

HOLD

TP: Rs 159 | ▲ 0%

STAR CEMENT

| Cement

| 10 November 2023

Cost relief in an otherwise weak quarter

- **Monsoon impact in northeast markets kept Q2 volumes flat YoY at 0.9mt while realisation slipped 2%**
- **Operating cost fell 8% YoY to Rs 5,432/t despite higher maintenance cost, giving earnings a breather**
- **Maintain HOLD with unchanged TP of Rs 159, valuing the stock at 8x FY25E EV/EBITDA**

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Revenue growth muted on listless volumes, weak realisations: STRCEM's revenue fell 2% YoY (-23% QoQ) to Rs 5.9bn in Q2FY24 as volumes were flat YoY (-23% QoQ) at 0.9mn tonnes and realisation fell 2% YoY (flat QoQ) to Rs 6,532/t. Sales in the northeast market formed 75% of STRCEM's total in Q2 vs. 74% in Q1FY24, indicating volume pressure in this key region in a traditionally weak monsoon quarter.

Operating cost declines: Overall cost declined 8% YoY (flat QoQ) to Rs 5,432/t as energy cost excluding raw material inventory impact fell 11% YoY (-13% QoQ) to Rs 2,798/t. Further, logistics cost softened 16% YoY (-7% QoQ) to Rs 1,007/t as STRCEM operated its own fleet and a key transport route was restored. Other expenditure increased 3% YoY (+10% QoQ) to Rs 887mn due to kiln maintenance.

Lower cost aids margin expansion: EBITDA increased 42% YoY (-24% QoQ) to Rs 986mn accompanied by margin expansion of 510bps YoY (-15bps QoQ) to 16.8%. EBITDA/t expanded to Rs 1,100 from Rs 782 in Q2FY23 (flat QoQ) and adj. PAT grew 31% YoY (-56% QoQ) to Rs 407mn.

Capacity expansion plans: The grinding unit in Guwahati, Assam, is due to be commissioned by Q3FY24 and the 3mt Meghalaya clinker plant is scheduled for Q4FY24. The Silchar grinding unit in Assam has been deferred as STRCEM plans to sweat the Guwahati unit before commissioning another in the vicinity.

Maintain HOLD: Despite tepid revenue growth in Q2FY24, we maintain our estimates for STRCEM as we expect a government-led infrastructure focus in its core northeast market to trigger healthy realisations and volume growth. Further, the company's sound balance sheet despite being in capex mode and its plans to derisk revenue are likely to support ROE/ROCE expansion to an estimated 14%/19% by FY25. We maintain HOLD with an unchanged TP of Rs 159, valuing STRCEM at 8x FY25E EV/EBITDA, which implies a replacement cost of Rs 6.7bn/mt – 10% discount to the industry.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	STRCEM IN/Rs 159
Market cap	US\$ 810.7mn
Free float	33%
3M ADV	US\$ 1.5mn
52wk high/low	Rs 182/Rs 93
Promoter/FPI/DII	67%/1%/6%

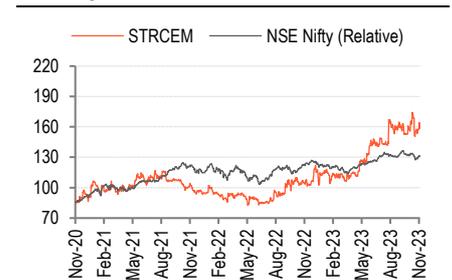
Source: NSE | Price as of 10 Nov 2023

Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
Total revenue (Rs mn)	25,756	32,869	40,504
EBITDA (Rs mn)	4,684	5,355	7,492
Adj. net profit (Rs mn)	2,477	2,688	4,147
Adj. EPS (Rs)	5.9	6.4	9.9
Consensus EPS (Rs)	5.9	6.4	7.6
Adj. ROAE (%)	10.8	10.6	14.7
Adj. P/E (x)	26.9	24.8	16.1
EV/EBITDA (x)	13.6	12.6	8.4
Adj. EPS growth (%)	0.4	8.5	54.3

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Earnings call highlights

Parameter	Q2FY24	Q1FY24	Our view
Volumes and Realisation	<p>Volumes for Q2FY24 stood at 0.9mt and management expects 13-14% growth for FY24.</p> <p>Trade volume share stood at ~89%, premium product sales formed ~6.9% of the mix and management expects the premium share to reach ~10% by FY24.</p> <p>Capacity utilisation in H1FY24 was ~88%.</p>	<p>Volumes for Q1FY24 stood at 1.1mt (including 0.8mt in the northeast). Management has guided for 12-13% volume growth for FY24.</p> <p>Trade sales stood at 88% of overall volumes in Q1. Premium sales stood at 4%, with the proportion guided to double over the next two quarters and reach double digits by FY24-end.</p> <p>Siliguri capacity utilisation stood at 71%.</p>	<p>We expect volumes to recover in H2FY24 given the government's focus on building up infrastructure in the northeast region.</p>
Margins	<p>Cement prices improved by ~Rs 10/bag in the northeast and ~Rs 50/bag in other regions at the end of Q2FY24, with the impact likely to be visible in Q3. Only a slight rollback of Rs 5-7/bag is expected from the slowdown due to festivities.</p> <p>Fuel mix was ~6% FSA, 32% Nagaland coal, 5% biomass, and 57% spot option and trade purchase. Fuel cost stood at Rs 1.9/kcal while the lead distance was 214km.</p> <p>Logistics cost/t declined 16%/7% YoY/QoQ to Rs 1,007 due to strategic management of owned fleets and restoration of an under-repair bridge which had previously escalated freight cost.</p> <p>Margins were affected QoQ by a volume slowdown due to the monsoons and scheduled maintenance shutdown cost of ~Rs 150mn.</p>	<p>STRCEM witnessed stable prices in the northeast region and eastern markets, with no decline in Q1 despite the monsoons. Management guided that they do not foresee much volatility in prices.</p> <p>In Q1, the fuel mix was ~30% Nagaland coal, 7% biomass, and 55% coal spot contract. STRCEM's lead distance was 207km, falling from 224km the previous quarter. Fuel cost was Rs 2.35/kcal and management expects it to be Rs 1.95 in Q2, resulting in cost savings of ~Rs 180/t in cement and ~Rs 300/t in clinker.</p> <p>Margin were under pressure as incentives aggregating to Rs 300-350/t expired. Management indicated that annual plant maintenance will take place in Q2FY24.</p>	<p>We expect margins and EBTIDA/t to move up following the blip in the monsoon quarter.</p>
Capacity	<p>The 2mt Guwahati grinding unit is expected to be commissioned in Q3FY24 and the 3mt Meghalaya clinker plant in Q4FY24. Commissioning of the 2mtpa Silchar grinding unit has been strategically delayed till mid-FY25 although 73-75% of the land acquisition is complete.</p>	<p>STRCEM has guided for its 2mt grinding unit in Guwahati to be commissioned by Q3FY24 and its clinker plant by Q4FY24. Its grinding plant at Silchar (Assam) has been delayed by 3-4 months due to delayed land acquisitions (75% complete) and will be commissioned by Q3FY25.</p>	<p>In our view, Silchar capacity postponement is a right move strategically.</p>
Capex	<p>Capex has been guided at ~Rs 8bn post Q1FY24 with ~Rs 2bn incurred during Q2. Guidance for FY25 is more than ~Rs 6bn, majorly towards the Meghalaya clinker plant and Guwahati grinding unit. Capex on these projects during H1FY24 totalled ~Rs 7bn and ~Rs 2.1bn respectively.</p> <p>Management indicated that it may opt for debt of Rs 3bn in Q3-Q4 of FY24 to meet its capex target considering expected cash reserves of Rs 3.2bn for the fiscal year (Rs 2.1bn as on Q2FY24).</p>	<p>The budgeted capex for FY24 is ~Rs 11bn, with Rs 8bn to be spent on clinker and grinding expansion and the balance on renewable energy and other such projects. Of the Rs 8bn, a sum of Rs 5.8bn has already been spent on the clinker plant and Rs 1.4bn on the grinding unit. The FY25 budget is Rs 4bn-5bn.</p> <p>STRCEM has reserves of Rs 3.8bn and is forecasting a cash profit of Rs 3bn-4bn in FY24, resulting in debt requirements aggregating to Rs 5bn from Q3-Q4 of FY24 to fund capex plans.</p>	<p>Capital expenditure burden on the balance sheet need to be minimised, in our view.</p>

Parameter	Q2FY24	Q1FY24	Our view
Other key points	<p>The WHRS plant at Lumshnong, Meghalaya, has led to cost savings of ~Rs 100mn for STRCM.</p> <p>For its fly-ash landed cost reduction plans at the Siliguri plant, STRCEM is currently negotiating and ordering BTAP wagons and expects to have these in place by Q1FY25.</p> <p>Management indicated that STRCEM will commission a new clinker line one year before Dalmia Bharat and that competitive intensity after a year may lead to price corrections but will be made up by volume growth. The company is targeting 30%+ market share in the northeast.</p>	<p>Management have guided for annual savings of Rs 450mn-500mn from WHRS as utilisation peaks in Q3.</p> <p>STRCEM is exploring investing in BTAP wagons to reduce landed fly ash costs and improve profitability of the Siliguri plant.</p> <p>Management have guided that its new capacity expansion in the northeast will be commissioned in FY25 before large competitors (Dalmia Bharat) raise capacities in the region, which will enable it to leverage a first-mover advantage.</p>	<p>Cost-saving measures by STRCEM are likely to yield positive results over the medium term.</p>

Source: Company, BOBCAPS Research | FSA: Fuel Supply Agreement, BTAP: Bogey Tank Wagon for Alumina Powder, WHRS: Waste Heat Recovery System

Fig 2 – Key metrics

(Rs)	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)
Volumes (mn mt)	0.9	0.9	0.6	1.2	(23.0)
Cement realisations (Rs/mt)	6,532	6,669	(2.1)	6,533	(0.0)
Operating costs (Rs/mt)	5,432	5,887	(7.7)	5,423	0.2
EBITDA (Rs/mt)	1,100	782	40.7	1,111	(1.0)

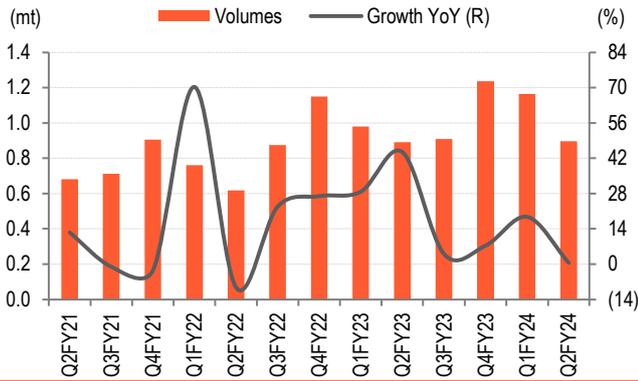
Source: Company, BOBCAPS Research

Fig 3 – Quarterly performance

(Rs mn)	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)
Net Sales	5,853	5,942	(1.5)	7,605	(23.0)
Expenditure					
Change in stock	(105)	219	-	81	-
Raw material	1,300	1,449	(10.3)	1,922	(32.4)
purchased products	0	0	0.0	0	0.0
Power & fuel	1,312	1,147	14.3	1,731	(24.2)
Freight	902	1,062	(15.1)	1,260	(28.4)
Employee costs	571	506	12.9	510	12.1
Other expenses	887	863	2.8	808	9.8
Total Operating Expenses	4,867	5,245	(7.2)	6,312	(22.9)
EBITDA	986	697	41.5	1,293	(23.8)
EBITDA margin (%)	16.8	11.7	512bps	17.0	(16bps)
Other Income	58	136	(57.4)	87	(33.9)
Interest	32	26	23.1	22	44.8
Depreciation	360	315	14.2	318	13.2
PBT	651	490	32.7	1,040	(37.4)
Non-recurring items	0	0	0.0	0	0.0
PBT (after non-recurring items)	651	490	32.7	1,040	(37.4)
Tax	244	180	35.7	107	127.9
Tax Rate (%)	37.5	36.7	83bps	10.3	2720bps
Reported PAT	407	311	31.0	933	(56.4)
Adjusted PAT	407	311	31.0	933	(56.4)
NPM (%)	7	5	172bps	12	(531bps)
Adjusted EPS (Rs)	1.0	0.7	34.6	2.3	(55.5)

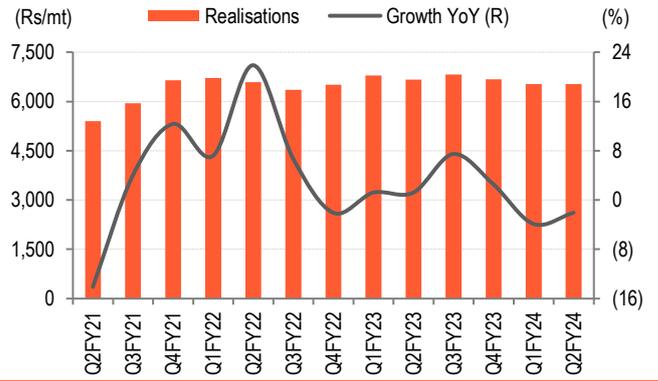
Source: Company, BOBCAPS Research

Fig 4 – Tepid volumes are typical of a monsoon quarter



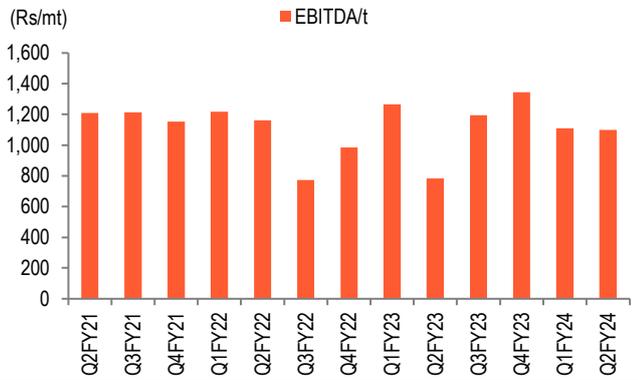
Source: Company, BOBCAPS Research

Fig 5 – Realisations likely to recover in H2



Source: Company, BOBCAPS Research

Fig 6 – EBITDA/t expected to move up...



Source: Company, BOBCAPS Research

Fig 7 – ...on operating cost levers



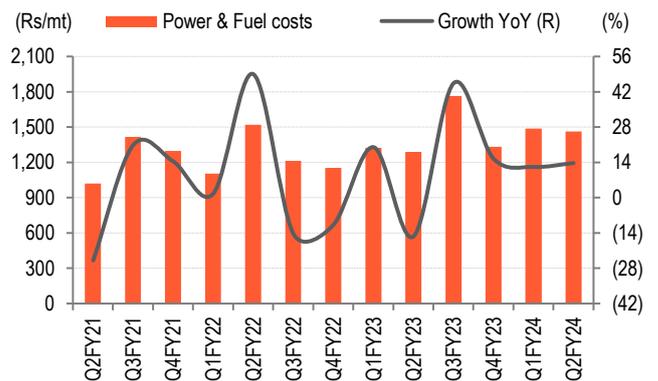
Source: Company, BOBCAPS Research

Fig 8 – Logistics cost savings in Q2FY24 due to own fleet



Source: Company, BOBCAPS Research

Fig 9 – Fuel cost may revert to higher levels



Source: Company, BOBCAPS Research

Valuation methodology

Despite tepid revenue growth in Q2FY24, we maintain our estimates for STRCEM as we expect a government-led infrastructure focus in its core northeast market to trigger healthy realisations and volume growth. Further, the company's sound balance sheet despite being in capex mode and its plans to derisk revenue by way of spreading into other geographies are likely to support ROE/ROCE expansion to an estimated 14%/19% by FY25.

We maintain HOLD with an unchanged TP of Rs 159, valuing STRCEM at 8x FY25E EV/EBITDA, which implies a replacement cost of Rs 6.7bn/mt – 10% discount to the industry.

Fig 10 – Key assumptions

Parameter	FY22	FY23	FY24E	FY25E
Volumes (mt)	3.30	3.80	4.56	5.65
Realisations (Rs/mt)	6015	6767	6970	6970
Operating costs (Rs/mt)	5,694	5,885	6,042	5,846
EBITDA/mt (Rs)	1,048	1,233	1,166	1,318

Source: Company, BOBCAPS Research

Fig 11 – Valuation summary

(Rs mn)	FY25E
Target EV/EBITDA (x)	8.0
EBITDA	7,492
Target EV	60,686
Total EV	60,686
Net debt	(3,630)
Target market capitalisation	64,316
Target price (Rs/sh)	159
Weighted average shares (mn)	404

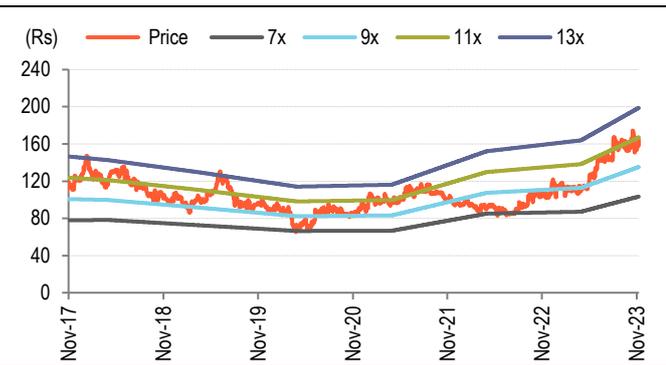
Source: BOBCAPS Research

Fig 12 – 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
STRCEM IN	HOLD	159	13.6	12.6	8.4	110	123	113	10.8	10.6	14.7	16.9	14.7	19.7
ORCMNT IN	SELL	128	11.5	9.3	7.7	63	62	63	7.9	10.4	13.2	10.5	12.8	13.5
JKLC IN	SELL	551	10.1	9.5	8.7	81	84	93	12.8	13.4	14.4	16.2	17.3	17.2

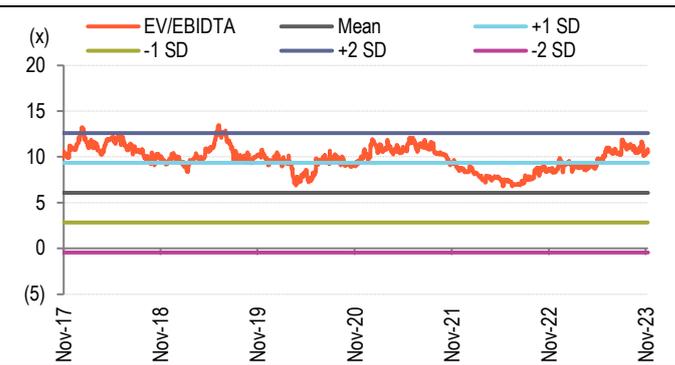
Source: BOBCAPS Research

Fig 13 – FY25E valuations look reasonable



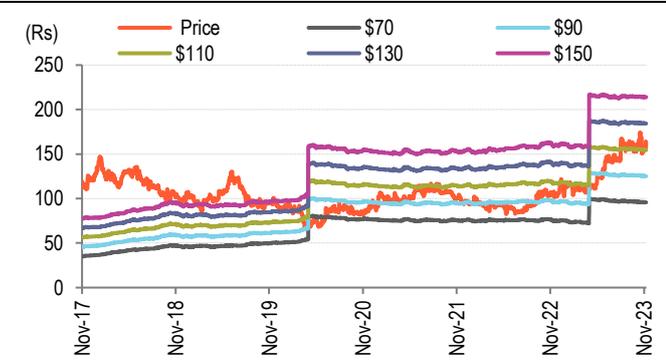
Source: Company, BOBCAPS Research

Fig 14 – Presence in niche markets keeps valuation high



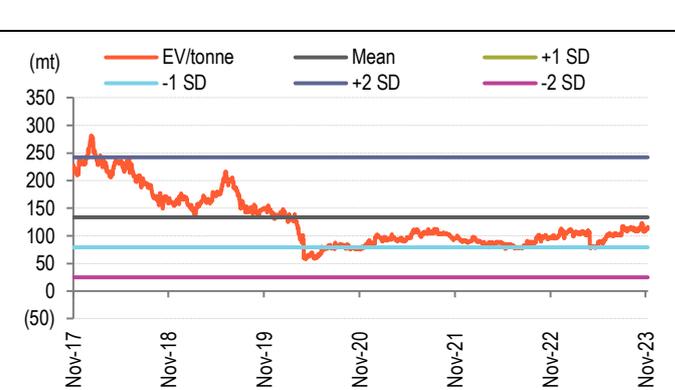
Source: Company, BOBCAPS Research

Fig 15 – Replacement cost higher due to STRCEM's positioning



Source: Company, BOBCAPS Research

Fig 16 – Replacement cost likely to stay elevated



Source: Company, BOBCAPS Research

Key risks

- Strong demand resurgence following the 2024 general elections represents a key upside risk to our estimates.
- Increasing competitive intensity in key areas of operations along with continued challenges in terms of coal availability and cost inflation are key downside risks.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
ACC	ACC IN	4.2	1,825	2,158	BUY
Ambuja Cements	ACEM IN	10.1	418	449	HOLD
Dalmia Bharat	DALBHARA IN	4.7	2,090	2,286	HOLD
JK Cement	JKCE IN	3.3	3,464	3,578	HOLD
JK Lakshmi Cement	JKLC IN	1.1	777	551	SELL
Orient Cement	ORCMNT IN	0.5	213	128	SELL
Shree Cement	SRCM IN	11.6	26,359	24,792	HOLD
Star Cement	STRCEM IN	0.8	159	159	HOLD
The Ramco Cements	TRCL IN	2.8	986	661	SELL
Ultratech Cement	UTCEN IN	30.6	8,711	9,396	HOLD

Source: BOBCAPS Research, NSE | Price as of 10 Nov 2023

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
Total revenue	17,186	20,902	25,756	32,869	40,504
EBITDA	3,326	3,453	4,684	5,355	7,492
Depreciation	(900)	(1,216)	(1,311)	(1,508)	(1,616)
EBIT	2,708	2,570	3,894	4,114	6,188
Net interest inc./(exp.)	(70)	(133)	(96)	(120)	(108)
Other inc./(exp.)	282	334	521	267	311
Exceptional items	(646)	0	0	0	0
EBT	1,993	2,437	3,798	3,994	6,080
Income taxes	(120)	31	(1,321)	(1,306)	(1,932)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	1,872	2,468	2,477	2,688	4,147
Adjustments	646	0	0	0	0
Adjusted net profit	2,518	2,468	2,477	2,688	4,147

Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
Accounts payables	985	1,146	2,820	2,793	3,351
Other current liabilities	3,643	4,501	3,972	4,369	5,024
Provisions	99	66	97	91	100
Debt funds	153	54	261	5,057	1,157
Other liabilities	0	0	0	0	0
Equity capital	412	404	404	404	404
Reserves & surplus	20,329	21,280	23,760	25,991	29,679
Shareholders' fund	20,741	21,684	24,164	26,395	30,083
Total liab. and equities	25,621	27,451	31,314	38,705	39,715
Cash and cash eq.	4,717	3,847	3,117	4,104	4,787
Accounts receivables	1,317	1,287	1,047	1,936	2,386
Inventories	2,347	1,953	3,741	2,882	3,329
Other current assets	4,189	4,863	4,377	4,466	4,511
Investments	17	1,637	1,725	1,637	1,637
Net fixed assets	8,219	9,225	8,850	19,579	20,045
CWIP	1,266	1,091	5,506	859	(541)
Intangible assets	10	10	60	62	64
Deferred tax assets, net	3,539	3,539	2,890	3,179	3,497
Other assets	0	0	0	0	0
Total assets	25,622	27,451	31,314	38,705	39,715

Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
Cash flow from operations	3,455	4,333	4,543	4,152	5,726
Capital expenditures	(1,173)	(1,959)	(5,394)	(7,593)	(683)
Change in investments	(1)	(1,620)	(89)	89	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(1,174)	(3,579)	(5,482)	(7,505)	(683)
Equities issued/Others	20	420	422	0	0
Debt raised/repaid	20	(99)	207	4,796	(3,900)
Interest expenses	6	7	8	9	10
Dividends paid	(419)	(419)	(419)	(419)	(419)
Other financing cash flows	(3)	(1,525)	-	(37)	(41)
Cash flow from financing	(383)	(1,624)	210	4,340	(4,360)
Chg in cash & cash eq.	1,897	(870)	(729)	987	682
Closing cash & cash eq.	4,717	3,847	3,118	4,105	4,787

Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23A	FY24E	FY25E
Reported EPS	4.5	5.9	5.9	6.4	9.9
Adjusted EPS	6.0	5.9	5.9	6.4	9.9
Dividend per share	1.0	1.0	1.0	1.0	1.0
Book value per share	49.5	51.7	57.6	63.0	71.8

Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23A	FY24E	FY25E
EV/Sales	3.6	3.0	2.5	2.1	1.6
EV/EBITDA	18.7	18.2	13.6	12.6	8.4
Adjusted P/E	26.5	27.0	26.9	24.8	16.1
P/BV	3.2	3.1	2.8	2.5	2.2

DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23A	FY24E	FY25E
Tax burden (Net profit/PBT)	94.0	101.3	65.2	67.3	68.2
Interest burden (PBT/EBIT)	97.4	94.8	97.5	97.1	98.3
EBIT margin (EBIT/Revenue)	15.8	12.3	15.1	12.5	15.3
Asset turnover (Rev./Avg TA)	69.9	78.8	87.7	93.9	103.3
Leverage (Avg TA/Avg Equity)	1.2	1.3	1.3	1.4	1.4
Adjusted ROAE	12.4	11.6	10.8	10.6	14.7

Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23A	FY24E	FY25E
YoY growth (%)					
Revenue	(6.6)	21.6	23.2	27.6	23.2
EBITDA	(15.8)	3.8	35.7	14.3	39.9
Adjusted EPS	(11.8)	(2.0)	0.4	8.5	54.3
Profitability & Return ratios (%)					
EBITDA margin	19.3	15.5	17.3	16.3	18.5
EBIT margin	15.7	11.6	14.4	12.5	15.3
Adjusted profit margin	14.7	11.8	9.6	8.2	10.2
Adjusted ROAE	12.4	11.6	10.8	10.6	14.7
ROCE	13.4	12.1	16.9	14.7	19.7
Working capital days (days)					
Receivables	28	22	15	22	22
Inventory	50	34	53	32	30
Payables	26	22	46	37	37
Ratios (x)					
Gross asset turnover	1.2	1.4	1.6	1.1	1.3
Current ratio	2.7	2.1	1.8	1.8	1.8
Net interest coverage ratio	38.8	19.3	40.6	34.2	57.4
Adjusted debt/equity	0.0	0.0	0.0	0.2	0.0

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

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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): STAR CEMENT (STRCEM IN)



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

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