Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Dalmia Bharat Ltd

Mixed Q1; On a steady growth path

Cement	Sharekhan code: DALMIABHA	Result 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. 2,147**	
Price Target: **Rs. 2,410**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 40,173 cr
52-week high/low:	Rs. 2,374/652
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	13.1
DII	5.8
Others	25.1

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	14.7	39.7	85.7	199.4
Relative to Sensex	14.9	34.4	72.4	161.6

Sharekhan Research, Bloomberg

Summary

- In Q1FY2022, revenues and net profit were lower than expected while operational profitability in terms of EBITDA/tonne largely remained in-line.
- Dalmia announced a capital allocation plan over the next decade addressing medium and longer-term growth plans. Cement capacity to grow at 14-15% CAGR maintaining Net debt/EBITDA below 2x.
- Transparency, corporate governance, treasury allocation, non-core asset divestments, green fuel, shareholder returns are key outcomes of the plan.
- We maintain a Buy on stock with a revised PT of Rs. 2,410, as we see further upside considering its strong earnings growth outlook over FY2021-FY2024E.

Dalmia Bharat (Dalmia) reported lower-than-expected revenues and net profit for Q1FY2022 while operational profitability in terms of EBITDA/tonne largely remained in-line. Consolidated net revenues rose 36% y-o-y to Rs. 2,589 crore led by volume growth (up 33.6% y-o-y to 4.9 million tonnes, marginally lagging our estimates) while realisations were lower than estimate at Rs. 5294/tonne (up 1.9% y-o-y, up 8% q-o-q). The company had lost some market share during April and May 2021 due to stoppage of the Cuttack grinding unit amid the pandemic for a few days. The company has started regaining market share now. The company's EBITDA/tonne stood at Rs. 1,431 (down 14.8% y-o-y, up 20.4% q-o-q) which was marginally higher than our estimate of Rs. 1407. The EBITDA/tonne was aided by higher inventories in Q1FY2022 (leading to overall reduced cost of goods sold). The power & fuel costs (Rs. 1057/tonne, up 54.2% y-o-y, up 20.8% q-o-q), freight costs (Rs. 1057/tonne, +11.5% y-o-y, +1.3% q-o-q) and other costs (Rs. 812/tonne, up 37.6% y-o-y, up 7.5% q-o-q) largely remained on expected line. The OPM contracted by 531bps y-o-y (+278 bps q-o-q) to 27% leading to 14% y-o-y rise in operating profit at Rs. 700 crore (in-line with estimate). The company reported a Rs. 39 crore loss from discontinued operations (refractory business) in Q1FY2022 which led to standalone adjusted net profit of Rs. 223 crore (10% lower than our estimate). 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 happens). 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 tonne) over next three years initially expanding in Southern and North East regions. The company would be incurring around Rs. 5500 crore capex to reach 23.4-million tonne clinker and 48.5-million tonne cement capacities by FY2025 which comprises Rs. 1200-1300 crore towards clinker expansion, Rs. 3000 crore for cement and Rs. 1250-1300 crore towards ongoing capacity expansion. Further, it will increase cement capacity to 60-million tonne by FY2025 which would comprise expansion in Northern and Central regions, the detailed plan would be outlined over the next 9-10 months. 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+). We believe Dalmia has chalked out more predictable and sustainable growth path going ahead which is expected to crystalise further with details related to expansion in non-regional markets. In the interim, it is expected to benefit from the strong demand and pricing environment in Eastern and Southern India. We have marginally revised our estimates downwards for FY2022-FY2023 factoring lower OPM. We introduce FY2024E earnings in this note.

Key positives

- Capital allocation plan outlined towards more predictable and sustainable growth over a decade.
- Focus on transparency, corporate governance, treasury allocation are salient positive measures.
- EBITDA/tonne remained in-line aided by lower cost of goods sold.

Key negatives

- Loss of market share due to stoppage of grinding unit at Cuttack for few days.
- Expansion in non-regional markets to be beyond FY2025.

Our Call

Valuation – Maintain Buy with a revised PT of Rs. 2,410: Dalmia Bharat has addressed its medium and long term growth plans through its decadal capital allocation plan which would ensure more predictable, sustainable and profitable growth path going ahead. The plan also addresses key issues such as transparency, corporate governance, treasury allocation and divestment of non-core assets which are key positive takeaways. The company would be focusing on achieving 14-15% RoCE over next few years and maintain balance sheet quality. We have marginally lowered our estimates for FY2022-FY2023 factoring lower OPM. We introduce FY2024E earnings in this note. Dalmia is currently trading at an EV/EBITDA of 13x/11x 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 a revised price target of Rs. 2,410.

Key risk

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	22.0	20.9	21.0
Adjusted PAT	992	889	968	1,244
% y-o-y growth	*270.1*	*-10.4*	*8.8*	*28.6*
Adjusted EPS (Rs.)	53.6	48.1	52.3	67.3
P/E (x)	40.0	44.7	41.1	31.9
P/B (x)	3.1	3.0	2.8	2.6
EV/EBIDTA (x)	14.3	14.8	13.3	11.2
RoNW (%)	8.6%	6.8%	7.0%	8.3%
RoCE (%)	9.3%	6.6%	6.8%	7.8%

Source: Company; Sharekhan estimates

Revenues and net profit below estimate while operational profitability in-tact: Dalmia Bharat (Dalmia) reported lower-than-expected revenues and net profit for Q1FY2022 while operational profitability in terms of EBITDA/tonne largely remained in-line. Consolidated net revenues rose 36% y-o-y to Rs. 2,589 crore led by volume growth (up 33.6% y-o-y to 4.9 million tonnes, marginally lagging our estimates) while realisations were lower than estimate at Rs. 5294/tonne (up 1.9% y-o-y, up 8% q-o-q). The company had lost some market share during April and May 2021 due to stoppage of the Cuttack grinding unit amid the pandemic for a few days. The company has started regaining market share now. The company's EBITDA/tonne stood at Rs. 1,431 (down 14.8% y-o-y, up 20.4% q-o-q) which was marginally higher than our estimate of Rs. 1407. The EBITDA/tonne was aided by higher inventories in Q1FY2022 (leading to overall reduced cost of goods sold). The power & fuel costs (Rs. 1057/tonne, up 54.2% y-o-y, up 20.8% q-o-q), freight costs (Rs. 1057/tonne, +11.5% y-o-y, +1.3% q-o-q) and other costs (Rs. 812/tonne, up 37.6% y-o-y, up 7.5% q-o-q) largely remained on expected line. The OPM contracted by 531bps y-o-y (+278 bps q-o-q) to 27% leading to 14% y-o-y rise in operating profit at Rs. 700 crore (in-line with estimate). The company reported a Rs. 39 crore loss from discontinued operations (refractory business) in Q1FY2022 which led to standalone adjusted net profit of Rs. 223 crore (10% lower than our estimate).

Capital allocation plan over the coming decade: 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 happens). 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 tonne) over next three years initially expanding in Southern and North East regions. The company would be incurring around Rs. 5500 crore capex to reach 23.4-million tonne clinker and 48.5-million tonne cement capacities by FY2025 which comprises Rs. 1200-1300 crore towards clinker expansion, Rs. 3000 crore for cement and Rs. 1250-1300 crore towards ongoing capacity expansion. Further, it will increase cement capacity to 60-million tonne by FY2025 which would comprise expansion in Northern and Central regions, the detailed plan would be outlined over the next 9-10 months. 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

- **Capacity allocation strategy outlined:** The company outlined its capital allocation strategy for the next decade. The target for the same is 1) To be pan-India pure play cement player 2) to have a significant presence in its regional markets and 3) To reach 110-130-million tonne capacity by 2031 at a 14-15% CAGR. The capital allocation is based on outlining predictable, sustainable and profitable growth in a decade. The company would not exceed net debt/EBITDA ratio of 2x during the capacity expansion phase unless there are exceptional cases such as large acquisitions. The company would focus on transparency and corporate governance standards.
- **Capacity targets:** The company targets to reach 48.5-million tonne capacity over the next three years and 60-million tonne by March 2025. It targets to achieve 14-15% RoCE over next five years. Its clinker and grinding capacities would be increased to 23.4 million tonnes and 48.5 million tonnes respectively. The regional mix of 23.4-million tonne clinker capacity is South – 9.4 million tonnes, East – 8.3 million tonnes, North East – 3.3 million tonnes and Murli Industries – 2.4 million tonnes. The cement capacity expansion of 17.7 million tonnes entails 3-million tonne Greenfield units (1.5 million tonnes each in the South), 1.7-million tonne brownfield expansion at Bokaro and 5.2-million tonne de-bottlenecking across plants. The regional mix of 48.5-million tonne cement capacity would be South – 15.9 million tonnes, East – 23.1 million tonnes, North East – 5.5 million tonnes and Murli Industries – 4 million tonnes.

- **Pan-India aspiration:** The company is initially expanding in Southern and North East regions. It would expand in Central and Northern region, the detail of which will be outlined over the next 9-10 months which will increase its cement capacity to 60 million tonnes by March 2025.
- **Capex:** The company would be incurring a capex of ~Rs. 5500 crore, which comprises Rs. 1200-1300 crores towards clinker expansion, Rs. 3000 crore for cement and Rs. 1250-1300 crore towards ongoing capacity expansion.
- **Shareholders' return:** The company would earmark 10% of operating cash flows towards dividend payouts and share buybacks.
- **Weak Q1 volumes:** The company had lost some market share during April and May 2021 due to stoppage of Cuttack grinding unit due to COVID-19 for a few days. The company has started regaining market share now. It remains preferred brand in the Eastern region and has no issues regarding quality.
- **Green and Innovation fund:** It would allocate 10% of OCFs towards green and innovation fund which would be utilised in investing augmenting renewable capacity. It would utilise Rs. 1000-1200 crore towards expanding WHRS, solar power and green fuel capacities. The green fuel mix is slated to increase from 9.1% in Q1FY2022 to 20% by FY2022-end.
- **Divestment of non-core assets:** The company would divest its building materials business in 3-4 months. It had invested Rs. 99 crore in the business as on June 31, 2021 and would be investing additional Rs. 40 crore till date of divestment. The company is also in process of divesting refractory business which is pending approval from NCLT. It has divested 4.5% stake in IEX in Q1FY2022.
- **Treasury allocation:** The company would be investing 85% of its treasury corpus in AAA+ instruments and balance 15% in AA+ instruments.

Results (Consolidated) Rs cr

Particulars	Q1FY22	Q1FY21	y-o-y	Q4FY21	q-o-q
Net Sales	**2589**	**1901**	**36%**	**3146**	**-18%**
Total Expenditure	1889	1286	47%	2383	-21%
Operating profits	**700**	**615**	**14%**	**763**	**-8%**
Other Income	26	55	-53%	40	-35%
EBIDTA	726	670	8%	803	-10%
Interest	60	74	-19%	61	-2%
PBDT	666	596	12%	742	-10%
Depreciation	298	298	0%	327	-9%
PBT	**368**	**298**	**23%**	**415**	**-11%**
Tax	95	108	-12%	-213	-145%
Extraordinary items	-4	-1	-	-231	
Minority Interest	11	-2		13	
Reported Profit After Tax	227	190	19%	627	-64%
Adjusted PAT	**223**	**189**	**18%**	**396**	**-44%**
EPS	12	10	18%	21	-44%
OPMs	27.0%	32.4%	-531 bps	24.3%	278 bps
PAT	8.6%	9.9%	-133 bps	12.6%	-397 bps
Tax rate	25.8%	36.2%	-1043 bps	-51.3%	-

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.

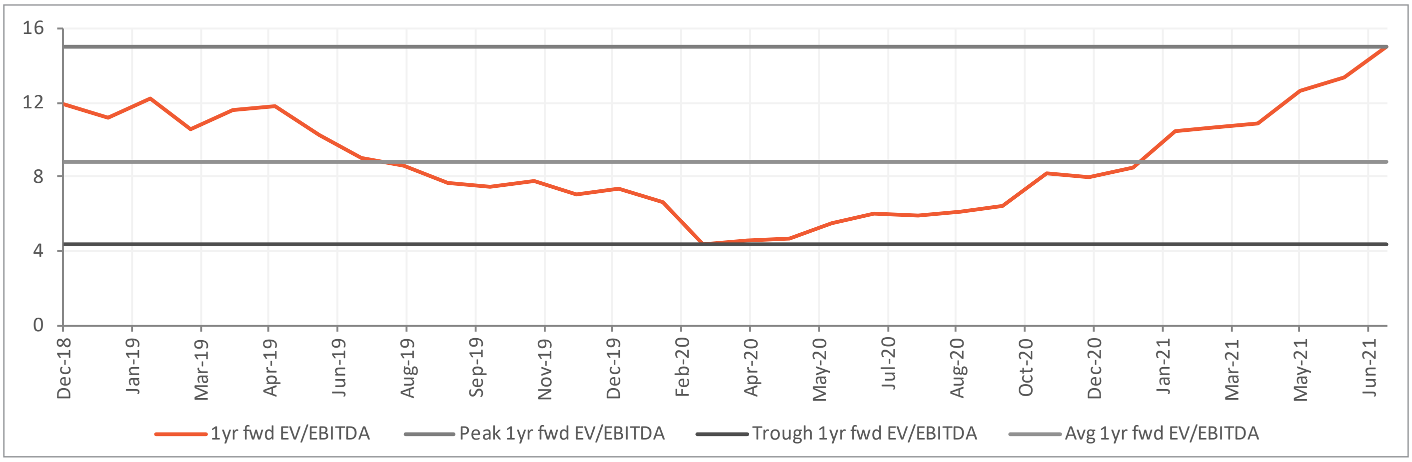
■ Company Outlook – Aggressive expansion plans to capture high growth opportunities

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 a revised PT of Rs. 2,410

Dalmia Bharat has addressed its medium and long term growth plans through its decadal capital allocation plan which would ensure more predictable, sustainable and profitable growth path going ahead. The plan also addresses key issues such as transparency, corporate governance, treasury allocation and divestment of non-core assets which are key positive takeaways. The company would be focusing on achieving 14-15% RoCE over next few years and maintain balance sheet quality. We have marginally lowered our estimates for FY2022-FY2023 factoring lower OPM. We introduce FY2024E earnings in this note. Dalmia is currently trading at an EV/EBITDA of 13x/11x 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 a revised price target of Rs. 2,410.

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 Cement	31.6	27.8	16.2	14.4	4.4	3.8	15.0	14.8
Dalmia Bharat	44.7	41.1	14.8	13.3	3.0	2.8	6.8	7.0
Shree Cement	38.1	33.4	20.0	17.3	5.7	4.9	15.9	15.7
The Ramco Cement	27.6	24.2	17.0	15.1	4.0	3.5	15.6	15.5

Source: Sharekhan Research

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 Website

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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