Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

JK Lakshmi Cement Limited

Cash pile to help gain size

Cement	Sharekhan code: JKLAKSHMI	Result Update

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 286**	
Price Target: **372**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 3,369 cr
52-week high/low:	Rs. 389/180
NSE volume: (No of shares)	1.7 lakh
BSE code:	500380
NSE code:	JKLAKSHMI
Free float: (No of shares)	6.3 cr

Shareholding (%)

Promoters	46.2
FII	10.4
DII	20.8
Others	22.6

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	1.8	49.0	-18.7	-13.3
Relative to Sensex	-2.9	28.7	-11.5	-15.2

Sharekhan Research, Bloomberg

Summary

- We retain a Buy rating with unchanged PT of Rs. 372 given an attractive valuation and likely earnings bounceback from FY2022.
- Standalone revenues were in-line in Q1FY2021, while OPM and PAT lagged estimates, owing to lower realisation led by higher clinker sales and unfavourable geographical sales mix.
- Management expected to announce much-awaited brownfield expansions in Q3FY2021 which would provide next leg of growth.
- Company has slashed debt and improves its cash position significantly, which would help planned expansions.

JK Lakshmi Cement Limited (JKL) reported in-line standalone revenue at Rs. 825 crore, down 20.8% y-o-y. Sales volume declined 18.2% y-o-y (better than our estimates) affected by the COVID-19 lockdown in April 2020, while blended realization declined by 3.1% y-o-y. Lower realisations can be attributed to higher clinker sales during the quarter and an unfavourable geographic mix (higher sales in eastern region due to early earlier commencement of operations). Consequently, blended EBITDA/tonne lagged estimates at Rs. 752 (up 3.3% y-o-y). Opex/tonne remained largely in-line with savings in power & fuel, freight and other expenses on a per tonne basis. Lower than expected OPM at 17.4% (up 107 bps y-o-y) and higher effective tax rate led to lower than expected operating profit and net profit (down 36.2% y-o-y at Rs. 44.4 crore) for the quarter. During June and July 2020, JKL witnessed improving demand as good as corresponding periods last year. It expects sustained rural demand along with a pick-up in infrastructure demand from Q3FY2021 to achieve flat y-o-y volume growth for FY2021. Cement prices are expected to improve from September onwards post marginal decline witnessed during July and August 2020 due to the onset of monsoons. The company is set to revive its Rs. 1,200-1,400 crore brownfield expansion plan which is expected to be announced during next quarter. During Q1FY2021, the company has been able to reduce its standalone net debt by Rs. 200 crore and improve its cash position to Rs. 700 crore (Rs. 450 crore in FY2020) which will aid equity investments for planned expansion plans. We have improved upon volume estimate for FY2021 and OPM for FY2021, FY2022 and FY2023 leading to upward revision in standalone net earnings. The company is one of our preferred picks in the cement sector owing to its healthy balance sheet, efficient operations, favourable regional operations and attractive valuation. JKL is currently trading at an EV/EBITDA of 5.6x/4.6x its FY2022E/FY2023E earnings which we believe is attractive considering earnings bounce back from FY2022 onwards. Hence, we retain our Buy rating on the stock with unchanged PT of Rs. 372.

Key positives

- Lower-than-expected volume decline.
- Operating cost structure remained in line with savings in key input costs.
- Increase in cash position along with expected announcement of brownfield expansion in Q3FY2021.

Key negatives

- Lower than expected realization owing to higher clinker and unfavourable regional sales mix.
- Key states viz. Chhattisgarh, Odisha and Gujarat suffered due to COVID-19 severity.

Our Call

Valuation –Retain Buy with unchanged PT of Rs. 372: JKL is expected to benefit from sustained rural sector demand along with improvement in infrastructure demand expected from Q3FY2021. The company is likely to announce its much-awaited brownfield capacity expansion in the near term which would provide further head room for growth post a couple of years. Consequently, the company has been consistently de-leveraging its balance sheet along with improving its treasury corpus. The company is one of our preferred picks in the sector owing to its healthy balance sheet, efficient operations, favourable regional operations and attractive valuation. JKL is currently trading at an EV/EBITDA of 5.6x/4.6x its FY2022E/FY2023E earnings, which we believe is attractive considering a likely earnings bounceback from FY2022 onwards. Hence, we retain our Buy rating on the stock with unchanged PT of Rs. 372.

Key risk

Weak demand in North and East India along with weak pricing negatively affects profitability.

Valuation (Standalone) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	3,882	4,044	3,515	3,908	4,369
OPM (%)	10.7	16.6	15.9	15.5	16.0
Adjusted PAT	80	235	186	227	305
% y-o-y growth	*-5*	*196*	*-21*	*22*	*34*
Adjusted EPS (Rs.)	6.8	22.6	15.8	19.3	25.9
P/E (x)	42.4	12.7	18.1	14.8	11.1
P/B (x)	2.2	2.0	1.8	1.6	1.4
EV/EBITDA (x)	9.5	5.6	6.3	5.6	4.6
RoNW (%)	5.3	16.4	10.3	11.4	13.7
RoCE (%)	7.4	12.9	9.8	10.6	12.3

Source: Company; Sharekhan estimates

Revenues remained in-line while OPM and PAT came in lower than estimate due to unfavourable sales mix: JK Lakshmi posted 21% y-o-y decline in standalone net sales to Rs. 825 crore (in-line with our estimate) as volumes declined 18.2% y-o-y, while realisations declined by 3.1%. The sales volume was impacted by lockdown restrictions during April 2020 along with gradual re-opening. Although volume decline was lower than expected, blended realisation declined higher than expected owing to higher clinker sales (3.01 lakh tones versus 1.12 lakh tones in Q1FY2020) and higher volume share from eastern region (fetching lower realisations). Consequently, EBITDA per tonne came in lower than expectation at Rs. 752 (up 3.3% y-o-y). The company's operating cost structure largely remained in line with lower power & fuel costs (down 28% y-o-y on per tonne basis), lower freight costs (down 4.8% y-o-y) and lower other expense (down 9.5% y-o-y). Higher OPM at 17.4% (up 107 bps y-o-y) led to lower decline in operating profit (down 15.6% y-o-y at Rs. 143 crore). Lower revenues along with higher effective tax rate (32% versus 23.1% in Q1FY2020) led to 36% y-o-y decline in standalone profit to Rs. 44.4 crore, lower than our estimates.

Expansion plans to be revived: The company has put its capacity expansion plans on hold during Q4FY2020. However, expecting a sustained rural sector demand and revival of infrastructure demand from Q3FY2021, JKL is likely to revive its Rs. 1200 crore to Rs. 1400 crore brownfield capacity expansion plans at either Sirohi or Udaipur during Q3FY2021. Due to availability of land, the company can complete the expansion over 20-24 months post commencement of work. JKL also improved its cash position from Rs. 450 crore as of FY2020 to Rs. 700 crore in Q1FY2021, which would aid in infusing equity for the planned expansion. The company has brought down its net debt by Rs. 200 crore from FY2020 to Rs. 800 crore. It will be repaying Rs. 200 crore p.a. over the next two years. To reduce its power costs, the company is enhancing its waste heat recovery (WHR) power capacity by 10MW at Sirohi entailing capex of Rs. 120 crore which is expected to be completed by H2FY2022.

Key Conference call takeaways

- **Lower blended realisation:** The company's blended realisation was affected by higher clinker sales of 3.01 lakh tonne (versus 1.12 lakh tonne in Q1FY2020), higher sales in the eastern region (relatively lower realisations) and lower ready-mix concrete (RMC) revenue of Rs. 12 crore (versus Rs. 40-45 crore run-rate).
- **Demand outlook:** The company witnessed healthy demand during June 2020 and July 2020. However, eastern regions like Chhattisgarh and Odisha has been lately affected by intermittent lockdowns. In Gujarat, demand was weak during May and June 2020 owing to increased COVID-19 severity. Urban demand was affected while rural segment continued to be robust driven by both pent-up demand and some new demand. The rural demand is expected to remain strong for the full year. Infrastructure demand suffered due to labour shortages at sites and is expected to pick up post Diwali. The company expects normal demand environment during Q3FY2021. For FY2021, it targets to achieve flat volume growth.
- **Cement pricing outlook:** The cement industry witnessed some decline in prices from July onwards and in August, with the onset of monsoon, which is expected to reverse from September onwards as per the general trend. The average price difference between trade and non-trade price is on an average Rs. 40 to Rs. 50 per bag.
- **Capacity expansion plan:** The company is expected to announce clinker plus grinding brownfield expansion plan to the tune of Rs. 1,200-1400 crore in the next quarter. The company can complete the expansion within 20-24 months post commencement of work.
- **Debt repayment:** The company's standalone net debt reduced from Rs. 1,000 crore in FY2020 to Rs. 800 crore. The company has further Rs. 200 crore repayment each year over the next two years. The company's cash improved from Rs. 450 crore in FY2020 to Rs. 700 crore. Its listed subsidiary's debt remained at Rs. 550 crore. The company generates 9.5% p.a. pre-tax return from its treasury corpus (9.75% on inter-corporate deposits) as against 8.3% p.a. pre-tax interest cost on Rs. 1,500 crore term loans.

Financials (Standalone) Rs cr

Particulars	Q1FY2021	Q1FY2020	YoY %	Q4FY2020	QoQ %
Net Sales	**825.2**	**1041.9**	**-20.8%**	**1061.2**	**-22.2%**
Total Expenditure	681.8	872.1	-21.8%	859.2	-20.6%
Operating profit	**143.3**	**169.8**	**-15.6%**	**202.0**	**-29.1%**
Other Income	8.2	5.9	38.5%	22.5	-63.7%
EBIDTA	151.5	175.7	-13.8%	224.5	-32.5%
Interest	37.8	39.9	-5.3%	42.5	-11.0%
PBDT	113.7	135.8	-16.3%	182.1	-37.5%
Depreciation	48.4	45.3	6.9%	51.0	-5.0%
PBT	**65.3**	**90.5**	**-27.8%**	**131.1**	**-50.2%**
Tax	20.9	20.9	0.0%	30.3	-31.2%
Extraordinary items	0.0	-30.2	-	0.0	-
Reported Profit After Tax	44.4	39.4	12.7%	100.8	-55.9%
Adjusted PAT	**44.4**	**69.6**	**-36.2%**	**100.8**	**-55.9%**
EPS (Rs.)	3.8	5.9	-36.2%	8.6	-55.9%
Margins					
OPMs	17.4%	16.3%	107	19.0%	(167)
PAT	5.4%	6.7%	(130)	9.5%	(411)
Tax rate	32.0%	23.1%	891	23.1%	883

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Improving demand brightens outlook

Cement industry has seen sustained improvement in demand in the past fifteen years, barring a couple of years, while regional cement prices, have been on a rising trajectory over trailing five years. The cement industry amidst COVID-19 led disruption continued to witness healthy demand from rural sector while infrastructure demand is expected to pick-up from Q3FY2021 onwards with labourers returning project sites. The sector's long term growth triggers in terms of low per capita consumption and demand pegged at 1.2x GDP remains intact. Evidently, the government's Rs. 111 lakh crore infrastructure investment plan from FY2020 to FY2025 would lead to a healthy demand environment going ahead.

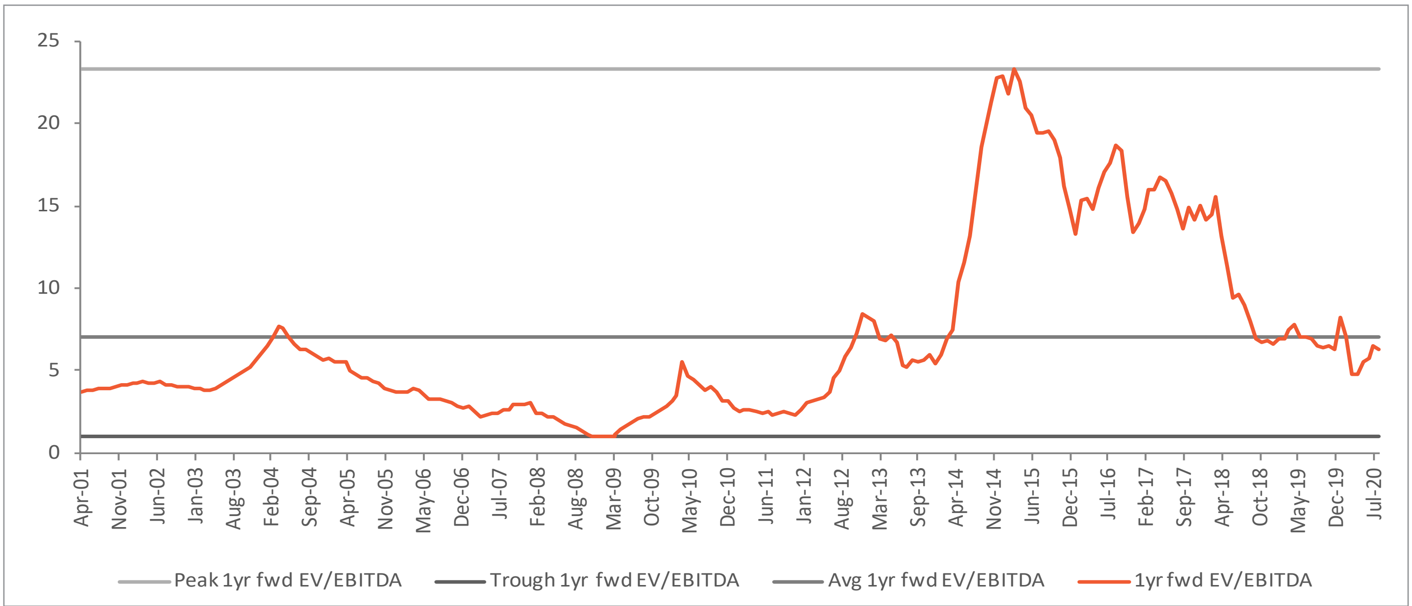
■ Company Outlook - Expect healthy earnings bounce back from FY2022 onwards

During June and July 2020, JKL witnessed improving demand as good as corresponding periods last year. It expects sustained rural demand along with pick up in infrastructure demand from Q3FY2021 to help achieve flat y-o-y volume growth for FY2021. Cement prices are expected to improve from September onwards post marginal decline witnessed during July and August 2020 due to onset of monsoon. The improving demand outlook along with healthy pricing discipline is expected to revive the company's earnings growth trajectory from FY2022 onwards. Further, the company is set to revive its Rs. 1,200-1,400 crore brownfield expansion plan which is expected to be announced during next quarter which would provide next leg of growth post couple of years.

■ Valuation - Retain Buy with unchanged PT of Rs. 372

JKL is expected to benefit from sustained rural sector demand along with improvement in infrastructure demand expected from Q3FY2021. The company is likely to announce its much-awaited brownfield capacity expansion in the near term which would provide further head room for growth post a couple of years. Consequently, the company has been consistently de-leveraging its balance sheet along with improving its treasury corpus. The company is one of our preferred picks in the sector owing to its healthy balance sheet, efficient operations, favourable regional operations and attractive valuation. JKL is currently trading at an EV/EBITDA of 5.6x/4.6x its FY2022E/FY2023E earnings, which we believe is attractive considering a likely earnings bounceback from FY2022 onwards. Hence, we retain our Buy rating on the stock with unchanged PT of Rs. 372.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
UltraTech	34.7	26.7	14.6	12.2	2.8	2.6	8.4	10.0
Shree Cement	58.7	42.7	21.1	17.0	5.6	5.1	10.0	12.5
JK Lakshmi Cement	18.1	14.8	6.3	5.6	1.8	1.6	10.3	11.4
The Ramco Cement	31.3	23.1	17.4	13.6	3.0	2.7	10.1	12.4

Source: Sharekhan Research

About company

JKL was set up in 1982 in Sirohi, Rajasthan. The company is part of JK Organisation, which operates in India and abroad and is present in the tyre, cement, paper, power transmission and sealing solutions, dairy products and textile industries. The company has a wide network of over 7,000 dealers across Rajasthan, Gujarat, Haryana, Delhi, Uttar Pradesh, Punjab, Jammu and Kashmir, Madhya Pradesh, Chhattisgarh, Odisha, South Bengal, Vidharbha, Mumbai and Pune.

Investment theme

JKL had undertaken capacity expansion plans of 8.6MT since FY2015, trebling its capacity to 13.3MT by FY2020. Moreover, JKL has been able to reduce its standalone net debt to equity at 0.7x in FY2020 from its peak of 1.5x in FY2015, which shows efficient capital management. The company has a brownfield expansion potential to reach 20MT in a short time. Now, it has two distinctive markets, i.e. the East and North West regions.

Key Risks

- Pressure on cement demand and cement prices in the north-west and east India can affect financial performance.
- Macroeconomic challenges leading to lower government spending on infrastructure and housing sectors can negatively affect the company's performance.

Additional Data

Key management personnel

Bharat Hari Singhania	Chairman
S A Bidkar	Chief Financial Officer
B K Daga	Vice President , Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Bengal & Assam Co Ltd	44.28
2	FRANKLIN TEMPLETON MUTUAL	9.49
3	Franklin Resources Inc	9.24
4	BANSAL SACHIN	3.84
5	HDFC Life Insurance Co Ltd	3.17
6	GOVERNMENT PENSION FUND - GLOBAL	2.63
7	Norges Bank	2.63
8	Axis Asset Management Co Ltd/India	2.60
9	India Capital Fund Ltd	2.40
10	ICICI Prudential Asset Management	1.89

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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