Equity Research

November 27, 2020

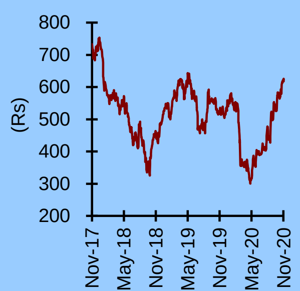
BSE Sensex: 44260

ICICI Securities Limited is the author and distributor of this report

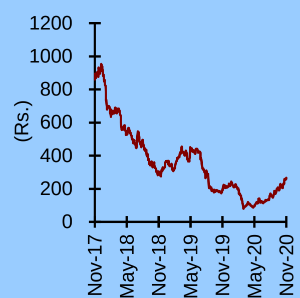
Sector update

Ceramic tiles

Kajaria Ceramics (ADD from Buy)



Somany Ceramics (BUY)



Research Analysts:

Nehal Shah

nehal.shah@icicisecurities.com

+91 22 6637 7235

Jigar Shah

jigar.shah@icicisecurities.com

+91 22 6637 7416

INDIA

ICICI Securities

Ceramic tiles industry

Market share gains sustain for top branded players

Our recent checks suggest that the top branded ceramic tile players have sustained their impressive recovery (witnessed post-Jul'20) into Q3-TD as well. This is largely attributable to market share gains for top branded players with Morbi firms intensifying their focus on exports. Pricing too has remained stable across ceramic, PVT and GVT categories. With Morbi exports likely to sustain their growth momentum in the near to medium term, we expect branded players to continue to gain market share. EBITDA margins too are likely to remain firm as higher operating leverage and product mix improvement offset marginal increase in gas prices.

- **Roll over valuations to Sep'22 earnings.** With improving demand and margin visibility for the top branded players, we now roll over valuations to Sep'22E earnings for our coverage universe. While retaining our revenue and PAT estimates over FY21E-FY23E, we downgrade KJC to **ADD** (from ***Buy*** earlier) with a revised TP of Rs711 (earlier: Rs700) valuing it at 33x Sep'22E earnings, and reiterate **BUY** on SOMC with a revised TP of Rs418 (earlier Rs380) valuing it at 18x Sep'22 earnings.
- **Exports for Morbi players sustain after initial pent-up demand.** Post the lockdown in Apr-May'20, Morbi's monthly exports surged to over Rs10bn in Jul'20 largely driven by pent-up demand. However, with Morbi witnessing a sharp spurt in shipments to the US, UK and Europe – driven by anti-China sentiment and US imposition of anti-dumping duty on Chinese tiles, Morbi's export turnover for the past three months (Aug-Oct'20) has crossed Rs35bn *vs* Rs100bn in FY20. Our interaction with various exporters in Morbi suggests export revenues could touch Rs100bn-120bn in the current fiscal.
- **Volume visibility improves further for branded players.** We expect demand tailwinds to sustain for top branded players like KJC and SOMC in the near to medium term, driven by: a) market share gains from Morbi players; b) sustained growth traction in tier-2 and above cities and towns; and c) recent opening up of demand in tier-1 and metro cities like Ahmedabad, Pune, Chennai, Delhi and Hyderabad. Realisations for both the players are also likely to improve in H2FY21 largely on the back of better product mix. We expect both KJC and SOMC to exhibit impressive revenue CAGRs of 16.1% and 14.5% respectively over FY21E-FY23E.
- **Expect EBITDA margins to remain firm in near term despite marginal increase in gas prices.** Despite marginal increase in gas prices, we expect gross margins for both the companies to improve in H2FY21 largely driven by product mix improvement. EBITDA margins too are likely to remain firm as a result of higher operating leverage and cost-cutting initiatives undertaken by both the companies in the wake of current pandemic. We estimate KJC to report relatively lower EBITDA margin in H2FY21 (18% *vs* 20.2% in Q2FY21) largely due to reversal of employee cost savings post Sep'20. SOMC on the other hand is estimated to maintain its margins at 11.5% levels in H2FY21 due to sustenance of lower employee costs.
- **Balance Sheet strengthening to continue.** Balance sheet of both the companies have seen material improvement post Covid breakout. The robust cash collections and inventory liquidation in the past two quarters has driven impressive free cash from operations (FCF) in H1FY21. Muted capex and likely strong FCF generation in H2FY21 are expected to result in material reduction in debt for SOMC in particular. Higher profitability and sharp debt reduction would lead to sharp improvement in RoCEs for both the companies in FY21E.

Valuation summary

	Reco	EPS (Rs)			P/E (X)			RoCE (%)		
		FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
KJC	ADD	15.2	20.0	23.1	41.4	31.4	27.2	15.8	19.2	20.3
Somany	BUY	9.4	21.1	25.4	28.6	12.7	10.6	6.9	11.7	13.5

Source: I-Sec research

Financial summary – Kajaria Ceramics

Table 1: Profit & loss statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Net Revenues	**28,080**	**25,834**	**30,300**	**34,800**
Operating Expenses	**23,921**	**21,605**	**24,982**	**28,875**
EBITDA	**4,159**	**4,230**	**5,318**	**5,925**
% margins	14.8%	16.4%	17.6%	17.0%
Depreciation & Amortisation	1,081	1,121	1,225	1,308
Gross Interest	195	118	124	98
Other Income	242	192	329	435
Recurring PBT	**3,125**	**3,183**	**4,298**	**4,954**
Less: Taxes	589	802	1,092	1,248
Less: Minority Interest	(18)	(29)	27	30
Net Income (Reported)	**2,553**	**2,410**	**3,180**	**3,675**
Extraordinaries (Net)	-	-	-	-
Recurring Net Income	**2,553**	**2,410**	**3,180**	**3,675**

Source: Company data, I-Sec research

Table 2: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Assets				
Total Current Assets	12,071	15,139	17,364	19,376
of which cash & cash eqv.	2,252	5,887	7,547	7,165
Total Current Liabilities & Provisions	4,594	5,044	5,200	5,993
Net Current Assets	**7,477**	**10,095**	**12,164**	**13,383**
Investments	101	101	101	101
Net Fixed Assets	11,863	11,843	11,868	12,060
Capital Work-in-Progress	266	-	-	-
Goodwill	85	-	-	-
Total Assets	**19,792**	**22,039**	**24,133**	**25,544**
Liabilities				
Borrowings	1,281	1,850	1,700	1,100
Deferred Tax Liability	731	731	731	731
Minority Interest	637	676	702	-
Equity Share Capital	159	159	159	159
Face Value per share (Rs)	1	1	1	1
Reserves & Surplus*	16,984	18,624	20,842	23,555
Less: Misc. Exp. n.w.o.				
Net Worth	**17,143**	**18,783**	**21,001**	**23,714**
Total Liabilities	**19,792**	**22,039**	**24,133**	**25,544**

*Excluding revaluation reserves
Source: Company data, I-Sec research

Table 3: Quarterly trend

(Rs mn, year ending March 31)

	Dec-19	Mar-20	Jun-20	Sep-20
Net revenues	7,413	6,520	2,776	7,125
% growth (YoY)	-2.3%	-20.0%	-60.3%	-0.3%
EBITDA	1,113	934	(76)	1,437
Margin (%)	15.0	14.3	(2.7)	20.2
Other income	51	69	26	48
Extraordinaries (Net)	-	-	-	-
Net profit	615	496	(271)	891

Source: Company data, I-Sec research

Table 4: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Operating Cashflow	**2,819**	**5,172**	**4,405**	**4,983**
Working Capital Changes	(780)	1,017	(409)	(1,601)
Capital Commitments	(1,350)	(750)	(1,250)	(1,500)
Free Cashflow	**689**	**5,439**	**2,746**	**1,881**
Cashflow from Investing Activities	**(98)**	**-**	**-**	**-**
Issue of Share Capital	-	(1,641)	-	-
Inc (Dec) in Borrowings	78	569	(150)	(600)
Dividend paid	(599)	(731)	(935)	(1,664)
Change in Deferred Tax Liability	**(342)**	**-**	**-**	**-**
Chg. in Cash & Bank balance	**(272)**	**3,635**	**1,660**	**(383)**

Source: Company data, I-Sec research

Table 5: Key ratios

(Year ending March 31)

	FY20	FY21E	FY22E	FY23E
Per Share Data (Rs)				
EPS	14.3	15.2	20.0	23.1
Cash EPS	22.9	22.2	27.7	31.3
Dividend per share (DPS)	3.0	4.0	5.0	5.0
Book Value per share (BV)	111.8	122.4	136.5	149.1
Growth (%)				
Net Sales	-5.0	-8.0	17.3	14.9
EBITDA	-7.5	1.7	25.7	11.4
PAT	-2.0	6.2	32.0	15.6
Cash EPS	15.1	-2.8	24.8	13.1
Valuation Ratios (x)				
P/E	44.0	41.4	31.4	27.2
P/CEPS	27.5	28.3	22.7	20.0
P/BV	5.6	5.1	4.6	4.2
EV / EBITDA	23.8	22.7	17.7	15.8
EV / Sales	3.5	3.7	3.1	2.7
Operating Ratios				
Raw Material / Sales (%)	39.1	39.5	41.1	40.9
Employee cost / Sales (%)	11.4	14.0	11.6	12.5
SG&A / Sales (%)	10.5	10.0	9.6	9.6
Other Income / PBT (%)	0.1	0.1	0.1	0.1
Effective Tax Rate (%)	26.6	25.2	25.4	25.2
Working Capital (days)	87.1	78.0	65.0	65.0
Inventory Turnover (days)	66.6	58.0	55.0	55.0
Receivables (days)	51.6	60.0	50.0	50.0
Payables (days)	31.1	40.0	40.0	40.0
Net D/E Ratio (x)	-0.1	-0.2	-0.3	-0.3
Return/Profitability Ratios (%)				
Net Income Margins	8.1	9.3	10.5	10.6
RoACE	17.3	15.8	19.2	20.3
RoAE	13.3	12.9	15.5	16.2
Dividend Payout	22.6	31.9	30.3	26.2
Dividend Yield	0.5	0.6	0.8	0.8
EBITDA Margins	14.8	16.4	17.6	17.0

Source: Company data, I-Sec research

Financial summary - Somany ceramics

Table 6: Profit & loss statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Net Revenues	**16,101**	**15,220**	**17,813**	**19,940**
Operating Expenses	**14,787**	**13,780**	**15,683**	**17,555**
EBITDA	**1,314**	**1,440**	**2,130**	**2,385**
% margins	8.2%	9.5%	12.0%	12.0%
Depreciation & Amortisation	590	615	636	672
Gross Interest	494	394	302	271
Other Income	127	101	89	100
Recurring PBT	**358**	**533**	**1,281**	**1,541**
Less: Taxes	(99)	135	322	388
Add: Profit from share of associates	-	-	-	-
Less: Minority Interest	45	(1)	63	79
Net Income (Reported)	**412**	**398**	**895**	**1,075**
Extraordinaries (Net)	(262)	-	-	-
Recurring Net Income	**150**	**398**	**895**	**1,075**

Source: Company data, I-Sec research

Table 7: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Assets				
Total Current Assets	7,393	8,548	9,564	8,740
of which cash & cash eqv.	201	512	501	657
Total Current Liabilities & Provisions	3,174	4,721	5,145	4,559
Net Current Assets	**4,219**	**3,826**	**4,419**	**4,180**
Investments	341	90	70	27
Net Fixed Assets	7,706	10,234	7,879	9,740
Capital Work-in-Progress	60	-	-	-
Goodwill	73	73	73	73
Total Assets	**12,399**	**14,223**	**12,441**	**14,020**
Liabilities				
Borrowings	4,981	6,060	3,585	4,341
Deferred Tax Liability	413	413	413	413
Minority Interest	941	1,411	1,344	1,226
Equity Share Capital	85	85	85	85
Face Value per share (Rs)	2	2	2	2
Reserves & Surplus*	5,980	6,254	7,015	7,956
Less: Misc. Exp. n.w.o.	-	-	-	-
Net Worth	**6,064**	**6,339**	**7,100**	**8,040**
Total Liabilities	**12,399**	**14,223**	**12,441**	**14,020**

*Excluding revaluation reserves
Source: Company data, I-Sec research

Table 8: Quarterly trend

(Rs mn, year ending March 31)

	Dec-19	Mar-20	Jun-20	Sep-20
Net revenues	4,362	3,561	1,694	4,239
% growth (YoY)	2.4	(31.3)	(56.9)	0.8
EBITDA	403	139	(116)	494
Margin (%)	9.2	3.9	(6.9)	11.7
Other income	31	30	19	40
Extraordinaries (Net)	-	-	-	-
Net profit	104	(93)	(220)	205

Source: Company data, I-Sec research

Table 9: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Operating Cashflow	**576**	**632**	**1,693**	**1,793**
Working Capital Changes	892	1,833	(640)	(346)
Capital Commitments	(1,006)	(300)	(400)	(700)
Free Cashflow	**462**	**2,165**	**653**	**747**
Cashflow from Investing Activities	**342**	**252**	**20**	**43**
Issue of Share Capital	-	-	-	-
Inc (Dec) in Borrowings	(750)	(1,981)	(550)	(500)
Dividend paid	(99)	(124)	(134)	(134)
Change in Deferred Tax Liability	**(154)**	**-**	**-**	**-**
Chg. in Cash & Bank balance	**(200)**	**312**	**(11)**	**156**

Source: Company data, I-Sec research

Table 10: Key ratios

(Year ending March 31)

	FY20	FY21E	FY22E	FY23E
Per Share Data (Rs)				
EPS	5.7	9.4	21.1	25.4
Cash EPS	17.5	23.9	36.1	41.2
Dividend per share (DPS)	2.0	2.5	2.7	2.7
Book Value per share (BV)	165.3	182.9	199.2	218.6
Growth (%)				
Net Sales	-6.3	-4.9	17.0	11.9
EBITDA	-20.2	9.6	47.9	12.0
PAT	-67.6	165.3	124.8	20.1
Cash EPS	-18.3	37.0	51.1	14.1
Valuation Ratios (x)				
P/E	76.0	28.6	12.7	10.6
P/CEPS	15.4	11.2	7.4	6.5
P/BV	1.6	1.5	1.4	1.2
EV / EBITDA	12.3	9.6	6.3	5.3
EV / Sales	1.0	0.9	0.7	0.6
Operating Ratios				
Raw Material / Sales (%)	37.1	43.6	42.9	42.7
Employee cost / Sales (%)	14.9	14.0	13.3	13.3
Other Income / PBT (%)	132.9	19.0	7.0	6.5
Effective Tax Rate (%)	-103.5	25.4	25.2	25.2
Working Capital (days)	99.2	73.0	73.0	73.0
Inventory Turnover (days)	74.9	55.0	55.0	55.0
Receivables (days)	63.8	60.0	60.0	60.0
Payables (days)	39.4	42.0	42.0	42.0
Net D/E Ratio (x)	0.7	0.3	0.2	0.1
Profitability Ratios (%)				
Net Income Margins	1.5	2.6	5.0	5.4
RoACE	6.6	6.9	11.7	13.5
RoAE	3.5	5.4	11.1	12.1
Dividend Payout	66.1	31.1	15.0	12.5
Dividend Yield	0.7	0.9	1.0	1.0
EBITDA Margins	8.2	9.5	12.0	12.0

Source: Company data, I-Sec research

In case of industry/sector reports or a report containing multiple stocks, the rating/recommendation for a particular stock may be based on the last released stock specific report for that company."

This report may be distributed in Singapore by ICICI Securities, Inc. (Singapore branch). Any recipients of this report in Singapore should contact ICICI Securities, Inc. (Singapore branch) in respect of any matters arising from, or in connection with, this report. The contact details of ICICI Securities, Inc. (Singapore branch) are as follows: Address: 10 Collyer Quay, #40-92 Ocean Financial Tower, Singapore - 049315, Tel: +65 6232 2451 and email: navneet_babbar@icicisecuritiesinc.com, Rishi_agrawal@icicisecuritiesinc.com.

"In case of eligible investors based in Japan, charges for brokerage services on execution of transactions do not in substance constitute charge for research reports and no charges are levied for providing research reports to such investors."

New I-Sec investment ratings (all ratings based on absolute return; All ratings and target price refers to 12-month performance horizon, unless mentioned otherwise)
BUY: >15% return; ADD: 5% to 15% return; HOLD: Negative 5% to Positive 5% return; REDUCE: Negative 5% to Negative 15% return; SELL: < negative 15% return

ANALYST CERTIFICATION

I/We, *Nehal Shah, CA; Jigar Shah, CA;* authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. Analysts are not registered as research analysts by FINRA and are not associated persons of the ICICI Securities Inc. It is also confirmed that above mentioned Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months and do not serve as an officer, director or employee of the companies mentioned in the report.

Terms & conditions and other disclosures:

ICICI Securities Limited (ICICI Securities) is a full-service, integrated investment banking and is, inter alia, engaged in the business of stock brokering and distribution of financial products. ICICI Securities Limited is a SEBI registered Research Analyst with SEBI Registration Number – INH000000990. ICICI Securities Limited SEBI Registration is INZ000183631 for stock broker. ICICI Securities is a subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on www.icicibank.com.

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities generally prohibits its analysts, persons reporting to analysts and their relatives from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

Recommendation in reports based on technical and derivative analysis centre on studying charts of a stock's price movement, outstanding positions, trading volume etc as opposed to focusing on a company's fundamentals and, as such, may not match with the recommendation in fundamental reports. Investors may visit icicidirect.com to view the Fundamental and Technical Research Reports.

Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

ICICI Securities Limited has two independent equity research groups: Institutional Research and Retail Research. This report has been prepared by the Institutional Research. The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, target price of the Retail Research.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we would endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the companies mentioned in the report in the past twelve months.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its associates or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts and their relatives have any material conflict of interest at the time of publication of this report.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts or their relatives do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities are engaged in various financial service businesses, they might have financial interests or beneficial ownership in various companies including the subject company/companies mentioned in this report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor ICICI Securities have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on ICICI Securities by any Regulatory Authority impacting Equity Research Analysis activities.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ICICI Securities and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

This report has not been prepared by ICICI Securities, Inc. However, ICICI Securities, Inc. has reviewed the report and, in so far as it includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.