

9 May 2019

Star Cement

*Forthcoming capex to drive growth; retaining a Buy*Rating: **Buy**

Target Price: ₹135

Share Price: ₹106

Sturdy demand continued to drive Star Cement's performance, though profitability suffered from higher costs. Its continuous efforts on cost rationalisation, however, government subsidies and a strong demand outlook would boost its performance. Despite capex for coming expansions, the company would still hold to a net cash position in FY21. We are sanguine about its prospects and retain our Buy rating, with a target of ₹135.

Decent revenue growth. On the 8.6% y/y volume growth to ₹0.81m tons, cement revenue grew 6.5% y/y. In its key north-eastern market, demand was chiefly driven by the infrastructure sector. It being a market leader and premium pricing in the north-east are likely to boost its performance in coming quarters. Its high, ~82%, share in retail markets would further aid realisations. We expect a 14% revenue CAGR over FY19-21 bolstered by capacity expansion at Siligudi (2m tons).

Cost pressures to persist. In Q4 FY19, EBITDA/ton declined 16% y/y, to ₹1,510, chiefly on the expiration of the transport subsidy, decrease in inventories and higher fuel costs (~₹100/ton). Management expects the ban on coal mining to continue in FY20. The impact would be ~₹200/ton, which we believe, the company will counter-balance through a small price hike. Ahead, various measures implemented in optimising costs and rationalising freight would lead to a better operational performance. We expect FY21 EBITDA/ton at ₹1,732.

Outlook and Valuation. The company's coming expansion plans are on track. The Siligudi plant is expected to be commissioned by Q3 FY20, and a debottlenecking exercise is expected in Q2 FY20. Capex estimated by the company for FY20 is ₹3.5bn. Despite capex plans, with the aid of subsidies, the net-debt-to-equity will be ~-0.2x in FY21. We expect a 12% PAT CAGR over FY19-21. With the better growth prospects and operational performance, we retain our Buy rating with a higher target price of ₹135 based on 10x FY21e EV/EBITDA. **Risk:** Rising operational costs.

Key Financials (YE Mar)	FY17	FY18	FY19	FY20e	FY21e
Sales (₹ m)	15,215	16,064	18,310	20,283	23,835
Net profit (₹ m)	1,947	3,307	2,988	3,176	3,778
EPS (₹)	4.6	7.9	7.1	7.6	9.0
PE (x)	30.2	14.7	14.9	14.0	11.8
EV / EBITDA (x)	16.6	10.2	9.5	7.7	6.6
EV / ton (\$)	268.7	212.1	172.8	117.6	116.7
RoE (%)	19.2	25.6	19.1	17.5	18.0
RoCE (%)	15.1	21.7	15.9	17.2	17.6
Dividend yield (%)	-	0.9	1.0	1.1	1.3
Net debt / equity (x)	0.6	0.3	-0.1	-0.2	-0.2

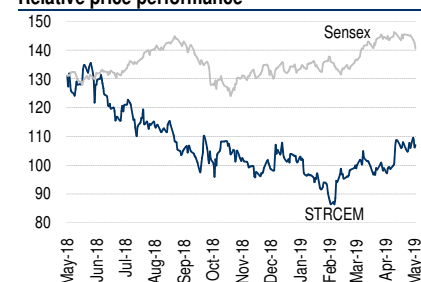
Source: Company, Anand Rathi Research

Key data	STRCEM IN
52-week high / low	₹137 / 80
Sensex / Nifty	37726 / 11340
3-m average volume	\$0.3m
Market cap	₹45bn / \$650.8m
Shares outstanding	419m

Shareholding pattern (%)	Mar'19	Dec'18	Sept'18
Promoters	68.0	68.9	68.9
- of which, Pledged	0.2	0.1	0.1
Free float	32.0	31.1	31.1
- Foreign institutions	1.2	1.2	1.0
- Domestic institutions	8.7	8.7	8.4
- Public	22.1	21.2	21.7

Estimates revision (%)	FY20e	FY21e
Sales	(3.8)	(3.4)
EBITDA	(0.4)	(1.4)
PAT	(0.6)	(1.8)

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY17	FY18	FY19	FY20e	FY21e
Sales volumes (m tons)	2.7	2.4	2.7	3.2	3.5
Net revenues	15,215	16,064	18,310	20,283	23,835
Growth (%)	-11.0	5.6	14.0	10.8	17.5
Direct costs	3,403	3,025	4,367	3,348	3,952
SG&A	7,792	7,907	9,451	11,601	13,760
EBITDA	4,021	5,132	4,492	5,334	6,123
EBITDA margins (%)	26.4	31.9	24.5	26.3	25.7
- Depreciation	1,179	1,207	1,056	1,250	1,300
Other income	87	125	55	32	32
Interest expenses	781	525	144	59	45
PBT	2,148	3,526	3,346	4,057	4,810
Effective tax rates (%)	6.47	4.65	20.00	20.00	20.00
+ Associates / (Minorities)	62	55	62	70	70
Net income	1,947	3,307	2,988	3,176	3,778
Adjusted income	1,947	3,307	2,988	3,176	3,778
WANS	419	419	419	419	419
FDEPS (₹/ sh)	4.6	7.9	7.1	7.6	9.0
FDEPS growth (%)	44.7	69.8	-9.6	6.3	18.9

Fig 3 – Cash-flow statement (₹ m)

Year-end: Mar	FY17	FY18	FY19	FY20e	FY21e
PBT	2,148	3,526	3,346	4,057	4,810
+ Non-cash items	1,179	1,207	1,056	1,250	1,300
Oper. prof. before WC	3,327	4,733	4,403	5,307	6,110
- Incr. / (decr.) in WC	898	91	-626	-2,446	1,031
Others incl. taxes	418	733	296	811	962
Operating cash-flow	2,011	3,909	4,733	6,942	4,116
- Capex (tang. + intang.)	679	231	818	4,500	3,100
Free cash-flow	1,332	3,678	3,915	2,442	1,016
Acquisitions	-	-	-	-	-
- Div. (incl. buyback & taxes)	-	505	551	586	695
+ Equity raised	-	0	-0	-	-
+ Debt raised	-1,383	-3,683	-3,811	-7	-
- Fin investments	0	-0	3	-3	-
- Misc. (CFI + CFF)	-6	-506	-2,365	-	-
Net cash-flow	-44	-3	1,915	1,852	321

Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 2 – Balance sheet (₹ m)

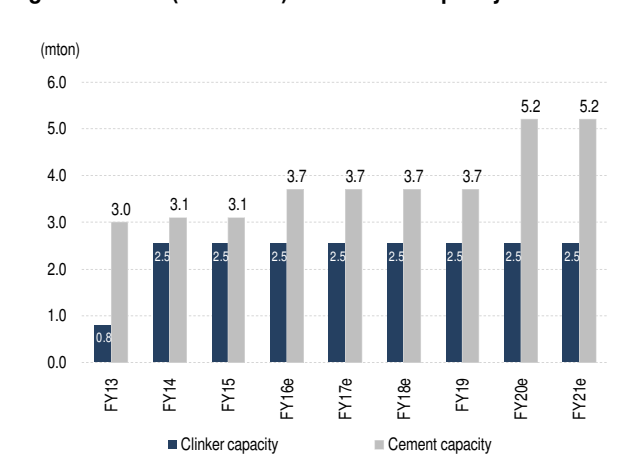
Year-end: Mar	FY17	FY18	FY19	FY20e	FY21e
Share capital	419	419	419	419	419
Net worth	11,460	14,764	17,237	19,826	22,909
Debt	8,007	4,324	513	507	507
Minority interest	566	621	683	753	823
DTL/(Assets)	-1,765	-2,329	-	-	-
Capital employed	18,268	17,380	18,433	21,086	24,239
Net tangible assets	8,631	7,845	7,219	10,212	10,012
Net intangible assets	2	2	2	2	2
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	549	357	743	1,000	3,000
Investments (strategic)	15	14	17	17	17
Investments (financial)	-	-	-	-	-
Current assets (ex cash)	13,641	14,311	12,872	11,503	13,517
Cash	201	198	2,113	3,965	4,286
Current liabilities	4,769	5,348	4,536	5,613	6,595
Working capital	8,872	8,963	8,336	5,891	6,922
Capital deployed	18,268	17,380	18,433	21,086	24,239
Contingent liabilities	566	545	-	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY17	FY18	FY19	FY20e	FY21e
P/E (x)	30.2	14.7	14.9	14.0	11.8
EV / EBITDA (x)	16.6	10.2	9.5	7.7	6.6
EV / Sales (x)	4.4	3.3	2.3	2.0	1.7
P/B (x)	5.1	3.3	2.6	2.2	1.9
RoE (%)	19.2	25.6	19.1	17.5	18.0
RoCE (%) - after tax	15.1	21.7	15.9	17.2	17.6
DPS (₹ / sh)	-	1.0	1.1	1.2	1.4
Dividend payout (%) - incl. DDT	-	15.3	18.4	18.5	18.4
Net debt / equity (x)	0.6	0.3	-0.1	-0.2	-0.16
WC days	202	203	172	128	98
EV / ton (\$)	268.7	212.1	172.8	117.6	116.7
NSR / ton (₹)	7,235	8,338	8,392	7,970	8,250
EBITDA / ton (₹)	1,467	2,138	1,653	1,690	1,732
Volumes (m tons)	2.7	2.4	2.7	3.2	3.5
CFO : PAT (%)	103.3	118.2	158.4	218.6	109.0

Source: Company, Anand Rathi Research

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



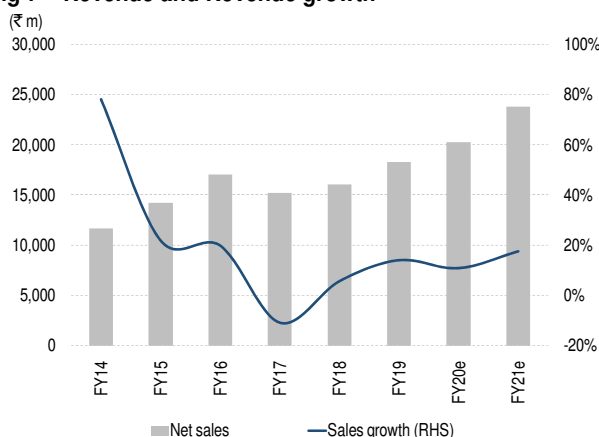
Source: Company

Other key highlights

Revenue growth

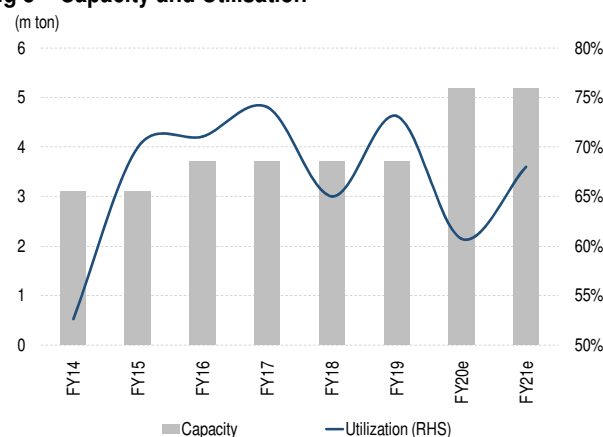
Cement revenue grew 6.5% y/y; however, overall revenue increased only 1.3% y/y to ₹5.34bn due to higher inter-segment sales. The continuous pick-up in demand led to a decent, 8.6%, rise in cement volumes to 0.81m tons. Favourable pricing in the north-east led to realisations increasing 1.84% y/y to ₹8,298 a ton, thus contributing to revenue growth. We expect a 14% CAGR in revenue over FY19-21.

Fig 7 – Revenue and Revenue growth



Source: Company, Anand Rathi Research

Fig 8 – Capacity and Utilisation

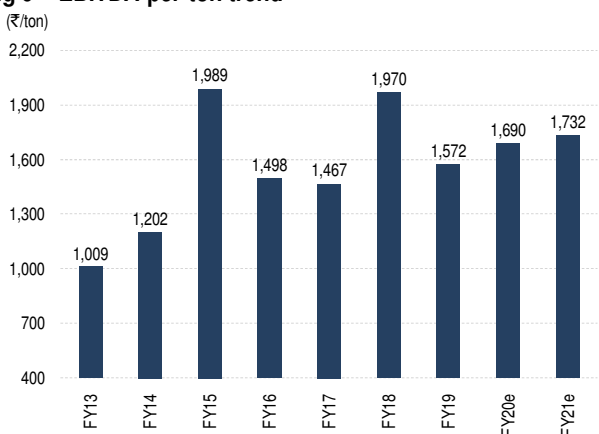


Source: Company, Anand Rathi Research

Operating performance

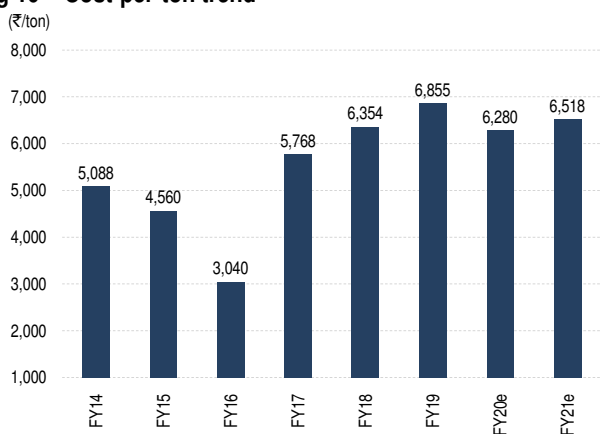
The Q4 FY19 EBITDA/ton dipped 16% y/y to ₹1,510. This was largely due to higher per-ton cost of purchase of traded goods, raw materials and staff costs, respectively 16.3%, 1.9% and 3% y/y. This was partially offset by savings in other-expenditure-per-ton, of 12.7% y/y. Adj. PAT was reported at ₹916m, down 15.9% y/y, due to the restrained operating performance and higher tax expenses. This was partially offset by the 65.4% y/y decline in interest, and 1.3% in depreciation.

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)	Q2 FY17	Q3 FY17	Q4 FY17	Q1 FY18	Q2 FY18	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	% Y/Y	%Q/Q
Sales	3,120	3,927	4,792	4,287	2,810	3,774	5,274	5,179	3,623	4,164	5,344	1.3	28.3
EBITDA	590	870	1,693	1,586	770	1,413	1,444	1,317	687	1,219	1,269	(12.2)	4.1
EBITDA margins (%)	19	22	35	37	27	37	27	25	19	29	24	-365bps	-554bps
EBITDA per ton (₹)	827	1,169	2,135	2,415	1,592	2,360	1,799	1,632	1,094	1,861	1,510	(16.0)	(18.9)
Interest	199	186	184	157	141	137	89	54	33	26	31	(65.4)	18.1
Depreciation	358	356	122	303	326	337	241	283	271	264	238	(1.3)	(10.0)
Other income	5	12	20	4	9	2	28	3	7	10	34	21.4	227.1
PBT	40	334	1,407	1,130	311	942	1,143	983	390	939	1,034	(9.5)	10.1
Tax	13	0	127	33	49	28	54	68	8	102	118	118.3	15.7
PAT	24	339	1,280	1,097	263	914	1,088	915	382	837	916	(15.9)	9.4

Source: Anand Rath Research

Fig 12 – Per-ton analysis

(₹ per ton)	Q2 FY17	Q3 FY17	Q4 FY17	Q1 FY18	Q2 FY18	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	% Y/Y	% Q/Q
Realisations	5,139	5,808	5,870	8,911	5,902	7,269	8,148	7,980	6,509	8,099	8,298	1.8	2.5
EBITDA	827	1,169	2,135	2,415	1,592	2,360	1,799	1,632	1,094	1,861	1,510	(16.0)	(18.9)
Sales volumes (m tons)	0.6	0.7	0.8	0.6	0.4	0.6	0.7	0.7	0.5	0.6	0.8	8.6	25.9
Costs													
Raw material	806	842	1,005	1,107	798	949	1,162	1,327	1,405	1,294	1,184	1.9	(8.5)
Purchase of traded goods	347	597	240	253	223	318	220	282	364	243	255	16.3	5.3
Staff cost	530	439	384	459	610	488	331	376	585	469	341	3.0	(27.2)
Other expenses	2,421	2,528	2,545	2,606	2,386	2,710	3,450	3,369	2,709	3,085	3,011	(12.7)	(2.4)

Source: Anand Rath Research

Change in estimates

Factoring in the Q4 FY19 performance, we lower our FY20e and FY21e revenue, respectively 3.8% and 3.4%. We also lower our FY20e and FY21e EBITDA 0.4% and 1.4% and PAT 0.6% and 1.8% respectively. With better volume growth expected in coming years and deleveraging, we expect Star Cement to post a better operating performance.

Fig 13 – Change in estimates

(₹ m)	New		Old		Variance	
	FY20e	FY21e	FY20e	FY21e	% chg	% chg
Sales	20,283	23,835	21,084	24,673	(3.8)	(3.4)
EBITDA	5,334	6,123	5,358	6,211	(0.4)	(1.4)
PAT	3,176	3,778	3,195	3,848	(0.6)	(1.8)

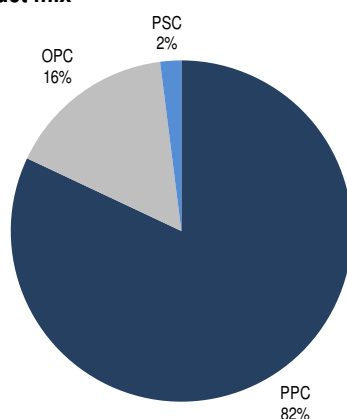
Source: Anand Rath Research

Concall Highlights

Operational and Financial highlights

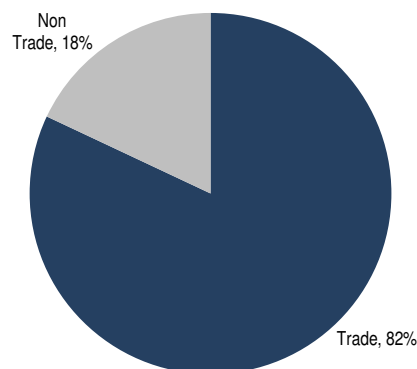
- Cement sales volumes in Q4 FY19 were 0.806m tons, up 8.6% y/y. In the north-east, sales volumes were 0.64m tons, increasing 10% y/y. Outside the north-east, it was 0.19m tons, increasing 4% y/y.
- Transport subsidies of ₹300-350/ton expired in Jan'18.
- The trade and non-trade sales-mix for the quarter was 82:18 (in Q4 FY18 it was 79:21).
- Freight cost for the quarter was ₹1,048.4m; for FY19, it was ₹3.63bn; Q4 FY19 power and fuel cost came at ₹743.9m; for FY19, ₹2.59bn.
- The PPC-OPC-PSC cement mix in Q4 FY19 was 82:16:2.

Fig 14 – Product mix



Source: Company, Anand Rath Research

Fig 15 – Sales mix



Source: Company, Anand Rath Research

- Average lead distance for FY19 was 275km (in FY18, it was 283km).
- Using imported coal due to the recent ban on coal mining in the north-east would impact EBITDA by ~₹200 a ton in FY20.

Subsidies

- The outstanding government subsidy amounts to ₹680m, expected to be received in FY20.

Capex / Capacity expansion

- The Siligudi plant is expected to be completed on schedule, by Q3 FY20.
- Capex estimated by the company for FY20 is ₹3.5bn.

Others

- The company expects ~15% demand growth in FY20.
- It said prices would mostly be steady in coming quarters, though with some upward pricing pressure.

Valuations

At the ruling price, the stock quotes at an EV/EBITDA of 6.6x and an EV/ton of \$116.7. We maintain our Buy recommendation on it, with a higher price target of ₹135 based on 10x FY21e EV/EBITDA.

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



Source: Bloomberg

Fig 17 – Peer comparison - Valuations

	CMP (₹)	P/E		EV/EBITDA		EV/ton(\$)	
		FY20e	FY21e	FY20e	FY21e	FY20e	FY21e
Star Cement	106	13.7	11.5	7.7	6.6	118	117
Birla Corp.	551	15.2	13.9	7.7	7.4	65	65
Dalmia Bharat	1,120	63.1	40.8	12.0	10.3	142	103
Deccan Cement	403	10.3	10.1	4.6	4.0	31	28
Heidelberg Cement	174	14.4	13.1	7.6	6.8	110	104
India Cement	99	14.8	10.9	7.4	6.7	57	57
JK Cement	842	16.9	15.6	10.2	8.7	80	76
JK Lakshmi	354	21.5	15.6	10.2	8.5	70	65
Mangalam Cement	267	51.8	12.4	10.8	6.0	43	39
NCL Indus	139	10.7	8.0	5.8	4.7	45	42
Orient Cement	110	18.7	14.3	8.2	7.3	69	75
Ramco Cement	746	30.2	21.9	17.7	13.6	179	150
Sagar Cement	616	16.1	11.4	7.9	6.9	51	39
Sanghi Industries	60	37.3	50.2	13.3	10.1	106	52

Source: Bloomberg

Risk

- Mounting operational costs.

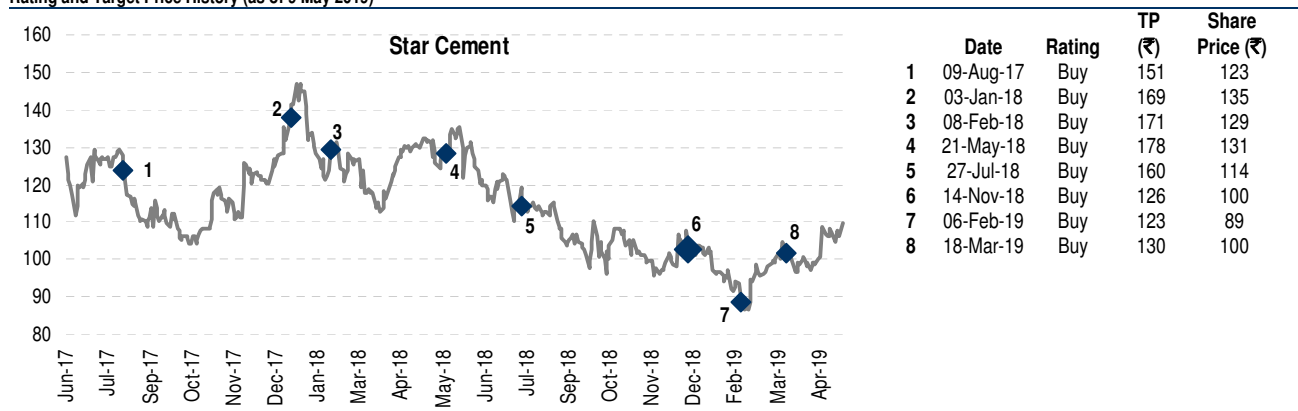
Appendix

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