Star Cement

BUY

Demand recovers!

We maintain BUY on Star Cement with a TP of Rs 135 (10x Sep'21E consol EBITDA), implying EV of USD 176/MT.

HIGHLIGHTS OF THE QUARTER

- During 2QFY20, Star reported mixed results. While demand uptick pushed up consolidated revenues by 6% YoY, NSR slide and elevated fuel cost pulled down EBITDA by 6% YoY. Despite this fall, PAT jumped 23% YoY, buoyed by rising cash balance and debt reduction.
- **Sales vol recovered to 9% YoY (-17% QoQ**) to 0.6 mn MT on demand recovery in the NE region and on market share gains across NE and outside regions. However, cement prices slid QoQ/YoY across all its markets, thus leading to 5% NSR decline YoY.
- **NSR slide and elevated fuel costs pull down EBITDA:** While Star's fixed costs fell 16% YoY on asset sweating, increased usage of imported coal/petcoke (amid local coal supply squeeze) moderated total op decline to 3% YoY. Thus, unitary EBITDA declined 14% YoY to Rs 1,067/MT, pulling down EBITDA. Other Income soared 10x YoY on rising cash surplus and Intt exp fell 77% on debt pay-off. These drove PAT rise despite EBITDA fall.
- **1HF20 performance summary:** Lower sales vol (-2% YoY), and NSR (-3%), amid stable opex pulled down revenue/EBITDA by 4/12%. However, higher income and lower capital charges led to 1% PAT growth.
- **Cashflows in 1HFY20**: STRCEM generated cash PAT of Rs 1.65bn, and released ~Rs 1.1bn in working capital (received Rs 1.8bn subsidy backlog). It spent ~Rs 1bn towards Siliguri expansion, and reduced its debt by ~Rs 0.3bn. Thus, cash balance/net cash increased by 74/130% to Rs 3.7/3.2bn respectively.
- **Capex outlook**: Star guided to start the Siliguri GU plant (2mn MT) in 4QFY20. It is awaiting environment clearances to start work on brown field clinker expansion in Meghalaya (2mn MT, expected to commission in 4QY22). Star will also add two WHRS units of 6-8 MW each in Meghalaya during FY21/22. A net cash balance sheet currently and healthy cashflow outlook should fund all these capex.

STANCE

We continue to like Star for its leadership positioning in the lucrative NE region, which will further enhance as Star ramps-up clinker capacity in NE region. Star's superior op margin should gain from increased local coal availability and cost reduction from upcoming WHRS. Star currently trades at a mere 7.1/7.1x FY21/22E EBITDA (EV of USD 125/MT). Maintain BUY with a revised TP of Rs 135.

Financial Summary (Consolidated)

Year Ending Mar (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	FY18	FY19	FY20E	FY21E	FY22E
Net Sales	3,825	3,623	*5.6*	4,609	*(17.0)*	16,145	18,310	18,363	20,517	22,947
EBITDA	644	687	*(6.3)*	1,121	*(42.6)*	5,214	4,492	4,260	4,991	5,594
APAT	446	364	*22.6*	839	*(46.8)*	3,307	2,988	3,089	3,595	4,196
Diluted EPS (Rs)	1.1	0.9	*22.6*	2.0	*(46.8)*	7.9	7.1	7.5	8.7	10.2
EV / EBITDA (x)						8.6	8.7	8.9	7.1	7.1
EV/MT (USD)						186	163	138	121	130
P/E (x)						12.1	13.4	12.9	11.1	9.5
RoE (%)						*24.1*	*17.9*	*16.7*	*17.7*	*18.2*

Source: Company, HDFC sec Inst Research

INDUSTRY	CEMENT
CMP *(as on 07 Nov 2019)*	**Rs 97**
Target Price	**Rs 135**
Nifty	12,012
Sensex	40,654

KEY STOCK DATA	
Bloomberg	STRCEM IN
No. of Shares (mn)	419
MCap (Rs bn) / ($ mn)	41/578
6m avg traded value (Rs mn)	16

STOCK PERFORMANCE (%)			
52 Week high / low			**Rs 140/85**
	3M	6M	12M
Absolute (%)	(1.1)	(8.0)	(4.4)
Relative (%)	(11.9)	(14.2)	(19.8)

SHAREHOLDING PATTERN (%)	**Mar-19**	**Jun-19**
Promoters	67.94	67.94
FIs & Local MFs	9.23	9.26
FPIs	1.05	0.75
Public & Others	21.78	22.05
Pledged Shares *	-	-

*Source : BSE *as % of total shares o/s*

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Demand recovery in the NE region and market share gains across NE & outside regions drove revenue growth

Lower pricing however pulled down EBITDA YoY

Other income soared on rise in cash surplus

Intt exp declined on debt reduction

Accelerated dep accounting drives YoY dep fall

Various tax incentives resulted in lower tax rate, despite of the fact that STRCEM has to pay MAT rate, which would eventually lead to a MAT credit pile up

Star's sales in the NE grew at 9% vs industry's growth of 6%. Outside the NE region, it grew at 10% versus industry's degrowth, thereby resulting in a gain in mkt share

Its fuel cost elevated on account of near term supply squeeze from the locally mined coal in Meghalaya

Consolidated Quarterly Financials' Snapshot

(Rs Mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	1HFY20	1HFY19	YoY (%)
Net Sales	**3,825**	**3,623**	***5.6***	**4,609**	***(17.0)***	**8,433**	**8,802**	***(4.2)***
Raw Materials	907	1,130	*(19.7)*	968	*(6.3)*	1,876	2,323	*(19.2)*
Power and Fuel	827	370	*123.3*	815	*1.5*	1,642	1,136	*44.6*
Transport	293	321	*(8.5)*	298	*(1.7)*	592	589	*0.5*
Employee	690	630	*9.4*	884	*(22.0)*	1,573	1,803	*(12.7)*
Other Exp	464	484	*(4.1)*	522	*(11.1)*	985	947	*4.0*
EBITDA	**644**	**687**	***(6.3)***	**1,121**	***(42.6)***	**1,765**	**2,004**	***(11.9)***
EBITDA margin (%)	*16.8*	*19.0*		*24.3*		*20.9*	*22.8*	
Depreciation	225	271	*(16.9)*	222	*1.6*	447	554	*(19.3)*
EBIT	**418**	**416**	***0.5***	**899**	***(53.5)***	**1,318**	**1,450**	***(9.1)***
Other Income (Including EO Items)	77	7	*1,069*	74	*5*	150	10	*1,414*
Interest Cost	8	33	*(76.5)*	28	*(72.3)*	35	87	*(59.3)*
PBT - Reported	**487**	**390**	***25.0***	**945**	***(48.4)***	**1,433**	**1,373**	***4.3***
Tax	34	8	*322.0*	106	*(67.8)*	140	76	*84.3*
Tax rate (%)	*7.0*	*2.1*		*11.2*		*9.8*	*5.5*	
(Minority Interest)/ Share of associates profit	(7)	(18)		-0		(7)	(30)	
RPAT	**446**	**364**	***22.6***	**839**	***(46.8)***	**1,285**	**1,267**	***1.4***
EO (Loss) / Profit (Net Of Tax)	-	-		-		-	-	
APAT	**446**	**364**	***22.6***	**839**	***(46.8)***	**1,285**	**1,267**	***1.4***
Adj PAT margin (%)	*11.7*	*10.0*		*18.2*		*15.2*	*14.4*	

Source: Company, HDFC sec Inst Research

Consolidated Quarterly Performance Analysis

	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	1HFY20	1HFY19	YoY (%)
External total sales vol (mn MT)	**0.60**	**0.56**	***8.5***	**0.73**	***(17.1)***	**1.33**	**1.36**	***(2.3)***
Total sales vol (includes clinker to on-lease units)	**0.64**	**0.57**	***11.3***	**0.77**	***(17.3)***	**1.41**	**1.43**	***(1.5)***
Rs/MT trend								
NSR	**6,014**	**6,342**	***(5.2)***	**5,993**	***0.3***	**6,002**	**6,173**	***(2.8)***
Raw materials	1,426	1,978	*(27.9)*	1,259	*13.3*	1,335	1,629	*(18.0)*
Power & fuel	1,300	648	*100.6*	1,060	*22.7*	1,169	797	*46.7*
Freight	1,084	1,103	*(1.7)*	1,149	*(5.7)*	1,120	1,265	*(11.4)*
Employee	461	562	*(17.8)*	388	*18.9*	421	413	*2.0*
Other Exp	729	847	*(13.9)*	678	*7.5*	701	664	*5.6*
Opex	3,114	2,599	*19.8*	2,888	*7.8*	2,990	2,725	*9.7*
EBITDA	**1,067**	**1,237**	***(13.7)***	**1,542**	***(30.8)***	**1,327**	**1,472**	***(9.8)***

Source: Company, HDFC sec Inst Research

We estimate an 8% volume CAGR in FY19-22E on demand recovery and on Siliguri expansions

We estimate Star's unitary EBITDA to recover to ~Rs 1500/MT levels during FY21-22E on increased utilisation and fuel cost stabilisation

We estimate capex spend of Rs 4/4.3/4.5bn towards the on-going expansions (2mn MT GU in Siliguri, 2.2 mn MT clinker expansions and 12-15 WHRS in Meghalaya) and towards annual maintenance capex

Consolidated Operational Trends and Assumptions

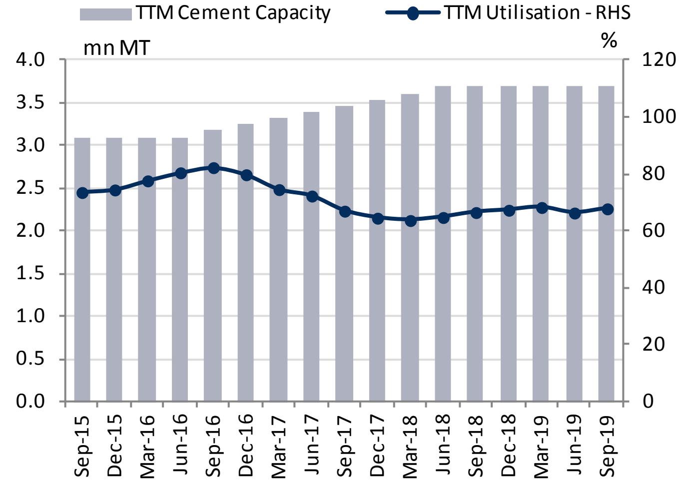
Particulars	FY16	FY17	FY18	FY19	FY20E	FY21E	FY22E
Cement Cap (mn MT)	**3.1**	**3.4**	**3.7**	**3.7**	**5.7**	**5.7**	**5.7**
Sales Volume (mn MT)	**2.8**	**2.8**	**2.6**	**2.9**	**2.9**	**3.3**	**3.6**
YoY change (%)	*17.0*	*2.1*	*(7.5)*	*9.8*	*2.1*	*12.8*	*9.8*
Utilisation (%)	*89.3*	*83.1*	*70.6*	*77.5*	*51.3*	*57.9*	*63.6*
(Rs/ MT trend)							
NSR	**5,345**	**5,112**	**5,864**	**6,098**	**6,008**	**6,103**	**6,225**
YoY change (%)	*(8.6)*	*(4.3)*	*14.7*	*4.0*	*(1.5)*	*1.6*	*2.0*
Raw material cost	1,169	1,134	1,099	1,455	1,200	1,224	1,248
Power and fuel cost	729	638	785	862	1,200	1,164	1,181
Transport cost	1,002	899	1,042	1,209	1,110	1,132	1,155
Employee cost	365	395	390	388	400	400	390
Other expenses	728	664	655	690	705	698	732
Total Opex	**3,993**	**3,731**	**3,970**	**4,602**	**4,615**	**4,618**	**4,707**
YoY change (%)	*(2.4)*	*(6.6)*	*6.4*	*15.9*	*0.3*	*0.1*	*1.9*
EBITDA per MT	**1,448**	**1,472**	**2,001**	**1,570**	**1,458**	**1,515**	**1,546**
YoY change (%)	*(21.5)*	*1.7*	*35.9*	*(21.5)*	*(7.1)*	*3.9*	*2.0*

Source: Company, HDFC sec Inst Research

We have plotted the trailing 12m (TTM) operational performance trends of Star Cement for the past five years

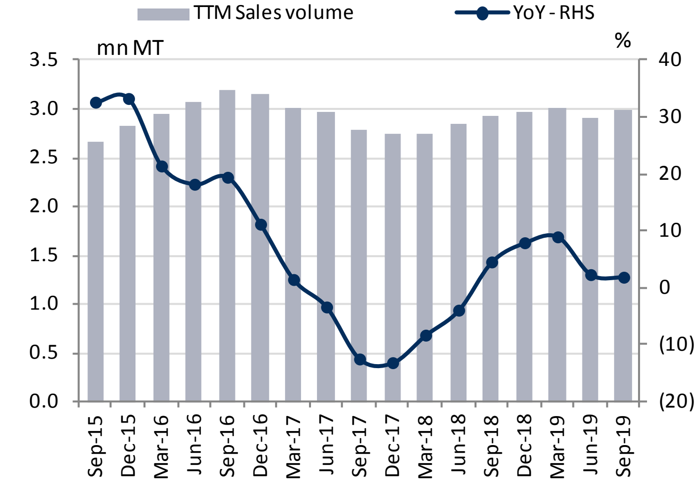
Long term performance trends

Star Cement's GU utilization continues to hover around 67% for past three years



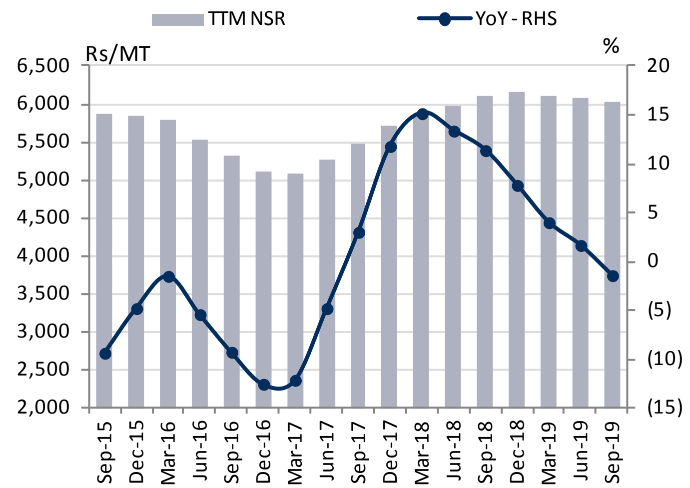
Source: Company, HDFC Sec Inst Research

Volume recovery in 2QFY20 kept TTM growth YoY in positive zone



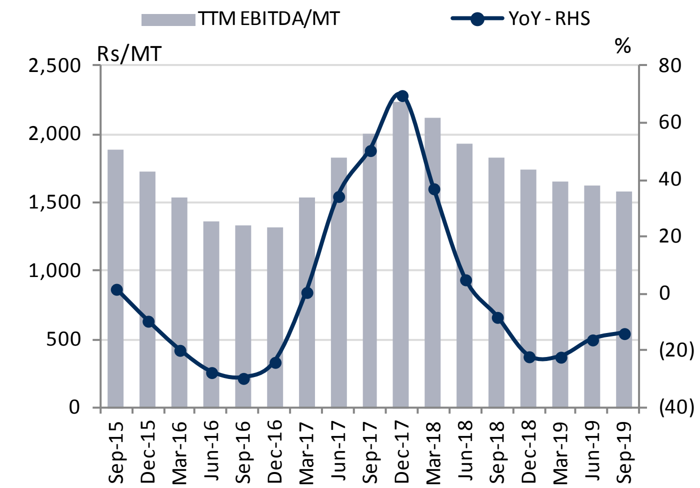
Source: Company, HDFC Sec Inst Research

NSR however is trending lower on sliding prices in the east



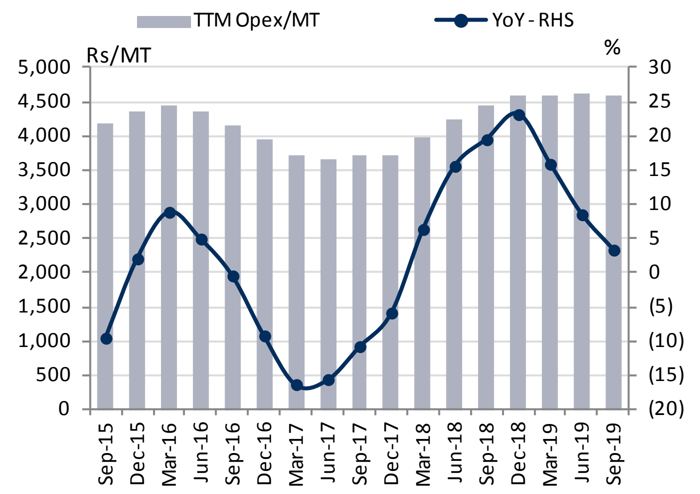
Source: Company, HDFC Sec Inst Research

Weak pricing and expiration of freight subsidy driving margin compression in the past 3- years



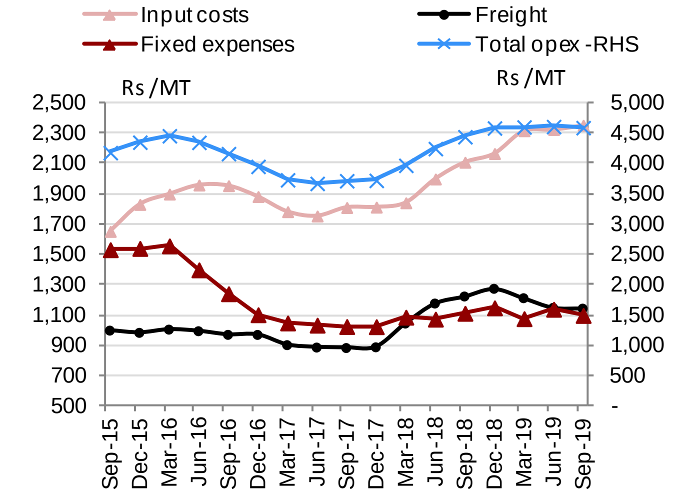
Source: Company, HDFC Sec Inst Research

Opex inflation is on the decline, thus moderating the impact of weak pricing



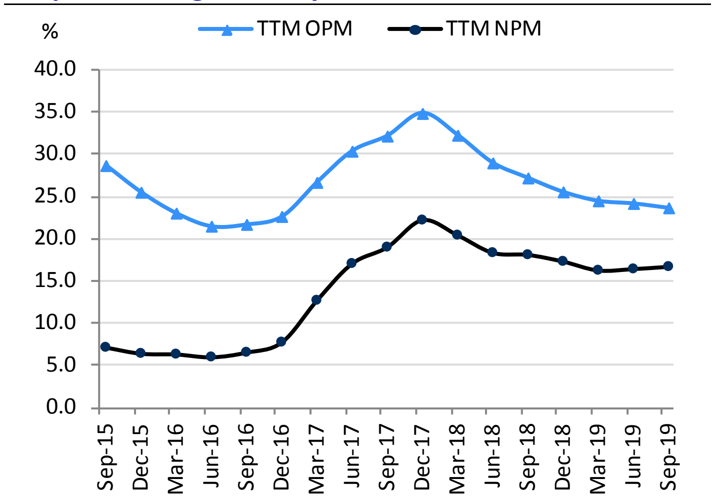
Source: Company, HDFC Sec Inst Research

Surge in input costs (freight subsidy expiration in 4QFY18 & higher fuel costs) impacting opex



Source: Company, HDFC Sec Inst Research

Op margin fell on sliding NSR; Debt decline, lower dep and rising treasury income boosts NPM



Source: Company, HDFC Sec Inst Research

We reduce our FY20/21E EBITDA est by 4/3% YoY to factor in lower sales volume

We also introduce FY22E estimates

Given that Star is generating industry leading margins/ return ratios and has a net cash balance sheet despite on-going expansions, the stock is trading at inexpensive valuations

Change in Estimates

Rs bn	FY20E Old	FY20E Revised	*Change %*	FY21E Old	FY21E Revised	*Change %*
Net Revenues	18.5	18.4	*(1.0)*	20.7	20.5	*(1.0)*
EBITDA	4.4	4.3	*(3.7)*	5.1	5.0	*(2.6)*
APAT	3.1	3.1	*(1.6)*	3.7	3.6	*(4.0)*
AEPS	7.5	7.5	*0.0*	7.1	7.1	*-*

Source: HDFC sec Inst Research

Peer Set Comparison

Company	Mcap (Rs bn)	CMP (Rs/sh)	Reco	TP	EV/EBITDA (x)			EV/MT (USD)			Net D:E (x)			RoE (%)		
					FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
UltraTech Cement	1,150.0	4,187	BUY	5,350	18.6	13.8	12.6	186	183	177	0.6	0.5	0.3	8.3	12.2	11.9
Shree Cement	698.2	20,041	NEU	20,000	25.3	18.1	15.9	259	244	227	0.0	(0.1)	(0.2)	13.5	16.9	16.4
Ambuja Cements	403.5	203	BUY	240	13.4	11.4	10.2	131	128	118	(0.7)	(0.7)	(0.7)	5.9	6.4	6.7
ACC	286.8	1,527	BUY	1,940	12.1	10.3	9.0	124	120	117	(0.3)	(0.4)	(0.4)	11.0	13.1	13.7
Ramco Cements	189.0	802	BUY	880	19.7	14.9	13.0	209	190	171	0.3	0.4	0.4	12.1	16.0	16.0
Dalmia Bharat	159.0	825	BUY	1,500	9.9	8.3	7.5	112	113	85	0.3	0.3	0.3	2.8	3.9	4.5
JK Cements	89.9	1,163	BUY	1,321	13.2	10.4	9.4	115	96	97	0.8	0.9	0.8	10.5	15.1	15.7
Star Cement	**41.0**	**97**	**BUY**	**135**	**8.9**	**8.9**	**7.1**	**166**	**138**	**121**	**(0.1)**	**(0.1)**	**(0.2)**	**17.9**	**16.7**	**17.7**
JK Lakshmi	36.3	309	BUY	483	11.7	6.8	6.1	69	66	67	0.8	0.6	0.5	5.3	15.7	17.2
Orient Cement	16.4	80	BUY	150	9.3	6.6	5.8	56	54	54	1.2	1.0	0.9	4.6	11.5	14.4
Deccan Cement	4.9	350	BUY	670	4.3	3.4	3.7	28	33	37	(0.2)	(0.0)	0.1	11.9	19.5	16.2

Source: Company, HDFC sec Inst Research, For ACC and Ambuja, the financial year is CY18/CY19E/CY20E resp

Consolidated Income Statement

(Rs Mn)	FY18	FY19	FY20E	FY21E	FY22E
Revenues	**16,145**	**18,310**	**18,363**	**20,517**	**22,947**
Growth %	***5.2***	***13.4***	***0.3***	***11.7***	***11.8***
Raw Material	3,025	4,367	3,667	4,115	4,602
Power & Fuel	2,160	2,587	3,667	3,913	4,355
Freight Expense	2,869	3,630	3,392	3,806	4,257
Employee cost	1,074	1,164	1,222	1,345	1,439
Other Expenses	1,805	2,071	2,153	2,347	2,699
EBITDA	**5,214**	**4,492**	**4,260**	**4,991**	**5,594**
EBIDTA Margin (%)	***32.3***	***24.5***	***23.2***	***24.3***	***24.4***
EBITDA Growth %	***25.7***	***(13.8)***	***(5.2)***	***17.2***	***12.1***
Depreciation	1,207	1,056	1,034	1,212	1,089
EBIT	**4,007**	**3,435**	**3,226**	**3,779**	**4,505**
Other Income (Including EO Items)	44	55	290	300	250
Interest	525	144	50	40	40
PBT	**3,526**	**3,346**	**3,466**	**4,039**	**4,715**
Tax	164	296	347	404	471
Minority Int	55	62	30	40	47
RPAT	**3,307**	**2,988**	**3,089**	**3,595**	**4,196**
EO (Loss) / Profit (Net Of Tax)	-	-	-	-	-
APAT	**3,307**	**2,988**	**3,089**	**3,595**	**4,196**
APAT Growth (%)	***64.5***	***(9.6)***	***3.4***	***16.4***	***16.7***
AEPS	**7.9**	**7.1**	**7.5**	**8.7**	**10.2**
AEPS Growth %	***64.5***	***(9.6)***	***5.1***	***16.4***	***16.7***

Source: Company, HDFC sec Inst Research

Consolidated Balance Sheet

(Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
SOURCES OF FUNDS					
Share Capital	419	419	413	413	413
Reserves And Surplus	14,344	16,817	17,942	20,323	23,305
Total Equity	**14,763**	**17,237**	**18,355**	**20,736**	**23,718**
Minority Interest	**621**	**683**	**713**	**753**	**801**
Long-term Debt	1,988	18	13	11	-
Short-term Debt	2,336	721	496	496	496
Total Debt	**4,324**	**738**	**509**	**506**	**496**
Deferred Tax Liability	(2,329)	(2,710)	(3,057)	(3,461)	(3,932)
Long-term Liab+ Provisions	-	-	-	-	-
TOTAL SOURCES OF FUNDS	**17,380**	**15,947**	**16,520**	**18,535**	**21,082**
APPLICATION OF FUNDS					
Net Block	7,847	7,223	10,439	10,278	10,188
Capital WIP	357	743	493	3,743	7,243
Goodwill	-	-	-	-	-
Other Non-current Assets	-	-	-	-	-
Total Non-current Investments	14	17	17	17	17
Total Non-current Assets	**8,219**	**7,984**	**10,950**	**14,038**	**17,449**
Inventories	2,946	2,772	2,571	2,667	2,754
Debtors	1,465	1,438	1,653	1,847	1,836
Cash and Cash Equivalents	198	2,113	1,838	1,440	1,302
Other Current Assets (& Loans/adv)	9,900	5,952	4,102	3,675	3,481
Total Current Assets	**14,509**	**12,275**	**10,163**	**9,628**	**9,373**
Creditors	1,889	1,254	1,258	1,405	1,572
Other Current Liabilities & Provns	3,459	3,057	3,335	3,726	4,168
Total Current Liabilities	**5,348**	**4,311**	**4,593**	**5,132**	**5,739**
Net Current Assets	**9,160**	**7,964**	**5,570**	**4,496**	**3,633**
TOTAL APPLICATION OF FUNDS	**17,380**	**15,947**	**16,520**	**18,535**	**21,082**

Source: Company, HDFC sec Inst Research

Consolidated Cash Flow

(Rs mn)	FY17	FY18	FY19	FY20E	FY21E
Reported PBT	3,526	3,346	3,466	4,039	4,715
Non-operating & EO Items	(42)	(49)	(290)	(300)	(250)
Interest Expenses	525	144	50	40	40
Depreciation	1,207	1,056	1,034	1,212	1,089
Working Capital Change	(67)	3,027	2,118	676	726
Tax Paid	(664)	(592)	(693)	(808)	(943)
OPERATING CASH FLOW (a)	**4,485**	**6,932**	**5,685**	**4,859**	**5,377**
Capex	(324)	(804)	(4,000)	(4,300)	(4,500)
Free Cash Flow (FCF)	*4,161*	*6,128*	*1,685*	*559*	*877*
Investments	26	(1,153)	-	-	-
Non-operating Income	44	45	290	300	250
Others					
INVESTING CASH FLOW (b)	**(253)**	**(1,911)**	**(3,710)**	**(4,000)**	**(4,250)**
Debt Issuance/(Repaid)	(3,685)	(3,598)	(229)	(3)	(11)
Interest Expenses	(522)	(144)	(50)	(40)	(40)
FCFE	(47)	2,386	1,406	516	826
Share Capital Issuance	-	-	(1,000)	-	-
Dividend	-	(516)	(971)	(1,214)	(1,214)
FINANCING CASH FLOW (c)	**(4,208)**	**(4,258)**	**(2,250)**	**(1,257)**	**(1,264)**
NET CASH FLOW (a+b+c)	**24**	**763**	**(276)**	**(398)**	**(137)**
EO Items, Others					
Closing Cash & Equivalents	**224**	**961**	**1,838**	**1,440**	**1,302**

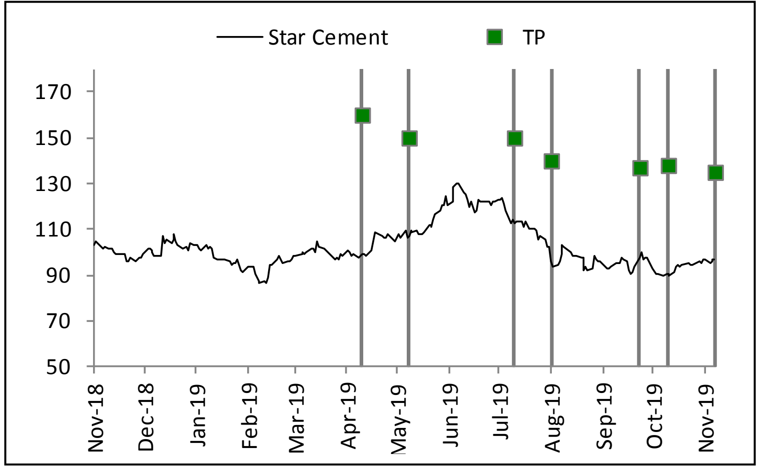
Source: Company, HDFC sec Inst Research

Consolidated Key Ratios & Valuations

	FY18	FY19	FY20E	FY21E	FY22E
PROFITABILITY %					
EBITDA Margin	32.3	24.5	23.2	24.3	24.4
EBIT Margin	24.8	18.8	17.6	18.4	19.6
APAT Margin	20.1	16.0	16.7	17.3	18.1
RoE	24.1	17.9	16.7	17.7	18.2
RoIC	21.7	20.2	21.2	25.7	24.8
RoCE	21.7	19.1	19.5	20.9	21.6
EFFICIENCY					
Tax Rate %	4.7	8.9	10.0	10.0	10.0
Fixed Asset Turnover (x)	1.6	1.7	1.4	1.3	1.4
Inventory (days)	67	55	51	47	44
Debtors (days)	33	29	33	33	29
Other Current Assets (days)	224	119	82	65	55
Payables (days)	43	25	25	25	25
Other Current Liab & Provns (days)	78	61	66	66	66
Cash Conversion Cycle (days)	203	117	74	54	37
Net Debt/EBITDA (x)	0.8	(0.3)	(0.3)	(0.2)	(0.1)
Net D/E (x)	0.3	(0.1)	(0.1)	(0.2)	(0.0)
Interest Coverage (x)	7.6	23.9	64.5	94.5	112.6
PER SHARE DATA (Rs)					
EPS	7.9	7.1	7.5	8.7	10.2
CEPS	10.8	9.6	10.0	11.7	12.8
Dividend	1.0	-	2.0	2.5	2.5
Book Value	35.2	41.1	44.5	50.3	59.4
VALUATION					
P/E (x)	12.1	13.4	12.9	11.1	9.5
P/Cash EPS (x)	8.8	9.9	9.7	8.3	7.5
P/BV (x)	2.7	2.3	2.2	1.9	1.7
EV/EBITDA (x)	8.6	8.7	8.9	7.1	7.1
EV/MT(USD)	186	163	138	121	130
Dividend Yield (%)	1.0	-	2.1	2.6	2.6
OCF/EV (%)	10.1	17.7	14.9	13.7	13.5
FCFF/EV (%)	9.3	15.6	4.4	1.6	2.2
FCFE/M Cap (%)	10.4	15.4	4.2	1.4	2.2

Source: Company, HDFC sec Inst Research,

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
10-Apr-19	99	BUY	160
8-May-19	107	BUY	150
10-Jul-19	114	BUY	150
2-Aug-19	96	BUY	140
22-Sep-19	93	BUY	137
10-Oct-19	91	BUY	138
8-Nov-19	97	BUY	135

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

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Disclosure:

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