Sharekhan
by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

JK Lakshmi Cement

Quality at attractive valuation

Cement	Sharekhan code: JKLAKSHMI	Company Update

Stock 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. 253**	
Price Target: **Rs. 372**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

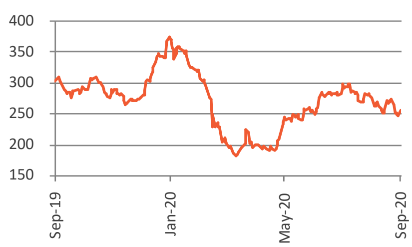
Company details

Market cap:	Rs. 2,976 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	-2.0	2.6	31.6	-15.2
Relative to Sensex	-0.3	-6.0	-1.9	-13.4

Sharekhan Research, Bloomberg

Summary

- We retain our Buy rating on JK Lakshmi Cement (JKL) with unchanged PT of Rs. 372, given attractive valuation and strong 28% CAGR net earnings over FY2021E-FY2023E.
- The company has seen improvement in demand for June and July, with July demand better than last year. Strong rural demand, infrastructure pick up to bring demand to normalcy in Q3FY2021.
- Expect announcement of much-awaited brownfield expansion in Q3FY2021, which would provide the next leg of growth. Strong cash balance and OCF generation over FY2021E-FY2023E to aid capacity expansion.
- The company is one of the preferred picks in the sector due to its healthy balance sheet, efficient operations, favourable regional dynamics, and attractive valuation.

JK Lakshmi Cement Limited (JKL)has been seeing improvement in demand as the country came out of the lockdown in May 2020. The company saw pick up in cement demand for June and July, with July demand better than last year. Although the urban sector had been hit by COVID-19, it had seen healthy demand from the rural sector with a mix of pent-up demand and new demand. JKL expects rural demand to continue to remain good for FY2021. Further, the infrastructure sector is expected to drive demand post Diwali, as labour shortages get completely resolved. Overall, JKL expects demand to return to normalcy in Q3FY2021. On the realisation front, cement prices are expected to improve post the monsoon season, following demand pick up from infrastructure, rural sector, and affordable housing segments. We expect JKL's standalone revenue to register an 11.5% CAGR over FY2021E-FY2023E, led by 6% volume CAGR over the same period. The company is set to revive its Rs. 1,200 crore-1,400 crore brownfield expansion plans, which is expected to be announced during the 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 crores in FY2020), which along with post tax operating cash flow generation of Rs. 1,400 crores+ will aid investments for planned expansion plans. We expect ROE to improve to 13.7% in FY2023E from 10.3% in FY2021E. 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 4.9x/4.0x its FY2022E/FY2023E earnings, which we believe is attractive considering earnings bounce back from FY2022. Hence, we retain our Buy rating on the stock with an unchanged price target (PT) of Rs. 372.

Our Call

Valuation –Retain Buy with an unchanged PT of Rs. 372: JKL is expected to benefit from sustained rural sector demand along with improvement in infrastructure demand expected from Q3FY2021. We expect its standalone net revenue to register an 11.5% CAGR during FY2021E-FY2023E. The company is likely to announce its much-awaited brownfield capacity expansion in the near term, which would provide further head room for growth. 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 4.9x/4.0x its FY2022E/FY2023E earnings, which we believe is attractive considering likely earnings bounce back from FY2022. Hence, we retain our Buy rating on the stock with an unchanged PT of Rs. 372.

Key Risks

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)	37.4	11.2	16.0	13.1	9.8
P/B (x)	2.0	1.7	1.6	1.4	1.3
EV/EBITDA (x)	8.6	5.0	5.6	4.9	4.0
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

Expect demand to improve briskly in post COVID-19 era

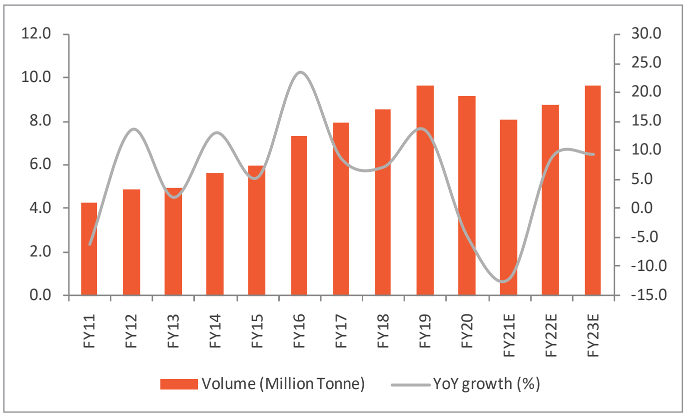
JKL had witnessed impact of COVID-19 like its sector peers, although it had reported better-than-estimated volume numbers for Q1FY2021. The company had witnessed improving demand environment in June and July, with July demand better than last year. The strong rural sector's demand supported by both pent-up demand and new demand had led to overall improvement in the demand environment. Post H1FY2021, we expect sustained rural demand along with demand emanating from infrastructure projects (as labour issue gets completely resolved) to bring pre-COVID normalcy. Further, cement prices are expected to inch up post the monsoon season, following improvement in the demand environment. We expect the company to report an 11.5% CAGR in standalone net revenue over FY2021E-FY2023E, led by healthy demand improvement along with firm realisations.

Expansion plans to provide further room for growth

The company had put its capacity expansion plans on hold during Q4FY2020. However, expecting sustained rural sector demand and revival of infrastructure demand from Q3FY2021, JKL is likely to revive its Rs. 1,200 crores to Rs. 1,400 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 along with strong post tax operating cash flows of over Rs. 1,400 crores during FY2021E-FY2023E would aid in investments for the planned expansion. The company's expansion plan would provide much needed head room for growth as demand picks up. The company has brought down its net debt by Rs. 200 crore from FY2020 to Rs. 800 crore. JKL will be repaying Rs. 200 crore per year 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.

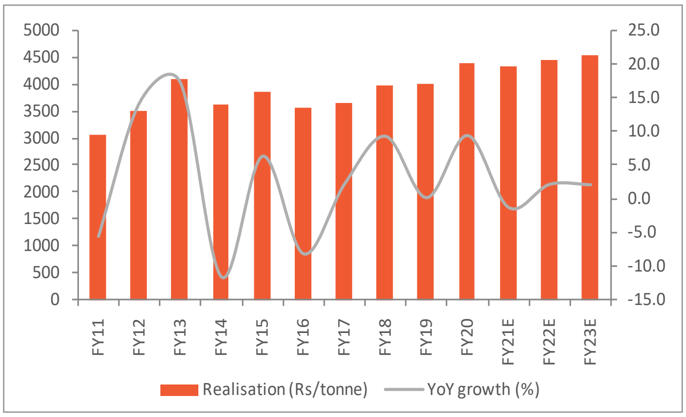
Financials in charts

Cement volume trend



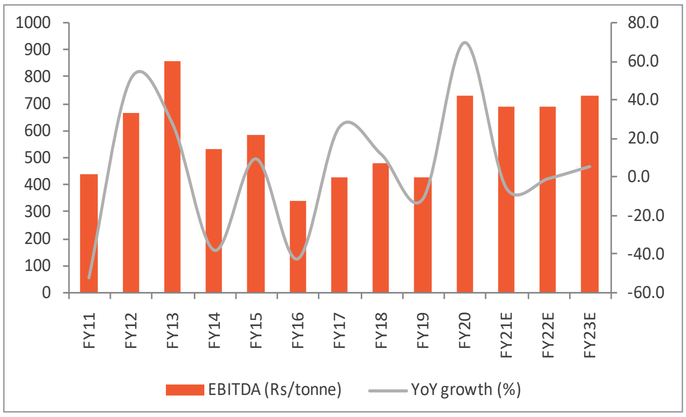
Source: Company, Sharekhan Research

Realisation trend



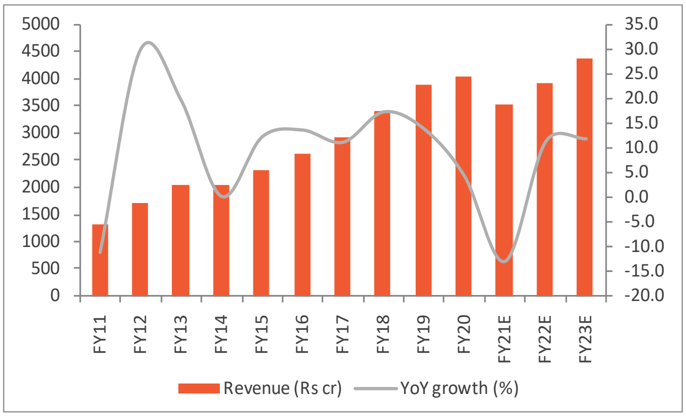
Source: Company, Sharekhan Research

EBITDA/tonne trend



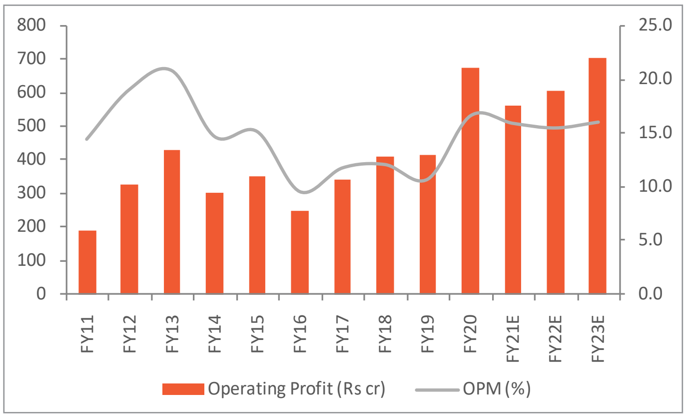
Source: Company, Sharekhan Research

Revenue trend



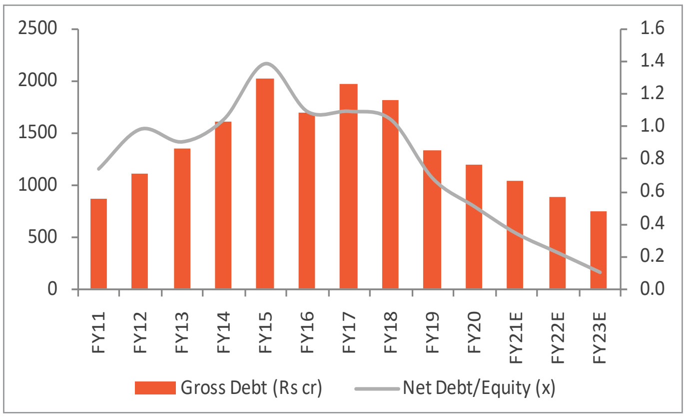
Source: Company, Sharekhan Research

Operating profit trend



Source: Company, Sharekhan Research

Leverage trend



Source: Company, Sharekhan Research

Outlook and Valuation

Sector view - Improving demand brightens outlook

The cement industry has seen sustained improvement in demand in the past 15 years, barring a couple of years, while regional cement prices have been on a rising trajectory over the trailing five years. Amidst COVID-19 led disruption, the cement industry continued to witness healthy demand from the rural sector, while infrastructure demand is expected to pickup from Q3FY2021, with labourers returning to project sites. The sector's long-term growth triggers in terms of low per capita consumption and demand pegged at 1.2x GDP remain 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.

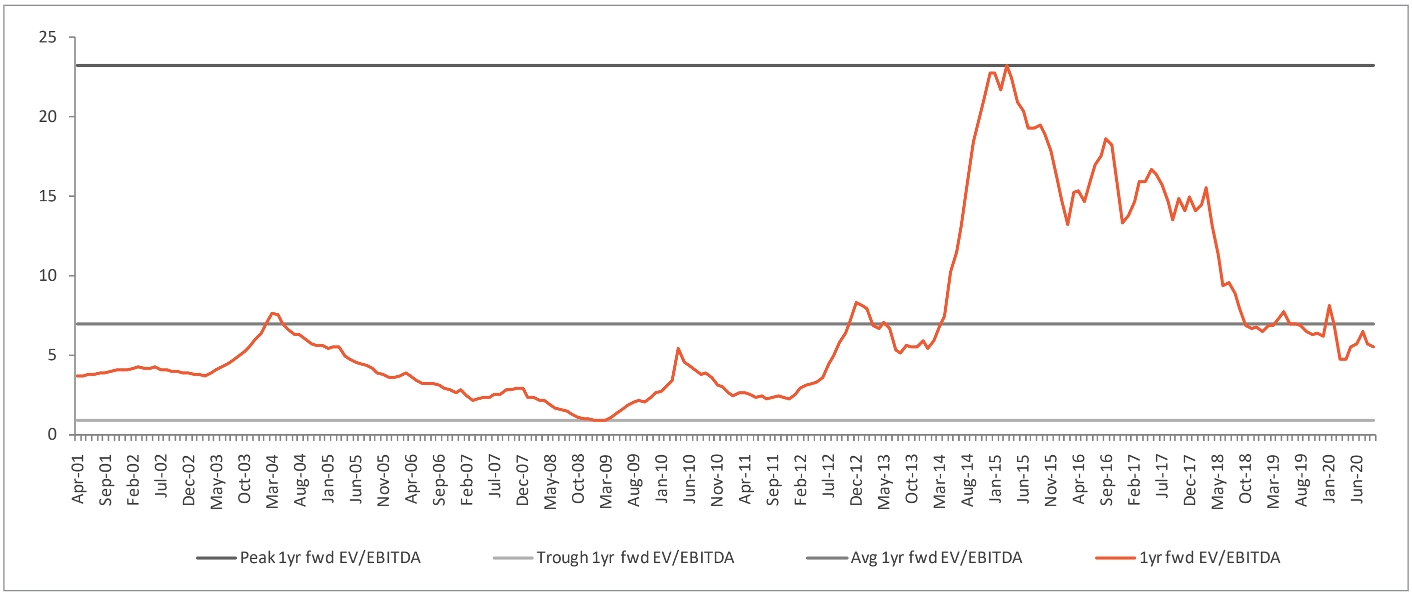
Company outlook - Expect healthy earnings bounce back from FY2022

During June and July 2020, JKL witnessed improving demand, as good as corresponding period last year. The company 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 post a marginal decline witnessed during July and August 2020 due to onset of the monsoon season. Improving demand outlook along with healthy pricing discipline is expected to revive the company's earnings growth trajectory from FY2022. Further, the company is set to revive its Rs. 1,200 crore-1,400 crore brownfield expansion plan, which is expected to be announced in the next quarter, which would provide the next leg of growth post couple of years.

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

JKL is expected to benefit from sustained rural sector demand along with improvement in infrastructure demand expected from Q3FY2021. We expect its standalone net revenue to register an 11.5% CAGR during FY2021E-FY2023E. The company is likely to announce its much-awaited brownfield capacity expansion in the near term, which would provide further head room for growth. 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 4.9x/4.0x its FY2022E/FY2023E earnings, which we believe is attractive considering likely earnings bounceback from FY2022. Hence, we retain our Buy rating on the stock with an unchanged PT of Rs. 372.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer valuation

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
UltraTech	34.0	26.2	14.3	11.9	2.7	2.5	8.4	10.0
Shree Cement	52.0	40.8	20.2	16.3	5.0	4.6	10.1	11.7
JK Lakshmi Cement	16.0	13.1	5.6	4.9	1.6	1.4	10.3	11.4
The Ramco Cement	28.7	22.4	16.8	13.5	3.2	2.8	11.7	13.4

Source: Company, 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, the company has two distinctive markets, i.e. the East and North West regions.

Key Risks

- Pressure on cement demand and cement prices in the northwest 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 and Compliance Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Bengal & Assam Co Ltd	44.28
2	FRANKLIN INDIA EQUITY FUND	9.24
3	FRANKLIN TEMPLETON MUTUAL	9.24
4	Franklin Resources Inc	8.90
5	BANSAL SACHIN	3.74
6	HDFC Life Insurance Co Ltd	2.98
7	India Capital Fund Ltd	2.87
8	GOVERNMENT PENSION FUND - GLOBAL	2.63
9	Norges Bank	2.63
10	Axis Asset Management Co Ltd/India	2.59

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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