

## Star Cement (STACEM)

₹ 124

### Star Cement the new entity...

Star Ferro & Cement (SFCL) have announced the reverse merger of Star Ferro & Cement with Star Cement (SCL) on August 1, 2016. Under this scheme, Star Ferro & Cement shareholders have received 1.33 shares of Star Cement for every share held. Consequently, Star Ferro & Cement now stands dissolved and Star Cement is the new entity. The merger will help the promoter gain listing benefits as previously the promoter shares were privately held. Hence, this represents the true holding of promoters i.e. 74.9% from 64.4%. Further, the reverse merger of Star Ferro & Cement with Star Cement will lead to 90.0% dilution in equity (i.e. from 22.2 crore shares to 41.9 crore shares) leading to a significant increase in market capitalisation. Although the NER region offers a good growth opportunity we believe the current valuation of \$238/t factors in most of the positives.

#### Improving market share, increased government spend to drive growth...

SCL is the largest cement player in the north-east region (NER) with over 27% market share. Demand growth in this region has consistently remained higher than growth at the pan-India level. With the government's thrust on infrastructure development, demand growth in NER is expected to grow at 10% CAGR in the next few years. This coupled with improving market share in NER region and expansion in eastern region is expected to drive revenue at 19.8% CAGR in FY17-19E.

#### ...but policy uncertainty key concern

EBITDA margins have declined from 30.4% in FY15 to 23.7% in FY17 mainly due to an increase in coal cost, higher freight and RM cost. Over the next two years, we expect cost pressures to continue to make it difficult for the company to regain 30% in operating margins. Further, the various benefits (like capital investment subsidy, interest subsidy on working capital and transport subsidy) that the company enjoys under the NE industrial policy (NEIIPP 2007) will expire in 2018. Consequently, we expect EBITDA margins to further fall to 21.1% in FY19E.

#### Receipt of subsidy key trigger

The company is entitled to receive ~₹ 700 crore of subsidy from the government. However, the receipt of subsidy has been delayed resulting in increased debt. The company received ₹ 86 crore subsidy till May 2017. It expects to receive ~₹ 250 crore by FY18E and rest by FY19E. We believe the receipt of subsidy could help make the company debt free (FY17 debt was at ₹ 657.6 crore) and act as a key trigger for the company.

#### Discontinuance of transport subsidy, equity dilution a key concern

SCL's utilisation has improved from 44.1% in FY13 to over 71% in FY17 led by robust demand in the North-East region (NER). Cement demand in NER is expected to grow at a CAGR of 10% over the next two or three years led by a pick-up in infrastructure activity. Higher cement demand coupled with limited capacity addition in the NER is expected to significantly benefit SFCL (a dominant player in the North East). However, discontinuance of transport subsidy beyond FY18E and margin pressure remain key concerns. Further, the reverse merger of Star Ferro & Cement with Star Cement will lead to 90% dilution in equity (i.e. from 22.2 crore shares to 41.9 crore shares) leading to a significant increase in market capitalisation. Based on an EV/tonne of \$230/t, we have arrived at a target price of ₹ 115 per share (i.e. FY19E EV/EBITDA of 10x). We have a **HOLD** recommendation on the stock.

#### Rating Matrix

Rating	: Hold
Target	: ₹ 115
Target Period	: 12-15 Months
Potential Upside	: -9%

#### What's Changed?

Target	Unchanged
EPS FY18E	Unchanged
EPS FY19E	Unchanged
Rating	Unchanged

#### Key Financials

₹ crore	FY16	FY17	FY18E	FY19E
Net Sales	1,715.0	1,728.0	2,276.3	2,480.6
EBITDA	399.4	408.8	558.3	522.1
Net Profit	134.0	171.6	283.5	235.3
EPS (₹)	3.2	4.1	6.8	5.6

#### Valuation Summary

	FY16	FY17	FY18E	FY19E
P/E	38.8	30.3	18.3	22.1
Target P/E	36.0	28.1	17.0	20.5
EV / EBITDA	14.8	14.3	10.2	10.8
EV / Tonne	250.1	246.4	241.1	237.7
Price/Book value	4.9	4.2	3.6	3.2
RoCE	12.3	13.8	19.4	16.1
RoNW	12.7	14.0	19.4	14.3

#### Stock Data

Market Capitalization	₹ 5198.1 Crore
Total Debt (FY17)	₹ 657.6 Crore
Cash and Investments (FY17)	₹ 20.1 Crore
EV	₹ 5835.6 Crore
52 week H/L	132 / 118
Equity capital	₹ 41.9 Crore
Face value	₹ 1

#### Price Chart\*

\* Star Cement was listed on June 16, 2017. Hence, there is no history for price comparison

#### Research Analysts

Rashesh Shah  
rashesh.shah@icicisecurities.com

Devang Bhatt  
devang.bhatt@icicisecurities.com

### Reverse merger of SFCL in Star Cement to simplify holding structure

The board has approved a reverse merger of Star Ferro & Cement with Star Cement. Under this scheme Star Ferro & Cement shareholders have received 1.33 shares of Star Cement for every share held. Consequently, Star Ferro & Cement now stands dissolved and Star Cement is the new entity. The merger will help the promoter gain listing benefits as previously the promoter shares were privately held. Hence, this represents the true holding of promoters i.e. 74.9% from 64.4%.

#### Exhibit 1: Pre-merger promoter holding of company

Pre-merger holding in Star Ferro & Cement		
SFCL	Number of shares	% Holding
Promoter	143,123,840.2	64.4
Others	79,049,149.8	35.6
<b>Total</b>	<b>222,172,990.0</b>	<b>100.0</b>

Pre-merger holding in Star Cement		
SCL	Number of shares	% Holding
SFCL	295,475,000.0	70.5
Promoters	123,673,559.9	29.5
Public	65,360.0	0.0
<b>Total</b>	<b>419,213,920.0</b>	<b>100.0</b>

Pre-merger effective promoter holding	
SCL	% Holding
Promoter Shr SFCL	45.4
Promoter	29.5
<b>Total</b>	<b>74.9</b>

Source: Company, ICICIdirect.com Research

Under the merger, every shareholder of SFCL will receive 1.33 shares of SCL for every share held. Hence, the number of shares will increase from 22.2 crore shares to 29.5 crore shares. Further, considering 12.4 crore shares of promoters in SCL the overall shares in SCL is expected to reach 41.92 crore

#### Exhibit 2: Post merger shareholding pattern

SCL	Number of shares	% Holding
Promoter	314,028,267.3	74.9
Others	105,135,369.3	25.1
Public	65,360.1	0.0
<b>Total</b>	<b>419,228,996.7</b>	<b>100.0</b>

Source: Company, ICICIdirect.com Research

## Financial summary

Profit and loss statement		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Total operating Income	1,715.0	1,728.0	2,276.3	2,480.6	
Growth (%)	19.9	0.8	31.7	9.0	
Raw material cost	363.1	426.5	521.9	552.2	
Inc/dec in stock	-17.6	-12.1	0.0	0.0	
Employees cost	107.8	118.5	177.5	187.8	
Others	862.3	786.3	1018.6	1218.6	
Total Operating Exp.	1,315.6	1,319.2	1,718.0	1,958.6	
EBITDA	399.4	408.8	558.3	522.1	
Growth (%)	-8.2	2.4	36.6	-6.5	
Depreciation	171.5	141.2	152.8	167.1	
Interest	83.4	78.0	63.0	53.5	
Other Income	6.9	2.2	2.4	2.6	
PBT	151.4	191.8	344.9	304.2	
Total Tax	6.0	14.3	51.7	60.8	
PAT	134.0	171.6	283.5	235.3	
Growth (%)	60.7	28.0	65.1	-17.0	
Adjusted EPS (₹)	3.2	4.1	6.8	5.6	

Source: Company, ICICIdirect.com Research

Cash flow statement		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Profit after Tax	134.0	171.6	283.5	235.3	
Add: Depreciation	171.5	141.2	152.8	167.1	
(Inc)/dec in Current Assets	-372.5	-62.0	-182.0	-152.9	
Inc/(dec) in CL and Provisions	183.2	-12.6	118.5	70.5	
CF from operating activities	116.3	238.2	372.8	320.0	
(Inc)/dec in Investments	0.0	-0.1	0.0	0.0	
(Inc)/dec in Fixed Assets	-70.7	-91.2	-145.1	-145.0	
Others	-257.1	17.9	9.7	8.0	
CF from investing activities	-327.7	-73.4	-135.5	-137.0	
Issue/(Buy back) of Equity	19.7	0.0	0.0	0.0	
Inc/(dec) in loan funds	57.3	-91.5	-100.0	-80.0	
Dividend paid & dividend tax	-25.9	0.0	-49.0	-49.0	
Inc/(dec) in Sec. premium	247.2	1.0	0.0	0.0	
Others	-83.4	-78.0	-63.0	-53.5	
CF from financing activities	215.0	-168.4	-212.1	-182.5	
Net Cash flow	3.5	-3.7	25.2	0.5	
Opening Cash	20.3	23.8	20.1	45.3	
Closing Cash	23.8	20.1	45.3	45.8	

Source: Company, ICICIdirect.com Research

Balance sheet		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
<b>Liabilities</b>					
Equity Capital	41.9	41.9	41.9	41.9	
Reserve and Surplus	1,013.4	1,186.1	1,420.5	1,606.7	
Total Shareholders funds	1,055.3	1,228.0	1,462.4	1,648.6	
Total Debt	749.1	657.6	557.6	477.6	
Deferred Tax Liability	107.6	119.6	119.6	119.6	
Minority Interest / Others	53.0	58.9	68.6	76.6	
Total Liabilities	1,965.0	2,064.1	2,208.2	2,322.5	
<b>Assets</b>					
Gross Block	1,725.1	1,810.4	2,010.4	2,155.4	
Less: Acc Depreciation	805.9	947.1	1,100.0	1,267.0	
Net Block	919.1	863.2	910.4	888.3	
Capital WIP	49.0	54.9	0.0	0.0	
Total Fixed Assets	968.1	918.1	910.4	888.3	
Investments	1.5	1.7	1.7	1.7	
Inventory	209.2	161.2	212.6	231.7	
Debtors	448.8	399.5	526.6	573.9	
Loans and Advances	813.6	973.1	953.2	1,038.7	
Other Current Assets	0.5	0.3	23.7	24.7	
Cash	23.8	20.1	45.3	45.8	
Total Current Assets	1,495.9	1,554.2	1,761.5	1,914.8	
Creditors	140.4	93.8	123.7	134.8	
Provisions	360.5	316.5	342.0	348.0	
Total Current Liabilities	500.9	410.3	465.7	482.8	
Net Current Assets	995.0	1,143.9	1,295.7	1,432.1	
Others Assets	0.0	0.0	0.0	0.0	
Application of Funds	1,964.6	2,063.7	2,207.8	2,322.1	

Source: Company, ICICIdirect.com Research

Key ratios					
(Year-end March)	FY16	FY17	FY18E	FY19E	
<b>Per share data (₹)</b>					
EPS	3.2	4.1	6.8	5.6	
Cash EPS	7.3	7.5	10.4	9.6	
BV	25.2	29.3	34.9	39.3	
DPS	1.0	0.0	1.0	0.0	
Cash Per Share	0.6	0.5	1.1	1.1	
<b>Operating Ratios (%)</b>					
EBITDA Margin	23.4	23.7	24.6	21.1	
PBT / Total Operating income	8.5	11.1	15.2	12.3	
PAT Margin	7.8	10.0	12.5	9.5	
Inventory days	44.7	34.2	34.2	34.2	
Debtor days	95.8	84.7	84.7	84.7	
Creditor days	30.0	19.9	19.9	19.9	
<b>Return Ratios (%)</b>					
RoE	12.7	14.0	19.4	14.3	
RoCE	12.3	13.8	19.4	16.1	
RoIC	12.0	13.5	18.7	15.6	
<b>Valuation Ratios (x)</b>					
P/E	38.8	30.3	18.3	22.1	
EV / EBITDA	14.8	14.3	10.2	10.8	
EV / Net Sales	3.5	3.4	2.5	2.3	
Market Cap / Sales	3.0	3.0	2.3	2.1	
Price to Book Value	4.9	4.2	3.6	3.2	
<b>Solvency Ratios</b>					
Debt/EBITDA	1.9	1.6	1.0	0.9	
Debt / Equity	0.7	0.5	0.4	0.3	
Current Ratio	3.0	3.8	3.8	4.0	
Quick Ratio	2.6	3.4	3.3	3.5	

Source: Company, ICICIdirect.com Research

## ICICIdirect.com coverage universe (Cement)

Company	CMP		Rating	M Cap (₹ Cr)	EPS (₹)			EV/EBITDA (x)			EV/Tonne (\$)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)			FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E
ACC*	1651	1850	Buy	31,029	35.6	63.7	67.5	23.6	15.8	14.0	162	139	136	6.9	11.4	11.5	7.7	12.7	12.4
Ambuja Cement*	240	280	Buy	47,656	4.9	6.4	6.9	28.7	22.6	19.9	170	165	165	3.8	7.1	7.9	5.1	6.5	6.8
UltraTech Cem	4,036	4750	Buy	110,748	86.4	95.8	118.9	22.0	22.0	19.0	259	257	254	12.3	14.1	14.8	11.0	12.4	12.8
Shree Cement	17,514	17800	Hold	60,949	385	510	563	26.1	19.2	16.6	375	358	344	12.3	15.9	16.2	17.4	19.0	17.6
Heidelberg Cem	131	145	Buy	2,969	3.4	5.8	7.2	15.3	11.4	10.0	118	114	111	8.2	12.4	14.5	7.9	12.6	14.6
India Cement	219	245	Buy	6,728	5.4	8.6	11.7	11.2	10.1	8.8	104	102	99	7.5	8.4	9.5	3.3	4.9	6.4
JK Cement	987	1265	Buy	6,902	37.1	47.9	55.2	14.2	11.9	10.4	131	126	115	12.6	14.5	15.9	14.5	15.3	15.4
JK Lakshmi Cem	490	525	Hold	5,767	7.0	13.1	20.2	20.2	14.0	11.1	105	95	88	7.5	10.9	13.8	5.9	10.1	13.6
Mangalam Cem	372	425	Buy	993	12.9	28.2	35.2	11.4	7.3	6.2	54	50	49	10.9	17.3	18.9	6.8	13.1	14.2
SFCL	124	115	Hold	5,198	4.1	6.8	5.6	14.3	10.2	10.8	246	241	238	13.8	19.4	16.1	14.0	19.4	14.3

Source: Company, ICICIdirect.com Research

## **RATING RATIONALE**

ICICIdirect.com endeavours to provide objective opinions and recommendations. ICICIdirect.com assigns ratings to its stocks according to their notional target price vs. current market price and then categorises them as Strong Buy, Buy, Hold and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock.

Strong Buy: > 15%/20% for large caps/midcaps, respectively, with high conviction;  
Buy: > 10%/15% for large caps/midcaps, respectively;  
Hold: Up to +/-10%;  
Sell: -10% or more;



**Pankaj Pandey**

**Head – Research**

**pankaj.pandey@icicisecurities.com**

**ICICIdirect.com Research Desk,  
ICICI Securities Limited,  
1st Floor, Akruiti Trade Centre,  
Road No 7, MIDC,  
Andheri (East)  
Mumbai – 400 093  
research@icicidirect.com**

## ANALYST CERTIFICATION

We /I, Rashesh Shah, CA, and Devang Bhatt, PGDBM Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

### Terms & conditions and other disclosures:

ICICI Securities Limited (ICICI Securities) is a full-service, integrated investment banking and is, inter alia, engaged in the business of stock brokering and distribution of financial products. ICICI Securities Limited is a Sebi registered Research Analyst with Sebi Registration Number – INH000000990. ICICI Securities is a wholly-owned subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on [www.icicibank.com](http://www.icicibank.com).

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities generally prohibits its analysts, persons reporting to analysts and their relatives from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we would endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the companies mentioned in the report in the past twelve months.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its associates or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts and their relatives have any material conflict of interest at the time of publication of this report.

It is confirmed that Rashesh Shah, CA, and Devang Bhatt, PGDBM Research Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts or their relatives do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities are engaged in various financial service businesses, they might have financial interests or beneficial ownership in various companies including the subject company/companies mentioned in this report.

It is confirmed that Rashesh Shah, CA, and Devang Bhatt, PGDBM Research Analysts do not serve as an officer, director or employee of the companies mentioned in the report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor ICICI Securities have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on ICICI Securities by any Regulatory Authority impacting Equity Research Analysis activities.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ICICI Securities and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.