

# Stock Update

Improving operational profitability; Upgrade to Buy with a revised PT of Rs. 18,660

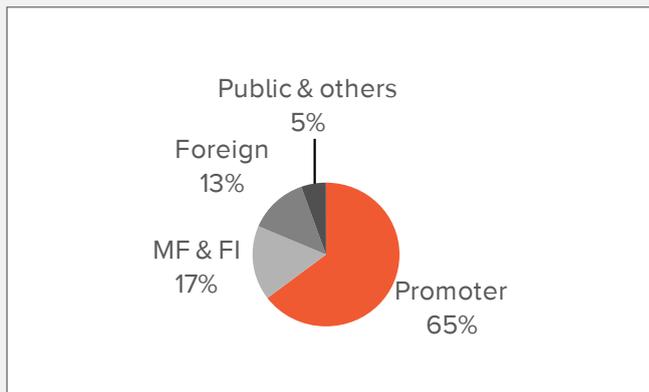
## Shree Cement

Reco: Buy | CMP: Rs16,050

### Company details

Price target:	Rs18,660
Market cap:	Rs55,914 cr
52-week high/low:	Rs19260/13125
NSE volume: (No of shares)	0.3 lakh
BSE code:	500387
NSE code:	SHREECEM
Sharekhan code:	SHREECEM
Free float: (No of shares)	1.2 cr

### Shareholding pattern



### Price chart



### Price performance

(%)	1m	3m	6m	12m
Absolute	-7.2	10.3	-3.7	-13.7
Relative to Sensex	-9.0	3.1	-4.0	-16.3

### Key points

- Healthy operational performance:** In Q3FY2019, revenue of Shree Cement grew by 20.8% y-o-y to Rs. 2,781 crore. Revenue growth was driven by 11.4% y-o-y rise in volume and 4.5% y-o-y rise in realisation. Operating profit margin for the quarter improved by 183 BPS y-o-y to 24.8% on account of lower freight costs (down 1.7% y-o-y on per tonne basis) and other expenses (down 0.7% y-o-y) along with higher realisation. Consequently, EBITDA per tonne grew by 6.4% y-o-y to Rs. 1,068 (adjusted for forex gain of Rs. 20 crore in Q3FY2019). However, lower other income (down 37% y-o-y), higher interest (up 2.9x y-o-y) and depreciation (up 1.6x y-o-y) led to a 9% y-o-y decline in PBT. Despite lower effective tax rate (19.6% in Q3FY2019 vs. 24.1% in Q3FY2018), adjusted net profit declined by 4% y-o-y to Rs. 281 crore.
- Capacity expansion plans on track to sustain volume growth:** Shree Cement commissioned 3MT clinker capacity at Gulbarga, Karnataka, in December 2018 for which equivalent cement capacity had been commissioned in June 2018. Further, it will be adding 5MTPA cement grinding capacity (3MTPA in Odisha + 2.5MTPA in Jharkhand) for a total cost of ~Rs. 903 crore to be added by Q2FY2020 and Q1FY2020-end, respectively. This is expected to take the domestic cement capacity from 37.8MT to 43.3MT by FY2020-end and further to 45.3MT by FY2021 with addition of 2MT Pune grinding unit. The proposed expansion plans are expected to benefit in terms of improving volume along with savings in logistics costs, as it is close to its regional markets.
- Outlook: Easing pressure on operating expenses and better utilisation to improve profitability:** Shree Cement is expected to sustain its healthy volume growth during FY2019-FY2021, backed by improving utilisation levels along with capacity expansion. Further, the company has been able to rein in operating expenses with operating margins improving over the trailing two quarters. Easing cost pressure from pet coke and diesel prices along with improving realisation is likely to aid in profitability during the same period. We estimate revenue and net earnings to report a 16% and 25% CAGR, respectively, during FY2019-FY2021.
- Valuation – Upgrade to Buy with a revised PT of Rs. 18,660:** We have fine tuned our estimates for FY2019, while we have lowered our estimates

for FY2020 (factoring higher depreciation and lower other income). We have introduced FY2021 estimates in this note. Shree Cement has been one of the efficient regional players with a healthy balance sheet. We expect the company to register a 25% CAGR in net earnings over FY2019-FY2021, backed by strong volume growth (12% CAGR) along with improvement

in operating margins (backed by stabilising operating expenses and likely improvement in realisation). We roll forward our valuation multiple to FY2021 and revise our price target (PT) to Rs. 18,660. We upgrade the stock to Buy.

- ◆ **Key risk:** Increased crude prices followed by higher pet coke prices remain the key downward risks to our call.

## Results

Particulars	Rs cr				
	Q3FY2019	Q3FY2018	y-o-y (%)	Q2FY2019	q-o-q (%)
<b>Net sales</b>	<b>2780.6</b>	<b>2302.7</b>	<b>20.8</b>	<b>2586.6</b>	<b>7.5</b>
Total expenditure	2090.6	1773.4	17.9	2013.3	3.8
<b>Operating profit</b>	<b>690.1</b>	<b>529.3</b>	<b>30.4</b>	<b>573.3</b>	<b>20.4</b>
Other income	55.3	87.3	-36.6	51.4	7.7
EBITDA	745.4	616.6	20.9	624.7	19.3
Interest	59.3	20.7	185.9	61.8	-4.0
PBDT	686.1	595.9	15.1	562.9	21.9
Depreciation	336.1	210.0	60.0	329.5	2.0
PBT	350.0	385.8	-9.3	233.4	49.9
Tax	68.7	92.8	-26.0	-47.6	-244.2
Exceptional items	-20.0	-40.3	-	231.7	-
<b>Reported PAT</b>	<b>301.3</b>	<b>333.3</b>	<b>-9.6</b>	<b>49.3</b>	<b>510.8</b>
<b>Adjusted PAT</b>	<b>281.3</b>	<b>293.0</b>	<b>-4.0</b>	<b>281.1</b>	<b>0.1</b>
<b>Margins (%)</b>			<b>BPS</b>		<b>BPS</b>
OPM	24.8	23.0	183	22.17	265
PAT	10.1	12.7	-261	10.9	(75)
Tax rate	19.6	24.1	-444	-20.4	4,002

## Valuation

Particulars	Rs cr			
	FY18	FY19E	FY20E	FY21E
Net sales	9,833.1	11,481.5	13,696.4	15,485.4
Growth y-o-y (%)	14.4	16.8	19.3	13.1
EBITDA	2,438.0	2,616.1	3,283.6	3,805.7
EBITDA margin (%)	24.8	22.8	24.0	24.6
Adjusted PAT	1,349.4	1,110.9	1,428.9	1,736.8
Growth y-o-y (%)	0.8	(17.7)	28.6	21.6
EPS diluted (Rs.)	387.3	298.6	410.1	498.5
P/E (x)	41.4	53.7	39.1	32.2
P/B (x)	6.3	5.9	5.2	4.6
EV/EBITDA (x)	22.0	20.6	16.4	14.1
EV/Sales (x)	5.5	4.7	3.9	3.5
RoE (%)	16.3	11.3	14.1	15.1
RoCE (%)	13.6	9.7	12.0	12.9

## Segmental analysis

**Cement division:** Revenue of the cement division increased by 16.3% y-o-y to Rs. 2,559 crore (net of GST) in Q3FY2019, driven by an 11.4% y-o-y increase in volumes, while realisation improved by 4.5% y-o-y. Further, lower freight cost (down 1.7% y-o-y on per tonne basis) and lower other expense (down 0.7% y-o-y) partially offset higher power and fuel cost (up 11.7% y-o-y) and raw-material cost (up 17.3% y-o-y). Overall, higher realisation covered increased

cost of production (up 3.9% y-o-y), leading to 6.4% y-o-y growth in EBITDA/tonne to Rs. 1,068.

**Power division:** The power division posted EBITDA profit of Rs. 57 crore in Q3FY2019 as compared to EBITDA loss of Rs. 5.2 crore in Q3FY2018 due to higher volume of 44.6 crore units (vs. 27.3 crore units in Q3FY2018) and higher realisation of Rs. 5.0/unit (vs. Rs. 3.8/unit in Q3FY2018) in Q3FY2019.

Segment revenue					Rs cr	
Particulars	Q3FY2019	Q3FY2018	y-o-y (%)	Q2FY2019	q-o-q (%)	
<b>Segment revenue</b>						
Cement	2559.4	2200.1	16.3	2407.1	6.3	
Power	502.6	349.6	43.8	442.4	13.6	
<b>Total</b>	<b>3062.0</b>	<b>2549.7</b>	<b>20.1</b>	<b>2849.5</b>	<b>7.5</b>	
Less: Inter segmental revenue	281.4	247.0	13.9	262.9	7.0	
Net segment revenue	2780.6	2302.7	20.8	2586.6	7.5	
<b>Segment results</b>						
Cement	172.0	224.9	-23.5	23.5	631.2	
Power	202.5	145.3	39.3	168.1	20.5	
<b>Total</b>	<b>374.4</b>	<b>370.2</b>	<b>1.1</b>	<b>191.6</b>	<b>95.4</b>	
<b>PBIT margin (%)</b>						
Cement	6.7	10.2	-350	1.0	574	
Power	40.3	41.6	-129	38.0	229	

## Per-tonne analysis of cement business

Particulars	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19	y-o-y (%)	q-o-q (%)
Volume	5,325,000	6,444,000	6,990,000	5,640,000	5,930,000	11.4	5.1
Realisation	4,132	4,157	4,105	4,268	4,316	4.5	1.1
<b>Cost break-up</b>							
RM cost	295	356	345	298	346	17.3	15.8
Employee expenses	275	231	244	301	281	2.0	-6.8
Power and fuel	747	755	787	842	834	11.7	-0.9
Transportation and handling	1,117	1,191	1,219	1,093	1,098	-1.7	0.4
Other expenses	694	668	648	787	689	-0.7	-12.4
Total expenditure per tonne	3,128	3,201	3,242	3,322	3,248	3.9	-2.2
EBITDA per tonne	1,004	956	863	946	1,068	6.4	12.9

## Per-unit analysis of power

Particulars	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19	y-o-y (%)	q-o-q (%)
Volume (core units)	27.3	34.5	45.1	40.0	44.6	63.4	11.6
<b>Realisation Rs./unit</b>	<b>3.8</b>	<b>3.8</b>	<b>4.4</b>	<b>4.5</b>	<b>5.0</b>	<b>32.0</b>	<b>10.5</b>
Revenue (Rs. cr)	102.6	132.2	200.5	179.5	221.3	115.7	23.2
Cost per unit	3.95	3.44	3.60	3.49	3.68	-6.8	5.5
Cost of generation (Rs. cr)	107.8	118.7	158.5	139.5	164.3	52.4	17.7
EBITDA (Rs. cr)	(5.2)	13.5	42.0	40.0	57.0	-	42.5
<b>EBITDA per unit</b>	<b>(0.19)</b>	<b>0.39</b>	<b>0.84</b>	<b>1.00</b>	<b>1.28</b>	<b>-</b>	<b>27.7</b>

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