HDFC securities

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20 YEARS

Initiating Coverage

Orient Cement Ltd.

17-December-2020

RETAIL RESEARCH

Orient Cement Ltd.

Industry	LTP	Base case Fair Value	Bull case Fair Value	Recommendation	Time Horizon
Cement	Rs. 76.75	Rs.88	Rs.97	Buy at LTP and add on dips to Rs.68-70 band	2 quarters

HDFC Scrip Code	ORICEMEQNR
BSE Code	535754
NSE Code	ORIENTCEM
Bloomberg	ORCMNT:IN
CMP Dec 16, 2020	76.75
Equity Capital (cr)	20
Face Value (Rs)	1
Eq- Share O/S(cr)	20.5
Market Cap (Rscr)	1573
Book Value (Rs)	55
Avg.52 Wk Volume	624909
52 Week High	89.70
52 Week Low	35.25

Share holding Pattern % (Sept, 2020)	
Promoters	37.37
Institutions	29.38
Non Institutions	33.25
Total	100.0

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Our Take:

Orient Cement Ltd.(OCL) is a CK Birla group company with three decades old history. It has a diversified market presence across different regions in India. It has 8 MTPA of cement capacity and 5.2 MTPA of clinker capacity. The company has been focusing on increasing captive power plant which can improve operating efficiency. Orient cement has also been working on reducing debt burden from the balance sheet.

We expect that Covid-19 led lockdown and slowdown in the economy could lead to subdued growth in volumes for Orient Cement for FY21 but benign raw material price, buoyant cement prices and aggressive control on variable costs are likely to drive EBIDTA growth. The industry has a high dependence on real estate and infra sector which is expected to be impacted due to expected slowdown in the economy. Going forward, we expect, a gradual recovery in cement demand and volumes are likely to pick-up from H2FY21 onwards. Also, on the demand side, key growth drivers are likely to be pick up in rural housing, Pradhan Mantri Awas Yojana (rural), Pradhan Mantri Gram Sadak Yojana and spending on key infrastructure projects.

Valuations & Recommendation:

We expect that the company will get benefit from the strong regional presence, improving utilization and cost efficiencies apart from industry triggers of higher realization. We like Orient Cement due to its strong & experienced management, substantial ongoing cost reduction focus. However, in short to medium term, demand recovery in core markets AP/Telengana and Maharashtra continues to be key monitorable.

We expect, 2% CAGR in top-line and 17% EPS CAGR over FY20-22E. At the LTP, the company is trading at FY22E EV/T of $44.7/T, 6.47x FY22E EV/EBITDA. We feel the base case fair value of the stock is Rs.88 (FY22E EV/T of $48.3/T, 6.6xFY22E EV/EBITDA) and the bull case fair value is Rs.97 (FY22E EV/T of $51.4/T, 7.1xFY22E EV/EBITDA). Investors can buy the stock at LTP and add on dips to Rs.68-70 band (FY22E EV/T of $41.7/T, 5.7xFY22E EV/EBITDA).

However, over the long term the company will have to expand capacity out of these areas of oversupply for valuations at high levels to sustain.

Financial Summary

Particulars (Rs cr)	Q2FY21	Q2FY20	YoY-%	Q1FY21	QoQ-%	FY19	FY20	FY21E	FY22E
Total Operating Income	478	515	-7%	410	16%	2,522.2	2,421.8	2,202.6	2,521.1
EBITDA	113	54	111%	98	15%	312.0	382.9	420.2	406.4
RPAT	35	-8	-552%	26	36%	47.6	86.6	117.8	118.2
Diluted EPS (Rs)	1.7	-0.4	-547%	1.3	36%	2.3	4.2	5.8	5.8
RoE-%						4.6	8.0	10.1	9.3
P/E (x)						33.1	18.2	13.3	13.3
EV/EBITDA						8.4	6.9	6.3	6.5

(Source: Company, HDFC sec)

Q2FY20 Result Update

- The volumes of the company have degrown by 17.7% to 1 MTPA in Q2FY21 compared to 1.2 MTPA in Q2FY20. Revenue has degrown by 7%, y-o-y to Rs.477 cr in Q2FY21 compared to Rs.515 cr in Q2FY20. NSR (Rs/T) has grown by 12.7% to Rs.4677/t, Y-o-Y. Higher rainfall impacted demand in Q2 as there was a fall in demand from individual housing.
- However, with the reduction in overall expenditure, the EBIDTA was at Rs.113 cr as compared to Rs.54 cr in the previous year. EBIDTA/T has improved YoY by 156.6% to Rs.1109/T. Consequently, PAT turned into profit from loss onYoY basis Strong profitability in H1FY21 was driven by steep price hikes in AP/Telangana markets despite demand decline.

Long term Triggers

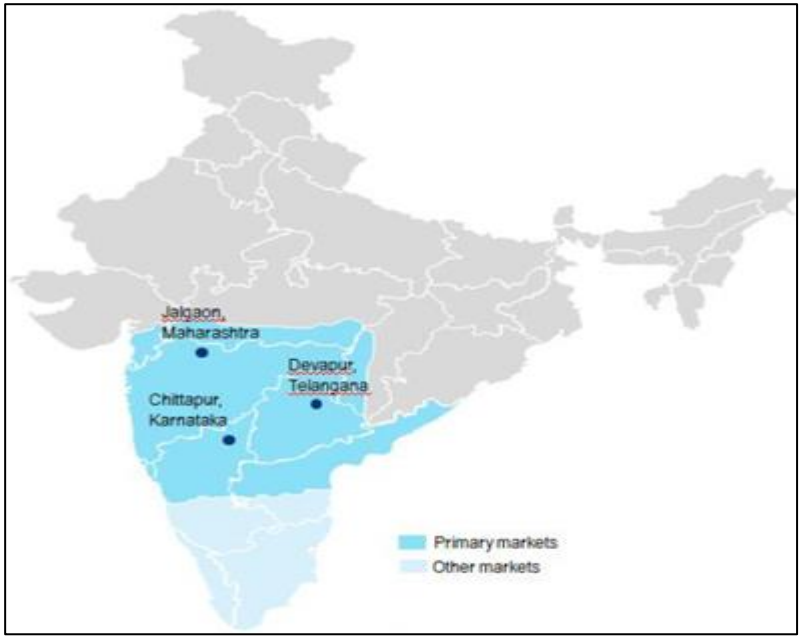
Experienced management group

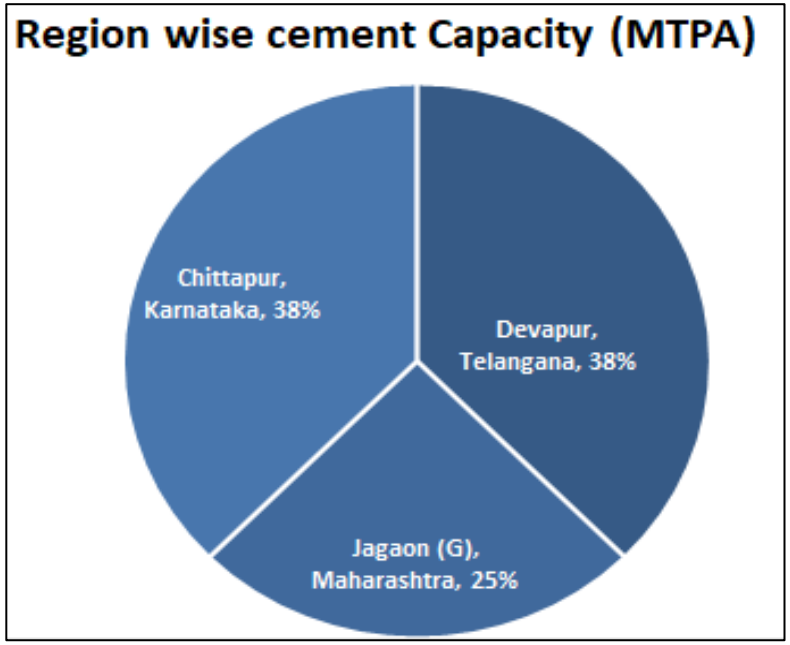
OCL is part of the C.K. Birla Group, which has a 37.37% stake in the company. This group is a leading industrial house of the country and has a major presence in a diverse range of products like automobiles, auto ancillary products, engineering products, chemical, cement, paper, fan and electrical items. The promoters have been operating the cement business for over three decades thereby having considerable experience.

The CK Birla Group, led by Mr Chandra Kant Birla is a diversified Indian conglomerate with total revenue of approximately US$2.4 billion that includes leading brands such as Birla A1 Premium Cement, Orient Electric, NBC Bearings, AVTEC Ltd, Charminar Aerocon, BM Birla Heart Research Centre, CMRI Hospital, Birla Institute of Technology, Mesra and Caterpillar Dealership represented by Gmmco.

Diversified presence

The company has manufacturing facilities at Adilabad in Telangana, Jalgaon in Maharashtra & Gulbarga in Karnataka with the strong distribution network. The Company sells its cement mainly in the states of Maharashtra, Telangana, Karnataka, Andhra Pradesh, and Madhya Pradesh. It also has a presence in the states of Chhattisgarh, Gujarat, Goa and Tamil Nadu.





Source – Company, HDFC sec Research

The Company associated with prominent events to enhance recall and relevance. The Company associated with the Premier Badminton League team called Hyderabad Hunters led by the champion shuttler of India, Ms P.V. Sindhu, enhancing market visibility.

The Company organized/sponsored multiple events in diverse categories like sports, festivals and local events. These events attracted a large number of participants and strong media coverage, enhancing rural visibility.

Focus on Improvement of operating performance

OCL meets majority of its power requirements through its coal-based captive power capacity of 95 MW. The company sources limestone for the cement division from its mines located nearby the respective plants in Telangana and Karnataka. The mines have sufficient proven reserves to support the operation for about next 35-40 years. Therefore, backward integration and proximity to the major raw material sources endow the company with operating benefits, thereby reducing its cost of production. However, the cement operations remain exposed to volatility in prices of coal and other inputs.

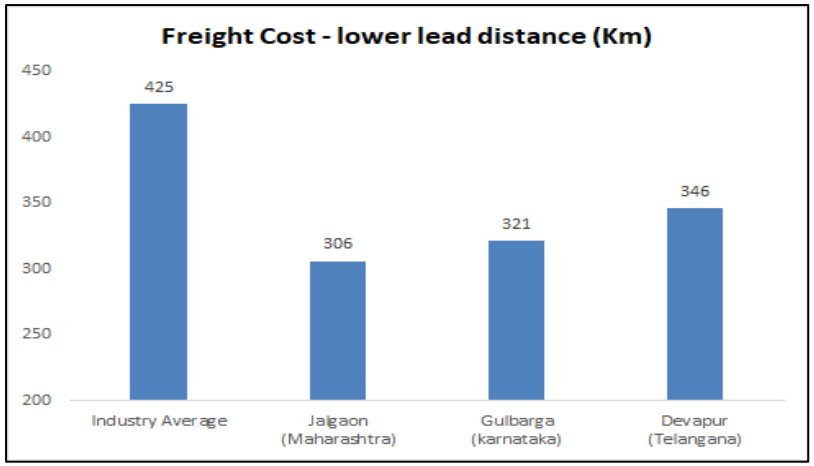
Devapur plant has 3 MT integrated cement capacity with CPP (captive power plant) of 50 MW. It is located 2 km from the high-quality limestone reserve belt. Linkage coal is available from Singareni. Fly ash is sourced from NTPC's thermal power plant. Both are located within ~50 km range.

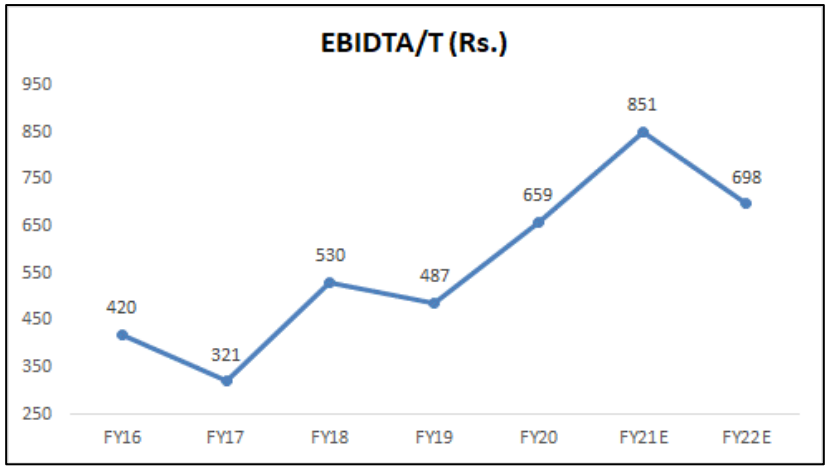
The Jalgaon plant has 2 MT grinding unit. It sources fly ash from NTPC's Bhusawal thermal power plant, located at a distance of ~20 km from the plant.

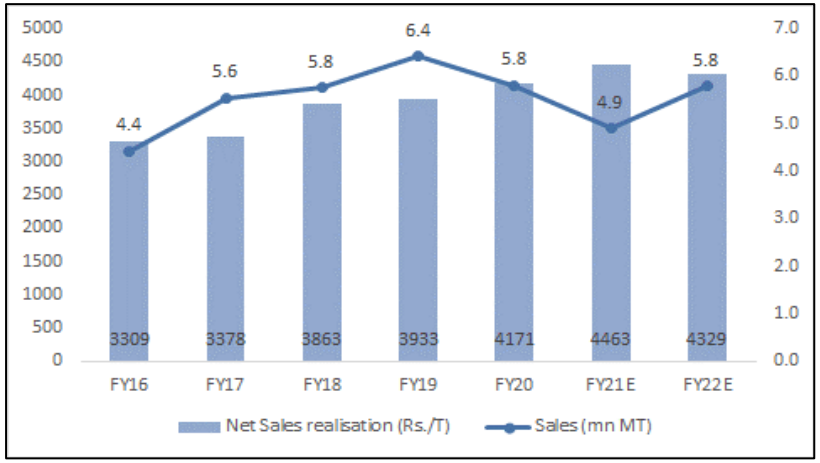
Chittapur plant has 3 MT integrated cement capacity with 45 MW CPP and 6 MW WHRS (Waste Heat Recovery system). This plant was commissioned in Q2FY16. To reduce freight cost, the company commissioned a railway siding in FY19.

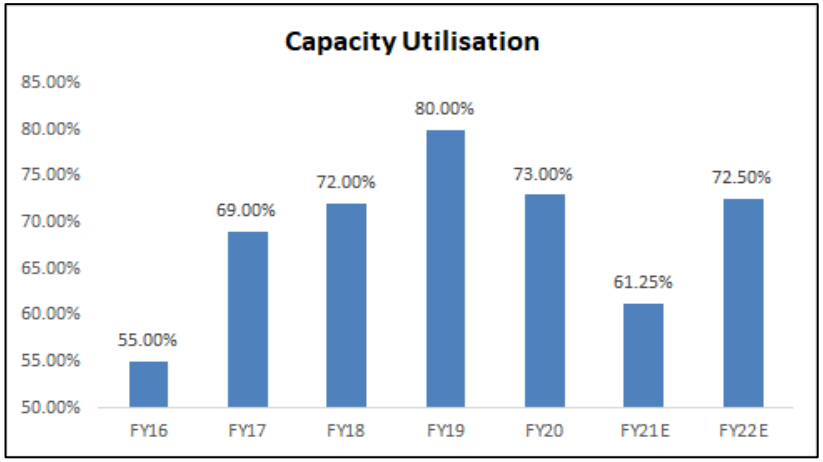
The company has a lower lead distance which keeps freight cost lower. The company has reduced delivery turnaround time and focused on limiting the average delivery distance to nearly ~300 km from its plants. The Company also enhanced rail deliveries, leveraging competitive railway freights to reduce costs. As a result, the Company increased rail dispatches to ~16% in FY20 compared to ~12% in FY19. By ensuring cost management at every possible stage, the Company achieves low costs of production. The company's effective raw material strategy includes alternative fuel sources, contracts for fly ash security, and better utilization of available resources.

Orient Cement Ltd.









Source – Company, HDFC sec Research

As cash flows improve, the Management is exploring the option of either using it for prepayment of additional debt or going for capital expenditure focused on WHRP (Waste heat recovery power plant) in Jalgaon and digital initiatives.

Orient Cement has entered into a share purchase agreement with AMPSolar Technology and AMPSolar Systems on 3 December 2020 for the acquisition of 26% stake in the share capital of AMPSolar Systems for putting up the solar power plant with capacity of 13.5 MW, under the captive scheme. The acquisition is expected to be completed by 6 months.

Cement sector demand drivers

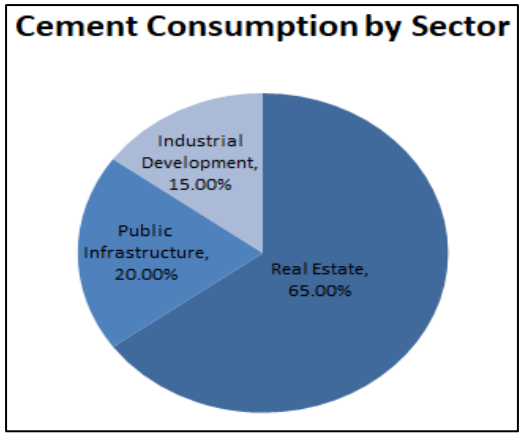
India's urbanization is expected to grow from 34% in 2019 to 40% in 2030, which is likely to strengthen housing and cement demand. India is experiencing a shortage of 10 million affordable housing units. With the Government's focus on plugging this gap, the cement sector is expected to enjoy sustained traction.

The national infrastructure pipeline projected infrastructure investment of Rs.102 lakh cr between 2019-20 and 2024-25.
The Government identified more than 574 projects under Sagarmala Pariyojana to be implemented for Rs.6.01 lakh cr between 2015 and 2035. Out of this, 121 projects entailing spending of Rs.30,228 cr had been completed till October 2019; 201 more projects are under implementation.

What could go wrong

Covid-19 led lockdown and slowdown in the economy affect future growth

Cement demand has fallen sharply in H1FY21. A decline in cement demand in FY21 may bring down capacity utilization of cement companies. Growth in the housing segment, that forms 60%-65% of cement demand, is likely to be affected given the impact of the slowdown in economic growth as lower income growth and income cuts will result on lower discretionary spending over the next year.



Source – Company, HDFC sec Research

The COVID-19 induced self-isolation impaired the home buying sentiments that has created an adverse impact on weak balance sheet builders and they tend to defer launches of new projects.

Fall in volumes will result in lower capacity utilization resulting in lower operating leverage.

Prolonged deterioration of core economy sectors can result in slowdown in cement demand which can result in lower volume offtake and lower cement prices. Cement industry is a highly fixed cost intensive business. Any slowdown in demand can result in negative operating leverage which can impact the overall profitability of the company.

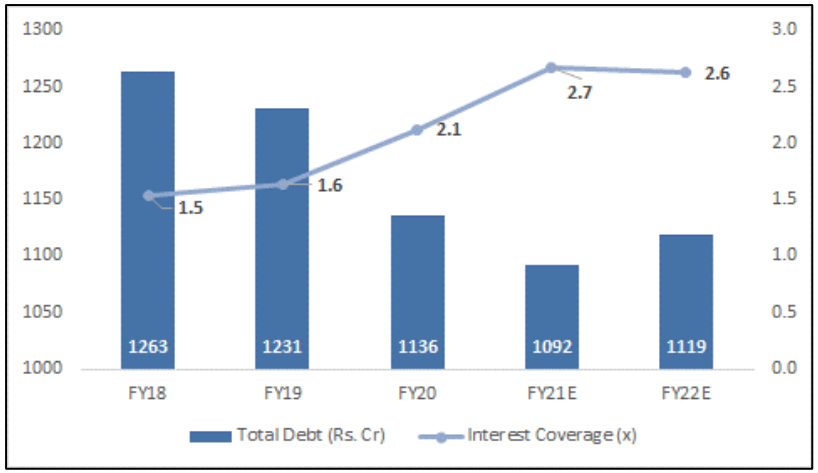
Any spike in key raw materials can result in higher input cost which can impact earnings.

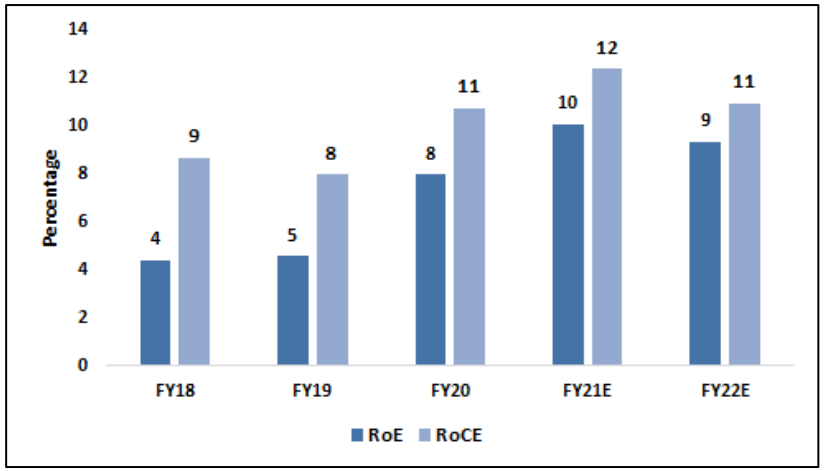
Average balance sheet strength

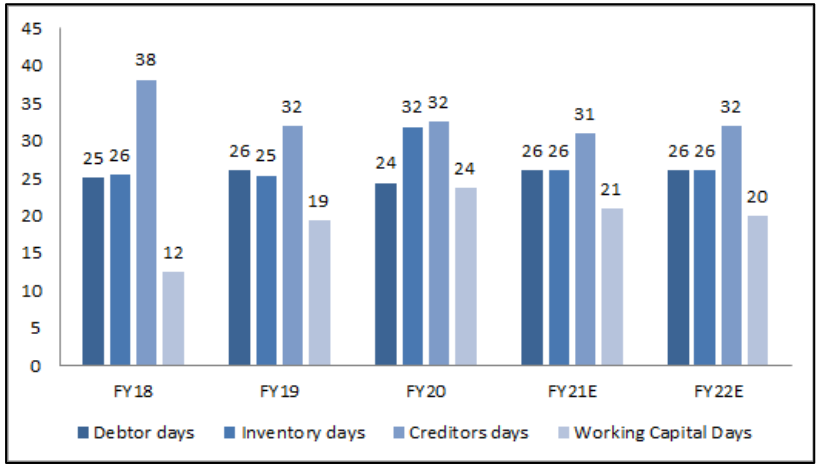
Orient Cement has a higher debt/equity which results in lower interest coverage and adversely affects the profitability. Also, the company has a subdued return ratio. Working capital days has grown higher which can further create pressure on balance sheet strength.

Limited capex and strong margins can result in faster deleveraging however balance sheet flexibility for growth projects is still a few years away.

Orient Cement Ltd.







Source – Company, HDFC sec Research

Orient Cement sells 25% of its volumes in AP/Telangana and 40%+ in Maharashtra. Higher dependence on these regions along with excess capacity overhang remains a concern in AP/Telangana leading to increased price volatility in these markets. OCL faces the risk of regional concentration and presence in over supply market which may result in lower than peer valuations.

Promoters have pledged 19.39% of their holding.

Costs rise in H2 could bring pressure on margins

Higher pet coke prices should lead to a 10-15% increase in energy costs for the industry, though its usage may come down in favour of coal. There was a salary cut of 10-15% in H1 for top management which has been restored from 1st October. Other operating expenses such as ad spend, marketing expense and maintenance expense should increase in H2.

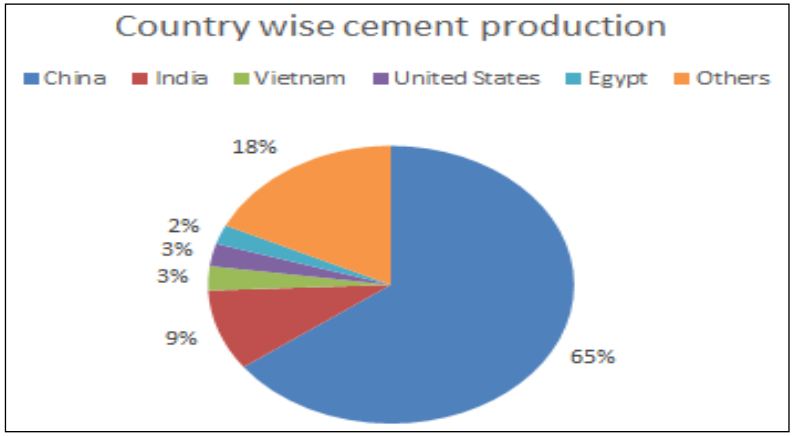
About the Company

Orient cement is a part of CK Birla Group. It established in 1979 as a part of Orient Paper & Industries which was demerged in the year 2012. Orient Cement began cement production in the year 1982 at Devapur in Adilabad District, Telangana. In 1997, a split-grinding unit was added at Nashirabad in Jalgaon, Maharashtra. The company's cement plants have an aggregate installed capacity of 8 mtpa are located at Telangana, Maharashtra and Karnataka. The company sells cement under the brand name of 'Birla A1' and 'Birla A1 StrongCrete'.

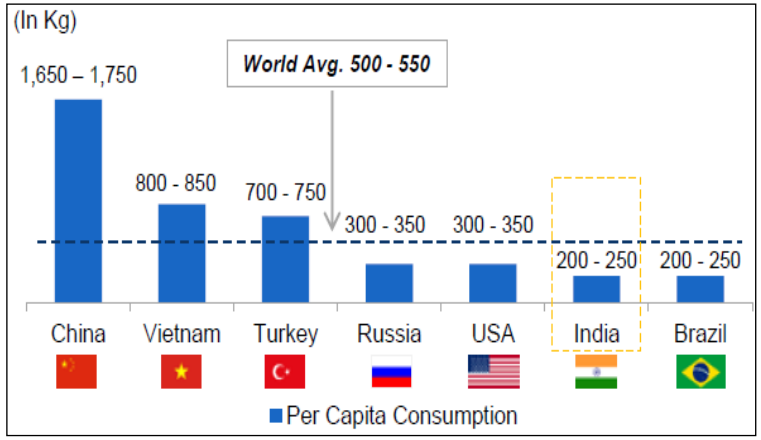
Brands

Industry

India is the second-largest cement producer in world. The cement industry occupies an important place in the Indian economy because of its strong linkages with other sectors such as construction, transportation, coal and power. The sector notably plays a critical role in the economic growth of the country, in its journey towards inclusive and decidedly conclusive growth. The construction sector alone constitutes about 7 per cent of the country's gross domestic product (GDP). India is the second-largest producer of cement in the world after China, with an installed capacity of ~509 MTPA. Presently, the Indian cement industry has 225 plants, owned by 65 players.



Lower per capita cement consumption in India

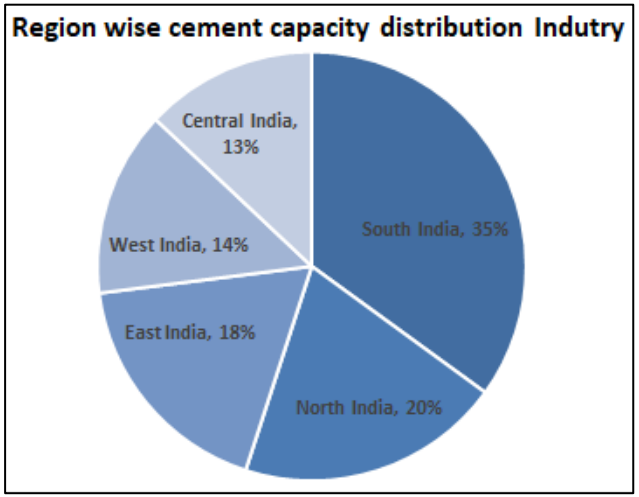


Source – Statista, Shree Cement earning presentation, HDFC sec Research

Although India is among the leading producers of cement in the world, its per capita cement consumption is at 200-250 kg, which is lowest among the developing countries. The world average is 500-580 kg, while countries such as China have a per capita cement consumption of 1650-1750 kg, followed by Vietnam (800-850 kg) and Turkey (700-750 kg). The factors that could trigger cement sales are infrastructural demand especially for Government projects, as well as higher housing demand in rural and semi-urban areas. A higher realization and rising dispatches are considered to be conducive for higher profits for the cement industry. All efforts are targeted to increase sales and reach the premium segment in prices.

The government also intends to expand the capacity of the railways and the facilities for handling and storage to ease the transportation of cement and reduce transportation costs. The demand for the cement industry is expected to reach 550-600 million tonnes per annum by 2025 because of the expanding demand of different end users i.e. housing, commercial construction and industrial construction. Government thrust on affordable housing for realizing its vision of "Housing for All" by 2022 and Smart City program should also help in demand growth for cement. The rate of new cement capacity additions has also slowed down considerably. Therefore, the outlook for the cement sector looks better.

Cement, being a bulk commodity, is a freight intensive industry and long-distance transportation can prove to be uneconomical. This has resulted in cement being largely a regional play with the industry divided into five main regions viz. north, south, west, east and the central region. Cement is relatively a highly concentrated industry in India: I) the top 10 companies constitute> 60% of the market; ii) the top 5 companies enjoy a market share of around > 48%, and iii) the top 2 cement groups (Lafarge Holcim and Aditya Birla Group) enjoy a market share of around 38%.



Source – Company, HDFC sec Research

Peer Comparison as per FY20 Financial

Company	CMP (As on 16-12-2020)	Mcap (Rs. Cr.)	Capacity (MTPA)	OPM%	NPM%	RoE%	RoCE%	D/E(x)	TTM P/E (x)	TTM EV/T ($)	EBIDTA/T (Rs.)
Orient Cement	77	1573	8.0	16	4	8	11	1.0	16	45	659
ACC	1633	30691	33.4	15	9	12	17	0.0	25	106	781
Ambuja Cement	247	49095	29.7	17	8	9	17	0.0	17	178	897
Dalmia Bharat	1089	20372	26.5	22	3	2	5	0.5	42	121	1091
Shree Cement	24244	87521	44.4	29	12	13	16	0.2	51	272	1458
The Ramco Cement	856	20156	16.5	21	11	12	13	0.6	33	184	981
Ultratech Cement	5114	147594	114.8	22	9	12	14	0.7	24	200	1141
India Cements	151	4673	15.6	12	1	1	4	0.7	54	66	530
Heidelberg Cement	212	4802	6.26	24	12	22	28	0.2	20	97	1122
Birla Corp	728.1	5606	15.6	19	7	11	11	0.8	11	84	962
JK Cement	1941	15003	17.1	21	8	17	15	1	27	137	1186
JK Lakshmi Cement	338	3981	13.3	17	6	15	17	0.7	14	55	732

Company	Regions wise Presence				
	North	West	South	East	Central
Ambuja Cement	Y	Y	Y	Y	Y
The Ramco Cement			Y	Y	
Ultratech Cement	Y	Y	Y	Y	Y
ACC	Y	Y	Y	Y	Y
Dalmia Bharat			Y	Y	Y
Shree Cement	Y	Y	Y	Y	Y
India Cements		Y	Y		
Heidelberg Cement					Y
JK Lakshmi Cement	Y	Y		Y	
JK Cement	Y	Y	Y		
Birla Corp	Y	Y		Y	Y
Orient Cement		Y	Y		Y

Financials

Income Statement

(Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
Net Revenue	**2222**	**2522**	**2422**	**2203**	**2521**
Growth (%)	18.5	13.5	-4.0	-9.1	14.5
Operating Expenses	1917	2210	2039	1782	2115
EBITDA	**305**	**312**	**383**	**420**	**406**
Growth (%)	**71.4**	**2.2**	**22.7**	**9.7**	**-3.3**
EBITDA Margin (%)	**13.7**	**12.4**	**15.8**	**19.1**	**16.1**
Other Income	20.2	14.0	17.7	16.7	25.0
Depreciation	126.2	132.7	140.9	139.9	147.2
EBIT	**199**	**193**	**260**	**297**	**284**
Interest	129.2	118.5	122.3	111.4	108.3
Exceptional Items	0.0	0.0	0.0	0.0	0.0
PBT	**70**	**75**	**137**	**186**	**176**
Tax	25.8	27.2	50.8	67.7	57.6
RPAT	**44**	**48**	**87**	**118**	**118**
Growth (%)	**-237.7**	**7.5**	**82.1**	**36.1**	**0.3**
EPS	2.2	2.3	4.2	5.8	5.8

Balance Sheet

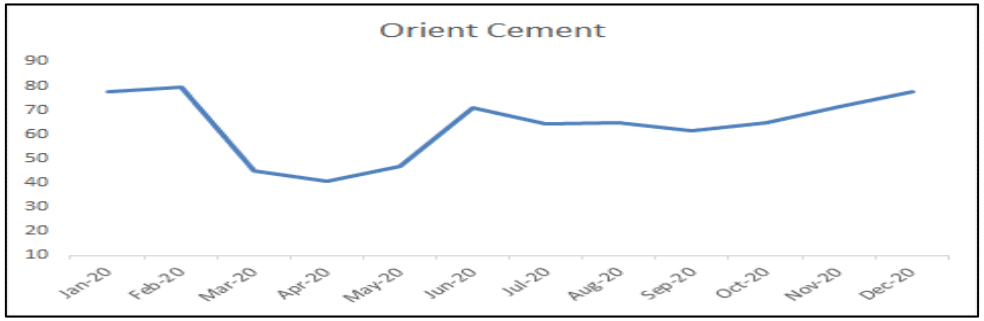
As at March	FY18	FY19	FY20	FY21E	FY22E
SOURCE OF FUNDS					
Share Capital	**20.5**	**20.5**	**20.5**	**20.5**	**20.5**
Reserves	1002	1033	1098	1200	1298
Minority Interest	0	0	0	0	0
Other Equity & Liabilities	0	0	0	0	0
Shareholders' Funds	**1022**	**1054**	**1118**	**1221**	**1319**
Long Term Debt	1138	1226	1135	1067	1094
Long Term Provisions & Others	134	139	163	112	186
Total Source of Funds	**2295**	**2419**	**2417**	**2400**	**2598**
APPLICATION OF FUNDS					
Net Block	2409	2402	2338	2405	2672
Non-Current Investments	0	0	0	0	0
Deferred Tax Assets (net)	0	0	0	0	0
Long Term Loans & Advances	72	69	77	81	91
Other Assets	0	0	0	0	0
Total Non-Current Assets	**2481**	**2471**	**2415**	**2486**	**2763**
Current Investments	0	0	0	0	0
Inventories	164	186	237	157	180
Trade Receivables	153	180	162	157	180
Short term Loans & Advances	103	58	46	47	49
Cash & Equivalents	33	29	36	81	62
Other Current Assets	3	4	4	4	4
Total Current Assets	**456**	**456**	**485**	**446**	**474**
Short-Term Borrowings	124	5	0	25	25
Trade Payables	200	187	176	151	185
Other Current Liab & Provisions	288	283	264	306	371
Short-Term Provisions	30	34	42	49	58
Total Current Liabilities	**642**	**508**	**483**	**531**	**639**
Net Current Assets	-186	-52	2	-86	-165
Total Application of Funds	**2295**	**2419**	**2417**	**2400**	**2598**

Orient Cement Ltd.

Cash Flow Statement

(Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
Reported PBT	70	75	137	186	176
Non-operating & EO items	-20	-14	-18	-17	-25
Interest Expenses	129	119	122	111	108
Depreciation	126	133	141	140	147
Working Capital Change	6	-138	-47	132	61
Tax Paid	-26	-27	-51	-68	-58
OPERATING CASH FLOW (a)	**285**	**146**	**285**	**484**	**410**
Capex	-139	-124	-71	-215	-414
Free Cash Flow	146	22	215	270	-4
Investments	-15	3	-8	-4	-10
Non-operating income	20	14	18	17	25
INVESTING CASH FLOW (b)	**-134**	**-108**	**-61**	**-202**	**-399**
Debt Issuance / (Repaid)	-41	93	-67	-119	100
Interest Expenses	-129	-119	-122	-111	-108
FCFE	-24	-3	25	39	-12
Share Capital Issuance	0	0	0	0	0
Dividend	-15	-62	-15	-15	-20
FINANCING CASH FLOW (c)	**-186**	**-88**	**-205**	**-246**	**-29**
NET CASH FLOW (a+b+c)	**-34**	**-49**	**20**	**37**	**-18**

One Year Price Chart



Key Ratios

(Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
Profitability (%)					
EBITDA Margin	13.7	12.4	15.8	19.1	16.1
EBIT Margin	9.0	7.7	10.7	13.5	11.3
APAT Margin	2.0	1.9	3.6	5.3	4.7
RoE	4.4	4.6	8.0	10.1	9.3
RoCE	8.7	8.0	10.7	12.4	10.9
Solvency Ratio					
D/E	1.2	1.2	1.0	0.9	0.8
Interest Coverage	1.5	1.6	2.1	2.7	2.6
PER SHARE DATA					
EPS	2.2	2.3	4.2	5.8	5.8
CEPS	8.3	8.8	11.1	12.6	13.0
BV	50	51	55	60	64
Dividend	0.8	0.8	0.8	0.8	1.0
Turnover Ratios (days)					
Debtor days	25	26	24	26	26
Inventory days	26	25	32	26	26
Creditors days	38	32	32	31	32
Working Capital Days	12	19	24	21	20
VALUATION					
P/E	35.6	33.1	18.2	13.3	13.3
P/BV	1.5	1.5	1.4	1.3	1.2
EV/EBITDA	8.6	8.4	6.9	6.3	6.5
Dividend Yield	1.0	1.0	1.0	1.0	1.3
Dividend Payout	1.7	32.3	17.7	13.0	17.3

Source: Company, HDFC sec Research

Disclosure:

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