

Star Cement Ltd (STRCEM IN)

4Q miss but still industry-best

Affected by one-offs; maintain BUY

Weaker-than-expected volume and higher costs caused STRCEM to miss consensus and our EBITDA estimates by 9% in 4Q19. We factor in higher fuel costs from higher consumption of imported coal as well as ASP increases by the industry in Apr 2019 for FY20/21E. Overall, this lowers our EBITDA by 9%/8%. Our TP is also down 9% to INR133. This remains set at 10x FY20E EV/EBITDA, on par with the sector. Growth plans are intact as it will add 47% capacity to 6.3m tonnes in FY20E. Reiterate BUY with catalysts anticipated from commissioning of capacity. Risks to our view include roll back of ASP increase, lower cement sales volume growth.

Demand to improve after elections

4QFY19 EBITDA/t was down YoY and QoQ to INR1,569, caused by higher discounts to sell cement and 9% volume-sales growth vs 15% on average in the last three quarters. Central-government elections lowered demand for infrastructure projects plus there was an unplanned maintenance shutdown by STRCEM in 4Q. STRCEM has guided for 15% volume growth for FY20, assuming an uptick in demand after elections and the commissioning of its Siliguri capacity in Dec 2019. In our sensitivity analysis, 1% deviation in volume impacts EBITDA by 2%.

Expansion on track, subsidy receipt by 1HFY20

STRCEM's 2mt Siliguri grinding project is on track for commissioning by Dec 2019. Operating cash flows of INR6-8b pa should be able to support its expansion in FY20E-21E. STRCEM also received a INR1.7b freight subsidy from the government in Apr 2019. Another INR0.7b is expected by 1HFY20.

Business moat intact; industry-best ROEs

We lower EBITDA for FY20/21E but continue to value the stock at 10x FY20E EV/EBITDA, on par with the sector. This can be justified, in our view, by its: a) market leadership; b) double-digit EPS growth thanks to volume growth and ASP hike; and c) potential ROEs of 22% vs 12% for peers due to higher profitability (EBITDA/t).

FYE Mar (INR m)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	16,145	18,310	22,055	25,945	30,113
EBITDA	5,214	4,492	5,206	6,066	7,050
Core net profit	3,307	2,995	3,860	4,586	5,491
Core EPS (INR)	8	7	9	11	13
Core EPS growth (%)	69.8	(9.4)	28.9	18.8	19.7
Net DPS (INR)	1	2	3	3	4
Core P/E (x)	14.7	13.8	11.6	9.8	8.2
P/BV (x)	3.3	2.5	2.3	2.0	1.8
Net dividend yield (%)	0.9	2.2	2.6	3.1	3.7
ROAE (%)	25.2	19.0	21.5	22.2	23.0
ROAA (%)	13.3	12.3	15.3	15.8	16.4
EV/EBITDA (x)	10.2	8.9	8.0	6.9	5.8
Net gearing (%) (incl perps)	26.8	net cash	net cash	net cash	net cash
Consensus net profit	-	-	3,602	4,138	na
MKE vs. Consensus (%)	-	-	7.2	10.8	na

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BUY

Share Price	INR 107
12m Price Target	INR 133 (+24%)
Previous Price Target	INR 147

Company Description

Star Cement Ltd. manufacturers and sells cement in the North Eastern and Eastern regions of India

Statistics

52w high/low (INR)	136/86
3m avg turnover (USDm)	0.3
Free float (%)	10.6
Issued shares (m)	419
Market capitalisation	INR44.8B USD645M

Major shareholders:

Promoter	69.8%
SBI Mutual Fund	5.4%
Sundaram Mutual Fund	2.1%

Price Performance



	-1M	-3M	-12M
Absolute (%)	10	22	(16)
Relative to index (%)	11	17	(22)

Source: FactSet

Lowering estimates

4Q EBITDA was 25% lower than consensus and our estimates. The deviations were: a) lower sales volume of 9% YoY vs our estimate of 15%; and b) higher discounts as demand was muted before elections.

We incorporate ASP hikes of 5%/2% for FY20E/21E vs our earlier assumption of 2% pa. This follows the industry's 5% price hike in April-19. Our volume-growth assumptions remain at 15% pa. We raise fuel costs to reflect its higher consumption of imported coal, possibly to 80% this year from 40% in FY19. The above cuts our EBITDA estimates by 8% and EPS by 10%/9%.

Fig 7: Revisions to our estimates

	Unit	New		Old		Change %	
		FY 20E	FY 21E	FY 20E	FY 21E	FY 20E	FY 21
Sales volume	mt	3.11	3.62	3.15	3.63	-1.3%	-0.4%
Revenue	INR m	22,055	25,945	21,949	25,510	0.5%	1.7%
ASP	INR /t	6,837	6,952	6,682	6,804	2.3%	2.2%
Opex cost	INR /t	5,162	5,275	4,874	4,988	5.9%	5.7%
EBITDA	INR m	5,206	6,066	5,724	6,594	-9.1%	-8.0%
EBITDA	INR/t	1,674	1,677	1,810	1,805	-7.5%	-7.1%
Depreciation	INR m	1,189	1,321	1,374	1,527	-13.5%	-13.5%
Interest Expense	INR m	24	0	24	0	0.0%	na
Net Profit	INR m	3,860	4,586	4,284	5,026	-9.9%	-8.8%
EPS	INR /sh	9.2	10.9	10.2	12.0	-9.9%	-8.8%

Source: Maybank Kim Eng

TP lowered by 9%; maintain BUY

Reflecting our forecast revisions, our TP drops to INR133. It remains based on 10x FY20E EV/EBITDA, on par with the sector. Reiterate BUY with catalysts still anticipated from commissioning of Siliguri plant.

Fig 8: Revised TP at INR133

		New	Old
EV/EBITDA Multiple	x	10.0	10.0
FY20E EBITDA	INR m	5,206	5,724
EV	INR m	52,056	57,241
Net Debt	INR m	(3,832)	(4,197)
No. of Shares	m	419	419
TP	INR /sh	133	147

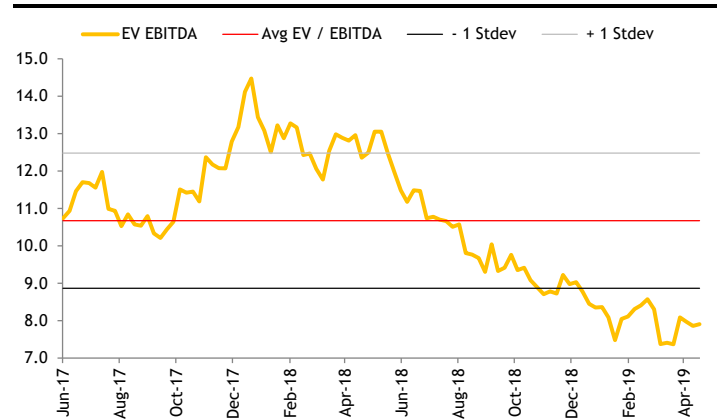
Source: Maybank Kim Eng

Fig 9: Share price



Source: Maybank Kim Eng, Bloomberg

Fig 10: Historically low EV/EBITDA (x)



Source: Maybank Kim Eng, Bloomberg

Fig 11: Comparisons with mid-cap cement players

Stock	Bloomberg Code	CMP INR/ sh	Rating	TP INR/ sh	Mkt Cap INR b	EV INR b	ROE %		PER x		PBV x		EV/EBITDA x	
							FY 20E	FY 21E	FY 20E	FY 21E	FY 20E	FY 21E	FY 20E	FY 21E
CEMENT STOCKS														
HEIDELBERGCEMENT	HEIM IN Equity	177	Not Rated	NA	40	43	21	21	14	12	3.0	2.5	10.3	9.5
Star Cement	STRCEM IN Equity	107	BUY	133	45	43	21	22	12	10	2.3	2.0	8.0	6.9
JK CEMENTS LTD	jkce IN Equity	840	Not Rated	NA	65	83	12	13	18	16	2.2	1.9	10.4	9.5
JK LAKSHMI CEMEN	JKLC IN Equity	352	Not Rated	NA	41	56	10	13	26	17	2.5	2.3	10.4	9.5
SAGAR CEMENTS	SGC IN Equity	608	Not Rated	NA	12	15	6	9	40	31	1.4	1.4	11.3	7.4
ORIENT CEMENT LT	ORCMNT IN Equity	109	Not Rated	NA	22	34	10	13	19	13	2.0	1.8	8.4	7.2
INDIA CEMENTS	ICEM IN Equity	99	Not Rated	NA	31	61	3	5	18	13	0.6	0.6	7.1	7.0
SANGHI INDUS LTD	SNGI IN Equity	62	Not Rated	NA	15	19	4	4	11	21	0.9	0.8	16.4	11.6
Cement stock - average							11	12	20	17	1.7	1.6	10.3	8.6

Source: Bloomberg, Maybank Kim Eng

Fig 1: Consolidated income statement for 4QFY19 and FY19

INR m	4QFY19	4QFY18	Change YoY	3QFY19	Change QoQ	FY19	FY18	Change YoY
Revenue	5,344	5,274	1%	4,164	28%	18,310	16,145	13%
Raw Material	1,374	714	93%	671	105%	4,367	2,741	59%
Employee cost	275	246	12%	300	-8%	1,164	1,074	8%
Power & fuel	782	750	4%	708	11%	2,625	2,176	21%
Freight	1,011	950	6%	777	30%	3,704	2,786	33%
Other exps	634	1,170	-46%	490	29%	1,958	2,155	-9%
Total expenditure	4,076	3,830	6%	2,945	38%	13,819	10,932	26%
EBITDA	1,269	1,444	-12%	1,219	4%	4,492	5,214	-14%
EBITDA Margins	24%	27%		29%		25%	32%	
Depreciation	238	241	-1%	264	-10%	1,056	1,207	-12%
Other income	34	28	21%	10	227%	55	44	26%
Interest	31	89	-65%	26	18%	144	525	-73%
PBT	1,034	1,143	-9%	939	10%	3,346	3,526	-5%
Tax	118	54	118%	102	16%	296	164	81%
Tax Rate %	11.4%	4.7%		10.9%		8.9%	4.7%	
PAT (before minority)	916	1,088	-16%	837	9%	3,050	3,362	-9%
PAT Margin	17%	21%		20%		17%	21%	

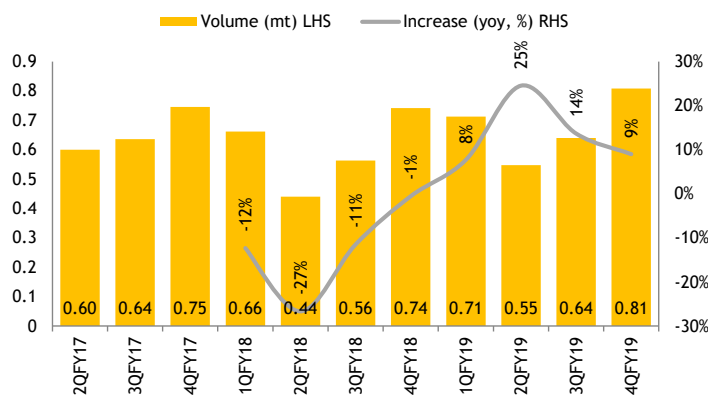
Source: Company

Fig 2: Per tonne analysis

INR/t	4QFY19	4QFY18	Change YoY	3QFY19	Change QoQ	FY19	FY18	Change YoY
Cement volume m tonne	0.81	0.74	9%	0.64	26%	2.71	2.40	13%
Revenue	6,608	7,108	-7%	6,507	2%	6,757	6,716	1%
EBITDA	1,569	1,947	-19%	1,905	-18%	1,658	2,169	-24%

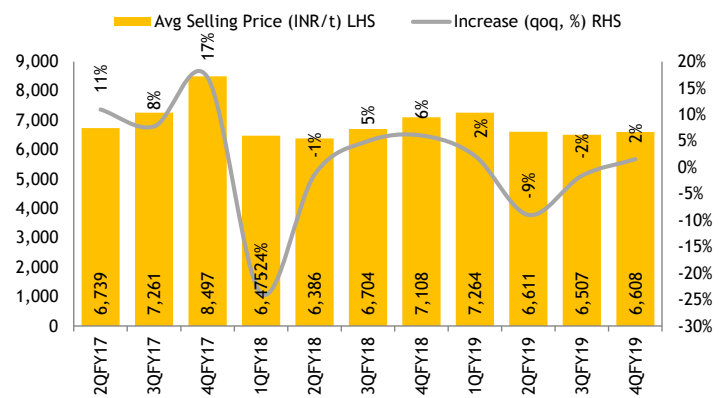
Source: Company

Fig 3: Volume growth at 9% YoY in 4QFY19



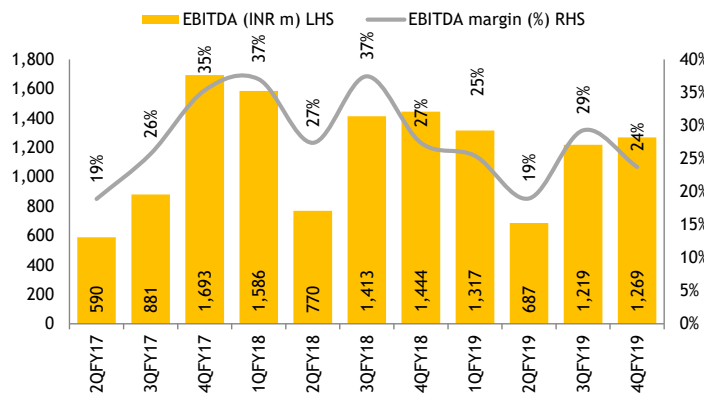
Source: Company

Fig 4: ASPs improved QoQ in 4QFY19 by 2%



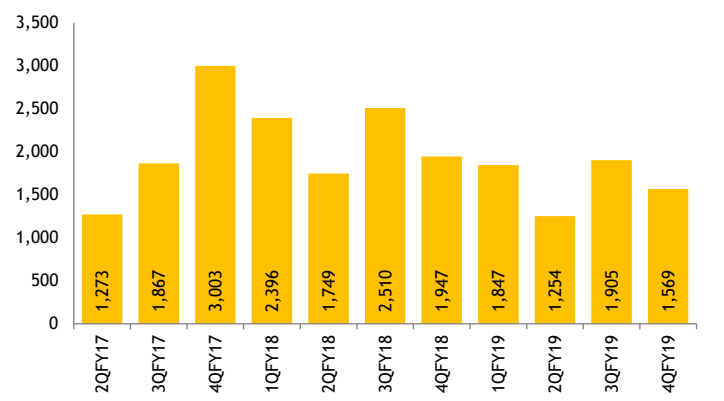
Source: Company

Fig 5: EBITDA margins declined QoQ



Source: Company

Fig 6: EBITDA/t (INR/t)

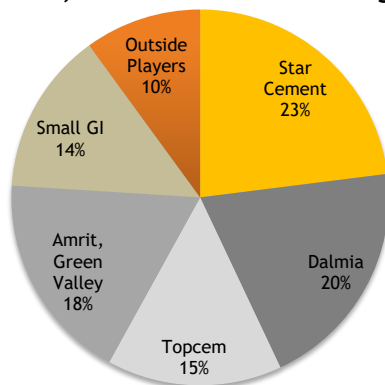


Source: Company

Value Proposition

- STRCEM is a market leader in the North East Region (NER) with a 23% market share.
- Government’s investment in the region in housing and infrastructure is expected to drive cement demand by 8-10% pa over the next 4-5 years in NER and ER (Eastern Region).
- STRCEM has industry leading profitability (EBITDA/t) due to premium pricing (NER) and government incentives.
- Locational advantage of its cement clinker and grinding unit provides it with an un-paralleled moat while doing business in the geographically difficult to access NER region of India.
- Highest ROE in the cement industry at 20%+.

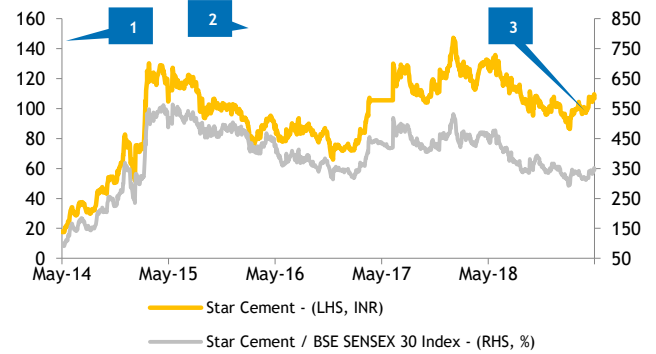
NER market share; STRCEM a leader in the region (FY18)



Source: Company

Price Drivers

Historical share price trend



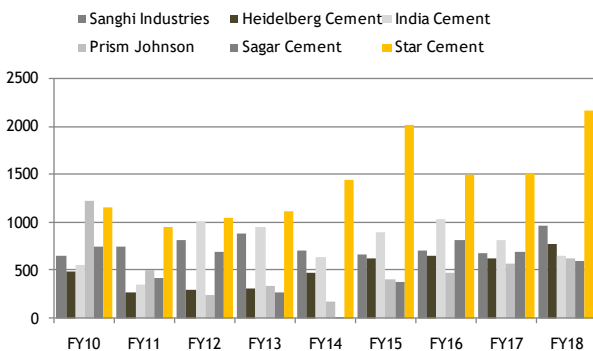
Source: Company, FactSet, Maybank Kim Eng

1. Listed in June 2017 on exchanges at price of INR130/sh.
2. Led by higher realization, posted highest quarterly EBITDA in 3QFY18 of INR2510/t.
3. Plant maintenance shutdown led to weak EBITDA/t at INR1254 in 2QFY19.

Financial Metrics

- Strengthening sales to the ER and rising demand from infra spending in NER leading to volume growth of 15% pa in FY20E/21E.
- Revenue growth of 20%/18% pa and EBITDA of 16%/17% in FY19E/20E (lower EBITDA growth is due to higher consumption of imported coal).
- Strong OCF of INR6-8b pa over FY20E-21E.
- Despite capex for Siliguri grinding unit and Meghalaya clinker unit, we forecast FCF yield of 7% in FY20E.

STRCEM’s industry leading profitability (EBITDA, INR/t)



Source: Company

Swing Factors

Upside

- Volume growth exceeds our current estimate of 15% pa during FY20-24E.
- Prices improve more than our assumption of 2% pa during FY20-21E.
- Commissioning of grinding unit in Siliguri by Dec-19.

Downside

- Increasing competition and resultant loss of market share in the NER.
- Weak demand in NER which leads to slower than forecast sales and profitability.
- Inability to pass on material increases in input cost.

FYE 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Key Metrics					
P/E (reported) (x)	14.9	15.4	11.6	9.8	8.2
Core P/E (x)	14.7	13.8	11.6	9.8	8.2
P/BV (x)	3.3	2.5	2.3	2.0	1.8
P/NTA (x)	14.7	13.8	11.6	9.8	8.2
Net dividend yield (%)	0.9	2.2	2.6	3.1	3.7
FCF yield (%)	8.1	17.2	6.0	2.4	4.4
EV/EBITDA (x)	10.2	8.9	8.0	6.9	5.8
EV/EBIT (x)	13.3	11.7	10.4	8.8	7.2
INCOME STATEMENT (INR m)					
Revenue	16,145.3	18,310.4	22,054.7	25,945.2	30,112.6
Gross profit	4,006.8	3,435.4	4,016.9	4,745.2	5,729.1
EBITDA	5,213.6	4,491.8	5,205.6	6,066.0	7,050.0
Depreciation	(1,206.9)	(1,056.4)	(1,188.6)	(1,320.8)	(1,320.8)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	4,006.8	3,435.4	4,016.9	4,745.2	5,729.1
Net interest income / (exp)	(524.6)	(143.8)	(23.6)	0.0	0.0
Associates & JV	0.0	0.0	0.0	0.0	0.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Other pretax income	43.9	54.7	302.1	346.6	355.8
Pretax profit	3,526.0	3,346.3	4,295.4	5,091.7	6,084.9
Income tax	(164.0)	(296.3)	(380.4)	(450.9)	(538.8)
Minorities	(55.2)	(55.2)	(55.2)	(55.2)	(55.2)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	3,306.8	2,994.8	3,859.8	4,585.6	5,490.9
Core net profit	3,306.8	2,994.8	3,859.8	4,585.6	5,490.9
BALANCE SHEET (INR m)					
Cash & Short Term Investments	197.8	2,528.1	3,832.0	3,869.4	4,502.2
Accounts receivable	1,464.7	1,707.0	1,812.7	2,132.5	2,475.0
Inventory	2,946.0	3,260.8	3,746.3	4,407.1	5,115.0
Property, Plant & Equip (net)	7,845.6	6,789.2	10,100.6	8,779.8	7,458.9
Intangible assets	0.0	0.0	0.0	0.0	0.0
Investment in Associates & JVs	0.0	0.0	0.0	0.0	0.0
Other assets	12,602.9	9,352.9	7,352.9	11,852.9	16,352.9
Total assets	25,057.1	23,638.0	26,844.5	31,041.7	35,904.1
ST interest bearing debt	2,336.2	536.2	0.0	0.0	0.0
Accounts payable	1,889.4	2,202.0	2,719.1	3,198.7	3,712.5
LT interest bearing debt	1,988.0	0.0	0.0	0.0	0.0
Other liabilities	3,459.0	3,543.0	4,243.0	4,971.0	5,750.0
Total Liabilities	9,672.5	6,281.4	6,962.5	8,169.6	9,462.6
Shareholders Equity	14,763.5	16,680.2	19,150.5	22,085.3	25,599.4
Minority Interest	621.1	676.4	731.6	786.9	842.1
Total shareholder equity	15,384.6	17,356.5	19,882.1	22,872.1	26,441.5
Total liabilities and equity	25,057.1	23,638.0	26,844.5	31,041.7	35,904.1
CASH FLOW (INR m)					
Pretax profit	3,526.0	3,346.3	4,295.4	5,091.7	6,084.9
Depreciation & amortisation	1,206.9	1,056.4	1,188.6	1,320.8	1,320.8
Adj net interest (income)/exp	524.6	89.1	(278.5)	(346.6)	(355.8)
Change in working capital	(345.4)	4,195.0	3,375.1	(34.1)	(36.5)
Cash taxes paid	(664.0)	(296.3)	(380.4)	(450.9)	(538.8)
Other operating cash flow	0.0	0.0	0.0	0.0	0.0
Cash flow from operations	4,206.2	8,390.4	8,200.3	5,581.0	6,474.6
Capex	(297.4)	(1,250.0)	(5,500.0)	(4,500.0)	(4,500.0)
Free cash flow	3,908.8	7,140.4	2,700.3	1,081.0	1,974.6
Dividends paid	0.0	(1,078.1)	(1,389.5)	(1,650.8)	(1,976.7)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	(2,988.4)	(3,788.0)	(536.2)	0.0	0.0
Other invest/financing cash flow	(478.3)	(89.1)	278.5	346.6	355.8
Effect of exch rate changes	0.0	0.0	0.0	0.0	0.0
Net cash flow	442.2	2,185.3	1,053.1	(223.2)	353.7

FYE 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Key Ratios					
Growth ratios (%)					
Revenue growth	5.7	13.4	20.4	17.6	16.1
EBITDA growth	27.7	(13.8)	15.9	16.5	16.2
EBIT growth	38.0	(14.3)	16.9	18.1	20.7
Pretax growth	64.2	(5.1)	28.4	18.5	19.5
Reported net profit growth	69.8	(9.4)	28.9	18.8	19.7
Core net profit growth	69.8	(9.4)	28.9	18.8	19.7
Profitability ratios (%)					
EBITDA margin	32.3	24.5	23.6	23.4	23.4
EBIT margin	24.8	18.8	18.2	18.3	19.0
Pretax profit margin	21.8	18.3	19.5	19.6	20.2
Payout ratio	12.7	30.0	30.0	30.0	30.0
DuPont analysis					
Net profit margin (%)	20.5	16.4	17.5	17.7	18.2
Revenue/Assets (x)	0.6	0.8	0.8	0.8	0.8
Assets/Equity (x)	1.7	1.4	1.4	1.4	1.4
ROAE (%)	25.2	19.0	21.5	22.2	23.0
ROAA (%)	13.3	12.3	15.3	15.8	16.4
Liquidity & Efficiency					
Cash conversion cycle	59.3	56.8	49.5	46.4	46.8
Days receivable outstanding	31.7	31.2	28.7	27.4	27.5
Days inventory outstanding	69.6	75.1	69.9	69.2	70.3
Days payables outstanding	41.9	49.5	49.1	50.2	51.0
Dividend cover (x)	7.9	3.3	3.3	3.3	3.3
Current ratio (x)	2.1	2.5	2.1	1.9	1.9
Leverage & Expense Analysis					
Asset/Liability (x)	2.6	3.8	3.9	3.8	3.8
Net gearing (%) (incl perps)	26.8	net cash	net cash	net cash	net cash
Net gearing (%) (excl. perps)	26.8	net cash	net cash	net cash	net cash
Net interest cover (x)	7.6	23.9	nm	nm	nm
Debt/EBITDA (x)	0.8	0.1	0.0	0.0	0.0
Capex/revenue (%)	1.8	6.8	24.9	17.3	14.9
Net debt/ (net cash)	4,126.3	(1,991.9)	(3,832.0)	(3,869.4)	(4,502.2)

Source: Company; Maybank

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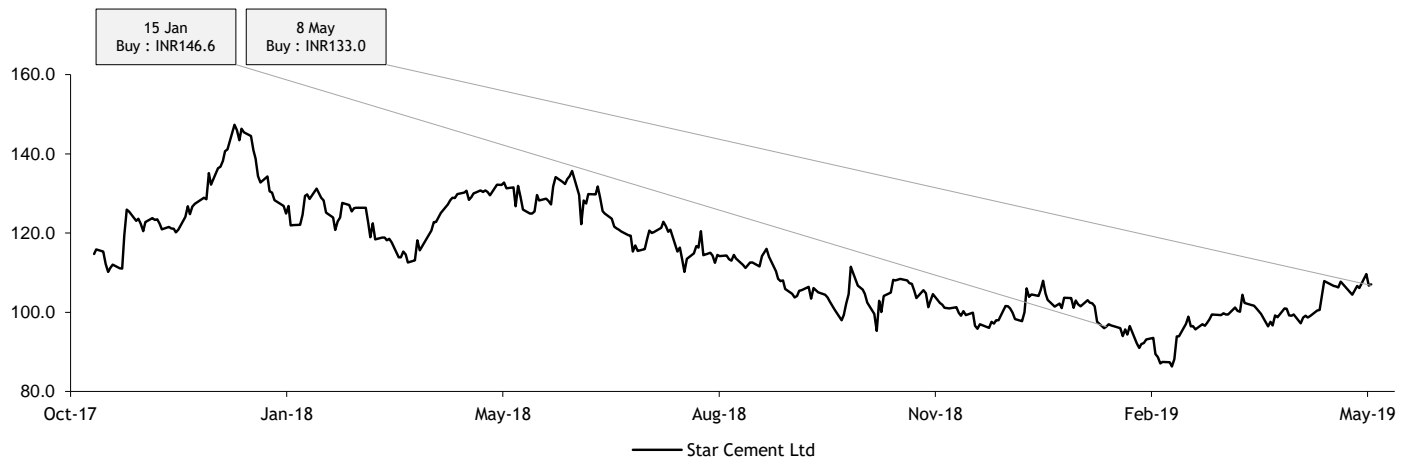
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