Rating Rationale for J K Cement Ltd's proposed long-term secured Non-Convertible Debentures Issue of ₹ 150 Crore with a tenor up to 10 years

NCD Issue Rating: BWR AA-	Outlook : Stable

Brickwork Ratings has assigned BWR AA- (Pronounced BWR Double A minus) for J K Cement Ltd's (JKCL or "the Company") proposed long term Secured Non Convertible Debentures (NCD) issue of ₹ 150 Crore having a tenor up to 10 years. Brickwork Ratings' 'BWR AA' stands for an instrument that is considered to offer **High** credit quality / safety in terms of timely servicing of principal and interest obligations.

The rating has, inter alia, factored JKCL's consistent growth, Management quality, significant presence in the northern and expanding presence in the southern and western parts of the country.

BWR has essentially relied upon the JKCL's audited financial performance up to the financial year ending March 2010, quarterly unaudited published results up to September 2010, projected financials, and information and clarification provided by the company.

Outstanding Ratings

Instruments	Amount	Rating	Assigned/ Reaffirmed	Tenor	Rating History
					Rating As on
Secured NCD	₹ 100 Crore	BWR AA- (Stable)	Initial Rating – August 2010	10 years	BWR AA- (Stable) August 2010

Background

JK Cement Ltd is one of the top ten Grey Cement producers in the country with 35 years of experience in manufacturing quality cement, a key component for infrastructure development. The present Grey cement capacity of JKCL has been enhanced to 7.50 MTPA in FY2010 from 4.50 MTPA in FY2009 with the commissioning of its new plant in Karnataka in Sep.'09. JKCL is the second largest producer of white cement in India with an installed capacity of 0.40 MTPA in Gotan, Rajasthan.

The proceeds from the proposed NCD issue would be utilized towards long Term working capital requirements and general corporate purposes of the Company. The issue is secured by pari-passu first charge by way of mortgage/hypothecation of fixed assets of the company.

Business Operations

J K Cement Ltd is a unit of the J K Organization, one of the important Industrial groups in India, with over three decades experience in cement industry and produces Grey cement (OPC and PPC) and White cement under the brand name "Sarvashaktiman", "JK Super" and "JK White Cement". The company has expanded its product mix to include value-added products such as "JK Wall Putty" and "JK Water Proof".

At present Grey Cement capacity of JKCL is 7.5 MTPA comprising of 3.25 MTPA in Nimbahera (Rajasthan), 0.75 MTPA in Mangrol (Rajasthan), 0.50 MTPA in Gotan (Rajasthan) and 3.00 MTPA in Mudhol (Karnataka). The company has a 0.40 MTPA capacity of white cement in Gotan (Rajasthan). JK Cement has large reserves of high quality limestone, which is estimated to be sufficient to support the planned capacity of its plants in Rajasthan for next 40 years and for about 25 years in case of its Mudhol plant in Karnataka.

JKCL is one of the largest cement production companies in Northern India. Company's Grey cement plants at Nimbahera & Mangrol are ISO 9001:2000 QMS and ISO 14001:2004 EMS certified. The Grey cement plants in northern region achieved capacity utilization of 88% in FY10. The company's White Cement plant at Gotan is ISO 14001:1998 EMS, OHSAS 18001:2005 and SA 8000 certified and has achieved capacity utilization of 75% in FY10.The company has national distribution network that comprises of 104 warehouses supporting a strong network of more than 4300 retailers. Network for Grey Cement is spread across India's northern region, southern region, western region and some parts of central region. White cement network is spread across the country. The Company exports White Cement to a number of countries, including South Africa, Nigeria, Singapore, Bahrain, Bangladesh, Sri Lanka, Kenya, Tanzania, United Arab Emirates and Nepal.

Ongoing Projects

The company has adopted expansion strategy that includes Greenfield projects and Brown field options that is expected to significantly boost future operations. JKCL has put on hold its plan to set up a 1.8 MTPA plant in Fujairah, UAE considering the present market conditions in the region. Further, it is also proposed to set up a 3.5 MTPA capacity cement plant at existing Mangrol unit with a split grinding unit in North India.

Power Projects

The company has invested in generation of power through coal based power plants and also set up a waste heat recovery power plant, which have resulted in a sustained source of low cost power resulting in higher savings in power costs. The company has commissioned 13.20 MW waste heat recovery power plant and 20 MW coal based power plant at Nimbahera (Rajasthan), and a 7.5 MW coal based power plant at Gotan (Rajasthan). Further, 50MW of coal based plant at Mudhol (Karnataka) also commissioned in FY 2009 -10. The Company presently has a total power generation capacity of over 100 MW which resulted in saving in the cost of power.

Management

The Board of JKCL consists of professionals with vast industry and management experience. It is headed by Dr. Gaur Hari Singhania, who also holds the Chairmanship in other companies such as JK Synthetic Limited, Juggilal Kamlapat Cotton Spg. & Wvg. Mills company Ltd. and JK Traders Limited. Mr. Yadupati Singhania is the MD & CEO of the Company and has been involved in the cement industry for over 30 years. He is also a member of managing committee of the Cement Manufacturers Association and Board of Governors of the National Council for Cement and Building Material. Operations of the company are managed by professionals with relevant industry and management experience.

Financial Performance

On a standalone basis, Gross sales of the Company increased by 19.80% from ₹ 1876.45 Crore in FY 09 to ₹ 2248.06 Crore in FY 10. Net Sales for FY 10 stood at ₹ 1826.78 Crore in FY 10 as against ₹ 1496.83 Crore in FY 09. PBITDA of the Company has increased from ₹ 331.90 Crore in FY 09 to ₹ 458.39 Crore in FY 10 and PAT has increased by 58.77% from ₹ 142.34 in FY 09 to ₹ 225.99 Crore in FY10.

Net-worth of the company stood at ₹ 1082.41 Crore in FY 10 as against ₹ 901.62 Crore in FY 09 and the total borrowings of the company increased from ₹ 564.40 in FY 09 to ₹ 1073.72 Crore in FY 10. The debt equity ratio and current ratio for the FY 10 stood at 1.01 and 1.85 respectively.

The company has taken up establishment of a Greenfield Grey Cement plant in free trade zone at Fujairah, U.A.E. under its subsidiary and construction work is to begin. Hence on a consolidated basis, there was no change in Gross sales of the company, but PAT declined to ₹ 224.55 crore as against the stand alone figure of ₹ 225.99 crore.

On a standalone basis, Net sales of the Company decreased by 3% from ₹ 431.02 Crore in Q2 FY10 to ₹ 419.58 Crore in Q2 FY11. Operating profit of the Company has decreased substantially by 106% from profit of ₹ 109.44 Crore in Q2 FY10 to loss of ₹ 6.41 Crore in Q2 FY11 and PAT has declined by 132% from profit of ₹ 65.39 in Q2 FY10 to loss of ₹ 20.84 Crore in Q2 FY11 mainly due to higher costs of raw material, higher power and fuel cost, higher employee cost and higher transportation, depreciation and handling charges. Net profit for the half year ended September 30, 2010 stood at ₹ 8.66 crore as compared to ₹ 135.6 crore in the corresponding previous half year.

Abridged balance sheet, P&L, Key financial ratios for the period FY08 – FY10 and the performance for half year ended September 30, 2010 have been given in Annexure I, II, III and IV respectively.

Industry Outlook

The growth of cement industry is associated with growth in other infrastructure activities such as real estate, roads, highways, power plants, hydel projects etc. In FY 10 the industry has shown signs of recouping from the economic slowdown, however, the growth rate of cement industry

declined to almost 8% as compared to double digit growth recorded in previous years. The Indian cement industry has had a good year in fiscal 2009-10. Northern region has witnessed healthier growth as compared to other region in the wake of the huge infrastructure activity on account of the Commonwealth Games 2010 held recently. Construction activity is picking up in various segments like housing, industrial and other infrastructure projects.

The pricing pressure however still remains for the cement industry. Cement prices have continued to fall mainly due to huge capacity addition of 49.4 million tonnes during 2009-10. Additional 45 million tonnes of new capacity by the end of Mar-11 could keep the prices down. The cost side pressure is also on the rise for cement industry. Imported coal price has touched a high of $ 107 per tonne in May 2010 as compared to $ 65 in Mar 2009. Input costs of the cement industry have risen much higher due to rise in prices of coal and petcoke. Exports have been hit after the recent financial crash in Dubai which has affected construction activity there.
Demand however is expected to go up due to thrust on infrastructure activities and real estate sector which is expected to help cement industry to sustain higher growth rates in future.

Increased supply in the southern region coupled with extended monsoons across India has significantly impacted the industry in the second quarter of FY2011 with most players reporting fall in profits or losses. Growth in demand is expected to remain sluggish in the near term.

JK Cement Ltd. is an established player in cement industry especially in the northern region that has witnessed significant increase in infrastructure activities. Historically the company has been able to adapt to changing environment by taking strategic decisions in reducing costs, marketing focus with well established client base and dealer network, consistent growth in production and sales and greenfield expansion plans. However in Q2 FY2011, the company reported a net loss of ₹ 20.8 crores due to prolonged monsoons, increasing operating costs coupled with high stabilization costs of its new plant in Karnataka. The company's revenues and profitability are expected to remain subdued in the near term, though the long term prospects remain positive.

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Brickwork Ratings (BWR) has adopted SEBI's standardized Rating Symbols and their definition advised vide SEBI circular CIR/MIRSD/4/2011 dated June 15,2011, with effect from June 21, 2011. While there is no change in the Rating symbol as a consequence to the above, for the amended definition of the Rating, please refer to http://www.brickworkratings.com/scale.html. It is clarified that the said change in the definition should not be construed as a change in the Rating.

Key Financials for JKCL

Annexure I: Balance Sheet (Standalone)

S. No	Particulars (in Rs. Crore)	2009-10	2008-09	2007-08
A	**Sources of Funds**			
1	Share Capital	69.93	69.93	69.93
2	Reserves & Surplus	1283.82	1116.12	983.41
3	Revaluation Reserves	265.24	277.85	291.15
4	**Net Worth (1 + 2 – 3-16)**	**1082.41**	**901.62**	**755.39**
5	Loans			
5.1	Secured Loans	937.61	436.86	382.79
5.2	Unsecured Loans	136.11	127.54	127.74
5.3	**Total Loans (5.1 + 5.2)**	**1073.72**	**564.40**	**510.53**
6	Deferred Tax Liability	185.80	100.60	50.99
7	**Total Sources of Funds**	**2613.27**	**1851.05**	**1614.86**
B	**Application of Funds**			
8	Gross Block	2376.70	1441.14	1249.77
9	Depreciation	324.49	225.40	160.63
10	**Net Block (8 - 9)**	**2052.21**	**1215.74**	**1089.14**
11	Capital W-I-P	225.28	35.06	133.84
12	Investments	5.99	10.74	9.50
13	**Current Assets, Loans & Advances**			
13.1	Inventories	237.62	136.13	114.53
13.2	Sundry Debtors	81.87	53.03	57.26
13.3	Cash & Bank Balance	131.67	125.20	145.44
13.4	Loans & Advances	231.83	581.49	352.50
13.5	**Sub Total (13.1 to 13.4)**	**684.79**	**897.18**	**671.06**
14	Less: Current Liabilities	357.69	310.11	290.63
15	**Net Current Assets (13.5-14)**	**327.10**	**587.07**	**380.43**
16	Miscellaneous Expenditure	2.69	2.44	1.95
17	**Total Application of Funds**	**2613.27**	**1851.05**	**1614.86**

Annexure II: Abridged Profit and Loss (Standalone)

S. No	Particulars (in Rs. Crore)	2009-10	2008-09	2007-08
1	Gross Sales	2248.06	1876.45	1812.84
2	Less: Excise Duty	194.84	210.94	218.33
	Sales Tax	226.43	168.76	136.25
3	**Net Sales (1 - 2)**	**1826.78**	**1496.83**	**1458.25**
4	**Expenditure:**			
4.1	Manufacturing Expenses	741.18	655.75	604.11
4.3	Employee Cost	99.43	87.30	67.63
4.4	Transport, Clearing & Forwarding	547.07	429.79	370.84
4.5	**Total Expenditure**	**1387.68**	**1172.84**	**1042.58**
5	PBIDT	458.39	331.90	423.52
6	Cost of Borrowings	61.63	45.53	35.88
7	PBDT	396.76	286.37	387.64
8	Depreciation	85.50	52.42	41.07
9	PBT	311.26	233.95	346.57
10	Taxes	85.27	91.61	81.41
11	**PAT**	**225.99**	**142.34**	**265.16**

Annexure III: Ratio Analysis (Standalone)

S. No	Particulars	2009-10	2008-09	2007-08
1	Debt - Equity Ratio (Times)	1.01	0.65	0.72
2	Interest Coverage Ratio (Times)	6.81	6.94	11.37
3	DSCR (Times)	1.60	1.51	2.96
4	Net Worth (Rs. Crore)	1082.41	901.62	755.39
5	Profitability Margin (%)	12.37	9.51	18.18
6	ROCE (%)	19.06	19.36	31.48
7	Net Cash Accruals to total Debt (%)	0.26	0.29	0.52
8	Current Ratio (Times)	1.85	0.99	1.01

Annexure IV: Performance for quarter ended 30th September 2010

S. No	Particulars (in Rs. Crore)	Half Year ended	
		30.09.2010	30.09.2009
1	Net Sales	941.38	859.36
2	Other operating income	19.14	10.83
3	**Total Income**	**960.52**	**870.19**
4	**<u>Expenditure</u> of which:**		
4.1	Consumption of Raw Material	116.31	85.73
4.2	Power & Fuel	248.85	165.65
4.3	Employee Cost	62.69	50.18
4.4	Transport, Clearing & Forwarding	224.41	162.42
4.5	Other Expenses	194.07	**151.31**
4.6	**Total Expenditure**	**846.33**	**615.31**
5	PBDIT	114.80	225.19
7	**PAT**	**8.66**	**135.60**