

Muted performance; outlook remains challenging...

HEG reported a subdued set of Q1FY21 numbers on account of a muted operational performance wherein it reported a loss at the EBITDA level. For standalone operations, topline came in at ₹ 233.3 crore (down 71% YoY) & reported EBITDA loss came in at ₹ 11.3 crore (vs. EBITDA profit of ₹ 347.8 crore in Q1FY20). For the quarter, it reported a negative EBITDA margin of 4.8% compared to positive margin of 42.6% in Q1FY20. During the quarter, as the lockdown was in force for a significant period, the company's operations and financial results were impacted. On account of Covid-19 related lockdowns, the company reported subdued volumes, leading to negative operating leverage. For Q1FY21, other expenses as a percentage of sales were at 33.5% compared to 16.9% in Q1FY20 and 30% in Q4FY20. Other income for the quarter aided the company to report a profit at the net level. Other income for the quarter was at ₹ 46 crore in comparison to ₹ 39.2 crore in Q1FY20. Hence, for standalone operations, HEG reported a profit of ₹ 10.8 crore in Q1FY21 (net profit of ₹ 234.4 crore in Q1FY20).

Graphite electrodes demand to remain muted...

Global and domestic demand for graphite electrode has been impacted by the partial closure of steel capacity and lower steel production. Furthermore, on account of the Covid-19 crisis, destocking of graphite electrode inventory at the customer end has been delayed and is happening at a slower pace than anticipated, thereby impacting demand prospects.

Model capacity utilisation of 50% in FY21E, 60% for FY22E...

On account of muted demand from the steel sector, we expect HEG's capacity utilisation levels to remain subdued. Going forward, we model capacity utilisation of 50% for FY21E and 60% for FY22E.

Valuation & Outlook

HEG reported a muted performance in Q1FY21 on the back of weak demand from the steel sector. Going forward, over the near term, demand for graphite electrodes is expected to remain subdued due to partial closure of steel capacities globally, lower steel production and de-stocking of electrode inventory at the customer end at a slower pace than anticipated, thereby adversely impacting demand prospects. FY21 is expected to remain a challenging year for the company as graphite electrode demand and realisation is expected to remain under pressure. We value the stock at 4x FY22E EV/EBITDA and arrive at a target price of ₹ 750. We have a **HOLD** recommendation on the stock.



Particulars

Particulars	Amount
Market Capitalisation	₹3003 crore
Debt in ₹ crore (FY20)	593
Cash & Cash Eq.(FY20)	1,594
EV	₹ 2245 crore
52 Week H / L (₹)	1473 / 413
Equity Capital (₹)	39
Face Value	₹ 10

Key Highlights

- For Q1FY21, capacity utilisation level at ~50% (~50% in Q4FY20, ~85% in Q1FY20)
- Maintain HOLD rating on stock with revised target price of ₹ 750

Research Analyst

Dewang Sanghavi
dewang.sanghavi@icicisecurities.com

Key Financial Summary

(₹ Crore)	FY18	FY19	FY20	FY21E	FY22E
Net Sales	2,750	6,593	2,149	1,223	1,448
EBITDA	1,722	4,658	-6	-65	284
EBITDA Margin (%)	62.6	70.7	(0.3)	(5.3)	19.6
Adj PAT	1,081	3,050	53	16	285
EPS (₹)	270.6	790.2	13.8	4.0	73.7
EV/EBITDA (x)	2.0	0.7	NA	NA	4.4
RoCE (%)	78.9	107.1	1.6	1.4	11.0
RoE (%)	59.8	82.0	1.6	0.5	7.9

Source: Company, ICICI Direct Research

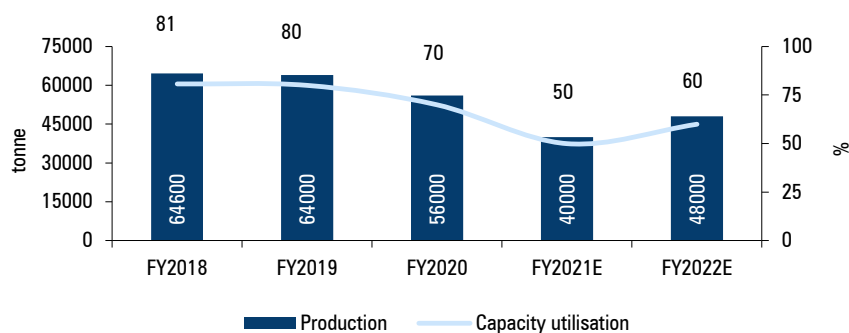
Exhibit 1: Variance Analysis

	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)	Comments
Total Operating Income	233.3	816.5	(71.4)	374.4	(37.7)	
Other Income	46.0	39.2	17.5	42.3	8.8	
Raw Material Expense	152.7	302.6	(49.6)	763.4	(80.0)	
Employee Expense	13.8	28.5	(51.7)	(3.8)	(462.4)	
Power & Fuel Expense	27.9	48.6	(42.5)	34.6	(19.4)	
Other Expenses	50.3	89.1	(43.5)	77.6	(35.2)	
Total Operating Expenses	244.6	468.7	(47.8)	871.8	(71.9)	
EBITDA	(11.3)	347.8	(103.3)	(497.4)	(97.7)	
EBITDA Margin (%)	(4.8)	42.6	-4744 bps	(132.9)	12800 bps	
Depreciation	17.8	17.7	0.3	18.9	(6.0)	
Interest	6.0	9.3	(35.5)	8.6	(30.6)	
Exceptional Items	-	-	-	-	-	
PBT	11.0	360.0	(96.9)	(482.6)	(102.3)	
Tax Outgo	0.2	125.6	(99.8)	(116.6)	(100.2)	
PAT	10.8	234.4	(95.4)	(366.0)	(102.9)	
Key Metrics						
Capacity Utilisation (%)	50	85		50		

Source: Company, ICICI Direct Research

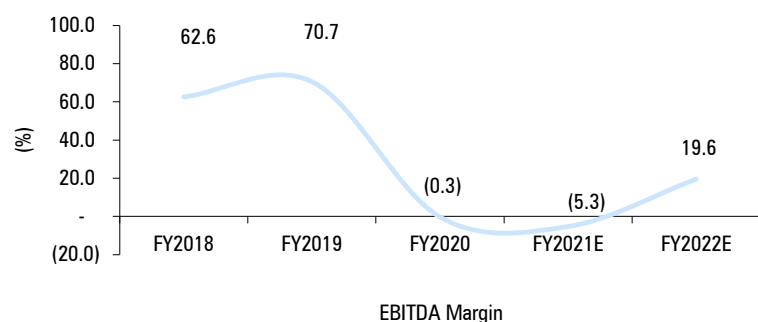
Financial story in charts

Exhibit 2: Trend in production and capacity utilisation level



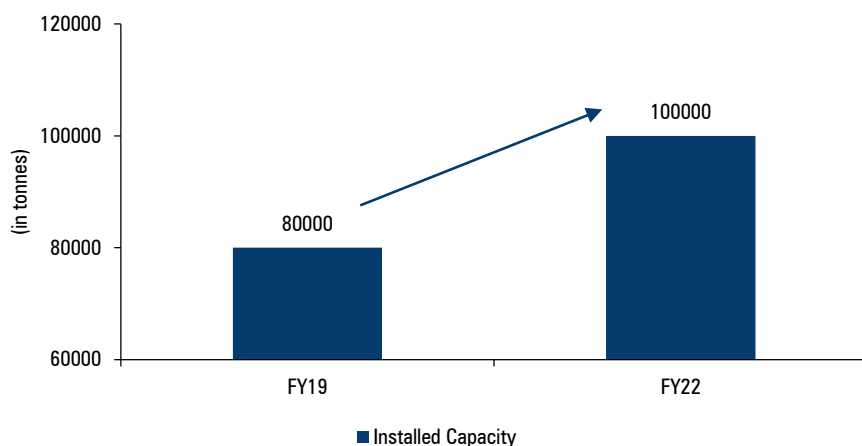
Source: Company, ICICI Direct Research

Exhibit 3: Trend in EBITDA margins



Source: Company, ICICI Direct Research

Exhibit 4: Capacity expansion plan chalked out



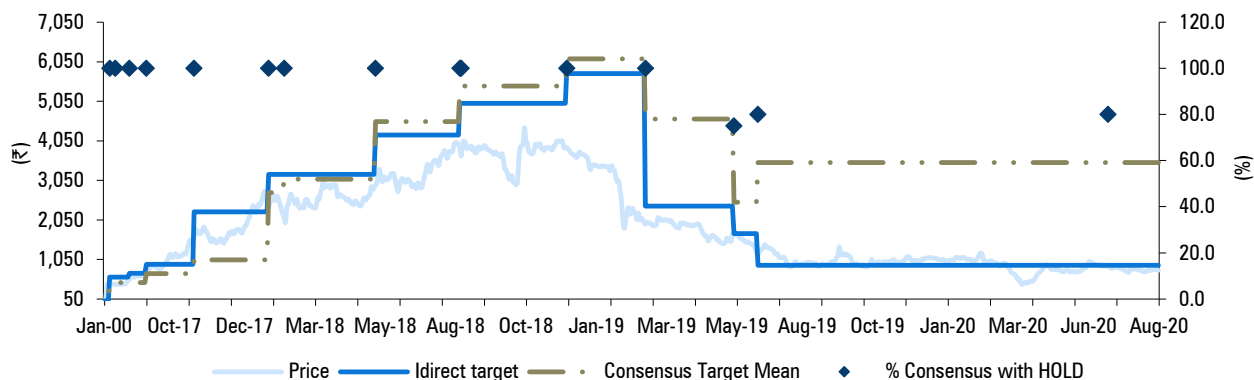
Source: Company, ICICI Direct Research

Exhibit 5: Valuation

	Sales (₹ Crore)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBIDTA (x)	P/ BV (x)	RoE (%)	RoCE (%)
FY17	860	4	-13	-231	NA	46.8	3.6	-5.7	0.9
FY18	2750	220	271	LP	2.9	2.0	1.7	59.8	78.9
FY19	6593	140	790	192	1.0	0.7	0.8	82.0	107.1
FY20	2149	-67	14	-98	56.1	NA	0.9	1.6	1.6
FY21E	1223	-43	4	-71	192.7	NA	0.9	0.5	1.4
FY22E	1448	18	74	1731	10.5	4.4	0.8	7.9	11.0

Source: Company, ICICI Direct Research

Exhibit 6: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 7: Top 10 Shareholders

Rank	Name	Latest Filing	% O/S	Position (m)	Change (m)
1	NORBURY INVESTMENTS	30-06-2020	13.9	5.4	0.0
2	MICROLIGHT INVESTMEN	30-06-2020	12.1	4.7	0.0
3	BHARAT INVESTMENTS G	30-06-2020	6.4	2.5	0.0
4	LIFE INSURANCE CORP	30-06-2020	6.3	2.4	0.0
5	MEKIMA CORPORATION	30-06-2020	4.5	1.7	0.0
6	PURVI VANIJYA NIYOJA	30-06-2020	4.3	1.6	0.0
7	RAGHAV COMMERCIAL LT	30-06-2020	3.8	1.4	0.0
8	LNJ FINANCIAL SERVIC	30-06-2020	3.5	1.3	0.0
9	SHASHI COMMERCIAL LT	30-06-2020	1.8	0.7	0.0
10	STICHTING DEPOST APG	30-06-2020	1.7	0.6	0.1

Source: Reuters, ICICI Direct Research

Exhibit 8: Shareholding Pattern

(in %)	Dec-19	Mar-20	Jun-20
Promoter	59.6	59.6	59.6
Public	40.4	40.4	40.4
Total	100.0	100.0	100.0

Source: Company, ICICI Direct Research

Financial summary

Exhibit 9: Profit and loss statement (₹ crore)				
(Year-end March)	FY19	FY20	FY21E	FY22E
Total Operating Income	6,593	2,149	1,223	1,448
Growth (%)	140	-67	-43	18
Raw Material Expenses	1,114.8	1,621.1	1,010.0	799.5
Employee Expenses	197.6	65.6	45.9	50.7
Other expenses	622.2	468.2	231.7	314.3
Total Operating Expenditure	1,935	2,155	1,288	1,164
EBITDA	4,658	-6	-65	284
Growth (%)	171	-100	LP	-540
Depreciation	72	72	75	78
Interest	18	37	30	22
Other Income	109	144	191	196
PBT	4,677	29	21	380
Exceptional Item	0	0	0	0
Total Tax	1,627	-24	5	96
Reported PAT	3,050	53	16	285
Adjusted PAT	3,050	53	16	285
Growth (%)	182	-98	-71	NA
EPS (₹)	790	14	4	74

Source: Company, ICICI Direct Research

Exhibit 10: Cash flow statement (₹ crore)				
(Year-end March)	FY19	FY20	FY21E	FY22E
Profit/(Loss) after taxation	3050	53	16	285
Add: Depreciation & Amortization	72	72	75	78
Net Increase in Current Assets	-1194	927	779	53
Net Increase in Current Liabilities	148	-327	-7	32
CF from operating activities	2076	726	864	447
(Inc)/dec in Investments	-718	-290	0	0
(Inc)/dec in Fixed Assets	-44	-111	-200	-200
Others	0	0	0	0
CF from investing activities	-762	-400	-200	-200
Inc / (Dec) in Equity Capital	-1	0	0	0
Inc / (Dec) in Loan	369	-74	-450	-100
Dividend & Dividend Tax	-1139	-113	-6	-117
Others	7	-260	-14	-14
CF from financing activities	-764	-447	-471	-231
Net Cash flow	550	-121	193	16
Opening Cash	8	558	437	630
Closing Cash	558	437	630	646

Source: Company, ICICI Direct Research

Exhibit 11: Balance sheet (₹ crore)				
(Year-end March)	FY19	FY20	FY21E	FY22E
Liabilities				
Equity Capital	39	39	39	39
Reserve and Surplus	3680	3384	3393	3562
Total Shareholders funds	3719	3423	3432	3600
Total Debt	666	593	143	43
Deferred Tax Liability	126	102	90	77
Non Current Liabilities	6	7	5	3
Total Liabilities	4518	4124	3669	3723
Assets				
Gross Block	1721	1749	1799	1849
Less: Acc Depreciation	932	1005	1080	1157
Net Block	788	745	719	692
Capital WIP	19	101	251	401
Total Fixed Assets	807	845	970	1092
Investments	867	1157	1157	1157
Inventory	1308	1005	617	606
Debtors	1187	399	241	238
Loans and Advances	68	306	105	98
Other Current Assets	274	200	168	136
Cash	558	437	630	646
Total Current Assets	3396	2348	1761	1724
Creditors	380	134	97	99
Other Current Liabilities (incl Provisions)	172	91	121	151
Current Liabilities & Prov	552	225	218	250
Net Current Assets	2844	2122	1543	1474
Others	0	0	0	0
Application of Funds	4518	4124	3669	3723

Source: Company, ICICI Direct Research

Exhibit 12: Key ratios				
(Year-end March)	FY19	FY20	FY21E	FY22E
Per share data (₹)				
EPS	790	14	4	74
BV	963	887	889	933
DPS	80	25	1	26
Cash Per Share	145	113	163	167
Operating Ratios (%)				
EBITDA margins	70.7	-0.3	-5.3	19.6
PBT margins	70.9	1.4	1.7	26.3
Net Profit margins	46.3	2.5	1.3	19.7
Inventory days	247	170	175	190
Debtor days	66	68	72	60
Creditor days	124	30	35	45
Return Ratios (%)				
RoE	82.0	1.6	0.5	7.9
RoCE	107.1	1.6	1.4	11.0
RoIC	119.8	-2.2	-4.8	6.9
Valuation Ratios (x)				
P/E	1.0	56.1	192.7	10.5
EV / EBITDA	0.7	NA	NA	4.4
EV / Revenues	0.5	1.5	2.1	1.7
Market Cap / Revenues	0.5	1.4	2.4	2.1
Price to Book Value	0.8	0.9	0.9	0.8
Solvency Ratios				
Debt / Equity	0.2	0.2	0.0	0.0
Debt/EBITDA	0.1	NA	NA	0.2
Current Ratio	6.2	10.4	8.1	6.9
Quick Ratio	3.8	6.0	5.2	4.5

Source: Company, ICICI Direct Research

Exhibit 13: ICICI Direct coverage universe (Metals and Mining)

	CMP	TP	M Cap	EPS (₹)			P/E (x)			EV/EBITDA (x)			ROCE(%)			ROE(%)		
	(₹)	(₹) Rating		(₹ Cr)	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E
Coal India	136	150 Hold	84390	27.1	22.2	22.9	5.0	6.1	5.9	2.8	4.4	4.5	55.5	40.2	40.1	51.9	39.0	36.9
Hindalco	193	225 Buy	43432	18.2	16.4	29.2	10.6	11.7	6.6	5.6	7.6	5.5	7.8	6.0	8.4	6.9	6.0	9.7
Hind Zinc	230	195 Hold	97161	16.1	12.4	18.8	11.8	15.3	10.1	6.6	8.2	4.8	20.8	20.0	26.0	16.9	14.5	19.0
JSW Steel	270	210 Hold	65156	19.5	3.3	22.2	10.5	61.3	9.2	8.9	11.7	6.5	7.2	4.5	10.6	12.7	2.1	12.5
NMDC	95	90 Hold	28981	11.8	9.4	10.8	8.0	10.1	8.8	4.2	6.3	4.7	20.3	11.6	12.9	13.1	9.1	9.9
Ratnamani	1125	1320 Buy	5252	65.8	49.5	66.0	17.1	22.7	17.0	12.5	16.0	11.4	22.2	14.8	19.8	18.0	12.3	14.4
Graphite Ind.	179	200 Hold	3473	2.0	1.0	21.0	80.8	231.3	8.7	NA	NA	3.2	-2.6	-5.4	6.0	1.0	0.3	8.7
Tata Steel	425	450 Hold	51177	41.4	-20.3	56.7	10.1	NA	7.4	9.1	12.6	5.7	5.0	2.0	8.9	6.4	-3.2	8.0
HEG	776	750 Hold	3004	14.0	4.0	74.0	56.1	192.7	10.5	NA	NA	4.4	1.6	1.4	11.0	1.6	0.5	7.9

Source: Company, ICICI Direct Research

RATING RATIONALE

ICICI Direct endeavors to provide objective opinions and recommendations. ICICI Direct assigns ratings to its stocks according to their notional target price vs. current market price and then categorizes them as Buy, Hold, Reduce and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock

Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

**ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com**

ANALYST CERTIFICATION

I/We, Dewang Sanghavi MBA (Finance) Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. It is also confirmed that above mentioned Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months and do not serve as an officer, director or employee of the companies mentioned in the report.

Terms & conditions and other disclosures:

ICICI Securities Limited (ICICI Securities) is a full-service, integrated investment banking and is, inter alia, engaged in the business of stock brokering and distribution of financial products. ICICI Securities Limited is a SEBI registered Research Analyst with SEBI Registration Number – INH000000990. ICICI Securities Limited SEBI Registration is INZ000183631 for stock broker. ICICI Securities is a subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on www.icicibank.com

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities generally prohibits its analysts, persons reporting to analysts and their relatives from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

Recommendation in reports based on technical and derivative analysis centre on studying charts of a stock's price movement, outstanding positions, trading volume etc as opposed to focusing on a company's fundamentals and, as such, may not match with the recommendation in fundamental reports. Investors may visit icicidirect.com to view the Fundamental and Technical Research Reports.

Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

ICICI Securities Limited has two independent equity research groups: Institutional Research and Retail Research. This report has been prepared by the Retail Research. The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, target price of the Institutional Research.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its associates or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts and their relatives have any material conflict of interest at the time of publication of this report.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts or their relatives do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities are engaged in various financial service businesses, they might have financial interests or beneficial ownership in various companies including the subject company/companies mentioned in this report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor ICICI Securities have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on ICICI Securities by any Regulatory Authority impacting Equity Research Analysis activities.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ICICI Securities and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.