

# Star Cement (STRCEM IN)

Declining margin trend appears to be a longer term concern

INDIA | CEMENT | Quarterly Update

7 February 2020

## Top takeaways from Q3FY20

- ✓ Operating performance was ahead of our estimates. EBITDA beats us 9%.
- ✓ Volumes remained exactly in-line; realisations were 6% lower but costs were too 9% lower and the key driver for positive surprise.
- ✓ From Q3 perspective EBITDA/tonne was 9% better than our estimate.
- ✗ However, this may not enough to compensate loss of earnings. We see our current estimates at risk as Star Cement has consistently been way below the 1500/tonne EBITDA mark consecutively for two quarters.
- ✗ We see risks to the earlier management guidance of sustainable long term EBITDA/tonne at Rs1,500-1,600/tonne.
- ✗ Resultantly, we cut our EBITDA estimates for Star Cement by 12% for FY21.
- ✓ We continue to realign all our target multiples in-line to our supply-chain thesis.
- ✗ We roll-over to FY22 and value Star Cement at 9x EBITDA revising our PO to Rs110 (vs. Rs125) earlier. We maintain BUY.

## Key highlights

Star Cement's Q3 performance was a beat but that may just not be enough to compensate the earnings loss, now sustainably for 2 quarters. We are concerned about a 6% qoq drop in realisation and we also see this as an indication of dilution of pricing power for Star Cement – an advantage Star Cement has sustainably enjoyed in our view in the past. We highlighted in our previous note in Q1 that cautious management commentary then on near term market outlook is a risk – this appears to be playing out.

## Q3 conference call takeaways

- Expansion plans are on track. Siliguri expansion to be commissioned within the next 3 months.
- Management remains positive on Q4 outlook – both pricing and demand.
- Prices within North-East have already increased by Rs10-12/bag and outside of North-East it has improved by Rs20-25/bag.
- 12-15 MW WHRS is being planned at the Meghalaya site – with a view to save costs and deliver on sustainability initiatives like reducing carbon footprints. Usage of alternate fuels also being planned in-line to same goals.
- Expects recent consolidation moves to be helpful for the industry to regain pricing power.
- Subsidies now outstanding of only Rs520 mn, expected to be received in this fiscal.
- Overall, a confident management commentary but we will like to remain cautious given the recent volatility seen in Star Cement earnings, especially Star Cement largely being a single region player (though it has some exposure to East India as well beyond North-East).

## Buy (Maintain)

CMP RS 88 / TARGET RS 110 (+25%)

SEBI CATEGORY: SMALL CAP

### COMPANY DATA

O/S SHARES (MN) :	419
MARKET CAP (RSBN) :	39
MARKET CAP (USDBN) :	0.5
52 - WK HI/LO (RS) :	138 / 35
LIQUIDITY 3M (USDMN) :	0.3
PAR VALUE (RS) :	1

### SHARE HOLDING PATTERN, %

	Dec 19	Sep 19	Jun 19
PROMOTERS :	67.1	67.9	67.9
FII / NRI :	1.1	1.6	1.7
FI / MF :	8.2	8.4	8.6
NON PRO :	15.5	15.4	14.8
PUBLIC & OTHERS :	8.2	6.6	7.0

### KEY FINANCIALS

Rs mn	FY19	FY20E	FY21E
Net Sales	18,310	19,592	24,216
EBIDTA	4,492	4,190	4,809
Net Profit	2,988	2,525	2,808
EPS, Rs	7.1	6.1	6.8
PER, x	12.9	15.1	13.5
EV/EBIDTA, x	8.5	9.5	8.5
P/BV, x	2.2	2.0	1.8
ROE, %	17.3	13.1	13.0

### CHANGE IN ESTIMATES

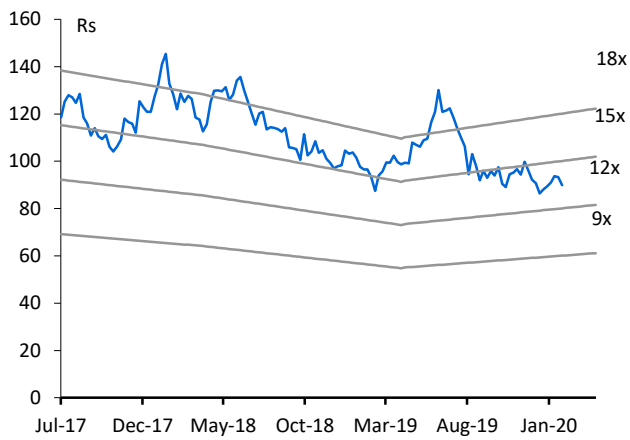
Rs bn	Revised Est.		% Revision	
	FY21E	FY22E	FY21E	FY22E
Revenue	24.2	29.9	0%	-
EBITDA	4.8	5.6	-12%	-
Core PAT	2.8	3.3	-18%	-
EPS (Rs)	6.8	8.0	-17%	-

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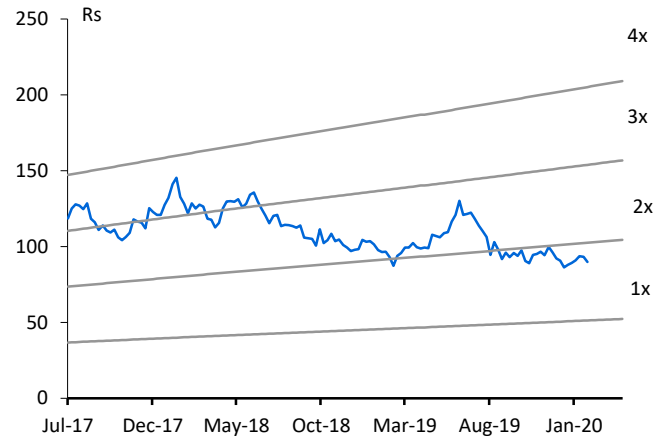
(Rs mn)	Q2FY20	Q3FY19	yoy	Q2FY20	qoq vs. expect. %	Comments
<b>Net Sales</b>	<b>4,512</b>	<b>4,164</b>	<b>8%</b>	<b>3,825</b>	<b>18%</b>	-5%
Volumes	0.75	0.66	15%	0.60	25%	Volumes in-line to estimate
Net Realisation	5,984	6,358	-6%	6,343	-6%	Realisations were lower
Total Expenditure	3,572	2,945	21%	3,181	12%	Costs surprised positively
<b>EBITDA</b>	<b>940</b>	<b>1,219</b>	<b>-23%</b>	<b>644</b>	<b>46%</b>	9% EBITDA surprise driven by lower cost
EBITDA margin	21%	29%		17%		
EBITDA/tonne	1,246	1,861	-33%	1,067	17%	
Depreciation	232	264	-12%	225	3%	
Other Income	65	10		76		
<b>EBIT</b>	<b>772</b>	<b>965</b>	<b>-20%</b>	<b>494</b>	<b>56%</b>	
Interest	38	26	47%	8	399%	
<b>PBT</b>	<b>734</b>	<b>939</b>	<b>-22%</b>	<b>487</b>	<b>51%</b>	
<b>PAT</b>	<b>712</b>	<b>837</b>	<b>-15%</b>	<b>452</b>	<b>57%</b>	

One-year forward band chart

PE band



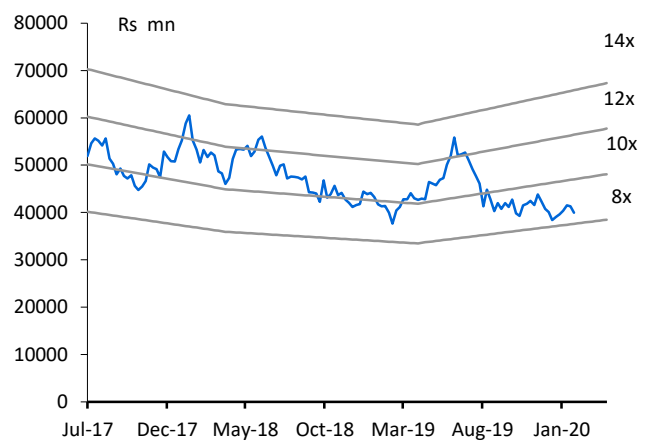
PBV band



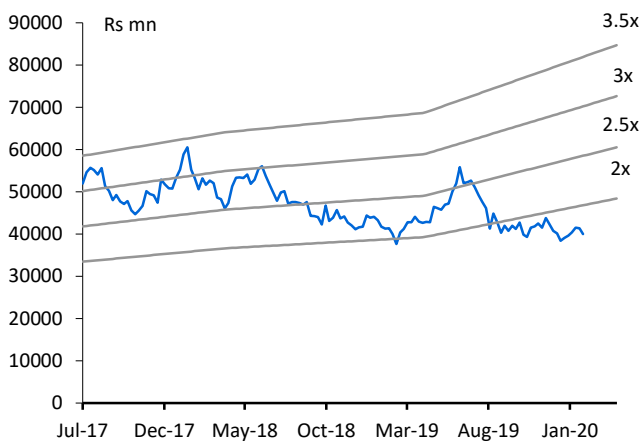
M-cap/sales band



EV/EBIDTA band



EV/sales band



Source: PhillipCapital India Research Estimates

## Financials

### Income Statement

Y/E Mar, Rs mn	FY19	FY20e	FY21e	FY22e
<b>Net sales</b>	<b>18,310</b>	<b>19,592</b>	<b>24,216</b>	<b>29,931</b>
Growth, %	13	7	24	24
Total income	18,310	19,592	24,216	29,931
Raw material expenses	-4,367	-4,720	-5,865	-7,289
Employee expenses	-1,164	-1,283	-1,586	-1,960
Other Operating expenses	-8,287	-9,399	-11,956	-15,065
<b>EBITDA (Core)</b>	<b>4,492</b>	<b>4,190</b>	<b>4,809</b>	<b>5,617</b>
Growth, %	(13.8)	(6.7)	14.8	16.8
Margin, %	24.5	21.4	19.9	18.8
Depreciation	-1,056	-1,102	-1,362	-1,492
<b>EBIT</b>	<b>3,435</b>	<b>3,088</b>	<b>3,447</b>	<b>4,126</b>
Growth, %	(14.3)	(10.1)	11.6	19.7
Margin, %	18.8	15.8	14.2	13.8
Interest paid	-144	-117	-141	-235
Other Non-Operating Income	55	60	66	73
<b>Pre-tax profit</b>	<b>3,346</b>	<b>3,032</b>	<b>3,373</b>	<b>3,964</b>
Tax provided	-296	-455	-506	-595
<b>Profit after tax</b>	<b>3,050</b>	<b>2,577</b>	<b>2,867</b>	<b>3,369</b>
Others (Minorities, Associates)	-62	-52	-58	-68
<b>Net Profit</b>	<b>2,988</b>	<b>2,525</b>	<b>2,808</b>	<b>3,301</b>
Growth, %	(9.6)	(15.5)	11.2	17.5
<b>Net Profit (adjusted)</b>	<b>2,988</b>	<b>2,525</b>	<b>2,808</b>	<b>3,301</b>
Unadj. shares (m)	419	413	413	413
Wtd avg shares (m)	419	413	413	413

### Balance Sheet

Y/E Mar, Rs mn	FY19	FY20e	FY21e	FY22e
Cash & bank	2,113	1,093	1,093	1,093
Debtors	1,438	1,692	2,301	3,128
Inventory	2,772	3,263	4,436	6,032
Loans & advances	3,462	3,704	4,578	5,660
Other current assets	5,200	5,564	6,878	8,502
Total current assets	14,985	15,316	19,286	24,415
Investments	17	17	17	17
Gross fixed assets	7,223	9,725	11,225	11,725
Add: Capital WIP	743	1,500	500	500
Net fixed assets	7,966	11,225	11,725	12,225
<b>Total assets</b>	<b>22,969</b>	<b>26,559</b>	<b>31,028</b>	<b>36,657</b>
Current liabilities	3,300	3,531	4,364	5,395
Provisions	113	121	149	184
Total current liabilities	3,413	3,651	4,513	5,579
Non-current liabilities	1,636	2,892	4,108	5,778
Total liabilities	5,049	6,543	8,621	11,357
Paid-up capital	419	413	413	413
Reserves & surplus	16,817	18,867	21,200	24,025
Shareholders' equity	17,920	20,015	22,407	25,300
<b>Total equity &amp; liabilities</b>	<b>22,969</b>	<b>26,559</b>	<b>31,028</b>	<b>36,657</b>

### Cash Flow

Y/E Mar, Rs mn	FY19	FY20e	FY21e	FY22e
Pre-tax profit	3,346	3,032	3,373	3,964
Depreciation	1,056	1,102	1,362	1,492
Chg in working capital	1,907	-1,113	-3,107	-4,064
Total tax paid	-296	-455	-506	-595
<b>Cash flow from operating activities</b>	<b>6,013</b>	<b>2,566</b>	<b>1,121</b>	<b>797</b>
Capital expenditure	-818	-4,360	-1,862	-1,992
Chg in investments	-3	0	0	0
Other investing activities	-515	0	0	0
<b>Cash flow from investing activities</b>	<b>-1,336</b>	<b>-4,360</b>	<b>-1,862</b>	<b>-1,992</b>
Free cash flow	4,677	-1,794	-741	-1,194
Debt raised/(repaid)	-2,762	1,256	1,216	1,670
<b>Cash flow from financing activities</b>	<b>-2,762</b>	<b>774</b>	<b>741</b>	<b>1,194</b>
Net chg in cash	1,915	-1,020	0	0

### Valuation Ratios

	FY19	FY20e	FY21e	FY22e
<b>Per Share data</b>				
EPS (INR)	7.1	6.1	6.8	8.0
Growth, %	(9.6)	(14.3)	11.2	17.5
Book NAV/share (INR)	41.1	46.6	52.3	59.1
FDEPS (INR)	7.1	6.1	6.8	8.0
CEPS (INR)	9.6	8.8	10.1	11.6
CFPS (INR)	14.2	6.1	2.6	1.8
<b>Return ratios</b>				
Return on assets (%)	13.3	10.9	10.4	10.6
Return on equity (%)	17.3	13.1	13.0	13.5
Return on capital employed (%)	16.1	12.6	12.1	12.4
<b>Turnover ratios</b>				
Asset turnover (x)	1.0	1.0	1.0	1.1
Sales/Total assets (x)	0.8	0.8	0.8	0.9
Sales/Net FA (x)	2.3	2.0	2.1	2.5
Working capital/Sales (x)	0.5	0.5	0.6	0.6
Receivable days	28.7	31.5	34.7	38.1
Inventory days	55.3	60.8	66.9	73.6
Payable days	33.1	31.8	31.2	30.8
Working capital days	190.8	199.2	208.4	218.6
<b>Liquidity ratios</b>				
Current ratio (x)	4.5	4.3	4.4	4.5
Quick ratio (x)	3.7	3.4	3.4	3.4
Interest cover (x)	23.9	26.5	24.4	17.5
Total debt/Equity (%)	9.5	15.0	19.0	23.6
Net debt/Equity (%)	(2.8)	9.3	14.0	19.2
<b>Valuation</b>				
PER (x)	12.9	15.1	13.5	11.5
PEG (x) - y-o-y growth	(1.3)	(1.1)	1.2	0.7
Price/Book (x)	2.2	2.0	1.8	1.6
EV/Net sales (x)	2.1	2.0	1.7	1.4
EV/EBITDA (x)	8.5	9.5	8.5	7.6
EV/EBIT (x)	11.1	12.9	11.9	10.4

Source: Company, PhillipCapital India Research Estimates

## Stock Price, Price Target and Rating History



## Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year. We have different threshold for large market capitalisation stock and Mid/small market capitalisation stock. The categorisation of stock based on market capitalisation is as per the SEBI requirement.

### Large cap stocks

Rating	Criteria	Definition
BUY	$\geq +10\%$	Target price is equal to or more than 10% of current market price
NEUTRAL	$-10\% > \text{to} < +10\%$	Target price is less than +10% but more than -10%
SELL	$\leq -10\%$	Target price is less than or equal to -10%.

### Mid cap and Small cap stocks

Rating	Criteria	Definition
BUY	$\geq +15\%$	Target price is equal to or more than 15% of current market price
NEUTRAL	$-15\% > \text{to} < +15\%$	Target price is less than +15% but more than -15%
SELL	$\leq -15\%$	Target price is less than or equal to -15%.

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