Sharekhan by BNP PARIBAS

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Dalmia Bharat Ltd

Strong Q2; On track of expansion

Cement	Sharekhan code: DALMIABHA

Reco/View	Reco: **Buy**	↔	CMP: **Rs. 1,990**	Price Target: **Rs. 2,601**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 30.70

Updated Oct 08, 2021

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

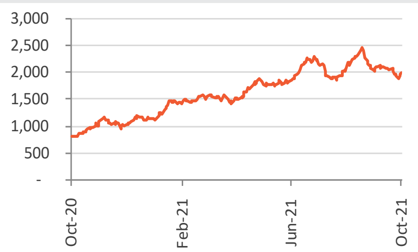
Company details

Market cap:	Rs. 37,242 cr
52-week high/low:	Rs. 2547/805
NSE volume: (No of shares)	2.0 lakh
BSE code:	542216
NSE code:	DALMIABHA
Free float: (No of shares)	8.2 cr

Shareholding (%)

Promoters	56.0
FII	13.8
DII	6.1
Others	24.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-4.1	-6.8	29.5	137.1
Relative to Sensex	-5.1	-20.7	9.0	86.2

Sharekhan Research, Bloomberg

Summary

- In Q2FY2022, revenues remain in-line while operational profitability surprised positively led by tight control on key input costs.
- The company expects demand and prices to pick up in H2. Its capacity expansion plans remain on track to achieve 48.5MTPA cement capacity by FY2024.
- It remains focused on improving green fuel mix, transparent treasury allocation, sale of non-core assets and improving shareholder returns.
- We maintain a Buy on stock with an unchanged PT of Rs. 2,601, as we see further upside considering its strong earnings growth outlook over FY2021-FY2024E.

Dalmia Bharat (Dalmia) reported in-line consolidated revenues at Rs. 2577 crore (up 11.4% y-o-y) led by volume growth of 6.3% y-o-y and blended realization growth of 4.9% y-o-y. It positively surprised on EBITDA/tone which stood at Rs. 1218 mainly led by sequential decline in power & fuel and freight costs despite increase in pet coke/coal price and diesel prices. Hence, operating profit/adjusted net profit at Rs. 621 crore/Rs. 217 crore were much higher than our estimates. The company expects demand and cement prices to improve in east in H2. It is on track to reach 48.5MTPA cement capacity by March 2024 from current 33MTPA.

Key positives

- Better than expected operational profitability led by tight control on key input costs.
- Addition of 2.25MT Odisha unit and 3MT Murli unit to take capacity to 36MTPA by FY2022. On track to achieve 48.5MTPA capacity by FY2024.
- Cement price increase by Rs. 10-25 per bag from 1st October and slated to further increase in November.

Key negatives

- Weak demand and pricing environment in East led by floods, drop in cement demand.
- Pet coke prices currently at $220-240 as against $80-100 last year.

Management Commentary

- The management expects demand and pricing environment to rise in H2.
- The company would be incurring Rs. 3000 crore capex in FY2022 and expects to reach cement capacity of 36MT by March 2022 and 48.5MT by March 2024.
- The company is using various measures like using lignite, usage of green fuel, lower heat consumption for clinker and lower power consumption for cement to control the rising power & fuel costs.

Revision in estimates – We have revised our estimates upwards factoring higher operational profitability.

Our Call

Valuation – Maintain Buy with an unchanged PT of Rs. 2,601: Dalmia Bharat has addressed its medium and long-term growth plans through its decadal capital allocation plan, which would ensure a more predictable, sustainable, and profitable growth path going ahead. The company would be focusing on achieving 14-15% RoCE over the next few years and maintain its balance sheet quality. Dalmia is currently trading at an EV/EBITDA of 12x/10x its FY2023E/FY2024E earnings, which we believe leaves room for further upside, considering its strong earnings growth trajectory over the next three years. Hence, we retain Buy with an unchanged price target (PT) of Rs. 2,601.

Key Risks

1) Pressure on cement demand and cement prices in the East, North-east and South of India can affect financial performance; and 2) Macroeconomic challenges leading to lower government spending on infrastructure and housing sectors can also impact performance.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	10,522	12,163	14,282	16,869
OPM (%)	26.4	23.2	21.9	22.0
Adjusted PAT	992	997	1,065	1,360
% y-o-y growth	270.1	0.5	6.8	27.7
Adjusted EPS (Rs.)	53.6	53.9	57.6	73.5
P/E (x)	37.1	36.9	34.6	27.1
P/B (x)	2.9	2.7	2.5	2.3
EV/EBIDTA (x)	13.2	13.0	11.7	9.8
RoNW (%)	8.6%	7.6%	7.6%	8.9%
RoCE (%)	9.3%	7.2%	7.2%	8.3%

Source: Company; Sharekhan estimates

Revenues remained in-line while EBITDA/T surprised positively

Dalmia Bharat reported consolidated net revenues growth of 11.4% y-o-y at Rs. 2577 crore which was largely in-line with our estimate. Cement volumes were up 6.3% y-o-y (+4.3% q-o-q) at 5.1 MnT while blended realizations were up 4.9% y-o-y (-4.5% q-o-q) at Rs. 5053/T. Blended consolidated EBITDA/T at Rs. 1218 (-16.3% y-o-y, -16.5% q-o-q) was higher than our estimate of Rs. 946/T. The better than expected EBITDA/T was led primarily due to by lower than expected raw material costs at Rs. 655/T (-5.9% y-o-y, +20.8% q-o-q), power & fuel costs at Rs. 990/T (+37.4% y-o-y, -6.3% q-o-q) and freight costs at Rs. 986/T (+0.1% y-o-y, -6.7% q-o-q). Other expense stood at Rs. 816/T (+28.8% y-o-y, +1.8% q-o-q). Overall, consolidated operating profit declined by 11% y-o-y (-13% q-o-q) at Rs. 621 crore but was much higher than our estimate. The consolidated adjusted net profit of Rs. 217 crore was down 6% y-o-y (-3% q-o-q) aided by higher other income and lower interest expense.

Capacity expansion plans on track

The company commercialized 2.25MT cement capacity near Cuttack, Odisha and began trial run production of 3MT plant at Maharashtra (erstwhile Murli Industries). The company would be incurring Rs. 3000 crore capex in FY2022 and expects to reach cement capacity of 36MT by March 2022 and 48.5MT by March 2024. It has outlined its capital allocation strategy over the next decade to increase capacity at 14-15% CAGR to reach 110-130 million tonnes by 2031 which would be done through both organic and inorganic routes maintaining Net Debt/EBITDA below 2x (unless a large ticket-size acquisition happens). Dalmia would also focus on increasing transparency and improve corporate governance apart from allocating treasury corpus toward higher rated instruments (85% towards AAA+, 15% in AA+).

Key conference call takeaways:

- **Q2 performance:** The sequential decline in realisation was on account of dip in prices in eastern region and southern region. Heavy rains, floods and drop in cement demand led to weakening of cement prices in east. The company's product mix shifted to Portland composite cement from Portland slag cement. The blended cement mix was 75% versus 80% last year.
- **Outlook:** The company expects cement demand and prices to increase from here on.
- **Cement price:** The company has increased cement prices from 1st October in east to the tune of Rs. 10-25 per bag. It further expects price to increase in November.
- **Power & fuel price:** The average fuel consumption price for Q2 was $120-130. The pet coke prices are currently at $220-240 versus $80-100 last year. The pet coke consumption was reduced to 34% from 47% in Q1FY22. Imported coal comprised 28-30%, domestic coal/lignite 28-30% and balance green fuel. The power & fuel cost per tonne dropped q-o-q owing to lower pet coke consumption, usage of lignite, increase in heat consumption, lower power consumption for cement and usage of greenfuel.
- **Lead distance:** The company brought down lead distance by 12-14km.
- **Green power:** In Q2, the green fuel percentage was 12%. The company will be adding 9MW WHRS and 70MW+ solar power in later part of the year.
- **Capacity expansion:** The addition of 2.25MT Odisha capacity has taken its total cement capacity to 33MT. It also undertook 0.2MT clinker de-bottlenecking. The company would start commercial production of Murli unit in December 2021 which will take its total cement capacity to 36MT by March 2022. The company is on time to reach 48.5MT capacity by March 2024.
- **Exceptional items:** The company accrued Rs. 56 crores incentives related to April 2019 to June 2021 in Q2. It also wrote back Rs. 24 crore liabilities. It made provision of Rs. 30 crore for inter-corporate loan. The company received Rs. 16 crore rail incentives which is also expected in next year.
- **Incentives:** The company booked Rs. 113 crore incentives in H1 and Rs. 80-85 crore in Q2. It will book Rs. 120 crore in H2. The company expects to receive Rs. 200 crore plus incentives for FY2023 and FY2024. The incentives for Bihar unit will be there till March 2024.
- **Capex:** The company incurred Rs. 440 crore capex in Q2 and Rs. 780 crore in H1. The company would be incurring Rs. 3000 crore capex for FY2022.
- **IEX share sale:** The company sold 21.4 lakh shares of IEX reducing its stake to 14.8%.

Results (Consolidated) Rs cr

Particulars	Q2FY22	Q2FY21	y-o-y	Q1FY22	q-o-q
Net Sales	**2577**	**2313**	**11.4%**	**2587**	**-0.4%**
Total Expenditure	1956	1615	21.1%	1874	4.4%
Operating profits	**621**	**698**	**-11.0%**	**713**	**-12.9%**
Other Income	45	40	12.5%	26	73.1%
EBIDTA	666	738	-9.8%	739	-9.9%
Interest	50	73	-31.5%	60	-16.7%
PBDT	616	665	-7.4%	679	-9.3%
Depreciation	303	299	1.3%	297	2.0%
PBT	**313**	**366**	**-14.5%**	**382**	**-18.1%**
Tax	93	136	-31.6%	98	-5.1%
Extraordinary items	13	-1	-	-4	
Minority Interest	5	0		11	
Reported Profit After Tax	204	232	-12.1%	227	-10.1%
Adjusted PAT	**217**	**231**	**-6.1%**	**223**	**-2.7%**
EPS	12	12	-6.1%	12	-2.7%
OPMs	24.1%	30.2%	-608 bps	27.6%	-346 bps
PAT	8.4%	10.0%	-157 bps	8.6%	-20 bps
Tax rate	29.7%	37.2%	-745 bps	25.7%	406 bps

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Improving demand brightens outlook

The cement industry has seen sustained improvement in demand over the past 15 years, barring a couple of years, while regional cement prices have been on a rising trajectory over the trailing five years. Amid COVID-19 led disruptions, the cement industry continued to witness healthy demand from the rural sector, while infrastructure demand is expected to pick-up 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 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.

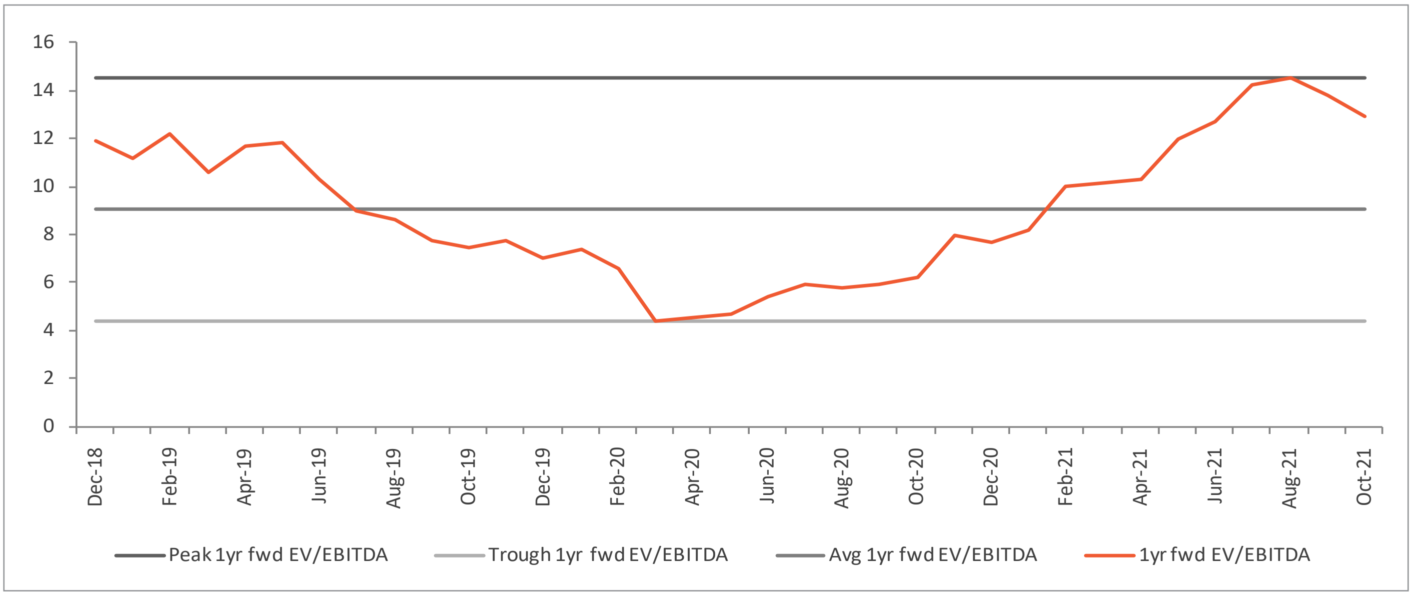
■ Company outlook - Aggressive expansion plans to capture high growth opportunities

Dalmia is on a strong growth trajectory for the next five years with capacity expansion plans lined up for the medium and long term. The company outlined its capital allocation strategy over the next decade to increase capacity at 14-15% CAGR to reach 110-130-million tonnes by 2031, which would be done through both organic and inorganic routes maintaining Net Debt/EBITDA below 2x (unless a large ticket size acquisition is done). It also highlighted allocation towards shareholders' returns (10% of OCFs) and Green & Innovation fund (10% of OCF). It targets to reach 48.5-million tonne cement capacity (current 30.8-million tonnes) over the next three years initially expanding in Southern and North East regions.

■ Valuation - Maintain Buy with an unchanged PT of Rs. 2,601

Dalmia Bharat has addressed its medium and long-term growth plans through its decadal capital allocation plan, which would ensure a more predictable, sustainable, and profitable growth path going ahead. The company would be focusing on achieving 14-15% RoCE over the next few years and maintain its balance sheet quality. Dalmia is currently trading at an EV/EBITDA of 12x/10x its FY2023E/FY2024E earnings, which we believe leaves room for further upside, considering its strong earnings growth trajectory over the next three years. Hence, we retain Buy with an unchanged price target (PT) of Rs. 2,601.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
UltraTech Cement	29.1	24.1	14.9	12.3	3.8	3.3	13.8	14.6
Dalmia Bharat	34.6	27.1	11.7	9.8	2.5	2.3	7.6	8.9
Shree Cement	35.4	30.3	18.3	15.4	5.1	4.5	15.5	15.8
The Ramco Cement	26.2	23.6	15.8	14.2	3.2	2.9	13.0	12.9

Source: Company, Sharekhan estimates

About company

Dalmia Bharat started its journey in 1939 and has a legacy of eight decades. The company possesses India's fifth largest installed cement manufacturing capacity of 26.5 MT spread across 13 manufacturing plants in nine states. The company's addressable market spans 22 states in the East, North East and Southern India. Dalmia Bharat comprises ~5% of the country's cement capacity. It has captive power generation capacity of 195MW (including solar and waste heat recovery plants).

Investment theme

Dalmia is on a strong growth trajectory for the next five years with capacity expansion plans lined up for medium and long term. The company is slated to increase its capacity from current 28.5 MTPA to 37.3 MTPA by FY2022E. The capacity expansion would help it consolidate its leadership position in the East and venture into the West through the acquisition of Murli Industries. Further, it is chalking out a capital allocation strategy to double its capacity over the next three years. The detailed plan is expected to be shared over the next quarter. However, it aims to become a large pan-India player through both organic and inorganic routes. Also, despite, its expansion plans, the company would turn net cash surplus by FY2023E.

Key Risks

- Pressure on cement demand and cement prices in the east, north east and west 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

Mr. Pradip Kumar Khaitan	Chairman
Mr. Gautam Dalmia	MD
Mr. Puneet Yadu Dalmia	CEO,MD

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	RAMA INV CO PVT LTD	42.75
2	SITA INV CO LTD	7.44
3	Dharti Investment & Holdings	1.69
4	IEPF	1.46
5	JH DALMIA TRST	1.39
6	KAVITA DALMIA PARIVAR	1.39
7	Valiant Mauritius Partners Ltd	1.35
8	Franklin Resources Inc	1.34
9	KRITAGYATA TRUST	1.10
10	Dalmia Bharat Sugar & Industries	1.01

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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