Sanghi Industries - *Continuously Evolving*

Company Specific

- Sanghi Industries manufactures and markets cement and cement products in domestic and export markets (Cement, Clinker and RMC).
- The company manufactures different types of Cements such as Ordinary Portland Cement (OPC), Portland Pozollana Cement (PPC) and Portland Slag Cement (PSC).
- One of the largest integrated cement plants in gujarat. This is a positive sign considering the current lag in securing approvals from GPCB to set up a cement plant in Gujarat.
- Sanghi Industries has a strategic location and fits well within the company's ecosystem.
- Grade A limestone reserves also provide a logistical edge.
- Advantage of being reliant on lignite as a fuel, as it reduces fuel costs and ability to change fuels during a period of price fluctuations.
- Currently 6.1 MTPA grinding capacity and 6.6MTPA clinker capacity which is under refurbishments, and will be running at full capacity by end of H2 FY25. Will increase to 7 MTPA.
- 130 MW captive Thermal power plant and 13MW waste heat recovery system.
- Plans to run existing kilns at full capacity and add two more kilns of 4 million tons each in the future (capex for a total of 8M).
- Repayment of Inter corporate deposits (ICD) to Ambuja (@8%) to improve financial structure and move towards a higher credit rating.
- Fundraise commitment announcement of Rs 2200 Cr.
- Rating upgrade from D to AAA, post capital infusion from holding company, which improved its short and medium term working capital needs.
- Adani acquired at an EV of Rs5185Crs, currently at an EV of ~Rs4150Crs.
- Part of inorganic growth strategy to increase market share to 20% by FY28.

Master Supply Agreement With Ambuja and ACC

to 19.1%. The Master Supply Agreement volume stood at 3.4 million tons against 2.4 million tons, an increase of 42%. You have to further look at the Master Supply Agreements which the companies have entered with Sanghi and for the quarter, Sanghi to Ambuja was 4.2 lakh tons and Sanghi to ACC was 2.5 and that itself is additional volume gain which has come in from these MSAs.

Optimum Utilization of Plant Installed Capacity:	The above arrangement under MSA is anticipated to substantially improve the capacity utilization, **expected to be around 80%** (in contrast, it was below 25% in past).

- Sanghi Industries volumes stood at 3.4 MTPA (+42% YoY against 2.4 MTPA) in FY24 under MSA (Master Supply Agreement).

- Targeted to achieve 5 million tons from Sanghi in FY25 with an EBITDA margin of approximately 9%.

Industry

- Between FY12 and FY23, the installed capacity grew by 61% to 570 MT from 353 MT in FY22. The Indian cement sector's capacity is expected to expand at a compound annual growth rate (CAGR) of 4-5% over the four year period up to the end of FY27. It would thus begin the 2028 financial year at 715-725 MT/ year in installed capacity.
- Cement is pure logistical play in regional terms. And Freight and Fuel Cost take away a good chunk of profitability.

> ***"Gaining even Rs1-2/bag of cost efficiencies at production level is a very tedious and herculean task but wiping off even Rs10-20/bag (or even higher) of profits by indulging in supply-chain inefficiencies is a matter of fraction of seconds but unfortunately, that is not being attended to!"***
>
> ***-Anonymous***

- *" India is the world's second-largest producer of cement in the world, and almost all large players have been rapidly adding capacities as they look to capture the continued growth in demand expected over the next few years." - J. M. Baxi & Co*
- The overall cement industry in the country is likely to add 150-160 million tonnes of capacity in five years, as per CRISIL. In the last five years, cement-makers have added close to 120 million tonnes of capacity, taking the country's total to around 600 million tonnes. More consolidation is on the cards for the cement sector.
- In 2023, the market size of India's cement industry reached 3.96 billion tonnes and is expected to touch 5.99 billion tonnes by 2032, exhibiting a CAGR of 4.7% during 2024-32.

Key Numbers **:**

Narration	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Sales	**281**	**355**	**339**	**230**	**134**	**226**	**167**	**181**	**189**	**285**
% Growth YOY					*-52%*	*-36%*	*-51%*	*-21%*	*41%*	*26%*
Expenses	239	311	320	232	152	238	263	209	212	226
Operating Profit	**42**	**44**	**19**	**-2**	**-18**	**-13**	**-96**	**-28**	**-23**	**59**
Other Income	4	2	6	12	1	1	4	95	-58	-10
Depreciation	16	17	24	23	23	23	24	27	31	25
Interest	20	20	45	46	77	70	73	78	90	42
Profit before tax	10	9	-44	-59	-118	-105	-189	-39	-201	-19
PBT Margin	*4%*	*3%*	*-13%*	*-26%*	*-88%*	*-46%*	*-114%*	*-21%*	*-106%*	*-7%*
% Growth YOY					*-1272%*	*-1276%*	*331%*	*-34%*	*71%*	*-82%*
Tax	3	3	-11	-15	26	-	-	-	0	-
Net profit	**8**	**6**	**-33**	**-44**	**-144**	**-105**	**-189**	**-39**	**-202**	**-19**
% Growth YOY					*-2009%*	*-1754%*	*476%*	*-12%*	*40%*	*-82%*
OPM	*15%*	*12%*	*6%*	*-1%*	*-13%*	*-6%*	*-58%*	*-15%*	*-12%*	*21%*

- Sharp recovery in sales post MSA, currently stands at 285 Cr.
- This is at pre-Optimal Capacity Utilization target of 80% for FY25.
- Losses have greatly reduced from -202Cr to -9 Cr, indicating operational efficiency.
- Reduction in Interest Expense. (post working capital aid from parent co)
- Improvement in OPM% from negative to 21%.

Key Positive triggers for valuation rerating

- Change in ownership aiding in repayments of entire external debt through the parent's fund.
- Revenue contribution from parent's end leading to higher capacity utilization and improvement of profitability. This also provides visibility in the turnaround of SANGHIIND.
- Aid from parent co in near and medium term Working capital needs which inturn contributes to better financial position.

Advance payment with Purchase Order	Under MSA, **SIL will receive monthly advance payment** for all the orders **which in turn will help for meeting its working capital requirements to ensure smooth functioning and improve capacity utilization**.

- The previously commissioned capexes by previous promoters were met with financial difficulties and had been turning into a much larger burden than expected, until the co was acquired and working capital and CWIP needs were taken care of when capital was infused.

Optimum Utilization of Plant Installed Capacity:	The above arrangement under MSA is anticipated to substantially improve the capacity utilization, **expected to be around 80%** (in contrast, it was below 25% in past).

to us. Therefore, we reiterate, adding a large capacity is the least challenge we foresee, and that does not scare us, but the bigger contest would always be to ensure that we sell our products in the right markets with the best possible acceptable retentions and margins.

- Sanghi might actually be at an inflection point both operationally and financially, with both increased capacity and much faster financial turnaround.

SNGI is currently where Shree was at the beginning of its Ras unit advantage playing out: SNGI's entry to Adani Cement is a story that is yet to play-out while Shree Cement's Ras unit advantage has already played out. SNGI's potential at Sanghipuram is still unexplored, and also this site offers much larger scalability potential, which is why when it plays out, it will do what Ras unit did for Shree Cement or even better than that! There are more reasons as well, which we will discuss later in this note.

Benefits as per ACL :

Highlights / Benefits:

✓ Reduction in financial complexity w.r.t. terms of delivery, opening of letter of credits including delayed supply of coal and consistent quality issue.
✓ Availing superior and consistent quality of coal with efficient and improved logistics
✓ Savings in logistic cost as fly ash is available near to plant location
✓ Availing shared business services which is cost efficient and will provide administrative convenience.

Risks

- ACC-Ambuja will acquire clinker & cement in Bulk from Sanghi at a capped margin of 10%. (post inclusion of cost, but excluding interest and depreciation)

Pricing:	In view of above the pricing will be as under: **Manufacturing Plant's Cost of Production (Excluding Interest and Depreciation) of previous Quarter, plus 10% markup**. This will help in improving overall profitability of the company from negative EBITDA in the past to substantially positive EBITDA going forward. It will also ensure to meet all the financing requirements of the company, apart from investments required for improving plant efficiency, capacity and evacuation infrastructure.

- Additionally it is proposed to take from ACL unsecured loan by way of Inter CorporateDeposits of up to Rs. 500 Crore at 8% ROI. This can lead to higher than present interest cost, further reducing overall profitability.
- Going forward Sanghi will be reliant on parent co for revenues and capacity utilization.
- Cement sector as a whole is dependent upon Government initiatives and capex plans, and any change in it can directly affect the whole industry.
- Cement as a business is Cyclical.

Key monitorbles

- As with any Commodity business, fixed costs play a major role in overall profitability, and under or sub-par utilization can quickly lead to financial disaster.
- As Sanghi has its capex on the line, tracking the new capacity utilization, post commissioning is a must.
- It's now heavily reliant on parent co for revenues and capacity utilization, so tracking related party transactions is also a must.

Personal Take

The acquisition has brought both negative and positive pointers to the table for Sanghi investors. On one hand there is a visibility in revenues and increased capacity utilization. On the other hand margins have been capped at 10% (post costs and excluding interest and Depreciation). The situation as I see it should be looked at from the promoter's POV. Adani owns a much higher stake in Ambuja which stands at a much larger market capitalization than Sanghi. The incentive for Adani is to look out for greater interest in the case of Ambuja but also make sure Sanghi has a turn around. Adani Cements in this case brings experience and much higher consumptionary need for cement as a commodity. Sanghi surely has a visibility in revenue and capacity utilization terms, but we must also look out for its business efficiency as a whole. As the interest cost has risen a bit post ICD, and given fixed cost will also increase post commissioning of new capacity, unit economics should be carefully tracked. EBITDA/Tonne is a key metric in this case. Sanghi's acquisition is a strategic play in the cement industry and it will be an example for other players to make themselves efficient.