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Stock Update

JK Lakshmi Cement Limited

Demand prospects stay firm

Cement	Sharekhan code: JKLAKSHMI	Results 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. 350**	
Price Target: **Rs. 410**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

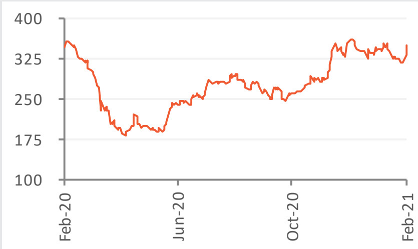
Company details

Market cap:	Rs. 4,123 cr
52-week high/low:	Rs. 369/180
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	10.7
DII	24.7
Others	18.4

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	1.5	24.4	19.0	1.0
Relative to Sensex	-1.9	0.7	-15.8	-23.9

Sharekhan Research, Bloomberg

Summary

- We retain a Buy rating on JK Lakshmi Cement with an unchanged PT of Rs. 410 given attractive valuations and healthy net earnings CAGR over FY2021E-FY2023E.
- JKL reported better-than-expected performance for Q3FY2021 led by a beat in volume offtake, higher other income, fall in interest costs and lower ETR. EBITDA/tonne rose 9% to Rs. 712.
- We expect strong demand environment to sustain during Q4 along with increase in prices expected during February 2020 in its region of operations. Impact of higher petcoke prices to be felt from Q1FY2022.
- Company to raise equity at UCW level through rights issue for its Rs. 1,500 crore expansion plan, which is expected to ease clinker and capacity constraints.

JK Lakshmi Cement Limited (JKL) reported better-than-expected performance for Q3FY2021 led by strong cement volume offtake. Standalone revenues grew 18.7% y-o-y to Rs. 1,193 crore led by 15.8% y-o-y rise in cement volume to 2.7 million tonne (much higher than ours as well as the street's estimates). The company witnessed strong demand in its regions of operations during Q3 which is expected to sustain in Q4 as well. Trade mix largely remained stable at 50% while share of valued added products increased from Rs. 73 crore in Q3FY2020 to Rs. 91 crore. It targets revenue of Rs. 500 crore from value-added products in FY2022. Pricing environment remained stable in all regions in January except in Gujarat where prices showed uptrend. Blended realizations improved by 1.0% q-o-q (up 2.5% y-o-y) to Rs. 4426/tonne. On the opex front, lower power & fuel costs (down 11.9% y-o-y on a per tonne basis led by lower petcoke price inventory) was offset by higher raw material costs (up 15.7% y-o-y). EBITDA/tonne increased by 9% y-o-y (down 9.1% q-o-q) to Rs. 712 (versus our estimate of Rs. 691/tonne). Consequently, operating profit grew 26.3% y-o-y (up 2.7% q-o-q) to Rs. 192 crore. Further, higher other income (up 41% y-o-y), lower interest (down 14% y-o-y) and lower effective tax rate (19.5% versus 34.7% in Q3FY2020) led to standalone net profit growth of 108% y-o-y (up 27% q-o-q) to Rs. 102.3 crore (much higher than our as well as street estimate). The company is undertaking 1.5mtpa additional clinker unit with WHRS and 2.5mtpa grinding unit in its subsidiary Udaipur Cement Works at an estimated cost of Rs. 1500 crore (debt of Rs. 1,000 crore). Financial closure of the project is expected during H1FY2022 post which it will take three more years before commencement of operations. The equity portion of Rs. 500 crore is expected to be funded majorly through raising of equity at UCW level through rights issue. As of December 2020, the company has a strong cash surplus of Rs. 900 crore while net debt stands at Rs. 550 crore. The planned capex is likely to ease clinker and capacity constraints for JK Lakshmi. We have improved volume estimates for FY2021E-FY2023E leading to an 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 5.2x/4.3x its FY2022E/FY2023E earnings, which we believe is attractive considering healthy net earnings CAGR over FY2021E-FY2023E. Hence, we retain a Buy rating on the stock with unchanged PT of Rs. 410.

Key positives

- Strong beat on volume offtake with 15.8% y-o-y rise for Q3.
- Low pet coke price per tonne led by inventory gains.
- Standalone cash surplus at Rs. 900 crore and net debt of Rs. 550 crore.

Key negatives

- Raw material and other expenses per tonne was higher than expected.

Our Call

Valuation –Retain Buy with unchanged PT of Rs. 410: JKL is expected to benefit from a strong demand in its region of operations viz. North, West and East led by rural sector demand and uptick in infrastructure demand. The pricing environment in its key regions remains healthy apart from the Eastern region, which is expected to get better going ahead. The company's announcement of much-awaited brownfield capacity expansion would ease clinker and capacity constraints and also provide further head room for growth. The company has also been generating strong operating cash flows and lowering leverage which would reduce incremental debt requirement for planned capex. JKL is currently trading at an EV/EBITDA of 5.2x/4.3x its FY2022E/FY2023E earnings, which we believe is attractive considering healthy net earnings CAGR over FY2021E-FY2023E. Hence, we retain our Buy rating on the stock with unchanged PT of Rs. 410.

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	4,328	4,637	5,117
OPM (%)	10.7	16.6	17.1	15.5	15.7
Adjusted PAT	80	235	323	322	394
% y-o-y growth	-5	196	37	0	23
Adjusted EPS (Rs.)	6.8	22.6	27.4	27.3	33.5
P/E (x)	51.8	15.5	12.8	12.8	10.5
P/B (x)	2.7	2.4	2.0	1.8	1.5
EV/EBITDA (x)	11.3	6.7	5.3	5.2	4.3
RoNW (%)	5.3	16.4	17.3	14.8	15.7
RoCE (%)	7.4	12.9	14.3	13.0	14.0

Source: Company; Sharekhan estimates

Strong beat on volume boost net earnings: JK Lakshmi Cement Limited (JKL) reported better-than-expected performance for Q3FY2021 led by a strong cement volume offtake. Standalone revenues grew 18.7% y-o-y to Rs. 1,193 crore led by 15.8% y-o-y rise in cement volume to 2.7 million tonne (much higher than our as well as the street's estimates). The company witnessed strong demand in its region of operations during Q3 which is expected to sustain in Q4 as well. Trade mix largely remained stable at 50% while share of value-added products increased from Rs. 73 crore in Q3FY2020 to Rs. 91 crore. It eyes a revenue of Rs. 500 crore from value-added products in FY2022. Pricing environment remained stable in all regions in January except in Gujarat where prices showed uptrend. The blended realisation improved by 1.0% q-o-q (up 2.5% y-o-y) to Rs. 4,426/tonne. On the opex front, lower power & fuel cost (down 11.9% y-o-y on per tonne basis led by lower petcoke price inventory) was offset by higher raw material costs (up 15.7% y-o-y). EBITDA/tonne increased by 9% y-o-y (down 9.1% q-o-q) to Rs. 712 (versus our estimate of Rs. 691/tonne). Consequently, operating profit grew 26.3% y-o-y (up 2.7% q-o-q) to Rs. 192 crore. Further, higher other income (up 41% y-o-y), lower interest (down 14% y-o-y) and lower effective tax rate (19.5% Vs 34.7% in Q3FY2020) led to standalone net profit growth of 108% y-o-y (up 27% q-o-q) to Rs. 102.3 crore (much higher than ours as well as the street's estimates).

Capacity expansion at Udaipur: The company is undertaking 1.5mtpa additional clinker unit with WHRS and 2.5mtpa grinding unit in its subsidiary Udaipur Cement Works at an estimated cost of Rs. 1500 crore (debt of Rs. 1000 crore). Financial closure of the project is expected during H1FY2022 post which it will take three more years before commencement of operations. The equity portion of Rs. 500 crore is expected to be funded majorly through raising of equity at UCW level through rights issue. As ofDecember 2020, the company has a strong cash surplus of Rs. 900 crore while net debt stands at Rs. 550 crore. The planned capex is likely to ease clinker and capacity constraints for the company.Apart from that, JKL's 10MW WHRS expansion at Sirohi is expected to get delayed by one to two months (earlier expected to commission by September 2021) to due labour issues on account of the COVID-19 pandemic.

Key Conference call takeaways

- **UCW capacity expansion:** The company is undertaking brownfield capacity expansion in its listed subsidiary Udaipur Cement Works (UCW) at a capex of Rs. 1500 crore. Financial closure of the project is expected in Q1FY2022 or Q2FY2022 post which it will take three years for commencement of plant operations. The capacity expansion includes 1.5MT clinker, 2.5MT cement, WHRS plant and railway sliding. It will cater mainly to Rajasthan and Gujarat markets. The project will have Rs. 1,000 crore of debt and Rs. 500 equity. The equity portion will have some contribution of internal accruals and equity raise (rights issue likely at UCW level). UCW requires equity support due to its high D/E.
- **Merger of UCW and JK Lakshmi:** As previously highlighted by management, merger of UCW with JK Lakshmi will take three to four years due to differential tax rates (34% for JK Lakshmi while UCW is under new tax regime at lower rate). JKL has MAT credit entitlement of Rs. 200 crore which would take 3-4 years to exhaust.
- **Demand and pricing:** Q3 cement demand was strong and is expected to sustain during Q4 too. The company can increase blending ratio (64% in Q3) to cater higher demand. The company would keep up growth at least at Industry growth rate. Gujarat region saw cement price rise in January while in North and East prices are stable. The east comprised 30% of the total volume which is a drag on realization.
- **Higher other expenses:** In Q3, other expenses were higher on account of provision for managerial remuneration, BCG costs for an additional assignment (Rs. 10 crore) and pick up in advertising activities. The other expense is expected to be higher in Q4 too.

- **Sirohi WHRS:** The project which was earlier envisaged to complete by September 2021 could face one to two month delay on account of labour issues during COVID-19.
- **VAP sales:** Value-added product sales for Q3FY2021 stood at Rs. 91 crore versus Rs. 73 crore in Q3FY2020. The company targets to achieve Rs. 500 crore from VAPs for FY2022.
- **Premium products:** The premium cement comprised 10% of overall sales and 20% of trade sales.
- **Trade mix:** The Company's trade sales was 50% in Q3FY2021 while it was 53% during 9MFY2021.
- **Pet coke price rise:** The Company's fuel mix is coal 27%, pet coke 68% and other alternate fuels 5%. During Q3, the average power fuel cost for the company stood at Rs. 6500 per unit while currently it is at over Rs. 9500. The rise in petcoke prices is expected to impact Q4 to some extent while the full impact will be seen from Q1FY2022 onwards.
- **Debt:** As ofDecember 2020, standalone debt stood at Rs. 1450 crore, cash at Rs. 900 crore and net debt of Rs. 550 crore. Consolidated debt stood at Rs. 1975 crore and net debt at Rs. 1020 crore.

Results (Standalone) Rs cr

Particulars	Q3FY2021	Q3FY2020	% y-o-y	Q2FY2021	% q-o-q
Net Sales	**1192.8**	**1005.0**	**18.7%**	**1044.8**	**14.2%**
Total Expenditure	1001.0	853.1	17.3%	858.1	16.7%
Operating profit	**191.8**	**151.9**	**26.3%**	**186.7**	**2.7%**
Other Income	20.7	14.7	40.6%	18.3	12.7%
EBIDTA	212.5	166.6	27.5%	205.1	3.6%
Interest	36.7	42.8	-14.3%	38.1	-3.8%
PBDT	175.8	123.8	42.0%	166.9	5.3%
Depreciation	48.7	48.5	0.4%	49.3	-1.4%
PBT	**127.2**	**75.4**	**68.7%**	**117.6**	**8.1%**
Tax	24.8	26.2	-5.1%	37.0	-32.9%
Extraordinary items	0.0	0.0	-	0.0	
Reported Profit After Tax	102.3	49.2	108.1%	80.6	27.0%
Adjusted PAT	**102.3**	**49.2**	**108.1%**	**80.6**	**27.0%**
EPS (Rs.)	8.7	4.2	108.1%	6.8	27.0%
Margins			BPS		BPS
OPMs	16.1%	15.1%	97	17.9%	(179)
PAT	8.6%	4.9%	368	7.7%	86
Tax rate	19.5%	34.7%	(1,521)	31.5%	(1,195)

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 fifteen years, barring a couple of years, while regional cement prices, have been on a rising trajectory over trailing five years. The cement industry continued to witness healthy demand from rural sector amid COVID-19 led disruption,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.

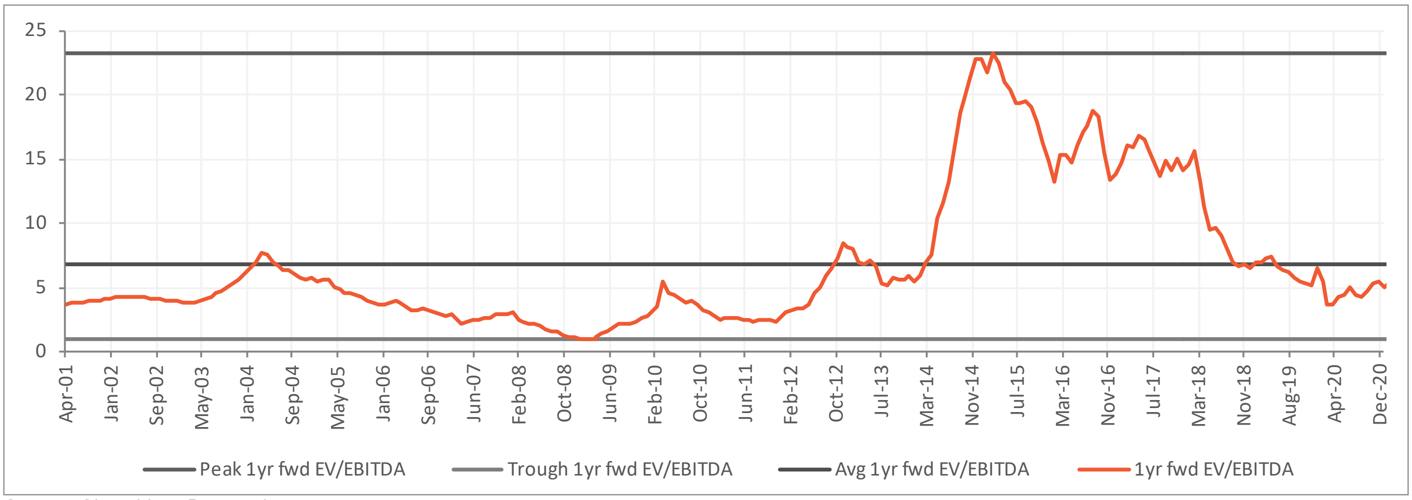
Company Outlook – Healthy demand and pricing environment

JKL is expected to benefit from sustained rural sector demand along with improvement in infrastructure demand. Pricing environment in its key regions remains healthy apart from Eastern region which is expected to get better going ahead. The company's announcement of much-awaited brownfield capacity expansion would ease clinker and capacity constraints along with providing further head room for growth. The company has also been generating strong operating cash flows and lowering leverage which would reduce incremental debt requirement for its planned capex. The company is one of our preferred picks in the sector owing to its healthy balance sheet, efficient operations, favourable regional operations and attractive valuations.

Valuation – Retain Buy with unchanged PT of Rs. 410

JKL is expected to benefit from a strong demand in its region of operations viz. North, West and East led by rural sector demand and uptick in infrastructure demand. The pricing environment in its key regions remains healthy apart from the Eastern region, which is expected to get better going ahead. The company's announcement of much-awaited brownfield capacity expansion would ease clinker and capacity constraints and also provide further head room for growth. The company has also been generating strong operating cash flows and lowering leverage which would reduce incremental debt requirement for planned capex. 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. We have improved upon volume estimates for FY2021E-FY2023E leading to an upward revision in standalone net earnings. JKL is currently trading at an EV/EBITDA of 5.2x/4.3x its FY2022E/FY2023E earnings, which we believe is attractive considering healthy net earnings CAGR over FY2021E-FY2023E. Hence, we retain our Buy rating on the stock with unchanged PT of Rs. 410.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
UltraTech	32.7	27.4	16.1	13.5	3.7	3.3	12.0	12.7
Shree Cement	38.4	33.7	18.8	16.3	5.6	4.9	15.6	15.5
JK Lakshmi Cement	12.8	10.5	5.2	4.3	1.8	1.5	14.8	15.7
The Ramco Cement	22.5	20.4	13.9	12.3	3.3	2.8	15.4	14.9

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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