

Better times ahead...

For Q4FY21, HEG's standalone topline came in at ₹ 380 crore, up 2% YoY, 19% QoQ. However, at the EBITDA level, the company reported a loss of ₹ 5 crore. Other income for the quarter was at ₹ 25 crore. Ensuing net loss for the quarter was at ₹ 7 crore. The Q4FY21 performance was impacted by a sharp rise in other expenses. Other expenses for Q4FY21 were at ₹ 120 crore compared to ₹ 71 crore in Q3FY21 and ₹ 78 crore in Q4FY20. During Q4FY21, other expenses as a percentage of sales were at 32% in Q4FY21 compared to 21% in Q4FY20 and 22% in Q3FY21. During the quarter, other expenses included ₹ 35 crore spent on CSR activities, which led to higher total other expense. However, adjusting for CSR expense, HEG's adjusted EBITDA would have been ~₹ 30 crore.

Global steel production uptrend augurs well for graphite electrode demand...

Over the last few months, there has been a healthy uptick in global steel prices as well as global steel production levels. Graphite electrode players are likely to be one of the key beneficiaries of the current upcycle in steel. During the first four months of CY21, global crude steel production witnessed healthy growth, auguring well for graphite electrode majors. During January-April 2021, global steel production was at 663 million tonnes (MT), up 13.7% YoY. In addition to higher global steel output, steel prices witnessed healthy strength. Both above-mentioned factors, higher global steel output and strength in global steel prices, have put graphite electrode players such as HEG in a sweet spot.

Graphite electrode prices start moving northwards...

The uptick in steel production has augured well for graphite electrode demand. Going forward also, the growth trend in global steel production is likely to continue with a healthy demand recovery in major steel consuming industries. Furthermore, the domestic steel industry is also poised to grow with increased government spending on infrastructure. The combination of these factors is expected to drive demand for graphite electrodes and also have a positive rub-off effect on graphite electrode prices. Graphite electrode prices have already started to move northwards, auguring well for graphite electrode companies.

Valuation & Outlook

HEG's capacity utilisation has sequentially improved from ~45% in Q1FY21 to ~85% in Q4FY21. Going forward, we assume capacity utilisation of 80% for FY22E and 82.5% for FY23E. We value the stock at 6.5x FY23E EV/EBITDA and arrive at a target price of ₹ 2800. On the back of an improved industry outlook, we upgrade the stock from HOLD to **BUY**.

Key Financial Summary

(₹ Crore)	FY18	FY19	FY20	FY21	FY22E	FY23E
Net Sales	2,750	6,593	2,149	1,256	2,886	3,581
EBITDA	1,722	4,658	-6	-59	1,054	1,532
EBITDA Margin (%)	62.6	70.7	(0.3)	(4.7)	36.5	42.8
Adj PAT	1,081	3,050	53	-25	831	1,236
EPS (₹)	270.6	790.2	13.8	(6.5)	215.3	320.2
EV/EBITDA (x)	5.7	2.0	NA	NA	8.2	5.4
RoCE (%)	78.9	107.1	1.6	(0.5)	27.1	34.3
RoE (%)	59.8	82.0	1.6	(0.7)	21.1	26.1

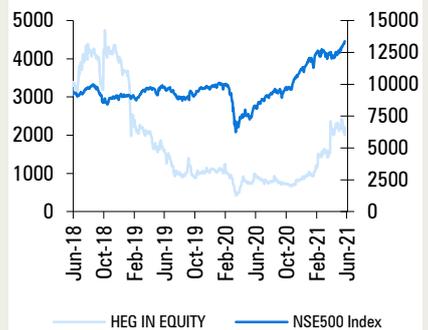
Source: Company, ICICI Direct Research



Particulars

Particulars	Amount
Market Capitalisation	₹9145 crore
Debt in ₹ crore (FY21)	297
Cash & Cash Eq.(FY21)	1,521
EV	₹ 7921 crore
52 Week H / L (₹)	2564 / 659
Equity Capital (₹)	38.6 crore
Face Value	₹ 10

Price Performance



Key risks to our call

- Lower-than-expected increase in blended graphite electrode realisation
- Higher-than-expected increase in operating cost (especially needle coke)

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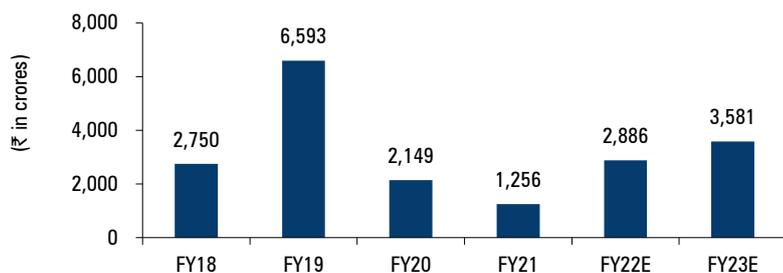
Exhibit 1: Variance Analysis

	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)	Comments
Total Operating Income	380	374	2	320	19	
Other Income	25	42	-41	25	-1	
Raw Material Expense	201	763	-74	204	-2	
Employee Expense	15	-4	-494	13	10	
Power & Fuel Expense	50	35	43	32	56	
Other Expenses	120	78	55	71	69	During Q4FY21, other expenses as a percentage of sales were at 32% in Q4FY21 compared to 21% in Q4FY20 and 22% in Q3FY21. During the quarter, other expenses included ₹ 35 crore spent on CSR activities, which led to higher total other expense
Total Operating Expenses	385	872	-55.8	321	20.0	
EBITDA	(5)	(497)	-99.1	(1)	269.3	
EBITDA Margin (%)	(1.2)	(132.8)	13161 bps	(0.4)	-84 bps	
Depreciation	18	19	-2	19	0	
Interest	1	9	-87	1	-14	
Exceptional Items	-	-	-	-	-	
PBT	1	-483	NA	4	-80	
Tax Outgo	8	(117)	-	(0)	-	
PAT	(7)	(366)	NA	5	PL	
Key Metrics						
Capacity Utilisation (%)	50	85		50		

Source: Company, ICICI Direct Research

Financial story in charts

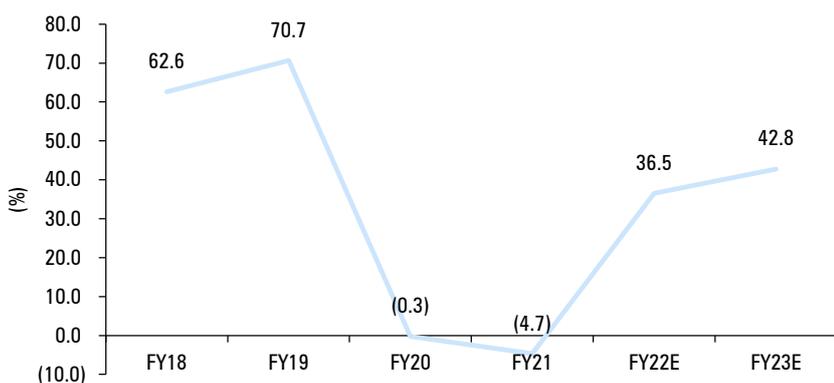
Exhibit 3: Trend in topline



We expect topline of ₹ 2886 crore of FY22E and ₹ 3581 crore for FY23E

Source: Company, ICICI Direct Research

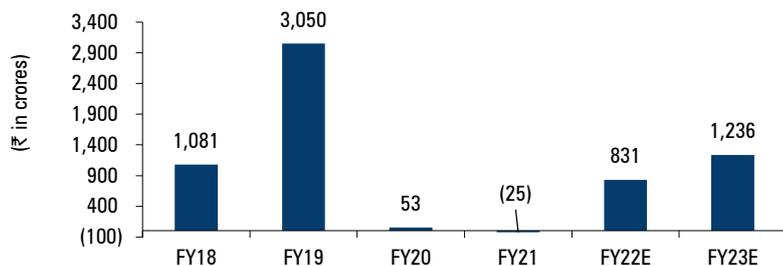
Exhibit 4: Trend in EBITDA margins



We expect EBITDA margin of 36.5% for FY22E and 42.8% for FY23E

Source: Company, ICICI Direct Research

Exhibit 5: Trend in PAT



We expect PAT of ₹ 831 crore for FY22E and ₹ 1236 crore for FY23E

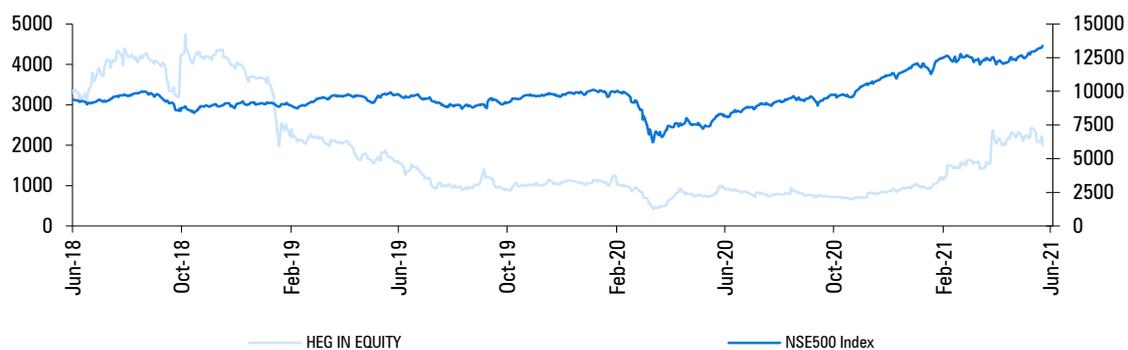
Source: Company, ICICI Direct Research

Exhibit 6: Valuation Matrix

	Sales (₹ Crore)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	P/ BV (x)	RoE (%)	RoCE (%)
FY18	2750	220	271	LP	8.8	5.7	5.3	59.8	78.9
FY19	6593	140	790	192	3.0	2.0	2.5	82.0	107.1
FY20	2149	-67	14	-98	172.2	NA	2.7	1.6	1.6
FY21	1256	-42	-7	-147	NA	NA	2.7	-0.7	-0.5
FY22E	2886	130	215	LP	11.1	8.2	2.3	21.1	27.1
FY23E	3581	24	320	49	7.4	5.4	1.9	26.1	34.3

Source: Company, ICICI Direct Research

Exhibit 7: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 8: Shareholding Pattern

(in %)	Sep-20	Dec-20	Mar-21
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 (Standalone)

Exhibit 9: Profit and loss statement				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
Total Operating Income	2,149	1,256	2,886	3,581
Growth (%)	-67	-42	130	24
Total Operating Expenditure	2155	1315	1832	2049
EBITDA	-6	-59	1,054	1,532
Growth (%)	PL	PL	LP	45
Depreciation	72	73	76	100
Interest	37	11	11	9
Other Income	144	113	144	229
PBT	29	-31	1,111	1,652
Exceptional Item	0	0	0	0
Total Tax	-24	-5	280	416
Reported PAT	53	-25	831	1,236
Adjusted PAT	53	-25	831	1,236
Growth (%)	-98	PL	LP	49
EPS (₹)	14	-7	215	320

Source: Company, ICICI Direct Research

Exhibit 11: Balance sheet				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
Liabilities				
Equity Capital	39	39	39	39
Reserve and Surplus	3384	3360	3900	4704
Total Shareholders funds	3423	3399	3939	4742
Total Debt	593	297	197	97
Deferred Tax Liability	102	97	97	97
Non Current Liabilities	7	8	8	8
Total Liabilities	4124	3799	4240	4943
Assets				
Net Block	745	694	667	1618
Capital WIP	101	373	973	48
Total Fixed Assets	845	1067	1641	1666
Investments	1157	1262	1262	1262
Inventory	1005	581	753	982
Debtors	399	289	474	736
Loans and Advances	306	305	298	335
Other Current Assets	200	94	62	77
Cash	437	551	189	387
Total Current Assets	2348	1819	1776	2517
Creditors	134	257	317	350
Other Current Liabilities (incl Provis)	91	91	121	151
Current Liabilities & Prov	225	348	438	502
Net Current Assets	2122	1471	1337	2015
Others	0	0	0	0
Application of Funds	4124	3799	4240	4943

Source: Company, ICICI Direct Research

Exhibit 10: Cash flow statement				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
Profit/(Loss) after taxation	53	-25	831	1236
Add: Depreciation & Amortization	72	73	76	100
Net Increase in Current Assets	927	642	-319	-543
Net Increase in Current Liabilities	-327	26	90	63
CF from operating activities	726	716	679	856
(Inc)/dec in Investments	-290	-105	0	0
(Inc)/dec in Fixed Assets	-111	-295	-650	-125
Others	0	0	0	0
CF from investing activities	-400	-400	-650	-125
Inc / (Dec) in Equity Capital	0	0	0	0
Inc / (Dec) in Loan	-74	-296	-100	-100
Dividend & Dividend Tax	-113	-12	-291	-433
Others	-260	105	0	0
CF from financing activities	-447	-203	-391	-533
Net Cash flow	-121	114	-362	199
Opening Cash	558	437	551	189
Closing Cash	437	551	189	387

Source: Company, ICICI Direct Research

Exhibit 12: Key ratios				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
Per share data (₹)				
EPS	14	-7	215	320
BV	887	880	1,020	1,229
DPS	25	3	75	112
Cash Per Share	113	143	49	100
Operating Ratios (%)				
EBITDA margins	-0.3	-4.7	36.5	42.8
PBT margins	1.4	-2.4	38.5	46.1
Net Profit margins	2.5	-2.0	28.8	34.5
Inventory days	170	161	150	175
Debtor days	68	84	60	75
Creditor days	30	116	100	100
Return Ratios (%)				
RoE	1.6	-0.7	21.1	26.1
RoCE	1.6	-0.5	27.1	34.3
RoIC	-2.2	-4.2	28.9	36.8
Valuation Ratios (x)				
P/E	172.2	NA	11.1	7.4
EV / EBITDA	NA	NA	8.2	5.4
EV / Revenues	4.3	7.1	3.2	2.5
Market Cap / Revenues	4.3	7.3	3.2	2.6
Price to Book Value	2.7	2.7	2.3	1.9
Solvency Ratios				
Debt / Equity	0.2	0.1	0.0	0.0
Debt/EBITDA	NA	NA	0.2	0.1
Current Ratio	10.4	5.2	4.1	5.0
Quick Ratio	6.0	3.6	2.3	3.1

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)	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E
Coal India	156	140	Hold	92904	20.3	21.0	22.7	6.5	6.3	5.9	3.7	4.1	4.3	39.6	35.6	33.0	33.6	30.3	28.2
Hindalco	395	475	Buy	89775	25.5	42.6	45.7	15.6	9.3	8.7	7.8	6.1	5.4	8.8	11.7	12.0	8.5	13.4	12.7
Hind Zinc	340	340	Hold	140332	18.7	23.6	27.2	15.0	12.0	10.4	9.2	7.0	5.8	27.3	30.4	30.1	25.1	27.5	26.9
JSW Steel	715	800	Buy	172082	32.9	76.0	70.2	20.6	8.9	9.7	10.7	6.5	6.7	13.8	21.4	17.6	17.0	28.3	20.8
NMDC	182	125	Hold	54319	17.1	11.9	3.7	6.6	9.5	8.2	4.7	5.6	5.0	21.4	13.2	14.0	16.7	10.9	11.9
Ratnamani	2037	2400	Buy	9159	59.0	76.2	96.0	33.9	26.2	20.8	22.1	16.1	13.0	15.7	19.3	20.1	13.9	15.7	16.9
Graphite Ind.	779	825	Buy	14949	3.0	55.0	84.0	224.0	12.6	8.2	NA	9.1	4.6	-5.4	19.0	25.2	1.3	19.3	23.4
Tata Steel	1128	1500	Buy	134858	77.1	189.3	152.9	14.8	6.0	7.5	7.2	4.2	4.5	13.1	23.2	18.4	12.4	23.6	15.7
Sail	123	130	Buy	50665	9.0	15.0	17.0	10.7	6.6	6.0	6.0	5.2	4.6	11.2	12.2	12.3	9.3	12.7	12.5
Jindal Stainless	93	125	Buy	4604	8.6	9.4	10.2	11.0	10.1	9.3	5.4	5.4	5.5	16.0	14.2	12.7	13.0	12.5	11.9
Jindal Stainless Hisar	175	244	Buy	4165	29.0	27.0	32.0	6.3	6.8	5.7	5.2	5.1	4.1	18.6	15.8	16.9	23.2	17.4	16.8
Vedanta	278	300	Hold	102353	33.0	37.9	41.0	8.4	7.4	6.8	5.3	4.0	3.5	17.3	22.5	23.6	19.7	19.9	18.9
HEG	2380	2800	Buy	9145	-7.0	215.0	320.0	NA	11.1	7.4	NA	8.2	5.4	-0.5	27.1	34.3	-0.7	21.1	26.1

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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