

# MANAGEMENT DISCUSSION & ANALYSIS

## GLOBAL ECONOMY

The world economy has strengthened during FY 2017-18, as lingering fragilities in the global financial markets began subsiding. According to IMF – World Economy Report, global growth is projected to rise at 3.9% in 2018 vis-à-vis 3.8% in 2017. The improvement in global economy provides an opportunity to countries to adopt more sustainable policies that work towards low-carbon economic growth, economic diversification, reducing inequalities and eliminating deep-rooted barriers to the growth and development of an economy.

## INDIAN ECONOMY

During FY 2017-18, India's economy was marked by various structural reform initiatives aimed at strengthening the country's macro-economic scenario for sustainable future developments. Despite a tepid performance in the first half of FY 2017-18, owing to disruptions like the implementation of Goods and Services Tax (GST), India maintained its stability to record a growth of ~6.7%.

India has also emerged as a major global investment economy, gaining the top 5th spot as an international investment destination. Moreover, Moody's Investors Service upgraded India's sovereign rating to Baa2 with stable economic conditions. According to the World Bank report, India has improved its ranking by 30 spots in terms of 'Ease of Doing Business' and is ranked at 100 out of the 190 countries.

## INDIA'S GDP GROWTH (%)

2014-15	2015-16	2016-17	2017-18
7.3	7.6	7.1	6.7

Source: Central Statistics Office (CSO)

## OUTLOOK

India's GDP is expected to reach US\$ 6 trillion by FY 2027 owing to consistent reforms, digitisation, globalisation and favourable demographic conditions. Over the next 10-15 years, India is expected to be among the top three economic powers, backed by its strong democracy and partnerships.

Government initiatives for infrastructure development, emphasis on creation of smart cities and focus on affordable housing programme is likely to bolster India's industrial development. Additionally, the services sector is expected to continue to thrive owing to services exports, financial inclusion and rising per capita income. The GDP growth of the country is estimated to rise to ~7.4% in FY 2018-19.

## INDIAN CEMENT INDUSTRY

India is the world's second largest cement market, both in terms of production and consumption. During FY 2017-18, the cement sector grew by 6% owing to increased infrastructure spending by the Government of India and re-materialisation of demand from the private sector.



A view of Mangrol plant

India needs an investment of ₹ 50 lacs crore in the infrastructure sector and the Government of India has undertaken various infrastructure projects to facilitate it including:

- Selected cities for the Smart City project with a cost of ₹ 2.04 lacs crore
- Planned ~35,000 km of road development under the Bharatmala project Phase I with an outlay of ₹ 5.35 lacs crore
- Chalked out construction plan of 10 million houses in rural India and 20 million toilets under Pradhan Mantri Awas Yojana and Swachh Bharat mission, respectively

Additionally, the implementation of GST has eliminated multiple points of taxations and increased access across markets for the organised sector, allowing smoother movement of goods. Also, the introduction of Real Estate Regulatory Act (RERA) ensures accountability for all real estate projects and assures timely completions, which are likely to increase buyer confidence. These factors will impact the cement industry positively by facilitating access to various markets and bolstering the real estate market.

### INDUSTRY TRENDS

- Increasing presence of small and mid-sized cement players diminishing market concentration
- Growing adoption of cement instead of bitumen in construction of roads
- Huge investments in infrastructure development by the government

### Grey Cement

As per IBEF Report, June 2018 India has a cement production capacity of ~455 MT, of which almost 98% is dominated by the private sector. The top 20 companies account for ~70% of the total production. Grey cement is one of the most important building materials used in construction and infrastructure activities. The rise in real estate sector, housing demand and infrastructure spending will augment grey cement demand.

### Performance

Grey cement registered a growth of 16% in production volumes over the last year. The North and South region recorded a rise to the tune of 17% and 14%, respectively.

### White Cement

White cement provides a classy touch to architectural designs and is used in combination with inorganic pigments to produce

brightly coloured concretes and mortars. It is also used as an input for the manufacture of value-added products like wall putty and primers.

### Performance

White cement registered a growth of 2% y-o-y in production volumes, whereas the value-added product, wall putty showed a growth of 14% on y-o-y basis.

### INDUSTRY GROWTH DRIVERS

#### Housing

- Housing forms the major portion of cement demand at ~65%
- Improved rural incomes, higher rural credit and increased allocation for rural, agriculture and allied sectors are likely to encourage rural housing demand
- Government initiatives provide demand impetus in the sector

#### Infrastructure

- 100 smart cities planned
- Projects like dedicated freight corridors and ports under development
- Metro rail projects underway in most major cities

#### Urbanisation

- Development of 500 cities with population of more than 100,000 under new Urban Development Mission

### INDUSTRY OUTLOOK

India's cement production capacity is expected to reach 550 million tonnes by 2025. Growth in the cement sector in 2018-19 is likely to be fairly high driven by the slew of infrastructure projects like Bharatmala, Smart Cities, PM Awas Yojana and Housing for All. The Union Budget 2018-19 looks promising with increased allocations to infrastructure spending, energising the segment.

### INDUSTRY RISKS

#### Inflation rate

Inflation plays a pivotal role in Indian economy. In 2017-18, average inflation dipped to a six-year low of 3.3%, however, it is expected to rise 4.40% during FY 2018-19. One of the major causes of inflation is overall increase in demand for goods and services, which escalate their prices. Besides, in case normal monsoon is affected, inflation may further rise making commodity prices dearer.



A view of Fujairah plant

### Interest rate

Reserve Bank of India has kept repo rate unchanged for the last year at 6.0%. However, due to increasing cost of funds for banks, the marginal cost of lending rate has started increasing. All banks have started lending on the basis of marginal cost of funds-based lending rate (MCLR), leading to higher cost of borrowing for property buyers, resulting in lower demand in the housing segment.

### Raw material risk

The cement industry depends on limestone and other raw materials. However, availability of limestone is limited and thus, it is essential to promote the use of blended cement, which uses alternative raw materials such as fly ash and slag. The increase in the cost of these alternative materials — now fly ash is available on auction and slag on the basis of prevailing market prices — may further increase production costs.

### Competition risk

India's cement sector has become highly competitive with multiple large players operating in the domestic market. While earlier most companies were catering to specific parts of the country, now most players are expanding their reach pan-India, thus creating greater market competition.

### Infrastructure risk

Infrastructure sector drives overall development of the economy and is a major focus of the Government of India. Any pull back by the government on its initiatives will result in de-growth for the cement industry. Moreover, too many regulatory approvals and compliances might be a hindrance to the segment's progress.

### Power and fuel risk

Cement industry is highly energy intensive and ~23% of its total expenditure consists of power and fuel costs. At J.K. Cement, ~80% of our requirement for kiln fire is met by petcoke, which is a derivative of crude oil. Thus, any rise in crude oil prices will adversely impact prices of petcoke and operating costs of the

Company. In case of increase in petcoke prices or non-availability, we use imported or indigenous coal (through e-auction) as the availability of linkage coal is limited. Further, owing to the ban on using petcoke for captive power generation, production costs would escalate more. Therefore, we are looking towards adoption of green energy, which offers almost same calorific value as of low grade coal for a more sustainable and cost-efficient energy option.

### Logistics risk

With the rise in diesel prices, cost of road transportation increases. At J.K. Cement, we currently use railways for only 10-15% of our logistics needs for cement. This cost increase and huge dependence on road transportation would have an impact on our operational costs.

### ABOUT J.K. CEMENT

J.K. Cement Limited is an affiliate of the industrial conglomerate J.K. Organisation, which was founded by Late Lala Kamlapat Singhania. With over four decades of experience, J.K. Cement has partnered India's multi-sectoral infrastructure needs on the strength of its product excellence, customer orientation and technology leadership. The Company is the third largest white cement manufacturer in the world with 1.20 MTPA capacity, including 0.6 MTPA white cement plant at Fujairah, U.A.E. Besides, it is the second largest producer of wall putty in India with installed capacity of 0.7 MTPA. The Company intends to add up to 8 MTPA capacity by December 2022, taking the total installed capacity to 18 MTPA for grey cement. Further capacity expansion of wall putty by 0.2 MTPA at Katni, Madhya Pradesh is likely to commission shortly.

### Mangrol expansion project

With a view to tap the growing demand for grey cement, J.K. Cement commenced its brownfield expansion plan of 4.2 MTPA capacity. This integrated unit at Mangrol will have a clinker capacity of 2.5 MTPA that would cater to the requirement of split grinding units of 1.5 MTPA at Aligarh, Uttar Pradesh and 0.7 MTPA at Balsinor, Gujarat along with an additional grinding capacity of 1 MTPA each at Nimabhera and Mangrol locations.

The cost of the project is ~₹ 2,000 crores, which will be financed by debt and internal accruals/equity. The project is likely to be commissioned by March 2020.

Once complete the project will provide the following key advantages:

- Reduce power cost through waste heat recovery of 13 MW
- Diminish logistics and raw material costs through strategically located split grinding units
- Decrease limestone transportation cost, as well as serve the environment through conveyor belts at limestone mines
- Scale down costs with increase in grinding capacity at Mangrol and Nimabhera

**Business drivers**

- Superior product mix offering blended products such as PPC and PSC
- Use of alternative materials, reducing use of existing natural resources
- Multi-region presence provides a wide market coverage
- Captive power generation ensures meeting power requirement at lower cost
- Access to captive limestone reserves adjacent to manufacturing facility

**Performance highlights**

	FY 2017-18	FY 2016-17	y-o-y growth (%)
Revenue from operations (₹ in crore)	4,758.17	4,379.83	9%
EBITDA (₹ in crore)	760.65	693.42	10%
PAT (₹ in crore)	341.87	210.78	62%
EPS (₹)	48.89	30.14	62%

**SUSTAINABILITY GOALS**

As a socially and environmentally responsible company, J.K. Cement consistently adopts sustainable practices to demonstrate corporate citizenship. Besides, working on its group-wide transformational strategy to leverage synergies, develop best-in-class practices and seek future growth opportunities, the Company is undertaking active measures to preserve and conserve its surroundings.

It is focussed on conservation of resources, better environment management and community engagement to create value for all its stakeholders. The Company's environmental actions emphasise on managing biodiversity, promoting energy-efficiency, encouraging initiatives related to resource optimisation, reducing effects on climate change and pioneering water and waste management.

The Company is promoting the use of blended cement to preserve the depleting natural resources. Moreover, it is replacing the use of fossil fuels with alternative fuels like agro waste, carbon black, fibre mass, ETP sludge, liquid mixed waste and solid mixed waste. The use of alternative fuels will support reduced utilisation of existing natural resources and increased application of waste products, along with being more cost-effective for the Company.

J.K. Cement believes in giving back to the society. Therefore, it has undertaken various initiatives to uplift communities around it. The Company has been focussing on imparting education, promoting community healthcare, contributing for infrastructure development, and encouraging cleanliness and sanitation to enhance the living standards of the society.

**HUMAN RESOURCES (HR)**

J.K. Cement, as part of the group legacy, has deeply imbibed the belief of 'People first'. The Company firmly believes that its people provide it the most significant competitive advantage and are the reason for its success. The Company's HR team works relentlessly to attract, engage and nurture top talent in the industry through progressive human capital acquisition and development initiatives. It endeavours to provide a congenial workplace environment for consistent innovation and improvement by rewarding employees for their dedicated efforts in helping the Company achieve its objectives. Its manpower strength stood at 2,967 as on March 31st 2018.

The Company began its HR transformation journey last year, which is now culminating into technology-oriented systems and processes. In a pioneering move, it adopted the SAP success factors as its cloud-based HR platform to simplify processes. Moreover, the employer brand building initiatives have duly emphasised on positioning J.K. Cement as a competitive and preferred employer across all segments and generations of employees.

In line with its philosophy of nurturing talents and enriching careers, the Company has undertaken several training and development programmes. The HR team consistently address the skills gaps within the Company's talent pipeline and helps to strengthen the Company's leadership bench strength. Additionally, women's safety has always been an important aspect at J.K. Cement and as responsible corporate citizen, POSH (Prevention of Sexual Harassment) at workplace has been adequately emphasised and addressed.

**ADEQUACY OF INTERNAL CONTROLS**

The Company has well placed internal control system according to the size, scale and complexity of its operations. The management of the Company is responsible for ensuring that all internal financial controls are adequate and operates effectively. It has inbuilt policies and procedures for safeguarding its assets, prevention and detection of fraud and errors if any, accuracy and completeness of the accounting and timely preparation of financial information based on IND AS.

Further, internal audit functions are looked by internal audit department, which reports to the Audit Committee of the Board. Internal audit function works independently and evaluates the efficacy and adequacy of internal control system, its compliance with operating system and policies of the Company and accounting procedure at all locations, namely plant, marketing office and depots. Based on the input of internal audit report, designated process owner takes corrective actions in their respective area, thereby strengthening controls and checks. In case any significant observations is noticed same is brought to the knowledge of Members of Audit Committee for corrective actions.