

16 August 2020

Star Cement

Expansion would help; retaining a Buy

Rating: **Buy**

Target Price: ₹115

Share Price: ₹88

With April a washout, Star's Q1 revenue/EBITDA/PAT fell 37%/42%/48%. On the Siligudi GU commissioning, operating costs would shrink. The EC for the Meghalaya clinker expansion continues to be delayed. Curtailed rural demand and floods in the company's markets are negatives, but management expects rising non-trade demand and government spending (at elections) to boost institutional demand. We retain our Buy on the stock, with a target of ₹115 (earlier ₹122).

Expansion to boost volumes. With East/North-east volumes falling 45%/35%, overall sales volumes slid 38% to 0.45m tons; realisation dipped 1.4% y/y to ₹8,199/ton. Local operators captured market share, but management is confident of regaining this. After Jun, prices in the NE fell; demand was hit by floods and shrinking rural demand. Management expects FY21 volumes similar to FY20, helped by expected government spending (on elections) and on the Siligudi plant commencing.

Cost rationalisation in process. EBITDA/ton slid 5.7% y/y to ₹1,455. Of the coal it required, 80% came locally, leading to savings. On various savings (advertising/travel/contracts renegotiated etc.), other expenses fell 38% y/y. With no salaries cut, employee cost rose 1.5% y/y. On the Siligudi GU commencing, rationalisation would be seen in logistic costs. We expect EBITDA/ton of ₹1,268/₹1,431 for FY21/22 (vs. ₹1,337 in FY20).

Outlook, Valuation. The Siligudi plant is now expected to commence by Sep'20 and the 12MW WHRS by end-FY22. Environmental clearance for the 2m-ton clinker expansion at Meghalaya has been delayed. Management expects the unlocking and greater institutional demand to normalise the lead distance and trade-nontrade mix to pre-Covid levels. The balance sheet is expected to be net cash (net D/E: -0.11x) in FY22. We expect volumes to dip 7% in FY21 and grow 15% in FY22. We retain our Buy rating, with a lower target price of ₹115 (10x FY22e EV/EBITDA). **Risks:** Rising operational costs, extensions of the lockdown.

Key Financials (YE Mar)	FY18	FY19	FY20	FY21e	FY22e
Sales (₹ m)	16,064	18,310	18,439	16,818	19,556
Net profit (₹ m)	3,307	2,988	2,855	2,047	2,671
EPS (₹)	7.9	7.1	6.9	5.0	6.5
PE (x)	14.7	13.8	9.8	17.7	13.6
EV / EBITDA (x)	10.2	8.9	6.5	9.6	7.5
EV / ton (\$)	189.5	143.8	92.3	78.2	78.9
RoE (%)	25.6	19.1	16.0	10.9	12.8
RoCE (%)	21.7	19.6	17.3	11.7	13.6
Dividend yield (%)	0.9	0.9	1.5	1.1	1.1
Net debt / equity (x)	0.3	-0.1	-0.1	-0.1	-0.1

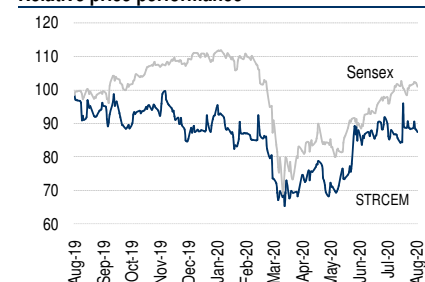
Source: Company, Anand Rathi Research

Key data	STRCEM IN
52-week high / low	₹106 / 56
Sensex / Nifty	37877 / 11178
3-m average volume	\$0.3m
Market cap	₹36bn / \$481.5m
Shares outstanding	412m

Shareholding pattern (%)	Jun-20	Mar-20	Dec-19
Promoters	66.8	66.8	67.1
- of which, Pledged	-	-	-
Free float	33.2	33.2	32.9
- Foreign institutions	0.2	0.2	0.3
- Domestic institutions	8.4	8.3	9.0
- Public	24.6	24.7	23.7

Estimates revision (%)	FY21e
Sales	(25.7)
EBITDA	(38.4)
PAT	(39.6)

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
Sales volumes (m tons)	2.4	2.7	2.9	2.7	3.1
Net revenues	16,064	18,310	18,439	16,818	19,556
<i>Growth (%)</i>	5.6	14.0	0.7	-8.8	16.3
Direct costs	3,025	4,367	4,019	3,646	4,112
SG&A	7,907	9,451	10,469	9,699	10,954
EBITDA	5,132	4,492	3,951	3,473	4,491
<i>EBITDA margins (%)</i>	31.9	24.5	21.4	20.7	23.0
- Depreciation	1,207	1,056	930	1,006	1,288
Other income	125	55	287	235	274
Interest expenses	525	144	93	55	50
PBT	3,526	3,346	3,215	2,647	3,427
<i>Effective tax rates (%)</i>	4.65	8.86	10.64	20.00	20.00
+ Associates / (Minorities)	55	62	18	70	70
Net income	3,307	2,988	2,855	2,047	2,671
Adjusted income	3,307	2,988	2,855	2,047	2,671
WANS	419	419	412	412	412
FDEPS (₹ / sh)	7.9	7.1	6.9	5.0	6.5
<i>FDEPS growth (%)</i>	69.8	-9.6	-2.9	-28.3	30.5

Fig 3 – Cash-flow statement (₹ m)

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
PBT	3,526	3,346	3,215	2,647	3,427
+ Non-cash items	1,207	1,056	930	1,006	1,288
Oper. prof. before WC	4,733	4,403	4,145	3,653	4,714
- Incr. / (decr.) in WC	91	-3,112	-1,309	-119	827
Others incl. taxes	733	683	342	529	685
Operating cash-flow	3,909	6,832	5,111	3,243	3,202
- Capex (tang. + intang.)	231	818	2,300	2,450	3,100
Free cash-flow	3,678	6,014	2,811	793	102
Acquisitions					
- Div. (incl. buyback & taxes)	505	458	1,517	412	412
+ Equity raised	0	-0	-	-	-
+ Debt raised	-3,683	-3,586	-402	-0	-
- Fin investments	-0	3	-1	-	-
- Misc. (CFI + CFF)	-506	52	187	-	-
Net cash-flow	-3	1,915	707	380	-311

Source: Company, Anand Rathi Research

Fig 5 – Price movement


Source: Bloomberg

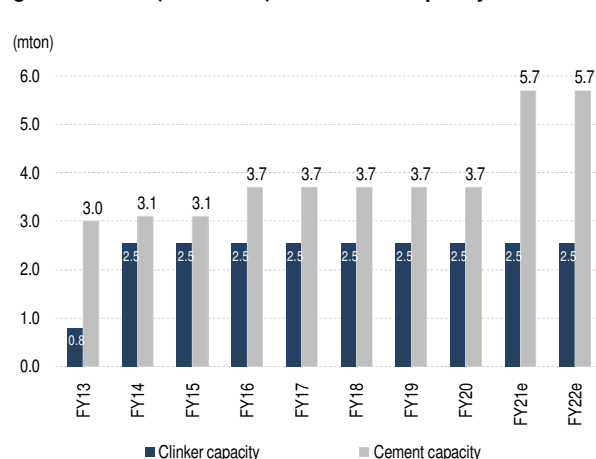
Fig 2 – Balance sheet (₹ m)

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
Share capital	419	419	412	412	412
Net worth	14,764	17,237	18,571	20,206	22,465
Debt	4,324	738	336	336	336
Minority interest	621	683	701	771	841
DTL / (Assets)	-2,329	-2,710	-2,893	-2,893	-2,893
Capital employed	17,380	15,947	16,714	18,419	20,748
Net tangible assets	7,845	7,221	6,957	9,178	9,590
Net intangible assets	2	2	2	2	2
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	357	743	2,375	1,600	3,000
Investments (strategic)	14	17	16	16	16
Investments (financial)	-	-	-	-	-
Current assets (ex cash)	14,311	10,161	8,516	8,201	9,644
Cash	198	2,113	2,820	3,200	2,889
Current liabilities	5,348	4,311	3,974	3,778	4,393
Working capital	8,963	5,851	4,542	4,423	5,251
Capital deployed	17,380	15,947	16,712	18,419	20,748
Contingent liabilities	545	712	-	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
P/E (x)	14.7	13.8	9.8	17.7	13.6
EV / EBITDA (x)	10.2	8.9	6.5	9.6	7.5
EV / Sales (x)	3.3	2.2	1.4	2.0	1.7
P/B (x)	3.3	2.4	1.5	1.8	1.6
RoE (%)	25.6	19.1	16.0	10.9	12.8
RoCE (%) - after tax	21.7	19.6	17.3	11.7	13.6
DPS (₹ / sh)	1.0	0.9	1.0	1.0	1.0
Dividend payout (%) - incl. DDT	15.3	15.3	17.4	20.1	15.4
Net debt / equity (x)	0.3	-0.1	-0.1	-0.14	-0.11
WC days	203	148	103	97	90
EV / ton (\$)	189.5	143.8	92.3	78.2	78.9
NSR / ton (₹)	7,681	7,979	8,076	8,156	8,276
EBITDA / ton (₹)	1,970	1,572	1,337	1,268	1,431
Volumes (m tons)	2.4	2.7	2.9	2.7	3.1
CFO : PAT (%)	118.2	228.7	179.0	158.4	119.8

Source: Company, Anand Rathi Research

Fig 6 – Cement (incl. hired) and clinker capacity


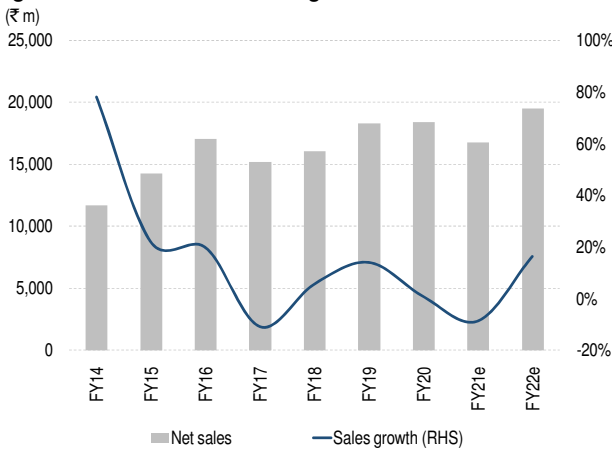
Source: Company

Other key highlights

Revenue growth

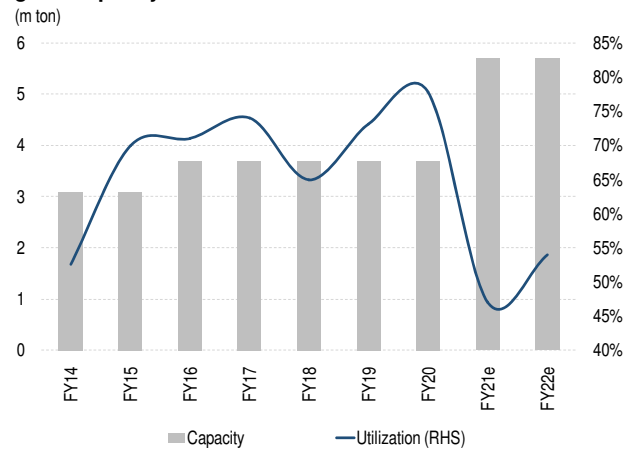
During the quarter, overall revenue declined 37% y/y to ₹2.9bn (cement ~down 39%, power 27%). In Apr, the company sold 15,000 tons, in May ~90% of May'19, and Jun volumes rose 2% over Jun'19. In Q1 FY21 0.447m tons of cement were sold, down 38% y/y. In the north-east, 0.343m tons were sold, down 35% y/y. Outside the north-east, the figure was 0.104m tons, down 45% y/y. Per management, May prices in the north-east have been flat; in the East, however, prices rose by ₹30-35/bag in May, then were rolled back by ₹20-25/bag in Jun'20. Gross realisations slipped 1.36% y/y to ₹8,199/ton in Q1 FY21.

Fig 7 – Revenue and Revenue growth



Source: Company, Anand Rathi Research

Fig 8 – Capacity and Utilisation

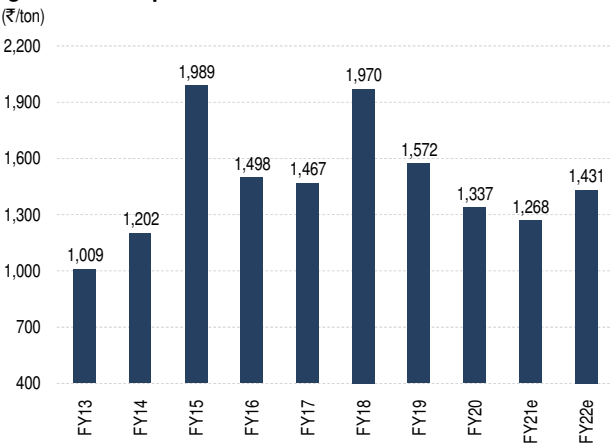


Source: Company, Anand Rathi Research

Operating performance

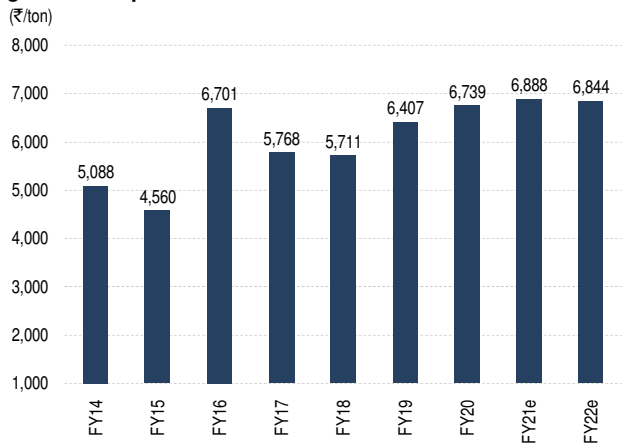
EBITDA for the quarter declined 41.75% y/y to ₹653m, with a 22.4% EBITDA margin. Raw material cost and Other expenses declined 39% and 38% respectively. Employee cost increased 1.5% with no salary reduction. EBITDA/ton declined 5.7% y/y to ₹1,455/ton. Adjusted profit declined 47% y/y to ₹442m on falling operating profit and other income (down 20% y/y) partially offset by depreciation down 8% y/y and interest cost down 40% y/y.

Fig 9 – EBITDA-per-ton trend



Source: Company, Anand Rathi Research

Fig 10 – Cost-per-ton trend



Source: Company, Anand Rathi Research

Result Highlights

Fig 11 – Quarterly performance

(₹ m)	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	% Y/Y	%Q/Q
Sales	3,774	5,274	5,179	3,623	4,164	5,344	4,609	3,825	4,512	5,494	2,920	(36.6)	(46.9)
EBITDA	1,413	1,444	1,317	687	1,219	1,269	1,121	644	940	1,246	653	(41.7)	(47.6)
EBITDA margins (%)	37	27	25	19	29	24	24	17	21	23	22	-196bps	-31bps
EBITDA per ton (₹)	2,360	1,799	1,632	1,236	1,861	1,510	1,542	1,067	1,248	1,426	1,455	(5.7)	2.0
Interest	137	89	54	33	26	31	28	8	38	20	17	(40.3)	(15.7)
Depreciation	337	241	283	271	264	238	222	225	232	250	204	(8.2)	(18.5)
Other income	2	28	3	7	10	34	74	77	65	72	59	(20.2)	(18.1)
PBT	942	1,143	983	390	939	1,034	945	487	734	1,048	492	(48.0)	(53.1)
Tax	28	54	68	8	102	118	106	34	22	180	49	(53.7)	(72.6)
PAT	914	1,088	915	382	837	916	839	453	712	868	442	(47.3)	(49.1)

Source: Company, Anand Rathi Research

Fig 12 – Per-ton analysis

(₹ per ton)	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	% Y/Y	%Q/Q
Realisations	7,269	8,148	7,980	7,352	8,099	8,298	8,312	8,105	7,745	8,134	8,199	(1.4)	0.8
EBITDA	2,360	1,799	1,632	1,236	1,861	1,510	1,542	1,067	1,248	1,426	1,455	(5.7)	2.0
Sales volumes (m tons)	0.6	0.7	0.7	0.5	0.6	0.8	0.7	0.6	0.7	0.8	0.4	(37.8)	(47.0)
Costs													
Raw material	949	1,162	1,327	1,405	1,294	1,184	1,166	1,213	1,213	1,129	1,409	20.9	24.8
Purchase of traded goods	318	220	282	364	243	255	311	228	273	180	259	(16.6)	44.3
Staff cost	488	331	376	585	469	341	415	490	450	415	678	63.3	63.3
Other expenses	2,710	3,450	3,369	2,709	3,085	3,011	3,088	3,306	3,141	3,255	3,077	(0.4)	(5.5)

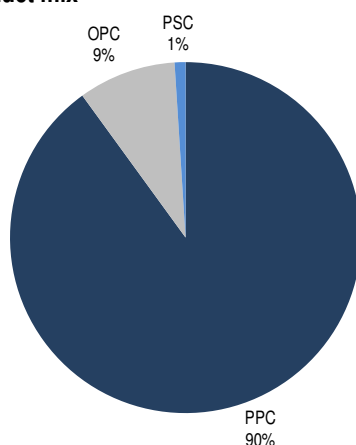
Source: Company, Anand Rathi Research

Concall Highlights

Operational and Financial highlights

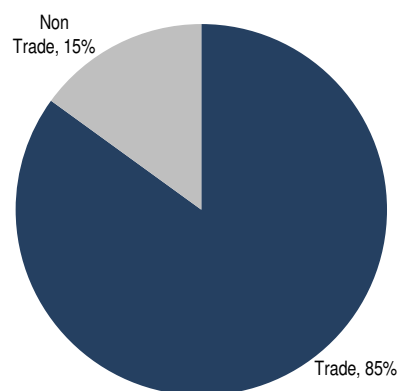
- In Q1 FY21, 0.447m tons of cement were sold, down 38% y/y. In the north-east, 0.343m tons were sold, down 35% y/y. Outside the north-east, the figure was 0.104m tons, down 45% y/y. Clinker sales declined to 0.02m tons (0.08m tons a year ago).
- The trade-nontrade sales-mix was 85:15. With improving institutional sales, management expects it to normalize again at 80:20.
- The PPC-OPC-PSC cement mix was 90:9:1.
- The lead distance increased to 290km (271km earlier) due to logistical hiccups from the lockdown.
- Greater availability of local coal led to the share of local coal used increasing to 80%. Imports were 20%.

Fig 13 – Product mix



Source: Company, Anand Rathi Research

Fig 14 – Trade: Non Trade mix



Source: Company, Anand Rathi Research

Capex / Capacity expansion

- The Siligudi plant is now expected to commence by Sep'20 and the 12MW WHRS, by end-FY22.
- The company is in the process of obtaining environmental clearances for the 2m-ton clinker expansion at the Meghalaya plant. The estimated timeline for completion is 24-30 months from commencing construction.

Others

- In Apr, the company sold 15,000 tons, in May ~90% of May'19, and Jun volumes increased 2% over Jun'19's.
- Management expects the Siligudi GU commencement to change the current Northeast-East sales-mix from ~70:30 to 60:40 and to rationalise logistic costs. Further, clinker exports (to Nepal) will shrink.
- In Jul, cement prices in the North-east fell a little due to floods; in the East, prices were flat.
- Though demand has now been affected by floods and shrinking rural demand, management expects a rise in government spending with

elections in West Bengal, Assam and Bihar, and FY21 volumes to be flat y/y.

- Coal India will auction 3.5m tons of coal, sufficient for what is required at Meghalaya for four years. The first auction, of 0.2m tons, will be held in the next 15-20 days.
- The clinker plant will be de-bottlenecked during the maintenance shutdown in Aug/Sep'20.
- Some market-share shift was seen toward local brands but the company expects this to soon reverse.
- The premium-cement contribution is 3-4% of overall sales volumes; management is aiming at 10% in the next 18-24 months.

Valuations

At the ruling price, the stock quotes at an EV/EBITDA of 7.5x and an EV/ton of \$79. We maintain our Buy recommendation on it, with a lower target price of ₹115 (earlier ₹122) based on 10x FY22e EV/EBITDA.

Change in estimates

We introduce FY22e, and reduce FY21e revenue, EBITDA and PAT by respectively 25.7%, 38.4% and 39.6% to give effect to the impact of the lockdown.

Fig 15 – Change in estimates

(₹m)	New estimates FY21e	Old estimates FY21e	Variance % chg
Sales	16,818	22,649	(25.7)
EBITDA	3,473	5,635	(38.4)
PAT	2,047	3,390	(39.6)

Source: Anand Rathi Research

Fig 16 – 12-month-forward EV/EBITDA: Mean and Standard deviation



Source: Bloomberg

Risk

- Extensions of the lockdown
- Mounting operational costs.

Fig 17 – Peer comparison - Valuations

	CMP (₹)	P/E		EV/EBITDA		EV/ton(\$)	
		FY21e	FY22e	FY21e	FY22e	FY21e	FY22e
Star Cement	88	17.1	13.2	9.6	7.5	78	79
Birla Corp.	613	15.6	12.2	7.8	6.8	61	51
Dalmia Bharat	790	NA	NA	8.3	7.3	102	90
Deccan Cement	295	8.9	6.4	4.4	2.9	21	18
Heidelberg Cement	181	18.6	13.5	9.0	6.9	82	76
India Cement	115	NA	30.0	12.8	9.4	57	58
JK Cement	1,513	31.5	20.1	15.0	10.9	119	113
JK Lakshmi	276	17.3	11.3	7.3	5.3	47	41
Mangalam Cement	203	14.7	8.3	7.0	5.0	38	35
NCL Indus	89	10.8	7.6	5.3	4.5	30	30
Orient Cement	69	24.5	12.3	7.4	5.6	40	37
Prism Johnson	48	NA	21.4	12.0	7.3	53	50
Ramco Cement	711	39.9	26.3	21.9	15.3	129	125
Sanghi Industries	24	NA	13.7	11.8	7.7	42	41

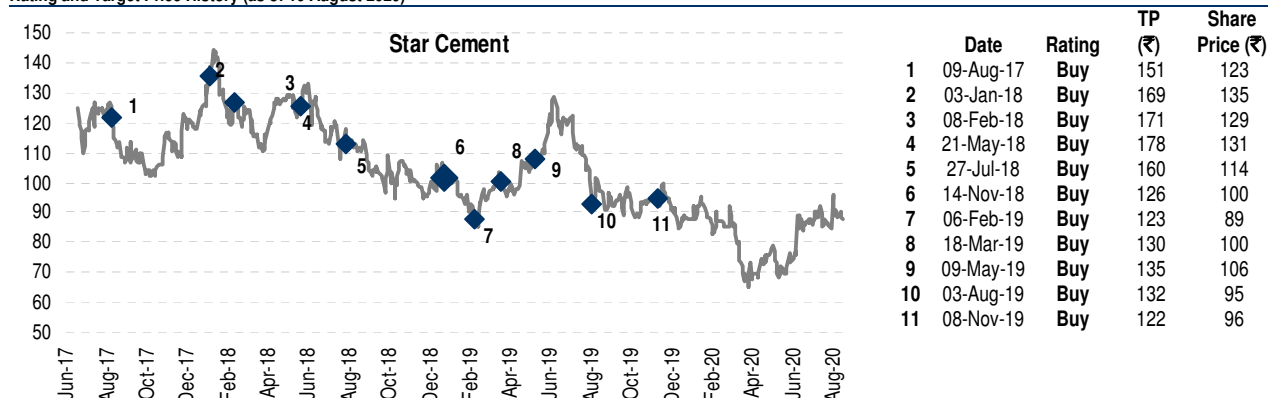
Source: Anand Rathi Research

Appendix

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Large Caps (>US\$1bn)	>15%	5-15%	<5%
Mid/Small Caps (<US\$1bn)	>25%	5-25%	<5%

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