

Sanghi Industries

22 May 2019

Reuters: SNGI.NS; Bloomberg: SNGI IN

Weakness Continues, Challenges Unabated

Sanghi Industries' (SNGI) performance in 4QFY19 was steady with revenue growth of 9% YoY at Rs2.8bn as volume jumped 13%. Realisation, however, fell 4% YoY to Rs3,866/tn as dominant sales (~68%) were in the non-trade segment (adjusted to ready-mix concrete revenues of Rs69mn). SNGI's key market continues to be Gujarat with 83% of sales volume contributed by the state. Cement volume jumped 13% YoY (including domestic and export cement sales and small quantity of clinker sales) to 0.70mt in 4QFY19. Operating costs were well controlled, staying flat YoY at Rs3,304/tn, largely because of lower energy and logistic costs. However, this was negated by the jump in other expenditure by 75% to Rs298mn driven by higher advertising and technology-related expenses. Effectively, EBITDA margin declined by 270bps to 16.7% from 19.4% in 4QFY18 as EBITDA fell ~7% YoY to Rs460mn. EBITDA/tn fell 17% YoY to Rs661/tn (higher than our estimate of Rs618/tn). Depreciation provision declined following a change in the policy (redefined life of assets) to Rs134mn (Rs45mn lower as the effect of change) versus Rs185mn in 4QFY18. Adjusted PAT, consequently, was flat at Rs264mn compared to Rs266mn (FY19 fall was ~95% at Rs526mn versus Rs1.01bn in FY18). Following the continued weak performance (4Q performance could have been better) and factoring in the challenging business environment continuing for SNGI, we have retained our FY20/FY21 EPS estimates at Rs2.5/Rs3.1, respectively. We continue to value SNGI at Rs3.7bn/mt, ~50% lower to the replacement cost of Rs7.5bn/mt, to arrive at a fair valuation. The incremental discount is because of the continued disappointing performance by SNGI (especially on weak volume growth), challenges from new markets like Mumbai that SNGI plans to tap aggressively and cost inflation. Further, the planned capital expenditure will impact the balance sheet with a peak debt of ~Rs12.5bn. We have retained Sell rating on the stock with a target price of Rs43.

Volume drives revenue realisation drop: Cement volume grew 13% YoY to ~0.70mt including a small quantity of clinker sales (6,500tn) and export of 5,900tn in 4QFY19. However, in FY19 the volume grew only 5% to 2.63mt despite the addition of Mumbai market following the availability of ships. Following higher non-trade exposure (65%-68% of total sales) realisation (adjusted to RMC revenues of Rs69.0mn) fell ~5% YoY/flat QoQ at Rs3,885/tn.

Cost inflation contained: With the shift in the fuel (imported coal over lignite) energy costs declined ~8% YoY (adjusted to raw material cost increase by 2.5%). SNGI shifted the fuel from lignite to imported coal (75% of total requirement) because of continued non-availability of lignite from GMDC. Logistics costs fell 7% because of higher near-market sales in 4QFY18. However, this was negated by the jump in other expenditure by 75% to Rs298mn driven by higher advertisement and technology-related expenses. Overall operating costswere flat (marginal decline of 0.5%) at Rs3,304/tn. With a 4% fall in realisation, the EBITDA margin fell to 16.7% from 19.4% in 4QFY18. However, the margin improved from a low of 12.1% in 3QFY19.

Retain our estimates: Following the weak yearly performance (earnings down by 95% YoY) and the continued challenging business environment, we have retained our FY20/FY21 EPS estimates at Rs2.5/Rs3.1, respectively, despite a marginal improvement in the performance of SNGI in 4QFY19. Penetration in new markets will be challenging, logistic cost will be volatile and severe completion in the home state of Gujarat will impact SNGI's performance. The company continues to disappoint on the volume growth front. Hence, we expect EBITDA margin to be in the ~15%/16% range in FY20/FY21.

Outlook: We have valued SNGI at Rs3.7bn/mt (from Rs4.3bn/mt earlier), ~50% lower to the replacement cost of Rs7.5bn/mt, to arrive at a fair valuation. The incremental discount is because of continued disappointing performance by SNGI, challenges from new markets like Mumbai that SNGI plans to tap and cost inflation. Further, the planned capital expenditure will impact its balance sheet with a peak debt of ~Rs12.5bn. We have retained our Sell rating on the stock with a target price of Rs43.

Y/E March (Rsmn)	4QFY19	4QFY18	YoY %	3QFY19	QoQ %
Net sales	2,760	2,536	8.8	2,661	3.7
Operating expenses	2,299	2,044	12.5	2,338	(1.7)
EBITDA	460	493	(6.6)	322	42.8
EBITDA margin (%)	17	19	(274bps)	12	456bps
Other income	74	131	(43.5)	55	34.2
Interest costs	136	173	(21.4)	147	(7.5)
Depreciation	134	185	(27.4)	187	(28.2)
PBT	264	266	(0.6)	44	499.1
Non-recurring items	-	(80)	-	-	-
PBT (after non-recurring items)	264	186	42.1	44	499.1
Tax	-	-	-	-	-
Reported PAT	264	266	(0.6)	44	499.1
Adjusted PAT	264	266	(0.6)	44	499.1
NPM (%)	9.6	10.5	(91bps)	1.7	792bps
Adjusted EPS (Rs)	1.1	1.1	(0.6)	0.2	499.1

Source: Company, Nirmal Bang Institutional Equities Research

SELL

Sector: Cement

CMP: Rs63

Target Price: Rs43

Downside: 32%

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Key Data

Current Shares O/S (mn)	251.0
Mkt Cap (Rsb/US\$m)	15.7/224.6
52 Wk H / L (Rs)	102/50
Daily Vol. (3M NSE Avg.)	103,726

Price Performance (%)

	1 M	6 M	1 Yr
Sanghi Industries	2.8	(0.2)	(36.1)
Nifty Index	1.0	11.2	11.1

Source: Bloomberg

Key conference-call takeaways

- Sales of PPC cement increased to 36% in 4QFY19 from 31% in 4QFY18. SNGI sold 33% of PPC cement in 3QFY19. Trade sales, however, continued to be lower, ~32%-35%, impacting the realisation.
- SNGI has shifted towards imported coal as a key fuel over lignite because of non-availability and quality problems. Currently, SNGI uses 75% (27% in 4QFY18) of imported coal as fuel and 25% lignite. This has also helped the company push higher blended cement sales compared to FY18.
- SNGI holds three to four months of coal inventory to guard itself from uncertainty and price volatility. This has taken the inventory higher, thus impacting the working capital cycle.
- SNGI's logistics is mainly through roadways and there is no rail transport. Near-market sales helped the company with savings in logistic costs in 4QFY19. However, this cannot be factored in as sustainable because of varying demand-supply dynamics in nearby markets.
- The 4mt brownfield expansion project work is on schedule and is expected to be completed by March 2020 (the grinding units in Surat and Kutch may be completed in 1HFY21). Around Rs6bn was spent on expansion in FY19. Land acquisition has been completed in Surat and 80% of the civil work is complete.
- The current debt of the company is Rs8.1bn including working capital loans. The company is expected to spend another Rs6bn for project completion.

Exhibit 1: Operational details

(Rs)	4QFY19	4QFY18	YoY %	3QFY19	QoQ %	4QFY19E	Deviation %
Volume (mmt)	0.70	0.62	13.2	0.67	4.7	0.69	0.4
Cement realisation (Rs/mt)	3,866	4,026	(4.0)	3,897	(0.8)	3,885	(0.5)
Operating costs (Rs/mt)*	3,304	3,323	(0.6)	3,516	(6.0)	3,361	(1.7)
EBITDA (Rs/mt)	661	801	(17.4)	485	36.4	618	7.0

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Detailed quarterly financials

(Rsmn)	4QFY19	4QFY18	YoY %	3QFY19	QoQ %	4QFY19E	Deviation %
Net sales	2,760	2,536	8.8	2,661	3.7	2,759	-
Expenditure							
Change in stock	16.7	(70.4)		221.1	(92.4)	(95.0)	
Raw material costs	251.5	230.2	9.2	217.4	15.7	246.2	2.1
Purchased products	-	-	-	-	-	-	-
Power & fuel expenses	701.5	678.8	3.3	686.5	2.2	842.5	(16.7)
Freight costs	928.3	883.6	5.1	937.7	(1.0)	991.6	(6.4)
Employee costs	103.4	150.9	(31.5)	85.0	21.6	110.0	(6.0)
Other expenses	298.1	170.7	74.6	190.5	56.5	235.0	26.8
Total operating expenses	2,299	2,044	12.5	2,338	(1.7)	2,330	(1.3)
EBITDA	460	493	(6.6)	322	42.8	429	7.3
EBITDA margin (%)	16.7	19.4	(274bps)	12.1	456bps	15.5	114bps
Other income	74	131	(43.5)	55	34.2	55	34.2
Interest	136	173	(21.4)	147	(7.5)	157	(13.6)
Depreciation	134	185	(27.4)	187	(28.2)	190	(29.5)
PBT	264	266	(0.6)	44	499.1	137	93.4
Non-recurring items	-	(80)	-	-	-	-	-
PBT (after non-recurring items)	264	186	42.1	44	499.1	137	93.4
Tax	-	-	-	-	-	-	-
Reported PAT	-	-	-	-	-	-	-
Adjusted PAT	264	266	(0.6)	44	499.1	137	93.4
NPM (%)	264	266	(1bp)	44	499bps	137	93bps
Adjusted EPS (Rs)	9.6	10.5	(91)	1.7	792	5.0	462.4

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Trend in operating costs/mt

Costs per mt (Rs)	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	YoY %	QoQ %
Raw material costs	163	149	211	416	260	173	248	659	385	48.3	(41.6)
Power and fuel costs	861	1,037	958	822	1,104	1,228	1,292	1,032	1,008	(8.7)	(2.4)
Freight costs	1,184	1,412	1,253	1,133	1,437	1,445	1,390	1,410	1,334	(7.2)	(5.4)
Total costs per mt	2,613	3,336	3,324	2,991	3,323	3,455	3,528	3,516	3,304	(0.6)	(6.0)

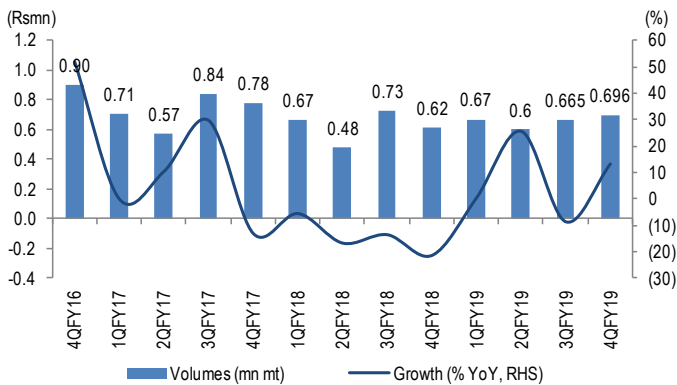
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Our estimates remain unchanged

(Rsmn)	Old		New		Variance (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Net sales	11,742	13,638	11,742	13,638	-	-
Operating profit	1,867	2,184	1,867	2,184	-	-
Net profit	662	771	662	771	-	-
EPS (Rs)	2.6	3.1	2.6	3.1	-	-
Target price (Rs)		43		43		
Rating		Sell		Sell		

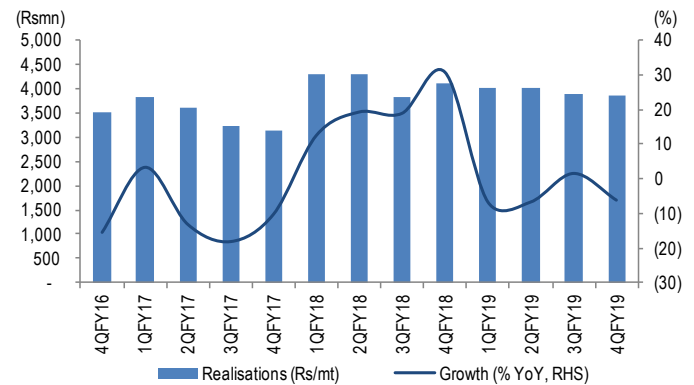
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Volume gain in a traditionally strong quarter



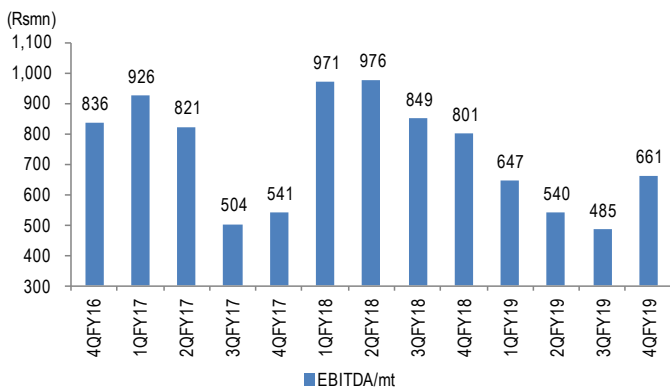
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Dent in realisation because of higher non-trade sales



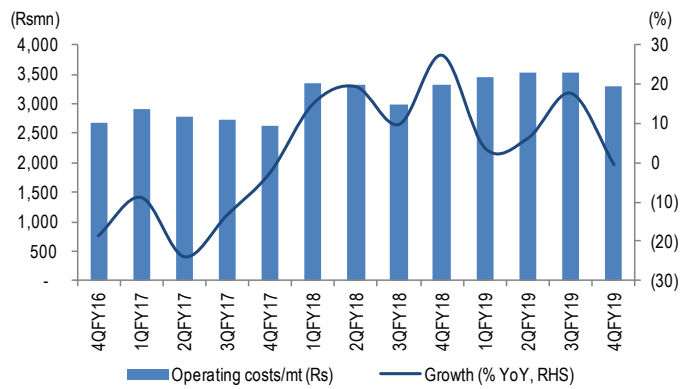
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: EBITDA/tn continues to remain in a lower trajectory



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Cost inflation contained on the back of lower energy and logistic costs



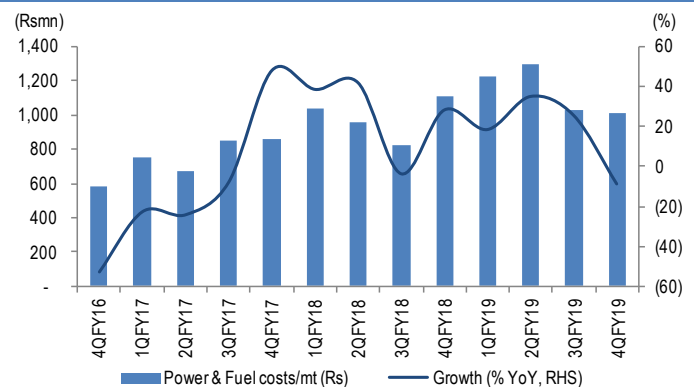
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: Logistics cost decline because of near-market sales



Source: Company, Nirmal Bang Institutional Equities Research

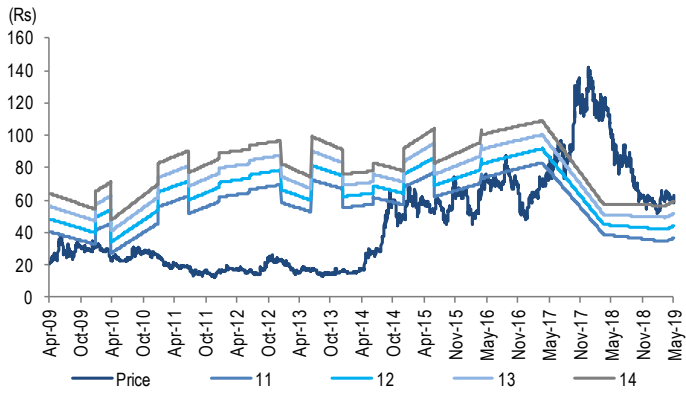
Exhibit 10: Gradual replacement of imported fuel helps



Source: Company, Nirmal Bang Institutional Equities Research

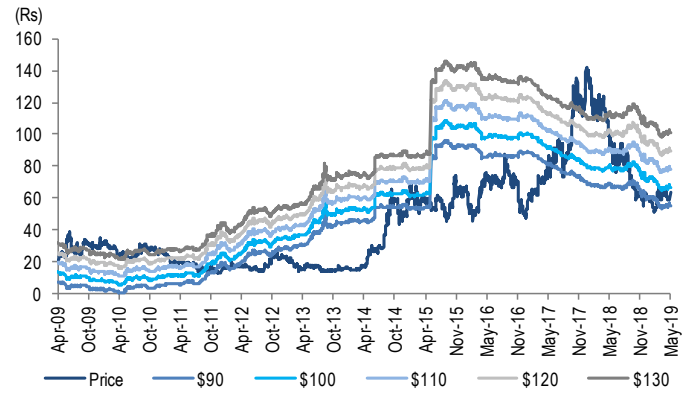
Exhibit 11: Valuation charts

EV/EBITDA



Source: Company, Nirmal Bang Institutional Equities Research

EV/tn



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 12: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19P	FY20E	FY21E
Net sales	9,975	10,264	10,610	11,742	13,638
Growth (%)	(1.8)	2.9	3.4	10.7	16.1
Operating expenses	(7,993)	(8,106)	(9,069)	(9,875)	(11,454)
EBITDA	1,982	2,158	1,540	1,867	2,184
Growth (%)	(1.7)	8.9	(28.6)	21.2	16.9
Depreciation & amortisation	(731)	(644)	(713)	(770)	(791)
EBIT	1,274	1,734	1,100	1,378	1,663
Other income	22	220	273	280	270
Interest paid	(642)	(721)	(573)	(650)	(816)
Extraordinary/exceptional items					
PBT	631	1,013	526	727	847
Tax	-	-	-	(65)	(76)
Effective tax rate (%)	-	-	-	(9)	(9)
Net profit	631	1,013	526	662	771
Minority interest	-	-	-	-	-
Reported net profit	631	1,013	526	662	771
Non-recurring items	-	-	-	-	-
Adjusted net profit	631	1,013	526	662	771
Growth (%)	(38.0)	60.5	(48.0)	25.7	16.5

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 14: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19P	FY20E	FY21E
Cash & bank balances	163	4,281	1,667	945	2,781
Other current assets	3,718	3,655	4,452	5,479	6,505
Investments	-	-	-	-	-
Net fixed assets	16,190	18,023	21,452	27,556	27,653
Goodwill & intangible assets	-	-	-	-	-
Other non-current assets	-	-	-	-	-
Total assets	20,071	25,958	27,570	33,981	36,939
Current liabilities	3,522	3,162	2,879	4,739	5,356
Borrowing	5,868	7,138	8,857	12,821	14,371
Other non-current liabilities	(459)	(320)	(670)	(745)	(725)
Total liabilities	8,931	9,980	11,065	16,814	19,001
Share capital	2,200	2,510	2,510	2,510	2,510
Reserves & surplus	8,940	13,468	13,995	14,657	15,428
Shareholders' funds	11,140	15,978	16,505	17,167	17,938
Minority interest	-	-	-	-	-
Total equity & liabilities	20,071	25,958	27,570	33,981	36,939

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 13: Cash flow

Y/E March (Rsmn)	FY17	FY18	FY19P	FY20E	FY21E
Pre-tax profit	631	1,013	526	727	847
Depreciation	728	719	713	770	791
Chg in working capital	(1,153)	(107)	(1,405)	902	(408)
Total tax paid	(65)	(51)	(25)	(210)	(56)
Other operating activities	-	-	-	-	-
Operating CF	141	1,574	(190)	2,189	1,174
Capital expenditure	(1,311)	(2,552)	(4,142)	(6,874)	(888)
Chg. in investments	-	-	-	-	-
Other investing activities	-	-	-	-	-
Investing CF	(1,311)	(2,552)	(4,142)	(6,874)	(888)
FCF	(1,170)	(978)	(4,332)	(4,685)	286
Equity raised/(repaid)	-	3,905	-	-	-
Debt raised/(repaid)	504	1,270	1,718	3,964	1,550
Dividend (incl. tax)	-	-	-	-	-
Other financing activities	(1)	(80)	-	-	-
Financing CF	503	5,095	1,718	3,964	1,550
Net chg. in cash & bank bal.	(667)	4,118	(2,614)	(721)	1,836
Closing cash & bank bal.	163	4,281	1,667	945	2,781

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 15: Key ratios

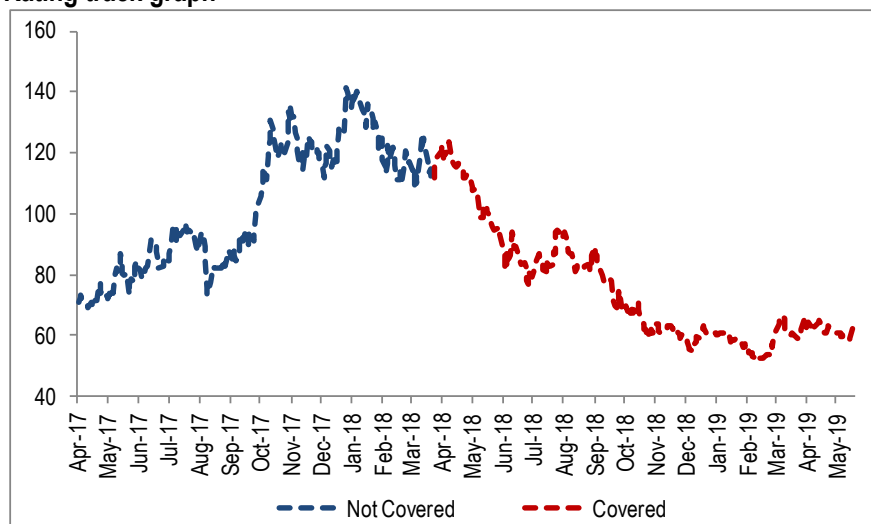
Y/E March (Rsmn)	FY17	FY18	FY19P	FY20E	FY21E
Profitability and return ratios (%)					
EBITDAM	19.9	21.0	14.5	15.9	16.0
EBITM	12.8	16.9	10.4	11.7	12.2
NPM	6.3	9.9	5.0	5.6	5.7
RoE	5.8	7.5	3.2	3.9	4.4
RoCE	7.8	8.8	4.6	5.1	5.5
RoIC	8.1	9.9	5.3	4.9	5.3
Per share data (Rs)					
O/s shares	220.0	251.0	251.0	251.0	251.0
EPS	2.9	4.0	2.1	2.6	3.1
FDEPS	2.9	4.0	2.1	2.6	3.1
CEPS	6.2	6.6	4.9	5.7	6.2
BV	50.6	63.7	65.8	68.4	71.5
DPS	-	-	-	-	-
Valuation ratios (x)					
PE	21.9	15.6	30.0	23.9	20.5
P/BV	1.2	1.0	1.0	0.9	0.9
EV/EBITDA	9.9	7.7	13.7	13.8	11.7
EV/Sales	2.0	1.6	2.0	2.2	1.9
Other key ratios					
D/E (x)	0.5	0.2	0.4	0.7	0.6
DSO (days)	9	11	15	9	11
DuPont analysis - RoE					
NPM (%)	6.3	9.9	5.0	5.6	5.7
Asset turnover (x)	0.5	0.4	0.4	0.4	0.4
Leverage factor (x)	1.8	1.7	1.6	1.8	2.0
RoE (%)	5.8	7.5	3.2	3.9	4.4

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 March 2018	Accumulate	115	116
22 May 2018	Accumulate	98	111
6 June 2018	Accumulate	82	90
8 August 2018	Accumulate	88	91
19 November 2018	Accumulate	63	63
11 February 2019	Sell	53	43
9 April 2019	Sell	61	43
22 May 2019	Sell	63	43

Rating track graph



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