Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

The Ramco Cements Ltd

Downgrade to Hold owing to near term headwinds

Cement	Sharekhan code: RAMCOCEM	
Reco/View: Hold ↓	CMP: **Rs. 704**	Price Target: **Rs. 780** ↓

↑ 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 32.63

Updated Aug 08, 2022

High Risk

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

Source: Morningstar

Company details

Market cap:	Rs. 16,637 cr
52-week high/low:	Rs. 1,119/575
NSE volume: (No of shares)	9.0 lakh
BSE code:	500260
NSE code:	RAMCOCEM
Free float: (No of shares)	13.6 cr

Shareholding (%)

Promoters	42.3
FII	6.6
DII	37.1
Others	13.9

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-2.8	-6.7	-2.4	-34.2
Relative to Sensex	-8.0	-10.5	-14.7	-35.3

Sharekhan Research, Bloomberg

Summary

- We downgrade The Ramco Cements Limited (Ramco) to Hold with a revised PT of Rs. 780 due to limited upside potential considering near-term headwinds.
- The company positively surprised on cement volume growth of 22% y-o-y while disappointed on operational profitability which stood at multi year low at Rs. 383 EBITDA/tonne.
- Management ups volume growth guidance for FY2023 to 25-30% and expects 23% volume growth for FY2024. However, elevated power & fuel costs during H2FY2023 is expected to lead to weak operational profitability than earlier envisaged.
- It announced new brownfield grinding capacity of 0.9mtpa at Odisha at a capex of only Rs. 130 crores. Net Debt rise to over Rs. 4700 crore although not expected to significantly rise in H2FY2023.

Ramco Cements Limited (Ramco) positively surprised with sales volumes while it disappointed in operational profitability for Q2FY2023. Standalone revenues rose by 19.5% y-o-y at Rs. 1784 crore (flattish blended realisations both y-o-y & 1.5% q-o-q) with a 22.3% y-o-y rise in volumes. Blended EBITDA/tonne of Rs. 383 (down 68% y-o-y) was at eight years low on account of a steep rise in power & fuel costs (up 90% y-o-y on per tonne basis). Consequently, standalone operating profit/net profit declined by 53%/95% y-o-y at Rs. 184 crore/Rs. 11.5 crore, which was much below our as well as street expectations. The company expects to achieve 25-30% y-o-y volume growth (earlier 12-15%) for FY2023 and 23% y-o-y volume growth for FY2024. However, power & fuel costs are expected to remain at elevated levels during H2FY2023 denting operational profitability. It also revised its capex for FY2023 to Rs. 1717 crore (aided by the increased scope of work to accommodate future expansions) from Rs. 850 crores while its net debt increased by almost Rs. 600 crore q-o-q to Rs. 4741 crores.

Key positives

- Cement volumes rose 22% y-o-y to 3.31mt which was much higher than our expectation.
- It announced a brownfield grinding capacity addition of 0.9mtpa in Odisha at the cost of only Rs. 130 crores which is expected to be operational within 9-12 months.

Key negatives

- EBITDA/tonne at Rs. 383 (down 68% y-o-y) stood at eight-year low led by steep rise in power & fuel costs (which increased by 90% y-o-y on a per tonne basis).
- The net debt increased by almost Rs. 600 crores q-o-q to Rs. 4741 crores on account of low cash flow generation and rise in inventory (built up of inventory as its major supplier undertakes one-month shutdown).

Management Commentary

- It would focus on premiumisation, increased productivity and completion of announced capacity expansion plans. The government's focus on infrastructure, good monsoons and upcoming elections is expected to drive demand going ahead.
- The blended fuel consumption for Q3FY2023 is expected to decrease by $10-15 before reverting to $199 in Q4FY2023.
- Capex revision includes increased capex for preparatory work at the Kurnool plant for future expansion. The second line at Kurnool can be put with a lower capex of Rs. 500-600 crores.
- It does not expect any significant increase in net debt in H2FY2023.

Revision in estimates – We have lowered our estimates for FY2023 factoring in increased power & fuel costs offsetting the increased volumes. We lower our FY2024 net earnings by factoring higher interest and depreciation expense.

Our Call

Valuation – Downgrade to Hold with a revised PT of Rs. 780: Ramco is expected to face near-term headwinds in terms of increased power & fuel costs compared to its peers although it is expected to report outperform industry peers on volume growth. The increased leverage and consistently upwardly revised Capex outlay pose uncertainty on free cash flow generation. The company would have to increase cement prices and focus on improving operational efficiencies to improve upon operational profitability post-FY2023. We introduce our FY2025E earnings in this note. At CMP, the stock is currently trading at an EV/EBITDA of 13.3x/11.3x its FY2024E/FY2025E earnings, which we believe leaves limited room for upside considering near term headwinds. Hence, we downgrade the stock to Hold with a revised price target (PT) of Rs. 780.

Key Risks

Weak demand and pricing environment in South India would affect profitability.

Valuation (Standalone) Rs cr

Particulars	FY22	FY23E	FY24E	FY24E
Revenue	5,980	7,438	9,260	10,557
OPM (%)	21.5	12.6	17.5	17.8
Adjusted PAT	893	201	679	842
% YoY growth	17.3	-77.4	237.1	24.1
Adjusted EPS (Rs.)	37.8	8.5	28.7	35.7
P/E (x)	18.6	82.6	24.5	19.7
P/B (x)	2.5	2.5	2.3	2.1
EV/EBITDA (x)	15.7	23.2	13.3	11.3
RoNW (%)	14.7%	3.1%	9.8%	11.1%
RoCE (%)	9.7%	3.0%	6.5%	7.3%

Source: Company; Sharekhan estimates

Strong volume growth while EBITDA/tonne at multi year low

Ramco Cements Limited (Ramco) was positively surprised on sales volumes while disappointed with operational profitability for Q2FY2023. Standalone revenues rose by 19.5% y-o-y at Rs. 1784 crore (flattish blended realisations both y-o-y & 1.5% q-o-q) with a 22.3% y-o-y rise in volumes. Blended EBITDA/tonne of Rs. 383 (down 68% y-o-y) was at eight year low on account of a steep rise in power & fuel costs (up 90% y-o-y on a per tonne basis). Consequently, standalone operating profit/net profit declined by 53%/95% y-o-y at Rs. 184 crore/Rs. 11.5 crore, which was much below our as well as street expectations.

Capacity expansion plans

The Company proposed to increase the grinding capacity of the Haridaspur plant, Odisha by 0.9 MTPA at the cost of only Rs.130 Crores since other infrastructures are already in place, thereby doubling its capacity to 1.8 MTPA. It commenced cement production in Kolimigundla from September 2022 leading to an increased cement capacity to 21 MTPA with a clinker capacity of 14 MTPA. The 6 MW of WHRS in Kolimigundla will be commissioned in November 2022 while the balance 6 MW of WHRS will be commissioned in March 2023, TPP of 18 MW and railway siding will be commissioned in 2023-24. The modernisation of RR Nagar plant will be commissioned before March 2023. Concerning the expansion of capacity of its dry mix products, two units in Tamilnadu are ready for commissioning and market trials for products are in progress. The remaining two units in AP & Orissa will be commissioned during 2023-24.

Key Conference call takeaways

- **Guidance:** The management expects to achieve 25-30% y-o-y volume growth (earlier 12-15%) for FY2023 and 23% y-o-y volume growth for FY2024. However, power & fuel costs are expected to remain elevated in H2FY2023. The high net debt is expected to remain during FY2023.
- **Outlook:** It would focus on premiumisation, increased productivity and completion of announced capacity expansion plans. The government's focus on infrastructure, good monsoons and upcoming elections is expected to drive demand going ahead.
- **Q2FY2023 performance:** The sales volume for Q2FY2023 rose by 22% y-o-y to 3.31 million tonnes aiding overall standalone revenue growth of 19.5% y-o-y to Rs. 1784 crore. Lower cement prices along with steep rise in power & fuel costs, led to eight years low blended EBITDA/tonne of Rs. 383. The depreciation in the Indian rupee by 12%, along with a change in OPC:PPC mix aided in a substantial increase in power & fuel costs. Consequently, standalone profit dipped 98% y-o-y to Rs. 11.5 crores.
- **Power & fuel costs:** The blended fuel consumption per tonne is as follows Q2FY2023 - $199, Q1FY2023 - $164 and H1FY2023 - $181. The same for FY2022 is as follows Q1FY2022 - $85, Q2FY2022 - $97, Q3FY2022 - $149 and Q4FY2022 - $199. The blended fuel consumption for Q3FY2023 is expected to come down by $10-15 before reverting to $199 in Q4FY2023.
- **Capex revision:** The company revised its overall capex for FY2023 from Rs. 850 crores to Rs. 1717 crore. Capex revision includes increased capex for preparatory work at Kurnool plant for future expansion. The second line at Kurnool can be put with a lower capex of Rs. 500-600 crores. The company incurred Rs. 504 crore capex in Q2FY2023 and Rs. 986 crores in H1FY2023. The capex for FY2024 is estimated at Rs. 892 crore.
- **Rise in net debt:** The company's net debt increased to Rs. 4741 crores from Rs. 4148 crores in Q1FY2023. It does not expect any significant increase in net debt in H2FY2023.

- **Ongoing Capacity expansion:** It commissioned 1.5mtpa cement capacity at Kurnool, A.P., in September 2022. The modernisation of RR Nagar plant is expected to commission before March 2023. About expansion of capacity of its dry mix products, two units in Tamilnadu are ready for commissioning and market trials for products are in progress. The remaining two units in AP & Orissa will be commissioned during 2023-24.
- **New capacity expansion:** The Company proposes increasing the grinding capacity of the Haridaspur plant, Odisha by 0.9 MTPA at the cost of only Rs.130 crores since other infrastructures are already in place, thereby doubling its capacity to 1.8 MTPA. The proposed capacity is expected to commission in 9-12 months.
- **Price hikes:** Tamil Nadu saw Rs. 15-20/bag increase in cement price in October. A.P. did not see any price rise. In Kerala, prices increased by Rs. 25-30/bag in October and Rs. 15/bag in November. Karnataka saw price rise of Rs. 20-25/bag in October and Rs. 5-10/bag in November. Odisha saw a price increase of Rs. 40-45/bag in early October but the company was able to hold on to only Rs. 10-15/bag increase. West Bengal saw price rise of Rs. 10-15/bag in October while it is attempting Rs. 10/bag in November.
- **RoCE:** The company targets a minimum of 15-16% post-tax RoCE for incremental capex.
- **Premium sales:** It targets to achieve premium products' revenue share of 30-35% of topline over 2-3 years from 25%. Premium products have Rs. 15-25/bag higher price and 2-3% higher margins than expected.
- **Trade share:** The trade share mix was 68%.

Results (Standalone) Rs cr

Particulars	Q2FY2023	Q2FY2022	y-o-y	Q1FY2023	q-o-q
Net Sales	**1784.4**	**1493.1**	**19.5%**	**1772.5**	**0.7%**
Total Expenditure	1600.6	1099.3	45.6%	1471.8	8.7%
Operating profits	**183.8**	**393.8**	**-53.3%**	**300.7**	**-38.9%**
Other Income	8.8	7.9	11.8%	6.9	28.1%
EBIDTA	192.7	401.7	-52.0%	307.6	-37.4%
Interest	55.1	29.4	87.2%	47.5	15.9%
PBDT	137.6	372.3	-63.0%	260.1	-47.1%
Depreciation	121.6	98.5	23.4%	106.4	14.3%
PBT	**16.0**	**273.8**	**-94.1%**	**153.7**	**-89.6%**
Tax	4.6	-243.2	-	41.4	-89.0%
Extraordinary items	0.0	305.6	-100.0%	0.0	
Reported Profit After Tax	11.5	517.1	-97.8%	112.3	-89.8%
Adjusted PAT	**11.5**	**211.5**	**-94.6%**	**112.3**	**-89.8%**
EPS (Rs.)	0.5	9.0	-94.6%	4.8	-89.8%
OPM	10.3%	26.4%	-1608 bps	17.0%	-666 bps
PAT	0.6%	14.2%	-1352 bps	6.3%	-569 bps
Tax rate	28.4%	-88.8%	-	27.0%	145 bps

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Improving demand brightens the outlook

The cement industry has seen a sustained improvement in demand in the past 15 years. Barring a couple of years, regional cement prices have been on a rising trajectory over the trailing five years. The cement industry is expected to witness improvement in demand as the situation normalises from the second wave of COVID-19, led by infrastructure and rural demand. A strong pick-up in the residential real estate sector is expected to sustain after the second wave of COVID-19. The sector's long-term growth triggers in terms of low per capita consumption and demand pegged at 1.2x GDP remain intact. The government's Rs. 111-lakh crore infrastructure investment plans from FY2020 to FY2025 would lead to healthy demand going ahead.

■ Company Outlook – Capacity additions expected to capture growth opportunities

The company's ongoing capex plan is to create new grinding and clinkerisation capacities that would help it tap the growth potential in the Eastern region and establish itself as a significant player. It proposed to increase the grinding capacity of the Haridaspur plant, Odisha by 0.9 MTPA at the cost of only Rs.130 Crores. It commenced cement production in Kolimigundla from September 2022, leading to an increased cement capacity to 21 MTPA with a clinker capacity of 14 MTPA. The 6 MW of WHRS in Kolimigundla will be commissioned in November 2022, while balance of 6 MW of WHRS will be commissioned in March 2023, TPP of 18 MW and railway siding will be commissioned in 2023-24. The modernisation of the RR Nagar plant will be commissioned before March 2023.

■ Valuation – Downgrade to Hold with a revised PT of Rs. 780

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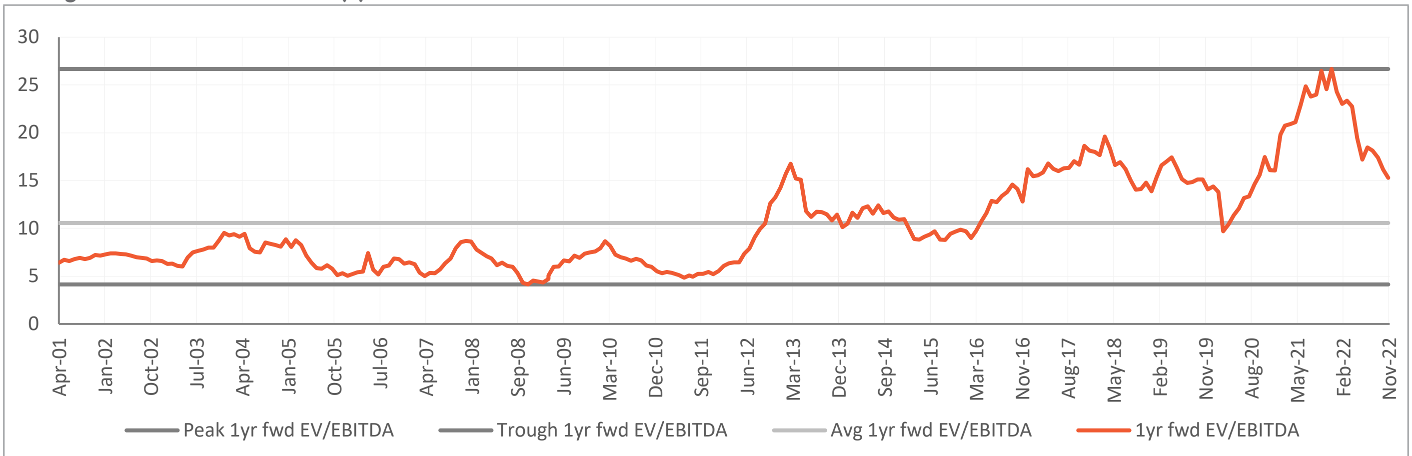
One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer Comparison

Companies	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
UltraTech	35.8	28.8	18.0	14.7	3.7	3.3	10.7	12.0
Shree Cement	71.5	43.0	26.6	18.4	4.6	4.2	6.6	10.3
The Ramco Cement	82.6	24.5	23.2	13.3	2.5	2.3	3.1	9.8
Dalmia Bharat	56.1	40.9	13.7	11.5	2.0	1.9	3.6	4.7

Source: Company; Sharekhan Research

About company

Ramco is the fifth largest cement producer in the country, operating in southern India with an installed capacity of 18.79mtpa. The company also produces ready-mix concrete and dry mortar products and operates one of the largest wind farms in the country.

Investment theme

Southern India has started showing signs of cement price improvement along with rising capacity utilisation over the trailing five quarters. Ramco, being one of the most efficient cement players, is expected to reap benefits from healthy demand, better pricing, and a benign opex environment. Ramco has embarked on a capex plan to outpace its industry peers on cement volume growth. This, along with improving cement prices, is expected to lead to healthy growth in net earnings during FY2022-FY2025.

Key Risks

- Correction in cement prices in the south and/or sharp upward movement in power and fuel and freight costs to negatively affect profitability.
- Deterioration in cement demand in south leading to lower utilisation to negatively affect net earnings.

Additional Data

Key management personnel

Mr. P R Venketrama Raja	Executive Director-Chairperson
A V Dharmakrishna	Chief Executive Officer
S Vaithiyanathan	Chief Financial Officer
K Selvanayagam	Company Secretary andCompliance Of-ficer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Ramco Industries Ltd.	21.03
2	Rajapalayam Mills Ltd.	14.02
3	Kotak Mahindra Asset Management Co.	6.87
4	L&T Mutual Fund Trustee Ltd./India	4.09
5	Republic of India	3.39
6	GOVT TAMIL NADU	3.39
7	SBI Funds Management	3.01
8	HDFC LIFE INSURA	2.29
9	Sundaram Asset Management Co. Ltd.	2.09
10	DSP Investment Managers	2.08

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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