BUY

CMP: **INR 228** Target Price: **INR 271** ▲ 19%

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07 April 2024

India | Equity Research | Initiating Coverage

Star Cement

Cement

North-eastern delight

Star Cement (Star) has been on top of its game – evidence of which is apparent in: 1) it being a major beneficiary of the favourable demand-supply dynamics in India's north-east (NE) region (where prices stood firm in Q4FY24 vs. a steep >8% QoQ drop in east India) – outlook for NE remains sanguine; 2) the rationale that while capex completion shall drive ~21% CAGR volume growth over FY25-FY26E, project incentives (of ~INR 300/t) will be an icing on the cake; and 3) its slated increase in share of green power (from ~21% in FY24E to ~50% in FY26E) with greater FSA coal allocation, in tandem, will likely uplift efficiency (by ~INR 150/t). A strong debt-free balance-sheet, high RoE and its imminent entry into the 'INR 10bn-plus EBITDA club' make for a compelling investment case. We recommend **BUY** with an INR 271 TP, valued at 11x FY26E EV/EBITDA.

Virtues of being a NE major

~75% of Star's volumes cater to the NE, a region where the – 1) demand outlook remains buoyant with continued ~8% growth prospects (I-sec estimates); 2) industry operates at near-full utilisations, and where despite capacity adds by regional majors (both Star and Dalmia Bharat Ltd), we expect utilisations to remain firm (~90%); and 3) pricing environment remains conducive. In Q4FY24, prices in NE stood firm, bucking the trend of a steep >8% QoQ drop in east India.

Imminent capex benefits of volume surge and incentive accrual

Completion of the 3.3mtpa clinker (4mtpa cement, in phases) is likely to not only drive a volume surge (~21% CAGR over FY25-FY26), but also generate project incentives (SGST/IGST refund) that can catapult EBITDA/t by >INR 300. Given that these incentives will only be for a brief span, being prudent, we bake in NPV of the same into our valuation.

Positives galore; initiate with 'BUY'

Star is set to surpass the INR 10bn-plus EBITDA milestone in FY26E, complimented by: 1) expected cost savings of ~INR 150/t, owing to the slated jump in share of green power and increase in FSA coal allocation; 2) a strong balance-sheet with net cash of ~INR 8bn in FY26E (vs. ~INR 5bn in FY23) despite capex; and 3) firm RoE of ~18% over FY25-FY26. Factoring in the multiple positives, we value Star at 11x FY26E EV/core EBITDA (ex-incentives), which yields a TP of INR 271. We initiate coverage with a **BUY**.

Financial Summary

Y/E March (INR mn)	FY23A	FY24E	FY25E	FY26E
Net Revenue	27,048	28,552	36,990	42,463
EBITDA	4,684	5,537	9,194	10,367
EBITDA (%)	17.3	19.4	24.9	24.4
Net Profit	2,476	3,160	5,306	6,300
EPS (INR)	6.1	7.8	13.1	15.6
EPS % Chg YoY	0.3	27.6	67.9	18.7
P/E (x)	37.2	29.1	17.3	14.6
EV/EBITDA (x)	18.5	16.4	9.7	8.1
RoCE (%) (post-tax)	11.0	12.5	17.8	17.7
RoE (%)	10.8	12.3	17.7	17.6

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Market Data

Market Cap (INR)	92bn
Market Cap (USD)	1,105mn
Bloomberg Code	STRCEM IN
Reuters Code	STATf.BO
52-week Range (INR)	242 /110
Free Float (%)	20.0
ADTV-3M (mn) (USD)	2.2

Price Performance (%)	3m	6m	12m
Absolute	26.5	44.8	101.8
Relative to Sensex	23.4	31.7	77.4

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Capex benefits - volume surge and incentive accrual

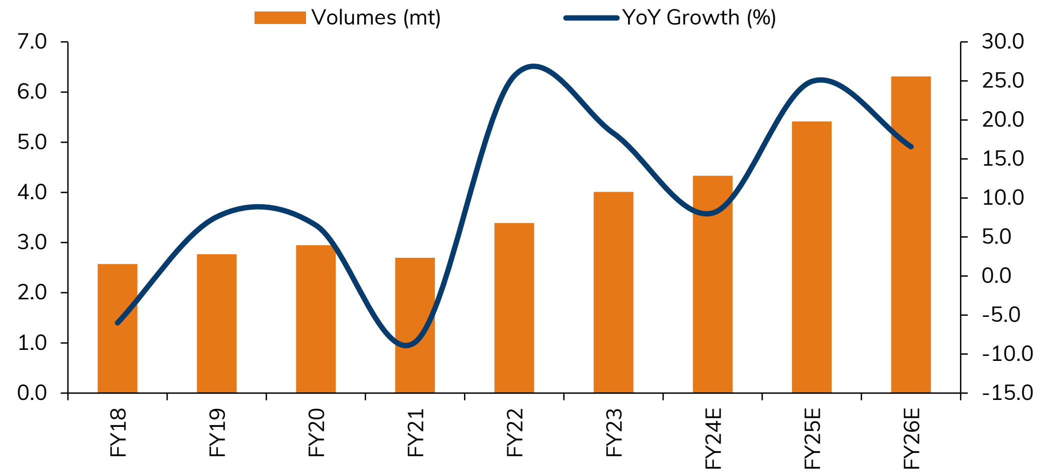
Volumes projected to rise ~21% CAGR over FY25-FY26

Star is about to commission a new 3.3mtpa brownfield clinker line at its mother unit in Lumshnong, Meghalaya, taking its total clinker capacity to 6.1mtpa. The timing of the expansion is on the nose given its existing clinker capacity of 2.8mtpa is brimming at optimal utilisation in FY24E.

While the 2mtpa cement grinding unit (brownfield) in Guwahati has already been commissioned in Mar'24, the other 2mtpa greenfield grinding unit at Silchar, in Assam, is scheduled to be commissioned by Q3FY26.

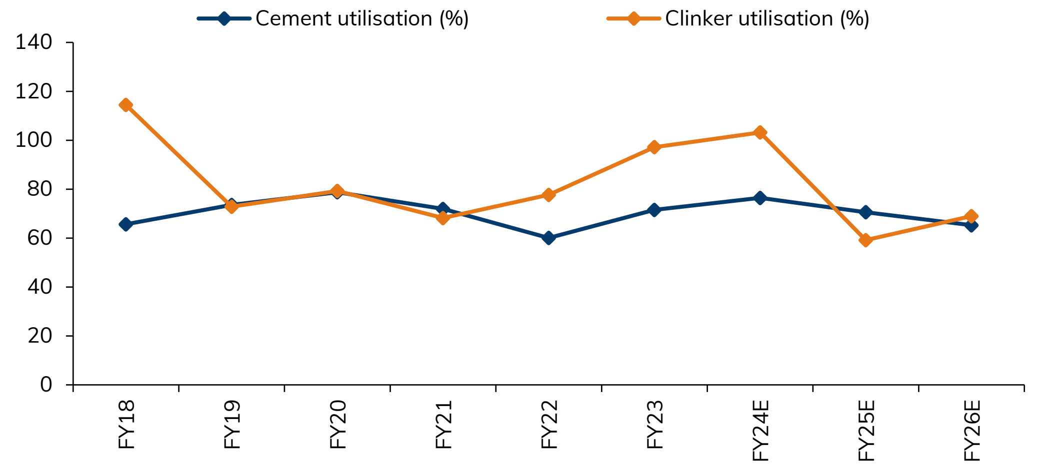
We reckon the timely commissioning of the said capex shall drive a 25% volume surge in FY25E, and another 17% in FY26E – implying ~21% volume CAGR over FY25E-FY26E.

Exhibit 1: Volumes set to surge



Source: I-Sec research, Company data

Exhibit 2: Cement and clinker utilisation trend



Source: I-Sec research, Company data

Our volumes estimates are conservative as they imply new clinker line utilisation of a mere ~22% in FY25E and ~40% in FY26E.

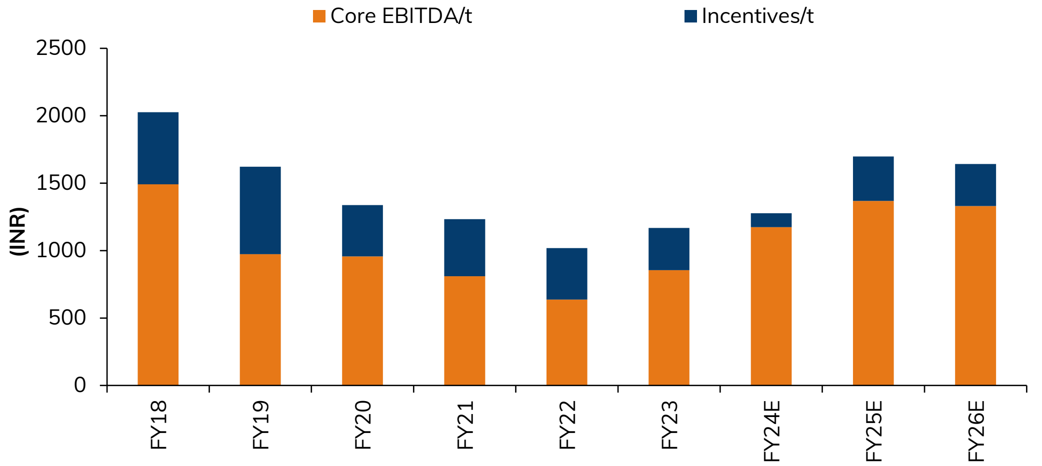
Project incentives could boost EBITDA/t by ~INR 300

The project capex is eligible for incentives – mainly in the form of SGST/IGST refund (i.e. 14% of selling price). The incentive pool is 200% of the eligible capex and is available for a maximum period of 20 years (from the date of commissioning). We believe Star will endeavour to utilise the incentive pool within the first 7-8 years itself.

SGST incentives on the erstwhile capex (grinding unit in Guwahati) expired in Jan'23; hence, its resumption comes as a shot in the arm for Star.

In recent years, the company booked incentives of ~INR 1.3bn in FY22 (i.e. INR 382/t) and of ~INR 1.25bn in FY23 (i.e. INR 313/t). We project incentive accruals to the tune of ~INR 1.8bn in FY25 and ~INR 2bn in FY26, implying ~INR 321 on a per tonne basis.

Exhibit 3: Reported EBITDA/t and incentives/t



Source: I-Sec research, Company data

Given these incentives are for a limited period with a cap on the overall pool, we assume NPV of the incentives for valuation purpose. As such, we value Star on core EBITDA basis (see 'Outlook and valuation' section for details).

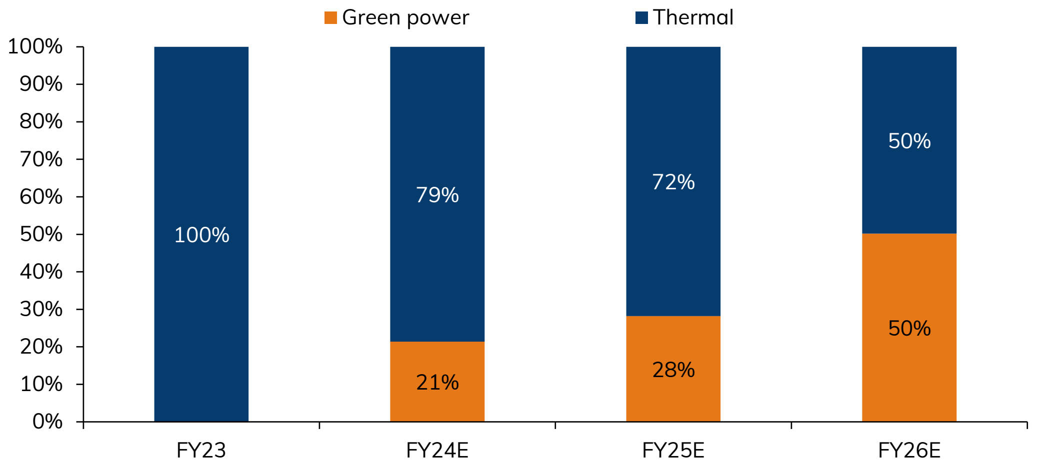
Energy cost on the mend; potential savings of ~INR 150/t

Share of green power set to rise to ~50% in FY26E (~21% in FY24E)

Star is focussing on energy cost optimisation. It has embarked on a journey to increase the share of green power to ~50% by FY26E, from ~21% in FY24E.

To that end, the company is: 1) adding 12MW WHRS power plant (along with its new 3.3mtpa clinker line); and 2) pursuing renewal power addition of another ~25MW (solar power + wind power combined) via a JV – which is expected to be available to Star Q1FY26 onwards.

Exhibit 4: Rising share of green power



Source: I-Sec research, Company data

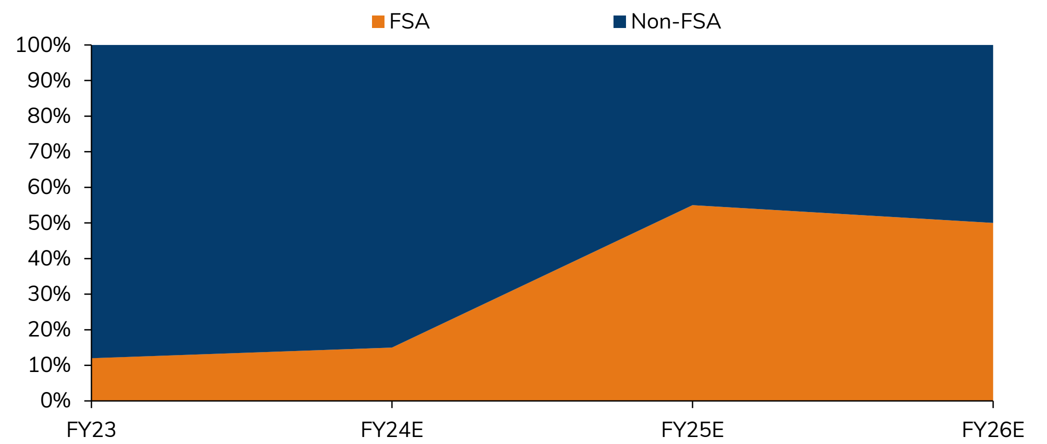
The increase in share of green power has potential to save ~INR 30/t in FY25E and another ~INR 45/t FY26E.

Benefits of increased FSA coal allocation

Star is also set to benefit from the recent increase in coal allocation under a Fuel Supply Agreement (FSA) with Coal India Ltd. On 29 Feb'24, Star intimated stock exchanges of having been declared as a successful bidder for procurement of ~0.3mt coal p.a. for next 10 years.

The said allocation will increase FSA coal exposure to >50% in its overall fuel mix as against ~15-20% in FY24E. The assured supply will not only help insulate Star against a surge in global fuel rates (if any), but also help generate savings of ~INR 75/t.

Exhibit 5: Fuel mix swinging in favour of FSA



Source: I-Sec research, Company data

Sanguine outlook for NE region; Star a major beneficiary

Demand outlook remain optimistic

For Star, ~74% of its capacity as well as volumes are from the NE region. Hence, the outlook of the region assumes high significance for the company.

NE is an ecologically sensitive region with a hilly topography, forest land and tribal areas, which impedes capacity addition. In the past decade (FY13-FY23), the region's capacity addition paced at a mere ~4% CAGR compared to ~8% demand CAGR over the same period. As a result, the region has been operating at optimal utilisations since the past few years.

Going ahead too, the demand outlook for NE remains optimistic given the central government's focus due to the region's geopolitical importance. As such, the central government has initiated various projects/schemes for overall development of the region (as enumerated in Star's Annual Report of 2023).

Exhibit 6: Various ongoing projects in North-East India

Projects/Schemes	Tenure	Amount (INR bn)
375 road Projects in North-eastern states	Ongoing	1,050
Additional 19 rail projects sanctioned		779
Schemes of Ministry of Development of North Eastern Region	FY23-FY26	129
North East Gas Grid (NEGG) project		93
North East Special Infrastructure Scheme (NESIDS) for railways, waterways, telecom & air		81
The Prime Minister's Development Initiative for North East Region (PM-DevINE) Scheme	FY23-FY26	66
Development of national waterway 2 & 16.		60
Civil aviation sector		20
Packages for various autonomous bodies		15
Package to illuminate border villages of Arunachal Pradesh		6
Projects under implementation stage in North-east region		**2,299**

Source: Company data

Industry consolidation on the rise in NE

Star and Dalmia Bharat (Dalmia, not rated) have a lion's share of 69% of the region's capacity. Of the top five players' pool in the NE, there is a conspicuous gap between the top-two and bottom-three players in the region. The gap is likely to broaden in the near-term, as only the top two players are pursuing significant capacity addition in the region. As discussed above, while Star is adding 4mtpa cement capacity in phases (2mtpa commissioned on 12 Mar'24 and balance 2mtpa expected by Q3FY26), Dalmia is adding 2.4mtpa by Q4FY25.

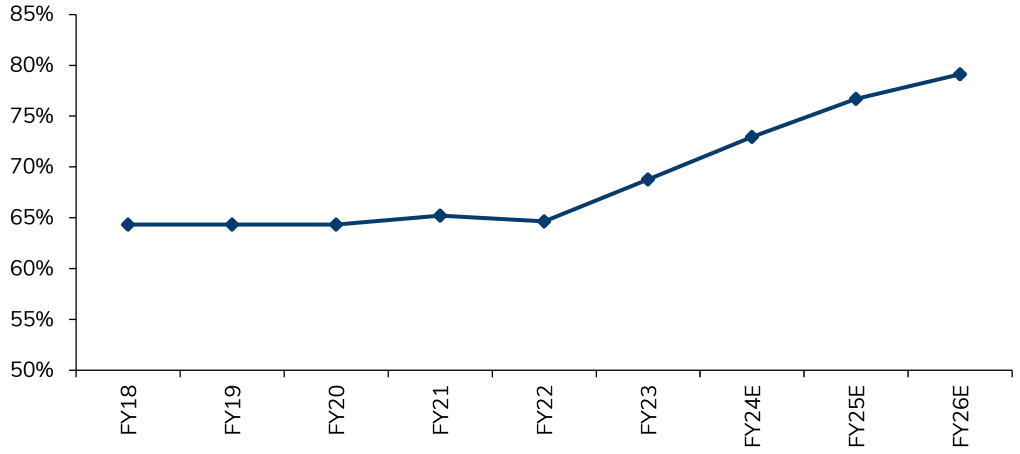
Exhibit 7: Capacities of top-5 cement players in North-east region

Companies	Capacity (mtpa)	
	FY24E	FY26E
Star Cement	5.7	7.7
Dalmia Bharat	5.2	7.6
Amrit Cement	1.5	1.5
Goldstone Cement	0.9	0.9
Topcem Cement	0.7	0.7
Total	**14.0**	**18.4**

Source: I-Sec research, Company data

Capacity share of the top-2 players is set to rise to 79%.

Exhibit 8: Capacity share of Top-2 companies in NE

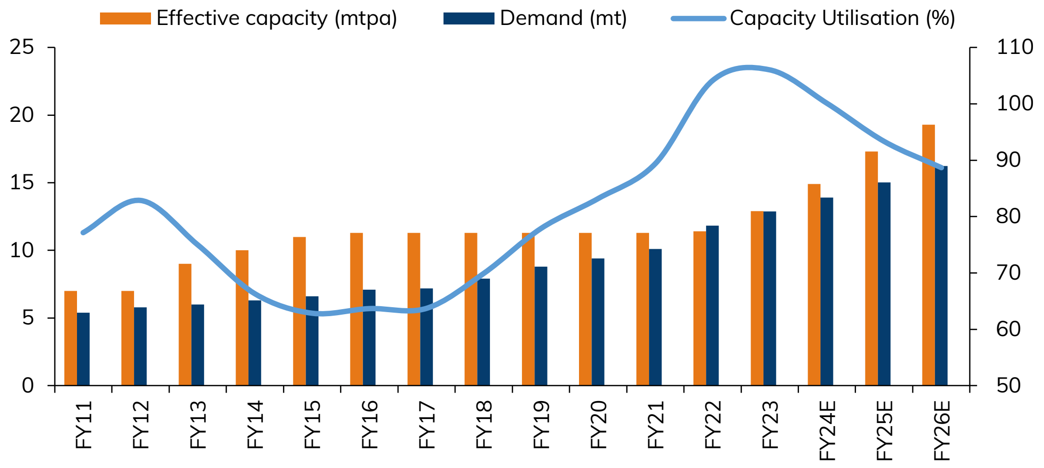


Source: I-Sec research, Company data

Industry utilisations to come-off peak; yet will remain healthy

Assuming 8% demand growth and the capacity additions by regional majors, the industry's utilisation levels are likely to come-off from its peak of ~100% in FY24E. However, they are still likely to remain healthy at ~90%.

Exhibit 9: Demand – Supply trend in NE



Source: I-Sec research, Company data

Key risk to our regional hypothesis stems from entry of new players with significant capacity addition. In the recent past, companies such as UltraTech Cement and JK Lakshmi Cement have indicated interest to foray into the region; another entity called MeghaTop Private Limited has moved for environment clearance to set up a 2.8mtpa cement capacity in the region. Formal capex announcement is pending from all the aforementioned prospective new entrants into the region.

Exhibit 10: Recent capacity announcements – North-East region

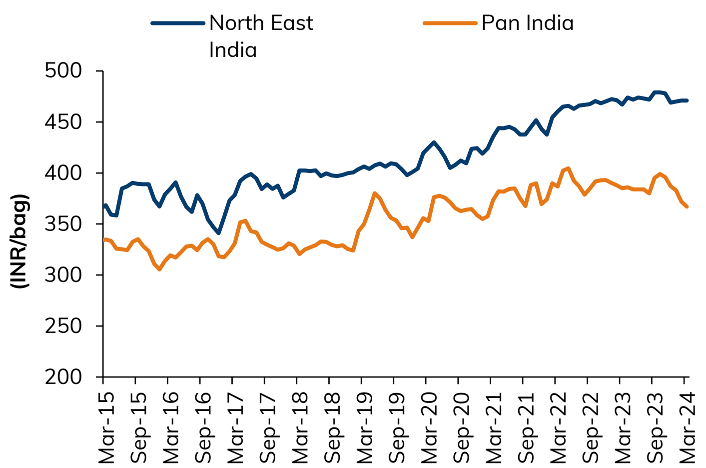
Company	Capacity (mtpa)		Type or details	Location	State	Tentative commissioning
	Clinker	Cement				
Star Cement	-	2.0	Brownfield	Guwahati	Assam	Commissioned
Star Cement	-	2.0	Greenfield	Silchar	Assam	Q3FY26
Star Cement	3.3		Brownfield	Lumshong	Meghalaya	Q1FY25
Dalmia Bharat	3.6	2.4	Greenfield	Umrangshu	Assam	Clinker - H1FY26 Cement – Q4FY25
UltraTech Cement	-	-	Incorporated a wholly-owned Subsidiary viz. "Letein Valley Cement Limited"; It will carry business of mining of limestone and other raw materials; manufacture and sale of cement.	Shillong	Meghalaya	TBA
JK Lakshmi	1.0	1.5	JK Lakshmi board approves 85% acquisition in Trivikram Consortium, which has limestone mining reserves ~335mt.	TBA	Assam	TBA
Total	**7.9**	**7.9**				

Source: I-Sec research, Company data; (TBA- to be announced)

The expected high utilisations and rising consolidation bode well for the pricing environment as well. Our optimism is rooted in the fact that in Q4FY24, cement prices in NE continued to stay firm even as they plunged >8% in east India.

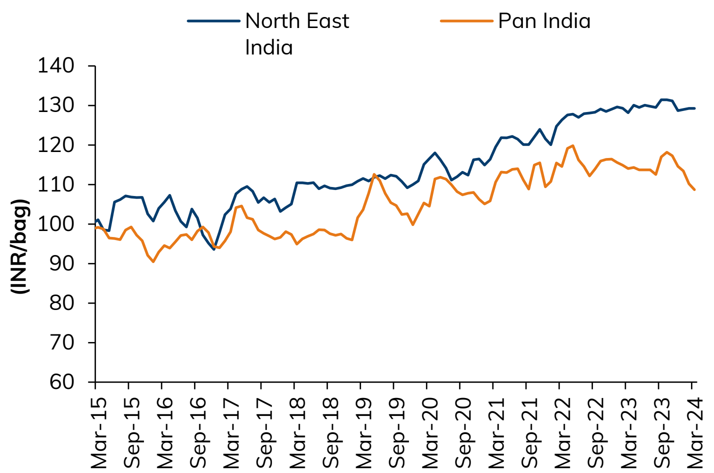
Historically too, we observe pricing in the region faring better versus the pan-India price trend.

Exhibit 11: Cement prices in NE vs Pan-India prices



Source: I-Sec research, Company data

Exhibit 12: Cement price trend – NE vs Pan-India (indexed)



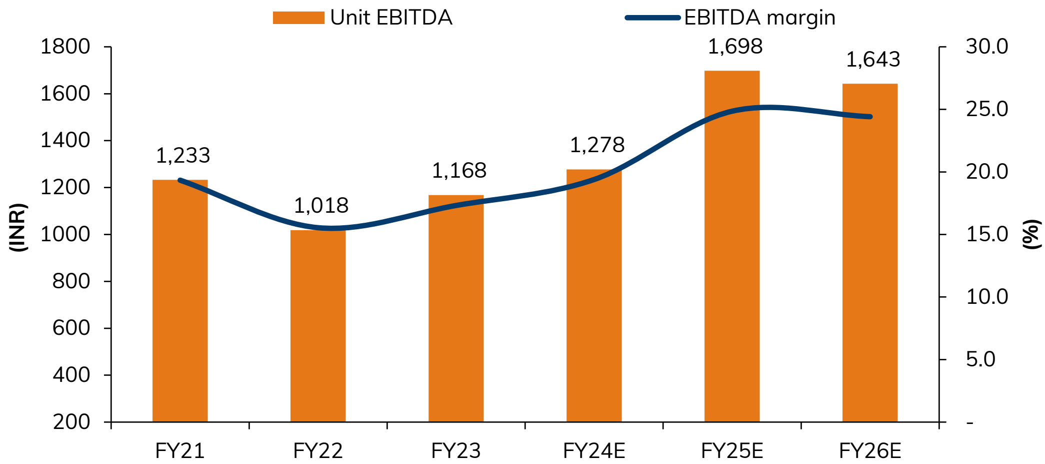
Source: I-Sec research, Company data

Outlook and valuations: Positives galore

EBITDA set to surge at 37% CAGR over FY25-FY26

Assuming 21% CAGR volume growth and incentive benefits of ~INR 321/t, we estimate Star's EBITDA to surge at 37% CAGR over FY25-FY26.

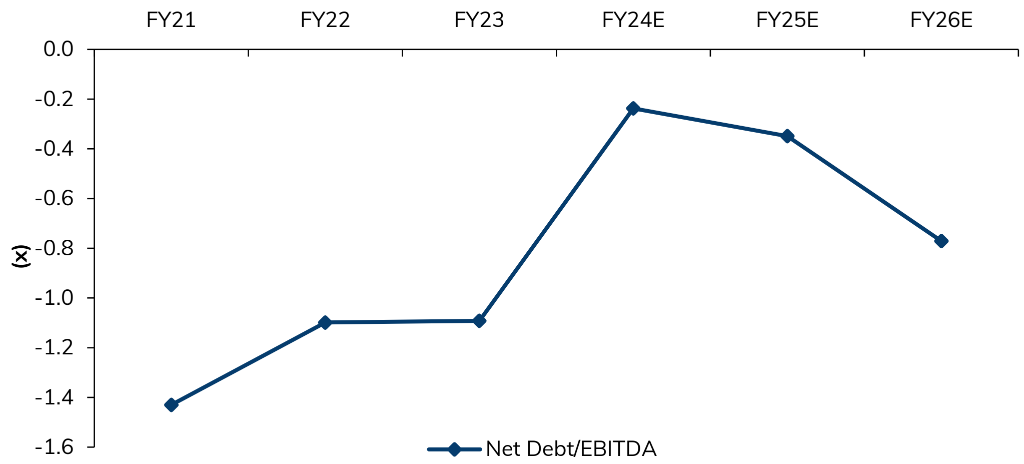
Exhibit 13: EBITDA and EBITDA margin trend



Source: I-Sec research, Company data

All along, its balance –sheet is expected to stay strong with net-cash position.

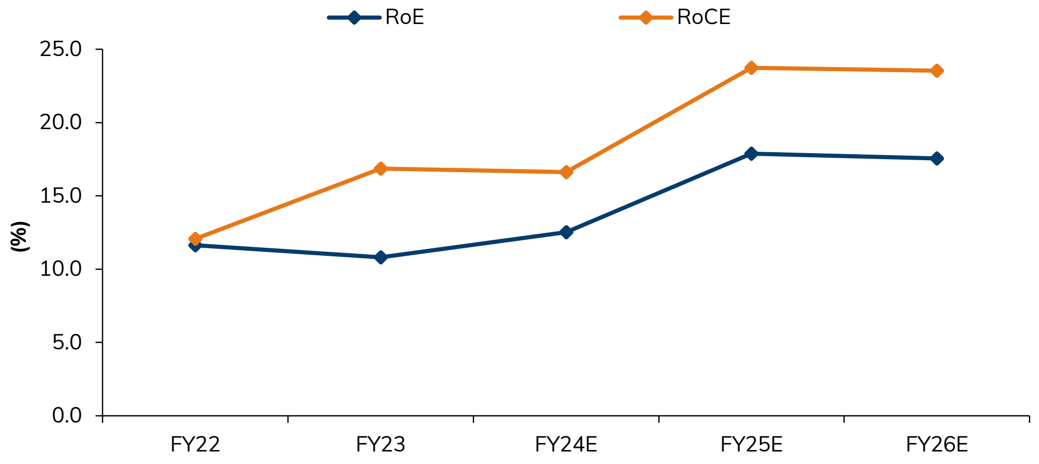
Exhibit 14: Net debt/EBITDA trend



Source: I-Sec research, Company data

Its RoE too is expected to improve further – from ~13% in FY24E to ~18% for both FY25-FY26E.

Exhibit 15: RoE and RoCE trend



Source: I-Sec research, Company data

Star is set to enter the INR 10bn-plus EBITDA galaxy

Star is set to surpass the INR 10bn-plus EBITDA milestone in FY26E, complimented by: 1) expected cost savings of ~INR 150/t, owing to the slated jump in share of green power and increase in FSA coal allocation; 2) a strong balance-sheet with net cash of ~INR 8bn in FY26E (vs. ~INR 5bn in FY23) despite capex; and 3) firm RoE of ~18% over FY25-FY26.

Factoring in the multiple positives, we value Star's core EBITDA (excluding incentives) at 11x FY26E EV/EBITDA multiple. Being prudent, we have assumed an NPV of the fiscal incentives that are likely to accrue beyond FY26.

Our ascribed valuation multiple of 11x is 1-standard deviation higher than the past 5-year EV/EBITDA mean of ~9.5x (on reported EBITDA, including incentives). However, it is at par to the past 3-year average (EV/EBITDA) when we consider core EBITDA (excluding incentives).

With a target price of INR 271, we initiate coverage on Star with a **BUY.**

Exhibit 16: Valuation Table

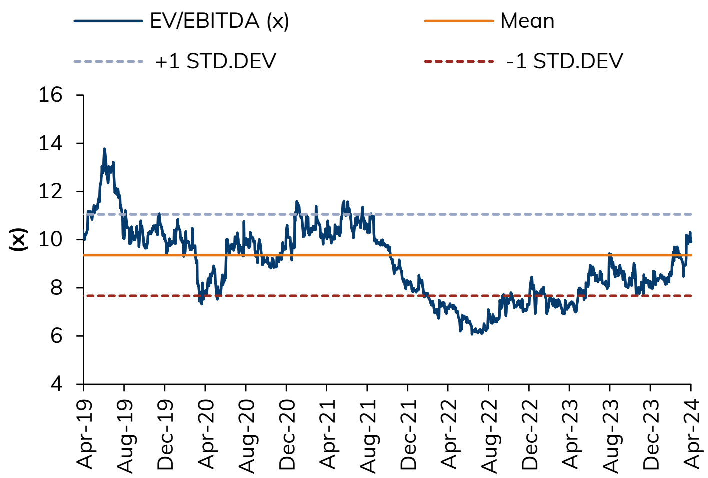
(INR Mn)	FY26E
Assumed EV/EBITDA multiple (x)	11.0
Core EBITDA (ex-incentives)	8,396
EV	92,359
Less: Net debt	-7,991
Net Present Value (NPV) of incentives	9,266
M-Cap	1,09,617
Shares o/s (mn)	404.2
Value per share (INR)	271
Potential Upside (%)	19%

Source: I-Sec research, Company data

Key Risk: A sharp drop in cement prices or sharp increase in fuel cost are the key risks to our recommendation.

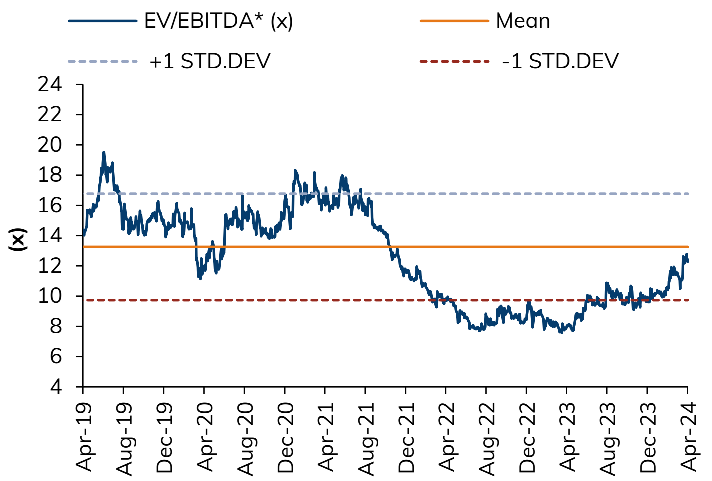
Valuation charts

Exhibit 17: Rolling EV/EBITDA chart



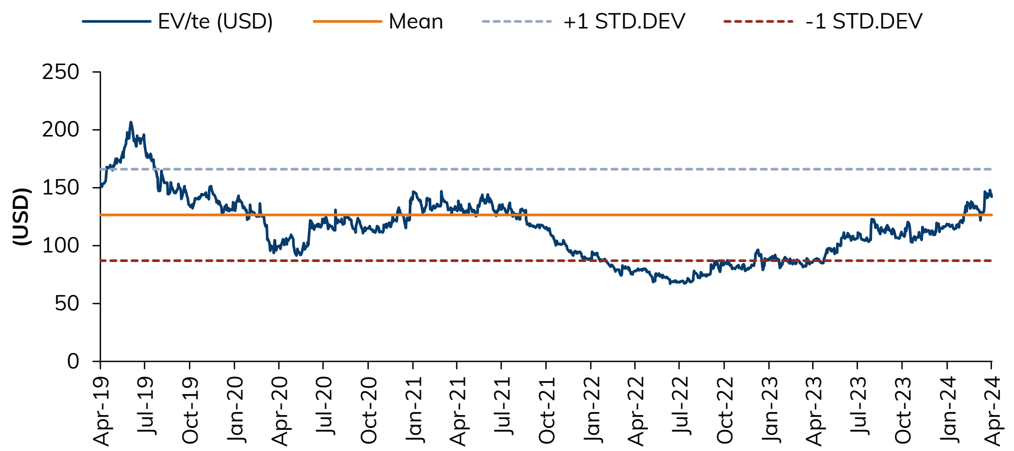
Source: I-Sec research, Company data

Exhibit 18: Rolling EV/EBITDA chart (EBITDA excludes incentives)



Source: I-Sec research, Company data, * EBITDA is excluding incentives

Exhibit 19: Rolling EV/t chart



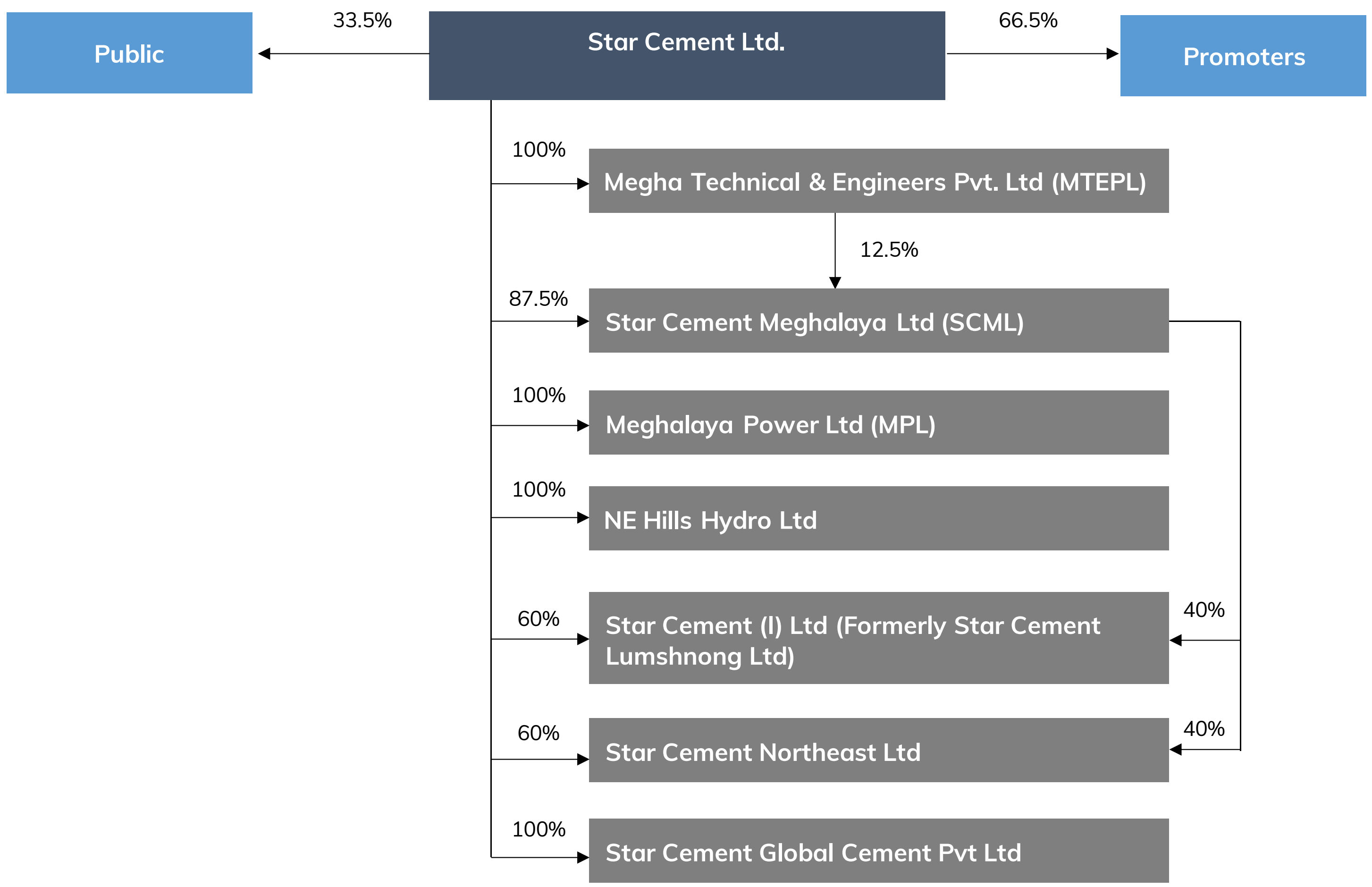
Source: I-Sec research, Company data

Company Description

Star Cement Ltd. (Star) began operations in 2005 and was earlier known as Cement Manufacturing Company Ltd (CMCL). Through a series of restructuring, Star was made the holding company in 2016 and all its products were rebranded as 'Star Cement'.

The current organisation structure is as below –

Exhibit 20: Star Cement – Organisation Structure



Source: Company data, I-Sec research

The promoters' control 66.5% in the company with Mr. Sajjan Bhajanka being the Chairman and Managing Director and Mr Rajendra Chamaria being its Vice Chairman and Managing Director. The day-to-day affairs of the company are looked into by –

Mr Sanjay Agarwal – Managing Director

Mr Prem Kumar Bhajanka – Managing Director

Mr Tushar Bhajanka– Deputy Managing Director

The company enjoys leadership in NE India with market share of >24% (as on Sep'23-end). As on Mar'24, Star's consolidated cement manufacturing capacity stands at 7.7mtpa, clinker capacity at 2.80mtpa, 12.3 MW of WHRS and a captive power plant of 51MW. Star is in the process of commissioning a 3.3mtpa of clinker unit in Lumshnong, Meghalaya (expected to commissioned in Q1FY25), taking its total clinker capacity to 6.1mtpa.

Going ahead, it shall commission 2mtpa of grinding unit capacity in Silchar, Assam by Q3FY26, taking its total cement capacity to 9.7mtpa. Star aims to be a 15mtpa player over the next 4-5 years.

Exhibit 21: Capacity Snapshot

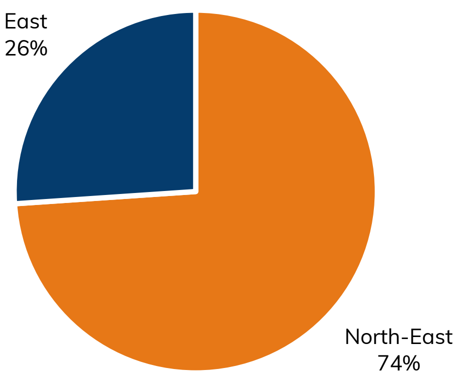
Particulars	Unit	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Clinker	MTPA	2.8	2.8	2.8	2.8	2.8	6.1	6.1
Cement	MTPA	3.7	3.7	5.7	5.7	7.7	7.7	9.7
Waste Heat Recovery System	MW	-	-	-	12	12	24	24
Captive Thermal Power	MW	51	51	51	51	51	51	51

Source: Company data, I-Sec research

Exhibit 22: Product offerings under the brand

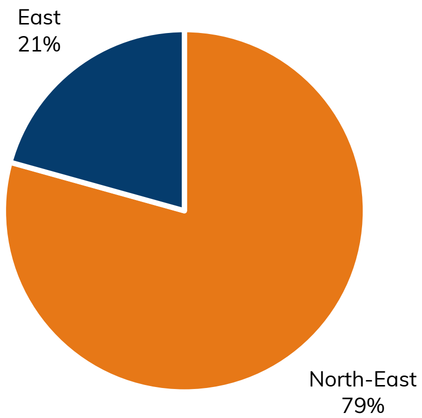
Source: Company data

Exhibit 23: Regional Capacity Mix- FY24



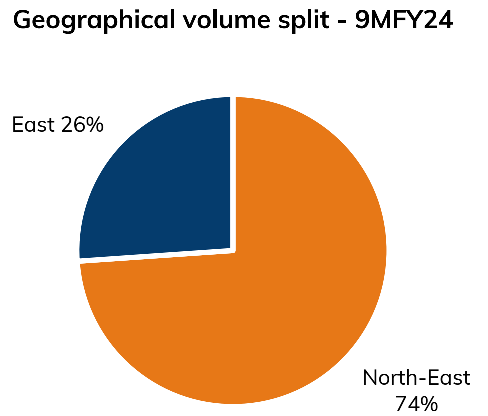
Source: I-Sec research, Company data

Exhibit 24: Regional Capacity Mix- FY26E



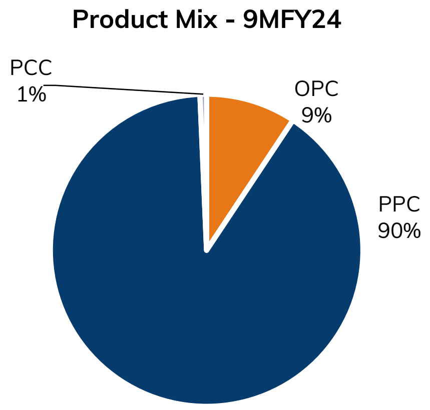
Source: I-Sec research, Company data

Exhibit 25: East India volume exposure stood at 26%



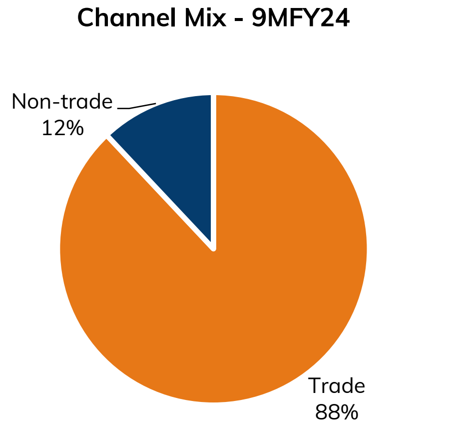
Source: I-Sec research, Company data

Exhibit 26: OPC contributes 9% to the sales mix



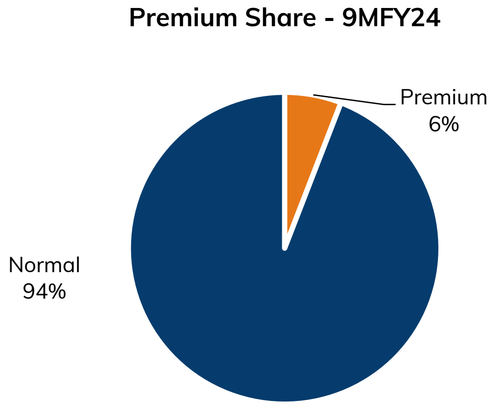
Source: I-Sec research, Company data

Exhibit 27: Despatches to non-trade is 12%



Source: I-Sec research, Company data

Exhibit 28: Premium cement is 6% of trade sales



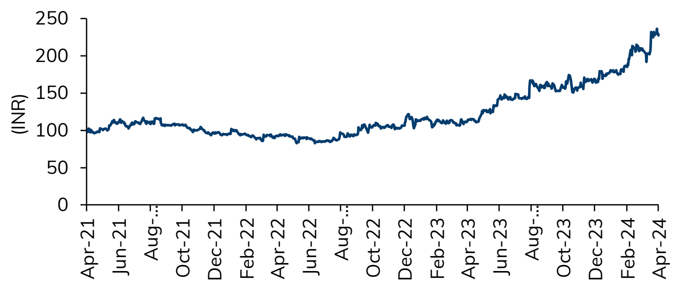
Source: I-Sec research, Company data

Exhibit 29: Shareholding pattern

%	Jun '23	Sep '23	Dec '23
Promoters	66.8	66.6	66.5
Institutional investors	6.9	6.9	7.1
MFs and other	6.0	6.0	6.0
Banks/ FIs	0.0	0.0	0.0
Insurance Cos.	0.2	0.1	0.0
FIIs	0.7	0.8	1.1
Others	26.3	26.5	26.4

Source: Bloomberg, I-Sec research

Exhibit 30: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 31: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Net Sales	27,048	28,552	36,990	42,463
Operating Expenses	**16,107**	**16,756**	**20,818**	**23,961**
EBITDA	4,684	5,537	9,194	10,367
EBITDA Margin (%)	**17.3**	**19.4**	**24.9**	**24.4**
Depreciation & Amortization	1,311	1,434	2,176	2,263
EBIT	3,373	4,103	7,018	8,104
Interest expenditure	97	117	115	104
Other Non-operating Income	521	228	172	401
Recurring PBT	3,797	4,213	7,074	8,401
Profit / (Loss) from Associates	-	-	-	-
Less: Taxes	1,321	1,053	1,769	2,100
PAT	**2,476**	**3,160**	**5,306**	**6,300**
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	-	-	-	-
Net Income (Reported)	2,476	3,160	5,306	6,300
Net Income (Adjusted)	**2,476**	**3,160**	**5,306**	**6,300**

Source Company data, I-Sec research

Exhibit 32: Balance sheet

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Total Current Assets	9,974	7,774	11,008	16,542
of which cash & cash eqv.	3,117	807	2,624	7,400
Total Current Liabilities & Provisions	5,024	5,172	5,924	6,394
Net Current Assets	**4,950**	**2,602**	**5,084**	**10,148**
Investments	1,725	500	500	500
Net Fixed Assets	8,870	20,476	22,299	25,036
ROU Assets	-	-	-	-
Capital Work-in-Progress	5,506	1,006	2,006	506
Total Intangible Assets	40	-	-	-
Other assets	4,666	4,666	4,666	4,666
Deferred Tax assets	-	-	-	-
Total Assets	**26,290**	**29,450**	**34,756**	**41,056**
Liabilities				
Borrowings	**261**	**261**	**261**	**261**
Deferred Tax Liability	-	-	-	-
provisions	77	77	77	77
other Liabilities	1,788	1,788	1,788	1,788
Equity Share Capital	404	404	404	404
Reserves & Surplus	23,760	26,919	32,225	38,526
Total Net Worth	**24,164**	**27,324**	**32,629**	**38,930**
Minority Interest	-	-	-	-
Total Liabilities	**26,290**	**29,450**	**34,756**	**41,056**

Source Company data, I-Sec research

Exhibit 33: Cashflow statement

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Operating Cashflow	**4,846**	**5,764**	**9,365**	**10,768**
Working Capital Changes	(417)	(132)	(664)	(288)
Capital Commitments	(5,694)	(8,500)	(5,000)	(3,500)
Free Cashflow	**9,447**	**13,079**	**11,933**	**11,880**
Other investing cashflow	2,978	1,728	-	-
Cashflow from Investing Activities	**(2,717)**	**(6,772)**	**(5,000)**	**(3,500)**
Issue of Share Capital	-	-	-	-
Interest Cost	(107)	(117)	(115)	(104)
Inc (Dec) in Borrowings	207	-	-	-
Dividend paid	-	-	-	-
Others	-	-	-	-
Cash flow from Financing Activities	100	(117)	(115)	(104)
Chg. in Cash & Bank balance	**1,135**	**(2,311)**	**1,818**	**4,776**
Closing cash & balance	3,117	807	2,624	7,400

Source Company data, I-Sec research

Exhibit 34: Key ratios

(Year ending March)

	FY23A	FY24E	FY25E	FY26E
Per Share Data (INR)				
Reported EPS	6.1	7.8	13.1	15.6
Adjusted EPS (Diluted)	6.1	7.8	13.1	15.6
Cash EPS	9.4	11.4	18.5	21.2
Dividend per share (DPS)	-	-	-	-
Book Value per share (BV)	59.8	67.6	80.7	96.3
Dividend Payout (%)	-	-	-	-
Growth (%)				
Net Sales	21.7	5.6	29.6	14.8
EBITDA	35.7	18.2	66.1	12.8
EPS (INR)	0.3	27.6	67.9	18.7
Valuation Ratios (x)				
P/E	37.2	29.1	17.3	14.6
P/CEPS	24.3	20.0	12.3	10.7
P/BV	3.8	3.4	2.8	2.4
EV / EBITDA	18.5	16.4	9.7	8.1
EV / te (USD)	209.6	145.8	139.5	104.7
Dividend Yield (%)	-	-	-	-
Operating Ratios				
Gross Profit Margins (%)	76.9	78.1	81.1	80.8
EBITDA Margins (%)	17.3	19.4	24.9	24.4
Effective Tax Rate (%)	34.8	25.0	25.0	25.0
Net Profit Margins (%)	9.2	11.1	14.3	14.8
NWC / Total Assets (%)	18.8	8.8	14.6	24.7
Net Debt / Equity (x)	(0.2)	0.0	(0.1)	(0.2)
Net Debt / EBITDA (x)	(1.1)	(0.2)	(0.3)	(0.8)
Profitability Ratios				
RoCE (%) (Post Tax)	11.0	12.5	17.8	17.7
RoE (%)	10.8	12.3	17.7	17.6
RoIC (%)	13.0	13.5	18.9	20.6
Fixed Asset Turnover (x)	3.0	1.9	1.7	1.8
Inventory Turnover Days	61	81	78	81
Receivables Days	16	14	13	14
Payables Days	53	62	59	60

Source Company data, I-Sec research

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