

Regional shift impacts performance; Maintain Buy

Star Cement (STRCEM) operating performance was impacted in 3QFY20 as the company shifted focus towards eastern region (29% of sales versus 24% in 3QFY19). This impacted the realisation that slide 6% while volume grew by 16% to 0.79mn tonnes that kept the revenue growth steady at 8% to Rs4.5bn. Additionally, the cost/tonne inflated by 5% YoY due to the fuel shift from domestic coal to imported coal. Lower realisations and inflated cost hit the EBITDA margins that fell to 20.9% from 29.3% in 3QFY19 and the EBITDA decreased 23% to Rs940mn. Effectively the EBITDA/tn slipped to Rs1,250 versus Rs1,864 YoY. The PAT fell was ~13% YoY to Rs712mn from Rs823mn aided by higher other income of Rs65mn (Rs10mn in 3QFY19). STRCEM shift towards eastern region to de-risk single region presence will check the EBITDA margins. This with the higher cost (contributed by the fuel cost) will stay for next couple of quarters as STRCEM shifts to imported coal from domestic coal as dominant fuel. Factoring the same we revise our FY21e earnings to Rs7.7 (earlier Rs8.7) while we retain FY20 earnings. We have introduced FY22 earnings with an EPS estimate of Rs8.3. We retain our BUY rating on the stock and revise our target price to Rs103 (earlier Rs114) valuing the stock at the replacement cost of Rs7.5bn (earlier 10% premium) due to the earnings impact in the short term following the regional diversification. The stock trades at 8.0x EV/EBITDA at our revised earnings estimates.

Healthy volume growth; realisation take a hit as focus shifts to eastern region

Volume grew by 16% YoY at ~ 0.79mn tonnes driven by higher sales in the eastern region. The clinker external sales were 33000 tonnes and lease unit sales were at 37,000 tonnes. The core north-eastern region contributed 71% (77% in 2QFY20) of the total volume and the eastern region sales were 27% (23% in 2QFY20) of the total dispatches in 3QFY20. The regional shift however hit the realisations that fell by 6% YoY to Rs5,718/tn (9% fall QoQ).

Cost escalation further hits EBITDA margin

Operating costs inflated ~5% YoY at Rs4,527/tn contributed by energy and raw material cost escalation. This was largely due to shift in the fuel mix from domestic coal to imported coal (Rs100/150 per tonne) as local coal availability continues to be scarce. STRCEM is shifting to relatively lower cost fuel (pet coke) that will help savings in FY21. Raw material cost was also higher in 3QFY20. These impact largely offset the benefit of lower logistics and other expenditure. Weaker realisation and cost increase impacted the EBITDA that fell by 23% YoY to Rs940mn and EBITDA margins weakened to 20.8% from 29.3% in 3QFY19.

Earnings Revised:

We have revised our FY21e earnings to Rs7.7 (earlier Rs8.7) while we retain FY20 earnings factoring the impact on realisations and the higher cost inflation. We have introduced FY22 earnings with an EPS estimate of Rs8.3 factoring 16% volume jump to account for the commissioning of the grinding unit in Siliguri (West Bengal). However, we have kept realisation flat with marginal 1.5% rise over FY21 (assumed flat realisation over FY20). We will revisit the earnings in case of realisation gains of faster cost controls by STRCEM.

Valuation and Ratings: Maintain Buy

We retain our BUY rating on the stock however with a revised target price of Rs103 (earlier 114) valuing the stock at the replacement cost of Rs7.5bn (earlier 10% premium) based on FY22 capacities. Despite its leadership position in the North-east markets, relatively better earnings visibility and healthy balance sheet we feel the earnings in the short term will be impacted due to the regional shift. The stock trades at 8.0x EV/EBITDA at our revised earnings estimates. We will keenly watch STRCEM's performance and revisit our earnings and rating on the stock accordingly.

Financial and valuation summary

YE Mar (Rs mn)	3QFY20	3QFY19	YoY %	2QFY20	QoQ %	FY19	FY20E	FY21E	FY22E
Revenue	4,512	4,164	8.3	3,825	18.0	18,310	19,572	21,662	25,047
EBITDA	940	1,219	(22.9)	644	46.0	4,492	3,976	4,615	5,245
EBITDA marg.(%)	20.8	29.3	-845bps	16.8	400bps	24.5	20.3	21.3	20.9
Adj. PAT	712	823	(13.5)	446	59.6	2,988	2,888	3,241	3,477
Diluted EPS	1.7	2.0	(13.5)	1.1	59.6	7.1	6.9	7.7	8.3
P/E(x)						12.6	13.1	11.6	10.9
EV/EBITDA(x)						8.1	7.8	6.4	6.9
RoE (%)						17.9	15.3	15.4	14.8

Source: Company, Centrum Research estimates

Please see Appendix for analyst certifications and all other important disclosures. In the interest of timeliness, this document is not edited.

Result Update

India I Cement

7 February 2020

Buy

Target Price: Rs103

Price: Rs88

Forecast return: 17%

Institutional Research

Market Data

Bloomberg:	STRCEM IN
52 week H/L:	Rs140/82
Market cap:	Rs36bn
Shares outstanding:	412mn
Free float:	11.2%
Avg. daily vol. 3mth:	240350

Source: Bloomberg

Changes in the report

Rating:	No change
Target price:	To Rs103 from Rs114
EPS:	No change – FY20; (11.3)% - FY21

Source: Centrum Research estimates

Star Cement relative to Nifty Midcap 100



Source: Bloomberg

Shareholding pattern

	Dec-19	Sep-19	Jun-19	Mar-19
Promoter	67.1	67.9	67.9	68.0
FIs	0.3	0.8	1.1	1.2
DIs	8.2	8.4	8.6	8.7
Public/others	24.5	22.9	22.4	22.1

Source: BSE

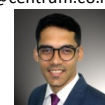


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The Metals & Cement Team

Thesis Snapshot

Estimate revisions

YE Mar (Rs mn)	FY20E New	FY20E Old	% chg	FY21E New	FY21E Old	% chg	FY22E
Net Sales	19,572	19,572	0.0	21,662	21,878	(1.0)	25,047
EBITDA	3,976	3,976	0.0	4,615	5,127	(10.0)	5,245
EBITDA margin (%)	20.3	20.3	0.0	21.3	23.4	(9.1)	20.9
Net profit	2,888	2,888	0.0	3,241	3,656	(11.3)	3,477
Diluted EPS (Rs)	6.9	6.9	0.0	7.7	8.7	(11.3)	8.3

Source: Centrum Research estimates

Centrum estimates vs Actual results

YE Mar (Rs bn)	Actual 3QFY20	Centrum 3QFY20	Variance (%)
Revenue	4,512	4,516	0
EBITDA	940	839	12
EBITDA margin (%)	20.8	18.6	226bps
Adj. PAT	712	584	22
Diluted EPS	1.7	1.4	22

Source: Centrum Research estimates

Star Cement versus Nifty Midcap 100

	1m	6m	1 year
STRCEM IN	(2.4)	(10.8)	0.9
Nifty Midcap 100	7.9	17.1	9.0

Source: Bloomberg, NSE

Key Assumptions

	FY18	FY19	FY20E	FY21E	FY22E
Cement Capacity(mn MT)	3.44	3.44	5.44	5.44	5.44
Sales Volume(mn MT)	2.61	2.88	3.11	3.44	3.94
YoY change - %	(7.5)	10.5	8.1	10.6	14.5
Utilisation - %	76%	84%	57%	63%	72%

Per tonne data(in
Rs/mMT)

	FY18	FY19	FY20E	FY21E	FY22E
Cement Realisation	5,917	6,077	6,016	6,046	6,137
YoY change - %	15.7	2.7	-1.0	0.5	1.5
Power & fuel	785	859	880	942	970
Freight cost	1,052	1,205	1,217	1,253	1,291
Operating cost	3,970	4,586	4,620	4,732	4,883
EBITDA/tonne	2,001	1,560	1,277	1,341	1,331

Source: Company, Centrum Research estimates

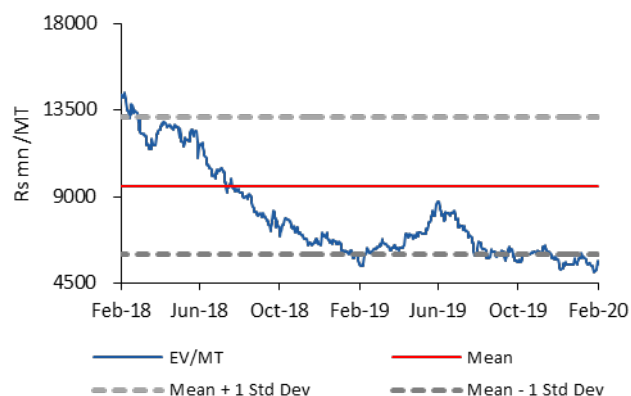
Valuations

We retain our BUY rating on the stock however with a revised target price of Rs103 (earlier 114) valuing the stock at the replacement cost of Rs7.5bn (earlier 10% premium) based on FY22 capacities. Despite its leadership position in the North-east markets, relatively better earnings visibility and healthy balance sheet we feel the earnings in the short term will be impacted due to new regional shift. The stock trades at 8.0x EV/EBITDA at our revised earnings estimates.

Target Valuations

Target Replacement Cost (\$)	108
Currency Assumption (Rs/\$)	70
Target Replacement Cost (Rs)	7,560
Total Capacity (Mn Tonnes)	5.4
Target EV (Rs mn)	41,962
Total Net Debt (Rs mn)	(1,355)
Target M-cap (Rs mn)	43,317
Total Equity Shares O/S (mn)	419.2
Target Price (Rs)	103

1-year forward EV/MT



1-year forward EV/EBITDA



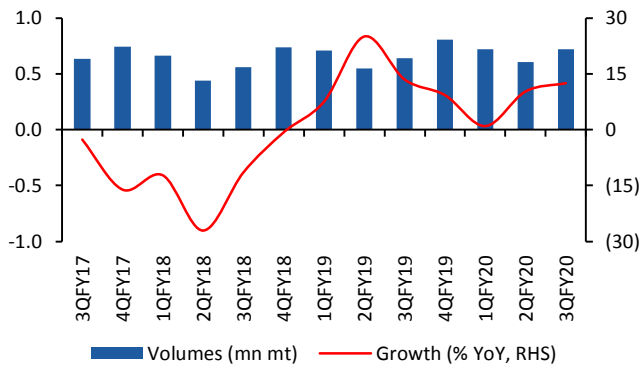
Source: Bloomberg, Centrum Research estimates

Peer comparison

Company	Mkt Cap Rs mn	CAGR FY19-FY21E (%)			EBITDA Margin(%)			EV/EBITDA (x)			EV/t (Rs mn/t)	RoE (%)			ROCE (%)		
		Rev	EBIDTA	PAT	FY19	FY20E	FY21E	FY19	FY20E	FY21E		FY19	FY20E	FY21E			
Star Cement	37,728	8.8	1.4	4.2	24.5	20.3	21.3	8.1	7.8	6.4	5748	17.9	15.3	15.4	19.1	18.5	18.6
Heidelberg Cement	44,995	6.8	10.0	13.7	22.7	24.0	24.1	9.8	8.4	7.7	8471	19.9	20.5	19.1	24.9	24.7	23.5
Orient Cement	37,728	8.8	1.4	4.2	24.5	20.3	21.3	8.1	7.8	6.4	5748	18.0	14.0	14.4	19.1	18.5	18.6

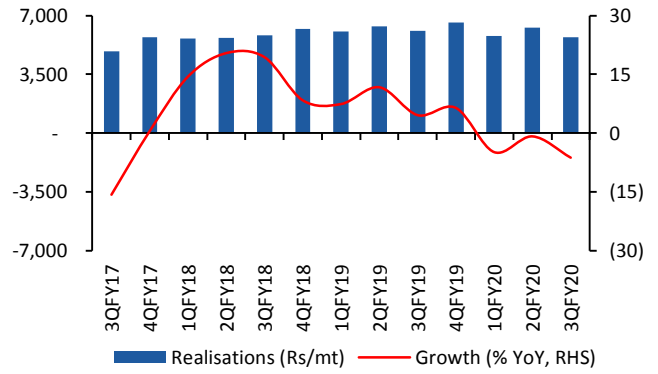
Source: Company, Centrum Research estimates

Fig 1: Regional shift helps volume growth



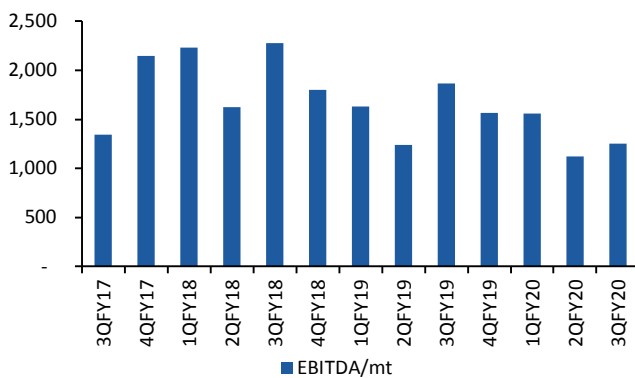
Source: Company, Centrum Research

Fig 2: Realisations impact due to eastern diversification



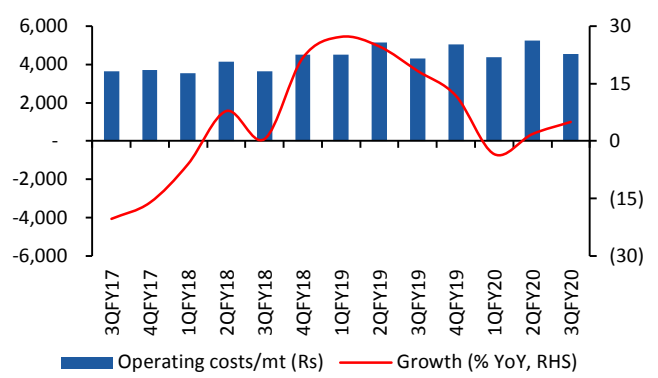
Source: Company, Centrum Research

Fig 3: EBITDA/tn weakens as realisation weakens cost inflates



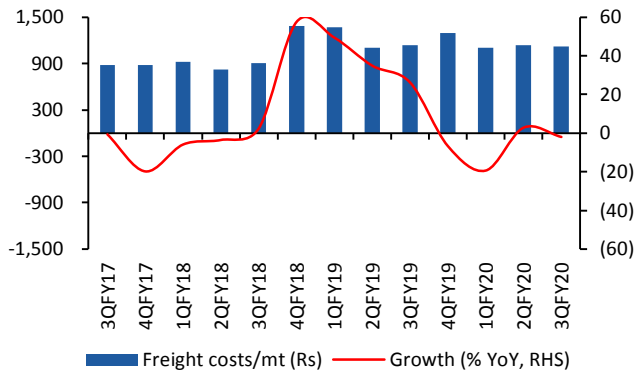
Source: Company, Centrum Research

Fig 4: Higher energy cost offsets other cost benefits



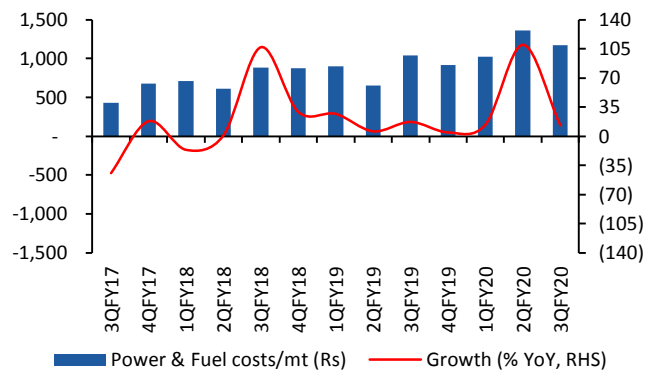
Source: Company, Centrum Research

Fig 5: Lower fuel cost helps lower logistic cost



Source: Company, Centrum Research

Fig 6: Shift to imported coal leads to higher energy cost



Source: Company, Centrum Research

Centrum Con-call Monitor

Centrum Quarterly monitor	3QFY20	2QFY20	Our Views
Capacity addition	Siliguri grinding unit will now be commissioned by March 2020. Company has still not received the EC for Meghalaya clinker plant.	Siliguri grinding unit to be commissioned by January 2020. Debottlenecking of Meghalaya clinker completed in 2QFY20. Company has still not received the EC for 2mnt clinker plant in Meghalaya.	Siliguri grinding unit postponed by a quarter. Meghalaya clinkerisation unit further delayed and will be commissioned in FY2023.
Volume and EBITDA/t guidance	Company expects North east market to grow 8-9% and East markets to grow 5-6% in FY20. Volumes: No change in guidance EBITDA/t guidance: ~Rs1400/tn for FY20	Volumes: Double digit growth in FY20 Maintains guidance on EBITDA/t in FY20	Sustenance of price hikes taken in January will uplift the EBITDA/tn for the year. Volume growth toned down.
Subsidies	Outstanding transport subsidy is ~Rs500mn	Outstanding transport subsidy is ~Rs500mn	Most of the subsidy payments likely to be cleared in FY20.
Cost saving initiatives	Company is using predominantly imported coal for its energy requirements. Sourcing of pet-coke in North East region is not feasible for the company. Imported coal is ~85% and the rest is sourced from domestic sources. WHRP to be commissioned with the new clinker plant	Shift to pet-coke (mix of imported and domestic) to bring energy cost to normalised level WHRP to be commissioned with the new clinker plant	Utilisation of the coal reserves in North Meghalaya to start in ~2-3quarters after the modalities are worked out by NGT and Coal India. These reserves will last for 3 years and reduce fuel cost for the Star India. Major cost savings initiatives are unlikely in FY20/FY21.
Cash	Cash: Rs4.7bn (31st Dec'19)	Cash: Rs3.66bn (30th Sept'19)	
Capital expenditure	Meghalaya Clinker project: Rs1bn spend in 9MFY20. Total capex: Rs11bn	Siliguri project: Rs2.25bn spend in 1HFY20. Total: Rs3.5bn for FY20	Capex guidance unchanged for FY20/FY21.

Source: Company, Centrum Research

Quarterly financial analysis

Fig 7: Quarterly financials

(Rs mn)	3QFY20	3QFY19	YoY %	2QFY20	QoQ %	3QFY20E	Deviation %
Net Sales	4,512	4,164	8.3	3,825	18.0	4,516	(0.1)
Expenditure							
Change in stock	(79)	(313)		44		31	
Raw material	872	828	5.4	727	20.1	985	(11.4)
purchased products	196	155	26.3	137	43.3	170	15.4
Power & fuel	925	708	30.7	827	11.8	813	13.8
Freight	880	778	13.2	690	27.7	818	7.6
Employee costs	324	300	7.9	293	10.4	335	(3.3)
Other exp	453	489	(7.3)	464	(2.3)	525	(13.7)
Total Operating Expenses	3,572	2,945	21.3	3,181	12.3	3,677	(2.9)
EBITDA	940	1,219	(22.9)	644	46.0	839	12.0
EBITDA margin (%)	20.8	29.3	-845bps	16.8	400bps	18.6	226bps
Other Income	65	10	520.4	77	(15.4)	70	(7.0)
Interest	38	26	47.4	8	398.5	30	27.8
Depreciation	232	264	(12.2)	225	3.1	230	1.0
PBT	734	939	(21.8)	487	50.6	649	13.2
Non-recurring items	-	-		-		-	
PBT (after non recurring items)	734	939	(21.8)	487	50.6	649	13.2
Tax	22	102	(78.4)	34	(35.5)	65	(66.0)
Tax Rate (%)	3	11		7		10	
Reported PAT	712	823	(13.5)	446	59.6	584	21.9
Adjusted PAT	712	823	(13.5)	446	59.6	584	21.9
NPM (%)	16	20	-398bps	12	412bps	13	285bps
Adjusted EPS (Rs)	1.7	2.0	(13.5)	1.1	59.6	1.4	21.9

Source: Company, Centrum Research estimates

P&L					
YE Mar (Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
Revenues	16,291	18,310	19,572	21,662	25,047
Materials cost	3,025	4,367	5,233	5,288	5,968
% of revenues	18.6	23.9	26.7	24.4	23.8
Power & fuel	2,160	2,587	2,863	3,374	3,959
% of revenues	13.3	14.1	14.6	15.6	15.8
Others	5,747	6,864	7,499	8,385	9,875
% of revenues	35.3	37.5	38.3	38.7	39.4
EBITDA	5,359	4,492	3,976	4,615	5,245
EBITDA margin (%)	32.9	24.5	20.3	21.3	20.9
Depreciation & Amortisation	1,207	1,056	944	884	1,087
EBIT	4,152	3,435	3,032	3,731	4,158
Interest expenses	525	144	100	80	207
Other income	44	55	350	350	450
Exceptional items	-	-	-	-	-
PBT	3,672	3,346	3,282	4,001	4,401
Taxes	164	296	328	680	836
Effective tax rate (%)	4	9	10	17	19
PAT	3,507	3,050	2,954	3,321	3,565
Minority/Associates	(55)	(62)	(66)	(80)	(88)
Extraordinary Items	-	-	-	-	-
Reported PAT	3,452	2,988	2,888	3,241	3,477
Adjusted PAT	3,452	2,988	2,888	3,241	3,477

Ratios					
YE Mar	FY18	FY19	FY20E	FY21E	FY22E
Growth Ratio (%)					
Revenue	6.2	12.4	6.9	10.7	15.6
EBITDA	29.3	(16.2)	(11.5)	16.1	13.6
Adjusted PAT	71.8	(13.5)	(3.3)	12.2	7.3
Margin Ratios (%)					
Operating	32.9	24.5	20.3	21.3	20.9
EBITDA	32.9	24.5	20.3	21.3	20.9
Adjusted PAT	21.2	16.3	14.8	15.0	13.9
Return Ratios (%)					
ROE	25.2	17.9	15.3	15.4	14.8
ROCE	22.5	19.1	18.5	18.6	17.1
ROIC	22.5	20.2	22.8	29.4	21.4
Turnover Ratios (days)					
Gross block turnover ratio (x)	1.6	1.7	1.5	1.4	1.3
Debtors	33	29	37	37	37
Inventory	66	55	47	44	44
Creditors	42	25	35	35	35
Cash conversion cycle	56	59	49	45	45
Solvency Ratio (x)					
Net debt-equity	0.3	(0.1)	(0.3)	(0.4)	(0.1)
Debt-equity	0.3	0.0	0.0	0.0	0.1
Interest coverage ratio	7.9	23.9	30.3	46.6	20.1
Gross debt/EBITDA	0.8	0.2	0.0	0.0	0.4
Current Ratio	2.7	2.6	2.0	2.1	1.4
Per share Ratios (Rs)					
Adjusted EPS	8.2	7.1	6.9	7.7	8.3
BVPS	35.2	41.1	45.7	51.0	59.2
CEPS	11.1	9.6	9.1	9.8	10.9
DPS	1.0	-	2.0	2.0	2.0
Dividend payout %	14	-	34	30	28
Valuation (x)*					
P/E (adjusted)	14.6	12.6	13.1	11.6	10.9
P/BV	3.4	2.2	2.0	1.8	1.5
EV/EBITDA	10.2	8.1	7.8	6.4	6.9
Dividend yield %	1.1	0.0	2.2	2.2	2.2

Source: Company, Centrum Research estimates

Balance Sheet					
YE Mar (Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
Equity Share Capital	419	419	419	419	419
Reserves & surplus	14,344	16,817	18,719	20,973	23,464
Shareholders' fund	14,763	17,237	19,138	21,393	23,883
Total Debt (incl. pref shares if its thr)	4,324	738	13	11	2,300
Def tax liab. (net)	(2,329)	(2,710)	(2,874)	(2,874)	(2,874)
Minority interest	621	683	749	829	917
Total Liabilities	17,380	15,947	17,026	19,357	24,225
Gross Block	10,556	10,961	15,261	15,761	23,761
Less: Acc. Depreciation	(2,709)	(3,738)	(4,682)	(5,566)	(6,653)
Net Block	7,847	7,223	10,579	10,195	17,108
Capital WIP	357	743	(957)	1,043	2,543
Net Fixed Assets	8,205	7,966	9,622	11,238	19,651
Investments	26	1,181	1,181	1,181	1,181
Inventories	2,946	2,772	2,544	2,599	3,006
Sundry debtors	1,465	1,438	1,957	2,166	2,505
Cash	186	949	4,581	6,097	2,491
Loans & Advances	132	288	331	380	438
Other assets	9,768	5,664	2,771	2,294	2,585
Total Current Asset	14,497	11,111	12,185	13,537	11,023
Trade payables	1,889	1,254	1,877	2,077	2,402
Other current Liab.	3,405	2,992	4,022	4,451	5,147
Provisions	54	65	64	71	82
Net Current Assets	9,149	6,800	6,222	6,938	3,393
Total Assets	17,380	15,947	17,026	19,357	24,225

Cash Flows					
YE Mar (Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
Operating profit bef working capital changes	4,969	4,375	4,226	4,885	5,488
Trade and other receivables	(87)	27	(520)	(209)	(338)
Trade payables	575	(1,049)	1,653	630	1,020
Net change - WC	(91)	3,112	4,210	800	(61)
Direct Taxes	(728)	(678)	(492)	(680)	(836)
Cash flow from operations	4,150	6,809	7,944	5,005	4,591
Net Capex	(322)	(790)	(2,600)	(2,500)	(9,500)
Acquisitions, net	-	-	-	-	-
Others	27	(1,155)	-	-	-
Cash flow from investing activities	(295)	(1,946)	(2,600)	(2,500)	(9,500)
FCF	3,855	4,863	5,344	2,505	-
Issue of share capital	-	-	-	-	-
Increase/(decrease) in debt	(3,683)	(3,586)	(725)	(3)	2,289
Dividend	(494)	-	(987)	(987)	(987)
Cash flow from financing	(3,832)	(4,101)	(1,712)	(989)	1,303
Net change in cash	23	762	3,632	1,516	(3,606)

Source: Company, Centrum Research estimates

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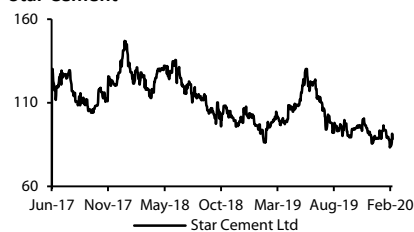
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Star Cement



Source: Bloomberg

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