Sharekhan by BNP PARIBAS

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Stock Update

JK Lakshmi Cement Limited

Sharp price hike in region of operations bodes well

Cement	Sharekhan code: JKLAKSHMI	Company 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. 434**	
Price Target: **Rs. 525**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

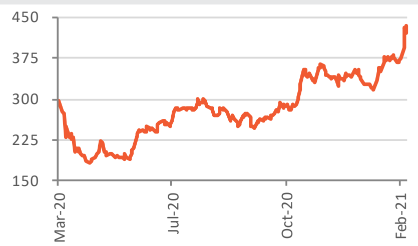
Company details

Market cap:	Rs. 5,109 cr
52-week high/low:	Rs. 440 / 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	24.0	20.0	67.7	46.2
Relative to Sensex	23.7	8.1	35.3	14.1

Sharekhan Research, Bloomberg

Summary

- We retain a Buy rating on JK Lakshmi Cement (JKL) with a revised PT of Rs. 525 given attractive valuations and healthy net earnings estimates over FY2021E-FY2023E.
- Average cement prices in the West and North (together ~75% of sales mix) in Q4FY2021 till date are up 3.7% and 2.0% versus Q4FY2020. Prices in the East rose sharply by 7.4% m-o-m in March 2021 leading to positive q-o-q growth for Q4.
- We expect JKL to benefit from strong non-trade demand environment in North and West and sustained healthy trade demand in East.
- Company to raise equity at UCW level through a rights issue for its Rs. 1,500 crore expansion plan, which is expected to ease clinker and capacity constraints.

JK Lakshmi Cement Limited (JKL) had reported strong performance for Q3FY2021 earnings, led by strong volume offtake (+15.8% y-o-y, +13.0% q-o-q) and rise in EBITDA/ tonne (+9.0% y-o-y, -9.1% q-o-q). The company witnessed strong demand in its key regions of operations in Q3 which is expected to sustain in Q4 as well which is expect to lead to a 7% volume growth for FY2021 (+4.0% 9MFY2021 volume offtake). Further, as per our channel check, average cement prices in the Western and Northern regions (together account of ~75% sales mix) during Q4FY2021 till date are up 3.7% and 2.0%, respectively versus Q4FY2020. Further, prices in the eastern region rose sharply by 7.4% m-o-m during February-end till date leading to an improvement in cement prices by 1.4% q-o-q for Q4FY2021 till date. Firm cement prices in the North and West and a sharp improvement in the East bodes well for JK Lakshmi. Further, the rise in non-trade demand in North and West and trade environment in East is expected to lead to healthy volume offtake for the company. Its trade mix is expected to remain stable at 50% and targets revenue of Rs. 500 crore from value-added products in FY2022. The company is undertaking 1.5 mtpa additional clinker unit with a WHRS and a 2.5 mtpa grinding unit in its subsidiary Udaipur Cement Works (UCW) 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 commencing operations. The equity portion of Rs. 500 crore is expected to be funded majorly through raising of equity at UCW level through a 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. 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 its FY2023E earnings, which is lower than its historical average considering healthy net earnings CAGR over FY2021E-FY2023E. Hence, we retain a Buy rating on the stock with revised PT of Rs. 525.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 525: JKL is expected to benefit from a strong non-trade demand in North and West along with high trade demand in East. Prices stay firm in its key regions apart from the Eastern region which is witnessing a sharp improvement. The company's announcement of a 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 5.6x its FY2023E earnings, which is lower than its historical average considering healthy net earnings CAGR over FY2021E-FY2023E. Hence, we retain a Buy rating on the stock with revised PT of Rs. 525.

Key Risks

Weak demand in North and East India and subdued pricing would negatively affect profitability.

Valuation (Standalone) Rs cr

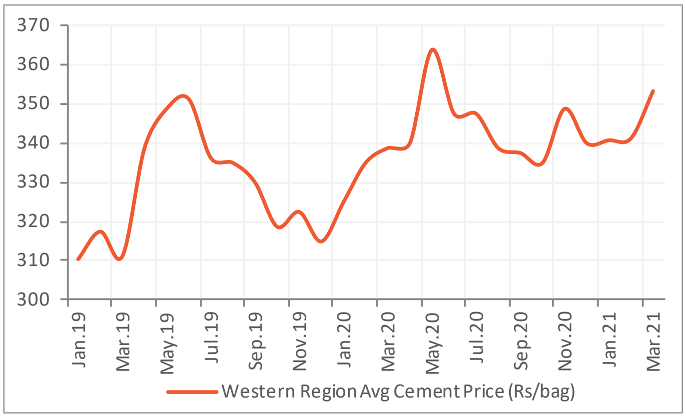
Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	3,882	4,044	4,328	4,637	5,117
OPM (%)	10.7	16.6	17.1	15.5	15.7
Adjusted PAT	80	235	323	322	394
% y-o-y growth	-5	196	37	0	23
Adjusted EPS (Rs.)	6.8	22.6	27.4	27.3	33.5
P/E (x)	64.2	19.2	15.8	15.9	13.0
P/B (x)	3.4	3.0	2.5	2.2	1.9
EV/EBITDA (x)	13.7	8.1	6.6	6.6	5.6
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

Cement prices up y-o-y in West and North during March 2021; East sharp uptick

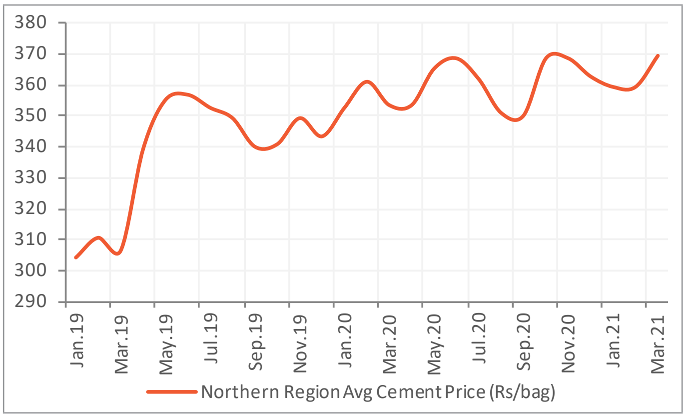
As per our channel checks, pan-India cement prices during March 2021 were higher 3.8% m-o-m (+6.6% y-o-y) as companies hiked prices from February 2021 end till date. Average cement prices for the West and North are up 3.5% and 2.8% m-o-m respectively. In the East, average cement prices rise sharply by 7.4% m-o-m for March 2021. Average cement prices in the Western and Northern regions (together accounting for ~75% sales mix) during Q4FY2021 till date are up by 3.7% and 2.0%, respectively versus Q4FY2020. Further, prices in the eastern region rose sharply by 7.4% m-o-m during February end till date leading to improvement in cement prices by 1.4% q-o-q for Q4FY2021 till date. Firm cement prices in North and West along with sharp improvement in the East bodes well for JK Lakshmi.

West price 3.7%/+1.1% (Q4FY21 vs. y-o-y/ q-o-q)



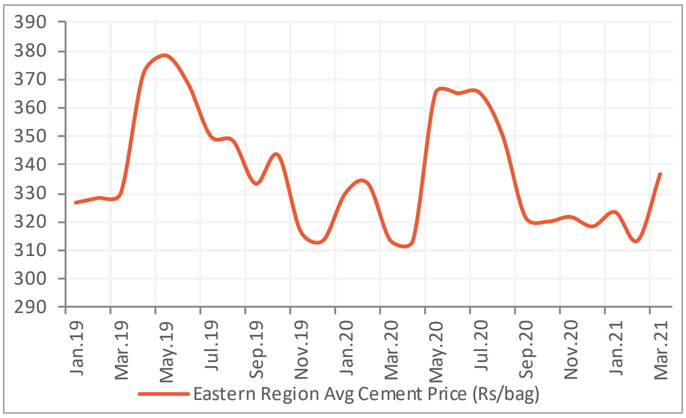
Source: Industry, Sharekhan Research

North price 2.0%/-1.1% (Q4FY21 vs. y-o-y/ q-o-q)



Source: Industry, Sharekhan Research

East price -0.3%/1.4% (Q4FY21 vs. y-o-y/q-o-q)



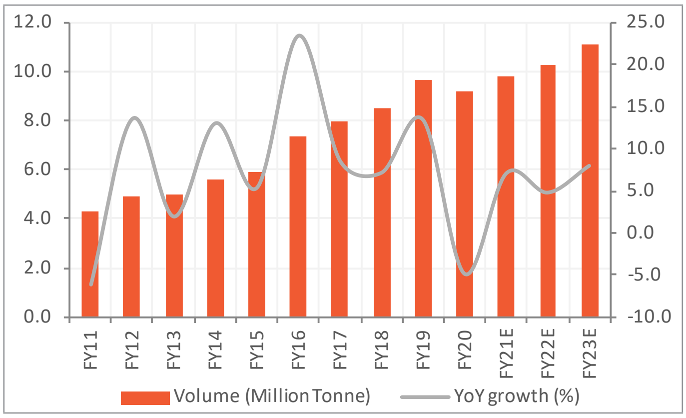
Source: Industry, Sharekhan Research

Demand environment remain healthy

JKL had reported a strong 15.8% y-o-y rise (up 13.0% q-o-q) in cement volume for Q3FY2021 maintaining a healthy volume growth trend y-o-y witnessed in Q2FY221 too. Hence, cement volumes for 9MFY2021 showed a marginal growth of 4.0% y-o-y (Q1FY2021 had volume dip of 18.2% y-o-y). The company witnessed strong demand in its regions of operations during Q3 which is expected to sustain in Q4 as well which is expect to lead to 7% volume growth for FY2021 the rise in non-trade demand in North and West along with sustained trade environment in East is expected to lead to healthy volume offtake for the company. We expect JKL's volumes to be healthy during Q4FY2021.

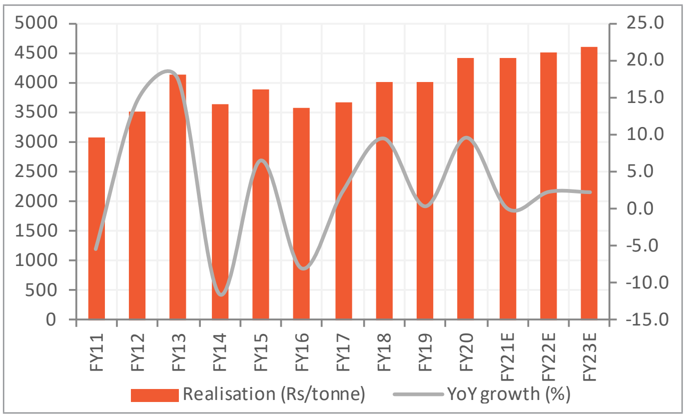
Financials in charts

Cement volume trend



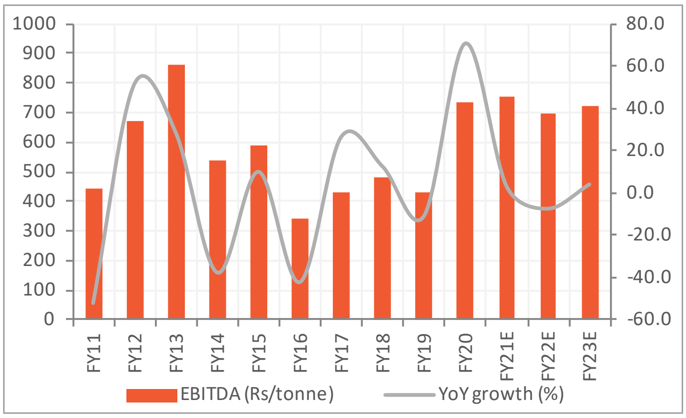
Source: Company, Sharekhan Research

Realisation trend



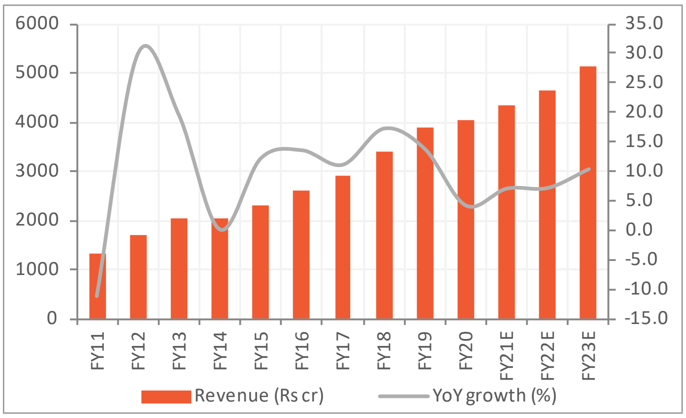
Source: Company, Sharekhan Research

EBITDA/tonne trend



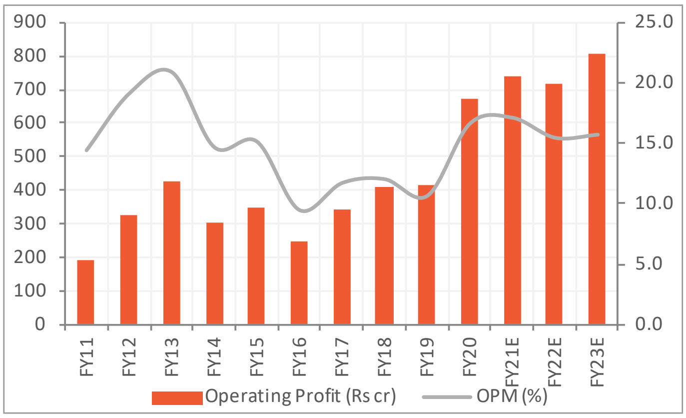
Source: Company, Sharekhan Research

Revenue trend



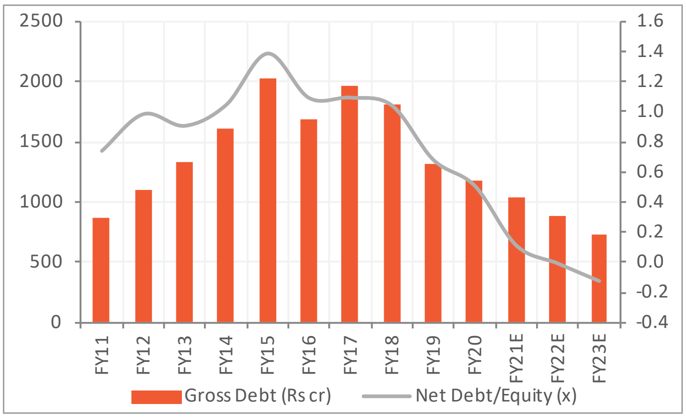
Source: Company, Sharekhan Research

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 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 healthy demand environment going ahead.

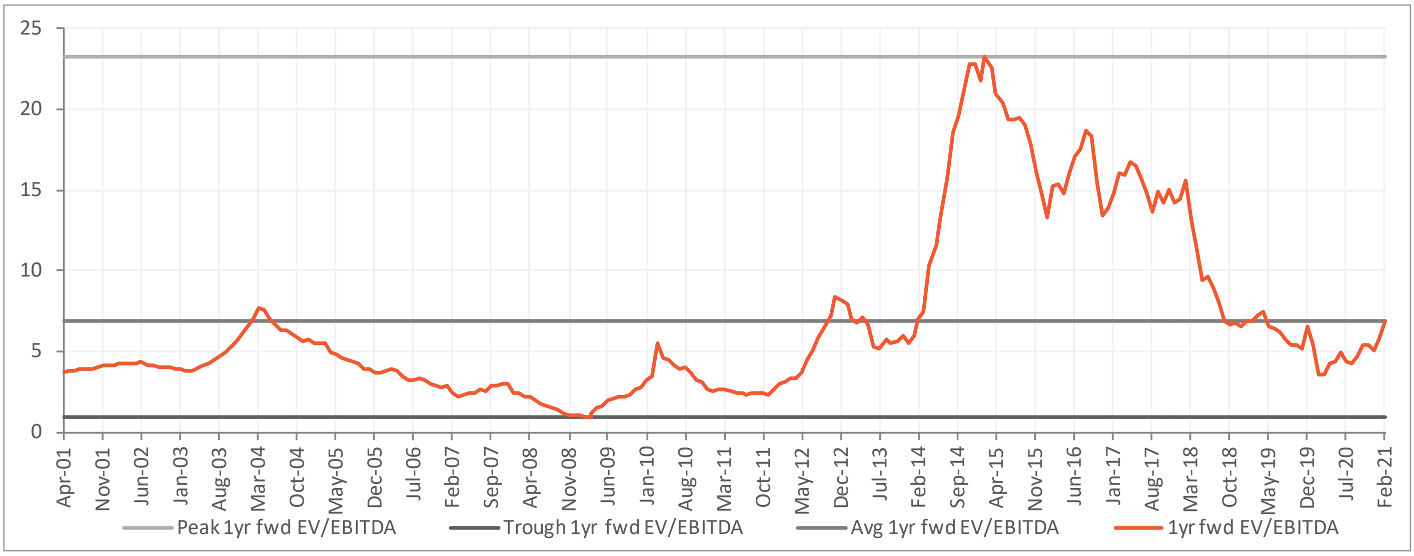
■ Company outlook - Healthy demand and pricing environment

JKL is expected to benefit from sustained rural sector demand and an 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 headroom 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 a revised PT of Rs. 525

JKL is expected to benefit from a strong non-trade demand in North and West along with high trade demand in East. Prices stay firm in its key regions apart from the Eastern region which is witnessing a sharp improvement. The company's announcement of a 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 5.6x its FY2023E earnings, which is lower than its historical average considering healthy net earnings CAGR over FY2021E-FY2023E. Hence, we retain a Buy rating on the stock with revised PT of Rs. 525.

One-year forward EV/EBITDA (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
Shree Cement	41.7	36.6	19.8	17.2	6.1	5.3	15.6	15.5
UltraTech	36.1	30.3	17.8	15.0	4.1	3.6	12.0	12.7
The Ramco Cement	28.2	24.9	16.7	14.7	3.8	3.3	14.2	14.1
JK Lakshmi Cement	15.9	13.0	6.6	5.6	2.2	1.9	14.8	15.7
Dalmia Bharat	30.9	25.4	10.1	8.6	2.4	2.2	8.0	9.0

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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