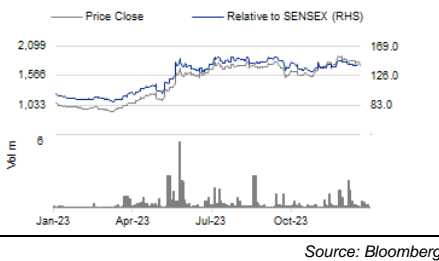


India

HOLD (previously ADD)

Consensus ratings*:	Buy 4	Hold 1	Sell 0
Current price:	Rs1,759		
Target price:	Rs1,800		
Previous target:	Rs2,462		
Up/downside:	2.3%		
InCred Research / Consensus:	-23.1%		
Reuters:	HEG IN		
Bloomberg:	HEG IN		
Market cap:	US\$816m		
	Rs67,872m		
Average daily turnover:	US\$7.2m		
	Rs601.4m		
Current shares o/s:	38.6m		
Free float:	44.2%		
*Source: Bloomberg			



Price performance	1M	3M	12M
Absolute (%)	(0.3)	7.7	68.0
Relative (%)	(0.2)	(2.9)	42.3

Major shareholders	% held
Promoter & Promoter Group	55.8
FII	6.2
Insurance Companies	4.8

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HEG Limited

Concern over utilization of cash on its books

- HEG has a total of Rs7,500m cash on its books, as per Sep 2023 balance sheet. The company has decided to invest Rs2,000m in listed stocks.
- Although the long-term fundamental story remains intact, and we remain quite bullish on the same, the utilization of cash on its books is a cause of concern.
- We retain our earnings estimates for HEG but value it at 1.6x P/BV, instead of 1.8x P/BV earlier. Downgrade its rating to HOLD with a lower TP of Rs1,800.

HEG has healthy cash balance, but utilization is an area of concern

HEG has Rs7,500m of cash on its books as of Sep 2023-end. The company is currently incurring capex for its ~Rs18,000m graphite anode facility. Out of this, Rs10,000m capex has already been incurred from internal accruals. However, HEG is expected to generate a healthy Rs8,000m in cash flow from operations by the end of FY24F owing to declining inventory and a favourable working capital situation. HEG has not taken any debt for its capex plan, funding it entirely via internal accruals, and it won't have any problems in doing so. However, the decision of its management to invest Rs2,000m in listed stocks/ corporate bodies, instead of opting for share buyback/dividends, makes us slightly concerned about the utilization of cash on its books, leading us to downgrade the stock.

Long-term thesis on graphite electrodes remains intact

Graphite electrodes for electric arc furnace or EAF steel mills will be in a structural upcycle in the coming years, as the US, the world's largest EAF-based steel producer, is indulging in significant spending on infrastructure. This, coupled with the EU's ETS scheme, which will be applicable from 2025, will make the operation of blast furnaces in Europe for making steel almost unprofitable. Moreover, HEG has gained a significant market share in the US steel markets from Graftech and has become the largest graphite electrode exporter to US steel mills.

HEG is the only company to set up a graphite anode plant in India

HEG's 20,000mt graphite anode plant will be operational by FY26F. As mentioned in our earlier report, HEG is cost-competitive with China in terms of power costs (Rs5.5/ unit vs. Rs5.9/unit). Secondly, battery supply chain diversification is an important theme, as companies look to diversify their supply chain away from China. Hence, HEG will benefit from the same.

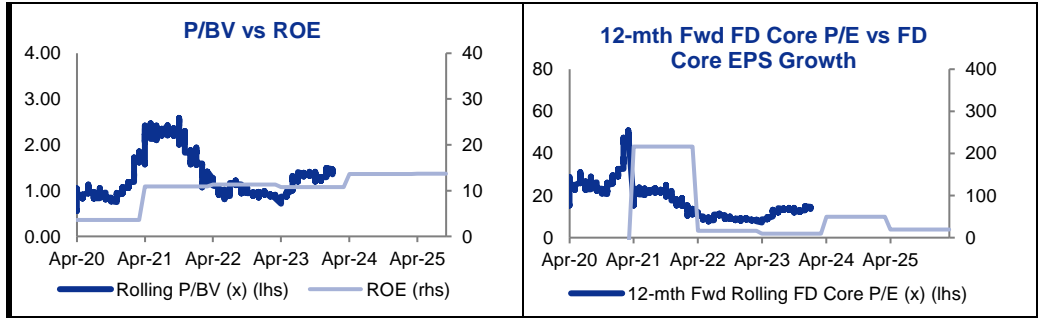
We value HEG at 1.6x P/BV; downgrade rating to HOLD

We retain our earnings estimates for HEG but value it at 1.6x P/BV, instead of 1.8x P/BV earlier. Downgrade its rating to HOLD (from ADD) with a lower target price of Rs1,800 (Rs2,462 earlier). We believe the uncertainty regarding utilization of cash on its books could be an overhang on the stock price, even though the fundamentals are solid. Upside risks: Clarity from HEG's management regarding the proper utilization of cash. Downside risks: Further erosion in its cash balance because of improper utilization of funds.

Financial Summary	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue (Rsm)	22,016	24,672	21,036	29,442	34,914
Operating EBITDA (Rsm)	5,272	6,197	7,363	11,188	13,267
Net Profit (Rsm)	3,906	4,555	4,970	7,421	8,852
Core EPS (Rs)	101.2	118.0	128.8	192.3	229.3
Core EPS Growth	215.8%	16.6%	9.1%	49.3%	19.3%
FD Core P/E (x)	17.37	14.90	13.66	9.15	7.67
DPS (Rs)	3.1	39.9	31.1	31.1	31.1
Dividend Yield	0.18%	2.27%	1.77%	1.77%	1.77%
EV/EBITDA (x)	12.99	11.03	9.46	5.68	4.15
P/FCFE (x)	(161.50)	175.30	13.46	1,364.67	91.65
Net Gearing	1.8%	1.3%	3.7%	(7.2%)	(18.1%)
P/BV (x)	1.80	1.59	1.36	1.15	0.97
ROE	10.9%	11.3%	10.7%	13.6%	13.7%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS



Profit & Loss

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Total Net Revenues	22,016	24,672	21,036	29,442	34,914
Gross Profit	13,726	15,521	13,674	20,021	23,742
Operating EBITDA	5,272	6,197	7,363	11,188	13,267
Depreciation And Amortisation	(793)	(1,023)	(1,456)	(2,013)	(2,185)
Operating EBIT	4,479	5,174	5,907	9,175	11,083
Financial Income/(Expense)	(75)	(260)	(75)	(75)	(75)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	795	1,091	795	795	795
Profit Before Tax (pre-EI)	5,200	6,005	6,627	9,895	11,803
Exceptional Items					
Pre-tax Profit	5,200	6,005	6,627	9,895	11,803
Taxation	(1,294)	(1,450)	(1,657)	(2,474)	(2,951)
Exceptional Income - post-tax					
Profit After Tax	3,906	4,555	4,970	7,421	8,852
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	3,906	4,555	4,970	7,421	8,852
Recurring Net Profit	3,906	4,555	4,970	7,421	8,852
Fully Diluted Recurring Net Profit	3,906	4,555	4,970	7,421	8,852

Cash Flow

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
EBITDA	5,272	6,197	7,363	11,188	13,267
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(5,548)	(3,899)	4,266	(3,734)	(2,931)
(Incr)/Decr in Total Provisions	(3)	(33)	(3)	(3)	(3)
Other Non-Cash (Income)/Expense	(290)	(193)	319	319	319
Other Operating Cashflow					
Net Interest (Paid)/Received	(399)	(768)	(88)	(88)	(88)
Tax Paid	(1,282)	(1,480)	(1,657)	(2,474)	(2,951)
Cashflow From Operations	(2,250)	(177)	10,200	5,209	7,614
Capex	(3,595)	(4,797)	(200)	(200)	(200)
Disposals Of FAs/subsidiaries	9	9	9	9	9
Acq. Of Subsidiaries/Investments	2,612	4,009	(442)	(442)	(2,156)
Other Investing Cashflow	(859)	568	(862)	(862)	(862)
Cash Flow From Investing	(1,834)	(211)	(1,496)	(1,496)	(3,210)
Debt Raised/(repaid)	3,663	775	(3,663)	(3,663)	(3,663)
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(121)	(1,538)	(1,199)	(1,199)	(1,199)
Preferred Dividends					
Other Financing Cashflow	(106)	(236)	(106)	(106)	(106)
Cash Flow From Financing	3,436	(1,000)	(4,969)	(4,969)	(4,969)
Total Cash Generated	(647)	(1,388)	3,736	(1,255)	(565)
Free Cashflow To Equity	(420)	387	5,041	50	741
Free Cashflow To Firm	(4,009)	(128)	8,780	3,788	4,479

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Total Cash And Equivalents	6,017	6,904	5,622	11,684	20,139
Total Debtors	5,899	4,897	4,551	6,366	7,548
Inventories	9,778	14,401	9,778	9,778	9,778
Total Other Current Assets	8,376	2,323	7,879	8,376	8,376
Total Current Assets	30,070	28,525	27,830	36,205	45,841
Fixed Assets	7,484	13,482	18,202	25,163	27,308
Total Investments	3,727	7,428	7,431	7,431	7,431
Intangible Assets	1	3	1	1	1
Total Other Non-Current Assets	10,428	7,482	10,428	5,613	5,613
Total Non-current Assets	21,640	28,394	36,063	38,208	40,353
Short-term Debt	6,634	7,409	7,409	7,409	7,409
Current Portion of Long-Term Debt					
Total Creditors	4,479	4,120	4,034	5,162	6,122
Other Current Liabilities	1,706	1,582	1,706	1,706	1,706
Total Current Liabilities	12,819	13,110	13,150	14,278	15,237
Total Long-term Debt					
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	71	51	45	45	45
Total Non-current Liabilities	71	51	45	45	45
Total Provisions	1,053	949	949	949	949
Total Liabilities	13,943	14,110	14,144	15,272	16,231
Shareholders Equity	37,767	42,809	49,749	59,140	69,962
Minority Interests					
Total Equity	37,767	42,809	49,749	59,140	69,962

Key Ratios

	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue Growth	75.3%	12.1%	(14.7%)	40.0%	18.6%
Operating EBITDA Growth	487.2%	17.5%	18.8%	52.0%	18.6%
Operating EBITDA Margin	23.9%	25.1%	35.0%	38.0%	38.0%
Net Cash Per Share (Rs)	(17.84)	(14.41)	(47.45)	109.59	328.63
BVPS (Rs)	978.68	1,109.04	1,288.83	1,532.13	1,812.50
Gross Interest Cover	59.82	19.90	78.75	122.33	147.77
Effective Tax Rate	24.9%	24.1%	25.0%	25.0%	25.0%
Net Dividend Payout Ratio	3.1%	33.8%	24.1%	16.2%	13.5%
Accounts Receivables Days	72.83	79.76	81.85	67.58	72.65
Inventory Days	343.07	482.21	599.33	378.81	319.44
Accounts Payables Days	155.24	171.48	202.11	178.15	184.33
ROIC (%)	9.4%	10.5%	9.8%	14.2%	16.3%
ROCE (%)	10.7%	10.7%	10.8%	14.6%	15.2%
Return On Average Assets	8.5%	8.7%	8.3%	10.8%	11.1%

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