

# MANAGEMENT DISCUSSION AND ANALYSIS



White Cement Plant at Fujairah (United Arab Emirates)

## GLOBAL ECONOMY

Global economic growth rate is gradually stabilizing. With buoyant financial markets and a long-awaited cyclical improvement in manufacturing and trade, global growth is expected to touch 3.5% in 2017 and 3.6% in 2018.

The US economy is performing better and US firms are growing more confident of future demand. The economy has also recorded a lower rate of unemployment. The British economy also saw a rise in domestic demand following Brexit. After a prolonged period of grappling with challenges, Eurozone's economy is also seeing a robust domestic demand led recovery in the second half of 2016. If these tailwinds persist, the global economy may gather momentum over the medium term.

During 2016-17, the picture for emerging market and developing economies (EMDEs) remained distinctly diverse:

- Growth rates in most countries in the Gulf region are projected to be gradual. According to MEED's annual UAE Outlook Report for 2016, a recovery in oil prices combined with growing public and private sector activity, boosted by Dubai's preparations for the Expo 2020 will see real GDP growth rise to between 4-5% a year from 2017- 2020, compared with about 3.1% growth in 2016.
- Stronger than expected growth in China, supported by continued policy stimulus.
- Weaker than expected activity in some Latin American countries (Argentina, Brazil and Turkey) which faced a sharp contraction in tourism revenues.
- Better than expected activity in Russia, in part reflecting firmer oil prices.

## Global growth pattern

|                                   | 2015 | 2016 | 2017 (P) | 2018 (P) |
|-----------------------------------|------|------|----------|----------|
| World Output                      | 3.2  | 3.1  | 3.4      | 3.6      |
| Advanced Economies                | 2.1  | 1.6  | 1.9      | 2.0      |
| United States                     | 2.6  | 1.6  | 2.3      | 2.5      |
| Euro Area                         | 2.0  | 1.7  | 1.6      | 1.6      |
| United Kingdom                    | 2.2  | 2.0  | 1.5      | 1.4      |
| Other Advanced Economies          | 2.0  | 1.9  | 2.2      | 2.4      |
| Emerging and Developing Economies | 4.1  | 4.1  | 4.5      | 4.8      |
| China                             | 6.9  | 6.7  | 6.5      | 6.0      |

## INDIAN ECONOMY

The Indian economy has continued to show resilience in the face of challenging global economic conditions and rising protectionist measures across the world. The country registered a robust GDP growth of 7.1% in FY 2016-17, amid several headwinds.

### Key indicators

- **Inflation:** The retail inflation stayed above the comfort zone of 5% till August 2016. However, it started moderating thereafter due to a normal monsoon, dropping to a two-year low of 3.4%. The average inflation for the FY 2016-17 stood at 4.5% (4.9% in FY 2015-16)
- **Fiscal deficit:** The fiscal deficit as a percentage of GDP stood at 3.5% for 2016-17. This has been revised to 3.2% for 2017-18.
- **Current account deficit:** The current account deficit as a percentage of GDP stood at 0.9% lowest in the last five years.
- **Currency:** The Rupee saw a marginal appreciation as it stood at ₹ 65.9 during 2016-17 (₹ 66 in 2015-16).

India has recently emerged as the world's sixth largest manufacturing country. Emerging urban clusters are driving this economic momentum. The result is that more consumers with higher disposable income are helping enhance India's economic potential. The country's economic prospects appear optimistic with policymakers creating enablers for strong and sustainable growth for the medium to long term.

On the political front also, the government gained major victories in many state elections, including the country's most populous state Uttar Pradesh. The result will boost Prime Minister Narendra Modi's economic reform agenda and market reaction to the outcome was also positive, with the country's stock market recording a new high in March 2017 and the rupee strengthening against US\$.



### Outlook

India's growth rate is likely to touch 7.4% in 2017-18, driven by a rebound in consumption demand following remonetisation. In addition, long-term consumption growth will be driven by major factors: government reforms across all sectors of the economy; low interest rates; benign inflation; favourable demographics (half of the population is below the age of 35), and an expanding addressable market size (India now has 50 large consumption hubs).

### INDUSTRY STRUCTURE AND DEVELOPMENT

The Indian cement industry having capacity of about 420 Mntpa is dominated by a few companies. The top 20 cement companies account for almost 70 per cent of the total cement production of the country. On the back of growing demand, due to increased construction and infrastructural activities, the cement sector in India has seen many investments and developments in recent times.

### CEMENT INDUSTRY OVERVIEW

#### Grey Cement

Though the Industry survived demonetisation shock quicker than expected but the production of major cement producer shows decline almost after a gap of 15 years. However, in the current year demand is expected to grow at @ 5-6% on YOY basis on account of various initiatives taken by the Government to boost infrastructure activities such as allocation for Pradhan Mantri Awaas Yojana-Gramin of ₹ 23,000 crore to complete 1 crore houses by 2019 for the homeless and those living in Kutcha houses.

Further, to promote affordable housing the real estate sector has been conferred infrastructure status and budget also proposed profit-linked income tax deduction for promotion of affordable housing considering carpet area instead of built up area of 30 and 60 Sq. meter. The 30 sq. meter will apply in case of limits of four metropolitan cities while for the rest of the country including peripheral areas of metros, limit of 60 sq. meter will apply.

The Prime Minister in his new year's evening address to the nation provided for an upfront subsidy to low-cost affordable housing along with an interest rate subsidy for loans up to ₹ 6 lakh. Loans up to ₹ 9 lakh will receive an interest subvention of 4 percent while those up to ₹ 12 lakh will be eligible for a 3% reduction in applicable interest rates.

Government has also allocated ₹ 7,000 crore in FY 2017-18 budget for development of roads on highways with special emphasis of laying 2000 kms of coastal roads.

All this will accelerate cement demand which in turn boosts economy at large. If India needs to perform to augur well with developing nations, infrastructure development is necessary which is based on steel and cement, where steel being refereed as the backbone and cement being the blood.

#### White Cement

White cement is used for decorative and architectural concrete, a key advantage of using White Cement is that it provides a neutral tinting base and consistent colour results. Every colour option is possible with it, from pure whites to bright and pastel colours. White concrete usually takes the form of pre-cast cladding panels, since it is not economical to use white cement for structural purposes. White Portland cement is used in combination with inorganic pigments to produce brightly coloured concretes and mortars. It is also used as basis input raw material for manufacture of Value Added Wall putty and Primaxx also.

Besides Grey Cement, company is one of the two manufacturers who are in White Cement business also. Its product portfolio is further enhanced with value added Wall Putty and recently launched Primaxx. Expanded capacity, extensive distribution network, and robust technical know-how have made the Company one of India's most reliable cement brand.

### PERFORMANCE DURING THE YEAR

- **Grey Cement:** Grey cement registered a de-growth of 2% in production volumes over last year. North registered growth of 1% whereas South registered de growth of 9%.
- **White Cement:** White Cement registered growth of 9% on YOY in production volumes whereas White Cement based Wall Putty registered growth of 14% on YOY basis.

### FINANCIAL HIGHLIGHTS

#### Standalone

| Particulars | (₹ /Lacs) |         |
|-------------|-----------|---------|
|             | 2016-17   | 2015-16 |
| Revenue     | 442071    | 413119  |
| EBITDA      | 73430     | 51989   |
| PAT         | 25958     | 10332   |
| EPS (₹)     | 37.12     | 14.78   |

### OPPORTUNITIES AND THREATS

The Government of India has allocated of ₹395,000 crore for the infrastructure sector in the Union budget for FY 2017-18. Indian railways saw the largest-ever rail budget of ₹131,000 crore for

2017-18. Indira Awaas Yojana, Pradhan Mantri Gram Sadak Yojana and Affordable Housing, 100 Smart City Projects and 100% FDI limits for townships, SEZs and settlements development projects are expected to boost the demand for cement consumption.

### ROBUST RISK GOVERNANCE

Our risk-management framework is vigilant enough to anticipate various internal and external risks and take appropriate remedial measures. The framework itself is reviewed regularly to ensure that our risk management objectives are fulfilled and the interests of stakeholders are protected.

#### Our risk management objectives

- Integrate all business processes with the Company's vision and mission.
- Institutionalise a standard framework of identification, analysis, mitigation, monitoring and reporting.
- Analyse operational risk events to prevent future occurrences.
- Communicate transparent and clear objectives across business verticals to support effective and timely decision-making.
- To remain flexible and responsive to societal megatrends and evolving business realities.

**Inflation Rate:** Inflation rates play key role in Indian economy. Inflation rate touched bottom low of 3.17 % in Jan'17, thereafter, it started moving up resulting increase in prices of food commodities and oil and gas etc. are moving up which in turn left less money with public at large. With more deposit than credit growth, bank has no avenues to deploy funds which will further fuel an asset price bubbles. Thus, in order to control inflation RBI hiked reverse repo rate to absorb excess liquidity from system. It is expected that inflation rate will hover around from current 3.81% to 4.5 % in first half and 5% in second half of 2017-18.

**Interest Rate:** Demonetisation drive carried by Government has generated mixed response from public, however drive resulted in bringing back the money which is not actually in the system and also curtailing parallel economy running through system. All these resulted in surplus liquidity in the system. Banks having more deposits than lending, resulted in lowering of interest rates. Most banks are offering interest rate to housing buyer from 8.35-8.65% p.a. Further Government offering special interest rate to low cost affordable housing may generate demand for having home especially from lower and middle-class people.

**Infrastructure Risk:** The housing sector alone constitutes 67% of total cement consumption and rest 33% is spread between

industrial and infrastructure sector. The need for overall development of the economy is the vision of our Government. India economy is based on agriculture, almost 2/3rd Indian population depends upon rural income and a good harvest could boost spending on consumer goods etc. which may add to Government hopes of achieving target growth of 7.5% this fiscal. Further, Indian Metrological Department have predicted normal monsoon this year despite lingering possibilities of the disruptive EL Nino weather pattern way back in 2014 and 2015.

**Raw Material Risk:** Limestone is the basic raw material for manufacture of cement, however its excavation results in depletion of natural resources, further license for new mining lease is subject to MMDR Act. However, in order to move toward sustainable development and greener environment we are using more and more alternate raw materials such as fly ash and slag in place of clinker, this results in reduction of raw material cost and overall cement cost.

**Power & Fuel Risk:** Cement industry is energy intensive, though we have in-house captive power generation sufficient to meet maximum demand still we need external power from Grid to meet out compulsory requirement and purchase power through exchange at cheaper cost. Moreover, to promote green power, we have purchased Solar Power, besides, generation of power through Waste Heat Recovery System. We have coal linkage for captive plant as well as cement plant but still we are using pet coke both indigenous and imported to meet the shortfall of coal. The company requires almost 1 million tonnes of coal and pet coke to meet the requirement of kiln & CPP. Though, pet coke has emerged as viable option replacing coal on account higher GCV and comparatively lower price than coal, price of Pet coke is dependent on international crude price and highly volatile. To mitigate this risk company has started increasing the usage of Alternate Fuel such as Agro Waste, Fibre mass, Carbon black, ETP sludge, Tyre chips, Liquid and Solid Mix Waste. All this have resulted in saving of natural resources with limited liability.

**Logistics Risk:** Logistic plays important role in cement industry for inward and outward movement both. Almost 80% of dispatches are made through road so any increase in diesel price may result in increase in freight cost making cement cost dearer to end-user. Though availability of rakes is a major concern, dispatches are made by rail as much as possible including interunit clinker transfer to reduce logistic cost.

**Taxation Impact:** Introduction of Goods and Services Tax (GST) is a significant step in the reform of indirect taxation in India. Amalgamating several Central and State taxes into a single tax would mitigate cascading or double taxation, facilitating a common national market. The simplicity of the tax should lead to easier administration and enforcement. From the consumer point of view, the biggest advantage would be in terms of a reduction



in the overall tax burden on goods, which is currently estimated at 25%-30%, free movement of goods from one state to another without stopping at state borders for hours for payment of state tax or entry tax and reduction in paperwork to a large extent will improve trade. GST is expected to be applicable from 1<sup>st</sup> July 2017.

### ENVIRONMENTAL SUSTAINABILITY

The journey towards sustainable development is improving on year on year basis. J.K Cement shared its 4th Annual Sustainability development report on triple bottom line performance for the year 2016-17 based on Global reporting initiative (GRI) G4 guidelines. The company has also been issuing a Business Responsibility Report as a part of its Annual report since 2015-16.

Our focus is overall development of company and society as a whole. With a vision to pay back to the society at large, we keep on engaging on activities which improve living standard of people living nearby plant and at the same time sustaining and preserving depleting natural resources. The way forward is to use alternate raw material and fuel in place of existing depleting natural resources. Adaption of rain water harvesting system to preserve our underground water resources is major concern for one and all. Use of more and more green energy such as Wind, Solar and Waste Heat Recovery for meeting shortfall of power is the need of day. In all, sustainable development is the development that meets the needs of the present, without compromising the ability of future generations to meet their own needs.

J.K Cement will continue to strive towards community development by way of imparting basic education to underprivileged children's, further imparting training of stitching handicrafts items to village women so that they can equally contribute towards family income along with male member, thereby increasing living standard of community at large.

### HUMAN RESOURCES

We are undergoing HR Transformation exercise under the umbrella of Project 'SAKSHAM' to align Human Resource to Business and build our organisational capabilities to the next level in preparation for future endeavours, which includes reviewing HR policies & processes and leveraging the technology.

While making our processes efficient and transparent, we continue to strive to ensure that company values and ethics be imbibed in our employees and our polices & processes are designed in a way which enables the desired culture building.

We believe in our home-grown talent and aim to develop the leaders within the organisation by imparting them the desired trainings, opportunities to work on various projects, assigning them tasks outside their routine work and relocating employees to various geographies etc.



■ Aerial View of Mangrol (Rajasthan) Plant

We believe in cultural and gender diversity. Our gender diversity has seen substantial increase over the years. We have been trying to ensure that our employees recommend our organisation to the outside world, thus enabling us to attract and retain best talent.

Further, continuous improvements as a part of ongoing change management initiatives aimed at building a future-ready and world class organisation persist as a way of life for us and a part of our organisation culture. As on March 31 2017, the people strength of J.K Cement is 2,855.

### INTERNAL CONTROLS SYSTEM AND THEIR ADEQUACY

The company has well placed internal control system looking to the size scale and complexity of operations. The management of the company is responsible for ensuring that all Internal Financial control are adequate and were operating effectively. The company 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 pursuant to notification, issued by the Ministry of Corporate Affair dated 16th Feb, 2015 .We have adapted the IND AS from current fiscal for which we have deployed both in house and KPMG team to assess the nature of impacts on company financial disclosures, the whole process of conversion is closely monitored by our management and management has also entrusted faith on its dedicated team of persons.

Further, Internal Audit functions is 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 location, i.e. plant, marketing office & 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 are noticed same is brought to the knowledge of members of audit committee for corrective actions.