

21 May 2018

Star Cement

More subsidies, more repayment of debt; retain Buy

Holding on to strong ~23% market share in the north-east and the receipt of the ₹2.8bn subsidy would help Star Cements do well in coming quarters. Further capacities added outside this region would help the company gain through infrastructure emphasis in the NE and diversification. We are upbeat about the company's prospects and retain our Buy rating on the stock, with a price target of ₹178.

Retaining its market share. Enjoying premium pricing in its key region, a well-known brand with a ~23% market-share in the north east and adding new capacities in east India would further benefit the company. With ~75% of its sales coming from the retail segment, Star Cement is already a high operating-leverage player.

Better profitability expected. A huge rise in pet coke prices and FoR dispatches, reflected in the high fuel and freight costs, led to EBITDA/ton in Q4 FY18 falling 13% y/y, to ₹1,866. We expect the better operational performance to come on the estimated 11% CAGR over FY18-20, given the cost optimisation measures undertaken by the company.

Subsidies to lower debt. In FY19, the company has so far received ₹2.8bn subsidies (balance due: ₹4.3bn for FY19), compared to FY18's ₹3.1bn. With this subsidy, it intends to repay debt. We expect the debt to come down to ₹1.3bn by FY20.

Valuations. With debt shrinking due to the subsidy receipts and better volume growth expected in coming years, we revise our target price to ₹178 and maintain our Buy recommendation on the stock, which trades at an FY20e EV/EBITDA of 8.5x and an EV/ton of \$157. **Risk.** Rising coal prices.

Key Financials(YE Mar)	FY16	FY17	FY18	FY19e	FY20e
Sales (₹ m)	17,095	15,278	16,145	19,920	24,756
Net profit (₹ m)	1,346	1,947	3,307	2,543	3,288
EPS (₹)	3.2	4.6	7.9	6.1	7.8
PE (x)	35.7	30.2	16.6	21.6	16.7
EV / EBITDA (x)	14.5	16.3	11.4	10.2	8.5
EV / ton (\$)	231	269	240	226	157
RoE (%)	16.1	18.3	25.6	16.5	18.4
RoCE (%)	11.9	14.4	21.9	18.1	21.4
Dividend yield (%)	0.5	-	0.9	0.7	0.9
Net debt / equity (x)	0.8	0.7	0.3	0.1	-0.0

Source: Company, Anand Rathi Research

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Rating: **Buy**

Target Price: ₹178

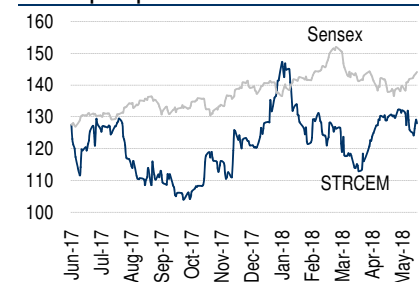
Share Price: ₹131

Key data	STRCEM IN
52-week high / low	₹152 / 102
Sensex / Nifty	34848 / 10596
3-m average volume	\$0.2m
Market cap	₹54bn / \$843m
Shares outstanding	419m

Shareholding pattern (%)	Mar'18	Dec'17	Sep'17
Promoters	68.9	73.3	74.6
- of which, Pledged	42.8	40.3	39.5
Free float	31.1	26.8	25.4
- Foreign institutions	1.9	2.0	0.4
- Domestic institutions	7.3	2.7	1.6
- Public	21.9	22.1	23.4

Estimates revision (%)	FY19e	FY20e
Sales	(10.8)	(6.6)
EBITDA	(0.1)	3.4
PAT	(0.2)	5.0

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
Sales Volume (m tons)	2.6	2.8	2.4	2.7	3.2
Net revenues	17,095	15,278	16,145	19,920	24,756
Growth (%)	19.8	-10.6	5.7	23.4	24.3
Direct costs	3,455	3,403	2,697	3,286	4,109
SG&A	9,701	7,792	8,235	11,123	14,193
EBITDA	3,938	4,083	5,214	5,511	6,454
EBITDA margins (%)	23.0	26.7	32.3	27.7	26.1
- Depreciation	1,715	1,179	1,207	1,500	1,500
Other income	69	24	44	62	62
Interest expenses	834	781	525	589	539
PBT	1,458	2,148	3,526	3,483	4,477
Effective tax rate (%)	4.10	6.47	4.65	25.00	25.00
+ Associates / (minorities)	53	62	55	70	70
Net income	1,340	1,947	3,307	2,543	3,288
Adjusted income	1,346	1,947	3,307	2,543	3,288
WANS	419	419	419	419	419
FDEPS (₹ / sh)	3.2	4.6	7.9	6.1	7.8
FDEPS growth(%)	-14.5	44.7	69.8	-23.1	29.3

Fig 3 – Cash-flow statement (₹ m)

Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
PBT	1,458	2,148	3,526	3,483	4,477
+ Non-cash items	1,715	1,179	1,207	1,500	1,500
Oper. prof. before WC	3,173	3,327	4,733	4,983	5,977
- Incr. / (decr.) in WC	2,651	-1,705	375	-1,639	851
Others incl. taxes	29	139	164	871	1,119
Operating cash-flow	493	4,894	4,194	5,751	4,007
- Capex (tang. + intang.)	707	679	231	2,000	2,000
Free cash-flow	-213	4,215	3,964	3,751	2,007
Acquisitions					
- Div. (incl. buyback & taxes)	222	-	590	459	590
+ Equity raised	197	-	0	-0	-
+ Debt raised	593	-1,303	-3,405	-3,042	-328
- Fin investments	-	-1	-0	2	-
- Misc. (CFI + CFF)	321	2,949	-29	-	-
Net cash-flow	34	-37	-3	248	1,090

Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 2 – Balance sheet (₹ m)

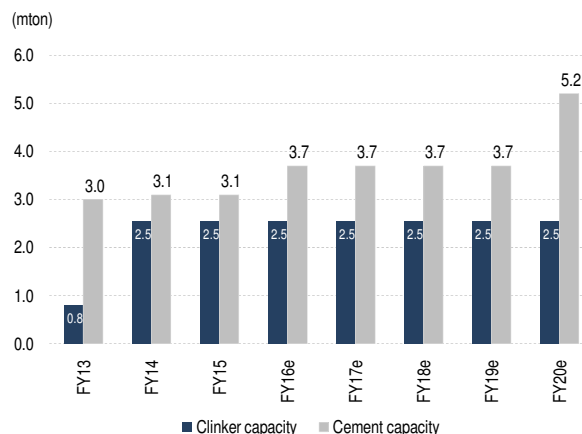
Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
Share capital	419	419	419	419	419
Net worth	10,553	11,460	14,769	16,853	19,551
Total debt	9,398	8,095	4,690	1,648	1,321
Minority interest	530	566	621	691	761
DTL / (assets)	117	-1,765	-2,329	-2,329	-2,329
Capital employed	20,599	18,355	17,751	16,863	19,303
Net tangible assets	9,190	8,631	7,845	8,203	9,103
Net intangible assets	2	2	2	2	2
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	490	549	357	500	100
Investments (strategic)	15	15	14	17	17
Investments (financial)	-	-	-	-	-
Current assets (ex cash)	14,725	13,641	14,311	13,207	15,396
Cash	238	201	198	446	1,536
Current liabilities	4,060	4,682	4,977	5,512	6,850
Working capital	10,665	8,959	9,334	7,695	8,546
Capital deployed	20,599	18,355	17,751	16,863	19,303
Contingent liabilities	191	299	-	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
P/E (x)	35.7	30.2	16.6	21.6	16.7
EV / EBITDA (x)	14.5	16.3	11.4	10.2	8.5
EV / sales (x)	3.3	4.4	3.7	2.8	2.2
P/B (x)	4.6	5.1	3.7	3.3	2.8
RoE (%)	16.1	18.3	25.6	16.5	18.4
RoCE (%) - after tax	11.9	14.4	21.9	18.1	21.4
DPS (₹ / sh)	0.5	-	1.2	0.9	1.2
Dividend payout (%) - incl. DDT	16.5	-	17.9	18.0	17.9
Net debt / equity (x)	0.9	0.7	0.3	0.1	-0.0
WC days	199	234	207	156	120
EV / ton (\$)	231	269	240	226	157
NSR / ton (₹)	6,018	5,518	7,065	7,418	7,789
EBITDA / ton (₹)	1,386	1,453	2,281	1,990	1,932
Volumes (m tons)	2.6	2.8	2.4	2.7	3.2
CFO: PAT(%)	36.7	251.3	126.8	226.2	121.9

Source: Company, Anand Rathi Research

Fig 6 – Cement (incl. hired) and clinker capacity



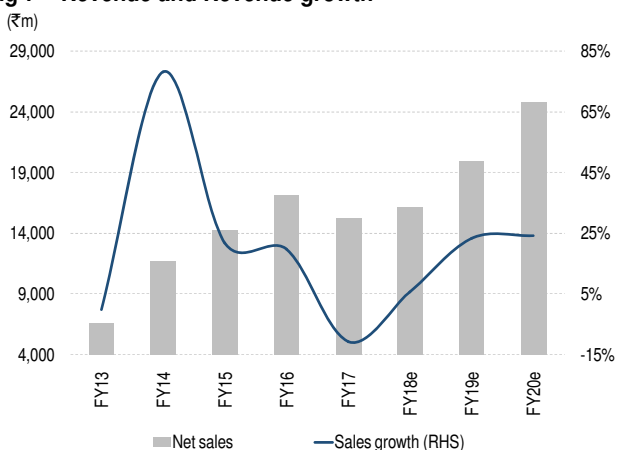
Source: Company

Other key highlights

Revenue growth

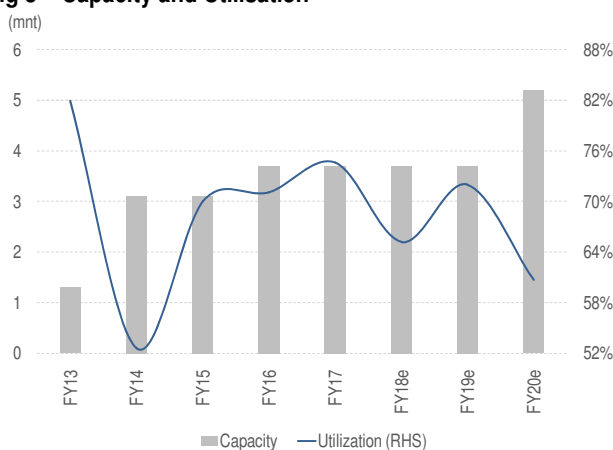
A good 8-8.5% growth in volumes, along with a pickup in demand and better pricing in the north-east, led to the 8% y/y rise in realisations in Q4 FY18 to ₹6,355 a ton. Volumes during the quarter grew a slight 1% y/y to 0.74m tons. Revenue rose 10% y/y to ₹5.2bn. We expect a 24% CAGR in revenue over FY18-20, boosted by a 14% CAGR in volumes, as the company expects an 8-9% growth in volumes and demand in FY19.

Fig 7 – Revenue and Revenue growth



Source: Company, Anand Rathi Research

Fig 8 – Capacity and Utilisation

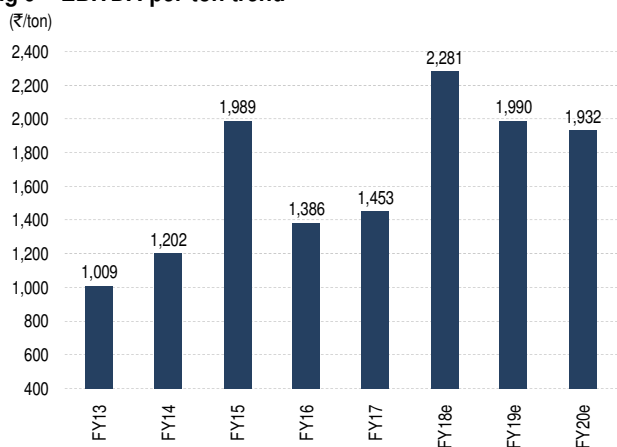


Source: Company, Anand Rathi Research

Operating performance

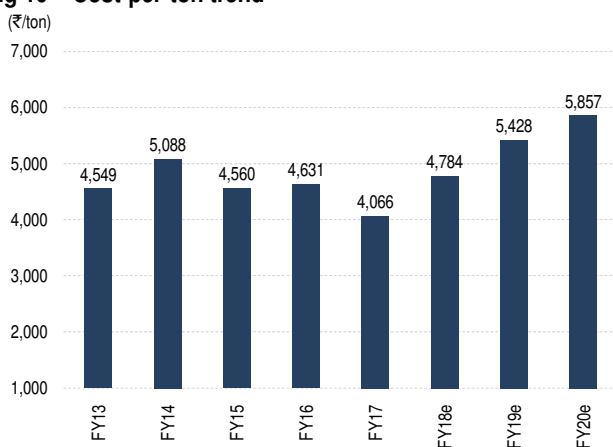
The EBITDA/ton for the quarter slipped 13% y/y, mainly due to the huge, 50% y/y, increase in other expenses, driven by the 38% y/y rise in power & fuel costs and the 101% y/y rise in freight costs. Freight cost increased due to withdrawal of the freight subsidy from Jan'18 and the shift to FoR sales. The huge increase in depreciation cost and in other income (respectively 97% and 42% y/y) led to a 14% y/y fall in PAT, to ₹1bn.

Fig 9 – EBITDA-per-ton trend



Source: Company, Anand Rathi Research

Fig 10 – Cost-per-ton trend



Source: Company, Anand Rathi Research

Result Highlights

Fig 11 – Quarterly performance (₹ m)

	FY18				FY17			
	Q4	Q3	Q2	Q1	Q4	FY18	FY19e	FY20e
Sales	5,274	3,774	2,810	4,287	4,792	16,145	19,920	24,756
EBITDA	1,444	1,413	770	1,586	1,693	5,214	5,511	6,454
EBITDA margins (%)	27.4	37.4	27.4	37.0	35.3	32.3	27.7	26.1
EBITDA per ton (₹)	1,866	2,142	1,629	2,415	2,135	2,281	1,990	1,932
Interest	89	137	141	157	184	525	589	539
Depreciation	241	337	326	303	122	1,207	1,500	1,500
Other income	28	2	9	4	20	44	62	62
PBT	1,143	942	311	1,130	1,407	3,526	3,483	4,477
Tax	54	28	49	33	127	164	871	1,119
PAT	1,088	914	262	1,097	1,280	3,362	2,613	3,358

Source: Anand Rathi Research

Fig 12 – Per-ton analysis

(₹ per ton)	FY18				FY17			
	Q4	Q3	Q2	Q1	Q4	FY18	FY19e	FY20e
Realization	6,355	5,484	6,029	7,234	5,870	7,065	7,418	7,789
EBITDA	1,866	2,142	1,629	2,415	2,135	2,281	1,990	1,932
Sales volumes (m tons)	0.7	0.6	0.4	0.6	0.8	2.4	2.7	3.2
Costs								
Raw material	744	862	817	1,107	1,005	881	1,271	1,334
Purchase of traded goods	220	199	126	253	240	206	-	-
Staff cost	331	443	624	459	384	445	434	455
Other expenses	3,868	2,551	2,543	2,606	2,545	2,969	3,742	4,042

Source: Anand Rathi Research

Change in estimates

Factoring in the Q4 FY18 performance, we have lowered our FY19 and FY20 estimates: revenue by 10.8% and 6.6% respectively. We lower our FY19e EBITDA and PAT 0.1% and 0.2% respectively and increase FY20e EBITDA and PAT 3.4% and 5%. With debt coming down due to the subsidy receipts and the better volume growth expected in coming years, we expect Star Cement to post a better operating performance.

Fig 13 – Change in estimates

	New		Old		Variance	
	FY19e	FY20e	FY19e	FY20e	% chg	% chg
Sales (₹ m)	19,920	24,756	22,340	26,502	(10.8)	(6.6)
EBITDA (₹ m)	5,511	6,454	5,517	6,244	(0.1)	3.4
PAT (₹ m)	2,542	3,288	2,547	3,130	(0.2)	5.0

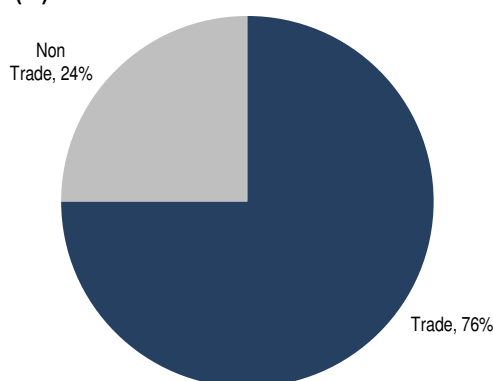
Source: Anand Rathi Research

Concall Highlights

Operational and Financial highlights

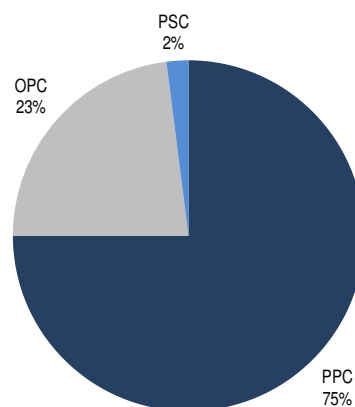
- Sales volume in the north-east were 0.55m tons (0.5m a year ago), stepping up 1% y/y.
- The company sold 67,000 tons of clinker in the quarter (42,000 a year ago).
- The trade and non-trade sales-mix for the quarter was 75:25.
- The PPC-OPC-PSC cement mix in Q4 FY18 was 75:23:2.
- Debt in Mar'18 was ₹4.25bn and is expected to come down to ₹1.45bn.

Fig 14 – Sales mix (%)



Source: Company

Fig 15 – OPC-PPC-PSC mix



Source: Anand Rathi Research

Subsidy

- Management expects ₹4.3bn in subsidies in FY19/20, compared to ₹7.1bn in FY18.
- It received ₹800m in Apr'18 and ₹2bn in May'18 as subsidy.

Capex / Capacity expansion

- The company plans expansion at Silligudi, with total capacity of 1.5m-2m tons in the next fifteen months at ₹3bn-3.5bn capex.

- Its clinker capacity in the north-east is being de-bottlenecked, increasing capacity to 3m tons (from 2.6m), expected to be complete by Q1 FY19 at an estimated ₹500m.
- Capex estimated by the company for FY19 and FY20 is ₹4bn, whereas ₹2bn is expected to be spent in FY19.

Volumes, demand and capacity utilisation

- The company expects ~8-10% volume growth in FY19.
- The FY17 volume mix would be: north east 60-65%, others 35-40%.
- Capacity utilised during the quarter was 90%.
- The power utilisation rate during the quarter was ~80%.

Others

- For the coming quarter, ~7-9% growth in demand is expected.
- Fly-ash prices in Guhawati rose during the quarter to ₹1,600 a ton.

Valuations

At the ruling price, the stock trades at an EV/EBITDA of 8.5x and an EV/ton of \$157. We maintain our Buy recommendation on it, with a revised price target of ₹178.

Fig 16 – 12-month-forward EV/EBITDA: Mean and Standard deviation



Source: Bloomberg

Fig 17 – Peer comparison - Valuations

	CMP (₹)	P / E		EV / EBITDA		EV / ton (\$)	
		FY19e	FY20e	FY19e	FY20e	FY19e	FY20e
Star Cement	131	21.0	16.3	10.2	8.5	226	157
JK Lakshmi	382	24.2	14.1	11.2	8.1	79	74
Birla Corp.	731	25.3	17.7	8.7	7.4	86	82
Dalmia Bharat	2,735	24.7	20.2	11.1	9.2	150	139
Deccan Cement	480	12.8	10.6	6.1	4.8	42.2	38.4
Heidelberg Cement	143	18.5	13.7	9.2	7.0	94	87
India Cement	129	15.8	11.8	6.9	6.0	64	63
JK Cement	958	18.5	17.8	10.1	10.0	115	93
Mangalam Cement	270	19.1	13.0	8.9	6.5	42	38
NCL Indus	207	11.5	8.2	6.4	4.8	56	50
Orient Cement	120	21.5	16.0	8.8	7.5	70	70
Ramco Cement	807	28.9	24.4	17.1	14.4	223	216
Sagar Cement	882	17.4	9.9	8.9	5.5	75	48
Sanghi Industries	100	31.7	23.6	14.5	14.7	110	125

Source: Bloomberg

Risk

- Higher coal prices

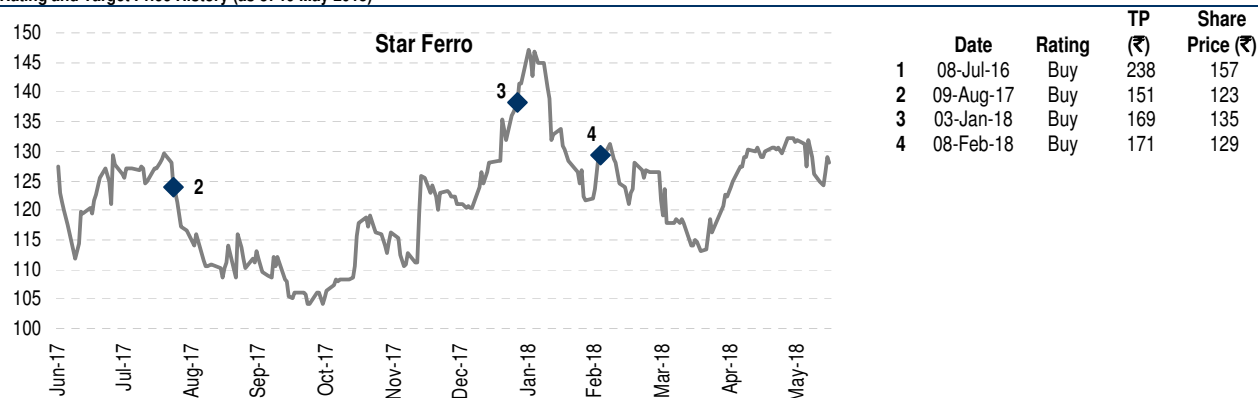
Appendix

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