

**HOLD****TP: Rs 24,792 | ▼ 6%****SHREE CEMENT**

Cement

09 November 2023

## Subpar quarter; earnings chasing valuations

- Q2 volume growth of 10% YoY could have been higher but for a pursuit of realisation gains (+10%)
- Operating efficiencies singed by higher power generation, with energy cost up 2% YoY despite lower pet coke prices
- TP reduces to Rs 24,792 (vs. Rs 25,731) as we cut FY25 EBITDA by 4%; maintain HOLD

Milind Raginwar | Shree Kirloskar  
 research@bobcaps.in

**Topline growth steady in a monsoon quarter:** SRCM's revenue grew 21% YoY (-8% QoQ) to Rs 45.8bn in Q2FY24, aided by volume growth of 10% YoY (-8% QoQ) to 8.2mn tonnes and a 10% YoY rise in aggregate realisations to Rs 5,594/t (flat QoQ). Higher volumes were helped by better YoY utilisation at 74% in the eastern region and 71% overall. SRCM's focus on higher pricing saw it foregoing better volume growth.

**Energy expenses rise on higher power sales:** Operating cost/tonne increased 4% YoY (flat QoQ) to Rs 4,533/t as energy cost grew 2% YoY to Rs 1,671/t. Although softer pet coke prices led to lower fuel cost, SRCM's energy cost increased due to higher power generation for external and captive sales at 880mn units (400mn units sold externally). Fuel cost declined to Rs 2.05/kcal from Rs 2.8/kcal in the year-ago quarter (Rs 2.34/kcal in Q1FY24). Raw material costs increased only 2% YoY to Rs 392/t and logistic cost was flat at Rs 1,160/t.

**Low base effect pushes up EBITDA:** Q2 EBITDA rose 66% YoY (-7% QoQ) to Rs 8.7bn coming off a soft base, with margin expansion to 19% from a weak 13.8% in Q2FY23 (flat QoQ). Power EBITDA stood at Rs 300mn. SRCM's EBITDA/t grew 46% YoY (-2% QoQ) to Rs 1,025/t and PAT rose 2.5x YoY (-16% QoQ) to Rs 4.9bn.

**Capacity expansion plans:** The 3mtpa Purulia grinding unit in West Bengal has been commissioned and the 3.5mtpa Nawalgarh (Rajasthan) unit is on track for Q4FY24. The 3mtpa integrated cement unit in Guntur, Andhra Pradesh, is also scheduled to be commissioned by FY24-end, which will take total capacity to 56mt, rising further to 62mt in FY25.

**Maintain HOLD:** SRCM's capacity expansion continues unabated, but the gap between dispatches and rated capacity has broadened. Opex remains high and we estimate relatively modest ROE of 12-13% in FY25. We maintain FY24 estimates but cut FY25 EBITDA by 4% and EPS by 12% to factor in higher depreciation related to capacity addition. Our TP thus reduces to Rs 24,792 (Rs 25,731 earlier), set at an unchanged 15x FY25E EV/EBITDA – 2.25x over the industry replacement cost. We find current valuations rich at 16x FY25E and hence retain HOLD.

## Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	SRCM IN/Rs 26,271
Market cap	US\$ 11.5bn
Free float	37%
3M ADV	US\$ 8.8mn
52wk high/low	Rs 27,299/Rs 21,410
Promoter/FPI/DII	63%/13%/12%

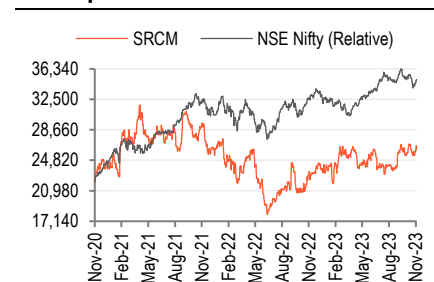
Source: NSE | Price as of 8 Nov 2023

## Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
Total revenue (Rs mn)	1,64,961	1,86,384	2,16,732
EBITDA (Rs mn)	25,504	40,431	50,928
Adj. net profit (Rs mn)	13,281	20,404	26,851
Adj. EPS (Rs)	368.1	565.5	744.2
Consensus EPS (Rs)	368.1	592.0	736.0
Adj. ROAE (%)	7.5	10.7	12.7
Adj. P/E (x)	71.4	46.5	35.3
EV/EBITDA (x)	33.6	21.2	16.5
Adj. EPS growth (%)	(43.9)	53.6	31.6

Source: Company, Bloomberg, BOBCAPS Research

## Stock performance



Source: NSE



**Fig 1 – Earnings call highlights**

Parameter	Q2FY24	Q1FY24	Our view
Volumes and Realisation	<p>Q2FY24 capacity utilisation was 71%, with that in the eastern region declining to ~74% from ~92% in Q1FY24 due to heavy rainfall in a few operating areas and capacity additions.</p> <p>Power sales during Q2 stood at ~Rs 3.4bn (~880mn units generated, of which ~400mn units were sold and ~440mn units consumed captively).</p> <p>Blended cement formed ~75% of volumes sold in Q2FY24 (76% in Q2FY23) and trade sales formed ~80% of the mix (80% in Q2FY23).</p>	<p>Volumes grew consistently across regions, with North India growing at 12-14% YoY, the eastern region at 25+% and the south at ~20%.</p> <p>Capacity utilisation in Q1FY24 was 79% (east 92%, south ~70% and north ~80%).</p> <p>Premium products formed 8.8% of volumes in Q1FY24 (6.3% in Q1FY23). Trade sales stood at ~79% share.</p>	Improving capacity utilisation without denting realisations is a key challenge for SRCM.
Margins	<p>Aggregate realisation grew 10%/YoY during Q2FY24 to Rs 4,843/t owing to an increase in selling price, a better product mix, cost reduction and better operational efficiency.</p> <p>Fuel and power cost stood at Rs 2.05/kcal (vs. Rs 2.8/kcal in Q2FY23) and management expects ~Rs 1.9/kcal in Q3FY24. Lead distance increased to 472km from 456km in Q1FY24.</p> <p>In terms of fuel mix, pet coke and coal constituted ~90% while AFR constituted ~10%.</p>	<p>Prices remained flat QoQ across most regions, except for some marginal hikes at the tail-end of Q1. Prices are under pressure, particularly as competition stiffens and capacity rises across the board.</p> <p>Fuel and power cost in Q1FY24 was at Rs 2.37/kcal.</p> <p>The energy mix was 81% pet coke and 19% AFR compared to the Q1FY23 mix of 60% pet coke, 30% coal, and 10% AFR.</p> <p>Lead distance reduced YoY by 7-8km.</p>	Margins fell short of expectations and are likely to underperform as the company explores new over-supplied regions.
Capacity expansion	<p>Management expects total capacity to increase to 56mtpa by FY24 and is on schedule to reach 80mtpa by FY28.</p> <p>The Guntur plant at Andhra Pradesh is expected to be commissioned by Q4FY24/Q1FY25, and the Nawalgarh plant at Rajasthan by Q4FY24 (delay of ~3 months).</p> <p>SRCM has received the required permissions for setting up a grinding unit at Uttar Pradesh. The grinding unit at Baloda Bazar, Chhatisgarh, is expected to come online within 18 months.</p> <p>The share of green power increased to 58% in Q2FY24 (from 51% in Q2FY23), and management aims to increase the same to 62% by Q1FY25. SRCM's green power generation capacity stood at 401MW as on Q2FY24.</p>	<p>The board has approved the following capacity expansion plans at a total cost of Rs 70bn.: 3.65mt clinker capacity in Pali, Rajasthan; 6mt cement capacity in Pali, Rajasthan and Etah, Uttar Pradesh; 3.65mt clinker capacity in Kodla, Karnataka; and 6mt cement capacity in Kodla and Bangalore, Karnataka. Split grinding capacity is likely to be 3mt per plant. Each plant is to have WHRS facilities, ranging from 40-50MW.</p> <p>The Purulia clinker plant (West Bengal) started trial production in Q1, raising domestic cement capacity to 49.9mt. The integrated plant at Nawalgarh (Rajasthan) is nearing completion and is expected to be commissioned in Q3FY24. The Guntur plant is on target for commissioning in Q2FY25.</p> <p>The share of green power in total power consumption rose to 56% in Q1FY24, from 55% in Q4FY23 and 46% in Q1FY23.</p>	Capex remains elevated. SRCM needs to sustain a strong volume-driven performance, else the capacity and dispatch gap will remain high.

Parameter	Q2FY24	Q1FY24	Our view
Other key points	<p>Union Cement dispatches to India are currently at a halt due to higher handling cost at Indian ports of ~Rs 150/bag (Rs 3,000/t).</p> <p>Management indicated that tax payment will be higher for 2-3 years till refunds are credited as SRCM has a policy of conservatively paying higher taxes.</p>	<p>Management have guided that annual incentives will remain at Rs 1.3bn-1.4bn as some older plants lose incentive coverage while newer and soon-to-be commissioned plants become eligible for coverage.</p>	<p>Temporary issues, such as the halt in dispatches, are unlikely to have a major impact on SRCM's operations.</p>

Source: Company, BOBCAPS Research | AFR: Alternate Fuel Resource; WHRS: xWaste Heat Recovery System

**Fig 2 – Key metrics**

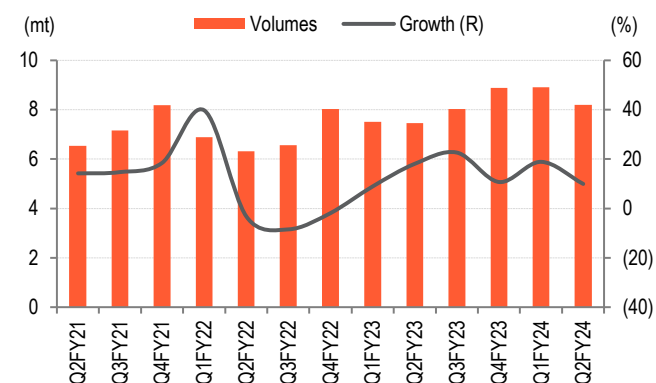
(Rs)	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)
Volumes (mn mt)	8.2	7.5	9.9	8.9	(8.1)
Cement realisations (Rs/mt)	5,594	5,071	10.3	5,607	(0.2)
Operating costs (Rs/mt)*	4,533	4,369	3.7	4,561	(0.6)
EBITDA (Rs/mt)	1,025	701	46.2	1,046	(2.0)

Source: Company, BOBCAPS Research | \*Aggregate cost

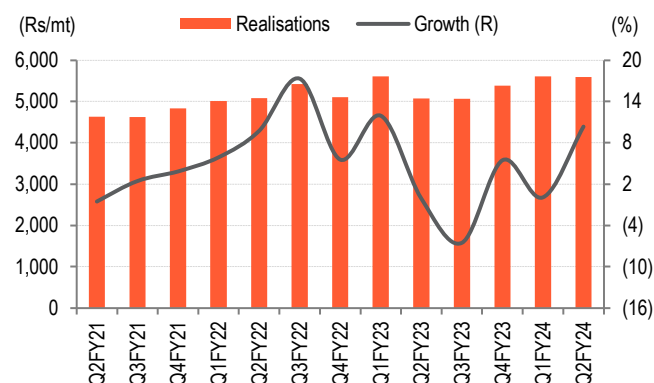
**Fig 3 – Quarterly performance**

(Rs mn)	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)
<b>Net Sales</b>	<b>45,846</b>	<b>37,806</b>	<b>21.3</b>	<b>49,991</b>	<b>(8.3)</b>
<b>Expenditure</b>					
Change in stock	(289)	691	(141.9)	489	(159.1)
Raw material	3,216	2,859	12.5	3,614	(11.0)
purchased products	1,630	146	1,013.7	1,656	-
Power & fuel	13,696	12,270	11.6	15,240	(10.1)
Freight	9,508	8,561	11.1	10,630	(10.5)
Employee costs	2,332	2,097	11.2	2,349	(0.7)
Other exp	7,053	5,955	18.4	6,688	5.5
Total Operating Expenses	37,146	32,579	14.0	40,665	(8.7)
<b>EBITDA</b>	<b>8,701</b>	<b>5,227</b>	<b>66.4</b>	<b>9,326</b>	<b>(6.7)</b>
EBITDA margin (%)	19.0	13.8	515bps	18.7	32bps
Other Income	1,261	1,569	(19.6)	1,617	(22.0)
Interest	681	676	0.8	753	(9.6)
Depreciation	3,315	3,628	(8.6)	3,085	7.5
PBT	5,965	2,493	139.3	7,105	(16.0)
Non-recurring items	0	0	-	0	-
PBT (after non-recurring items)	5,965	2,493	139.3	7,105	(16.0)
Tax	1,052	597	76.3	1,294	(18.7)
Reported PAT	4,913	1,896	159.2	5,811	(15.5)
<b>Adjusted PAT</b>	<b>4,913</b>	<b>1,896</b>	<b>159.2</b>	<b>5,811</b>	<b>(15.5)</b>
NPM (%)	10.7	5.0	570bps	11.6	(91bps)
<b>Adjusted EPS (Rs)</b>	<b>132.4</b>	<b>52.5</b>	<b>152.2</b>	<b>156.6</b>	<b>(15.5)</b>

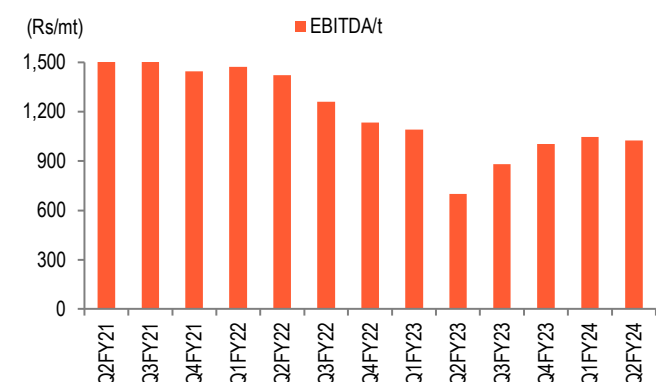
Source: Company, BOBCAPS Research

**Fig 4 – Volumes had potential to grow higher in Q2FY24**

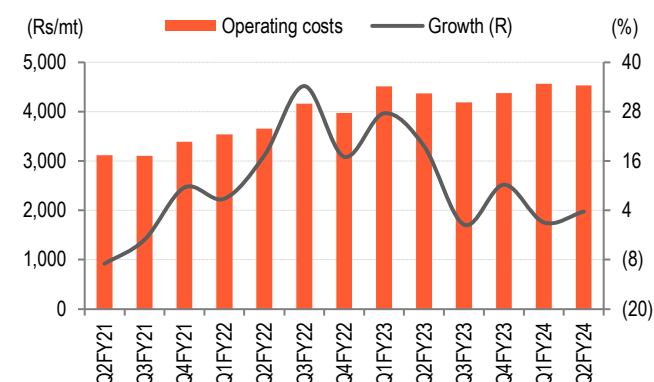
Source: Company, BOBCAPS Research

**Fig 5 – Prices in northern region aided realisation gains**

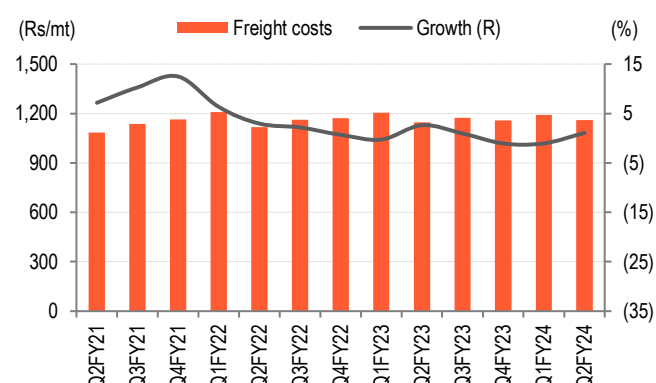
Source: Company, BOBCAPS Research

**Fig 6 – Cement EBITDA/t range-bound**

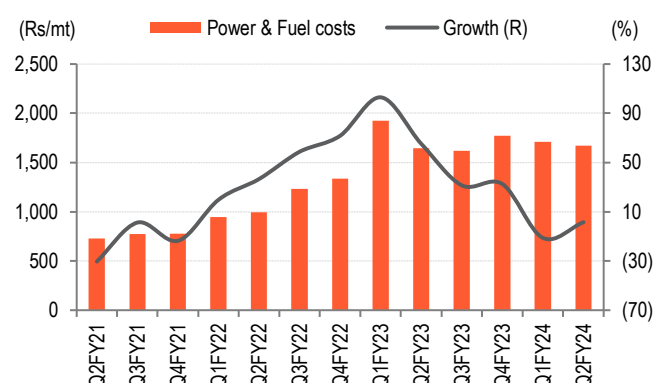
Source: Company, BOBCAPS Research

**Fig 7 – Operating cost softened less than expected**

Source: Company, BOBCAPS Research

**Fig 8 – Inflated freight cost a negative surprise**

Source: Company, BOBCAPS Research

**Fig 9 – Energy cost rises due to higher power generation**

Source: Company, BOBCAPS Research

## Valuation methodology

SRCM's capacity expansion continues unabated, with the company aiming to reach 56mt in FY25 and 80mt in FY28. However, the gap between dispatches and rated capacity has broadened, and higher capacity utilisation will require a strong demand uptick. Opex remains high and we estimate relatively modest ROE of 12-13% in FY25 as against the company's historical range of 18-20%.

We maintain FY24 estimates but cut our FY25 EBITDA and EPS forecasts by 4% and 12% respectively to factor in higher depreciation related to the capacity addition. Our TP thus reduces to Rs 24,792 (Rs 25,731 earlier), set at an unchanged 15x FY25E EV/EBITDA – 2.25x over the industry replacement cost. We find current valuations rich at 16x FY25E and hence retain HOLD.

**Fig 10 – Revised estimates**

(Rs mn)	New		Old		Change (%)	
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Revenue	1,86,384	2,16,732	1,86,384	2,16,732	0.0	0.0
EBITDA	40,431	50,928	40,431	53,045	0.0	(4.0)
Adj PAT	20,404	26,851	20,404	30,538	0.0	(12.1)
Adj EPS (Rs)	565.5	744.2	565.5	846.4	0.0	(12.1)

Source: BOBCAPS Research

**Fig 11 – Key assumptions**

Parameter	FY22	FY23	FY24E	FY25E
Volumes (mt)	27.1	31.8	35.6	39.6
Realisations (Rs/mt)	5,052	5,292	5,160	5,314
Operating costs (Rs/mt)	3,856	4,367	4,024	4,048
EBITDA/mt (Rs)	1,182	925	1,135	1,266

Source: Company, BOBCAPS Research

**Fig 12 – Valuation summary**

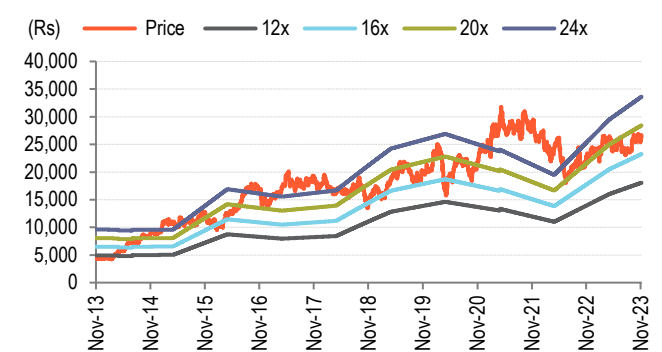
(Rs mn)	FY25E
Target EV/EBITDA (x)	15
EBITDA	50,928
Target EV	7,86,325
Total EV	7,86,325
Net debt	(1,09,151)
Target market capitalisation	8,95,476
<b>Target price (Rs/sh)</b>	<b>24,792</b>
Weighted average shares (mn)	36

Source: BOBCAPS Research

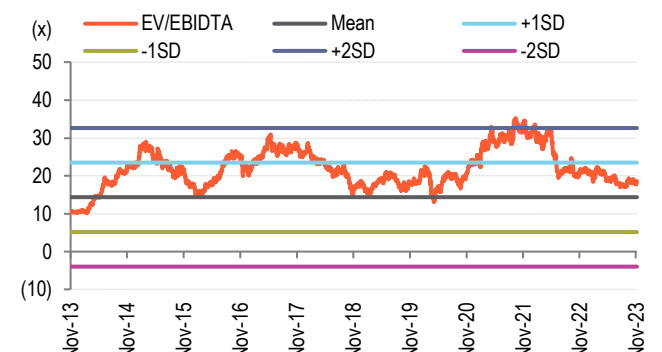
**Fig 13 – Peer comparison**

Ticker	Rating	TP (Rs)	EV/EBITDA (x)			EV/tonne (US\$)			ROE (%)			ROCE (%)		
			FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E
SRCM IN	HOLD	24,792	33.6	21.2	16.5	208	207	202	7.5	10.7	12.7	9.4	14.7	16.8
DALBHARA IN	HOLD	2,286	17.6	15.4	11.3	126	109	107	4.0	6.3	11.1	5.4	7.2	10.9
ACC IN	HOLD	2,158	22.9	12.2	9.0	121	106	98	5.2	8.1	11.2	7.9	11	14.5

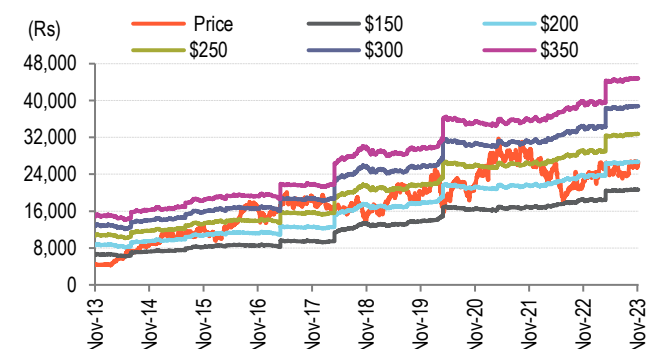
Source: BOBCAPS Research

**Fig 14 – Valuations elevated**

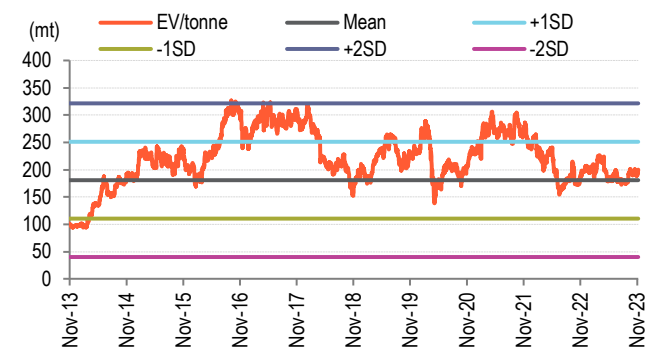
Source: Company, BOBCAPS Research

**Fig 15 – Earnings concerns likely to tell on valuations**

Source: Company, BOBCAPS Research

**Fig 16 – Replacement cost value elevated**

Source: Company, BOBCAPS Research

**Fig 17 – Replacement cost valuation premium continues**

Source: Company, BOBCAPS Research

## Key risks

- SRCM is trying to diversify into new regions that face higher supply pressure. Hence, pricing pressure may impact its performance more than estimated.
- Aggressive capacity addition can have an adverse impact on earnings in the event of an economic slowdown.
- Faster-than-expected easing of key raw material costs is a key upside risk to our estimates.

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
ACC	ACC IN	4.2	1,854	2,158	BUY
Ambuja Cements	ACEM IN	10.2	421	449	HOLD
Dalmia Bharat	DALBHARA IN	4.8	2,124	2,286	HOLD
JK Cement	JKCE IN	3.2	3,439	3,578	HOLD
JK Lakshmi Cement	JKLC IN	1.1	765	551	SELL
Orient Cement	ORCMNT IN	0.5	210	128	SELL
Shree Cement	SRCM IN	11.5	26,271	24,792	HOLD
Star Cement	STRCEM IN	0.8	164	159	HOLD
The Ramco Cements	TRCL IN	2.9	1,010	585	SELL
Ultratech Cement	UTCEN IN	30.6	8,699	9,396	HOLD

Source: BOBCAPS Research, NSE | Price as of 8 Nov 2023

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
<b>Total revenue</b>	<b>1,23,160</b>	<b>1,39,118</b>	<b>1,64,961</b>	<b>1,86,384</b>	<b>2,16,732</b>
EBITDA	36,943	32,201	25,504	40,431	50,928
Depreciation	(11,399)	(10,365)	(15,462)	(15,740)	(19,635)
EBIT	32,728	31,389	18,275	31,046	39,301
Net interest inc./(exp.)	(2,471)	(2,178)	(2,689)	(3,087)	(3,269)
Other inc./(exp.)	7,184	9,553	8,233	6,355	8,009
Exceptional items	0	0	0	0	0
EBT	30,257	29,211	15,586	27,958	36,033
Income taxes	(7,138)	(5,543)	(2,305)	(7,555)	(9,182)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>23,119</b>	<b>23,668</b>	<b>13,281</b>	<b>20,404</b>	<b>26,851</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>23,119</b>	<b>23,668</b>	<b>13,281</b>	<b>20,404</b>	<b>26,851</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
Accounts payables	7,858	17,853	20,968	14,597	16,981
Other current liabilities	22,343	23,307	28,789	33,437	36,179
Provisions	43	57	61	57	57
Debt funds	27,562	20,142	25,392	28,065	29,715
Other liabilities	(7,773)	(6,609)	(6,591)	(7,138)	(7,736)
Equity capital	361	361	361	361	361
Reserves & surplus	1,52,140	1,72,357	1,82,532	1,99,879	2,23,673
Shareholders' fund	1,52,501	1,72,709	1,82,883	2,00,237	2,24,032
<b>Total liab. and equities</b>	<b>2,02,533</b>	<b>2,27,458</b>	<b>2,51,502</b>	<b>2,69,256</b>	<b>2,99,228</b>
Cash and cash eq.	1,12,604	1,16,642	1,17,698	1,19,996	1,38,867
Accounts receivables	4,859	5,957	9,061	10,595	12,734
Inventories	14,772	21,614	24,226	27,737	32,684
Other current assets	18,673	20,303	23,987	24,539	25,103
Investments	0	0	0	0	0
Net fixed assets	37,702	46,887	45,651	45,592	37,637
CWIP	13,448	15,559	30,155	40,033	51,393
Intangible assets	475	497	722	765	811
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>2,02,533</b>	<b>2,27,458</b>	<b>2,51,500</b>	<b>2,69,256</b>	<b>2,99,229</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
<b>Cash flow from operations</b>	<b>43,507</b>	<b>35,924</b>	<b>27,274</b>	<b>27,867</b>	<b>43,362</b>
Capital expenditures	(9,928)	(21,154)	(28,261)	(25,601)	(23,086)
Change in investments	(21,352)	(4,953)	(1,046)	(3,315)	(8,708)
Other investing cash flows	0	0	0	0	0
<b>Cash flow from investing</b>	<b>(31,279)</b>	<b>(26,108)</b>	<b>(29,307)</b>	<b>(28,917)</b>	<b>(31,793)</b>
Equities issued/Others	0	(9)	0	7	0
Debt raised/repaid	(11,228)	(7,420)	5,250	2,673	1,651
Interest expenses	0	0	0	0	0
Dividends paid	0	(3,788)	(3,247)	(2,649)	(3,057)
Other financing cash flows	17	486	41	2	0
<b>Cash flow from financing</b>	<b>(11,212)</b>	<b>(10,731)</b>	<b>2,044</b>	<b>33</b>	<b>(1,406)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>1,016</b>	<b>(915)</b>	<b>10</b>	<b>(1,017)</b>	<b>10,163</b>
<b>Closing cash &amp; cash eq.</b>	<b>1,12,604</b>	<b>1,16,642</b>	<b>1,17,698</b>	<b>1,19,996</b>	<b>1,38,866</b>

### Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23A	FY24E	FY25E
Reported EPS	640.8	656.0	368.1	565.5	744.2
Adjusted EPS	640.8	656.0	368.1	565.5	744.2
Dividend per share	0.0	105.0	90.0	72.4	72.4
Book value per share	4,226.7	4,786.8	5,068.8	5,549.8	6,209.3

### Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23A	FY24E	FY25E
EV/Sales	7.0	6.1	5.2	4.6	3.9
EV/EBITDA	23.4	26.5	33.6	21.2	16.5
Adjusted P/E	41.0	40.0	71.4	46.5	35.3
P/BV	6.2	5.5	5.2	4.7	4.2

### DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23A	FY24E	FY25E
Tax burden (Net profit/PBT)	76.4	81.0	85.2	73.0	74.5
Interest burden (PBT/EBIT)	92.4	93.1	85.3	90.1	91.7
EBIT margin (EBIT/Revenue)	26.6	22.6	11.1	16.7	18.1
Asset turnover (Rev./Avg TA)	63.4	64.7	68.9	71.6	76.2
Leverage (Avg TA/Avg Equity)	1.4	1.3	1.3	1.4	1.3
Adjusted ROAE	16.4	14.6	7.5	10.7	12.7

### Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23A	FY24E	FY25E
<b>YoY growth (%)</b>					
Revenue	5.6	13.0	18.6	13.0	16.3
EBITDA	7.6	(12.8)	(20.8)	58.5	26.0
Adjusted EPS	47.4	2.4	(43.9)	53.6	31.6

### Profitability & Return ratios (%)

EBITDA margin	30.0	23.1	15.5	21.7	23.5
EBIT margin	26.6	22.6	11.1	16.7	18.1
Adjusted profit margin	18.8	17.0	8.1	10.9	12.4
Adjusted ROAE	16.4	14.6	7.5	10.7	12.7
ROCE	19.7	17.5	9.4	14.7	16.8

### Working capital days (days)

Receivables	14	16	20	21	21
Inventory	44	57	54	54	55
Payables	33	61	55	37	37

### Ratios (x)

Gross asset turnover	1.1	1.1	1.2	1.2	1.3
Current ratio	5.0	4.0	3.5	3.8	3.9
Net interest coverage ratio	13.2	14.4	6.8	10.1	12.0
Adjusted debt/equity	0.2	0.1	0.1	0.1	0.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets



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Registered office Address: **1704, B Wing, Parinee Crescenzo, G Block, BKC, Bandra East, Mumbai 400051**

SEBI Research Analyst Registration No: **INH000000040 valid till 03 February 2025**

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**Recommendation scale: Recommendations and Absolute returns (%) over 12 months**

**BUY** – Expected return >+15%

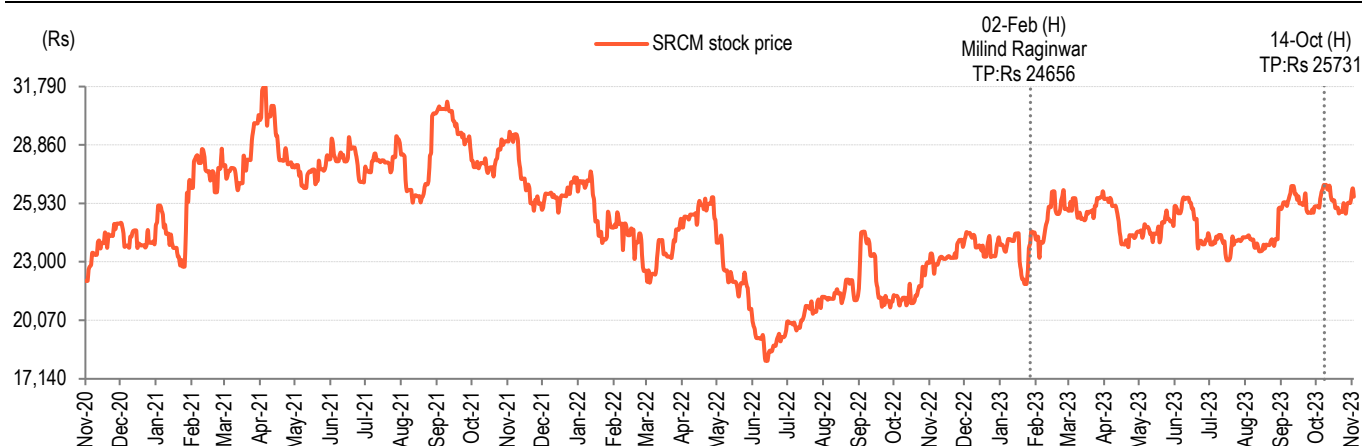
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

## Ratings and Target Price (3-year history): SHREE CEMENT (SRCM IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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