

Steady operational performance...

About the stock: HEG is one of the leading graphite electrode manufacturers and exporters globally.

- HEG has a graphite electrode manufacturing plant of 80000 tonnes per annum at Mandideep in Madhya Pradesh
- HEG has a captive power generation capacity of ~76.5 MW (two thermal power plants and one hydro power plant)

Q1FY23 Results: HEG reported a steady operational performance in Q1FY23.

- For Q1FY23, standalone operations capacity utilisation was at 92%. For Q1FY23, total operating income was at ₹ 722 crore, up 75% YoY, 7% QoQ
- Reported EBITDA for the quarter was at ₹ 184 crore, up 154% YoY, 17% QoQ. EBITDA margin for the quarter was at 25.5%, up 800 bps YoY, 220 bps QoQ
- Ensuing standalone net profit for the quarter was at ₹ 134 crore, up 139% YoY, 18% QoQ

What should investors do? HEG's share price has given a return of ~66% over the last two years (from ~₹ 798 in August 2020 to ₹ 1325 in August 2022).

- Rising energy costs and inflationary pressure on economic growth due to Russia-Ukraine conflict have adversely impacted demand prospects, particularly in the European Union. Hence, we downgrade the stock from BUY to HOLD

Target Price and Valuation: We value HEG at ₹ 1400, 6x FY24E EV/EBITDA.

Key triggers for future price performance:

- Going forward, demand for graphite electrode and realisation is expected to remain volatile in the near term while cost inflation may continue to add pressure on margins
- HEG's capacity expansion from 80000 tonnes to 100000 tonnes per annum is going on in full swing and is expected to be completed by end December 2022 with commercial production set to start in January-March 2023 quarter (i.e. Q4FY23E)
- Over FY22-24E, we expect topline to grow at 24% CAGR while EBITDA and PAT are expected to register a CAGR of 18.3% and 17.8%, respectively

Alternate Stock Idea: In our metal coverage, we like Jindal Stainless.

- Jindal Stainless (JSL) has a 1.1 million tonnes per annum (MTPA) integrated facility with backward integration
- BUY with a target price of ₹ 135



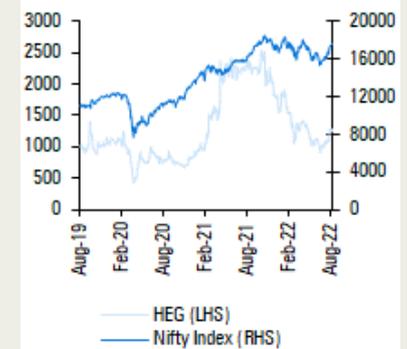
Particulars

Particulars	Amount
Market Cap (In ₹ crore)	5114 crore
Debt in ₹ crore (FY22)	663
Cash & Cash Eq. (FY22)	1,272
EV	₹ 4505 crore
52 Week H / L (₹)	2626 / 891
Equity Capital (₹)	38.6 crore
Face Value	₹ 10

Shareholding pattern

(in %)	Sep-21	Dec-21	Mar-22	Jun-22
Promoter	55.1	55.1	55.1	55.1
FIs	14.3	13.4	8.9	6.8
DIs	7.5	7.5	8.2	8.4
Others	23.1	24.0	27.8	29.7
Total	100.0	100.0	100.0	100.0

Price Chart



Key Risks

- Higher-than-expected increase in graphite electrodes realisation
- Higher -than-expected increase in operating cost

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Key Financial Summary

(₹ Crore)	FY19	FY20	FY21	FY22	CAGR (FY17-22)	FY23E	FY24E	CAGR (FY22-24E)
Net Sales	6,593	2,149	1,256	2,202	21%	2,804	3,376	24%
Reported EBITDA	4,658	-6	-59	527	46%	689	738	18%
Adjusted PAT	3,050	53	-25	391	LP	506	542	18%
Adjusted EPS (₹)	790.2	13.8	(6.5)	101.2		131.0	140.4	
EV/EBITDA (x)	1.1	NA	NA	8.5		6.5	5.8	
RoCE (%)	107.1	1.6	(0.5)	11.9		14.7	14.9	
RoE (%)	82.0	1.6	-0.7	10.3		12.4	12.3	

Source: Company, ICICI Direct Research

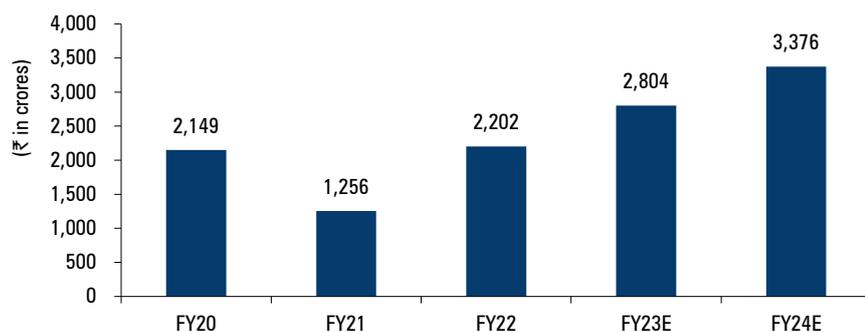
Exhibit 1: Variance Analysis (Standalone Performance)

	Q1FY23	Q1FY22	YoY (%)	Q4FY22	QoQ (%)	Comments
Total Operating Income	722	414	75	673	7	Standalone topline for the quarter was at ₹ 722 crore, up 75%, 7% QoQ
Other Income	21	22	-3	17	23	
Raw Material Expense	283	180	57	244	16	
Employee Expense	23	18	30	20	18	
Power & Fuel Expense	86	56	53	78	10	
Other Expenses	146	87	67	175	-16	
Total Operating Expenses	538	341	58	516	4	
EBITDA	184	72	154	157	17	EBITDA for the quarter increased 154% YoY and 17% QoQ to ₹ 184 crore
EBITDA Margin (%)	25.5	17.5	799 bps	23.3	218 bps	
Depreciation	21	19	12	21	-2	
Interest	4	1	244	1	303	
Exceptional Items	-	-	-	-	-	
PBT	180	75	142	152	19	
Tax Outgo	47	19	149	39	21	
PAT	134	56	139	113	18	PAT for the quarter increased 139% YoY and 18% QoQ to ₹ 134 crore

Source: Company, ICICI Direct Research.

Financial story in charts

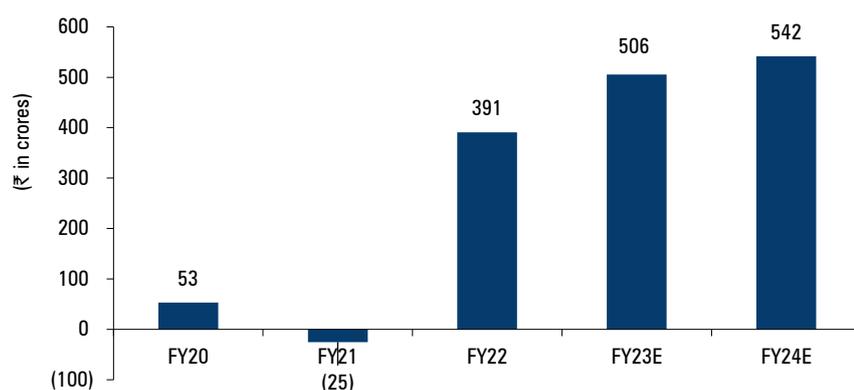
Exhibit 2: Trend in topline (In ₹ crore)



We expect topline to grow at a CAGR of 24% during FY22-24E

Source: Company, ICICI Direct Research

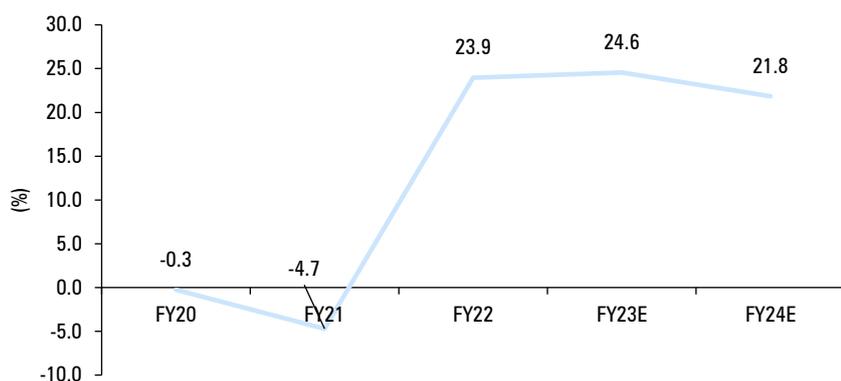
Exhibit 3: Trend in PAT (in ₹ crore)



We expect standalone PAT to grow at a CAGR of 18% during FY22-24E

Source: Company, ICICI Direct Research

Exhibit 4: Trend in EBITDA margin (in %)



We expect HEG to report EBITDA margin of 24.6% for FY23E and 21.8% for FY24E

Source: Company, ICICI Direct Research

Exhibit 5: Valuation Matrix

	Sales (₹ Crore)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBIDTA (x)	P/ BV (x)	RoE (%)	RoCE (%)
FY20	2149	-67	14	-98	95.8	NA	1.5	1.6	1.6
FY21	1256	-42	-7	PL	NA	NA	1.5	-0.7	-0.5
FY22	2202	75	101	LP	13.1	8.5	1.4	10.3	11.9
FY23E	2804	27	131	29	10.1	6.5	1.3	12.4	14.7
FY24E	3376	20	140	7	9.4	5.8	1.2	14.7	17.0

Source: Company, ICICI Direct Research

Financial summary (Standalone)

Exhibit 6: Profit and loss statement		₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E	
Total Operating Income	1,256	2,202	2,804	3,376	
Growth (%)	-42	75	27	20	
Total Operating Expenditure	1315	1674	2116	2639	
EBITDA	-59	527	689	738	
Growth (%)	PL	LP	31	7	
Depreciation	73	79	103	128	
Interest	11	7	7	6	
Other Income	113	80	97	120	
PBT	-31	520	676	724	
Exceptional Item	0	0	0	0	
Total Tax	-5	129	170	182	
Reported PAT	-25	391	506	542	
Adjusted PAT	-25	391	506	542	
Growth (%)	PL	LP	29	7	
EPS (₹)	-7	101	131	140	

Source: Company, ICICI Direct Research

Exhibit 7: Cash flow statement		₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E	
Profit/(Loss) after taxation	-25	391	506	542	
Add: Depreciation & Amortization	73	79	103	128	
Net Increase in Current Assets	642	-807	-190	-218	
Net Increase in Current Liabilities	26	276	204	214	
CF from operating activities	716	-61	623	665	
(Inc)/dec in Investments	-105	227	0	0	
(Inc)/dec in Fixed Assets	-295	-471	-400	-100	
Others	0	0	0	0	
CF from investing activities	-400	-244	-400	-100	
Inc / (Dec) in Equity Capital	0	0	0	0	
Inc / (Dec) in Loan	-296	367	-100	-50	
Dividend & Dividend Tax	-12	-154	-202	-219	
Others	105	144	0	0	
CF from financing activities	-203	357	-302	-269	
Net Cash flow	114	52	-79	296	
Opening Cash	437	551	602	523	
Closing Cash	551	602	523	820	

Source: Company, ICICI Direct Research

Exhibit 8: Balance sheet		₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E	
Liabilities					
Equity Capital	39	39	39	39	
Reserve and Surplus	3360	3738	4042	4364	
Total Shareholders funds	3399	3777	4080	4403	
Total Debt	297	663	563	513	
Deferred Tax Liability	97	96	96	96	
Non Current Liabilities	8	10	10	10	
Total Liabilities	3799	4547	4750	5023	
Assets					
Gross Block	1771	1920	2920	3090	
Less: Acc Depreciation	1078	1157	1260	1388	
Net Block	694	763	1660	1702	
Capital WIP	373	696	96	26	
Total Fixed Assets	1067	1459	1756	1728	
Investments	1262	1035	1035	1035	
Inventory	581	978	1159	1301	
Debtors	289	589	615	694	
Loans and Advances	305	339	347	355	
Other Current Assets	94	169	143	133	
Cash	551	602	523	820	
Total Current Assets	1819	2677	2788	3303	
Creditors	257	448	622	806	
Other Current Liabilities (incl Pro	91	177	207	237	
Current Liabilities & Prov	348	624	829	1043	
Net Current Assets	1471	2053	1959	2260	
Others	0	0	0	0	
Application of Funds	3799	4547	4750	5023	

Source: Company, ICICI Direct Research

Exhibit 9: Key ratios					
(Year-end March)	FY21	FY22	FY23E	FY24E	
Per share data (₹)					
EPS	-7	101	131	140	
BV	880	978	1,057	1,141	
DPS	3	40	52	56	
Cash Per Share	143	156	136	212	
Operating Ratios (%)					
EBITDA margins	-4.7	23.9	24.6	21.8	
PBT margins	-2.4	23.6	24.1	21.4	
Net Profit margins	-2.0	17.7	18.0	16.0	
Inventory days	161	213	200	180	
Debtor days	84	98	80	75	
Creditor days	116	197	200	200	
Return Ratios (%)					
RoE	-0.7	10.3	12.4	12.3	
RoCE	-0.5	11.9	14.7	14.9	
RoIC	-4.2	14.1	17.0	17.1	
Valuation Ratios (x)					
P/E	NA	13.1	10.1	9.4	
EV / EBITDA	NA	8.5	6.5	5.8	
EV / Revenues	3.9	2.4	1.8	1.4	
Market Cap / Revenues	4.1	2.3	1.8	1.5	
Price to Book Value	1.5	1.4	1.3	1.2	
Solvency Ratios					
Debt / Equity	0.1	0.2	0.1	0.1	
Debt/EBITDA	NA	1.3	0.8	0.7	
Current Ratio	5.2	4.3	3.4	3.2	
Quick Ratio	3.6	2.7	2.0	1.9	

Source: Company, ICICI Direct Research

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