Sharekhan by BNP PARIBAS

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Stock Update

Result Update

JK Lakshmi Cement Ltd

Fairly valued; Downgrade to Hold

Cement	Sharekhan code: JKLAKSHMI		
Reco/View: Hold ↓	CMP: Rs. 754	Price Target: Rs. 830 ↑	

↑ 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 41.62

Updated Dec 08, 2022

Medium Risk

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

Source: Morningstar

Company details

Market cap:	Rs. 8,868 cr
52-week high/low:	Rs. 897/369
NSE volume: (No of shares)	1.7 lakh
BSE code:	500380
NSE code:	JKLAKSHMI
Free float: (No of shares)	6.3 cr

Shareholding (%)

Promoters	46.3
FII	13.8
DII	25.6
Others	14.3

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-0.6	16.6	57.8	54.1
Relative to Sensex	-1.2	18.5	56.8	46.9

Sharekhan Research, Bloomberg

Summary

- We downgrade JK Lakshmi Cement Limited (JKL) to Hold with a revised PT of Rs. 830, rolling forward our valuation multiple to FY2025 earnings and considering unfavourable risk reward at the current valuation.
- JKL reported in-line standalone revenue, aided by equal growth in both blended realisations and sales volume. EBITDA/tonne came in lower than estimated on account of higher opex/tonne. PAT growth was aided by lower ETR.
- The company targets Rs. 1,000 EBITDA/tonne over 18-24 months with incremental delta of Rs. 200/ tonne from realisation and the balance from manufacturing and logistics. We believe it would take longer.
- UCW expansion may get delayed by a quarter to Q1FY2025. The target is to achieve 30mtpa capacity by 2030, through brownfield and greenfield expansions remain intact.

JK Lakshmi Cement Limited (JKL) reported in-line standalone revenue at Rs. 1,489 crore (up 24.7% y-o-y), led equally by higher blended realisation (up 11.6% y-o-y at Rs. 5,716/tonne) and volumes (up 11.8% y-o-y at 2.6 million tonne). Standalone EBITDA/tonne at Rs. 613 (down 2.5% y-o-y) came in lower than our estimate of Rs. 692/tonne on account of higher than-expected opex/tonne. Consolidated operating profit grew by 9% y-o-y to Rs. 160 crore, while net profit increased by 24.2% y-o-y to Rs. 73.6 crore (aided by lower effective tax rate). Management targets to reach Rs. 1,000 EBITDA/tonne over 18-24 months with incremental growth coming in from realisation (Rs. 200/tonne), manufacturing (Rs. 50/tonne), and supply chain management (Rs. 50-75/tonne). The company has reiterated its cement capacity target of 30MTPA (current 15MTPA, including outsourced unit) by 2030. The 2.55MTPA cement capacity expansion at UCW may get delayed by a quarter to Q1FY2025. We believe the company's targeted operational profitability may not accrue as per management's timeline and would take further time to accrue.

Key positives

- Blended realisations and sales volumes rose 12% y-o-y each.
- Operating margin of non-cement business improved to 7% from 5%/3% in Q2FY2023/Q3FY2022.

Key negatives

- EBITDA/tonne came below expectations on account of higher-than-expected opex/tonne.
- Fuel costs on per Kcal basis are expected to remain flat in Q4FY2023 before marginally declining from Q1FY2024.

Management Commentary

- The company is working on three expansion projects 1) Nagaur, Rajasthan – mining block; 2) Railway sliding at Durg; and 3) Kutch, Gujarat – mining block, which would help it in expanding capacities.
- The company started production of AAC blocks at Aligarh unit. The company did ground breaking for putty plant at Alwar, Rajasthan, which is expected to come on stream in nine months.
- For Q3FY2023, trade mix was 54%, blended cement – 66%, lead distance – 396 km (401 km in Q2FY2023), and premium cement – 11% of total volumes (25% of trade sales). The rail mix is 10%.

Revision in estimates – We have lowered our net earnings estimates for FY2023, factoring in higher opex/tonne, while we have fine-tuned our estimates for FY2024-FY2025.

Our Call

Valuation – Downgrade to Hold with a revised PT of Rs. 830: JKL is expected to focus on optimizing the sales mix based on the geographic sales mix, product mix, and increased revenue in the non-cement business. Additionally, JKL expects to derive benefits from increasing renewable power usage and reducing lead distance going ahead. Overall, the company targets to achieve Rs. 1,000 EBITDA/tonne over 18-24 months, which we believe may not accrue as per management's timeline and would take further time. JKL had appreciated more than 40% post our report dated November 4, 2023, making yearly high, before getting corrected by 15%. JKL is currently trading at a valuation of EV/EBITDA of 8x/6.5x its FY2024E/FY2025E earnings, which we believe is fairly valued. Hence, we downgrade the stock to Hold with a revised price target (PT) of Rs. 830, rolling forward our valuation multiple to FY2025 earnings and considering unfavourable risk-reward ratio.

Key Risks

Slow demand in North and East India along with weak pricing negatively affects profitability.

Valuation (Standalone) Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
Revenue	5,041	6,159	6,730	7,322
OPM (%)	16.1	12.5	14.0	14.6
Adjusted PAT	436	376	506	600
% y-o-y growth	20	-14	35	19
Adjusted EPS (Rs.)	39.0	31.9	43.0	51.0
P/E (x)	19.3	23.6	17.5	14.8
P/B (x)	3.6	3.2	2.8	2.4
EV/EBITDA (x)	10.5	10.5	8.0	6.5
RoNW (%)	20.3%	14.4%	17.0%	17.4%
RoCE (%)	15.6%	12.2%	14.5%	15.3%

Source: Company; Sharekhan estimates

Higher opex/tonne led to miss on operational profitability

JKL reported in-line standalone revenue at Rs. 1489 crore (up 24.7% y-o-y), led equally by higher blended realisations (up 11.6% y-o-y at Rs. 5716/tonne) and volumes (up 11.8% y-o-y at 2.6 million tonne). Higher non-cement business revenue on a y-o-y basis aided the strong rise in blended realisation during the quarter. Standalone EBITDA/tonne at Rs. 613 (down 2.5% y-o-y) came in lower than our estimate of Rs. 692/tonne on account of higher-than-expected opex/tonne. Power and fuel costs stood at Rs. 1,669/tonne (+33% y-o-y, +15% q-o-q), freight cost stood at Rs. 1,130/tonne (+6% y-o-y, +4% q-o-q), and other expense stood at Rs. 692/tonne (+9% y-o-y, +10% q-o-q) for Q3FY2023. Consolidated operating profit grew by 9% y-o-y to Rs. 160 crore, while net profit was up 24.2% y-o-y at Rs. 73.6 crore (aided by lower effective tax rate).

Key Conference call takeaways

- **Target of Rs. 1,000 EBITDA/tonne:** JKL is targeting to achieve Rs. 1,000 EBITDA/tonne over the next 18-24 months. As per management, Rs. 200/tonne plus would be contributed through topline levers, Rs. 50/tonne through manufacturing, and Rs. 50-75/tonne through supply chain management (outbound logistics).
- **Outlook:** Fuel cost on Kcal basis is expected to remain flat in Q4FY2023, while it is expected to decline marginally from Q1FY2024. JKL targets to increase the blended cement mix to 75% and trade mix to 60% through geo-mix.
- **Expansion:** The company's current cement capacity including outsourced Amethi, U.P. unit is 15MTPA. The company targets to increase cement capacity to 30MTPA by 2030. It is working on three expansion projects – 1) Nagaur, Rajasthan – mining block; 2) Railway sliding at Durg; and 3) Kutch, Gujarat – mining block, which would help it in expanding capacities.
- **UCW Expansion:** The completion of 2.55MTPA Udaipur Cement expansion may spill over to Q1FY2025 from Q4FY2024. Till December 2022, it has spent Rs. 700 crore out of Rs. 1,650 crore.
- **Solar power:** It would be investing Rs. 22 crore for a 26% stake for the supply of 40MW solar power at Durg, which is expected to be ready by Q4FY2024. It would be receiving power at Rs. 5.50/unit.
- **Non-cement business:** Non-cement business revenue stood at Rs. 116 crore for Q3FY2023 (Rs. 116 crore/ Rs. 99 crore during Q2FY2023/Q3FY2022) comprising RMC – Rs. 56 crore, AAC blocks – Rs. 40 crore, and PoP – Rs. 20 crore. Operating margin in the non-cement business stood at 7% in Q3FY2023 compared to 5%/3% in Q2FY2023/Q3FY2022. It started production of AAC blocks at Aligarh unit. It did ground-breaking for putty plant at Alwar, Rajasthan, which is expected to come on stream in nine months.
- **Fuel costs:** Fuel cost stood at Rs. 2.57/Kcal in Q3FY2023 compared to Rs. 2.30/Kcal in Q2FY2023.
- **Consolidated Capex:** JKL incurred capex of Rs. 250 crore in Q3FY2023. The company would be incurring Rs. 150-200 crore capex in Q4FY2023 and Rs. 750 crore capex in FY2024.
- **Debt:** Standalone gross debt and net debt are Rs. 850 crore and Rs. 200 crore, respectively. Consolidated gross debt and net debt are Rs. 1,875 crore and Rs. 1,225 crore, respectively.
- **Other highlights:** For Q3FY2023, trade mix was 54%, blended cement was 66%, lead distance – 396kms (401kms in Q2FY2023), and premium cement – 11% of total volumes (25% of trade sales). The rail mix is 10%.

Results (Standalone) Rs cr

Particulars	Q3FY2023	Q3FY2022	% y-o-y	Q2FY2023	% q-o-q
Net Sales	**1488.5**	**1193.4**	**24.7%**	**1302.7**	**14.3%**
Total Expenditure	1328.9	1047.0	26.9%	1164.0	14.2%
Operating profit	**159.6**	**146.4**	**9.0%**	**138.6**	**15.1%**
Other Income	15.6	16.4	-5.0%	21.4	-27.1%
EBIDTA	175.2	162.8	7.6%	160.0	9.5%
Interest	24.7	25.1	-1.4%	22.6	9.3%
PBDT	150.5	137.8	9.2%	137.4	9.5%
Depreciation	48.0	46.8	2.6%	48.1	-0.1%
PBT	**102.5**	**91.0**	**12.6%**	**89.4**	**14.7%**
Tax	28.9	31.8	-9.0%	30.4	-5.0%
Extraordinary items	0.0	0.0	-	0.0	-
Reported Profit After Tax	73.6	59.2	24.2%	59.0	24.8%
Adjusted PAT	**73.6**	**59.2**	**24.2%**	**59.0**	**24.8%**
EPS (Rs.)	6.3	5.0	24.2%	5.0	24.8%
Margins (%)			**BPS**		**BPS**
OPMs	10.7%	12.3%	(155)	10.6%	8
PAT	4.9%	5.0%	(2)	4.5%	42
Tax rate	28.2%	34.9%	(671)	34.0%	(584)

Source: Company, Sharekhan Research

Outlook and Valuation

Sector View – Improving demand brightens the 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 past 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. 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 plan from FY2020 to FY2025 would lead to healthy demand going ahead.

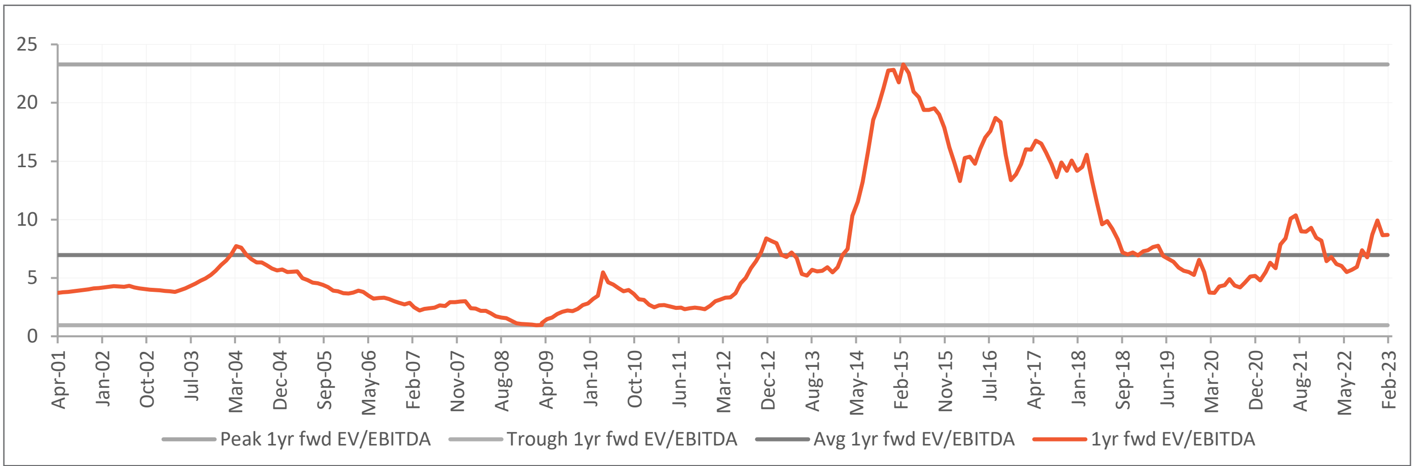
Company Outlook – Capacity expansion to provide the next leg of growth from FY2025

JKL is expected to benefit from sustained rural sector demand along with improvement in infrastructure demand. The pricing environment in key regions remains healthy. However, the company is facing capacity constraints with clinker capacity utilisation at peak level over the trailing peak quarters. JKL's expansion plans at UCW (1.5MTPA clinker, 2.5MTPA grinding unit) are expected to be completed by March 2024, which would provide the next leg of growth from FY2025. Meanwhile, the company's standalone debt de-leveraging would continue improving its balance sheet strength. On the other hand, the cement industry is on a strong growth trajectory for the next three years. The company's operational efficiency measures would aid in improving operational profitability going ahead.

Valuation – Downgrade to Hold with a revised PT of Rs. 830

JKL is expected to focus on optimizing the sales mix based on the geographic sales mix, product mix, and increased revenue in the non-cement business. Additionally, JKL expects to derive benefits from increasing renewable power usage and reducing lead distance going ahead. Overall, the company targets to achieve Rs. 1,000 EBITDA/tonne over 18-24 months, which we believe may not accrue as per management's timeline and would take further time. JKL had appreciated more than 40% post our report dated November 4, 2023, making yearly high, before getting corrected by 15%. JKL is currently trading at a valuation of EV/EBITDA of 8x/6.5x its FY2024E/FY2025E earnings, which we believe is fairly valued. Hence, we downgrade the stock to Hold with a revised price target (PT) of Rs. 830, rolling forward our valuation multiple to FY2025 earnings and considering unfavourable risk-reward ratio.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer Comparison

Company	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
UltraTech	43.1	32.2	20.8	16.1	3.9	3.5	9.3	11.3
Shree Cement	71.6	55.2	26.9	21.0	4.8	4.5	6.9	8.4
JK Lakshmi Cement	23.6	17.5	10.5	8.0	3.2	2.8	14.4	17.0
Dalmia Bharat	53.1	43.8	14.6	12.0	2.2	2.1	4.2	4.9

Source: Company, Sharekhan estimates

About company

JKL was set up in 1982 in Sirohi, Rajasthan. The company is part of JK Organisation, which operates in India and abroad and is present in the tyre, cement, paper, power transmission and sealing solutions, dairy products, and textile industries. The company has a wide network of over 7,000 dealers across Rajasthan, Gujarat, Haryana, Delhi, Uttar Pradesh, Punjab, Jammu and Kashmir, Madhya Pradesh, Chhattisgarh, Odisha, South Bengal, Vidharbha, Mumbai, and Pune.

Investment theme

JKL is expected to benefit from sustained rural sector demand along with improvement in infrastructure demand. The pricing environment in key regions remains healthy. However, the company is facing capacity constraints with clinker capacity utilisation at peak level over the trailing peak quarters. JKL's expansion plans at UCW (1.5MTPA clinker and 2.5MTPA grinding unit) are expected to be completed by Q1FY2025, which would provide the next leg of growth from FY2025.

Key Risks

- Pressure on cement demand and cement prices in the northwest and eastern regions of India 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

Bharat Hari Singhania	Chairman
Shri Arun Kumar Shukla	President and Director
S. A. Bidkar	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Bengal & Assam Co. Ltd.	44.28
2	Axis Asset Management Co. Ltd./India	6.37
3	L&T Mutual Fund Trustee Ltd./India	4.46
4	India Capital Fund Ltd.	2.40
5	DSP Investment Managers Pvt. Ltd.	2.02
6	ICICI Prudential Asset Management	1.91
7	The Goldman Sachs Group Inc.	1.80
8	The Vanguard Group Inc.	1.71
9	HDFC Life Insurance Co. Ltd.	1.35
10	IDFC Mutual Fund/India	1.26

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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