

# Shree Cement

BSE SENSEX	S&P CNX	CMP: INR2,237	TP: INR2,636	Buy						
16,739	5,049									
Bloomberg	SRCM IN									
Equity Shares (m)	34.8									
52-Wk Range (INR)	2,300/1,505									
1,6,12 Rel. Perf. (%)	-1/36/39									
M.Cap. (INR b)	77.9									
M.Cap. (USD b)	1.6									
Year	Net Sales	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/TON
End	(INR m)	(INR M)	(INR)	Gr. (%)	(X)	(X)	(%)	(%)	EBITDA	(US\$)
03/10A	36,321	10,168	291.9	55.0	7.7	4.3	66.8	31.9	5.3	138
03/11A	35,119	6,883	197.6	-32.3	11.3	3.9	36.0	6.5	9.2	128
03/12E	46,295	7,133	204.7	3.6	10.9	3.5	34.1	11.1	6.2	106
03/13E	54,748	7,585	217.7	6.3	10.3	2.8	30.6	21.2	4.9	98

Shree Cement's (SRCM) operating performance for 3QFY12 was better than expected. EBITDA was INR3.32b (v/s our estimate of INR3.22b), driven by strong cement business performance. However, higher depreciation restricted adjusted PAT to INR592m (v/s our estimate of INR983m).

- SRCM's 3QFY12 revenue grew 61% YoY (+47% QoQ) to INR12.6b (v/s our estimate of INR12.8b) and recurring PAT was INR592m (v/s our estimate of INR983m).
- EBITDA grew 111% YoY (~66% QoQ) to INR3.32b (v/s our estimate of INR3.22b), translating into EBITDA margin of 26.4% (v/s our estimate of 25.1%) - an improvement of 620bp YoY (+290bp QoQ). Higher depreciation was on account of commissioning of 150MW merchant power plant.
- Cement volumes grew 9% YoY (+15% QoQ) to 2.85m tons (v/s our estimate of 3m tons). Blended realization was higher by INR385/ton QoQ (+INR950/ton YoY) at INR3,797/ton (v/s our estimate of INR3,582/ton), driven by lower clinker sales and expansion into further markets. Cement EBITDA/ton at INR1,117 (v/s our estimate of INR935/ton) was higher by INR310/ton QoQ (+INR560/ton YoY).
- Merchant power volumes in 3QFY12 were ~392m units (including traded power) as against ~14m units in 2QFY12 (74m units in 3QFY11) and revenue was INR1.8b (v/s INR69m in 2QFY12 and INR335m in 3QFY11). EBITDA of merchant power business was ~INR144m (v/s our estimate of INR412m).

We have upgraded our earnings estimates by 3% for FY12 to INR204.7 and by 5% for FY13 to INR217.7, driven by better cement realization and profitability. The stock trades at 10.2x FY13E EPS, and at an EV of 4.9x EBITDA and USD98/ton (adjusting for merchant power assets of ~400MW). Maintain **Buy**.

Y/E March	Quarterly performance								(INR Million)	
	FY11				FY12				FY11	FY12E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Sales Dispatches (m ton)	2.49	2.28	2.62	2.88	2.69	2.49	2.85	3.12	10.21	11.14
YoY Change (%)	-2.4	-8.2	2.1	8.0	8.3	9.0	8.8	8.2	-0.4	9.2
Realization (Rs/ton)	3,272	3,010	2,851	3,299	3,405	3,412	3,797	3,853	3,132	3,632
YoY Change (%)	-5.9	-12.7	-11.0	-1.1	4.0	13.3	33.2	16.8	-7.1	16.0
QoQ Change (%)	-1.9	-8.0	-5.3	15.7	3.2	0.2	11.3	1.5		
Net Sales	9,445	7,176	7,796	10,701	10,340	8,546	12,586	14,823	35,119	46,295
YoY Change (%)	2.4	-20.2	-10.0	13.4	9.5	19.1	61.4	38.5	-3.3	31.8
EBITDA	2,895	1,427	1,575	2,959	2,591	2,004	3,324	4,145	8,856	12,190
Margins (%)	30.6	19.9	20.2	27.7	25.1	23.5	26.4	28.0	25.2	26.3
Depreciation	1,509	1,285	1,314	2,650	1,598	1,619	2,351	2,300	6,758	7,867
Interest	420	137	204	336	318	290	370	359	978	1,337
Other Income	287	255	19	25	1	24	18	26	468	70
PBT before EO Exp	1,253	260	77	-1	676	119	622	1,512	1,588	3,055
Extra-Ord Expense	9	75	59	343	83	-141	0	50	485	-8
PBT	1,244	185	18	-344	593	260	622	1,462	1,103	3,063
Tax	185	80	-257	-1,001	43	-125	30	358	-994	306
Rate (%)	14.9	43.0	-1,430.6	291.2	7.3	-47.9	4.9	24.5	-90.0	10.0
Reported PAT	1,059	105	275	657	550	385	592	1,105	2,097	2,757
Adj PAT	2,381	493	146	-2	627	177	592	1,142	3,018	2,750
YoY Change (%)	-19.2	-83.1	-91.3	-108.1	-73.7	-64.2	304.8	NA	-57.5	-8.9
Margins (%)	25.2	6.9	1.9	0.0	6.1	2.1	4.7	7.7	8.6	5.9

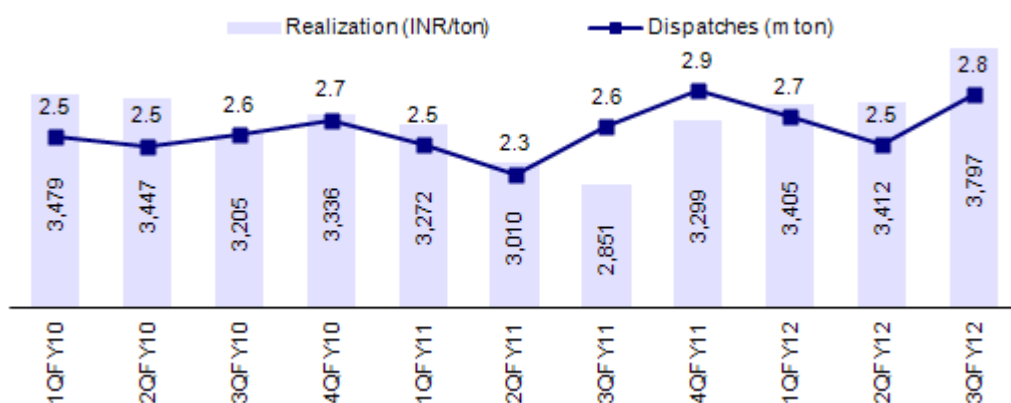
E:MOSL Estimates

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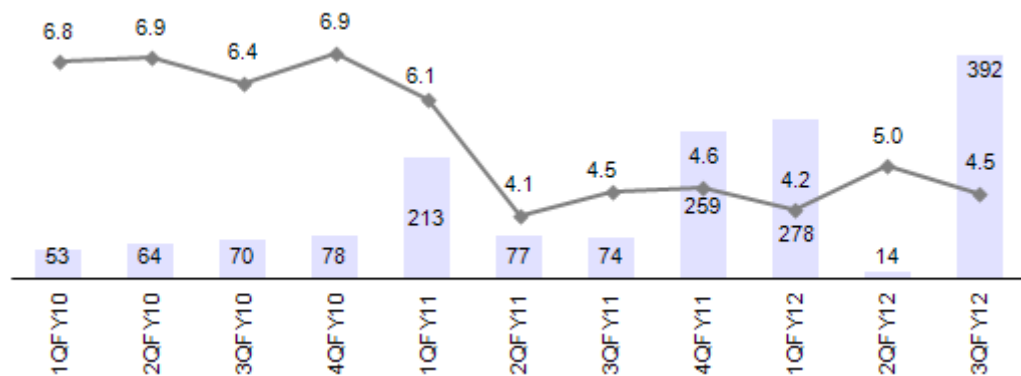
### Strong cement volumes and better product mix drive revenues; power volume picks-up

- Shree's 3QFY12 revenues grew by 61% YoY (+47% QoQ) to INR12.6b (v/s est INR12.8b).
- Cement volumes grew 9% YoY (+15% QoQ) to 2.85mt (v/s est 3mt).
- Blended cement realizations were higher by INR385/ton QoQ (+INR950/ton YoY) to INR3,797/ton (v/s est INR3,582/ton), driven by lower clinker sales and expanding to further markets. As a result, pure cement realizations were higher just by INR225/ton (v/s our est of INR170/ton improvement).
- Merchant power volumes in 3QFY12 was at ~392m units (inc traded power) as against ~14m units in 2QFY12 (v/s 74m unit in 3QFY11) and revenues of INR1.8b (v/s INR69m in 2QFY12 and INR335m in 3QFY11). EBITDA of merchant power business was ~INR144m (v/s est INR412m).

#### Trend in cement business volumes and realizations



#### Trend in merchant power business volumes and realizations



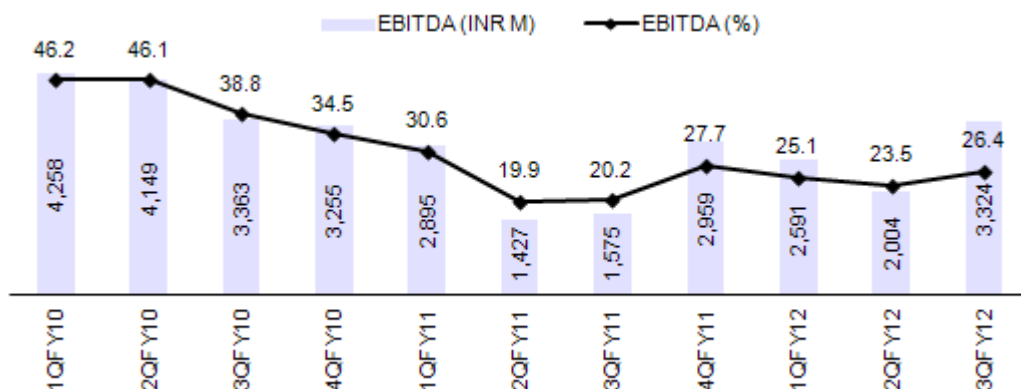
Source: Company/MOSL

### Better realizations boost profitability

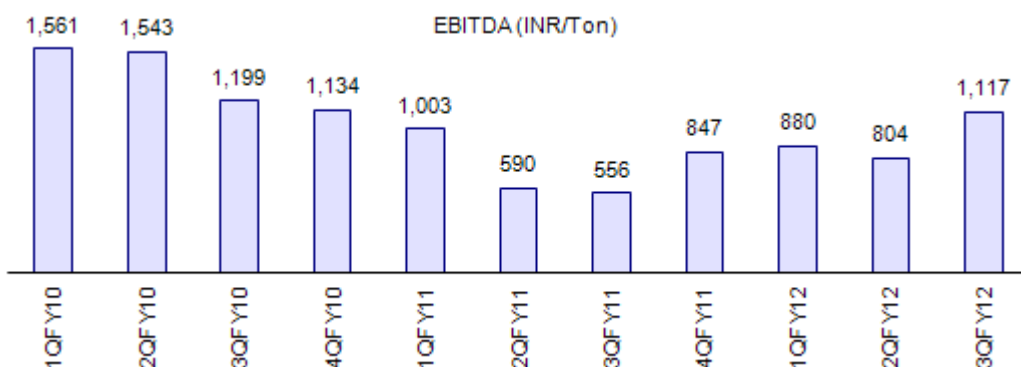
- EBITDA grew by 111% YoY (~66% QoQ) to INR3.32b, translating into EBITDA margins of 26.4% (v/s est 25.1%) - a improvement of 620bp YoY (+290bp QoQ). Higher depreciation was on account of commissioning of 150MW power plant. As a result, recurring PAT at INR592m (v/s est INR983m) grew 305% YoY (~235% QoQ).
- Cement EBITDA/ton at INR1,117/ton (v/s est INR935/ton) was higher by INR310/ton QoQ (+INR560/ton YoY). There was savings of INR110/ton QoQ on RM and energy cost, driven by lower pet-coke cost. However, freight cost was higher by ~INR160/ton QoQ impacted by adverse rail-road mix, increase in freight rates and lead distance.

- EBITDA of merchant power business was ~INR144m (v/s est INR412m), with EBITDA/unit of INR0.4/unit (v/s INR0.5/unit in 2QFY12 v/s INR1.6/unit in 3QFY11).

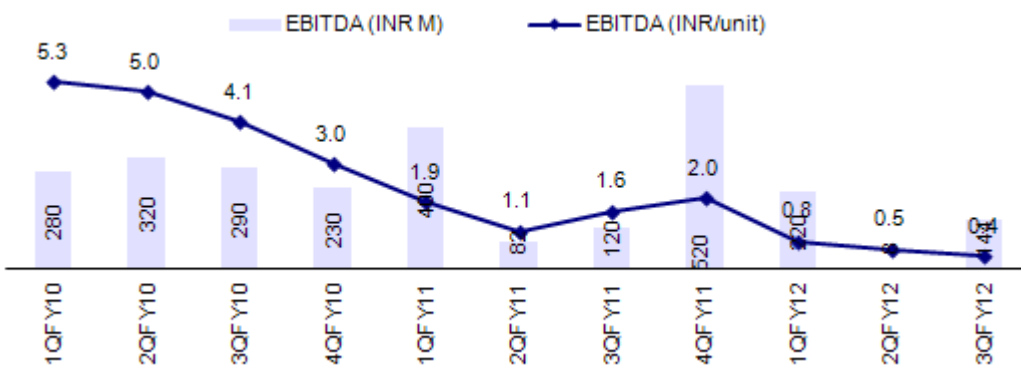
**Trend in EBITDA**



**Trend in cement EBITDA (INR/ton)**



**Trend in power EBITDA (INR/unit)**



**Cement business income statement (INR/ton)**

	3QFY12	3QFY11	YoY (%)	2QFY12	QoQ(%)
<b>Net Realization</b>	<b>3,797</b>	<b>2,851</b>	<b>33.2</b>	<b>3,405</b>	<b>11.5</b>
Raw Material Cost	549	337	63.1	480	14.4
Staff Cost	224	183	22.4	227	-1.4
Power & fuel	571	708	-19.4	660	-13.5
Freight & selling Exp	932	770	21.0	828	12.5
Other Exp	404	297	36.0	329	22.7
<b>Total Exp</b>	<b>2,680</b>	<b>2,295</b>	<b>16.8</b>	<b>2,524</b>	<b>6.2</b>
<b>EBITDA</b>	<b>1,117</b>	<b>556</b>	<b>100.8</b>	<b>880</b>	<b>26.8</b>
<b>EBITDA Margin (%)</b>	<b>29.4</b>	<b>19.5</b>		<b>25.9</b>	

Source: Company/MOSL

### Merchant power volumes to increase meaningfully, although outlook remains challenging

- It has commissioned 150MW, first phase of its 300MW merchant power plant in Sep-12. The second phase also commissioned operations in Jan-12.
- It has entered into contract to sell 225MW of power from October 2011 to June 2012 at INR4.2-4.5/unit, of which it has already sold ~16MW in 3QFY12.
- For the industry, we expect INR0.8/unit and INR0.5/unit decline in merchant power rates in FY12 and FY13 respectively, to INR4/unit and INR3.5/unit.
- For Shree, we are modeling in for decline of INR0.6/unit in FY12 to INR4.45/unit and INR0.45/unit decline in FY13 to INR4/unit. We model in volumes (incl traded power) of 1.3b units in FY12 (v/s 1.35b units earlier) and 2.1b units in FY13 (v/s 2.18b units earlier).

### Upgrading estimates

- We are upgrading our earnings estimates to factor in for better cement realizations and lower than estimated cost. Our EBITDA estimates for FY12 and FY13 have been upgraded by ~2%.
- We are upgrading our adj EPS (for higher depreciation) estimates for FY12 and FY13 by ~3% and 5% to INR204.7 and INR217.7.
- Our estimates model in cement volumes growth of 9.2% in FY12 to 11.1MT and 8.3% in FY13 to 12.1mt. We model in for INR25/bag higher realizations in FY12 and INR10/bag increase in FY13.

### Revised forecast (INR M)

	FY12E			FY13E		
	Rev	Old	Chg (%)	Rev	Old	Chg (%)
Net Sales	46,295	45,608	1.5	54,748	54,715	0.1
EBITDA	12,190	11,972	1.8	13,997	13,752	1.8
Net Profit	7,133	6,929	2.9	7,585	7,213	5.3
EPS (INR)	204.7	199	2.9	217.7	207	5.2

Source: MOSL

### Valuation and view

- Shree's cement would witness return of superior profitability, with EBITDA/ton of INR1,089/ton in FY13 v/s MOSL Cement Universe average of INR979/ton.
- It is well placed for next leg of growth in cement business with strong balance sheet (net cash of INR2b as of Dec-11). It is expanding capacity at its Rajasthan plant by ~1.6mt which would be operational by 1QFY14.
- The stock trades at 10.2x FY13E EPS, 4.9x EV/EBITDA and US\$98/ton (adjusting for Merchant Power assets of ~400MW). Maintain Buy with target price of INR2,636/share (SOTP based).

### Shree Cement: Fair value estimates (INR m)

	Parameter	Factor	FY12	FY13	FY14
Cement business	EV/EBITDA	6	69,114	78,886	91,698
Merchant Power	DCF	@ 15% WACC	4,717	4,159	3,686
<b>Total EV</b>			<b>73,831</b>	<b>83,045</b>	<b>95,384</b>
Less: Net Debt			-2,838	-8,770	-16,285
Equity Value			76,669	91,815	111,669
<b>Fair Value (INR/share)</b>			<b>2,201</b>	<b>2,636</b>	<b>3,205</b>
Upside (%)			-1.6	17.8	43.3

Source: MOSL

## Shree Cement: an investment profile

### Company description

Shree Cement is the largest single-location integrated cement plant in North India, with an installed capacity of 13m 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 North India. 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 India
- One of the efficient cement manufacturer, best positioned to manage downturn in the cycle
- De-risking its business by diversifying into merchant power.

### Key investment risks

- Being a single location plant, it is heavily dependent on North India; any downturn in prices in the North 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.

### Recent view

- Expanding capacity at Rajasthan plant by 1.6mt with investments of INR5b and expected commissioning by 1QFY14.

### Valuation and view

- The stock trades at 10.3x FY13E EPS, 4.9x EV/EBITDA and USD98/ton (adjusting for Merchant Power assets of ~400MW).
- Maintain **Buy** with target price of INR2,636/share (SOTP based).

### Sector view

- We believe we have already witnessed bottom-of-the-cycle utilization & profitability, and it should gradually improve hereon given sustainable demand drivers.
- Structural increase in cost base would necessitate higher cement prices.
- Revival in cement demand, which we expect to improve from 2HFY12, would be key catalyst for the stock performance.

### Comparative valuations

		Shree Cement	Birla Corp	India Cement
P/E (x)	FY12E	10.9	6.4	6.5
	FY13E	10.3	5.7	5.7
P/BV (x)	FY11E	3.5	0.9	0.5
	FY12E	2.8	0.8	0.5
EV/EBITDA (x)	FY11E	6.2	5.0	5.0
	FY12E	4.9	4.1	4.3
EV/Ton (US\$)	FY11E	106	52	63
	FY12E	98	47	60

### Shareholding Pattern (%)

	Dec-11	Sep-11	Dec-10
Promoter	64.8	64.8	64.8
Domestic Inst	5.0	4.5	6.4
Foreign	19.1	19.4	17.4
Others	11.2	11.4	11.5

### EPS: MOSL forecast v/s Consensus (INR)

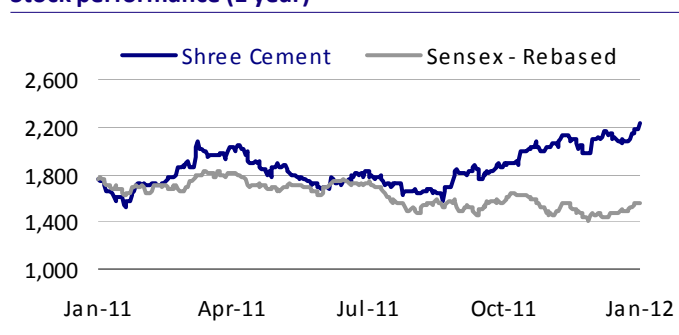
	MOSL Forecast*	Consensus Forecast	Variation (%)
FY12	204.7	-	-
FY13	217.7	-	-

\*Adjusted for accelerated depreciation

### Target Price and Recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
2,237	2,636	17.8	Buy

### Stock performance (1 year)



## Financials and Valuation

Income Statement					Ratios				
(INR Million)									
Y/E March	2010	2011	2012E	2013E	Y/E March	2010	2011	2012E	2013E
<b>Net Sales</b>	36,321	35,119	46,295	54,748	<b>Basic (Rs)</b>				
Change (%)	34.0	-3.3	31.8	18.3	<b>Adj. EPS *</b>	291.9	197.6	204.7	217.7
<b>EBITDA</b>	15,025	8,856	12,190	13,997	Cash EPS	455.6	391.5	430.6	362.9
Margin (%)	41.4	25.2	26.3	25.6	BV/Share	526.2	570.1	630.5	791.1
Depreciation	5,704	6,758	7,867	5,058	DPS	13.0	14.0	16.0	16.0
<b>EBIT</b>	9,321	2,099	4,322	8,939	Payout (%)	7.8	27.2	23.7	10.4
Int. and Finance Charges	1,291	978	1,337	1,234	<b>Valuation (x)</b>				
Other Income - Rec.	1,284	468	70	150	P/E		11.3	10.9	10.3
<b>PBT before EO Expense</b>	9,313	1,588	3,055	7,854	Cash P/E		5.7	5.2	6.2
EO Expense/(Income)	634	485	-8	0	P/BV		3.9	3.5	2.8
<b>PBT after EO Expense</b>	8,679	1,103	3,063	7,854	EV/Sales		2.7	1.9	1.5
Tax	1,918	-994	306	1,610	EV/EBITDA		9.2	6.2	4.9
Tax Rate (%)	22.1	-90.0	10.0	20.5	EV/ton (US\$-Cap)		128	106	98
<b>Reported PAT</b>	6,761	2,097	2,757	6,244	Dividend Yield (%)		0.6	0.7	0.7
<b>Adj PAT for EO items</b>	7,097	2,582	2,750	6,244	<b>Return Ratios (%)</b>				
Change (%)	18.6	-63.6	6.5	127.1	RoE	66.8	36.0	34.1	30.6
Margin (%)	19.5	7.4	5.9	11.4	RoCE	31.9	6.5	11.1	21.2
<b>Adj PAT *</b>	10,168	6,883	7,133	7,585	<b>Working Capital Ratios</b>				
<b>Balance Sheet</b>	<b>(INR Million)</b>				Inventory (Days)	36	42	40	40
Y/E March	2010	2011	2012E	2013E	Debtor (Days)	8	11	8	10
Equity Share Capital	348	348	348	348	Working Capital Turnover (l)	62	55	63	104
Total Reserves	17,984	19,513	21,618	27,210	<b>Leverage Ratio (x)</b>				
<b>Net Worth</b>	18,332	19,862	21,966	27,558	Current Ratio	1.6	1.6	1.8	2.3
Deferred Liabilities	-124	-723	-1027	-988	Debt/Equity	1.1	1.0	0.8	0.7
Total Loans	21,062	20,079	17,079	19,079	* Adj for accelerated depreciation & EO items				
<b>Capital Employed</b>	39,271	39,218	38,018	45,649	<b>Cash Flow Statement</b>	<b>(INR Million)</b>			
Gross Block	36,189	45,701	54,201	58,201		2010	2011	2012E	2013E
Less: Accum. Deprn.	21,995	28,752	36,620	41,678	Oper. Profit/(Loss) before T	14,498	8,856	12,190	13,997
<b>Net Fixed Assets</b>	14,194	16,949	17,582	16,523	Interest/Dividends Recd.	1,131	468	70	150
Capital WIP	3,000	5,000	1,500	2,500	Direct Taxes Paid	-1,897	395	-611	-1,571
Investments	15,922	11,965	10,965	10,965	(Inc)/Dec in WC	-61	1,294	1,677	243
<b>Curr. Assets</b>	15,822	14,389	17,577	27,384	<b>CF from Operations</b>	13,671	11,013	13,325	12,819
Inventory	3,581	4,042	5,073	6,000	(inc)/dec in FA	-11,710	-11,513	-5,000	-5,000
Account Receivables	824	1,082	1,015	1,500	(Pur)/Sale of Investments	-6,306	3,958	1,000	0
Cash and Bank Balance	4,164	4,608	8,952	16,884	<b>CF from investments</b>	-18,016	-7,555	-4,000	-5,000
Others	7,252	4,656	2,537	3,000	Issue of Shares	0	-482	8	0
<b>Curr. Liability &amp; Prov.</b>	9,667	9,084	9,605	11,723	(Inc)/Dec in Debt	5,729	-983	-3,000	2,000
Account Payables	4,668	6,264	6,342	7,500	Interest Paid	-1,332	-978	-1,337	-1,234
Provisions	4,999	2,820	3,263	4,223	Dividend Paid	-611	-571	-652	-652
<b>Net Current Assets</b>	6,155	5,305	7,972	15,661	<b>CF from Fin. Activity</b>	3,786	-3,014	-4,981	114
<b>Appl. of Funds</b>	39,271	39,218	38,018	45,649	Inc/Dec of Cash	-559	444	4,344	7,932
E: MOSL Estimates; * Adj for accelerated depreciation & EO items					Add: Beginning Balance	4,723	4,164	4,608	8,952
					<b>Closing Balance</b>	4,164	4,608	8,952	16,884

**N O T E S**

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