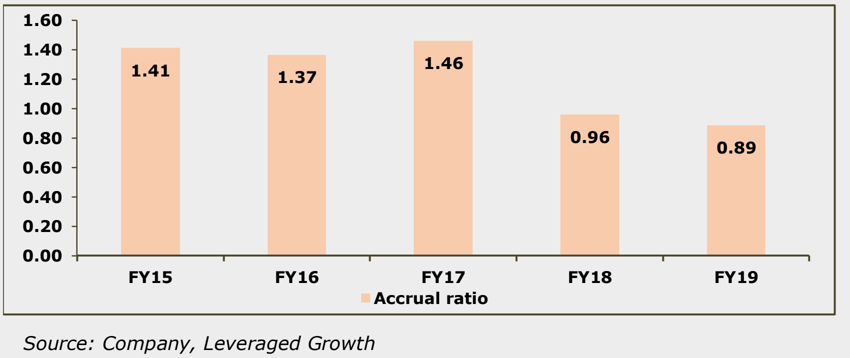
Capex for the year was Rs. 170 billion. Investments were made primarily for the completion of work on the green field plant in Manavar, for the Bara Grinding unit expected to be commissioned by Q2 FY20, for the Waste Heat Recovery Systems (WHRS) and for other modernisation capex schemes.



Source: Company, Leveraged Growth

Accrual Ratio

Cash Flow from Operations for the year was Rs. 39824.5 million and EBITDA after tax was Rs. 44950.74. The Accrual Ratio has decreased from 0.96 in FY18 to 0.89 in FY19.



Source: Company, Leveraged Growth

Quality of Earnings

- The Company capitalized R&D Expenditure up to Rs. 99.2 mn. This was 0.0274% of Net Sales, largely considered immaterial.
- Gross Block for the year is Rs. 433.6 bn whereas CWIP is only Rs. 10.7 bn. This makes CWIP 2.48% of the Gross Block, rendering it immaterial.
- Excess Provision for Bad Debts written back was Rs. 6.6 mn. Provision created for Doubtful Debts during the year was Rs. 101.1 mn, bringing the Closing Provision to Rs. 51.53, which is only 2.45% of Total Trade Receivables.
- Current Tax Payment amounted to Rs. 7.4 bn whereas Cash Tax Payment amounted to Rs. 7.0 bn in FY19, resulting in a difference of Rs. 357.5 mn due to non-cash items like depreciation, provisions, etc. Current Tax increased from Rs. 7.1 bn FY18 to Rs. 7.4 bn in FY19, while Deferred Tax decreased from Rs. 3.9 bn to Rs. 3.7 bn. Cash Tax Paid decreased from Rs. 8.4 bn in FY18 to Rs. 7.0 bn in FY19.
- The Company has Contingent Liabilities of Rs. 34.7 bn and Capital Commitments of Rs. 10.9 bn.
- The Supreme Court of India has allowed an appeal filed by the State of Rajasthan in a matter relating to transfer of mining lease in the name of the Company's wholly-owned subsidiary, Gotan Lime Stone Khanij Udyog Private Limited (GKUPL) and has directed the State to frame and notify its policy relating to transfer of mining lease and thereafter pass appropriate order in respect of the mining lease of GKUPL. State Government has notified the new policy related to transfer of new mining lease, based on which the Company has requested the State Government to consider reinstatement of the mines in its favour.
- During the year the Board approved a Scheme of Arrangement amongst Century Textiles and Industries Limited, the Company and their respective shareholders and creditors. In terms of the Scheme, Century will de-merge its cement business into the Company. Century's cement business consists of 3 integrated cement units in Madhya Pradesh, Chhattisgarh and Maharashtra with a total capacity of 12.6 MPTA and a grinding unit in West Bengal of 2.0 MTPA.
- Upon effectiveness of the Scheme, equity shares of the Company shall be issued to shareholders of Century, in the ratio of 1 equity share (face value Rs. 10/- each) for every 8 equity shares of Century. The Scheme has received approval of the stock exchanges, the Competition Commission of India and the shareholders of the Company and is now awaiting the approval of the National Company Law Tribunal and other regulatory authorities, as may be required.
- NCLAT by its order dated November 14, 2018, approved the Company's Resolution Plan for acquiring Binani Cement Limited (BCL) under the provisions of the IBC 2016.
    - UNCL has a capacity of 6.25 MTPA in the State of Rajasthan comprising an integrated cement unit with capacity of 4.85 MTPA and a split grinding unit with capacity of 1.4 MTPA. In addition, UNCL has investments in subsidiaries in China and UAE.
    - This acquisition will create value for shareholders as the acquisition adds 1/3rd additional ready to use capacity in the high-growth North market where the Company was already at high capacity utilisation levels so as to cater to the growing market. This acquisition also provides abundant additional limestone reserves sufficient to cater to even additional capacities at lower prices compared to auctioned prices and creates synergies in logistics and procurement which offers many advantages to the Company.
    - Consequent to the acquisition, the Holding Company subscribed to equity share capital of Rs. 15 bn and 8.75% preference share capital of Rs. 19 bn of UNCL, and provided an inter-corporate loan of Rs. 18 bn to UNCL. Further, UNCL obtained a loan (non-current borrowing) of Rs. 27 bn (pursuant to a corporate guarantee provided by the Holding Company). Subsequently, the group paid to financial and operational creditors as per the RP.

Quality of Earnings

- Loans and advances to related parties as at March 31st, 2019 was Rs. 18.8 bn, an increase of 215.8% Y-O-Y from Rs. 86.6 mn.
- The Company has invested in three companies, which have a business different from the company's own line of business. Investments in Aditya Birla Renewables SPV 1 Limited as at March 31, 2019 were Rs. 108.5 million as compared to Rs. 35.2 million last year. Investments in Green Infra Wind Power as at March 31, 2019 was Rs. 1.2 million as compared to Rs. 1.4 million last year. The company invested Rs. 2.4 million as at March 31, 2019 for the first time in Watsun Infrabuild Private Limited. Amongst the three, Aditya Birla Renewables SPV 1 Limited is an associate company.
- Dividend and Interest Income received from related parties was Rs.845.4 million in FY19 compared to Rs. 136.8 million in FY18.
- Sales of goods to related parties for FY19 was Rs. 5.2 bn and the total revenue was Rs. 361.7 bn. Therefore, 1.428% of revenue was from related parties and this is immaterial.
- Purchase of goods from related parties for FY19 was Rs. 4.8 bn and the total revenue was Rs. 361.8 bn. Therefore, the Company incurred expenses up to 1.32% of revenue from related parties and this is immaterial.

ConCall Key Takeaways

Demand and Volumes

- While institutional demand is clearly rising in the country, the industry is still a retail market. Affordable housing projects have started gaining momentum in several towns alongside the low-income housing program in the rural markets.

Revenues

- Volumes growing at well above GDP as the Compnaany is currently in its up-cycle.
- For FY19, the Company's numbers show that the industry will show a growth of about 13%.
- Selling prices have seen an improvement in almost all the regions in the country driven by strong demand and improving regional capacity utilization

Capacity

- For FY19, the effective annual new capacity during the year was around 6 million tonnes.
- Having reached the 84%, 85% capacity utilization for Q4, the Company has enough supply capacity to meet the growing demand and improve return on capital.

Costs

- There is a program in place to deliver a cost reduction of close to Rs 50 per tonne at acquired plants, which should be delivered by FY20. It would leverage the advantage gained due to the dedicated freight corridor passing by very close to both the acquired plants. It is expected to improve dispatches dramatically.

Financial Statements

Income Statement (Rs.mn)			
	FY2018	**FY2019**	**FY2020E**
Net Sale	2,93,626	3,61,833	
Other Operating Income	4,275	5,268	
Total Income	2,93,579	3,57,035	
EBITDA	58,833	65,203	
EBIT	41,197	45,100	
PBT(Before Exceptional Items)	35,281	35,623	
PBT(After Exceptional Items)	33,018	35,623	
Reported PAT	22,313	24,557	
Adjusted PAT	24,111	24,557	

Balance Sheet (Rs.mn)			
ASSETS	**FY2018**	**FY2019**	**FY2020E**
Net Block (Property, Plant and Equipment)	3,72,108	3,72,954	
Capital Work-in-Progress	14,739	10,797	
Financial Assets:	23,472	56974	
Total Non-Current Assets	4,37,874	4,69,577	
Total Current Assets	1,05,856	1,14,787	
TOTAL ASSETS	**5,43,730**	**5,84,365**	
EQUITY			
Equity Share Capital	2,746	2,746	
Other Equity	2,56,484	2,76,731	
Net Worth	**2,59,231**	**2,79,477**	
LIABILITIES			
Total Non-Current Liabilities	1,72,240	1,86,255	
Total Current Liabilities	1,12,259	1,18,633	
TOTAL EQUITY AND LIABILITIES	**5,43,730**	**5,84,365**	

Cash Flow (Rs.mn)			
	FY2018	**FY2019**	**FY2020E**
Operating Profit before Working Cap Changes	59,780	69,917	
Cash generated from Operations	47,303	50,890	
Net Cash generated from Operating Activities (A)	38,874	39,825	
Net Cash generated from Investing Activities (B)	18,570	(27,468)	
Net Cash used in Financing Activities (C)	(57,302)	(6,781)	

Source: Company, Leveraged Growth