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Ceramic Tiles & Bathware Industry

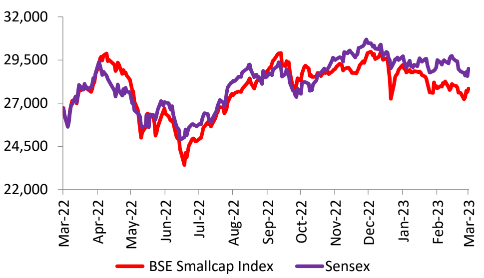
06 March 2023

Leading players gaining market-share with robust cash flows

SECTOR INITIATION REPORT

Industry	Building Materials

BSE Smallcap Index vs. Sensex



Source: BSE, Systematix Institutional Research

Coverage - Rating and target price

Company	Rating	TP (Rs)	Upside (%)
Cera Sanitaryware (CRS)	Initiate with BUY	7,335	16
Kajaria Ceramics (KJC)	Initiate with BUY	1,249	19
Somany Ceramics (SOMC)	Initiate with BUY	605	15
Carysil (CARYSIL)	Maintain BUY	705	25

We initiate coverage on India's ceramic tiles and bathware industry with a constructive view. Factors such as a) low per capita consumption in the segment, b) consumers' rising aspirations and affordability, and c) government's thrust on building smart cities and affordable housing, are the key enablers that would give a thrust to the sector. Kajaria Ceramics (KJC) and Cera Sanitaryware (CRS) have sustained market-share gains without compromising on financial discipline and cash flows (OCF/PAT over 100%). The companies continue to focus on channel expansion and branding. Somany Ceramics (SOMC) on the other hand, despite having faced a tough period during FY17-20 due to industry and company-level issues, has emerged stronger through corrective actions (credit discipline, cash flow focus, etc.). We initiate coverage on CRS, KJC and SOMC with a BUY rating, and reiterate BUY on Carysil (CARYSIL, Rs 705 TP). Price corrections in tiles stocks in last one year (on muted growth and margins; rebound likely 4Q onwards) have rendered KJC (TP: Rs 1.249) and SOMC's (TP: Rs 605) current valuations reasonable at 29x and 14x FY25E EPS, respectively, for a 15-20% return in a year. Even though CRS' stock price (TP: Rs 7,335) has risen ~45% in last one year on superior financial performance, we expect market share gain-driven performance to sustain. Key risks to our call: slowdown in economic and housing activity, keener competition

Industry shows robust prospects: India's ceramic tiles and bathware industry is on a strong footing for long-term sustainable growth (~8% CAGR, per experts). Factors such as a) low per capita consumption in the segment, b) consumers' rising aspirations and affordability, and c) government's thrust on building smart cities and affordable housing are key enablers for the robust expected growth. Leading players will likely witness much higher growth on market share gains, in our view.

Traction in exports from Morbi positive for KJC/SOMC: After a flattish FY22 impacted by COVID-19, exports from India rebounded sharply from Oct'22 with Rs 15.2bn recorded in Dec'22. We attribute the pick up to market share gains arising from production disruption in China (COVID related) and spike in energy costs in key European countries like Italy, Spain, Turkey. Industry estimates India's exports to cross Rs 170bn in FY23, surging 33% YoY. Domestic focused branded players such as KJC and SOMC would benefit immensely from the reducing competition, as Morbi-based manufacturers would be concentrated on meeting the huge export demand.

Reduction in gas cost to drive margins: KJC and SOMC saw huge contractions in their EBITDA margins from their peak in 1QFY22, as gas prices tripled during Sep'20-Mar'22. Power & fuel costs of these companies have surged to over 25% of revenue from 18-20% pre-COVID. A meaningful decline in Morbi gas price (~30% from its Mar'22 peak) along with decline in other regions augurs well for the margins of these companies (should reflect 4QFY23 onwards).

CRS and KJC are cash cows, which SOMC aspires to become: Strict credit policy, healthy margins and asset-light business model have helped CRS and KJC maintain strong cash flows (OCF/EBITDA ~65%, OCF/PAT over 100%) even in a tough business environment. CRS has significantly scaled up its non-sanitaryware business (~45% of revenue currently) in a decade without leverage, which is commendable. SOMC too has adhered to credit discipline, seen from its lower debtor days (42 currently from 90 days in FY19); we expect it to generate healthy cash flow in FY24/25.

Initiate with BUY on CRS (TP: Rs 7,335), KJC (TP: Rs 1,249) and SOMC (TP: Rs 605)

Maintain BUY on CARYSIL (TP: Rs 705, IC report link)

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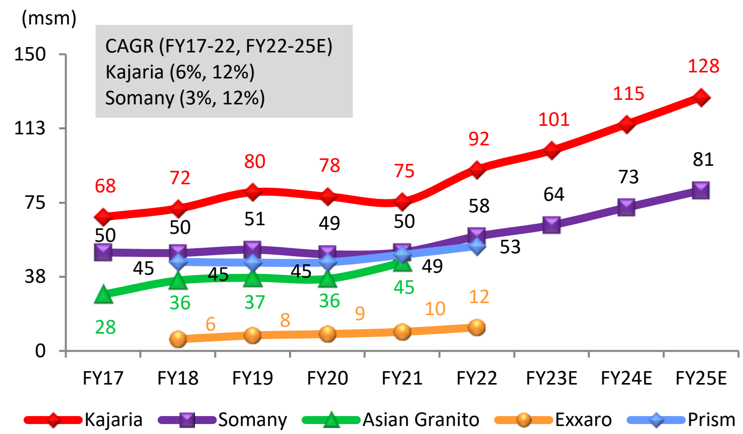


Exhibit 2: Tiles - blended NSR trend (Rs/ sqm)

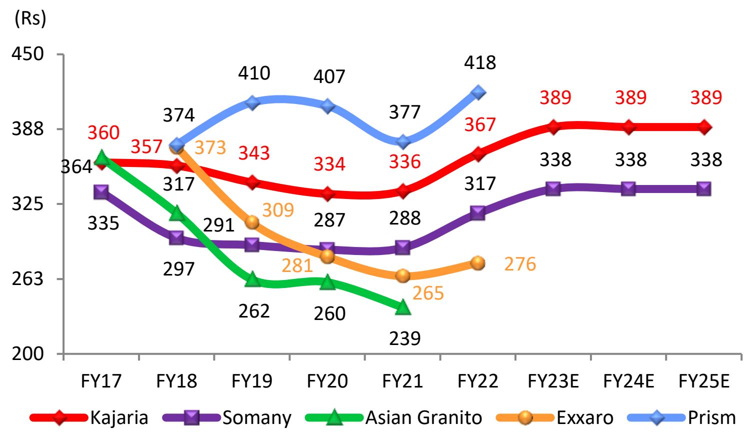


Exhibit 3: Power and Fuel cost (as % of revenue)

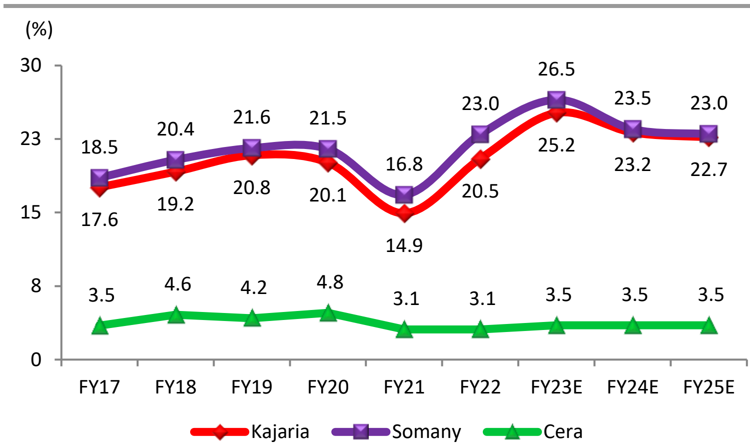


Exhibit 4: Gross margin trend

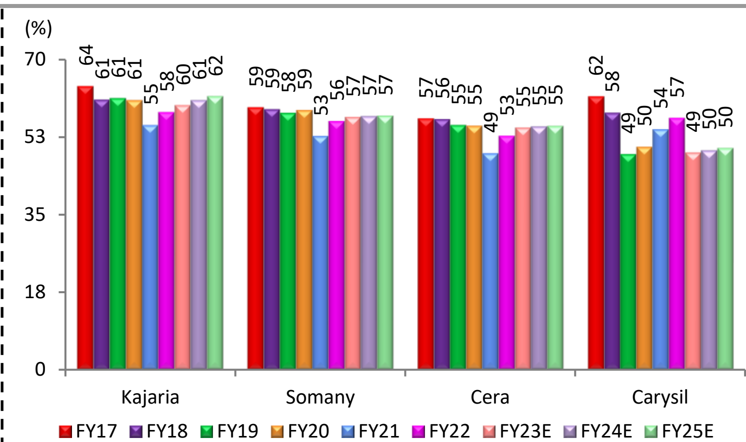


Exhibit 5: EBITDA margin trend

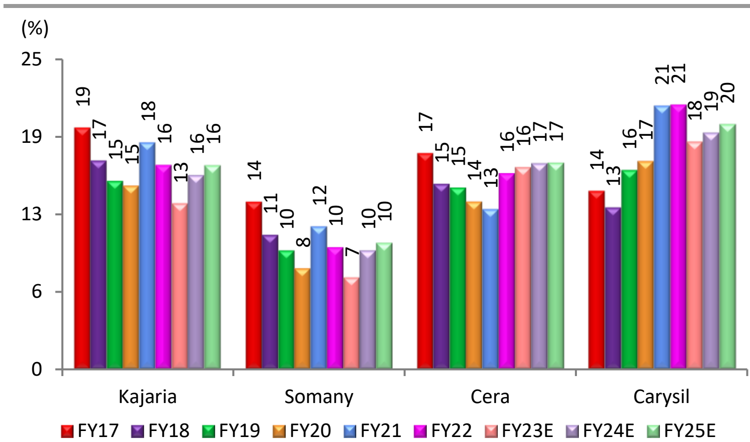
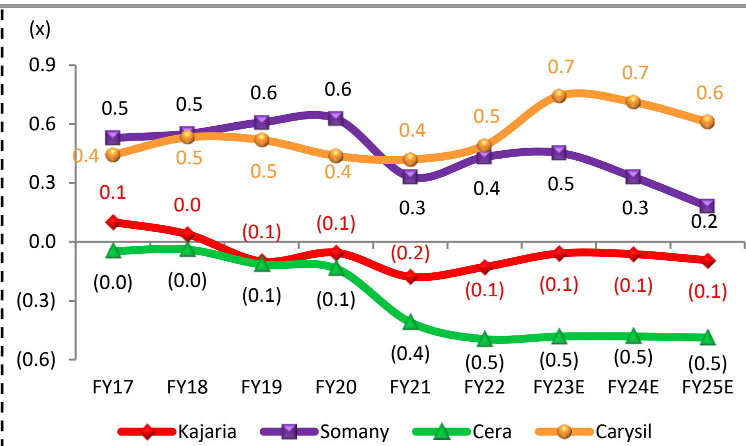


Exhibit 6: Net-Debt/ Equity trend



Source: Company, Systematix Institutional Research

Exhibit 7: Receivables cycle trend

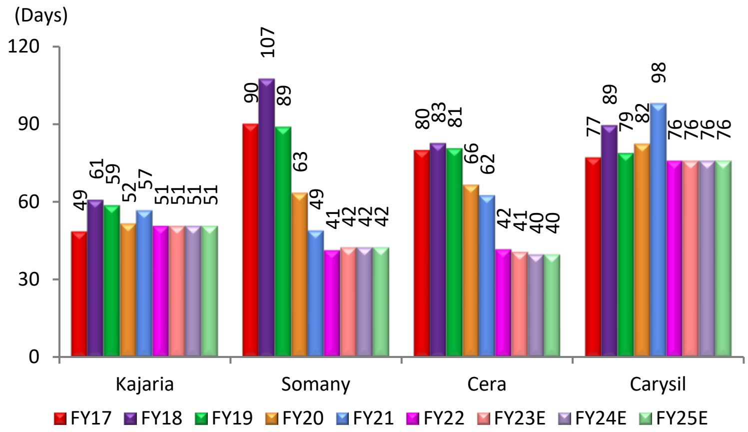


Exhibit 8: RoE trend

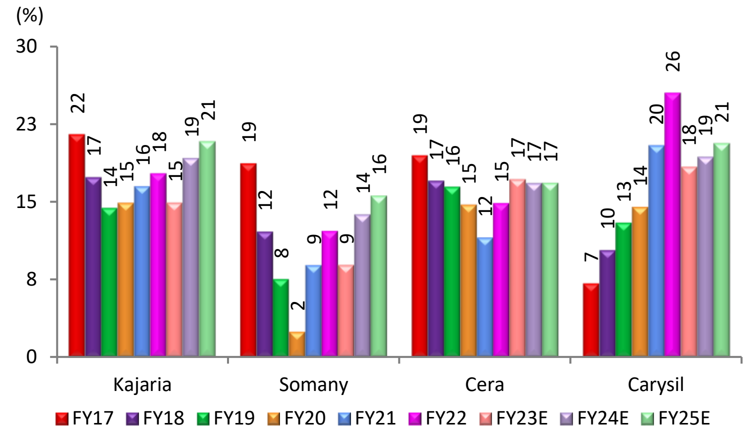


Exhibit 9: RoCE trend

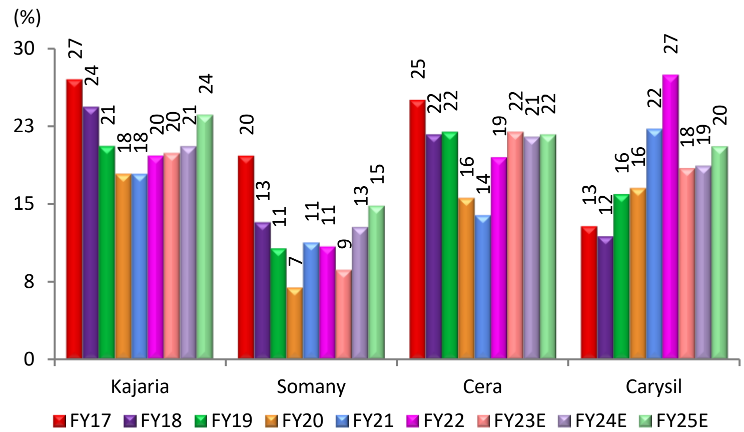


Exhibit 10: RoIC trend

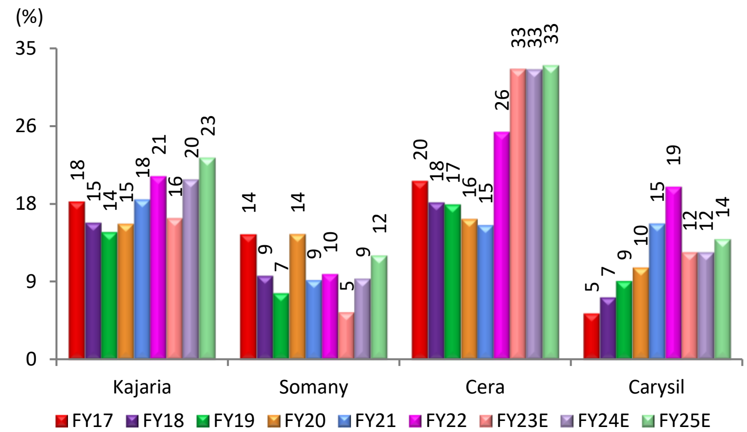


Exhibit 11: OCF/EBITDA (%) trend

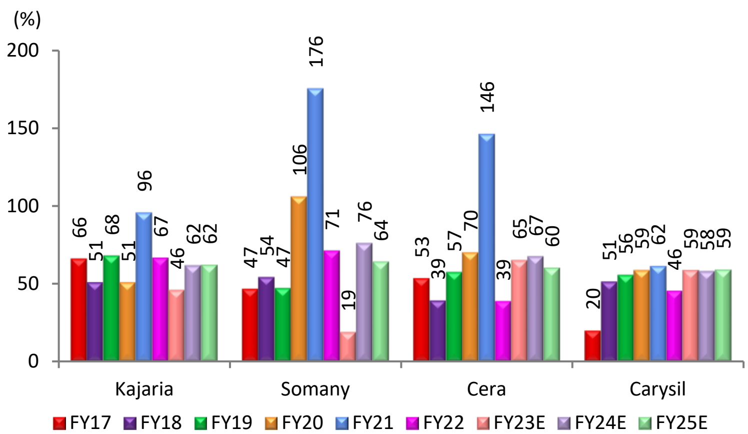
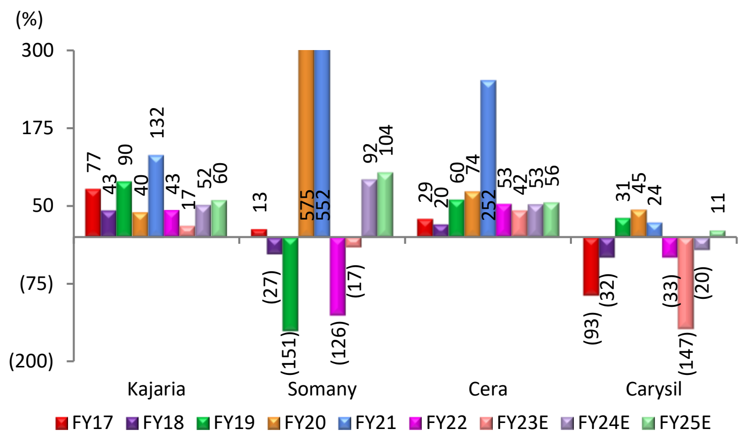


Exhibit 12: FCF/PAT (%) trend



Source: Company, Systematix Institutional Research

Stock Views

CRS (Initiate with BUY, TP: Rs 7,335; 16% upside potential)

We initiate coverage on Cera Sanitaryware (CRS) with a BUY rating and a target price of Rs 7,335, based on 36x FY25E P/E (vs. 34x for KJC). Robust FCFs across business cycles is commendable. Healthy revenue growth and margins, along with strict credit policy should help CRS maintain its OCF/EBITDA and OCF/PAT at robust ~70% and over 100% levels, respectively. A strong ~33% RoIC over FY23-25 will be driven by operational efficiency. Diverse product offerings, an extensive distribution network, a well-established brand recognition, strong financial standing, and expansion plans would enable it to sustain market share gains to achieve healthy growth over the long term. CRS has maintained performance (on the back of market-share gains) even as tiles and other building materials products categories have seen demand moderation in last 2 quarters. Management aims 20%+ revenue CAGR by FY26 from steady demand from home improvement. We estimate strong 17%/21% CAGR in revenue/PAT over FY22-25E (muted 7%/8% CAGR over FY17-22), factoring in continued market share gains by CRS and EBITDA margin expansion (~100bps to 16.7% in FY25E) owing to superior product mix and cost optimisation measures.

CRS – Financial Snapshot (Rs mn)

Y/E Mar	FY23E	FY24E	FY25E
Net sales	17,586	20,217	23,242
EBITDA	2,864	3,361	3,875
OPM (%)	16.3	16.6	16.7
PAT (adj.)	2,028	2,289	2,650
EPS (Rs)	155.9	176.0	203.7
PE (x)	40.4	35.8	30.9
P/B (x)	7.0	6.0	5.2
EV/EBITDA (x)	26.6	22.4	19.1
RoE (%)	17.2	16.8	16.8
RoCE (%)	21.9	21.4	21.6
Net-D/E (x)	(0.5)	(0.5)	(0.5)

KJC (Initiate with BUY, TP: Rs 1,249; 19% upside potential)

We initiate coverage on Kajaria Ceramics (KJC) with a BUY rating and a target price of Rs 1,249, based on 34x FY25E P/E. Our positive view is underpinned by KJC's 1) numero uno position in tiles, 2) execution capabilities, backed by strong management, 3) robust free cash flows (FCF), and 4) focus on market share gains, led by capacity addition and network expansion. While demand has been subdued in last two quarters, owing to extended monsoon and festive season, management expects a rebound from 4Q. Strong demand from the housing sector and shift in volumes to exports by Morbi players augur well for KJC's volumes. We estimate 12%/14% CAGR in volume/revenue over FY22-25E (6%/7% CAGR over FY17-FY22), on a) strong industry tailwinds, b) KJC's regular capacity additions in all regions, c) expansion in dealer network, and d) continued focus on branding. Notwithstanding near-term weakness, we believe KJC's medium to long term outlook to be robust.

KJC – Financial Snapshot (Rs mn)

Y/E Mar	FY23E	FY24E	FY25E
Net sales	43,791	49,805	56,221
EBITDA	5,852	7,801	9,256
OPM (%)	13.4	15.7	16.5
PAT (adj.)	3,370	4,792	5,849
EPS (adj.) (Rs)	21.2	30.1	36.7
PE (x)	49.6	34.9	28.6
P/B (x)	7.4	6.7	6.0
EV/EBITDA (x)	28.3	21.2	17.8
RoE (%)	15.0	19.2	20.8
RoCE (%)	19.9	20.5	23.5
Net-D/E (x)	(0.1)	(0.1)	(0.1)

SOMC (Initiate with BUY, TP: Rs 605; 15% upside potential)

We initiate coverage on Somany Ceramics (SOMC) with a BUY rating and a target price of Rs 605, based on 16x FY25E P/E (vs. 34x for KJC), for a low ~16% RoE in FY25E. The company went through a rough patch during FY17-20 due to industry and company-level issues, post which, it managed to meaningfully improve its financial position by adopting corrective measures (credit discipline, cash flow focus, strengthening operations, and cleaning up its balance sheet). We believe these should trigger a re-rating in its valuation multiples. Large capacity addition in the value-added premium segment should bode well for SOMC to improve its average realisation and margin, and enable the company to reposition itself as a premium tiles brand. SOMC aims to fund future capex mostly through internal accruals. After a low 3%/2% CAGR in volume/revenue over FY17-22 (impacted by industry and company level issues), we estimate 12%/14% CAGR over FY22-25E, as SOMC has realigned its fundamentals and continues to see positive traction from the housing sector. Through improved product mix, higher market share and brand visibility and cost optimisation, SOMC aims to move up the value chain and expand margins. We estimate 15%/22% CAGR in revenue/PAT over FY22-25E (flattish over FY17-22), anticipating ~400bps surge in its EBITDA margin to 10.2% in FY25E. RoE could rise to ~16% with healthy cash flow in FY25E. Notwithstanding the near-term weakness, SOMC's medium-to-long-term prospects are robust.

SOMC – Financial Snapshot (Rs mn)

Y/E Mar	FY23E	FY24E	FY25E
Net sales	24,711	28,134	31,549
EBITDA	1,829	2,702	3,219
OPM (%)	7.4	9.6	10.2
PAT (adj.)	705	1,233	1,606
EPS (adj.) (Rs)	16.6	29.1	37.8
PE (x)	31.6	18.1	13.9
P/B (x)	2.8	2.5	2.2
EV/EBITDA (x)	14.4	9.5	7.6
RoE (%)	8.9	13.8	15.6
RoCE (%)	8.6	12.8	14.8
Net-D/E (x)	0.5	0.3	0.2

CARYSIL (Maintain BUY, TP: Rs 705; 25% upside potential)

CARYSIL – Financial Snapshot (Rs mn)

Y/E Mar	FY23E	FY24E	FY25E
Net sales	6,200	7,627	9,266
EBITDA	1,137	1,455	1,832
OPM (%)	18.3	19.1	19.8
PAT (adj.)	561	715	941
EPS (Rs)	21.0	26.8	35.2
PE (x)	26.9	21.1	16.0
P/B (x)	5.0	4.1	3.3
EV/EBITDA (x)	15.3	12.2	9.8
RoE (%)	18.4	19.3	20.6
RoCE (%)	18.4	18.6	20.5
Net-D/E (x)	0.7	0.7	0.6

We maintain our BUY rating on Carysil (CARYSIL) with a target price of Rs 705, based on 20x FY25E EPS of Rs 35. The scrip has rallied over 10% since our initiation (IC report link) on 22 February 2023, after >40% fall since Apr'22, on fear of global demand slowdown. Impacted by channel de-stocking, the company has been reporting weak performance since 2QFY23. But we expect a strong rebound 4QFY23 onwards, considering its strong order book and volume visibility with large global customers. CARYSIL aspires to become a global one-stop shop for all kitchen and bathroom lifestyle products. Post strong 22%/32%/52% CAGR in revenue/EBITDA/PAT over FY17-22 (on a ~700bps EBITDA margin expansion to ~21% and forex gains), we estimate 24%/21% /13% CAGR over FY22-25E, expecting ~20% EBITDA margin and higher interest costs (rise in debt). Regular capacity addition and working capital needs will likely limit OCF/EBITDA at ~60% level; healthy RoE (~20%) will be maintained though.

Peer Valuation Comparison

Exhibit 13: Valuation Table – 1

	M-cap (Rs bn)	Reco	CMP 03-Mar	TP (Rs)	Upside (%)	T PE 25E (x)	1-yr fwd PE (5-yr)			P/E			RoIC (%)	
							Mean	+1 SD	-1 SD	FY23E	FY24E	FY25E	FY22	FY25E
Tiles/Ceramics														
Carysil	15	Buy	565	705	25	20	17	27	7	27	21	16	19	14
Cera	82	Buy	6,300	7,335	16	36	31	35	28	40	36	31	26	33
Kajaria Ceramics	167	Buy	1,050	1,249	19	34	36	47	26	50	35	29	21	23
Somany Ceramics	22	Buy	525	605	15	16	37	60	13	32	18	14	4	12
Plastic Pipes														
Apollo Pipes	21	Buy	533	650	22	25	31	52	9	93	28	20	13	19
Astral	387	Hold	1,924	1,862	(3)	50	64	86	43	98	62	52	28	38
Finolex Ind	105	Hold	170	181	7	18	17	26	8	49	20	17	28	14
Prince	64	Buy	579	705	22	26	33	57	10	77	27	21	22	24
Supreme	344	Hold	2,705	2,546	(6)	26	27	34	20	44	32	28	33	29
Wood Panel														
Greenpanel	35	Buy	284	455	60	18	14	22	6	15	13	11	21	20
Stylam	19	Buy	1,108	1,585	43	18	15	20	10	20	16	13	18	27
Century Ply	114	NR	514				28	38	18	31	28	24	23	20
Greenlam	37	NR	308				29	35	23	32	34	20	12	10
Greenply	17	NR	137				28	37	18	17	17	10	22	21

Source: BSE, Bloomberg, Systematix Institutional Research

Exhibit 14: Valuation Table – 2

	EPS (Rs)			CAGR (%) (FY17-22)			CAGR (%) (FY22-25E)			RoE (%)		RoCE (%)		EV/EBITDA (x)	
	FY23E	FY24E	FY25E	Rev	EBITDA	PAT	Rev	EBITDA	PAT	FY22	FY25E	FY22	FY25E	FY22	FY25E
Tiles/Ceramics															
Carysil	21	27	35	22	32	52	24	21	13	26	21	27	20	16	10
Cera	156	176	204	7	5	8	17	19	21	15	17	19	22	34	19
Kajaria Ceramics	21	30	37	8	4	8	15	15	16	18	21	20	24	27	18
Somany Ceramics	17	29	38	4	(2)	(2)	15	16	22	12	16	11	15	13	8
Plastic Pipes															
Apollo Pipes	6	19	26	27	25	26	17	23	27	12	18	16	23	21	11
Astral	20	31	37	18	23	27	14	14	16	21	19	29	28	54	35
Finolex Ind	3	8	10	12	13	16	2	(8)	(6)	27	13	26	16	11	13
Prince	8	22	27	16	21	27	9	7	6	20	17	25	21	16	12
Supreme	62	85	97	12	10	18	11	11	8	25	20	29	25	24	17
Wood Panel															
Greenpanel	19	22	25	39	136	164	11	6	9	25	19	27	23	9	7
Stylam	57	71	88	18	18	25	28	31	35	19	23	25	31	18	7
Century Ply	16	19	21	11	11	10	15	12	14	20	18	27	23	21	15
Greenlam	10	9	16	10	6	13	22	27	27	14	19	13	14	22	13
Greenply	8	8	13	14	23	46	20	27	20	18	19	16	20	13	7

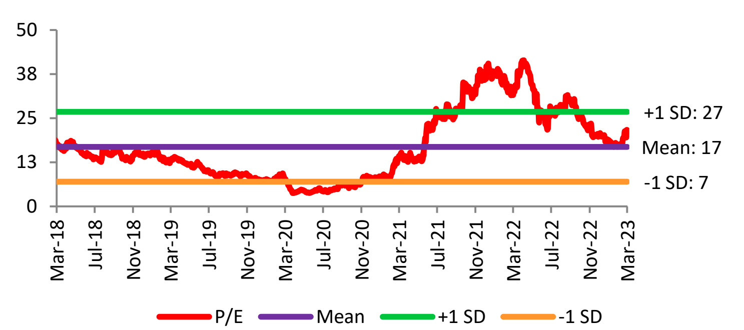
Source: Bloomberg, Systematix Institutional Research

PE Band and Stock Price Performance

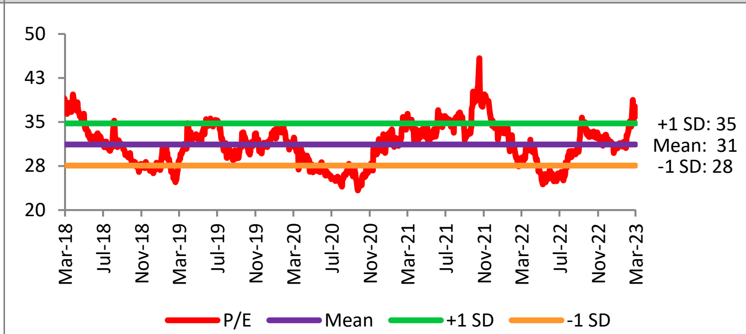
Exhibit 15: PE band and standard deviation (one-year forward)

Tiles/Ceramics

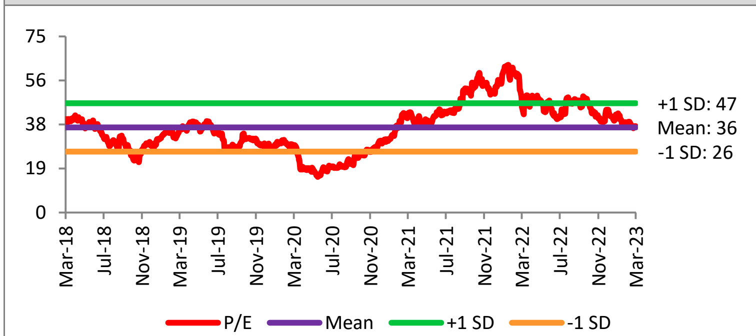
CARYSIL



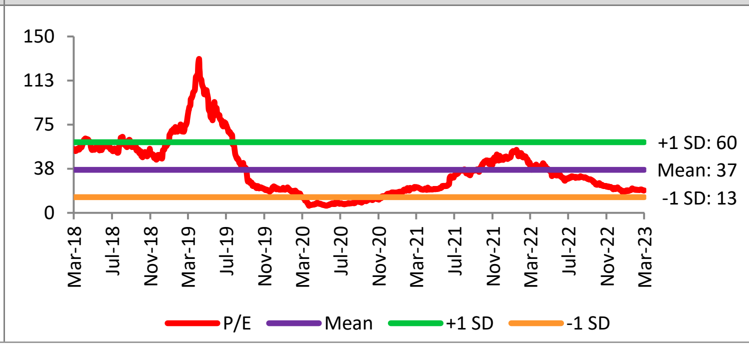
CRS



KJC



SOMC



Source: BSE, Company, Systematix Institutional Research

Exhibit 16: Building Materials - Stock price performance

	1-month	3-month	6-month	12-month	3-years
Tiles/Ceramics					
Carysil	29	14	(20)	(16)	412
Cera	20	18	28	44	152
Kajaria	(1)	(10)	(9)	9	91
Somany	(3)	5	(17)	(22)	206
Pipes					
Supreme	7	11	36	33	108
Apollo Pipes	5	7	(1)	16	287
Finolex Ind.	(1)	8	15	11	54
Prince	(7)	3	(2)	(8)	261
Astral	(7)	(0)	(17)	3	124
Wood Panel					
Stylam	0	(3)	(4)	20	425
Century Ply	(1)	(8)	(23)	(14)	223
Greenlam	(1)	(8)	(10)	(5)	64
Greenply	(3)	(16)	(28)	(20)	8
Rushil	(9)	(15)	(47)	(18)	205
Greenpanel	(12)	(27)	(37)	(41)	504

Source: BSE

Peers Quarterly Performance

Exhibit 17: Ceramic tiles & bathware - Company-wise quarterly results

(Rs mn)	3QFY20	3QFY21	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	YoY (%)	QoQ (%)	Over 3QFY20 (3-year CAGR)
Tiles/Ceramics (consolidated)										
Revenue	15,720	17,282	21,702	22,961	21,344	22,490	23,071	*6*	*3*	14
EBITDA	2,068	3,048	3,375	3,272	2,934	2,601	2,715	*(20)*	*4*	9
EBITDA margin (%)	*13.2*	*17.6*	*15.6*	*14.2*	*13.7*	*11.6*	*11.8*			
PAT	1,072	1,882	2,137	1,814	1,712	1,445	1,547	*(28)*	*7*	13
CARYSIL										
Revenue	732	875	1,280	1,389	1,713	1,392	1,378	*8*	*(1)*	23
EBITDA	123	202	279	282	337	224	250	*(10)*	*11*	27
EBITDA margin (%)	*16.9*	*23.1*	*21.8*	*20.3*	*19.7*	*16.1*	*18.2*			
PAT	68	121	173	164	187	92	121	*(30)*	*30*	21
CRS										
Revenue	3,213	3,098	3,870	4,387	3,958	4,143	4,558	*18*	*10*	12
EBITDA	429	397	611	824	612	660	729	*19*	*10*	19
EBITDA margin (%)	*13.4*	*12.8*	*15.8*	*18.8*	*15.5*	*15.9*	*16.0*			
PAT	284	291	423	521	396	507	564	*33*	*11*	26
Sanitaryware revenue	*1,478*	*1,394*	*2,063*	*2,313*	*2,120*	*2,254*	*2,461*	*19*	*9*	*19*
Faucets revenue	*803*	*868*	*1,336*	*1,458*	*1,365*	*1,417*	*1,504*	*13*	*6*	*23*
KJC										
Revenue	7,413	8,383	10,682	11,018	10,082	10,778	10,911	*2*	*1*	14
EBITDA	1,113	1,818	1,838	1,659	1,536	1,294	1,331	*(28)*	*3*	6
EBITDA margin (%)	*15.0*	*21.7*	*17.2*	*15.1*	*15.2*	*12.0*	*12.2*			
PAT	615	1,189	1,220	958	923	699	743	*(39)*	*6*	6
Power & Fuel cost (Rs/ scm)	*92*	*77*	*123*	*126*	*152*	*141*	*26*	*(79)*	*(82)*	(35)
Tiles volume (mn sqm)	*20*	*23*	*26*	*26*	*23*	*25*	*25*	*(1)*	*2*	*8*
Tiles revenue	*6,837*	*7,582*	*9,616*	*9,999*	*9,089*	*9,743*	*9,839*	*2*	*1*	*13*
Tiles NSR (Rs /sqm)	*334*	*336*	*375*	*385*	*390*	*391*	*387*	*3*	*(1)*	*5*
SOMC										
Revenue	4,362	4,925	5,870	6,168	5,591	6,178	6,224	*6*	*1*	13
EBITDA	403	631	646	507	449	422	406	*(37)*	*(4)*	0
EBITDA margin (%)	*9.2*	*12.8*	*11.0*	*8.2*	*8.0*	*6.8*	*6.5*			
PAT	104	280	322	172	205	147	120	*(63)*	*(19)*	5
Power & Fuel cost (Rs/ scm)	*71*	*76*	*133*	*113*	*159*	*140*	*125*	*(5)*	*(10)*	21
Tiles volume (mn sqm)	*13.3*	*14.9*	*15.6*	*16.1*	*14.3*	*15.9*	*16.2*	*4*	*2*	*7*
Tiles revenue	*3,805*	*4,283*	*5,126*	*5,358*	*4,799*	*5,418*	*5,431*	*6*	*0*	*13*
Tiles NSR (Rs /sqm)	*286*	*288*	*329*	*333*	*337*	*341*	*336*	*2*	*(1)*	*6*

Source: Company, Systematix Institutional Research

Systematix vs. Bloomberg Estimates

Exhibit 18: Ceramic tiles & bathware - Systematix vs. Bloomberg estimate

(Rs mn)	Systematix estimates			Bloomberg estimates			% Var with Systematix		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
CARYSIL									
Total Income	6,200	7,627	9,266	6,206	8,171	9,870	(0)	(7)	(6)
EBITDA	1,137	1,455	1,832	1,085	1,463	1,836	5	(1)	(0)
EBITDA margin (%)	*18.3*	*19.1*	*19.8*	*17.5*	*17.9*	*18.6*			
PAT	561	715	941	559	866	1,141	0	(17)	(18)
CRS									
Total Income	17,586	20,217	23,242	17,283	20,019	22,703	2	1	2
EBITDA	2,864	3,361	3,875	2,817	3,328	3,788	2	1	2
EBITDA margin (%)	*16.3*	*16.6*	*16.7*	*16.3*	*16.6*	*16.7*			
PAT	2,028	2,289	2,650	1,977	2,343	2,736	3	(2)	(3)
KJC									
Total Income	43,791	49,805	56,221	43,681	50,233	57,616	0	(1)	(2)
EBITDA	5,852	8,200	9,256	5,921	7,893	9,433	(1)	4	(2)
EBITDA margin (%)	*13.4*	*16.5*	*16.5*	*13.6*	*15.7*	*16.4*			
PAT	3,370	5,089	5,849	3,512	4,959	6,059	(4)	3	(3)
SOMC									
Total Income	24,711	28,134	31,549	24,247	27,398	30,867	2	3	2
EBITDA	1,829	2,702	3,219	1,880	2,682	3,185	(3)	1	1
EBITDA margin (%)	*7.4*	*9.6*	*10.2*	*7.8*	*9.8*	*10.3*			
PAT	705	1,233	1,606	727	1,235	1,602	(3)	(0)	0

Source: Bloomberg, Systematix Institutional Research

India is the 2nd largest producer & consumer of tiles globally

Industry estimates the Indian tiles, sanitaryware and bathroom fittings market to grow at 8.4% CAGR over FY22-27 to reach USD 12bn. Segments low per capita consumption, consumer's rising aspiration and affordability and government's thrust on building smart cities and affordable housing will be the key enablers. *(Source: company, imarcgroup.com, digitaljournal.com)*

India is the second largest producer and seller of ceramic tiles globally. The country has ~14/11% share in world tile production/consumption, second to China. It is also among top 5 exporters of tiles in the world. As per Industry veterans, ceramic tiles industry is pegged at Rs 520bn of which ~Rs 400bn is domestic market (~50% organised) & rest ~Rs 127bn is exports as on FY22.

Indian tiles market estimated to grow at ~8% CAGR over FY19-27

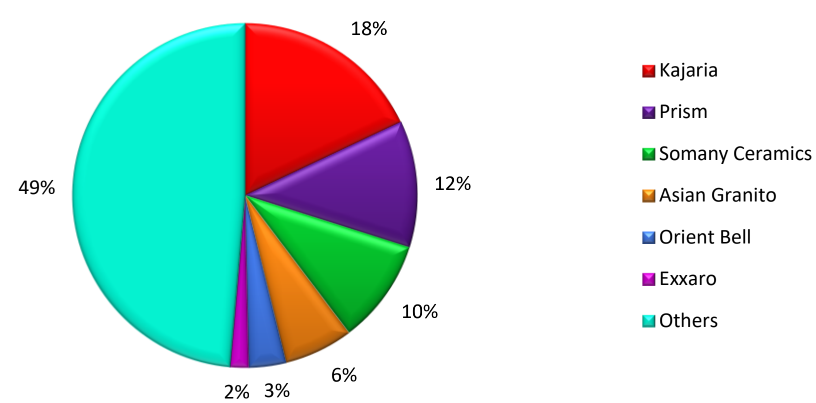
Per industry estimates, the Indian ceramic tiles market is estimated to grow at 8.6% CAGR. Low per capita consumption of tiles, consumers rising aspiration towards branded products and healthy traction in real estate sector fueled by government initiatives such as Smart City and Pradhan Mantri Awas Yojana are key drivers. The replacement and renovation market is also expected to report strong growth, along with new construction, catalysing the offtake of ceramic tiles.

Exhibit 19: Indian tiles industry - market size (Rs bn)

	Domestic market	Exports	Total size
FY17	256	14	270
FY21	179	121	300
FY22	393	127	520
FY23E	409	170	579
FY17-23E CAGR	**8%**	**51%**	**14%**

Source: Company, Industry estimates

Exhibit 20: India's tiles players' organised market share (~50% of industry) by value

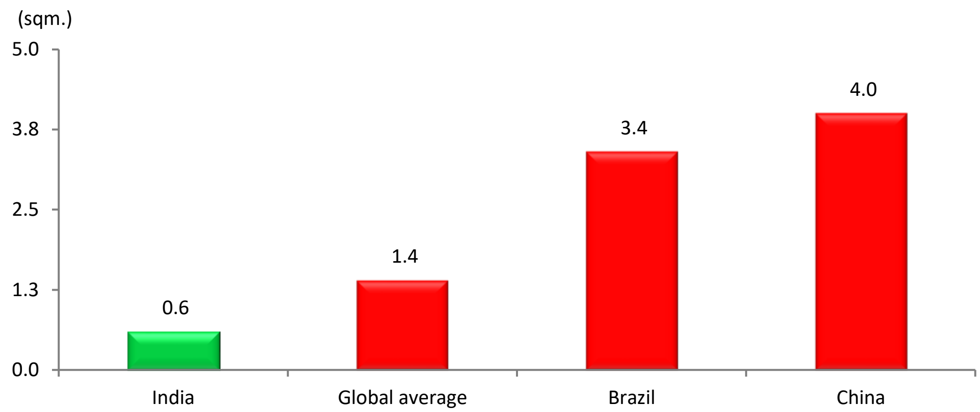


Source: Company, Industry reports, Systematix Institutional Research

Low per capita consumption of tiles in India provides robust prospect

India's per capita consumption of tiles is estimated to be ~0.6 sqm compared with 4.0 sqm for China, 3.4 sqm for Brazil and 1.4 sqm for the global average. The current low consumption provides large headroom for growth in the Indian tiles market over many decades.

Exhibit 21: India's low per capita consumption of tiles



Source: Industry, media reports

Exhibit 22: Tiles - Production Trend for Top Ten Countries

(Million Sq.m)

	CY17	CY18	CY19	CY20	CY21	
CHINA	10,146	9,011	8,225	8,474	8,863	→ 48%
INDIA	1,897	2,011	2,223	2,318	2,550	→ 14%
BRAZIL	867	872	909	840	1,049	
SPAIN	530	530	510	488	587	
IRAN	373	383	398	449	458	
TURKEY	355	335	296	370	438	
ITALY	422	416	401	344	435	
INDONESIA	307	383	347	304	410	
VIETNAM	560	602	560	534	370	
EGYPT	300	300	300	285	310	
OTHERS	2,451	2,587	2,634	2,695	2,869	
TOTAL WORLD PRODUCTION	18,208	17,430	16,803	17,101	18,339	

Source: Kajaria presentation

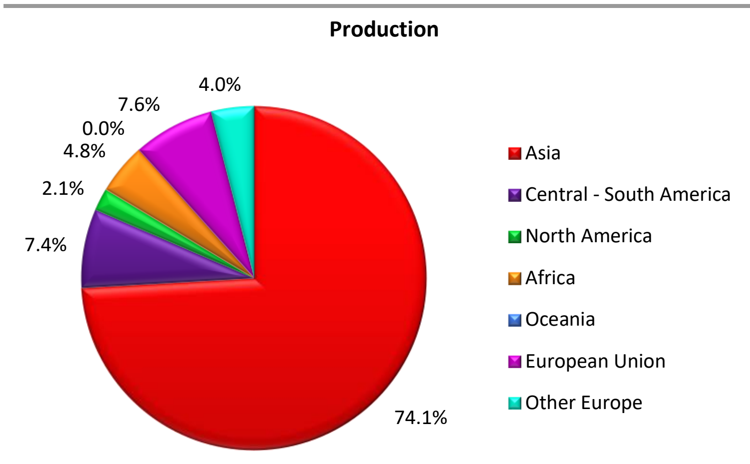
Exhibit 23: Tiles - Consumption Trend for Top Ten Countries

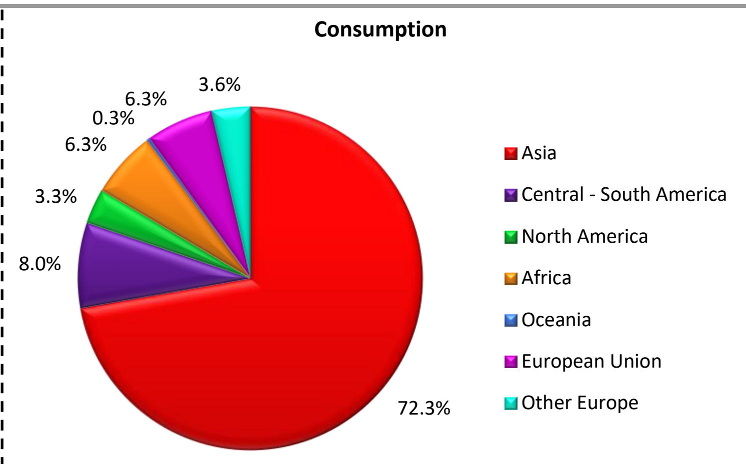
(Million Sq.m)

	CY17	CY18	CY19	CY20	CY21	
CHINA	9,244	8,163	7,453	7,859	8,268	→ 45%
INDIA	1,678	1,742	1,867	1,884	2,069	→ 11%
BRAZIL	765	775	802	829	902	
INDONESIA	336	450	413	357	478	
VIETNAM	580	542	467	400	300	
TURKEY	251	236	185	241	291	
USA	284	289	273	264	289	
EGYPT	252	236	239	237	278	
MEXICO	242	236	238	242	276	
SAUDI ARABIA	210	206	223	284	252	
OTHERS	4,195	4,438	4,478	4,453	4,806	
TOTAL WORLD CONSUMPTION	18,037	17,313	16,638	17,050	18,209	

Source: Kajaria presentation

Exhibit 24: World Production & Consumption (CY21)





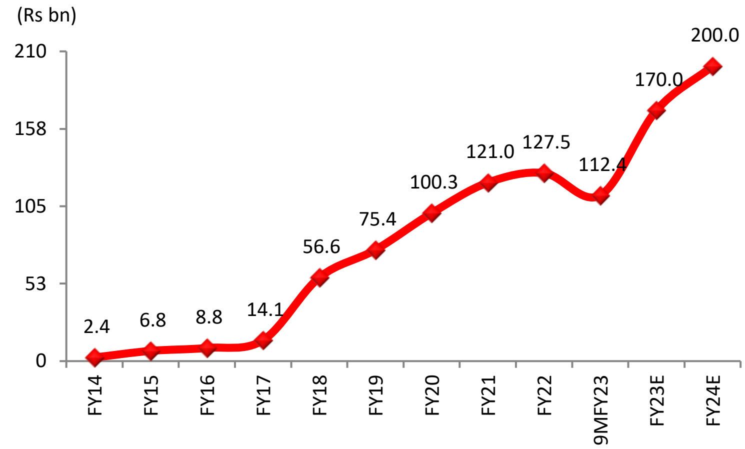
Source: Kajaria presentation

India tiles export likely to surge 33% YoY in FY23 to Rs 170bn+

Tiles export from India has seen substantial traction over the years (from Rs 2.4bn in FY14 to Rs 128bn in FY22) on the back India's cost competitive advantages (energy, labour etc.) and the right manufacturing ecosystem built in and around Morbi (Gujarat). After a flattish FY22 impacted by covid-19, exports from India have sharply rebounded since Oct'22 with Dec'22 month achieving Rs 15.2bn sales. This could be attributed to market share gains from production disruption in China (on covid related issue) and key European countries such as Italy, Span, Turkey (on spike in energy costs). Thus, after clocking Rs 112.4bn in 9MFY23, we expect India's exports to cross Rs 170bn in FY23, surging 33% YoY.

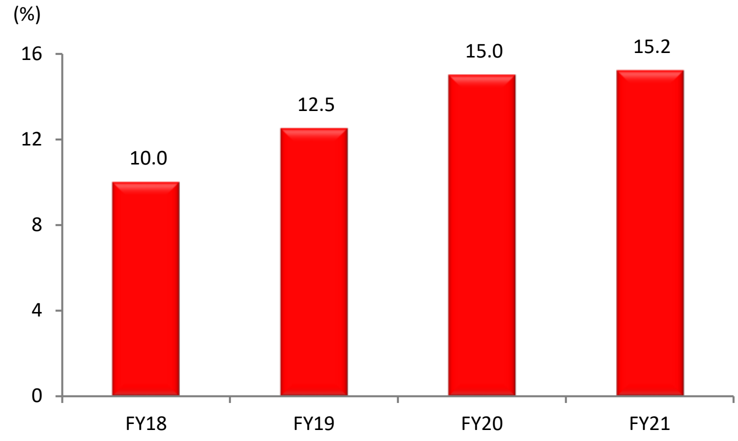
Positive read across for KJC, SOMC: Leading tile companies (KJC and SOMC) will hugely benefit from reducing competitive intensity in domestic markets as Morbi based manufacturers will be busy in meeting large demand from exports.

Exhibit 25: India's total tiles exports



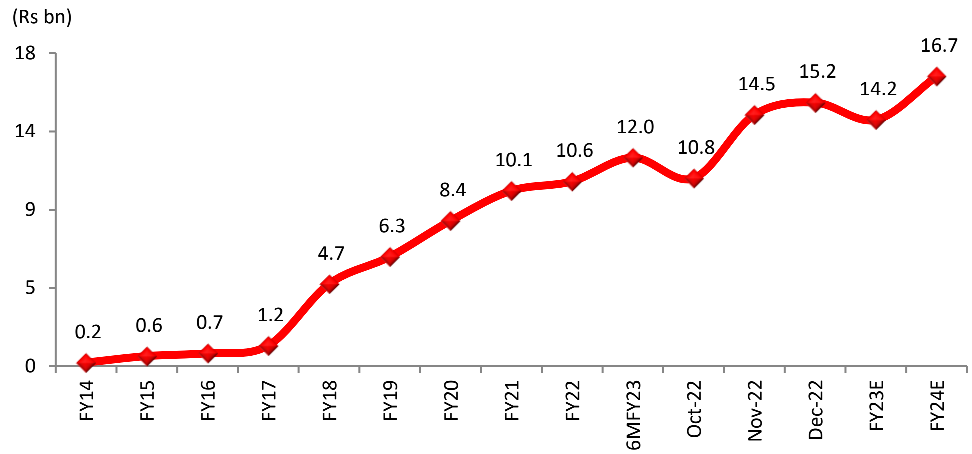
Source: DGFT

Exhibit 26: India's growing share in total global tiles exports



Source: Industry report

Exhibit 27: India's monthly tiles exports on rising trend

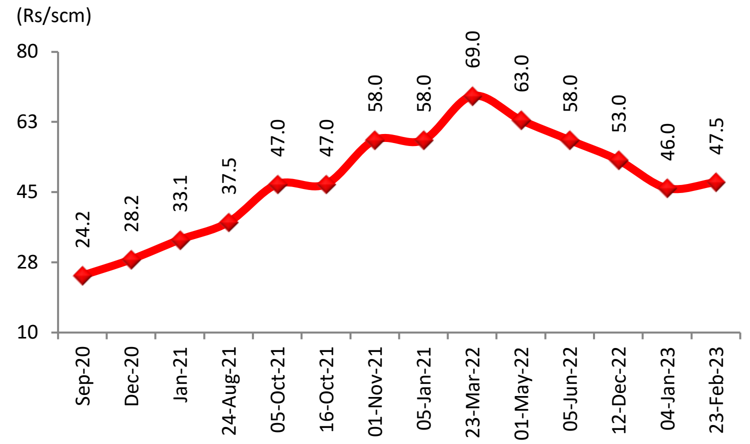


Source: DGFT, Company

Moderation in gas price bodes well for margins of KJC, SOMC

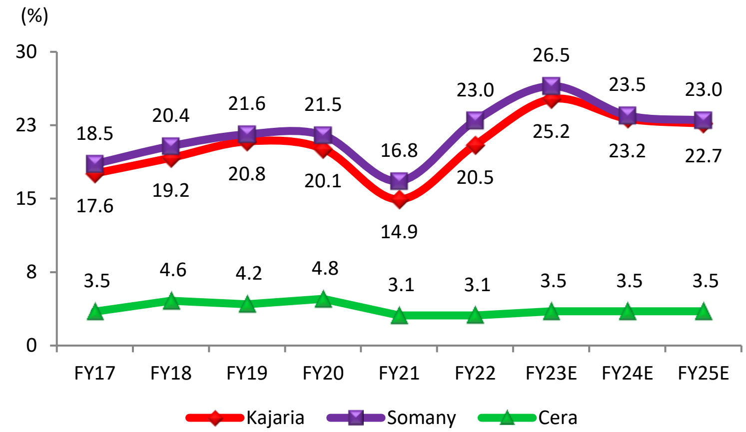
After a 3x spike during Sep'20 to Mar'22, natural gas price in Morbi has fallen ~30% from its peak in Mar'22 along with meaningful decline in prices across other regions from their relative peak levels. Given sharp rise, leading manufacturers switched consumption partly to alternative fuels such as LPG or propane, which were then meaningfully cheaper than gas. With decline in gas price, that parity has vanished. As power & fuel cost currently accounts for over 25% of revenue (18-20% pre-COVID) for KJC and SOMC, softening gas price augurs well for their margins (should reflect from 4QFY23 onwards).

Exhibit 28: Morbi gas price trend



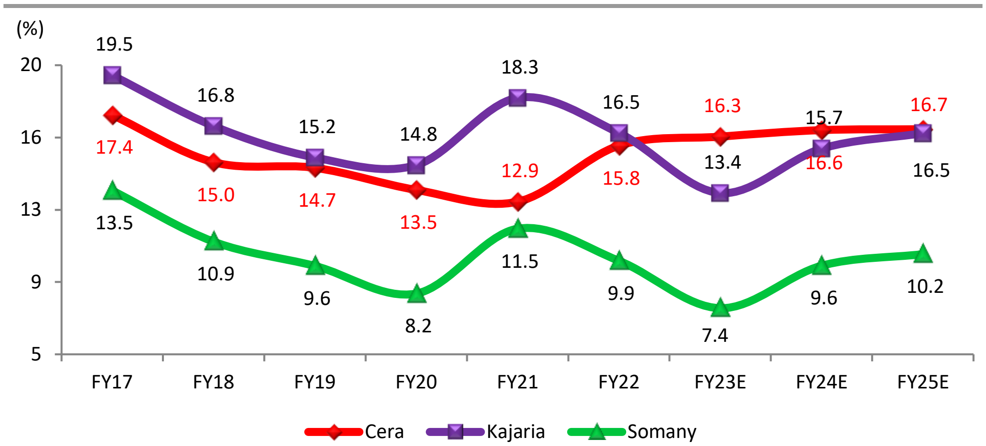
Source: Gujarat Gas, media reports

Exhibit 29: Power and Fuel cost (as % of revenue)



Source: Company, Systematix Institutional Research

Exhibit 30: EBITDA margins trend



Source: Company, Systematix Institutional Research

Indian sanitaryware & faucet industry overview

India is world's 2nd largest sanitaryware manufacturer after China. The Indian sanitaryware industry size is estimated to be around Rs 55bn, of which 75% is estimated to be the organised market. The industry is highly consolidated with the top 3 players (Parryware, Hindware, CERA – in the order) commanding 60-70% share in total market. Morbi and Thangadh (in the state of Gujarat) combined manufactures around 75% of India's total production. Easy availability of raw material and skilled labour are the key reasons.

The faucet market in India is worth over Rs 100bn, of which 60% is estimated to be the organized market. The industry is highly fragmented. Jaguar leads the industry with 15-20% market share. CERA and Hindware commands 4-5% market share each.

Per industry experts, the Indian sanitaryware and bathroom fittings market is estimated to grow at 8% CAGR over 2021-2027 driven by increased national drinking water outlay, hygiene & sanitation programmes (Swachh Bharat Abhiyaan), government's Housing for All, Smart Cities, social media influence, consumer preference and better living standards. Organised players such as CRS will continue to gain market share, in our view, owing to company's aggression towards capacity addition, brand building and channel expansion.

Exhibit 31: India sanitaryware industry structure

Total market size (Rs bn)	55.0
Organised market share	75%
Organised market (Rs bn)	41.3
CRS's FY23E revenue (Rs bn)	9.5
CRS's total market share	**17%**
CRS's organised market share	**23%**

Exhibit 32: India faucet industry structure

Total market size (Rs bn)	100.0
Organised market share	60%
Organised market (Rs bn)	60.0
Jaguar's total market share	**15-20%**
Hindware's total market share	**~5%**
CRS's total market share	**~5%**

Source: Company, media reports, Systematix Institutional Research

COMPANY SECTION

Cera Sanitaryware

06 March 2023

Market share gain-driven growth; solid cash flows

INITIATING COVERAGE

Sector: Building Materials **Rating: BUY**

CMP: Rs 6,300 **Target Price: Rs 7,335**

Stock Info	
Sensex/Nifty	59,809/17,594
Bloomberg	CRS IN
Equity shares (mn)	13.0
52-wk High/Low	6,741/3,838
Face value	Rs 5
M-Cap	Rs 81.9bn/USD 994mn
3-m Avg turnover	USD 1.8mn

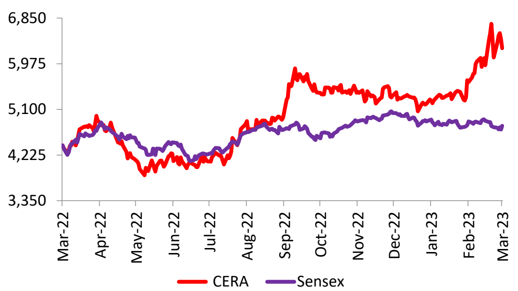
Financial Snapshot (Rs mn)

Y/E Mar	FY23E	FY24E	FY25E
Net sales	17,586	20,217	23,242
EBITDA	2,864	3,361	3,875
OPM (%)	16.3	16.6	16.7
PAT (adj.)	2,028	2,289	2,650
EPS (Rs)	155.9	176.0	203.7
PE (x)	40.4	35.8	30.9
P/B (x)	7.0	6.0	5.2
EV/EBITDA (x)	26.6	22.4	19.1
RoE (%)	17.2	16.8	16.8
RoCE (%)	21.9	21.4	21.6
Net-D/E (x)	(0.5)	(0.5)	(0.5)

Shareholding Pattern (%)

	Dec'22	Sep'22	Jun'22
Promoter	54.5	54.5	54.5
- Pledged			
FII	17.5	17.9	18.3
DII	9.4	9.7	10.6
Others	18.6	17.9	16.6

Stock Performance (1-year)



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We initiate coverage on Cera Sanitaryware (CRS) with a BUY rating and a target price of Rs 7,335, based on 36x FY25E P/E (vs. 34x for KJC). Robust FCFs across business cycles is commendable. Healthy revenue growth and margins, along with strict credit policy should help CRS maintain its OCF/EBITDA and OCF/PAT at robust ~70% and over 100% levels, respectively. A strong ~33% RoIC over FY23-25 will be driven by operational efficiency. Diverse product offerings, an extensive distribution network, a well-established brand recognition, strong financial standing, and expansion plans would enable it to sustain market share gains to achieve healthy growth over the long term. CRS has maintained performance (on the back of market-share gains) even as tiles and other building materials products categories have seen demand moderation in last 2 quarters. Management aims 20%+ revenue CAGR by FY26 from steady demand from home improvement.

A leading sanitaryware and faucet player with focus on small towns, retail sales: CRS is the 3rd-largest player in the Rs 55bn Indian sanitaryware industry with ~23% organised market share. We believe CRS has gained decent market share in sanitaryware and faucets in the past decade, aided by a) a solid balance sheet (owing to financial discipline), b) aggressively increasing sales touchpoints, c) refreshed and new SKUs, and d) brand-building efforts. CRS' ~70% revenue exposure from tier-2/3 towns (population below 2.5mn) is the result of incremental dealer additions over the years in these markets. Being risk averse, CRS is focused on retail sales (~80% of revenue) vs. institutional (inferior pricing and margin).

Vast product offerings; premiumisation-led growth: CRS has vast product offerings throughout its value chain (mass to luxury), which are sold through its four brands (*CERA*, *Senator*, *JEET* and *ISVEA*), pan-India point of sales (PoS), multi-layer marketing infrastructure and continued brand efforts. Starting from sanitaryware over 4 decade ago, CRS now has a wide product basket (added faucets in FY11 and tiles in FY13). Regular introduction of new SKUs, refreshing running SKUs and entry into new product lines have helped CRS in expanding product portfolio over years. Nearly 55% of its sanitaryware revenue comes from the premium category. Faucets have scaled up fast (Rs 5.9bn revenue likely in FY23, 34% mix) with high margins. Traction in tiles (Rs 2.2bn revenue likely in FY23, 11% mix) has been slow due to low brand salience and intense competition; CRS's focus is on the high margin GVT segment.

Solid OCF on strict credit policy; focus turning to in-house manufacturing: CRS' strong cash flows (OCF/EBITDA ~65%, OCF/PAT over 100%) are driven by its strict credit policy, healthy margins and asset-light business model. The company has significantly scaled up its non-sanitaryware business in the last decade to 45-50% of total revenue without compromising on its leverage position, which is commendable. It has also paid regular dividends in the last 30+ years. Despite planned ~Rs 2bn capex met through internal accruals, we estimate CRS to generate ~Rs 3.5bn FCF over FY23-25 to swell the cash surplus to ~Rs 9bn from ~Rs 6bn currently.

Initiate with a BUY on strong financials: We like CRS for its leading position in sanitaryware and faucets, wide product basket and network, and strong brand presence. Healthy FCF across business cycles is commendable. We estimate strong 17%/21% CAGR in revenue/PAT over FY22-25E (muted 7%/8% CAGR over FY17-22), factoring in continued market share gains by CRS and EBITDA margin expansion (~100bps to 16.7% in FY25E) owing to superior product mix and cost optimisation measures. **Key risks:** Slowdown in economy and housing market; high input costs

Investors are advised to refer disclosures made at the end of the research report.

Story in charts…

Exhibit 1: Revenue growth trend - segment wise

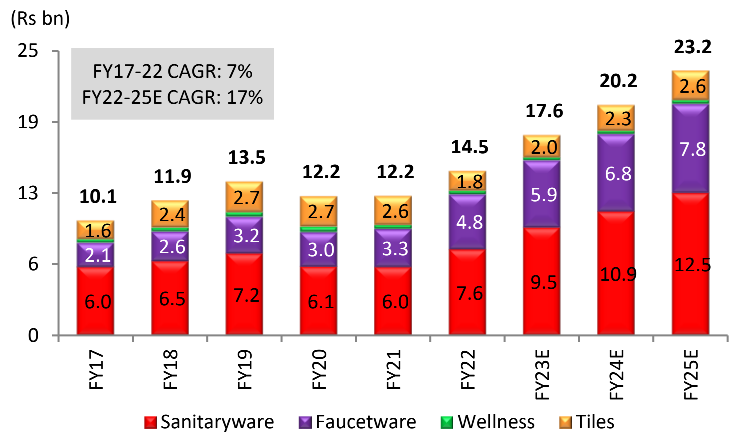


Exhibit 2: Revenue mix trend - segment wise

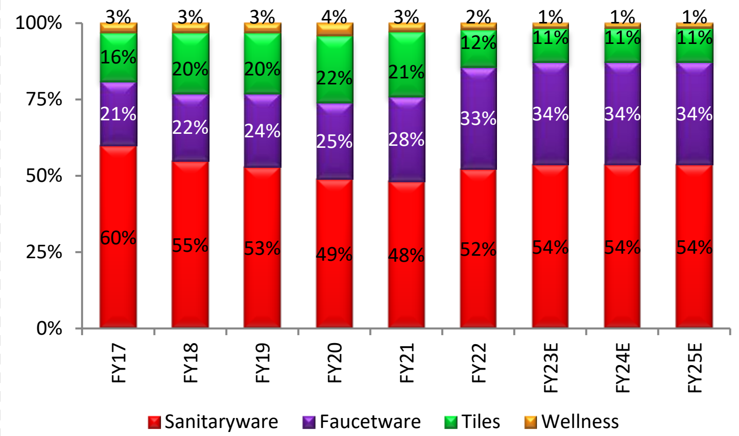


Exhibit 3: Consol. revenue growth

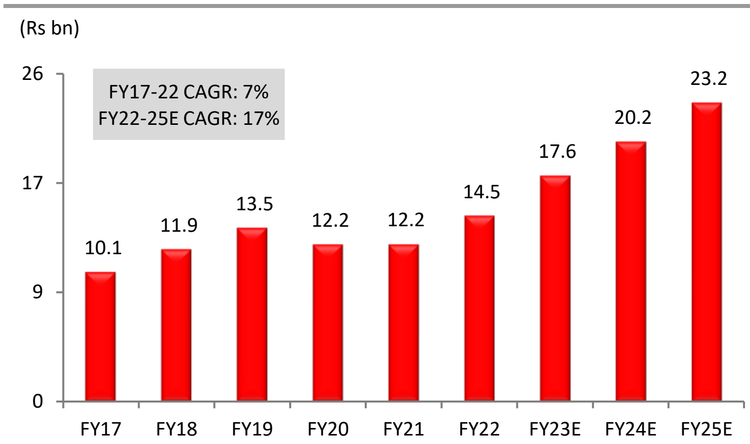


Exhibit 4: Gross, EBITDA margins trend

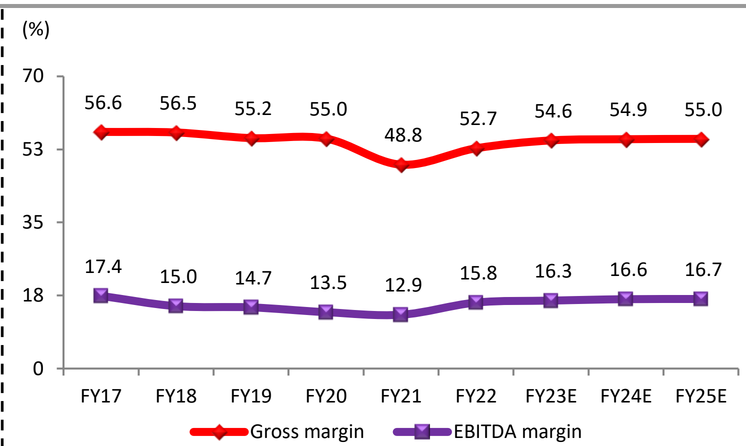


Exhibit 5: OCF/EBITDA, OCF/PAT trend

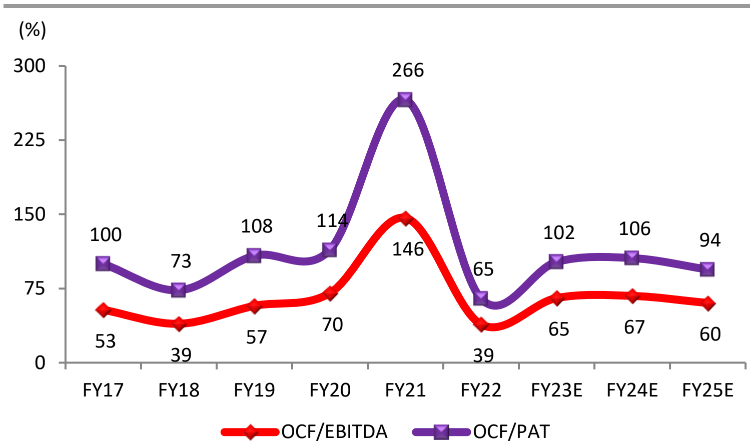
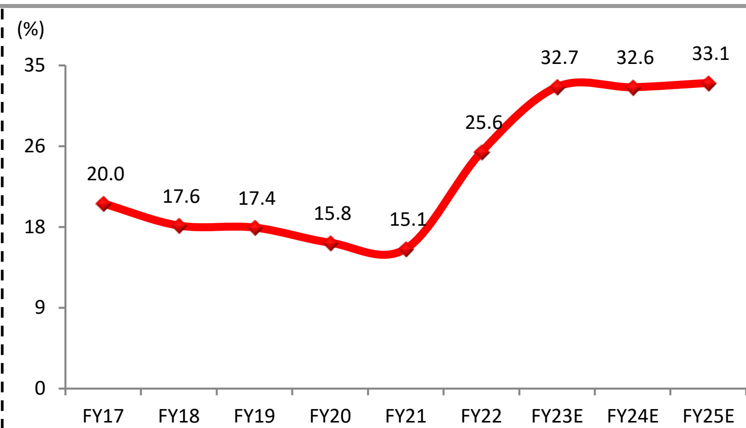


Exhibit 6: RoIC trend

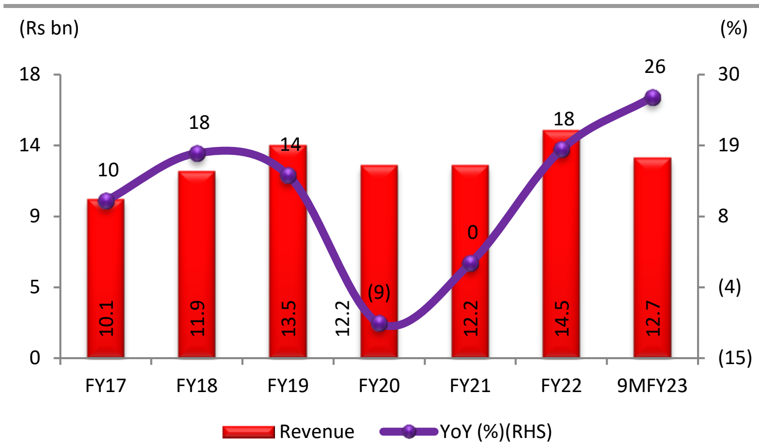


Source: Company, Systematix Institutional Research

Cera Sanitaryware - An overview

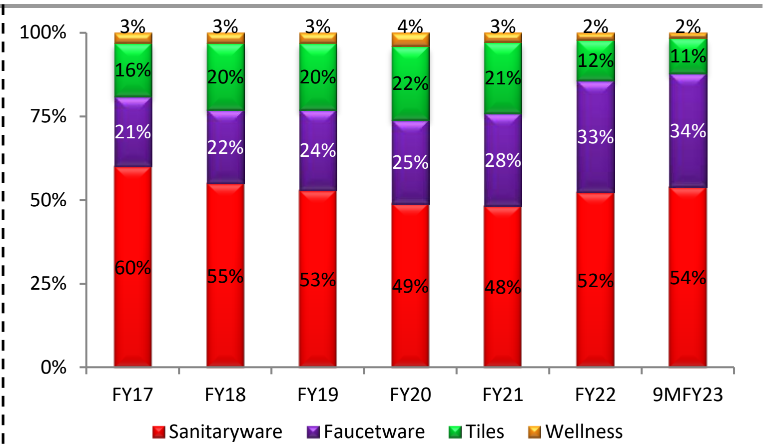
Founded in 1980 by Mr. Vikram Somany - the current CMD - CRS is India's 3rd-largest sanitaryware player and a leading faucet brand in the bathware industry. It has an annual capacity of 2.5mn pieces of sanitaryware and 3mn pieces of faucets, largely comprising products in the mid-premium range. Its manufacturing plants are based in Kadi (Gujarat), the ceramics hub of India. The company follows an asset-light model and outsources all its mass-mid range product requirements, which extends it with enough bandwidth to focus on marketing and brand building. CRS' four brands (*Cera*, *Senator*, *JEET* and *ISVEA*) cater to its products at different price points. After split from JV partners, CRS is currently outsourcing its tiles requirements. It also has a small business vertical of wellness products, comprising bathroom cubicles/ partitions/ shower panels. CRS has a highly penetrated distribution network with 17,000+ touchpoints across India, which included 5,000+ dealers and 12,000+ retailers. It has four different store formats to market its products, depending on size, ownership and purpose of the store, as classified in the table below. Most of its power requirements comes from captive wind and solar power plants which keeps its power & fuel costs at mere ~3% of revenue, unlike 20-25% for tile companies.

Exhibit 7: Revenue growth trend



Source: Company

Exhibit 8: Revenue mix trend



Source: Company

Joint Ventures (JVs)

1) In June 2016, CRS entered into a 51% JV with Packcart Packaging LLP in Mehsana, Gujarat, a packaging unit, to manufacture corrugated boxes.
2) In May 2018, it incorporated Race Polymer Arts LLP with 51% capital contribution to manufacture polymer products like seat cover, cistern, fittings and other products made from polypropylene (PP).

Exhibit 9: Key managerial personnel

Name	Designation	Remarks
Vikram Somany	Founder and CMD	He founded the business in 1980 and takes keen interest in business affairs and initiation and execution of strategy. He holds the FCMI (UK) certification.
Deepshikha Khaitan	Joint Managing Director	She is the daughter of Vikram Somany and joined Cera about 8 years ago. She handles all verticals including R&D, new launches, sales & marketing and finance.
Ayush Bagla	Executive Director	He joined Cera in Apr'18 and holds a 24-year experience incl. fund management and private equity. He manages investor relations & strategic planning roles.
Rajesh B Shah	CFO / COO	He is with Cera from past 34 years and handles overall finance related functions.

Source: Company

Exhibit 10: Strong leadership team

Name	Designation	Remarks
Anupam Gupta	Executive Director (Technical)	He is responsible for all aspects of manufacturing activities. He has 30+ years of experience in industries like cement, textiles, chemicals and ceramics. He spent over 17 years with the Aditya Birla Group.
Parthiv Dave	President - Sales & Strategic Affairs	He holds over 30 years of experience, especially in building materials and the aviation sectors. He has earlier worked with Cera for 13+ years as VP Sales overseeing the North, West and East zones in India
V Krishnamurthy	President - Marketing	He holds over 25 years of industry experience, and was conferred with the "Most Influential Global Marketing Leader" award in Nov'19 by the World Marketing Congress. At Cera, he is responsible for all procurements, vendor relations, devising and execution of media, marketing and positioning strategies.
Rahul Jain	VP – Marketing	He holds extensive experience in the sanitaryware and faucetware industry, and is responsible for the marketing function and other consumer relevant innovations that deliver measurable improvement in brand equity and market share at Cera.
Ajay Jain	VP - (Faucetware)	He has 23 years of experience with companies like HSIL, Kohler India and Hindalco; at Cera he is responsible for all aspects of faucet manufacturing.
Mr. Vivek Andankar	Asst. VP Production (Sanitaryware)	He is responsible for sanitaryware manufacturing at Cera. With 24 years of experience, he has previously worked with Kolher, LG Electronics, Electrolux.

Source: Company

Key shareholders: Nalanda India (10%), Tata MF (3%), HSBC MF (2.4%), Govt. of Singapore (2.3%), Canara Robeco (1.7%), HDFC Life (1.3%), Grandeur Peak (1.3%)

Recent performance and management commentary

Despite slowdown in most building product categories in last 2-3 quarters, CRS reported healthy performance, as its sanitaryware and faucet revenue (87% mix combined) grew at 19% and 13% YoY in 3QFY23, posting strong 16.4% EBITDA margin at CRS, driven by healthy demand from home renovation and optimal plant utilisation. Following the premiumisation trend, CRS launched new Lustre Series products, which include *Rose Gold*, *French Gold*, and *Platinum* sanitaryware and faucetware options. The ongoing ad campaign, featuring celebrities Kiara Advani and Vijay Deverakonda as brand ambassadors further boosted the company's brand visibility. By changing its strategy towards in-house manufacturing, the company plans to invest ~Rs 2bn on expanding capacities in the sanitaryware (greenfield) and faucet (brownfield) segments.

Exhibit 11: CERA - Quarter results (consolidated)

(Rs mn)	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	YoY (%)	QoQ (%)	9MFY23	9MFY22	YoY (%)
Total Income	**3,881**	**4,406**	**3,972**	**4,159**	**4,578**	**18**	**10**	**12,710**	**10,053**	**26**
Raw material costs	1,846	2,056	1,847	1,838	2,082	13	13	5,766	4,780	21
Employee costs	489	528	497	556	539	10	(3)	1,592	1,408	13
Other expenses	915	974	1,000	1,086	1,207	32	11	3,293	2,425	36
EBITDA	**630**	**848**	**628**	**679**	**750**	**19**	**10**	**2,058**	**1,440**	**43**
Depreciation	83	83	75	82	85	3	3	243	241	1
Finance costs	12	17	11	14	14	24	2	39	36	11
Other income	43	64	(6)	106	132	210	25	232	172	35
Exceptional items	-	(57)	-	-	-	-	-	-	-	-
PBT	**578**	**754**	**536**	**688**	**783**	**35**	**14**	**2,007**	**1,335**	**50**
Tax	147	221	137	177	214	46	21	529	339	56
PAT after JV/asso.	**424**	**530**	**395**	**507**	**564**	**33**	**11**	**1,467**	**981**	**49**
EPS (Rs)	32.6	40.7	30.4	39.0	43.4	33	11	112.8	75.5	49
As % Total Income						**YoY (bps)**	**QoQ (bps)**			**YoY (bps)**
Gross margin	**52.4**	**53.3**	**53.5**	**55.8**	**54.5**	**210**	**(129)**	**54.6**	**52.5**	**218**
Employee costs	12.6	12.0	12.5	13.4	11.8	(83)	(160)	12.5	14.0	(147)
Other expenses	23.6	22.1	25.2	26.1	26.4	279	26	25.9	24.1	178
EBITDA margin	**16.2**	**19.2**	**15.8**	**16.3**	**16.4**	**15**	**5**	**16.2**	**14.3**	**187**
Depreciation	2.1	1.9	1.9	2.0	1.9	(27)	(12)	1.9	2.4	(49)
Finance costs	0.3	0.4	0.3	0.3	0.3	1	(2)	0.3	0.4	(4)
Other income	1.1	1.5	(0.2)	2.5	2.9	179	35	1.8	1.7	11
Effective tax rate	25.4	29.3	25.6	25.7	27.3	192	162	26.3	25.4	91
PAT	**11.1**	**12.1**	**10.0**	**12.3**	**12.4**	**131**	**13**	**11.6**	**9.9**	**173**
Revenue break-up						**YoY (%)**	**QoQ (%)**			**YoY (%)**
Sanitaryware	2,063	2,313	2,120	2,254	2,461	19	9	6,835	5,229	31
Faucetware	1,336	1,458	1,365	1,417	1,504	13	6	4,286	3,359	28
Wellness	70	82	67	79	46	(35)	(42)	192	213	(10)
Tiles	401	535	406	394	547	36	39	1,346	1,230	9
Revenue mix (%)										
Sanitaryware	53	53	54	54	54			54	52	
Faucetware	35	33	35	34	33			34	34	
Wellness	2	2	2	2	1			2	2	
Tiles	10	12	10	10	12			11	12	

Source: Company, Systematix Institutional Research

Investment rationale

Leading sanitaryware co. focuses on small towns, retail sales

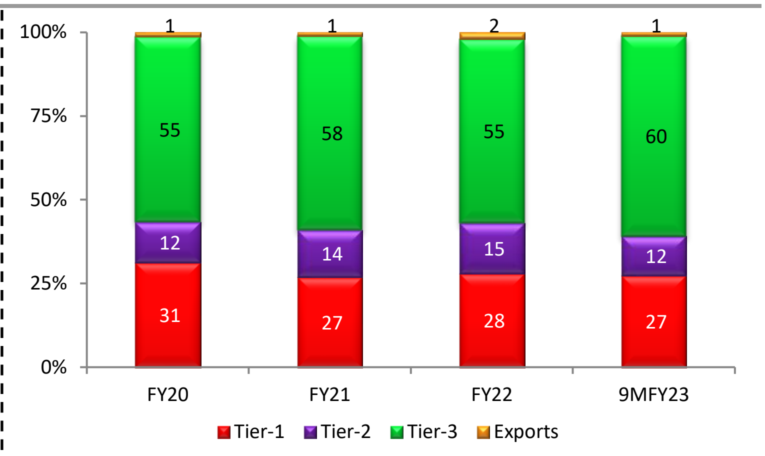
CRS is India's 3rd-largest player with ~23% organised market share in the Rs 55bn Indian sanitaryware industry. We believe CRS has gained a decent market share in sanitaryware and faucets in last 3-5 years, thanks to its solid balance sheet (through financial discipline), aggressively increasing sales touchpoints, refreshed and new SKUs and brand-building efforts. CRS' ~70% revenue exposure from tier 2/3 towns (population below 2.5mn) is the result of incremental dealer additions over the years in these markets. These smaller towns provide large growth opportunities (affordable housing) for CRS as it faces lesser competition from MNC brands and faster delivery time due to low-rise self-funded real estate projects. Rising aspirations and affordability of consumers is premiumization trend in smaller towns as well. Thus, we believe CRS will likely continue to make efforts in expanding its dealer count in tier 2/3 towns and raise its revenue mix to 75% in the coming years, despite the company increasing its presence in niche premium category. Being risk averse, CRS continues to focus on retail sales (~80% of revenue) over institutional (inferior pricing and margin).

Exhibit 12: CRS' market-share in India's sanitaryware industry

Total market size (Rs bn)	55.0
Organised market share	75%
Organised market (Rs bn)	41.3
CRS's FY23E revenue (Rs bn)	9.5
CRS's total market share	**17%**
CRS's organised market share	**23%**

Source: Company

Exhibit 13: CRS – Revenue mix by geography



Source: Company

Growing sales touchpoints, retail sales

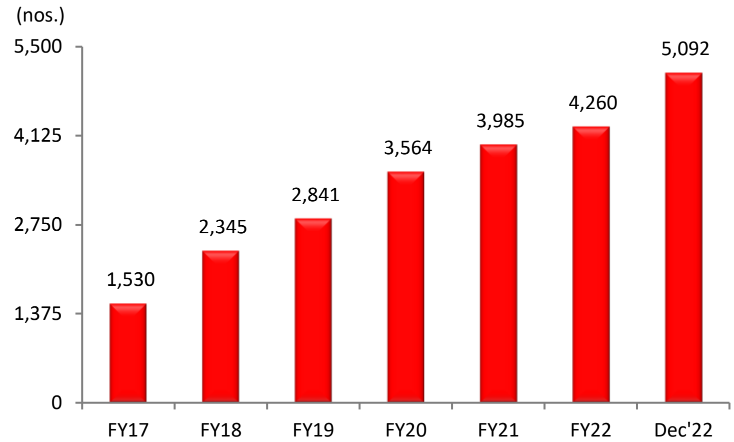
CRS has a highly penetrated distribution network with 17,000+ touchpoints across the country, which includes 5,000+ dealers and 12,000+ retailers. In addition to being focused on tier 2 and tier 3 towns, CRS has concentrated its attention on retail sales over institutional sales. This is because it commands better pricing and margins in retail sales compared to institution sales.

Customer focused and customer-centric approach

CRS has a strong after sales servicing team, which it manages internally. Its 13 service offices have 43 officer attending technicians who manage 364 technicians to attend complaints across every state. For complaints, CRS has a CRM module, wherein customers or trade partners can raise complaints through mobile applications that CRS targets to close in 1-2 working days.

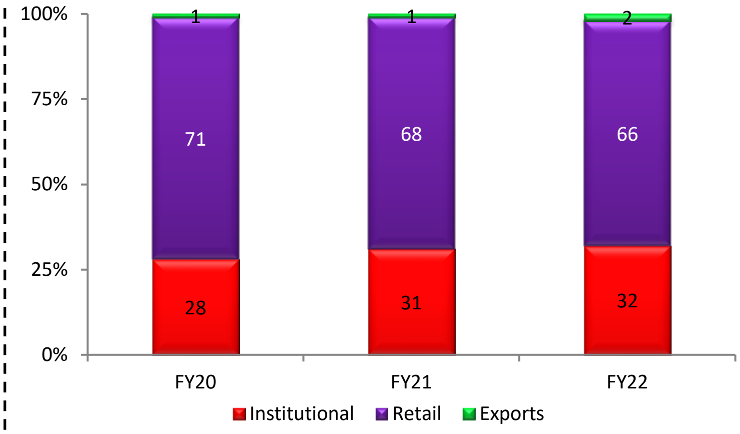
To strengthen its relationships with retailers, CRS launched a loyalty program called 'CERA Superstar'. The company received over 12,000 enrolments in the first seven months of the launch.

Exhibit 14: Dealer network



Source: Company

Exhibit 15: Bathware - Institutional vs. Retail (%)



Source: Company

Multi-layered marketing infrastructure

CRS has four different store formats to market its products, depending on size, ownership and purpose of the store. The various types of showrooms and galleries has helped it in marketing its vast product range and improve brand visibility. It owns and manages about 8 style studios across major cities. Its dealers own and manage over 150 style exclusive galleries. It also has a strong team of ~350 people for after sales service. High A&P spend (~4% of revenue) helps in branding.

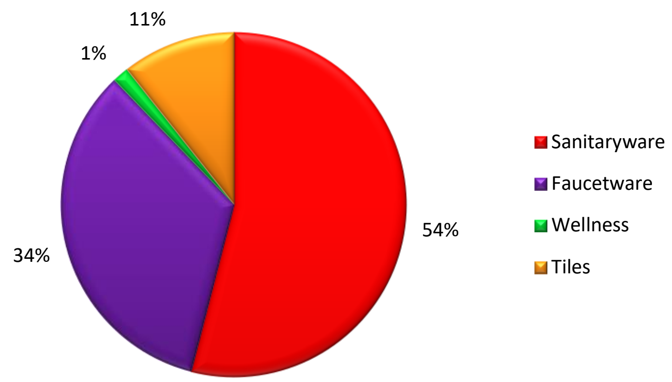
Exhibit 16: Cera style centre, studios and galleries

Source: Company

Vast product offerings; premiumisation-led growth

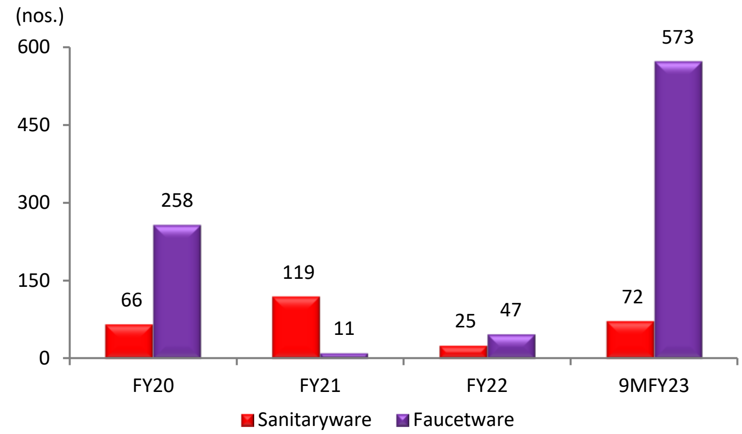
CRS has vast product offerings throughout the value chain (mass to luxury), which are sold through its four brands (*CERA*, *Senator*, *JEET* and *ISVEA*) pan India through PoS, multilayer marketing infrastructure and continued brand efforts. Starting from sanitaryware over 4 decades ago, CRS now has a wide product basket (added faucets in FY11 and tiles in FY13). Regular introduction of new SKUs, refreshing running SKUs and entry into new product lines have helped in expanding the portfolio over the years. While gaining strength in the mass-mid segment through its *CERA* and the new *JEET* brands, the company has also been focusing on the premium segment through its *Senator* brand. Premiumisation trend in tier 2/3 towns (CRS' focus) has also led the company to address the changing requirements of these markets. Mid and premium segments combined generated 73% of total revenue in 9MFY23 versus 65% in FY20.

Exhibit 17: Revenue mix (9MFY23)

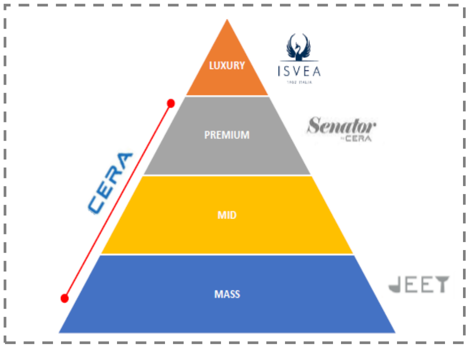


Source: Company, Systematix Institutional Research

Exhibit 18: SKU addition trend



Source: Company, Systematix Institutional Research



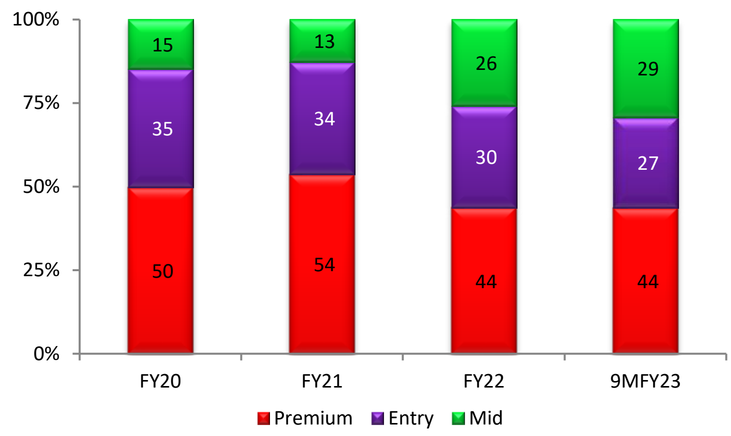
Wide range of offerings to customers through multiple brands

CRS outsources all its requirements in the mass-mid range of products through an asset-light model, which gives the company enough bandwidth to focus on marketing and brand building. Its four brands (*CERA*, *Senator*, *JEET* and *ISVEA*) cater to the company's products at different price points. *CERA* is the mother brand that encompasses the mass to premium range of products. The premium sanitaryware products are sold under the *Senator* brand, while the affordable range of bathware products are sold under the *JEET* brand.

Branding efforts

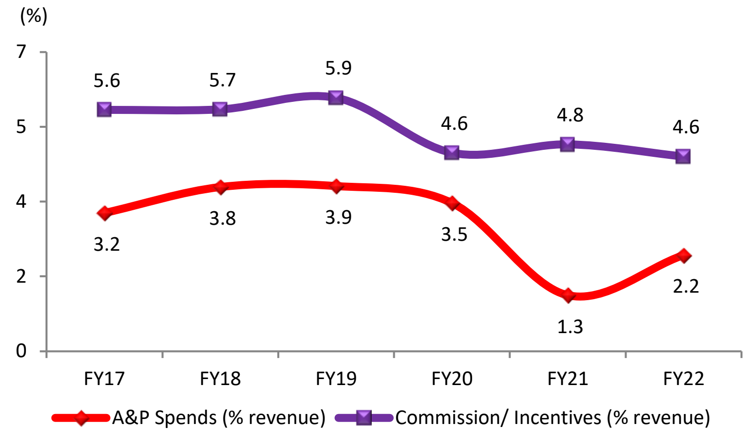
CRS usually spends ~4% of its revenue on A&P and 5-6% on commission and incentives. The company has hired celebrities Kiara Advani and Vijay Deverakonda as its brand ambassadors. With consistent investments towards advertisement & promotion exercises, CRS has created a strong brand recall in consumer's mind.

Exhibit 19: Revenue mix by product range (%)



Source: Company, Systematix Institutional Research

Exhibit 20: High A&P spend helps in increasing brand visibility



Source: Company

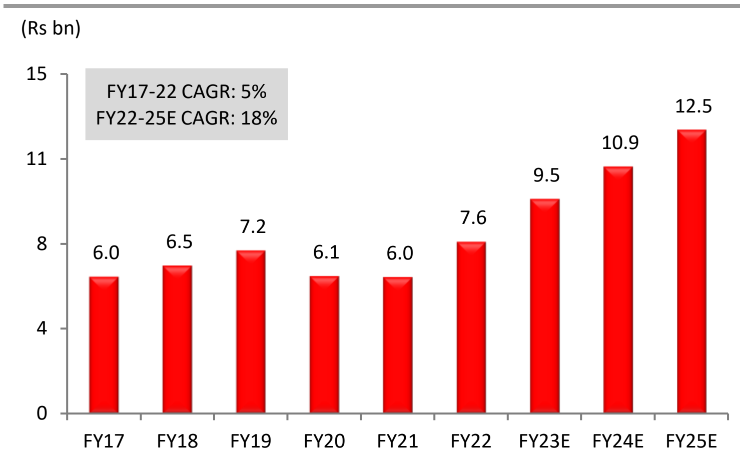
Exhibit 21: New brand campaigns launched

Source: Company

Sanitaryware and faucets revenues to grow at ~18% CAGR over FY22-25E

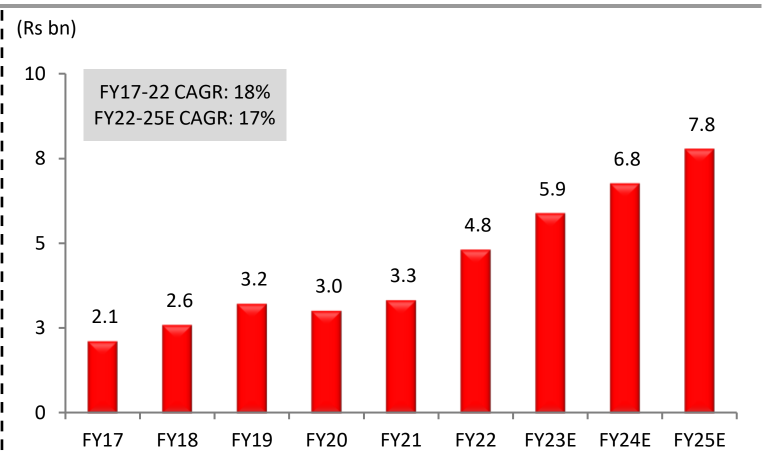
We estimate ~18% revenue CAGR over FY22-25 in the sanitaryware and faucet categories on the back of market share gains as CRS will continue to expand its channel and product basket with heightened branding efforts.

Exhibit 22: Sanitaryware revenue: 18% CAGR likely over FY22-25E



Source: Company, Systematix Institutional Research

Exhibit 23: Faucets revenue: 17% CAGR estimated over FY22-25E

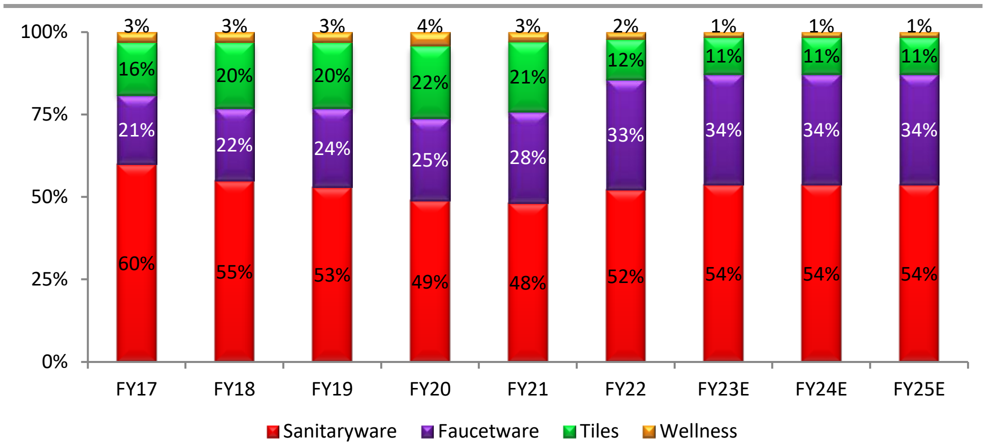


Source: Company, Systematix Institutional Research

Focus on profitable growth in tiles and adjacent categories

Starting from sanitaryware over 4 decades ago, CRS now has wide product basket in the bathware category. The company added faucets in FY11 and tiles in FY13. In the last 11 years, revenue share from non-sanitaryware products constitute 45-50% of the total, a substantial diversification from a single product line. Notably, all these diversifications happened without CRS leveraging its balance sheet. Over these years, while faucets have scaled up fast (Rs 5.9bn revenue likely in FY23, 34% mix) with best margins in the pack, traction in tiles (Rs 2.2bn revenue likely in FY23, 11% mix) has been slow due to low brand salience and intense competition. CRS is focusing mainly on the high-end GVT segment to profitably grow its tiles division. Wellness is a niche segment (comprising bathroom cubicles/ partitions/ shower panels) and will have limitation to scale.

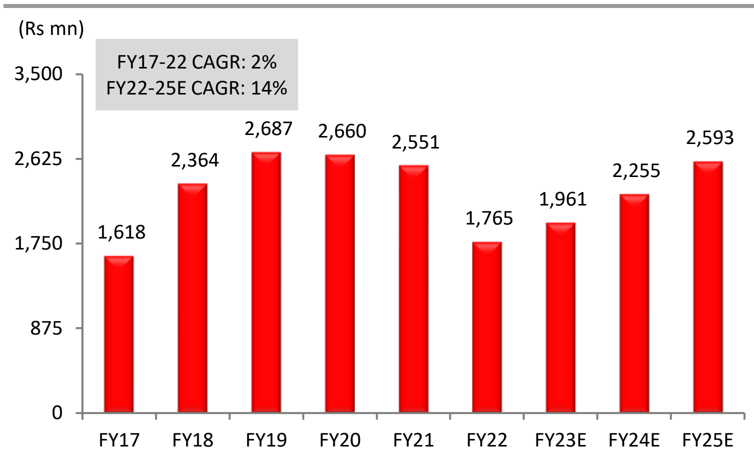
Exhibit 24: Revenue mix trend



Source: Company, Systematix Institutional Research

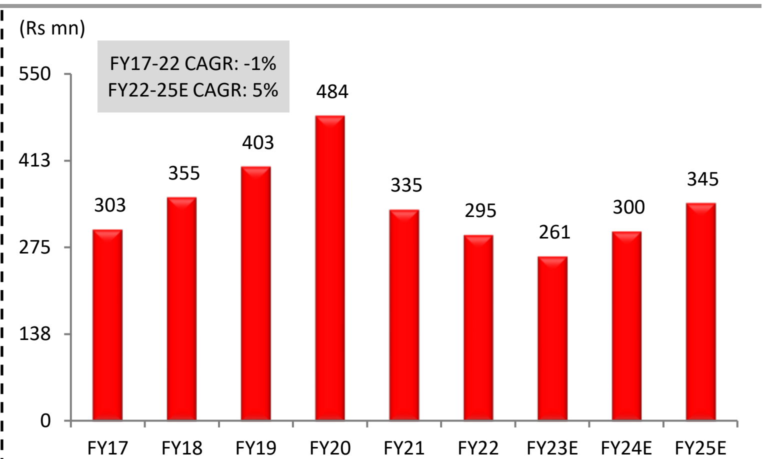
In 2015, CRS ventured into the tiles business via outsourcing and entered into a 51% JV with AP-based Anjani Tiles Ltd (ATL). Later it entered into a 26% JV with Morbi-based Milo Tiles LLP in 2019 for procuring high-end GVT tiles. Both the JVs were wounded up due to operational reasons and CRS is fully dependent on outsourcing for its tiles business. CRS is focusing mainly on the high-end GVT segment to profitably grow its tiles division.

Exhibit 25: Tiles - revenue trend



Source: Company, Systematix Institutional Research

Exhibit 26: Wellness - revenue trend

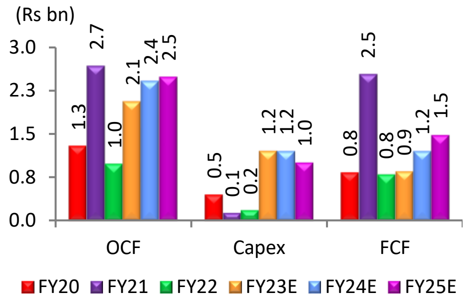


Source: Company, Systematix Institutional Research

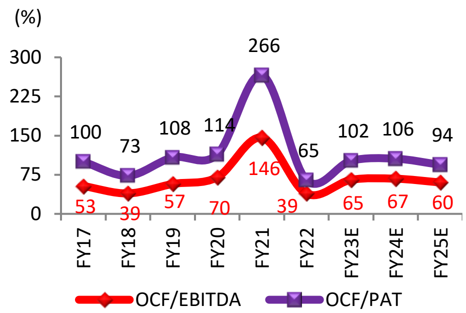
Solid OCF on strict credit policy; focus on in-house capacity

CRS' strong cash flows (OCF/EBITDA ~65%, OCF/PAT over 100%) are driven by its strict credit policy, healthy margins and asset-light business model. The company has significantly scaled up its non-sanitaryware business in the last decade to 45-50% of total revenue without compromising its leverage position, which is commendable. It has also paid regular dividends in the last 30+ years. Despite the company looking to meet its planned ~Rs 2bn capex through internal accruals, we estimate CRS to generate ~Rs 3.5bn FCF over FY23-25 to have surplus cash of ~Rs 9bn from ~6bn currently.

OCF, capex, FCF trend



Strong cash flow generation



Source: Company, Systematix Institutional Research

Strict credit policy: CRS follows a uniform credit policy for all its channel partners and does not offer higher credit to push sales. Its ERP system automatically shuts down fresh supplies to channel partners with dues in excess of 45-60 days.

Asset-light model helped in widening product offering faster: Until recently CRS had been following an asset-light model, wherein it outsourced low and mid-end products (50-60% of total volume), but manufactured premium products in house. This model has given it the bandwidth to direct its efforts towards marketing and branding, as also widen its product offerings with low capex.

Change in manufacturing strategy: CRS' present sanitaryware (2.5mn pieces) and faucet (3mn pieces) capacities have reached near optimal utilisation. With a change in strategy towards in-house manufacturing (in a bid to reduce import content) and better control on production and supply chain, the company plans to invest ~Rs 2bn on expanding capacities in sanitaryware (greenfield) and faucets (brownfield) in phases. These capacities will likely focus on meeting the increasing demand for high-end SKUs. Additional capacities at new locations would also mitigate the risk of production disruption at single location.

Phase 1

- **Sanitaryware:** 1.2mn pieces of greenfield capacity will likely be added to take the total capacity to 3.7mn pieces; a land parcel in Gujarat is likely to be finalised in Mar'23 for the purpose. Management expects the capacity to be operational in 24-30 months at capex of Rs 1.28bn.
- **Faucet:** 1.2mn pieces of brownfield capacity would take the total capacity to 4.2mn pieces; Management expects the capacity to be operational in 1QFY24 at a capex of Rs 700mn.

Phase 2

- **Sanitaryware:** Capacity of 2.4mn pieces would be added, which would take the total capacity to over 6mn pieces.
- **Faucet:** 1.2mn pieces capacity addition will increase the capacity to a total of 5.4mn pieces.

Financial Outlook

CRS reported muted 7%/5%/8% CAGR in revenue/EBITDA/PAT over FY17-22, impacted by demonetisation, GST-related channel destocking and slowdown in real estate activities. Yet, its OCF/EBITDA of ~70% and healthy FCF generation (~0.9bn annually) was commendable. We estimate strong 17%/19%/21% CAGR in revenue/EBITDA/PAT over FY22-25E, believing CRS' market share gains in its product segments would continue, with EBITDA margin likely expanding ~100bps to 16.7% in FY25E on superior product mix and cost optimisation measures. Despite the company looking to fund its planned ~Rs 2bn capex through internal accruals, we estimate strong FCF (~Rs 3.5bn over FY23-25) to result in ~Rs 9bn cash surplus in FY25E from ~6bn currently. Such significant cash could suppress RoE to ~17%, but we estimate high ~33% RoIC over the forecast period. The company's strict credit policy and healthy margins would keep its OCF/EBITDA and OCF/PAT at strong ~65% and over 100%, respectively. Notwithstanding the prevailing economic slowdown, management has an optimistic demand outlook, underpinned by steady demand for home improvement, and aims to double revenue at over 20% CAGR by FY26.

Exhibit 27: Revenue (consolidated)

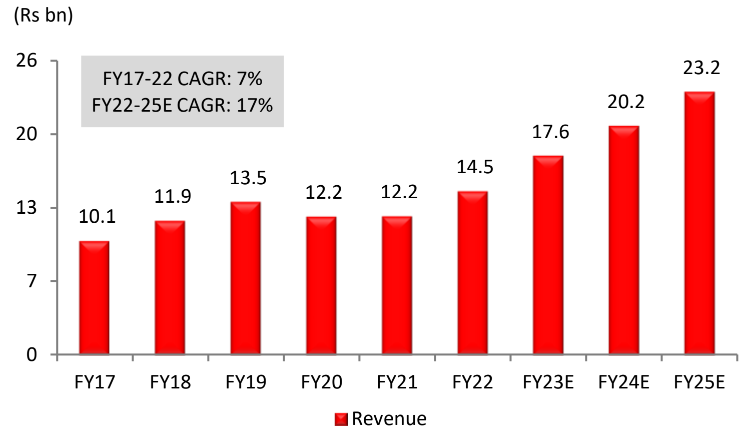


Exhibit 28: Gross, EBITDA margin (%)

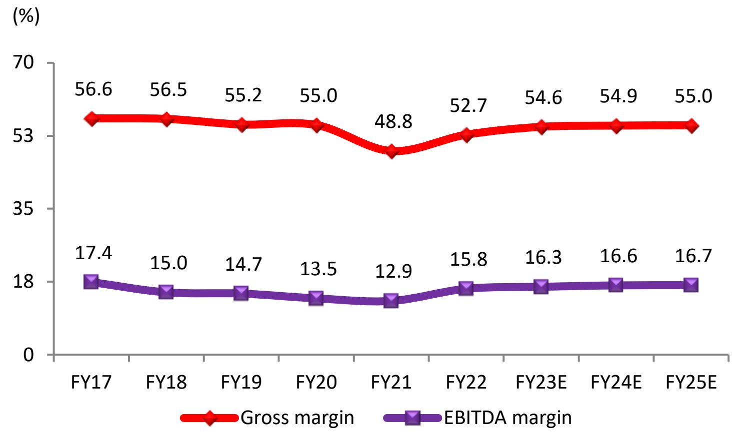


Exhibit 29: EPS, PAT margin (%)

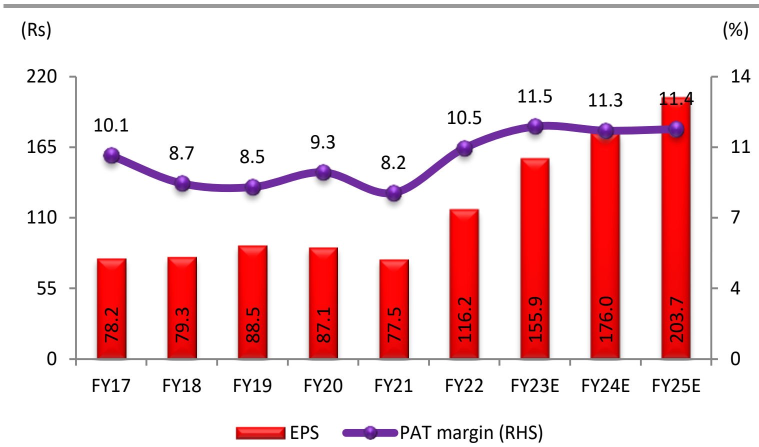
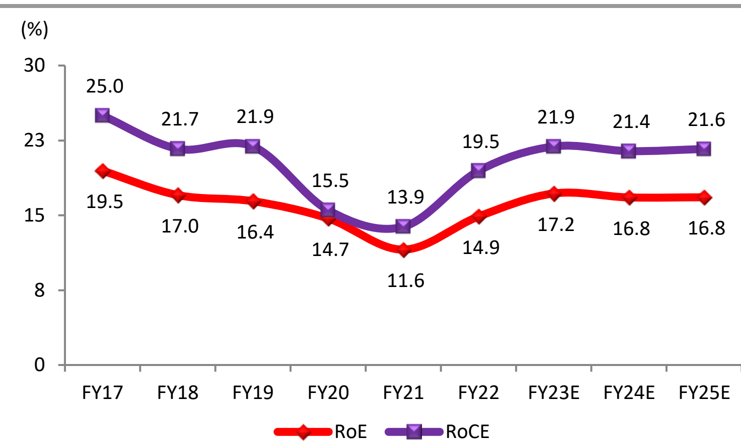


Exhibit 30: RoE, RoCE trend



Source: Company, Systematix Institutional Research

Exhibit 31: Working capital cycle

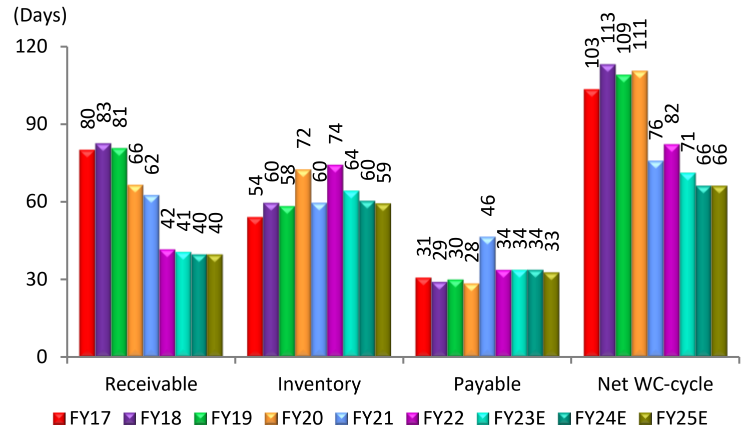


Exhibit 32: OCF, capex and FCF trend

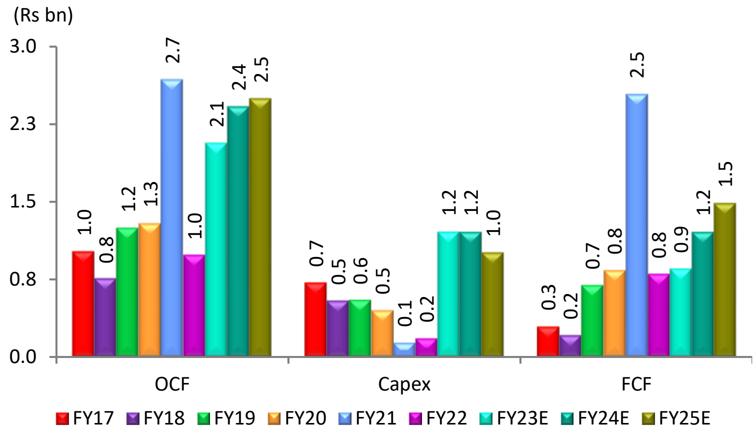


Exhibit 33: OCF/EBITDA, OCF/PAT trend (%)

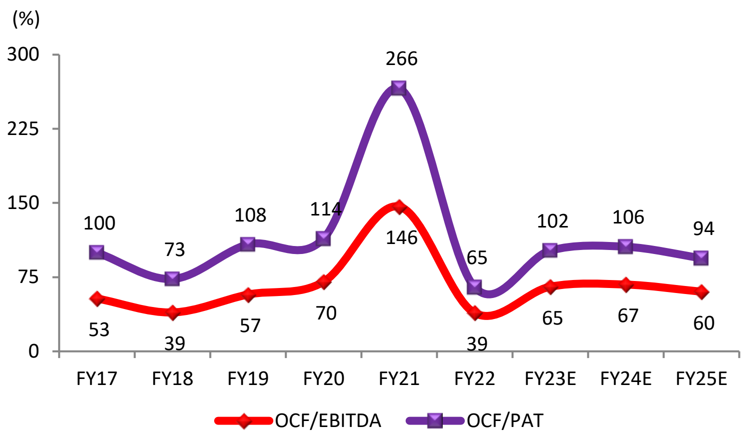


Exhibit 34: RoIC trend

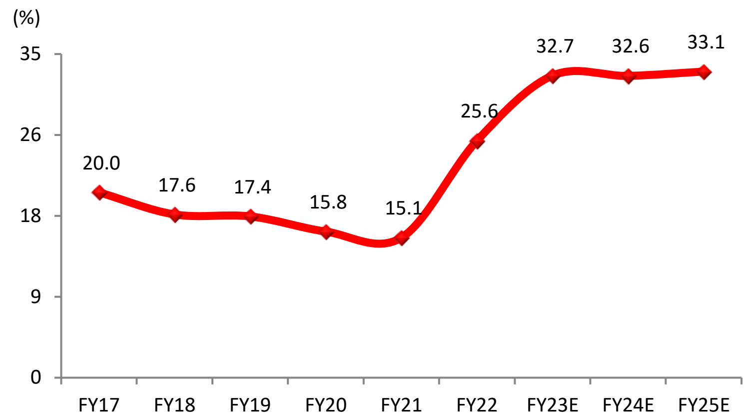


Exhibit 35: DuPont analysis

	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
RoE (%)	16.4	14.7	11.6	14.9	17.2	16.8	16.8
PAT margin (%)	8.5	9.3	8.2	10.5	11.5	11.3	11.4
Total Asset Turnover (x)	1.6	1.3	1.2	1.3	1.4	1.4	1.4
Equity Multiplier (x)	1.2	1.2	1.2	1.1	1.1	1.1	1.1

Source: Company, Systematix Institutional Research

Outlook and Valuation

We initiate coverage on CRS with a BUY rating and a target price of Rs 7,335, based on 36x FY25E P/E (vs. 34x for KJC). Healthy revenue growth and margins, and a strict credit policy should help CRS retain its OCF/EBITDA and OCF/PAT at healthy ~70% and over 100% levels, respectively. Significant cash could suppress RoE to ~17%, but we estimate high ~33% RoIC over FY23-25. Diverse product offerings, extensive distribution network, well-established brand recognition, strong financial standing, and expansion plans will likely enable CRS to sustain market-share gains and achieve healthy growth over the long term. CRS has maintained performance (on the back of market-share gains) even as tiles and other building materials products categories have seen demand moderation in the last 2 quarters. Management aims 20%+ revenue CAGR by FY26 from steady demand from home improvement.

We like CRS for its leading position in sanitaryware (3rd-largest in India) and faucets, comprehensive product portfolio, wide distribution reach and strong brand presence. Healthy FCF generation even during demand slowdown reflects its brand power and the company's financial discipline. We estimate strong 17%/19%/21% CAGR in revenue/EBITDA/PAT over FY22-25E (muted 7%/5%/8% CAGR over FY17-22), supported by continued market share gains; our estimate ~100bps EBITDA margin expansion to 16.7% in FY25E would result from a superior product mix and cost optimisation measures. Despite management intending to meet its planned ~Rs 2bn capex through internal accruals, we believe the company would generate strong FCF (~Rs 3.5bn over FY23-25) driving ~Rs 9bn cash surplus in FY25E from ~6bn currently.

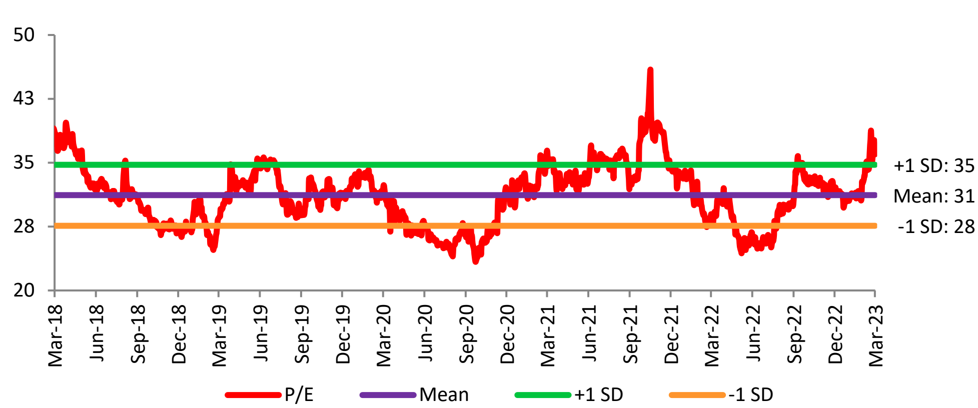
Key risks: Slowdown in economy and housing market; high input costs

Exhibit 36: Systematix vs. Bloomberg estimates

(Rs mn)	Systematix estimates			Bloomberg estimates			% Var with Systematix		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Total Income	17,586	20,217	23,242	17,283	20,019	22,703	2	1	2
EBITDA	2,864	3,361	3,875	2,817	3,328	3,788	2	1	2
EBITDA margin (%)	*16.3*	*16.6*	*16.7*	*16.3*	*16.6*	*16.7*			
PAT	2,028	2,289	2,650	1,977	2,343	2,736	3	(2)	(3)
EPS (Rs)	155.9	176.0	203.7	151	175	208	3	0	(2)

Source: Bloomberg, Systematix Institutional Research

Exhibit 37: CRS – one year forward PE band and standard deviation (SD)



Source: BSE, Systematix Institutional Research

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net revenues (Rs mn)	**12,243**	**14,458**	**17,586**	**20,217**	**23,242**
Growth (%)	*0.1*	*18.1*	*21.6*	*15.0*	*15.0*
Direct costs	6,268	6,836	7,984	9,120	10,465
Gross Margin (%)	*48.8*	*52.7*	*54.6*	*54.9*	*55.0*
SG&A	4,395	5,335	6,738	7,735	8,902
EBITDA	**1,581**	**2,287**	**2,864**	**3,361**	**3,875**
EBITDA margins (%)	*12.9*	*15.8*	*16.3*	*16.6*	*16.7*
- Depreciation	396	324	330	425	486
Other income	252	236	297	225	262
Interest Exp	97	53	55	42	43
PBT	1,339	2,090	2,777	3,120	3,608
Effective tax rate (%)	*25.4*	*26.8*	*26.4*	*26.0*	*26.0*
+ Associates/(Minorities)	9	(18)	(17)	(19)	(21)
Net Income	**1,008**	**1,511**	**2,028**	**2,289**	**2,650**
Adjusted income	1,008	1,511	2,028	2,289	2,650
WANS	13	13	13	13	13
FDEPS (Rs)	77.5	116.2	155.9	176.0	203.7
FDEPS growth (%)	*(11.0)*	*49.9*	*34.2*	*12.9*	*15.7*

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Share capital	65	65	65	65	65
Net worth	8,717	10,152	11,789	13,624	15,753
Total debt	1,221	657	627	597	567
Minority interest	117	142	152	162	172
DT Liability/(Asset)	303	354	360	366	372
Capital Employed	**10,358**	**11,305**	**12,929**	**14,749**	**16,865**
Net tangible assets	4,147	3,365	4,235	5,010	5,525
Net Intangible assets	8	5	5	5	5
Goodwill	-	-	-	-	-
CWIP	13	7	17	27	37
Investments (Strategic)	-	-	-	-	-
Investments (Financial)	4,743	5,621	5,621	5,621	5,921
Current Assets	4,762	5,434	5,901	6,384	7,152
Cash	104	149	775	1,630	2,428
Current Liabilities	3,418	3,276	3,624	3,927	4,203
Working capital	1,344	2,158	2,276	2,456	2,949
Capital Deployed	**10,358**	**11,305**	**12,929**	**14,749**	**16,865**
Contingent Liabilities	427	258	-	-	-

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
EBIT (before OI)	1,265	2,159	2,535	2,936	3,389
+ Non-cash items	396	324	330	425	486
OCF before WC changes	1,660	2,483	2,864	3,361	3,875
- Incr./(decr.) in WC	(1,126)	678	108	170	482
Others including taxes	106	825	691	771	897
Operating cash-flow	2,680	980	2,065	2,420	2,495
- Capex	140	182	1,210	1,210	1,010
Free cash-flow	2,540	798	855	1,210	1,485
Acquisitions					
- Dividend	-	169	390	455	520
+ Equity raised	-	-	-	-	-
+ Debt raised	(83)	214	(30)	(30)	(30)
- Fin Investments	2,313	665	-	-	300
- Misc. Items (CFI + CFF)	75	115	(191)	(130)	(164)
Net cash-flow	68	62	625	855	799

Source: Company, Systematix Institutional Research

Ratios @ Rs 6,300

YE: Mar	FY21	FY22	FY23E	FY24E	FY25E
P/E (x)	81.3	54.2	40.4	35.8	30.9
EV/EBITDA (x)	49.8	33.7	26.6	22.4	19.1
EV/sales (x)	6.4	5.3	4.3	3.7	3.2
P/B (x)	9.4	8.1	7.0	6.0	5.2
RoE (%)	11.6	14.9	17.2	16.8	16.8
RoCE (%)	13.9	19.5	21.9	21.4	21.6
ROIC	15.1	25.6	32.7	32.6	33.1
DPS (Rs per share)	13.0	35.0	30.0	35.0	40.0
Dividend yield (%)	0.2	0.6	0.5	0.6	0.6
Dividend payout (%)	16.8	30.1	19.2	19.9	19.6
Net debt/equity (x)	(0.4)	(0.5)	(0.5)	(0.5)	(0.5)
Receivables (days)	62	42	41	40	40
Inventory (days)	60	74	64	60	59
Payables (days)	46	34	34	34	33
CFO:PAT%	266	65	102	106	94

Source: Company, Systematix Institutional Research

Systematix

Institutional Equities

Kajaria Ceramics

06 March 2023

A leader in tiles with robust cash flows

INITIATING COVERAGE

Sector: Building Materials | **Rating: BUY**

CMP: Rs 1,050 | **Target Price: Rs 1,249**

Stock Info	
Sensex/Nifty	59,809/17,594
Bloomberg	KJC IN
Equity shares (mn)	159.2
52-wk High/Low	1,243/894
Face value	Rs 1
M-Cap	Rs 167bn/USD 2bn
3-m Avg turnover	USD 1.8mn

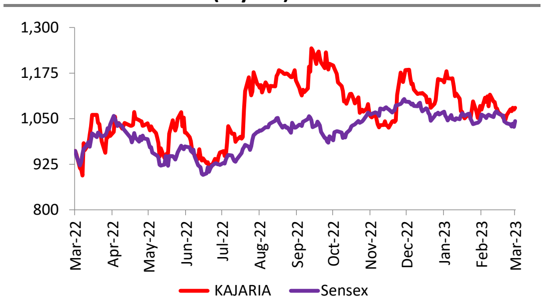
Financial Snapshot (Rs mn)

Y/E Mar	FY23E	FY24E	FY25E
Net sales	43,791	49,805	56,221
EBITDA	5,852	7,801	9,256
OPM (%)	13.4	15.7	16.5
PAT (adj.)	3,370	4,792	5,849
EPS (adj.) (Rs)	21.2	30.1	36.7
PE (x)	49.6	34.9	28.6
P/B (x)	7.4	6.7	6.0
EV/EBITDA (x)	28.3	21.2	17.8
RoE (%)	15.0	19.2	20.8
RoCE (%)	19.9	20.5	23.5
Net-D/E (x)	(0.1)	(0.1)	(0.1)

Shareholding Pattern (%)

	Dec'22	Sep'22	Jun'22
Promoter	47.5	47.5	47.5
- Pledged			
FII	18.6	19.4	19.6
DII	24.5	22.8	22.4
Others	9.4	10.3	10.5

Stock Performance (1-year)



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We initiate coverage on Kajaria Ceramics (KJC) with a BUY rating and a target price of Rs 1,249, based on 34x FY25E P/E. Our positive view is underpinned by KJC's 1) numero uno position in tiles, 2) execution capabilities, backed by strong management, 3) robust free cash flows (FCF), and 4) focus on market share gains, led by capacity addition and network expansion. While demand has been subdued in last two quarters, owing to extended monsoon and festive season, management expects a rebound from 4Q. Strong demand from the housing sector and shift in volumes to exports by Morbi players augur well for KJC's volumes. We estimate 12%/14% CAGR in volume/revenue over FY22-25E (6%/7% CAGR over FY17-FY22), on a) strong industry tailwinds, b) KJC's regular capacity additions in all regions, c) expansion in dealer network, and d) continued focus on branding. Notwithstanding near-term weakness, we believe KJC's medium to long term outlook to be robust.

India's number one player in tiles has strong retail presence: KJC is India's largest manufacturer of ceramic/vitrified tiles, and the 7th largest player in the world. In August 1988, the company started tile manufacturing operations with a capacity of 1 msm (million square meter) per annum, which is now risen to 84.45 msm. It has eight tile manufacturing plants located at Sikandrabad (UP), Gailpur (Rajasthan), Malootana (Rajasthan), Morbi (Gujarat), Vijaywada (AP), Srikalahasti (AP) and Balanagar (Telangana). KJC enjoys ~18% market share in India's organised tiles industry, as it has the widest pan India network of ~1,825 operative dealers (added ~350 in last 3 years), which comprise exclusive and multibrand outlets (MBOs); Management aims to add 500 dealers over the next 3 years. Through its deep distribution network, KJC has managed to penetrate India's uncovered markets (mostly Tier II and III towns), as its manufacturing plants are located across regions.

Robust cash flows despite regular high capex: Anticipating strong demand, KJC stepped up its capex since FY22 and is looking to invest over Rs 2.5bn annually to achieve its tiles volume growth guidance of 13-15%. We estimate 15%/16% CAGR in revenue/PAT over FY22-25E (~8% CAGR each over FY17-22), with healthy 20%+ RoE and ~Rs 3bn annual FCF, despite Rs 2.5bn of annual capex.

Industry tailwinds to aid volume growth in tiles: KJC's tiles volumes/revenue were up 12%/21% YoY during 9MFY23, respectively, and we estimate ~11%/17% YoY growth in FY23E. While demand has been subdued in last two quarters, owing to extended monsoon and festive season, company expects a rebound from 4Q. Strong demand from the housing sector and shift in volumes to exports by Morbi players augur well for KJC's volumes. We estimate 12%/14% CAGR in volume/revenue over FY22-25E (6%/7% CAGR over FY17-FY22), supported by a) strong industry tailwinds, b) KJC's regular capacity additions in all regions, c) expansion in dealer network, and d) continued focus on branding. Normalising gas prices (refer here) and sustained rising focus on value-added products should aid profitability ahead, in our view.

Expanding into adjacencies; bathware gaining scale: In the last decade, KJC has entered adjacent product categories such as bathware (sanitaryware, faucet under *Kerovit* brand), plywood and tile adhesives. These new product lines currently contribute mere ~10% to KJC's total revenue. After a slow start, management aims to profitably grow these segments faster in the coming years via channel expansion and branding efforts (hired Anushka Sharma and Ranveer Singh as brand ambassadors.

Key Risks: Slowdown in economy and construction activities; high volatility in gas prices, intensifying competition from Morbi.

Investors are advised to refer disclosures made at the end of the research report.

Story in charts…

Exhibit 1: Tiles - Volume trend

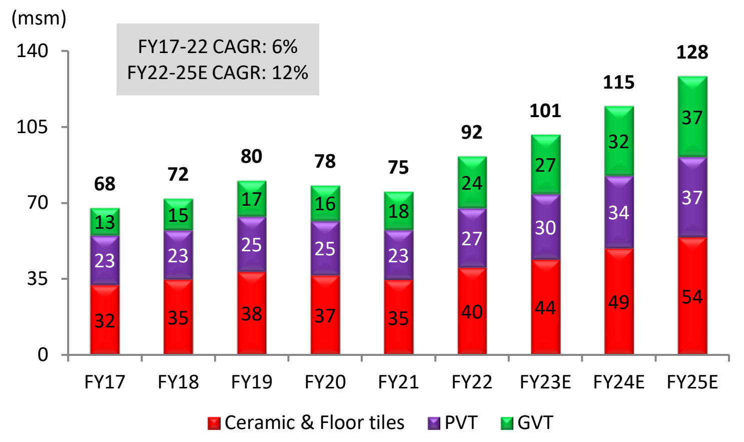


Exhibit 2: Tiles - Revenue trend

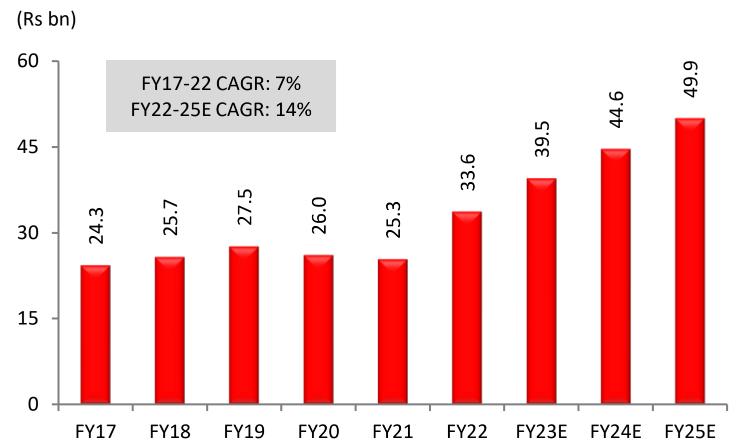


Exhibit 3: Total revenue trend

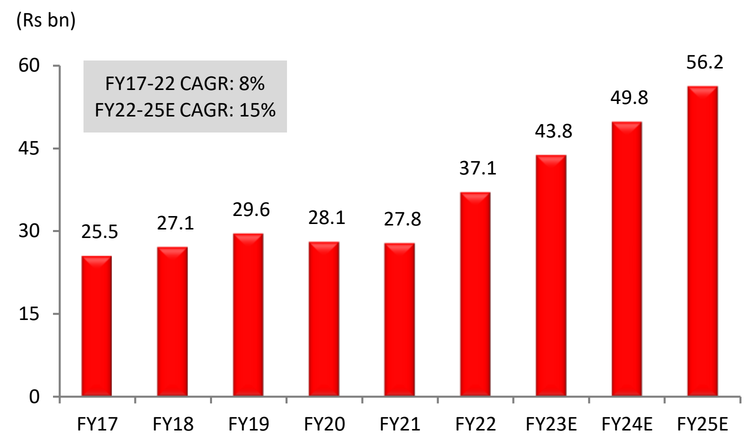


Exhibit 4: Gross, EBITDA margin trend

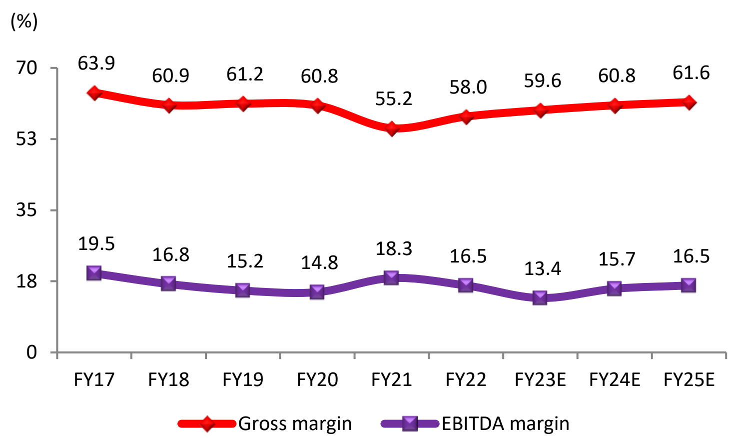


Exhibit 5: Power & fuel cost (as % of revenue)

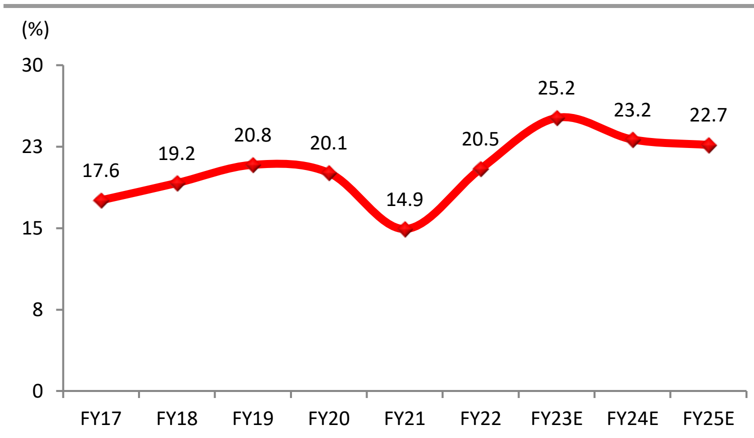
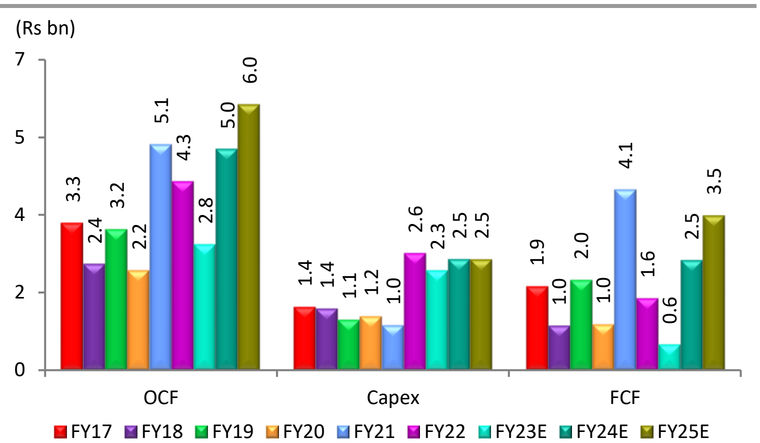


Exhibit 6: OCF, capex, FCF trend



Source: Company, Systematix Institutional Research

Brands

Kajaria

Kerovit By Kajaria

Kajaria PLY INDIA JAISA STRONG

Kajaria Ceramics - an overview

Kajaria Ceramics (KJC) is the largest manufacturer of ceramic/vitrified tiles in India and the 7th largest in the world. In August 1988, KJC started tile manufacturing operations with a capacity of 1 msm per annum, now at 84.45 msm. It has eight tile plants located at Sikandrabad (UP), Gailpur (Rajasthan), Malootana (Rajasthan), Morbi (Gujarat), Vijaywada (AP), Srikalahasti (AP) and Balanagar (Telangana). KJC has the widest network of ~1,825 operative dealers in India, and enjoys ~18% market share in the organised domestic tiles industry.

Exhibit 7: Tiles - Volume, revenue, EBITDA margin, PAT trend (FY17-9M23)

	FY17	FY18	FY19	FY20	FY21	FY22	9MFY23	CAGR FY17-22
Tiles volume (msm)	68	72	80	78	75	92	74	6
Revenue (Rs mn)	25,496	27,106	29,562	28,080	27,809	37,052	31,771	8
EBITDA margin (%)	*19.5*	*16.8*	*15.2*	*14.8*	*18.3*	*16.5*	*13.1*	
PAT (Rs mn)	2,528	2,350	2,266	2,554	3,081	3,770	2,365	8

Source: Company

Exhibit 8: Revenue mix – segment-wise (9MFY23)

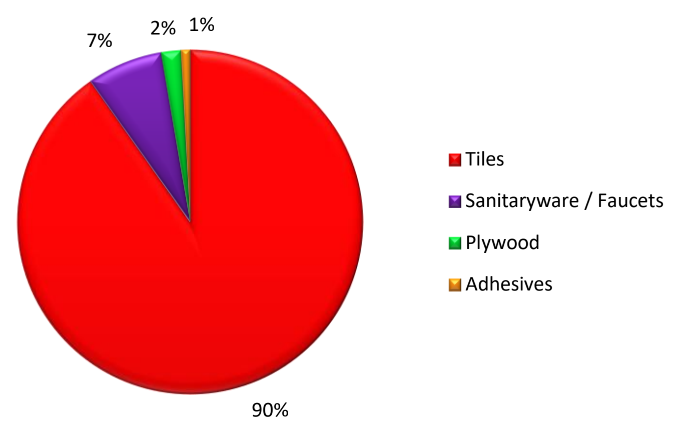
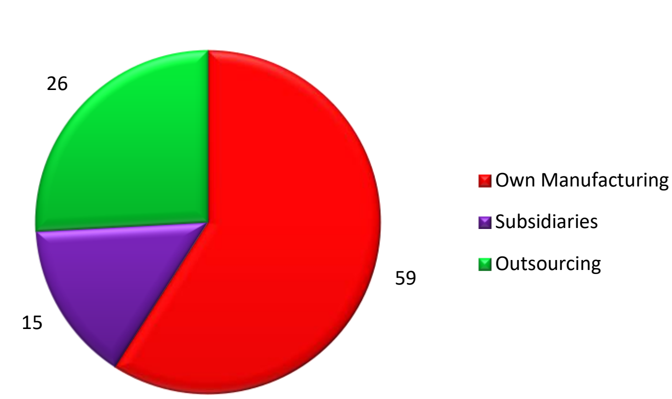


Exhibit 9: Tiles revenue mix (9MFY23)



Source: Company

Brand Ambassadors

- Akshay Kumar
- Ranveer Singh
- Anushka Sharma

Exhibit 10: Product verticals, plant locations and capacities

Products	Manufacturing Facilities	Capacity
Ceramic Wall & Floor Tiles	Gailpur (Rajasthan) and Vijayawada (Andhra Pradesh) and outsourced from quality conscious vendors in Gujarat.	37.05msm
Polished Vitrified Tiles	Malootana (Rajasthan), Morbi (Gujarat) and outsourced from quality-conscious vendors in Gujarat	15.4msm
Glazed Vitrified Tiles	Gailpur (Rajasthan), Sikandrabad (Uttar Pradesh) and Srikalahasti (Andhra Pradesh).	32.0msm
Bathware (Comprises of Faucets and Sanitaryware)	Faucet manufacturing facility at Gailpur (Rajasthan)	1mn pcs
	Sanitaryware manufacturing facility at Morbi (Gujarat)	0.75mn pcs
Plywood and Laminates	Trading of Plywood and Laminates	Outsourced

Source: Company

Exhibit 11: Details of subsidiaries

Subsidiary name	KJC's stake	Product	Plant location	Annual capacity	Current utilisation
Kajaria Vitrified *	87.4%	PVT	Morbi (Gujarat)	8.9 msm	95.0%
Vennar Ceramics **	51.0%	Ceramic wall tiles	Vijayawada (AP)	2.9 msm	79.0%
Kajaria Infinity	77.0%	GVT	Morbi (Gujarat)	5.7 msm	100.0%
South Asian Ceramics tiles	51.0%	Ceramic floor tiles	Hyderabad (Telangana)	4.75 msm	75.0%
Kajaria Bathware #	85.0%	Sanitaryware	Morbi (Gujarat)	0.75mn pieces	86.0%
		Faucet	Gailpur (Rajasthan)	1 mn pieces	100.0%
Kajaria Plywood	100.0%	Plywood, Laminate	Outsourcing from vendors in Gujarat, Uttarakhand, West Bengal and Karnataka	na	na
Kajaria International DMCC, Dubai	100.0%	Trading of all KJC products	na	na	na

Source: Company, board has approved stake increase to 95% ** to divest entire stake in a phased manner for Rs 183mn # WestBridge Crossover Fund LLP holds 15% stake*

Exhibit 12: Plant pictures

Gailpur, Rajasthan

Malootana, Rajasthan

Sikandrabad, UP

Srikalahasti, AP

Sanitaryware, Gujarat

Faucet, Rajasthan

Source: Company

Exhibit 13: Key management

Name	Designation	Remarks
Ashok Kajaria	CMD	He founded Kajaria in 1988 and has spearheaded the transformation of India's tile industry. He is an Engineer (BSME) from UCLA (California), USA.
Rishi Kajaria	Jt. MD	Rishi joined Kajaria in 2000. He led the acquisition of a ceramic tile plant in Vijayawada in AP in Apr'12, marking KJC's entry into South India. He is also a Chairman of Indian Council of Ceramic Tiles & Sanitaryware. He holds an engineering degree and MBA from Boston College,
Chetan Kajaria	Jt. MD	Chetan joined Kajaria in 2003, and spearheads the vitrified tile vertical. He is also responsible for company's expansion in the bathware segment. He holds a BBA from Boston University.

Source: Company

Key shareholders: Kotak AMC (4.7%), Government Pension Fund Global (4.6%), Mirae Asset AMC (4.1%), LIC (2.0%), Invesco MF (1.8%), DSP MF (1.8%), PGIM AMC (1.6%), UTI MF (1.2%), Kotak Offshore (1%), Smallcap World Fund (1%)

Recent quarter performance and management commentary

KJC performance has been weak since 2QFY23. A prolonged monsoon season and festive period in October impacted the company's volumes, while disruption in natural gas supply and an unprecedented increase in gas prices hurt margins. Management indicated some demand recovery during November and December, and is confident of a positive trend going forward. Fuel costs have begun to ease since December, primarily due to increased use of alternative fuels and some fall in gas prices. Based on these factors, management expects a strong rebound in 4Q. KJC remains focused on market share gains via dealer network expansion, particularly in unrepresented territories.

Exhibit 14: Quarter – table

(Rs mn)	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	YoY (%)	QoQ (%)	9MFY23	9MFY22	YoY (%)
Total Income	**10,682**	**11,018**	**10,082**	**10,778**	**10,911**	**2**	**1**	**31,771**	**26,034**	**22**
Power & Fuel	2,234	2,283	2,685	2,672	2,783	25	4	8,140	5,306	53
Other expenses	1,047	1,148	978	1,154	1,188	13	3	3,320	2,580	29
EBITDA	**1,838**	**1,659**	**1,536**	**1,294**	**1,331**	**(28)**	**3**	**4,161**	**4,448**	**(6)**
Depreciation	281	326	324	337	325	16	(3)	985	827	19
Finance costs	30	40	36	32	83	176	163	151	88	72
PAT (after JV/associate)	**1,220**	**958**	**923**	**699**	**743**	**(39)**	**6**	**2,365**	**2,812**	**(16)**
EPS (Rs)	7.7	6.0	5.8	4.4	4.7	(39)	6	14.9	17.7	(16)
As % Total Income						**YoY (bps)**	**QoQ (bps)**			**YoY (bps)**
Gross margin	**57.9**	**55.8**	**62.9**	**58.1**	**59.3**	**136**	**120**	**60.0**	**59.0**	**105**
Emp cost	10.0	9.6	11.3	10.6	10.7	71	12	10.9	11.6	(74)
Power & Fuel	20.9	20.7	26.6	24.8	25.5	459	71	25.6	20.4	524
Other exp	9.8	10.4	9.7	10.7	10.9	108	18	10.4	9.9	54
EBITDA margin	**17.2**	**15.1**	**15.2**	**12.0**	**12.2**	**(501)**	**19**	**13.1**	**17.1**	**(399)**
Effective tax rate	22.1	28.7	26.1	28.7	26.1	399	(254)	26.9	23.6	324
PAT margin	**11.7**	**8.8**	**9.2**	**6.4**	**6.8**	**(492)**	**36**	**7.4**	**11.0**	**(355)**
Segment Revenues						**YoY (%)**	**QoQ (%)**			**YoY (%)**
Own Manuf. (tiles)	*5,522*	*5,587*	*5,381*	*5,968*	*5,592*	*1*	*(6)*	*16,941*	*14,017*	*21*
Subsidiaries (tiles)	*1,381*	*1,439*	*1,321*	*1,354*	*1,640*	*19*	*21*	*4,314*	*3,656*	*18*
Outsourcing/Import (tiles)	*2,714*	*2,973*	*2,387*	*2,421*	*2,608*	*(4)*	*8*	*7,415*	*5,963*	*24*
Tiles - Total	**9,616**	**9,999**	**9,089**	**9,743**	**9,839**	**2**	**1**	**28,670**	**23,635**	**21**
Sanitary ware / Faucets	817	827	714	744	795	(3)	7	2,253	1,931	17
Plywood	249	192	203	194	188	(25)	(3)	585	468	25
Adhesives	-	-	77	97	90	-	(7)	263	-	-
Tiles sales volume (msm)						**YoY (%)**	**QoQ (%)**			**YoY (%)**
Own Manufacturing	14.4	14.4	13.4	14.8	14.0	(3)	(5)	42.2	37.6	12
Subs/JV's	3.8	3.7	4.2	4.2	5.2	37	24	13.6	10.6	28
Outsourcing/Imports	7.5	7.9	5.7	6.0	6.3	(15)	6	17.9	17.5	2
Total	**25.6**	**26.0**	**23.3**	**24.9**	**25.5**	**(1)**	**2**	**73.7**	**65.7**	**12**
Tiles NSR (/sq mtr)						**YoY (%)**	**QoQ (%)**			**YoY (%)**
Own Manufacturing	384	389	401	404	401	4	(1)	402	373	8
Subs/JV's	363	385	312	324	316	(13)	(2)	317	345	(8)
Outsourcing/Imports	364	378	421	406	414	14	2	414	340	22
Blended	**375**	**385**	**390**	**391**	**387**	**3**	**(1)**	**389**	**360**	**8**
Segment EBIT (%)						**YoY (bps)**	**QoQ (bps)**			**YoY (bps)**
Tiles	15.5	12.8	12.8	9.7	10.0	(548)	34	10.8	14.7	(395)
Others (S/w, Faucets, Ply)	6.2	5.6	4.4	0.4	1.0	(522)	55	1.9	5.7	(384)
Blended	**14.6**	**12.1**	**12.0**	**8.9**	**9.2**	**(537)**	**33**	**10.0**	**13.9**	**(391)**
Unallocated income/(exp)	*0.7*	*0.6*	*0.8*	*0.7*	*0.7*			*0.7*	*0.8*	
Net WC Cycle (Days)	**55**	**52**	**57**	**62**	**66**					
Net cash (Rs mn)	**3,380**	**3,730**	**3,400**	**1,980**	**1,880**			**1,880**	**3,380**	

Source: Company, Systematix Institutional Research

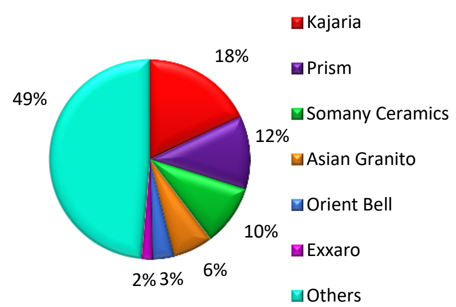
Investment rationale

The tiles leader has strong retail presence

As the largest domestic tiles manufacturer with 18% market share, KJC has the widest network of ~1,825 dealers pan India. These exclusive and MBOs use KJC's vast product basket serviced from its 8 tile manufacturing facilities and 2 bathware facilities located pan India. Setting up plants across regions helped KJC in deepening its distribution network to percolate into India's uncovered markets (mostly Tier II and III towns). After adding ~125 dealers in FY23 so far, management aims to add 500 more dealers over the next 3 years.

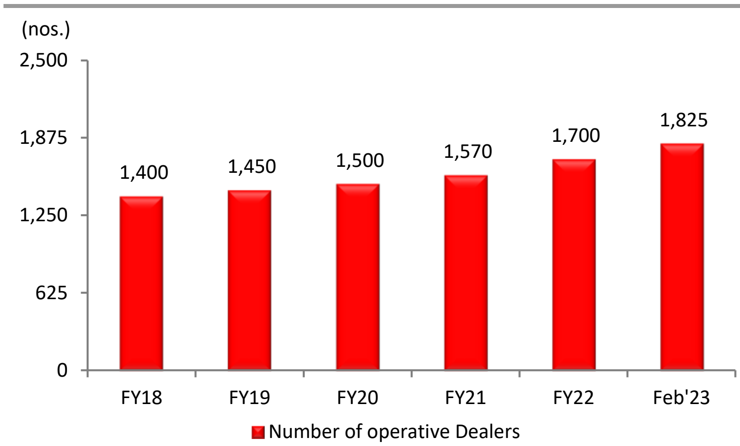
KJC recently opened a large 15,000 sq. ft. experience center in Mumbai (Andheri area) where it will showcase large slabs (emerging category) and bathroom products under *Kerovit* brand. It has outsourcing arrangement with Telangana-based South Asian Ceramic Tiles for ceramic wall and floor tiles, which has aided its entry into the markets in South India. Regular introduction of new SKUs, dedicated team to focus on enhancing look, feel and layout of dealer showrooms, brand spend (over 3% of revenue) and various brand awareness initiatives at the national/regional/local levels are factors that drive footfalls for its dealers.

India's leading tiles players' organised market share by value



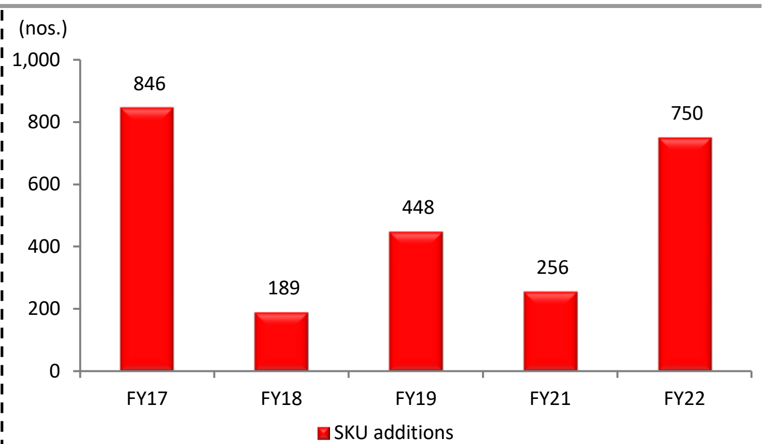
Source: Company, Systematix Institutional Research

Exhibit 15: Pan India dealer network



Source: Company

Exhibit 16: SKU net additions in tiles



Source: Company

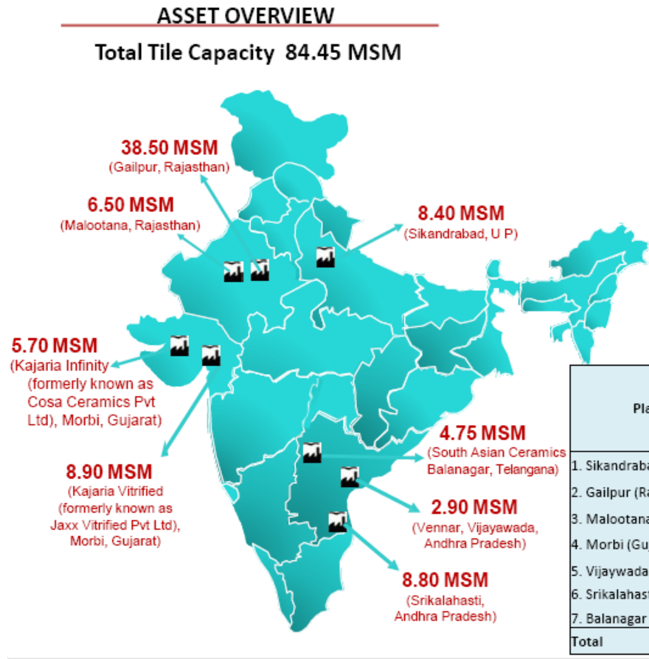
Exhibit 17: Tiles display at dealer showrooms

Source: Company

Exhibit 18: Five categories of exclusive outlets

Source: Company

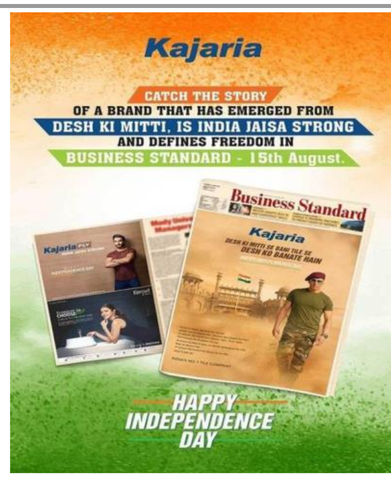
Exhibit 19: Manufacturing plants in all regions to serve pan India demand



Plant	Production Capacity (MSM)			
	Ceramic Wall & Floor Tiles	Polished Vitrified Tiles	Glazed Vitrified Tiles	Total
1. Sikandrabad (UP)	-	-	8.40	8.40
2. Gailpur (Rajasthan)	29.40	-	9.10	38.50
3. Malootana (Rajasthan)	-	6.50	-	6.50
4. Morbi (Gujarat)	-	8.90	5.70	14.60
5. Vijaywada (AP)	2.90	-	-	2.90
6. Srikalahasti (AP)	-	-	8.80	8.80
7. Balanagar (Telangana)	4.75	-	-	4.75
Total	37.05	15.40	32.00	84.45

Source: Company

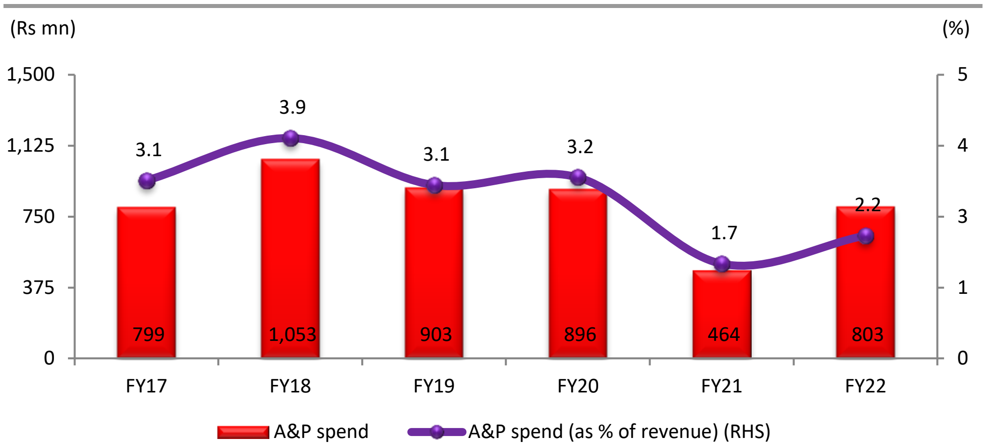
Exhibit 20: Branding efforts - Akshay Kumar as the brand ambassador for tiles



Branding at 30+ Indian airports

Source: Company

Exhibit 21: A&P spend has helped in market-share gains

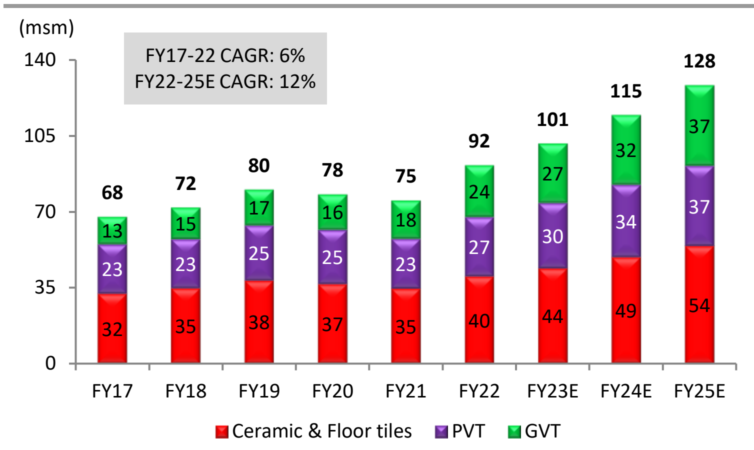


Source: Company

Tiles: Industry tailwinds to aid strong volume growth

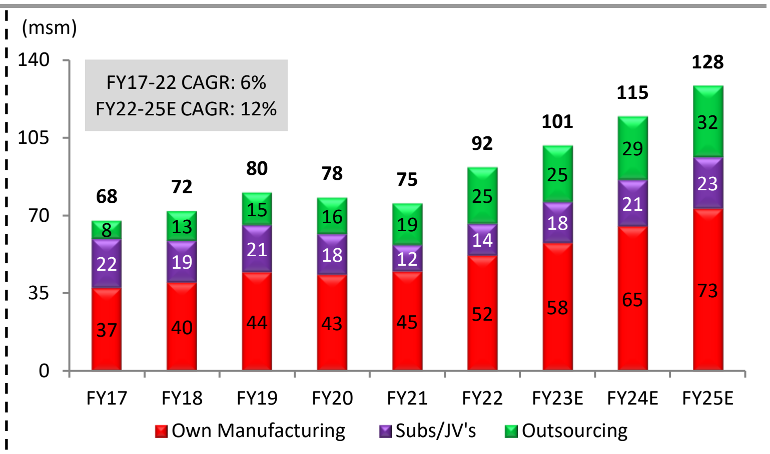
During 9MFY23 KJC's tiles volume/revenue increased 12%/21% YoY, and we estimate ~11%/17% YoY growth in FY23, respectively. While demand has been subdued in last two quarters owing to extended monsoon and festive season, we anticipate a rebound in 4Q. Strong demand from the housing sector and volume shift to exports by Morbi players augur well for KJC's volumes. Thus, we estimate 12%/14% CAGR in volume/revenue over FY22-25E (6%/7% CAGR over FY17-FY22), enabled by a) strong industry tailwinds, b) KJC's regular capacity additions in all regions, c) dealer network expansion and d) continued focus on branding.

Exhibit 22: Tiles volume mix trend – product wise



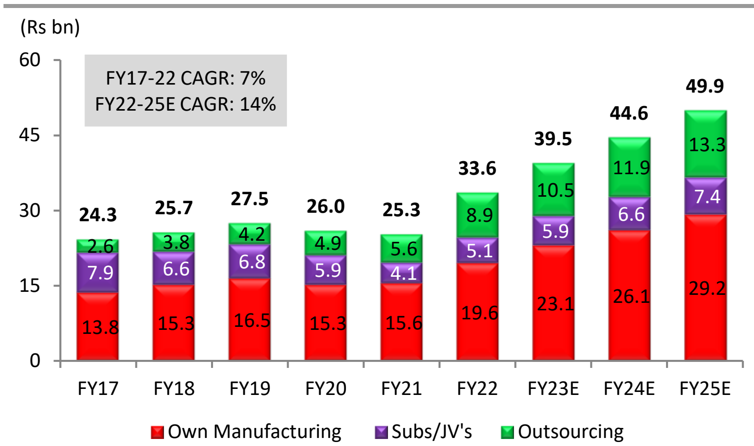
Source: Company, Systematix Institutional Research

Exhibit 23: Tiles volume mix trend – manufacturing & outsourcing



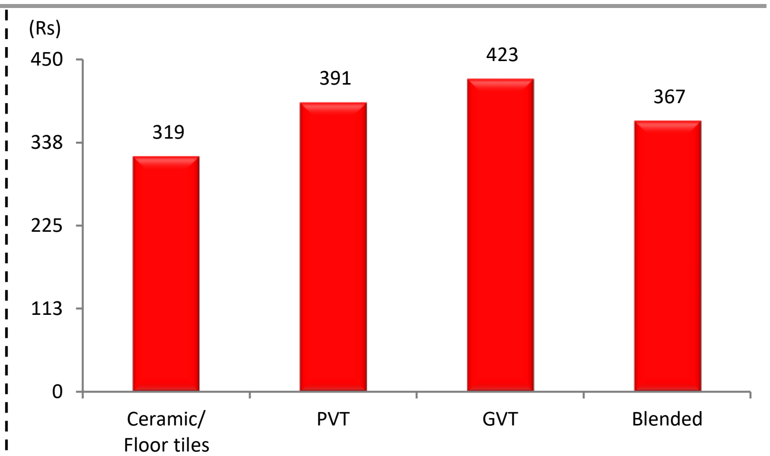
Source: Company, Systematix Institutional Research

Exhibit 24: Tiles - Revenue growth trend



Source: Company, Systematix Institutional Research

Exhibit 25: Net Sales Realisation (NSR, FY22)

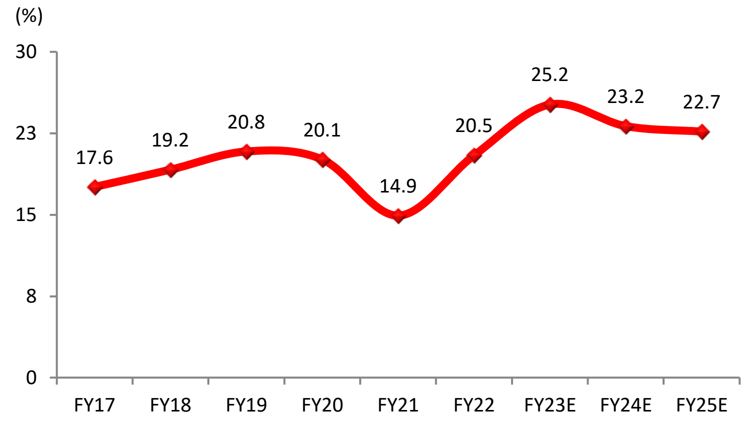


Source: Company, Systematix Institutional Research

Normalising gas prices, superior product mix to drive margins

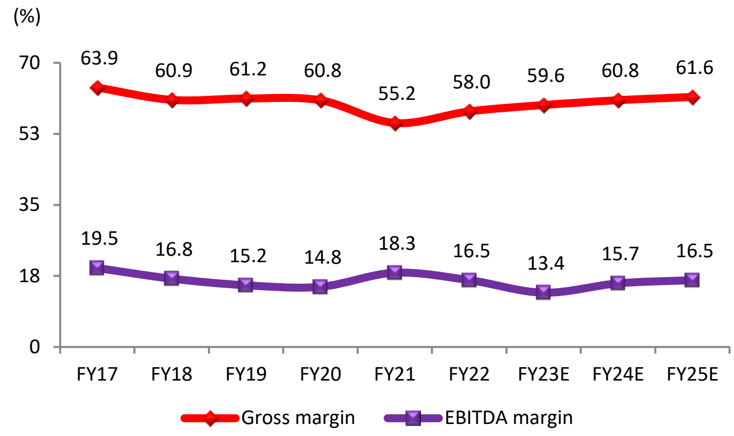
Power & fuel costs, which historically ranged 17-20% of revenue, surged to over 25% of revenue and thus hurt KJC's EBITDA margins (from 18.3% in FY21 to 13.4% in FY23E). Greater mix of higher-margin glazed vitrified tiles (GVT) and price hikes across its product range drove 16% increase in blended realisation during FY21-23E but was inadequate to sustain healthy margins. However, normalising gas prices and continued focus on value-added products should aid profitability ahead, in our view.

Exhibit 26: Power & fuel cost (as % of revenue)



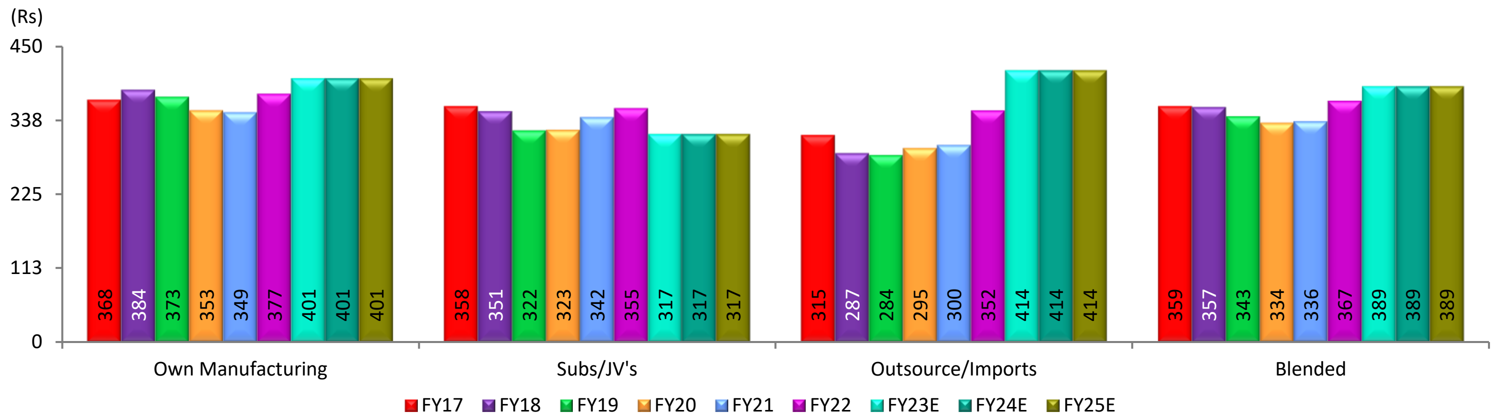
Source: Company, Systematix Institutional Research

Exhibit 27: Gross, EBITDA margin trend



Source: Company, Systematix Institutional Research

Exhibit 28: Tiles – blended NSR trend (/sq. m.)



Source: Company, Systematix Institutional Research

Large slabs, an emerging product

- KJC newly-launched *Vitronite* range as a replacement to granite slabs used on kitchen tops / table tops has gained high acceptance. This new application product will likely KJC in extending its distribution bandwidth to non-tile channels.
- Large slabs is an emerging and fast growing value-added product segment that is replacing marbles due to its lower price, superior uses (high resistance to oil stains) and attractive design. While large capacities have been added in the GVT category over last few years, there are only a few large slab manufacturers currently. KJC has set up capacities in Srikalahasti (AP) and plans to enhance capacities in Sikandarabad (UP) by 1.8 msm to 10.2 msm by 2QFY24.
- KJC makes 4x8 feet large slabs using Continua+ technology from SACMI, Italy, which provides enhanced strength to the product.

Expanding into adjacencies; bathware gaining scale

After retaining its numero uno status in tiles, KJC has entered adjacent product categories such as bathware (sanitaryware, faucets), plywood and tile adhesives over the last decade. While these new product lines contribute only ~10% to KJC's total revenue, management hopes to profitably grow them at a rapid pace in the coming years via channel expansion. It has therefore engaged celebrities like Anushka Sharma and Ranveer Singh as *Kerovit's* brand ambassadors.

Kerovit By Kajaria

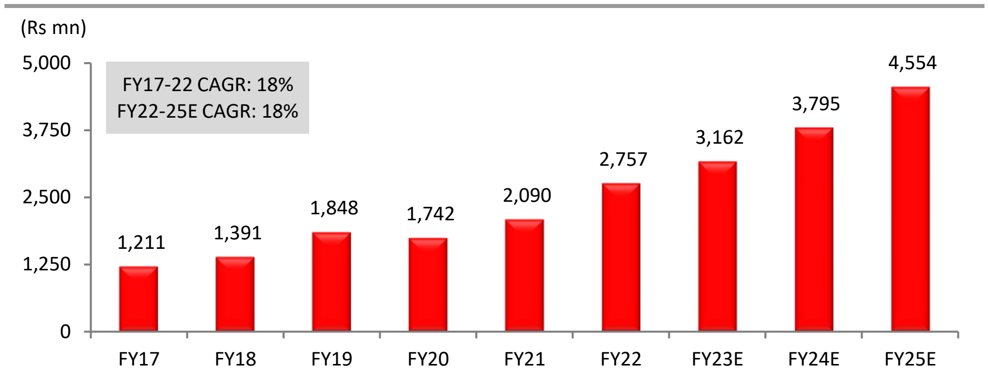
Branding efforts at Kajaria showroom

KJC entered the bathware segment by launching sanitaryware and faucets under the *Kerovit* brand. The company has carefully positioned its products between the premium MNC range and unbranded players, a relatively uncluttered space. Products are priced at par with *Cera* and *Hindware*, and at 2-3% discount to *Jaguar*.

The bathroom segment posted slow growth in the initial years due to the company's strategy of selling products only through large format stores (1,000-1,500 sq. ft.), which overlapped only 25% with its existing tiles stores. Now, under its new associate dealer programme, any dealer, even the one with 150 sq. ft. store size can sell KJC's bathroom products. The company plans to add over 100 stores in the next 12-18 months with a revenue potential of Rs 500mn. Management expects 30%+ CAGR and double-digit margins in the bathware segment in the coming years (18% CAGR over FY17-22), boosted by a) industry tailwinds, b) product innovation, c) strengthening dealer network, d) brand recall, and e) rising scale of operation.

KJC operates the bathware business under its subsidiary Kajaria Bathware in which it holds 85% stake. The balance 15% stake is owned by WestBridge Crossover Fund, LLC. KJC plans to enhance its capacities annually in sanitaryware (0.75mn pieces at Morbi) and faucet (1mn pieces at Gailpur) by 0.6mn each by investing Rs 700mn and Rs 50mn, respectively.

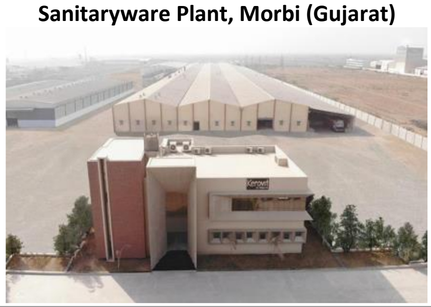
Exhibit 29: Bathware - Revenue trend



Source: Company, Systematix Institutional Research

Exhibit 30: Bathware manufacturing facilities

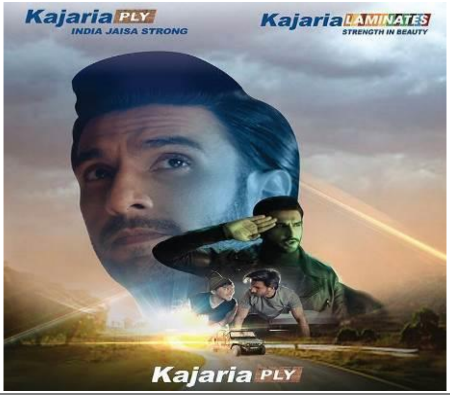
Sanitaryware Plant, Morbi (Gujarat)



Faucet Plant, Gailpur (Rajasthan)

Source: Company

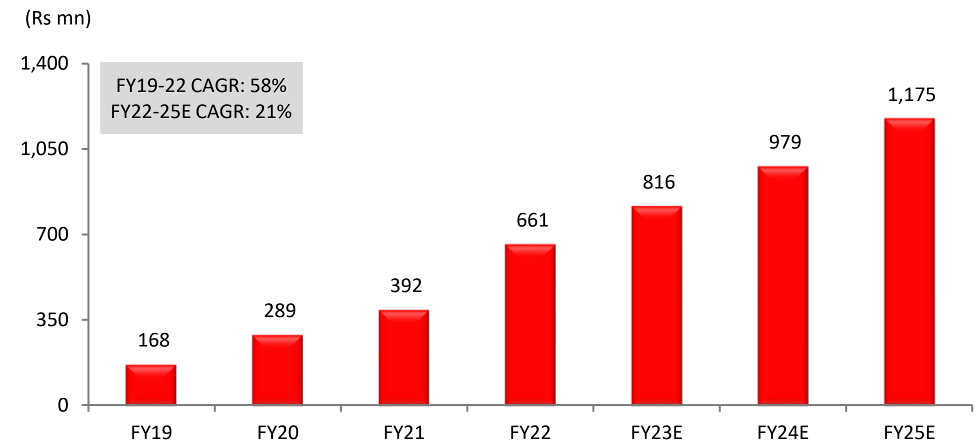
TV ad to promote wood-panel products



Plywood and laminates industry – Aims to become a meaningful player

Plywood and laminates is a vast ~Rs 300bn industry, 60% of which is dominated by the unorganised sector. In FY18, Kajaria entered the plywood sector to leverage its strong brand recall and distribution strength. It currently outsources products from vendors in Gujarat, Uttarakhand, West Bengal and Karnataka. The journey so far has been slow as it is yet to cross Rs 1bn revenue even after 8 years of existence, but the management is hopeful of scaling this business to large size in the coming years. The company has chosen celebrity Ranveer Singh as brand ambassador to increase visibility of its *KajariaPLY* and *KajariaLAMINATES* brands.

Exhibit 31: Plywood - Revenue trend

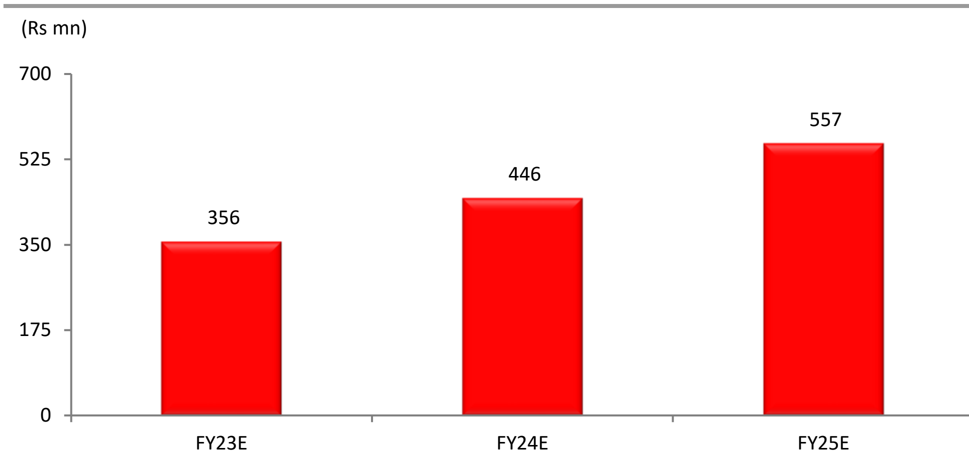


Source: Company, Systematix Institutional Research

Adhesives – Rs 350mn+ revenue likely in FY23

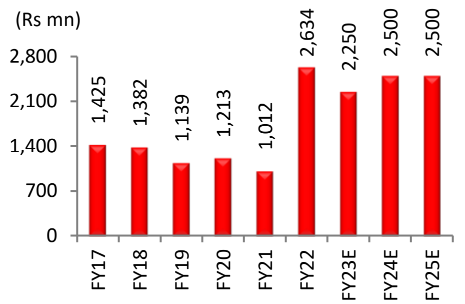
KJC has launched its tile adhesives products only in the last 2 years, which is estimated to clock Rs 350mn+ revenue in FY23. As a complementary product to its tiles division, the company aims to achieve significant growth in this product through increased awareness.

Exhibit 32: Adhesives - Revenue trend

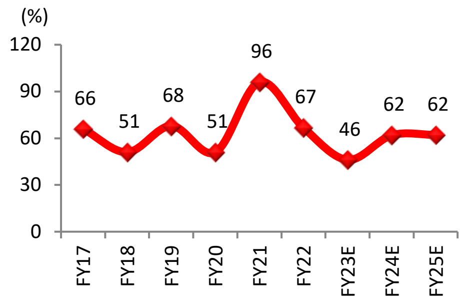


Source: Systematix Institutional Research

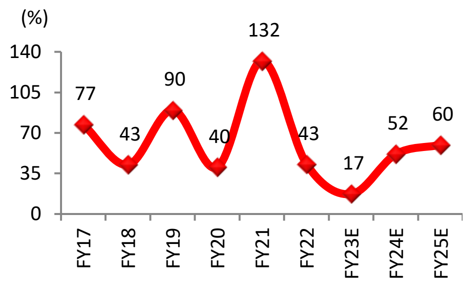
Capex



OCF/EBITDA (%)



FCF/PAT (%)



Source: Company, Systematix Institutional Research

Cash flows strong, despite regular high capex

KJC has stepped up the amount it seeks to invest in capex since FY22, anticipating strong demand in the coming years. It is looking to invest more than Rs 2.5bn annually to meet its volume growth guidance of 13-15%. During 9MFY23, it added ~14msm of capacity, which now is at 84.5msm. Continuous capex would increase capacity by ~10msm each year for the next few years. Additionally, KJC will continue to explore partnerships to outsource its products.

During 9MFY23, KJC added ~14msm of tile capacity, which includes 4.4msm PVT in Morbi, 6msm ceramic floor tiles in Rajasthan and Telangana, and 3.8msm GVT in AP. The 51% stake that KJC has acquired in South Asian Ceramic Tiles in Telangana operates at a capacity of 4.8msm, which will likely help in expanding its ceramic tiles business in the markets of South India.

KJC has stepped up the amount it seeks to invest in capex since FY22, anticipating strong demand in the coming years. It is looking to invest over Rs 2.5bn annually to achieve its volume growth guidance of 13-15%.

We cite the following key developments:

- **Modernisation of Gailpur facility** at Rs 511mn to produce larger-sized ceramic tiles likely to be completed by July 2023
- **Sikandrabad facility (UP)** expansion-cum-modernisation to manufacture larger-sized GVT products (by 1.8msm to 10.2msm) with the latest continua technology expected to be completed by Sep'23
- **Investment in Nepal:** KJC plans to set up 8msm of tile capacity in Nepal through a JV, and would invest up to Rs 1.25bn (50% of the project cost of Rs 2.5bn) on it.
- **Faucet plant at Gailpur** to add 0.6mn pieces for Rs 50mn to reach a total capacity of 1.6mn by Mar'23
- **Sanitaryware at Morbi** to add 0.6mn pieces for Rs 700mn to reach a total capacity of 1.35mn by Dec'23

Exhibit 33: Tiles capacity addition, Capex, OCF, FCF trend

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E	CAGR FY22-25E	CAGR FY17-22
Tiles Capacity (msm)	**68.90**	**68.40**	**68.00**	**73.00**	**70.40**	**70.40**	**87.59**	**93.59**	**99.59**	12	0
YoY (%)		*(1)*	*(1)*	*7*	*(4)*	*-*	*24*	*7*	*6*		
Sanitaryware capacity (mn pcs)	0.54	0.54	0.65	*0.75*	*0.75*	*0.75*	1.35	1.35	1.35	22	7
YoY (%)		-	*20*	*15*	-	-	*80*	-	-		
Faucets capacity (mn pcs)	1.00	1.00	1.00	1.00	1.00	1.00	1.60	1.60	1.60	17	-
YoY (%)		-	-	-	-	-	60	-	-		
Capex (Rs mn)	1,425	1,382	1,139	1,213	1,012	2,634	2,250	2,500	2,500		
OCF (Rs mn)	3,316	2,382	3,174	2,244	5,088	4,255	2,832	4,979	5,990		
FCF (Rs mn)	1,891	1,000	2,034	1,031	4,076	1,621	582	2,479	3,490		

Source: Company, Systematix Institutional Research

Financial Outlook

We estimate revenue/PAT of 15%/16% CAGR over FY22-25E (~8% CAGR each over FY17-22), with healthy 20%+ RoE and strong FCF. Healthy demand from the housing sector and shift in volumes to exports by Morbi players augur well for KJC's tiles volumes. We thus estimate 12%/14% CAGR in volume/revenue in tiles over FY22-25E (6%/7% CAGR over FY17-FY22), led by a) strong industry tailwinds, b) KJC's regular capacity additions in all regions, c) expansion in dealer network, and d) continued focus on branding. In its new product lines (bathware, wood panel, adhesives; ~10% of total revenue), management anticipates profitable growth at a rapid pace through branding efforts and channel expansion. We estimate ~Rs 3bn of annual FCF despite the company's annual spend of Rs 2.5bn towards capacity addition.

Exhibit 34: Key assumptions

	FY21	FY22	FY23E	FY24E	FY25E	CAGR FY22-25E
Consolidated Revenue (Rs mn)	27,809	37,052	43,791	49,805	56,221	15
YoY (%)	*(1)*	*33*	*18*	*14*	*13*	
Tiles Revenue (Rs mn)	25,328	33,634	39,456	44,585	49,936	14
YoY (%)	*(3)*	*33*	*17*	*13*	*12*	
Tiles Volume (msm)	75	92	101	115	128	12
YoY (%)	*(3)*	*21*	*11*	*13*	*12*	
Tiles Realisations (Rs/ sq.m.)	336	367	389	389	389	2
YoY (%)	*1*	*9*	*6*	-	-	
Bathware Revenue (Rs mn)	2,090	2,757	3,162	3,795	4,554	18
YoY (%)	*20*	*32*	*15*	*20*	*20*	
Plywood Revenue (Rs mn)	392	661	816	979	1,175	21
YoY (%)	*35*	*69*	*24*	*20*	*20*	
Adhesives revenue (Rs mn)*	-	-	356	446	557	25
YoY (%)	-	-	-	*25*	*25*	

**Adhesives revenue CAGR is for FY23-25*

Exhibit 35: Revenue (consolidated)

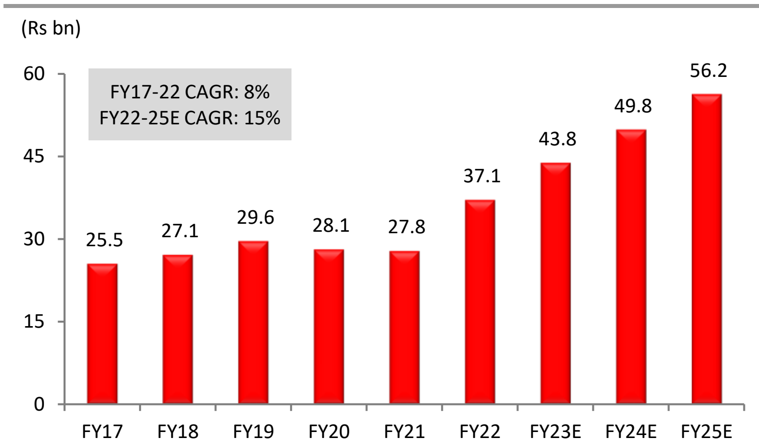
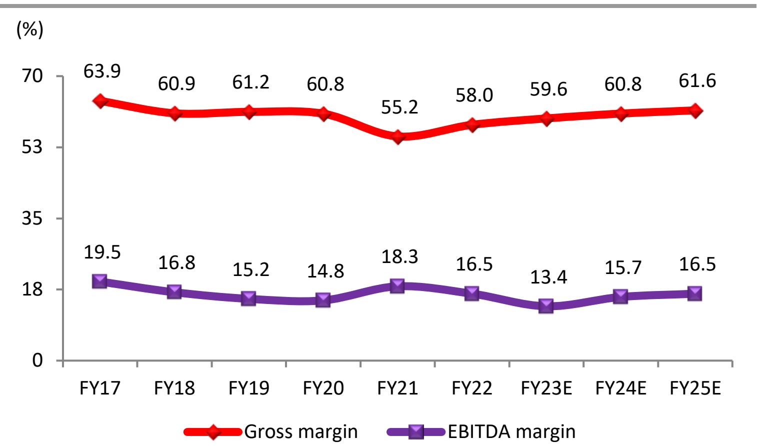


Exhibit 36: Gross, EBITDA margins (%)



Source: Company, Systematix Institutional Research

Exhibit 37: EPS, PAT margin (%)

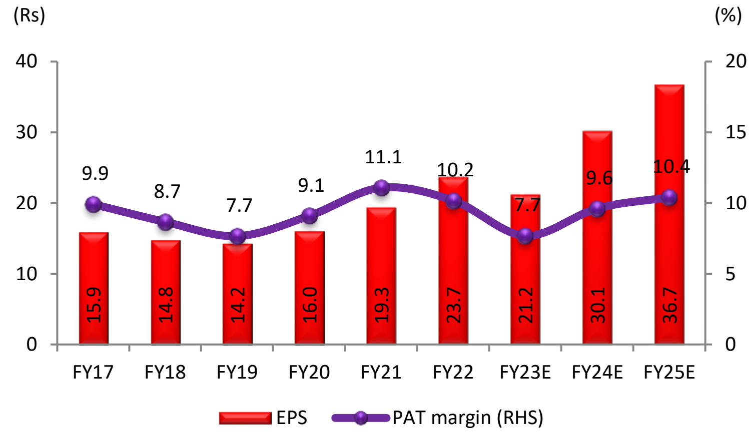


Exhibit 38: RoE, RoCE trend

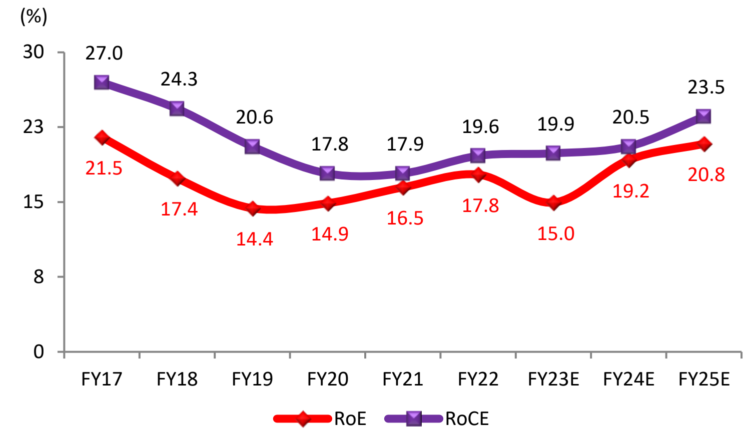


Exhibit 39: Working capital cycle

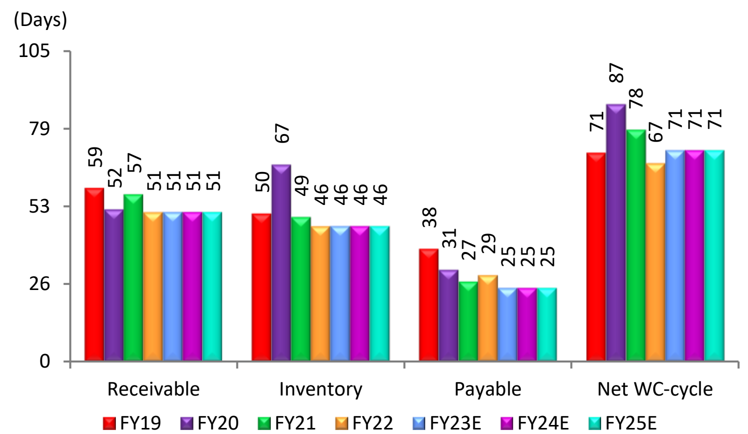


Exhibit 40: OCF, capex and FCF trend

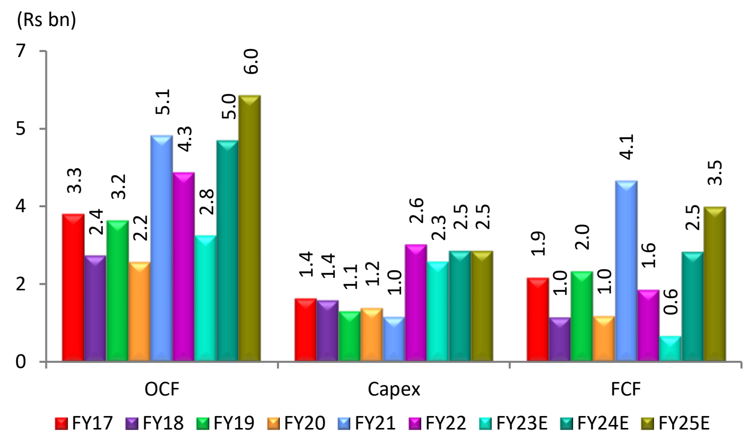


Exhibit 41: OCF/EBITDA (%)

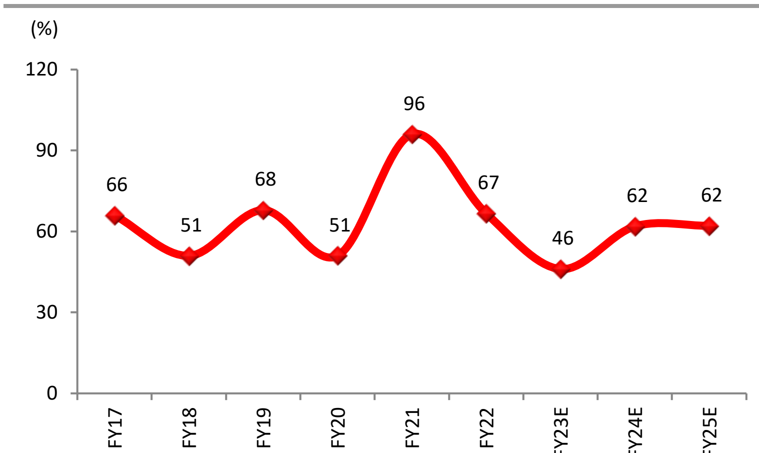


Exhibit 42: FCF/PAT (%)

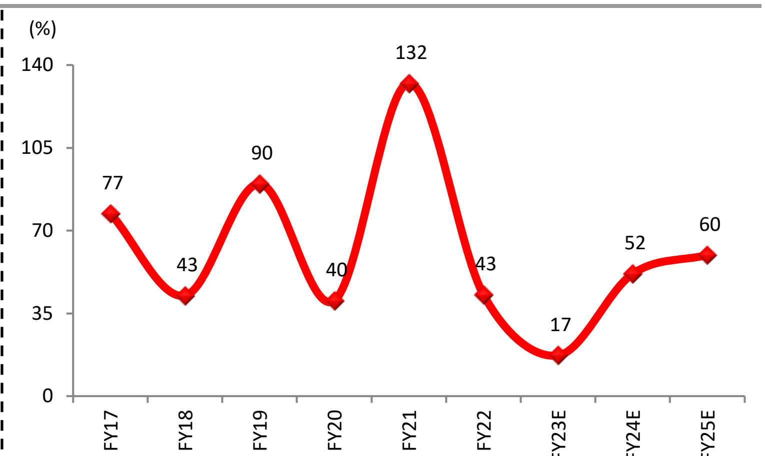


Exhibit 43: DuPont analysis

	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
RoE (%)	14.4	14.9	16.5	17.8	15.0	19.2	20.8
PAT margin (%)	*7.7*	*9.1*	*11.1*	*10.2*	*7.7*	*9.6*	*10.4*
Total Asset Turnover (x)	*2.3*	*1.8*	*1.6*	*2.0*	*2.2*	*2.3*	*2.3*
Equity Multiplier (x)	*0.8*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*

Source: Company, Systematix Institutional Research

Outlook and Valuation

We initiate coverage on KJC with a BUY rating and a target price of Rs 1,249, based on 34x FY25E P/E. The company's a) number one status in tiles, b) execution capabilities, backed by strong management, c) strong FCF, and d) focus on market share gains led by capacity addition and expansion in distribution reach are key positives. Notwithstanding the near-term weakness in volume and margins, we believe KJC's medium-to-long-term outlook is quite robust.

KJC's stock price has been consolidating since past one year owing to significant run-up in the previous 2 years and muted volume growth and margins since 2QFY23 on company's inability to fully pass on the rise in power & fuel costs. We expect its business performance to recover 4Q onwards spurred by improving demand, plummeting competition from Morbi (strong rebound in exports) and meaningful decline in gas prices. KJC's healthy outlook in the medium term is based on housing sector upcycle and market-share gains arising from KJC's continued focus on dealer network expansion and branding efforts. Factoring in these upsides, we expect KJC to record decent 15%/16% CAGR in revenue/PAT over FY22-25E, respectively, with healthy 20%+ RoE and strong FCF despite high capex.

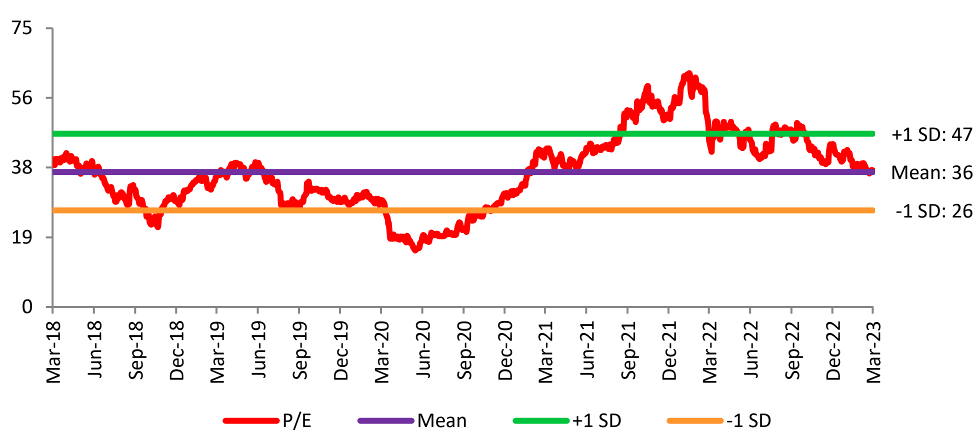
Key risks: Slowdown in economy and construction activities; high volatility in gas prices, intensifying competition from Morbi.

Exhibit 44: Systematix vs. Bloomberg estimates

(Rs mn)	Systematix estimates			Bloomberg estimates			% Var with Systematix		
	FY23	FY24	FY25	FY23	FY24	FY25	FY23	FY24	FY25
Total Income	43,791	49,805	56,221	43,681	50,233	57,616	0	(1)	(2)
EBITDA	5,852	8,200	9,256	5,921	7,893	9,433	(1)	4	(2)
EBITDA margin (%)	*13.4*	*16.5*	*16.5*	*13.6*	*15.7*	*16.4*			
PAT	3,370	5,089	5,849	3,512	4,959	6,059	(4)	3	(3)
EPS (Rs)	21.2	32.0	36.7	22.0	31.5	38.5	(4)	2	(4)

Source: Bloomberg, Systematix Institutional Research

Exhibit 45: KJC – one year forward PE band and standard deviation (SD)



Source: BSE, Systematix Institutional Research

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net revenues (Rs mn)	**27,809**	**37,052**	**43,791**	**49,805**	**56,221**
Growth (%)	*(1)*	*33*	*18*	*14*	*13*
Direct costs	12,470	15,551	17,691	19,523	21,589
Gross Margin (%)	*55.2*	*58.0*	*59.6*	*60.8*	*61.6*
SG&A	10,251	15,394	20,247	22,480	25,376
EBITDA	**5,088**	**6,107**	**5,852**	**7,801**	**9,256**
EBITDA margins (%)	*18.3*	*16.5*	*13.4*	*15.7*	*16.5*
- Depreciation	1,067	1,154	1,321	1,494	1,687
Other income	213	276	297	249	394
Interest Exp	107	127	201	125	112
PBT	4,127	5,102	4,628	6,432	7,851
Effective tax rate (%)	*25.2*	*25.0*	*26.4*	*25.5*	*25.5*
+ Associates/(Minorities)	(9)	(58)	0	-	-
Net Income	**3,081**	**3,770**	**3,370**	**4,792**	**5,849**
Adjusted income	3,081	3,770	3,370	4,792	5,849
WANS	159	159	159	159	159
FDEPS (Rs)	19	24	21	30	37
FDEPS growth (%)	*21*	*22*	*(11)*	*42*	*22*

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Share capital	159	159	159	159	159
Net worth	18,689	21,224	22,524	24,928	28,070
Total debt	1,142	1,521	1,426	1,431	1,436
Minority interest	646	648	653	658	663
DT Liability/(Asset)	674	726	705	684	663
Capital Employed	**21,151**	**24,119**	**25,308**	**27,701**	**30,832**
Net tangible assets	11,812	11,388	12,317	15,823	16,636
Net Intangible assets	28	24	24	24	24
Goodwill	85	85	85	85	85
CWIP	149	2,634	2,634	134	134
Investments (Strategic)	-	-	-	-	-
Investments (Financial)	50	-	-	-	-
Current Assets	8,703	11,485	13,306	14,935	16,671
Cash	4,428	4,244	2,761	2,990	4,072
Current Liabilities	4,102	5,739	5,817	6,289	6,789
Working capital	4,601	5,745	7,488	8,646	9,882
Capital Deployed	**21,151**	**24,119**	**25,308**	**27,701**	**30,832**
Contingent Liabilities	96	224	-	-	-

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
EBIT (incl. other income)	4,133	5,008	4,457	6,264	7,523
+ Non-cash items	1,067	1,154	1,321	1,494	1,687
OCF before WC changes	5,200	6,161	5,778	7,758	9,210
- Incr./(decr.) in WC	(753)	574	1,733	1,147	1,226
Others including taxes	865	1,333	1,213	1,631	1,993
Operating cash-flow	5,088	4,255	2,832	4,979	5,990
- Capex	1,012	2,634	2,250	2,500	2,500
Free cash-flow	4,076	1,621	582	2,479	3,490
Acquisitions					
- Dividend	1,591	1,273	2,070	2,388	2,706
+ Equity raised	53	52	-	-	-
+ Debt raised	(302)	281	(95)	5	5
- Fin Investments	(54)	(51)	-	-	-
- Misc. Items (CFI + CFF)	2,202	657	(96)	(125)	(281)
Net cash-flow	87	75	(1,486)	220	1,070

Source: Company, Systematix Institutional Research

Ratios @ Rs 1,050

YE: Mar	FY21	FY22	FY23E	FY24E	FY25E
P/E (x)	54.3	44.3	49.6	34.9	28.6
EV/EBITDA (x)	32.2	26.9	28.3	21.2	17.8
EV/sales (x)	5.9	4.4	3.8	3.3	2.9
P/B (x)	8.9	7.9	7.4	6.7	6.0
RoE (%)	16.5	17.8	15.0	19.2	20.8
RoCE (%)	17.9	19.6	19.9	20.5	23.5
ROIC	18.0	20.6	15.9	20.3	22.7
DPS (Rs per share)	10.0	11.0	13.0	15.0	17.0
Dividend yield (%)	1.0	1.0	1.2	1.4	1.6
Dividend payout (%)	51.7	46.5	61.4	49.8	46.3
Net debt/equity (x)	(0.2)	(0.1)	(0.1)	(0.1)	(0.1)
Receivables (days)	57	51	51	51	51
Inventory (days)	49	46	46	46	46
Payables (days)	27	29	25	25	25
CFO:PAT%	165	113	84	104	102

Source: Company, Systematix Institutional Research

SYSTEMATIX INSTITUTIONAL EQUITIES

Somany Ceramics

06 March 2023

Focus on margin and cash flow over market share

INITIATING COVERAGE

Sector: Building Materials	**Rating: BUY**
CMP: Rs 525	**Target Price: Rs 605**

Stock Info	
Sensex/Nifty	59,809/17,594
Bloomberg	SOMC IN
Equity shares (mn)	42.5
52-wk High/Low	711/455
Face value	Rs 2
M-Cap	Rs 22bn/USD 270mn
3-m Avg turnover	USD 0.5mn

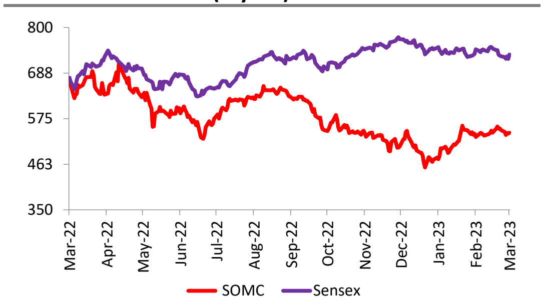
Financial Snapshot (Rs mn)

Y/E Mar	FY23E	FY24E	FY25E
Net sales	24,711	28,134	31,549
EBITDA	1,829	2,702	3,219
OPM (%)	7.4	9.6	10.2
PAT (adj.)	705	1,233	1,606
EPS (adj.) (Rs)	16.6	29.1	37.8
PE (x)	31.6	18.1	13.9
P/B (x)	2.8	2.5	2.2
EV/EBITDA (x)	14.4	9.5	7.6
RoE (%)	8.9	13.8	15.6
RoCE (%)	8.6	12.8	14.8
Net-D/E (x)	0.5	0.3	0.2

Shareholding Pattern (%)

	Dec'22	Sep'22	Jun'22
Promoter	54.8	54.8	54.8
- Pledged			
FII	1.7	2.3	2.4
DII	21.5	20.8	20.5
Others	22.0	22.1	22.3

Stock Performance (1-year)



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We initiate coverage on Somany Ceramics (SOMC) with a BUY rating and a target price of Rs 605, based on 16x FY25E P/E, for a low ~16% RoE in FY25E. The company went through a rough patch during FY17-20 due to industry and company-level issues, post which, it managed to meaningfully improve its financial position by adopting corrective measures (credit discipline, cash flow focus, strengthening operations, and cleaning up its balance sheet). We believe these should trigger a re-rating in its valuation multiples. Notwithstanding the near-term weakness, SOMC's medium-to-long-term prospects are robust.

India's leading tiles player is spreading its wings in small towns: SOMC is a leading tiles manufacturer in India, with an ~10% organised market share in value terms. Its 11 plants that manufacture tiles, sanitaryware and bath fittings are spread across India, which aid faster turnaround in serving over 9,000 point of sales (PoS) across regions. Management aims to expand its touchpoints at 10-15% CAGR over the next few years, with incremental focus on small towns. Its newly-commissioned plant in South India is helping in broad basing its sales footprint away from Morbi (Gujarat) and responding quicker to the needs in southern markets.

Focus on profitable growth, with stricter credit control: SOMC's financial performance was severely impacted during FY17-20 due to industry (weak demand, impacted by demonetisation and GST-related destocking by dealers) and company-specific (one-off losses related to defalcation by an employee, treasury management activities, stockbroker fraud, etc.) issues. The company broke its credit discipline and chose growth over higher credit (ballooned to 107 days in FY18 from ~60 days historically) to channels to combat intense competition from the unorganised sector. However, it has managed to achieve a meaningful turnaround since FY20 on the back of credit discipline and cash flows, which should allay investor concerns, in our view.

Capex does not depend on external funding: Following its stated strategy to aggressively expand capacities, SOMC added large ~11msm GVT capacity in 1HFY23, taking its total capacity to over 60msm. Another 4msm slab manufacturing plant is also likely to be operational during 1HFY24. Large capacity addition in the value-added premium segment should bode well for SOMC to improve its average realisation and margin, and enable the company to reposition itself as a premium tiles brand. SOMC aims to fund future capex mostly through internal accruals.

Improving financial strength: After a low 3%/2% CAGR in volume/revenue over FY17-22 (impacted by industry and company level issues), we estimate 12%/14% CAGR over FY22-25E, as SOMC has realigned its fundamentals and continues to see positive traction from the housing sector. Through improved product mix, higher market share and brand visibility and cost optimisation, SOMC aims to move up the value chain and expand margins. We estimate 15%/22% CAGR in revenue/PAT over FY22-25E (flattish over FY17-22), anticipating ~400bps surge in its EBITDA margin to 10.2% in FY25E. RoE could rise to ~16% with healthy cash flow in FY25E.

Initiate with a BUY: SOMC's stock price has significantly underperformed (down >25%) its peers in the last one year. After weak performance since 2QFY23 (on low volume growth and weak margin on inflationary pressure), management expects business recovery 4Q onward anticipating reduced competition from Morbi (strong rebound in exports) and decline in gas prices. On a healthy long-term outlook, we initiate coverage on SOMC with a **BUY** rating. ***Key Risks:*** Slowdown in the economy and construction activities, high gas prices, intensifying competition from Morbi.

Investors are advised to refer disclosures made at the end of the research report.

Story in charts…

Exhibit 1: Tiles volume growth

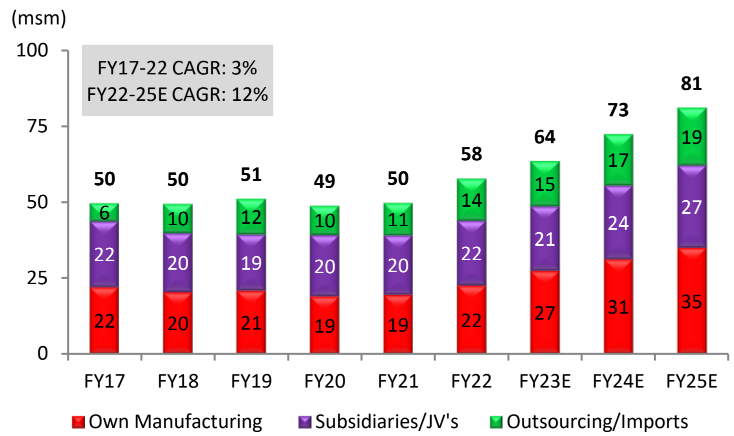


Exhibit 2: Tiles revenue growth

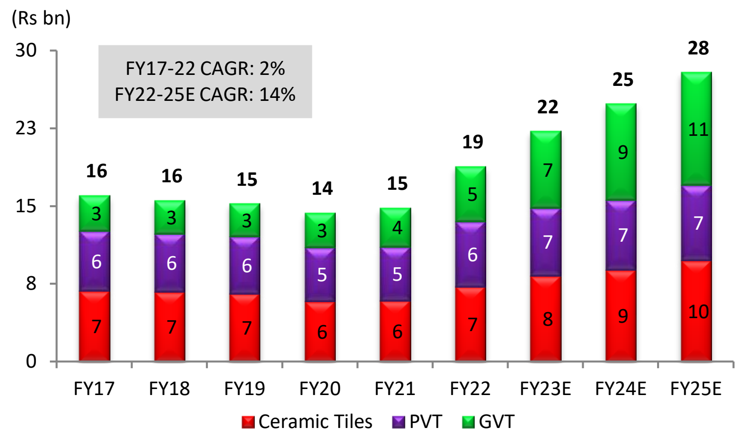


Exhibit 3: Consolidated revenue growth

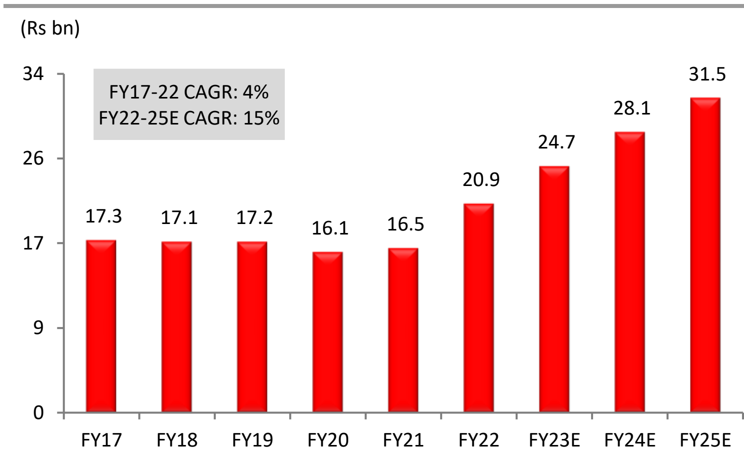


Exhibit 4: Gross, EBITDA margins

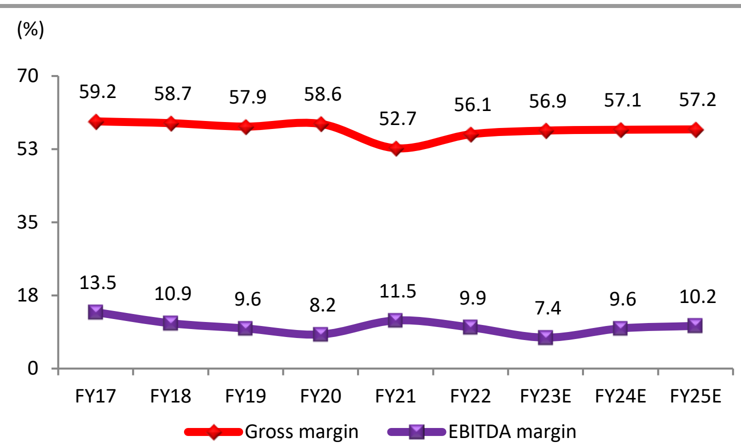


Exhibit 5: WC-cycle

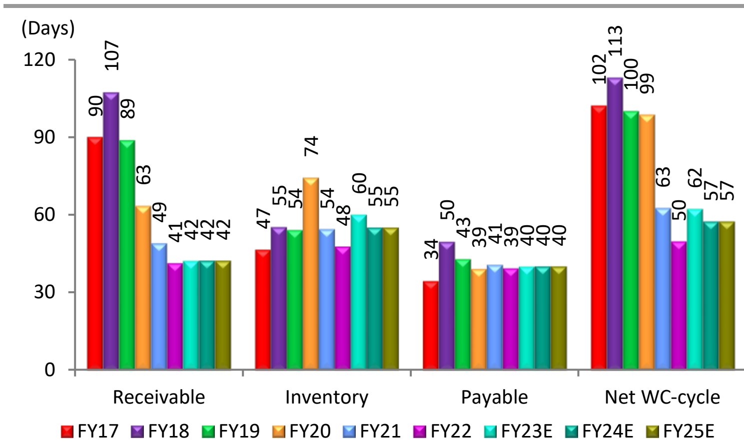
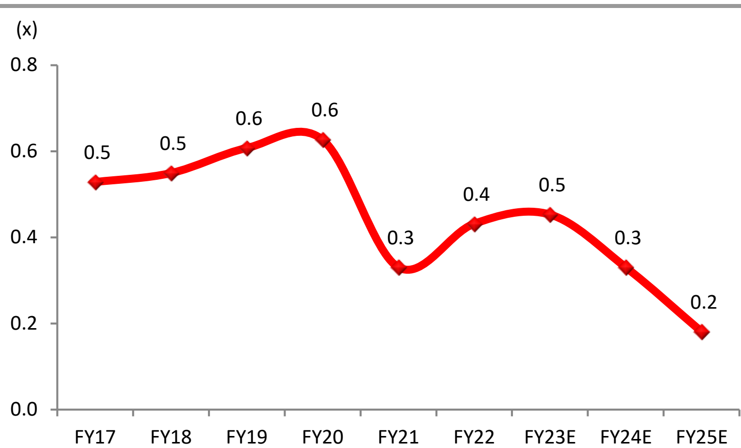


Exhibit 6: Net-debt/Equity

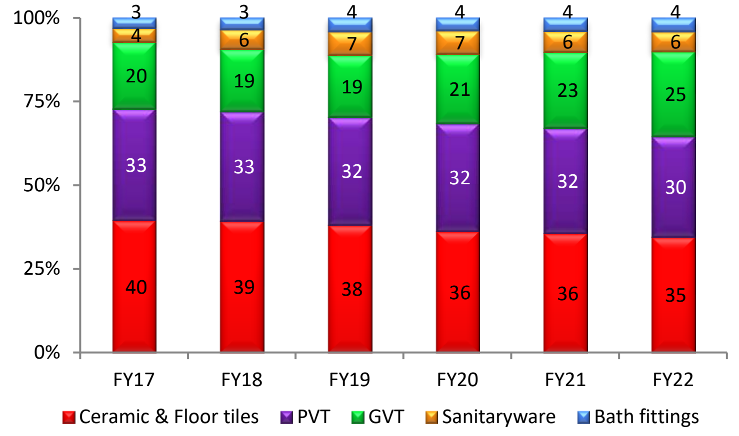


Source: Company, Systematix Institutional Research

Somany Ceramics - an overview

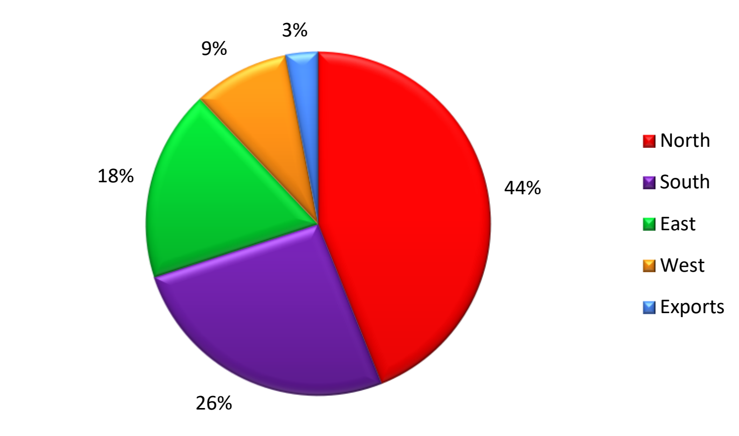
Somany Ceramics (SOMC), incorporated in 1968, is a leading tiles manufacturer in India with ~10% market share in the organised tile sector in value terms. The company has an aggregate production capacity of ~53 msm of tiles, 1.15 mn pieces of sanitaryware and 0.65 mn pieces of bath fittings, which it manufactures at its 11 units spread across India (helps in fast turnaround). The *Somany* brand is available across more than 9,000 PoS, which we estimate would grow at 10-15% CAGR in the coming years.

Exhibit 7: Revenue mix (product-wise) trend



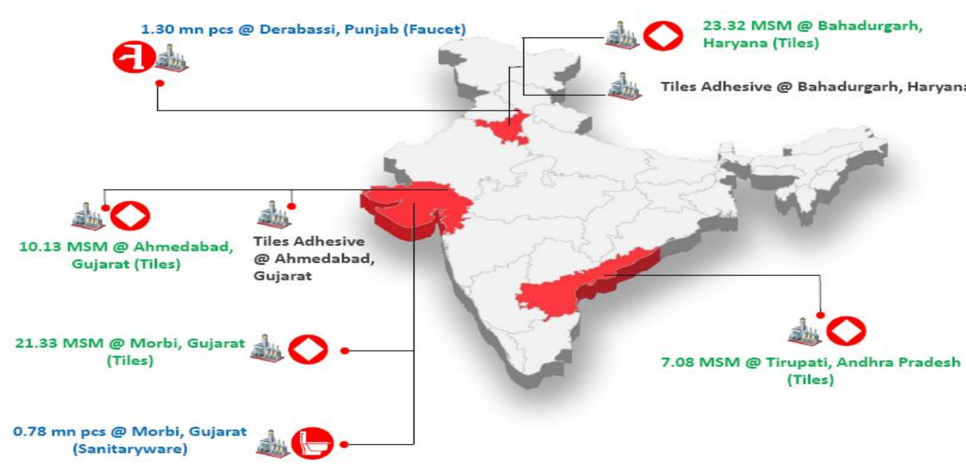
Source: Company

Exhibit 8: Revenue mix (zone-wise) FY22



Source: Company

Exhibit 9: Manufacturing capacity details



Source: Company

Exhibit 10: Key Managerial Personnel

Name	Designation	Remarks
Shreekant Somany	CMD	He has played key role in spearheading the *SOMANY* brand to national level. He is well known person in the India tiles & ceramics industry.
Abhishek Somany	MD & CEO	A 3rd generation entrepreneur, Abhishek has about three decades of experience. He takes keen interest in the operational part and overall functioning of the company.

Source: Company

Key shareholders: Kotak AMC (6.7%), Franklin MF (4.5%), HSBC AMC (3.7%), New Mark Capital (1.9%), PGIM MF (1.1%)

Exhibit 11: SOMC - Journey so far

Year	Journey
1968	Company created by Late Shri Hira Lall Somany, in collaboration with Pilkington Tile Holding (UK)
1971	Somany Pilkington Limited established its first manufacturing unit in Kassar, Haryana
1981	Established manufacturing plant in Kadi, Gujarat
1994	Indian promoters acquire Pilkington shareholding
1995	Installed a new production line at Kassar (increased capacity by 6,000 sqm/ day)
2000	Began importing tiles from Europe under the *Somany Global* brand
2001	New floor tiles manufacturing plant set up at Kadi, at a capacity of 6,000 sqm/ day
2007	Changed the name of the Company to Somany Ceramics Ltd.; ventured into the sanitaryware space
2009	Received a patent for its VC Shield product, India's highest abrasion-resistant tile, first in India's tile industry.
2010	Commissioned its first glazed vitrified tiles (GVT) manufacturing facility; widened the bathware vertical
2011	Rebranded itself with a changed logo
2012	Launched the *Duragress* range of products
2014	Acquired a subsidiary; commenced manufacturing sanitaryware
2018	Acquired a subsidiary; commenced manufacture of bath fittings
2019	Commissioned its first manufacturing facility in South India and engaged the celebrity Salman Khan as its brand ambassador; Ventured into the water heater business
2020	Became a net debt-free company at standalone level

Source: Company

Recent performance and management commentary

Overall muted demand in the industry caused pressure on volumes and sales realisations. Rising interest rates, coupled with an extended monsoon and festivity season led to lower volume uptake since 2QFY23. Substantial increase in gas costs took its toll on margins. However, with gas prices beginning to soften, management expects margins to improve in the coming quarters. Despite global challenges, India's tile industry is likely to benefit from government's infrastructure spending focus and softening gas prices. SOMC continues to work towards moving up the value chain by improving its product mix, increasing market share and brand visibility, as also optimising costs.

Exhibit 12: SOMC - Quarter results (consolidated)

(Rs mn)	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	YoY (%)	QoQ (%)	9MFY23	9MFY22	YoY (%)
Total Income	**5,870**	**6,168**	**5,591**	**6,178**	**6,224**	**6**	**1**	**17,993**	**14,777**	**22**
Raw material costs	2,435	2,960	2,163	2,636	2,784	14	6	7,583	6,245	21
Employee costs	664	660	712	737	758	14	3	2,571	1,912	34
Power & fuel	1,530	1,370	1,706	1,728	1,547	1	(10)	4,980	3,440	45
Other expenses	595	672	562	655	729	23	11	1,946	1,621	20
EBITDA	**646**	**507**	**449**	**422**	**406**	**(37)**	**(4)**	**1,277**	**1,559**	**(18)**
Depreciation	156	171	154	170	168	8	(1)	492	616	(20)
Finance costs	74	64	73	96	119	61	24	287	233	23
Other income	25	15	40	29	41	61	40	110	120	(8)
Exceptional items	-	-	-	(22)	-	-	-	(22)	-	-
PAT after JV/Associate	**322**	**172**	**205**	**147**	**120**	**(63)**	**(19)**	**472**	**715**	**(34)**
EPS (Rs)	7.6	4.0	4.8	3.5	2.8	(63)	(19)	11.1	16.8	(34)
As % Total Income						**YoY (bps)**	**QoQ (bps)**			**YoY (bps)**
Gross margin	**58.5**	**52.0**	**61.3**	**57.3**	**55.3**	**(326)**	**(206)**	**57.9**	**57.7**	**11**
Employee costs	11.3	10.7	12.7	11.9	12.2	87	25	14.3	12.9	135
Power & fuel	26.1	22.2	30.5	28.0	24.9	(122)	(311)	27.7	23.3	440
Other expenses	10.1	10.9	10.0	10.6	11.7	158	112	10.8	11.0	(16)
EBITDA margin	**11.0**	**8.2**	**8.0**	**6.8**	**6.5**	**(449)**	**(32)**	**7.1**	**10.5**	**(345)**
Effective tax rate	22.8	28.3	26.3	28.7	28.4	559	(36)	27.5	25.4	210
PAT	**5.8**	**3.3**	**3.5**	**1.9**	**1.8**	**(398)**	**(5)**	**2.4**	**4.9**	**(257)**
Segment revenue						**YoY (%)**	**QoQ (%)**			**YoY (%)**
Own Manufacturing	*1,956*	*1,906*	*1,928*	*2,465*	*2,369*	*21*	*(4)*	*6,762*	*5,218*	*30*
Subs (tiles)	*1,831*	*2,089*	*1,637*	*1,794*	*1,816*	*(1)*	*1*	*5,247*	*4,744*	*11*
Outsourcing/Imports	*1,338*	*1,362*	*1,234*	*1,158*	*1,246*	*(7)*	*8*	*3,639*	*3,038*	*20*
Tiles - Total	**5,126**	**5,358**	**4,799**	**5,418**	**5,431**	**6**	**0**	**15,648**	**13,000**	**20**
Bathware	**576**	**621**	**531**	**545**	**580**	**1**	**6**	**1,656**	**1,397**	**19**
Others	**77**	**61**	**70**	**99**	**107**	**40**	**9**	**276**	**168**	**64**
Tiles - sales volume (msm)						**YoY (%)**	**QoQ (%)**			**YoY (%)**
Own Manufacturing	6.1	5.8	5.8	7.3	7.0	16	(3)	20.1	16.7	21
Subs/JV's	5.5	6.4	4.9	5.1	5.3	(3)	3	15.3	15.2	1
Outsourcing/Imports	4.0	4.0	3.6	3.5	3.8	(6)	9	10.9	9.9	10
Total tiles volume	**15.6**	**16.1**	**14.3**	**15.9**	**16.2**	**4**	**2**	**46.3**	**41.8**	**11**
Tile - NSR (Rs/sq mtr)						**YoY (%)**	**QoQ (%)**			**YoY (%)**
Own Manufacturing	323	331	331	340	337	4	(1)	336	313	7
Subs/JV's	334	328	336	350	343	3	(2)	343	313	10
Outsourcing/Imports	331	342	348	330	327	(1)	(1)	335	307	9
Blended	**329**	**333**	**337**	**341**	**336**	**2**	**(1)**	**338**	**311**	**9**

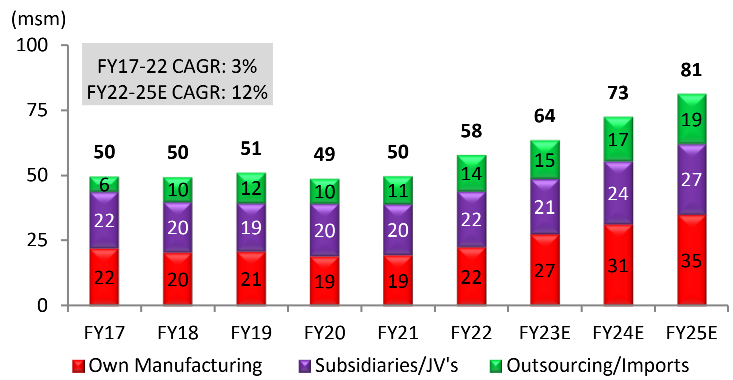
Source: Company, Systematix Institutional Research

Investment rationale

India's leading tiles player is spreading wings in small towns

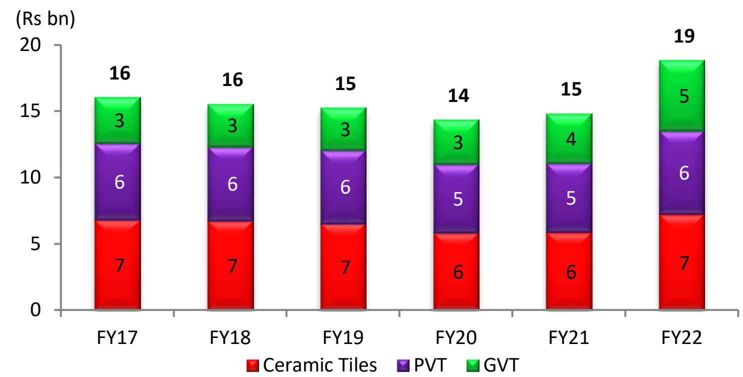
SOMC is India's leading tiles manufacturer, with ~10% market share in the organised tile sector in value terms. It's 11 plants that manufacture tiles, sanitaryware and bath fittings are spread across India. These enable faster turnaround in serving more than 9,000 PoS across these regions. Management expects to achieve 10-15% CAGR in its touchpoints over the next few years, and incrementally focus on small towns. Its newly commissioned plant in South India is helping in broad basing its sales footprint away from Morbi (Gujarat) and responding quicker to market needs in the southern markets.

Exhibit 13: Tiles - Volume trend



Source: Company, Systematix Institutional Research

Exhibit 14: Tiles - Revenue mix trend

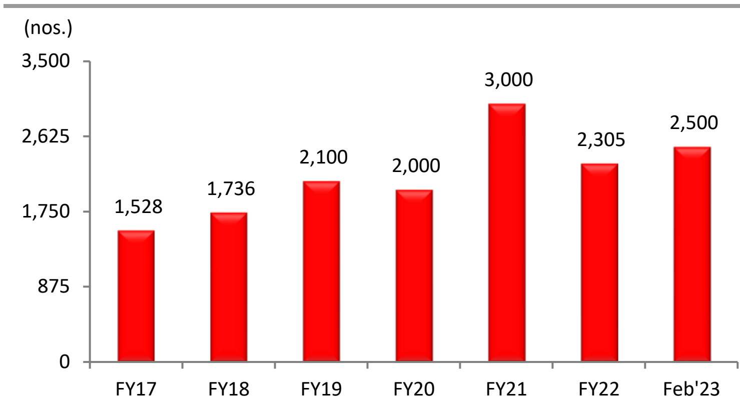


Source: Company

Expanding presence in small towns

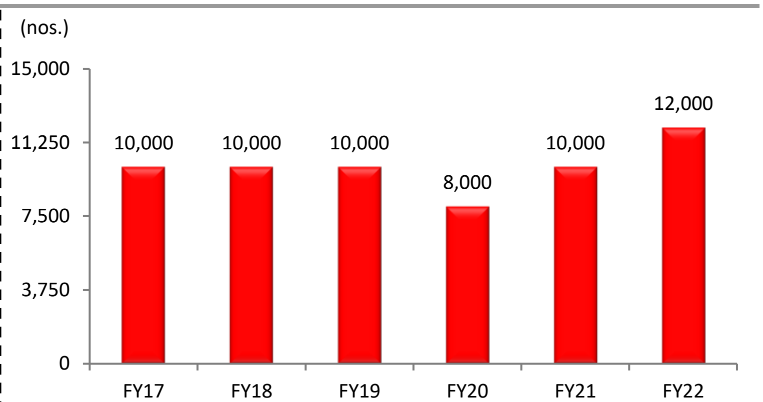
SOMC currently has over 9,000 PoS across regions, which include 3,000+ dealers and 6,000+ retailers. ~80% of these dealers are based in tier 3, 4 towns. Its long-standing associations with dealers (48% are associated since >5 years) has helped it in multiplying its stores. With keen focus on penetrating small towns, SOMC aims 10-15% CAGR in its touchpoints over next few years, 80% of which will be in tier 2 and below towns. Non-metro towns are relatively under-serviced by branded tile companies and, strengthening mind space and market share. To strengthen footprint and visibility, SOMC has set up 404 exclusive showrooms and 386 franchise outlets along with 18 company-owned display centres pan-India.

Exhibit 15: Active dealer trend



Source: Company

Exhibit 16: Point of sales

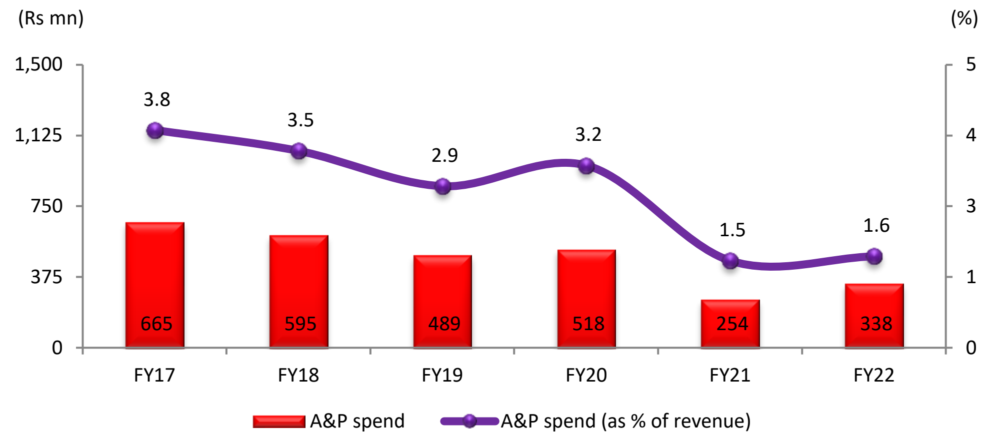


Source: Company

Branding efforts

Until FY20, SOMC was investing 3-4% of revenue on A&P, post which COVID hit and this fell to ~1.5% of revenue in last two years. Going forward, the company is looking to invest 2-3% of revenue in brand-building efforts. SOMC's brand ambassador engagement with actor Salman Khan was valid until 2022, which was likley to extend further. In addition to placing hoardings at major dealer points and at various tier 3, 4 towns, the company continued with its airport branding campaign '50 saalon ZSJ (Zameen se Judey)' at India's 4 major airports.

Exhibit 17: Trend in A&P spend (%)



Source: Company

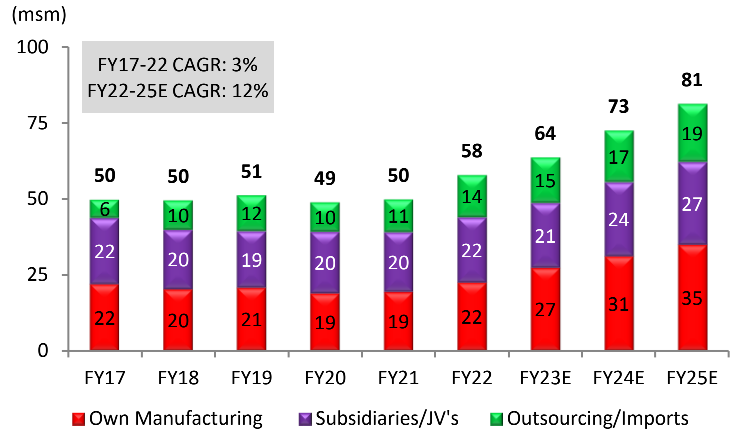
Exhibit 18: Branding efforts

Source: Company

Well placed to achieve robust volume growth in tiles

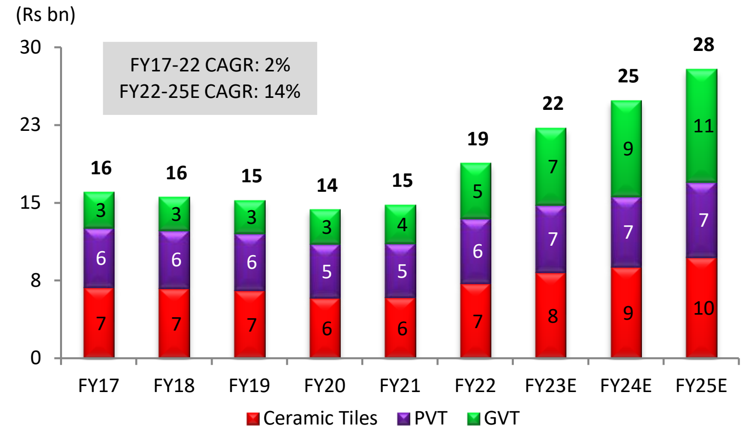
SOMC's 22% YoY revenue growth in 9MFY23 was driven by higher volumes in tiles (up 11%) and superior realisations. However, performance since 2QFY23 has been marred by muted demand and substantial rise in power & fuel costs which suppressed its EBITDA margin (down 345bps YoY to 7.1%). Despite global challenges, the Indian tile industry is likely to benefit from government's focus on infrastructure spending and softening gas prices since Jan'23. SOMC continues to benefit from improving its product mix (GVT), increasing market share and brand visibility, as also optimising costs. As a result, we estimate 12%/14% CAGR in volume/revenue over FY22-25E (low 3%/2% CAGR over FY17-22), with EBITDA margin expected to expand from 7.4% in FY23E to 10.2% in FY25E.

Exhibit 19: Tiles - Volume growth trend



Source: Company, Systematix Institutional Research

Exhibit 20: Tiles revenue growth (segment wise)

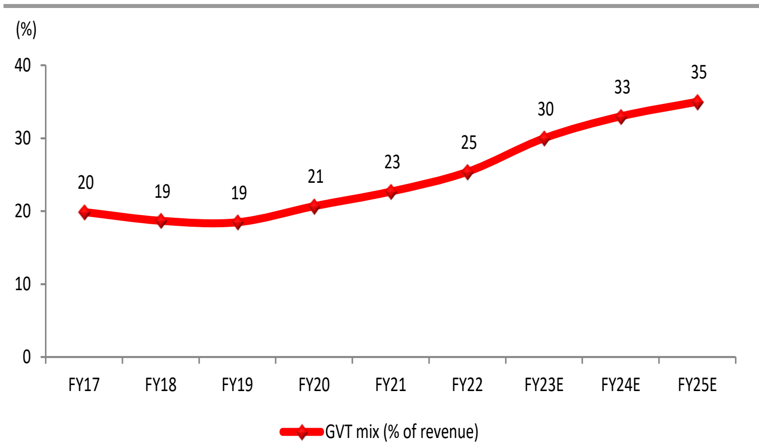


Source: Company, Systematix Institutional Research

Higher GVT mix augurs well for margins, brand premiumisation

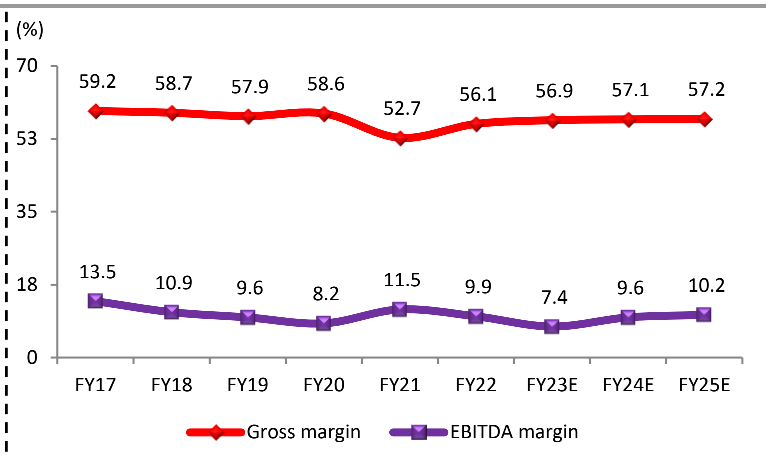
GVT enjoys best margins, followed by ceramic tiles and PVT for SOMC. The company has added ~11msm recently and 4msm more capacity will be added by 1QFY24. As a result, revenue mix of GVT has increased from 18.5% in FY19 to a likely ~30% in FY23 and is slated to touch 35% in the years to come. SOMC is also focusing on expanding in the fast-growing, value added large-slab vertical. Focus on value-added premium products is aiding SOMC's brand premuimisation.

Exhibit 21: GVT - Revenue mix trend



Source: Company, Systematix Institutional Research

Exhibit 22: SOMC - gross, EBITDA margin trend



Source: Company, Systematix Institutional Research

Focus on cash flow with stricter credit control

During FY17-20, SOMC's financial performance was largely hit due to industry (weak demand impacted by demonetisation and GST-related destocking by dealers) and company-related issues (one-off losses related to defalcation by an employee, treasury management activities and stockbroker fraud, etc.). The company broke its credit discipline and opted for growth at the cost of extending higher credits (ballooned to 107 days in FY18 from ~60 days historically) to channels amid intense competition from the unorganised sector. Weak performance and concerns pertaining to its fundamental strength and integrity led significant derating in the stock's valuations during this period. However, a meaningful turnaround since FY20 on the back of credit discipline and cash flows should allay investor concerns and lead to SOMC's valuations re-rating.

FY17-20 marred by industry and company-level issues

SOMC's financial performance took a beating during FY17-20 as the company broke its credit discipline and chose to grow at the cost of giving higher credits to channels, amid intense competition from the unorganised sector. Debtor days ballooned to 107 days in FY18 from ~60 days historically and led to a surge in debt levels. The tiles industry faced severe slowdown post demonetisation in Nov'16, followed by GST-related destocking by dealers in FY18, which put pressure on companies' realisations and margins, including for SOMC. This coupled with company-level issues (one-off losses related to defalcation by an employee, treasury management activities and stockbroker fraud, etc.) impacted SOMC's financial performance and raised concerns on its fundamental strength/integrity. Put together these issues led to significant derating in its scrip's valuation multiple.

Gains strength with stricter discipline and credit control

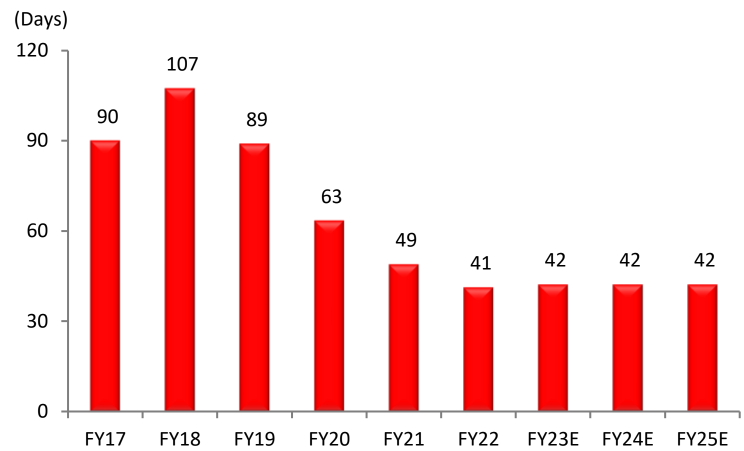
Since FY20, SOMC has been demonstrating meaningful turnaround through corrective steps towards improving its fundamentals, strengthening operations and cleaning up its balance sheet. Few key decisions that the company took during this period are:

- Made provisions (related to SREI bonds, etc.) to avoid negative surprises later on
- Did not indulge in any treasury management of ICDs, bonds, etc.
- Focused on cash flows and maintained credit discipline to achieve its desired RoCE of 25%
- Working towards increasing EBITDA margin to 15%+, in line with that of the industry leader
- Focus on retail sales (now at 80%+ of total) over builder (~5%), government and institutions
- Sales discipline - Enhance revenue visibility and moderate discounts by smoothening intra-month sales curve and discontinuing month-end schemes
- Averseness towards debt - Maintain low leverage by paying long-term debt
- Cost management – Sustain some of the cost-cutting measures taken in FY21
- Aggressively add capacity using internal cash flows
- Increase share of value-added products (GVT, etc.)
- Strengthen recall of the *Somany* brand around 'Affordable premium'.

Balance sheet strengthens on stricter credit control

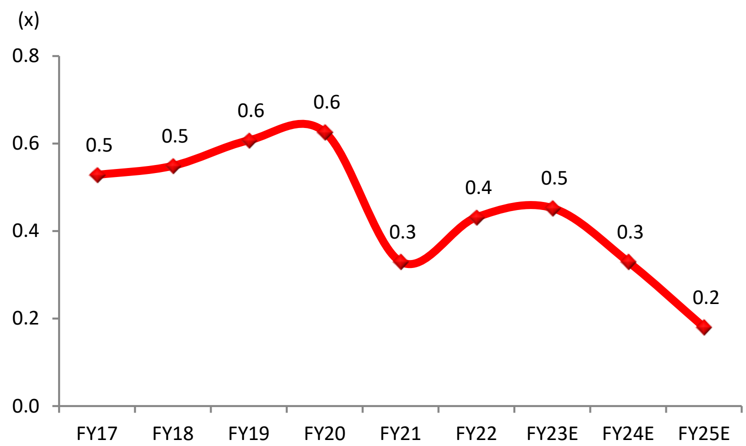
SOMC achieved meaningful turnaround in its business performance since FY20 through corrective steps, which involved improving fundamentals, strengthening operations and cleaning up its balance sheet. The company discontinued month-end discounts to push sales. It has been encouraging dealers to opt for advance cash purchase (~56% of revenue in FY22) to maintain financial discipline. Strict credit control has led to significant decline in receivables days from 107 in FY18 to ~40 currently. Its net debt/equity ratio is likely to moderate from 0.6x during FY17-20 to 0.2x in FY25E, as the company hopes to generate strong cash flows.

Exhibit 23: Receivable days



Source: Company, Systematix Institutional Research

Exhibit 24: Net debt to equity



Source: Company, Systematix Institutional Research

Capex no longer dependent on external funding

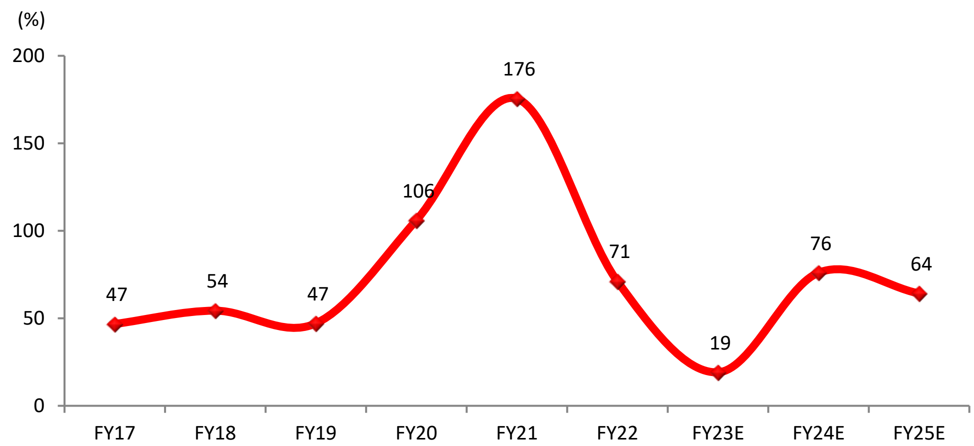
Following its stated strategy to aggressively expand capacities in the tiles business, SOMC added large ~11msm GVT capacity in 1HFY23 to increase it to over 60msm (adjusted for recently divested stake in Amora Ceramics). It is now working on another 4msm slab-manufacturing plant, likely to be operational in 1HFY24. Large capacity addition in the value-added premium segment should bode well for the company to improve its average realisation and margin. It would also enable SOMC to reposition itself as a premium tiles brand. The company aims to fund future capex mostly through internal accruals.

Exhibit 25: Tiles - Capacity addition, capex, OCF, FCF trend

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E	CAGR FY22-25E	CAGR FY17-22
Tiles Capacity (msm)	**38.4**	**52.0**	**53.0**	**53.0**	**53.0**	**53.0**	**60.0**	**64.0**	**70.0**	10	7
YoY (%)		*35*	*2*	*-*	*-*	*-*	*13*	*7*	*9*		
Capex (Rs mn)	1,045	1,299	1,559	664	414	2,680	500	1,000	500		
Operating cash-flow	1,172	1,109	859	1,527	3,563	1,566	379	2,139	2,168		
Free cash-flow	127	(190)	(700)	863	3,150	(1,115)	(121)	1,139	1,668		

Source: Company, Systematix Institutional Research

Exhibit 26: OCF/EBITDA (%)



Source: Company, Systematix Institutional Research

Financial outlook

We expect SOMC to clock healthy 12%/14% CAGR in tiles volume/revenue over FY22-25E, as the company has managed to realign its fundamentals and continued to achieve positive traction from the housing sector. During FY17-22, SOMC recorded low 3%/2% CAGR in tiles volume/revenue, impacted by industry and company-level issues. Despite global challenges, India's tiles industry should benefit from government's focus on infrastructure spending and softening gas prices since Jan'23. SOMC continues to work towards moving up the value chain by improving its product mix, increasing market share and brand visibility, in addition to optimising costs. These factors bode well for the company's slated margin expansion over the medium term. We thus estimate 15%/16%/22% CAGR in SOMC's revenue/EBITDA/PAT over FY22-25E (post flattish FY17-22), with ~400bps improvement in its EBITDA margin to 10.2% in FY25E, driven mainly by easing power & fuel costs (refer here). RoE will likely expand to ~16% in FY25E; strong OCFs will be used in future capex.

Exhibit 27: Key assumptions

	FY21	FY22	FY23E	FY24E	FY25E	CAGR FY22-25E
Consolidated Revenue (Rs mn)	16,506	20,945	24,711	28,134	31,549	15
YoY (%)	*3*	*27*	*18*	*14*	*12*	
Tiles Revenue (Rs mn)	14,377	18,358	21,472	24,479	27,416	14
YoY (%)	*3*	*28*	*17*	*14*	*12*	
Tiles Volume (msm)	50	58	64	73	81	12
YoY (%)	*2*	*16*	*10*	*14*	*12*	
Tiles Realisations (Rs/ sq.m.)	288	317	338	338	338	2
YoY (%)	*1*	*10*	*6*	*0*	*(0)*	
Bathware and Others (Rs mn)	2,125	2,587	3,239	3,655	4,133	17
YoY (%)	*2*	*22*	*25*	*13*	*13*	

Exhibit 28: Consol. revenue to grow at 15% CAGR over FY22-25E

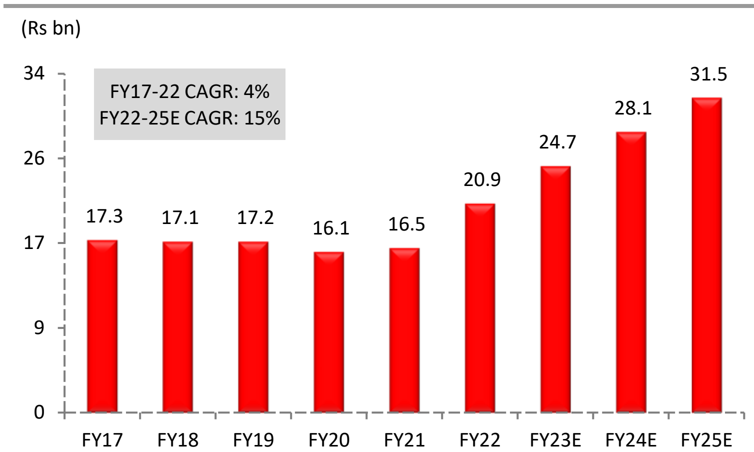
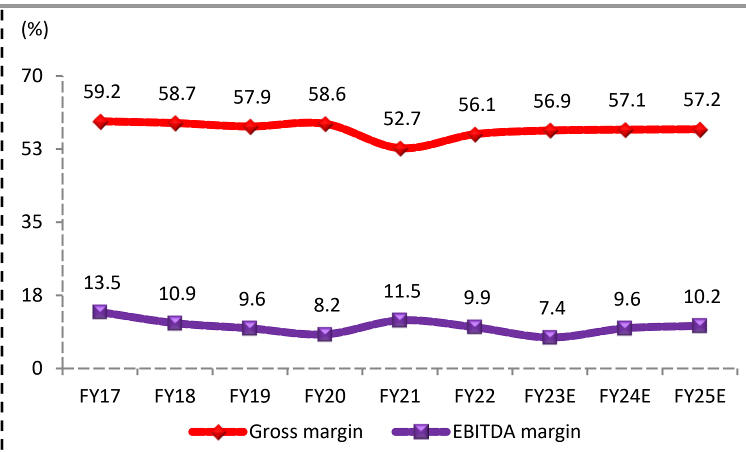


Exhibit 29: Gross, EBITDA margins trend (%)



Source: Company, Systematix Institutional Research

Exhibit 30: EPS, PAT margin trend

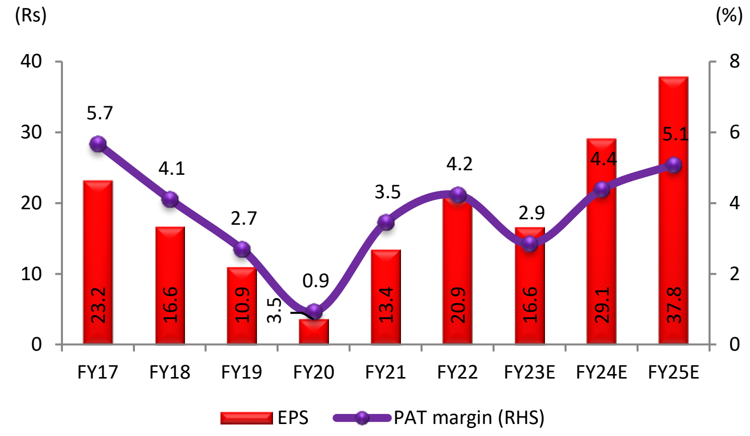


Exhibit 31: RoE, RoCE trend

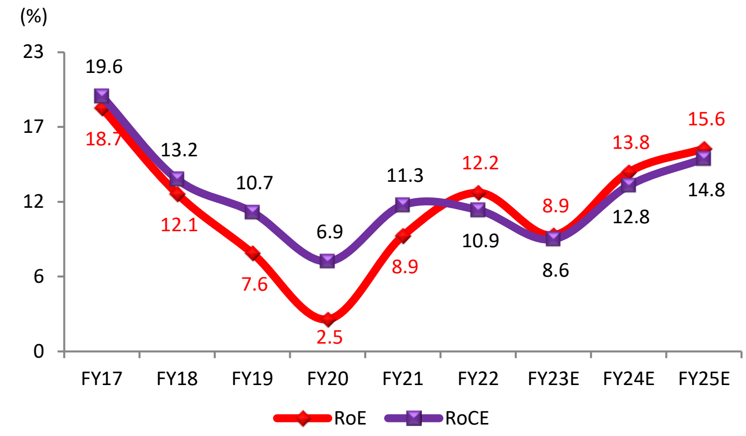


Exhibit 32: Working capital cycle trend

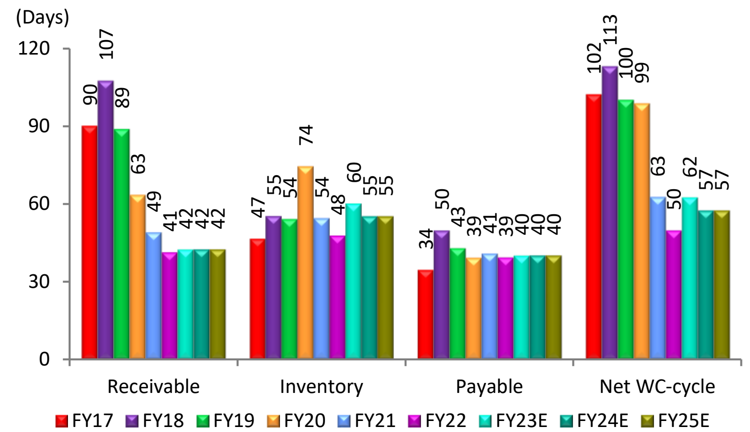


Exhibit 33: OCF, capex and FCF trend

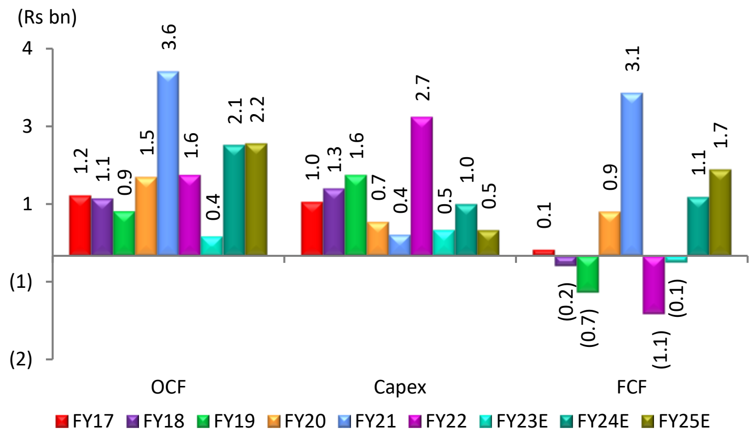


Exhibit 34: DuPont analysis

	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
RoE (%)	7.6	2.5	8.9	12.2	8.9	13.8	15.6
PAT margin (%)	*3.1*	*1.2*	*3.7*	*4.5*	*2.6*	*4.5*	*5.2*
Total Asset Turnover (x)	*1.3*	*1.3*	*1.3*	*1.5*	*1.6*	*1.7*	*1.8*
Equity Multiplier (x)	*2.1*	*2.0*	*2.0*	*2.0*	*1.9*	*1.8*	*1.7*

Source: Company, Systematix Institutional Research

Outlook and Valuation

We initiate coverage on SOMC with a BUY rating and a target price of Rs 605, based on 16x FY25E P/E (vs. 34x for KJC), for a ~16% RoE in FY25E. The company has emerged stronger after passing tough times during FY17-20 (industry and company-level issues), as it took corrective steps in terms of improving its fundamentals, strengthening operations and cleaning up its balance sheet. Notwithstanding near-term weakness in volumes and margin, we postulate robust medium-to-long-term outlook for SOMC.

SOMC's stock price has fallen >25% in last one year (large underperformance over peers); after having touched a low of Rs 450 in Dec'22, the stock price rebounded to Rs 530 currently. Subdued volume growth and company's inability to fully pass on the higher power & fuel costs have been suppressing margins since 2QFY23. 4Q onwards, we expect its business performance to recover as we expect a) demand to improve, competition from Morbi (strong rebound in exports) to reduce, and c) a meaningful decline in gas prices. SOMC's healthy outlook in the medium term is based on the upcycle in the housing sector and market share gains from continued focus on value-added products, dealer network expansion and branding efforts. We thus estimate decent 15%/22% CAGR in revenue/PAT over FY22-25E, an improved RoE of ~16% and healthy OCF to service future capex.

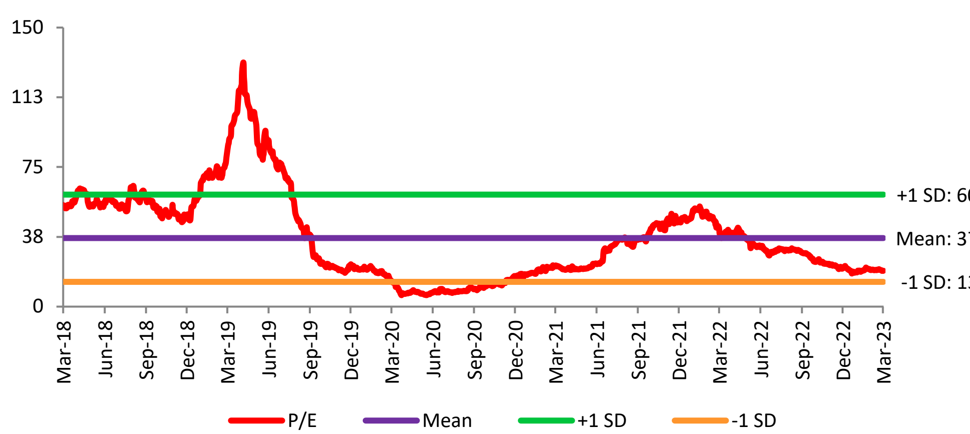
Key risks: Slowdown in economy and construction activities, high volatility in gas prices, intensifying competition from Morbi.

Exhibit 35: Systematix vs. Bloomberg estimates

(Rs mn)	Systematix estimates			Bloomberg estimates			% Var		
	FY23	FY24	FY25	FY23	FY24	FY25	FY23	FY24	FY25
Total Income	24,711	28,134	31,549	24,247	27,398	30,867	2	3	2
EBITDA	1,829	2,702	3,219	1,880	2,682	3,185	(3)	1	1
EBITDA margin (%)	*7.4*	*9.6*	*10.2*	*7.8*	*9.8*	*10.3*			
PAT	705	1,233	1,606	727	1,235	1,602	(3)	(0)	0
EPS (Rs)	16.6	29.1	37.8	17.1	29.1	37.8	(3)	(0)	0

Source: Bloomberg, Systematix Institutional Research

Exhibit 36: SOMC – one year forward PE band and standard deviation (SD)



Source: BSE, Systematix Institutional Research

Financials (Consolidated)

Profit & Loss Statement

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net revenues (Rs mn)	**16,506**	**20,945**	**24,711**	**28,134**	**31,549**
Growth (%)	*3*	*27*	*18*	*14*	*12*
Direct costs	7,806	9,205	10,640	12,058	13,490
Gross Margin (%)	*52.7*	*56.1*	*56.9*	*57.1*	*57.2*
SG&A	6,799	9,674	12,242	13,375	14,840
EBITDA	**1,902**	**2,065**	**1,829**	**2,702**	**3,219**
EBITDA margins (%)	*11.5*	*9.9*	*7.4*	*9.6*	*10.2*
- Depreciation	616	640	661	760	820
Other income	128	134	150	113	158
Interest Exp	401	296	408	338	315
PBT	828	1,264	888	1,717	2,241
Effective tax rate (%)	*26.8*	*26.1*	*27.0*	*27.0*	*27.0*
+ Associates/(Minorities)	(36)	(47)	57	(20)	(30)
Net Income	**570**	**887**	**705**	**1,233**	**1,606**
Adjusted income	570	887	705	1,233	1,606
WANS	42	42	42	42	42
FDEPS (Rs)	13	21	17	29	38
FDEPS growth (%)	*279*	*56*	*(21)*	*75*	*30*

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Share capital	85	85	85	85	85
Net worth	6,407	7,263	7,883	8,946	10,298
Total debt	4,837	5,686	5,986	5,786	5,586
Minority interest	997	1,076	1,086	1,096	1,106
DT Liability/(Asset)	321	323	304	285	266
Capital Employed	**12,562**	**14,348**	**15,259**	**16,114**	**17,256**
Net tangible assets	7,493	7,445	8,284	9,024	9,204
Net Intangible assets	22	3	3	3	3
Goodwill	73	73	73	73	73
CWIP	86	2,267	1,267	767	267
Investments (Strategic)	-	-	-	-	-
Investments (Financial)	898	600	600	600	600
Current Assets	5,472	6,009	7,828	8,401	9,311
Cash	1,491	1,486	1,322	1,866	2,922
Current Liabilities	2,974	3,534	4,116	4,620	5,124
Working capital	2,499	2,475	3,711	3,781	4,188
Capital Deployed	**12,562**	**14,348**	**15,259**	**16,114**	**17,256**
Contingent Liabilities	168	169	-	-	-

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
EBIT (before OI)	1,374	1,466	1,242	1,962	2,408
+ Non-cash items	616	640	661	760	820
OCF before WC	1,990	2,106	1,904	2,721	3,228
- Incr./(decr.) in WC	(1,828)	187	1,227	60	397
Others including taxes	255	352	298	522	664
Operating cash-flow	3,563	1,566	379	2,139	2,168
- Capex	414	2,680	500	1,000	500
Free cash-flow	3,150	(1,115)	(121)	1,139	1,668
Acquisitions					
- Dividend	102	-	85	170	255
+ Equity raised	-	-	-	-	-
+ Debt raised	(854)	878	300	(200)	(200)
- Fin Investments	750	(333)	-	-	-
- Misc. Items (CFI + CFF)	168	585	258	225	158
Net cash-flow	1,276	(488)	(164)	545	1,055

Source: Company, Systematix Institutional Research

Ratios @ Rs 525

YE: Mar	FY21	FY22	FY23E	FY24E	FY25E
P/E (x)	39.1	25.1	31.6	18.1	13.9
EV/EBITDA (x)	13.0	12.5	14.4	9.5	7.6
EV/sales (x)	1.5	1.2	1.1	0.9	0.8
P/B (x)	3.5	3.1	2.8	2.5	2.2
RoE (%)	8.9	12.2	8.9	13.8	15.6
RoCE (%)	11.3	10.9	8.6	12.8	14.8
ROIC	(0.9)	3.5	5.3	9.1	11.7
DPS (Rs per share)	2.4	-	2.0	4.0	6.0
Dividend yield (%)	0.5	-	0.4	0.8	1.1
Dividend payout (%)	17.9	-	12.0	13.8	15.9
Net debt/equity (x)	0.3	0.4	0.5	0.3	0.2
Receivables (days)	49	41	42	42	42
Inventory (days)	54	48	60	55	55
Payables (days)	41	39	40	40	40
CFO:PAT%	625	177	54	173	135

Source: Company, Systematix Institutional Research

SYSTEMATIX INSTITUTIONAL EQUITIES ™

Systematix

Institutional Equities

Carysil

06 March 2023

Global aspirations in kitchen and bathroom products

COMPANY UPDATE

Sector: Building Materials	**Rating: BUY**
CMP: Rs 565	**Target Price: Rs 705**

Stock Info	
Sensex/Nifty	59,809/17,594
Bloomberg	CARYSIL IN
Equity shares (mn)	26.7
52-wk High/Low	869/433
Face value	Rs 2
M-Cap	Rs 15.1bn/USD 183mn
3-m Avg turnover	USD 0.1mn

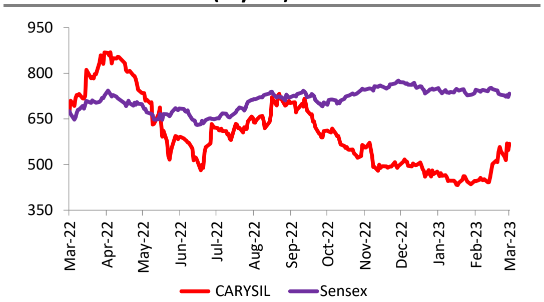
Financial Snapshot (Rs mn)

Y/E Mar	FY23E	FY24E	FY25E
Net sales	6,200	7,627	9,266
EBITDA	1,137	1,455	1,832
OPM (%)	18.3	19.1	19.8
PAT (adj.)	561	715	941
EPS (Rs)	21.0	26.8	35.2
PE (x)	26.9	21.1	16.0
P/B (x)	5.0	4.1	3.3
EV/EBITDA (x)	15.3	12.2	9.8
RoE (%)	18.4	19.3	20.6
RoCE (%)	18.4	18.6	20.5
Net-D/E (x)	0.7	0.7	0.6

Shareholding Pattern (%)

	Dec'22	Sep'22	Jun'22
Promoter	43.9	43.9	43.9
- Pledged			
FII	0.3	0.3	0.3
DII	6.5	6.4	6.2
Others	49.4	49.5	49.6

Stock Performance (1-year)



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We maintain BUY on Carysil (CARYSIL) with a Rs 705 TP (20x FY25E P/E). The scrip has rallied over 15% since our initiation (IC report link) on 22 February 2023, after >40% fall since Apr'22, on fear of global demand slowdown. Impacted by channel de-stocking, the company has been reporting weak performance since 2QFY23. But we expect a strong rebound 4QFY23 onwards, considering its strong order book and volume visibility with large global customers. CARYSIL aspires to become a global one-stop shop for all kitchen and bathroom lifestyle products. Post strong 22%/32%/52% CAGR in revenue/EBITDA/PAT over FY17-22 (on a ~700bps EBITDA margin expansion to ~21% and forex gains), we estimate 24%/21% /13% CAGR over FY22-25E, expecting ~20% EBITDA margin and higher interest costs (rise in debt). Regular capacity addition and working capital needs will likely limit FCF/PAT; healthy OCF/EBITDA (~60%) and RoE (~20%) will be maintained though.

A global leader in quartz sinks; leveraging global presence through adjacent categories: CARYSIL is the only Asian, and among the four global manufacturers of quartz sinks using Schock technology (industry CAGR: 20%+). To leverage its vast global presence, the company has widened its product portfolio over the years by adding adjacent categories such as steel sinks (Quadro and PVD range), kitchen appliances, countertops and bathroom fittings. It is also exploring new categories of ceramic sinks via the organic and inorganic routes. We expect CARYSIL to gain market share from large European peers, who are currently grappling with energy crisis.

Vast cross-selling opportunities with global customers, STL (UK): CARYSIL is into white label manufacturing for large home retailers and big brands like Kraus and Karren for their online supplies. In 2019, the company entered into an agreement with Grohe to supply quartz sinks, and extended the same in 2020 to supply stainless steel kitchen sinks as well. It began supplying quartz sinks to IKEA in 2021 for its global requirements, which is progressing well. From small quantities, we expect CARYSIL to expand its business with large customers multifold, as it adds new products and supplies for global requirements. Its STL UK acquisition would help it broaden its kitchen and bathroom offerings, by leveraging its loyal customer base.

Distribution, product portfolio expansion to drive domestic business: Domestic revenue grew 35% YoY to Rs 1bn in 9MFY23, contributing 22% to total revenue. With focus on in-house manufacturing, innovative products, projects, branding, marketing, and channel expansion (2x in last one year; expects to touch 3,000 dealers and 100+ distributors by Mar'23), CARYSIL aims 30% CAGR in domestic sales over 3-5 years.

US and UK markets recover; focus now on Gulf: Primary demand for sinks has recovered in the UK and US markets, after channel inventories corrected there in last few quarters. However, most of Europe continues to face demand challenges. Management expects strong rebound in sales 4Q onwards, based on its robust order book position. Regular participations in exhibitions globally (recently in Dubai and France) enable it to add new customers. CARYSIL plans to expand its presence in Dubai (set up showrooms) to improve brand visibility and expand in GCC countries.

Large capex ahead of demand to drive growth: Large capacity additions in quartz sinks over last 3-4 years have helped CARYSIL add large global retailers as customers and expand rapidly. It has also doubled its stainless steel sink capacity in FY23. Before coming on board, customers judge existing spare capacities to gauge comfort on sustained supply. CARYSIL expects to use a recently acquired land parcel (60 acres) near its Bhavnagar plants for existing and new product lines.

Story in charts…

Exhibit 1: Increasing product portfolio

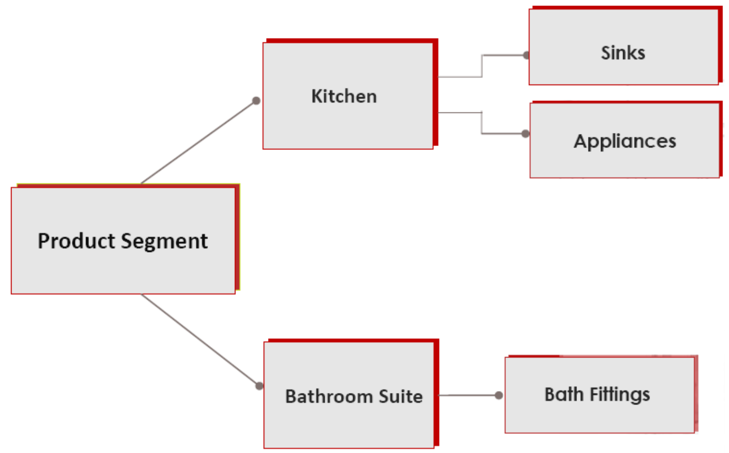


Exhibit 2: Revenue mix

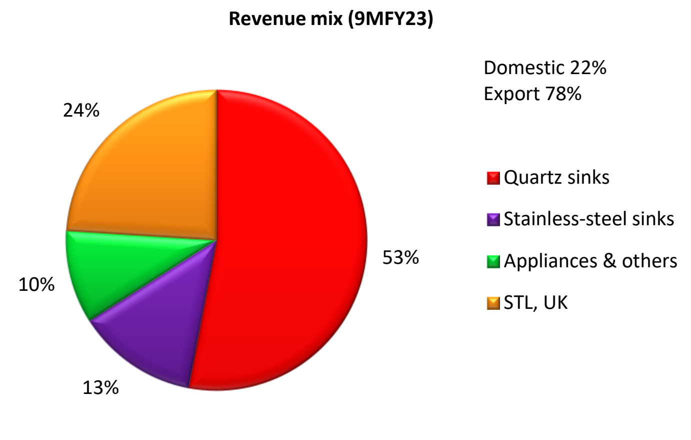


Exhibit 3: Quartz sink – volume trend

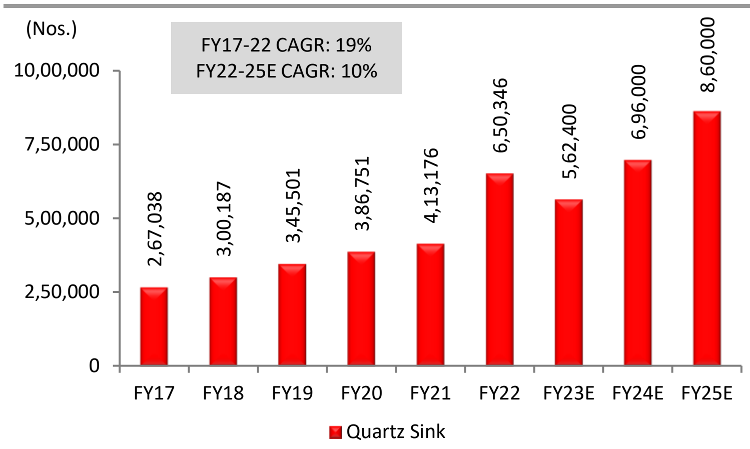


Exhibit 4: Stainless Steel sink – volume trend

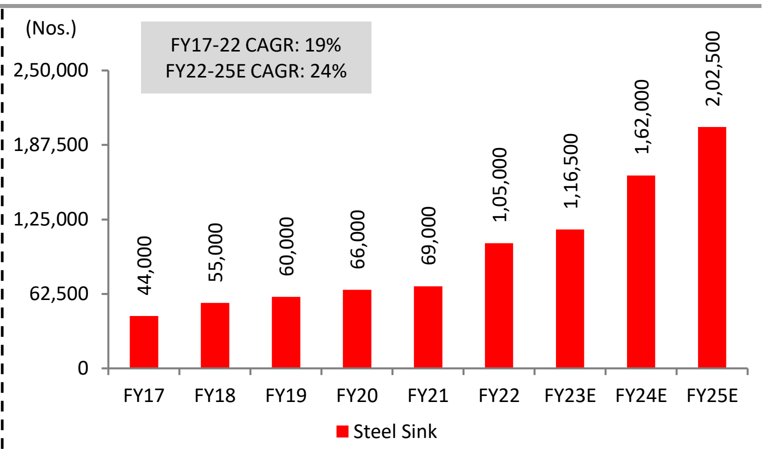


Exhibit 5: Revenue mix trend (category-wise)

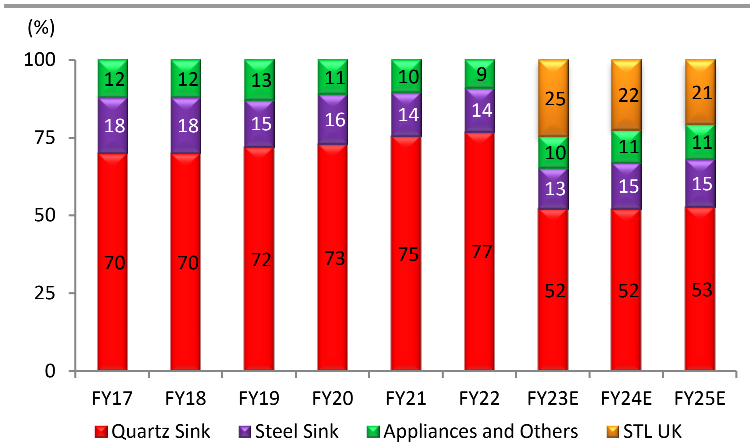
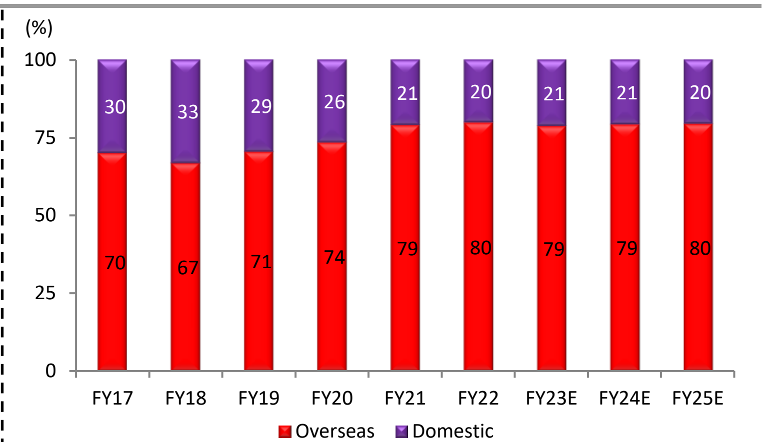


Exhibit 6: Revenue mix trend (geography-wise)



Source: Company, Systematix Institutional Research

Exhibit 7: Revenue, EBITDA margin trend

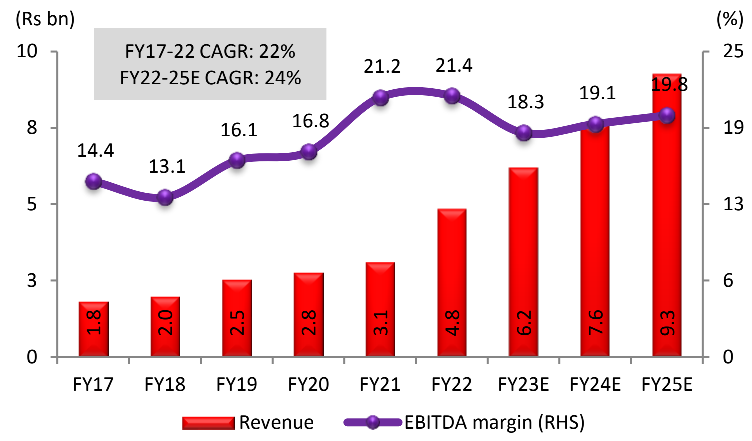


Exhibit 8: PAT and margin trend

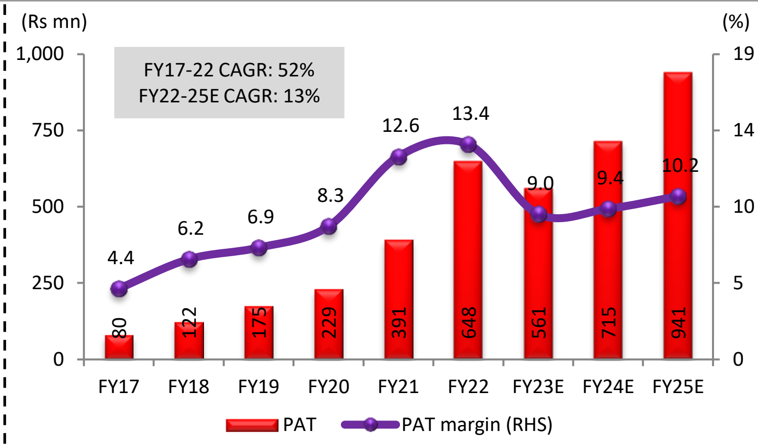


Exhibit 9: RoE, ROCE trend

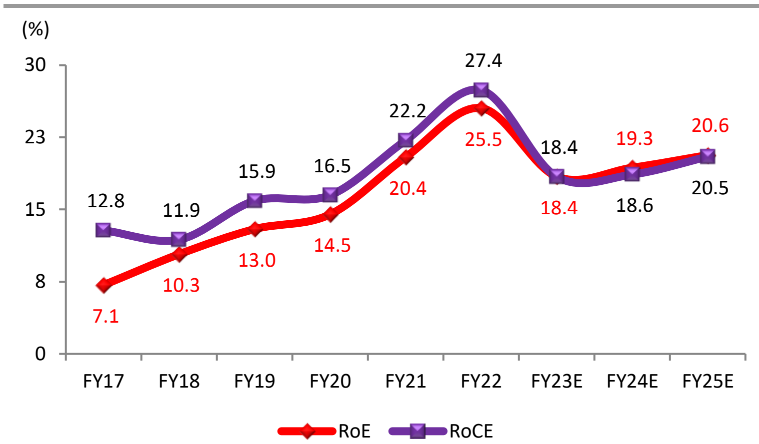


Exhibit 10: Capex has intensified since FY21

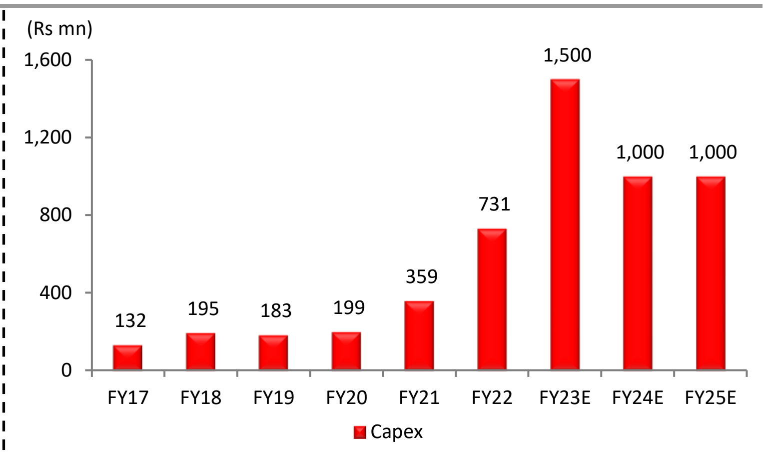


Exhibit 11: OCF/EBITDA trend

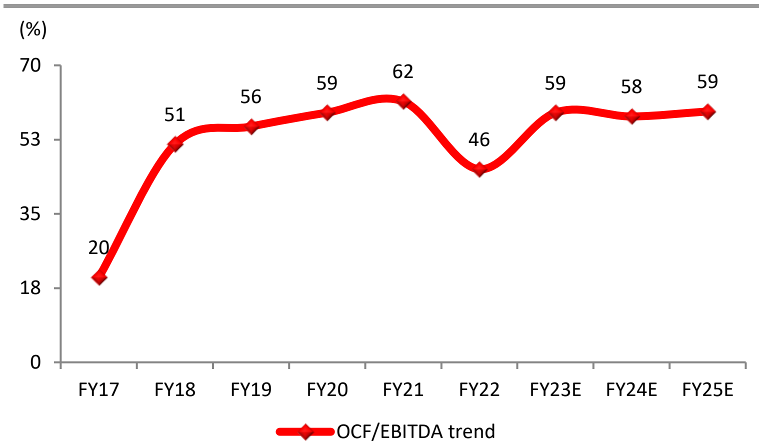
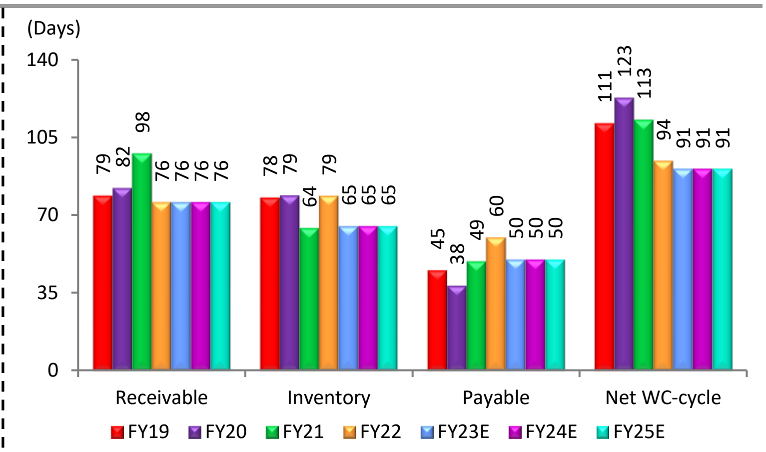


Exhibit 12: Net working capital cycle trend



Source: Company, Systematix Institutional Research

Outlook and View

We maintain our BUY rating on Carysil (CARYSIL) with a target price of Rs 705, based on 20x FY25E EPS of Rs 35. The scrip has rallied over 10% since our initiation (IC report link) on 22 February 2023, after >40% fall since Apr'22, on fear of global demand slowdown, visible from its results since 2QFY23. However, we believe the issue of above-normal channel inventory is behind us, and we thus expect a strong rebound in performance 4QFY23 onwards. Robust order book and volume visibility from large global customers underpin our thesis.

CARYSIL is the only company in Asia and among four companies worldwide to manufacture quartz kitchen sinks with Schock technology (Germany). The company also manufactures stainless steel kitchen sinks (with core focus on Quadro sinks), kitchen appliances and bathroom fittings. Factors that drive CARYSIL's strong growth potential are a) product supply approvals from world's leading retailers such as IKEA, Grohe, Menard, etc., are testimonies to its product quality, systems and processes, b) significant capacity addition in view of strong demand visibility from its key customers, and c) customised and dedicated moulds for key customers, which provide comfort in terms of quality and supply assurance to them.

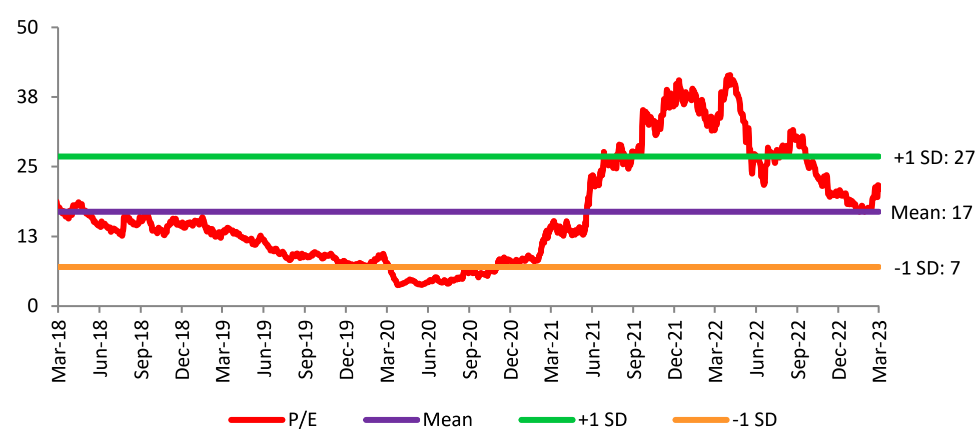
CARYSIL posted strong revenue/EBITDA/PAT at 22%/32%/52% CAGR over FY17-22 on EBITDA margin expansion (from ~14% to ~21%) and higher other income (forex gains). Over FY22-25E, we estimate 24%/21%/13% CAGR on EBITDA margin reacing ~20%, higher interest cost (due to rise in debt) and lower other income. Regular capacity additions ahead of demand and working capital needs will likely limit FCF/PAT; OCF/EBITDA (~60%) and RoE/ RoCE, at ~20%, would be healthy though.

Exhibit 13: Systematix vs. Bloomberg estimates

(Rs mn)	Systematix estimates			Bloomberg estimates			% Var with Systematix		
	FY23	FY24	FY25	FY23	FY24	FY25	FY23	FY24	FY25
Total Income	6,200	7,627	9,266	6,206	8,171	9,870	(0)	(7)	(6)
EBITDA	1,137	1,455	1,832	1,085	1,463	1,836	5	(1)	(0)
EBITDA margin (%)	*18.3*	*19.1*	*19.8*	*17.5*	*17.9*	*18.6*			
PAT	561	715	941	559	866	1,141	0	(17)	(18)
EPS (Rs)	21.0	26.8	35.2	20.9	32.4	42.7	0	(17)	(18)

Source: Bloomberg, Systematix Institutional Research

Exhibit 14: CARYSIL – one year forward PE band and standard deviation (SD)



Source: BSE, Systematix Institutional Research

Key risks

- Economic slowdown in domestic and global markets could hamper the demand for the company's products, which are discretionary in nature.
- A rising interest rate scenario could increase the interest cost burden on loans taken for capex and working capital requirements.
- As ~80% revenue comes from exports, any large currency fluctuations could significantly impact earnings.

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net revenues (Rs mn)	**3,097**	**4,839**	**6,200**	**7,627**	**9,266**
Growth (%)	*12.1*	*56.2*	*28.1*	*23.0*	*21.5*
Direct costs	1,418	2,095	3,165	3,851	4,633
Gross Margin (%)	*54*	*57*	*49*	*50*	*50*
SG&A	1,022	1,711	1,899	2,320	2,801
EBITDA	**658**	**1,033**	**1,137**	**1,455**	**1,832**
EBITDA margins (%)	*21.2*	*21.4*	*18.3*	*19.1*	*19.8*
- Depreciation	127	177	263	344	406
Other income	80	101	9	23	37
Interest Exp	73	96	149	175	204
PBT	538	861	734	958	1,259
Effective tax rate (%)	*27.0*	*24.2*	*23.0*	*25.0*	*25.0*
+ Associates/(Minorities)	1	2	3	3	3
Net Income	**391**	**648**	**561**	**715**	**941**
Adjusted income	391	648	561	715	941
WANS	27	27	27	27	27
FDEPS (Rs/share)	15	24	21	27	35
FDEPS growth (%)	*71.1*	*65.5*	*(13.4)*	*27.5*	*31.6*

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Share capital	53	53	53	53	53
Net worth	1,914	2,537	3,044	3,695	4,555
Total debt	1,013	1,373	2,473	2,773	3,073
Minority interest	26	32	32	32	32
DT Liability/ (Asset)	40	46	51	56	61
Capital Employed	**2,992**	**3,988**	**5,600**	**6,556**	**7,721**
Net tangible assets	1,261	1,806	3,043	3,699	4,292
Net Intangible assets	258	257	257	257	257
Goodwill	-	-	-	-	-
CWIP	100	207	207	207	207
Investments (Strategic)	-	-	-	-	-
Investments (Financial)	-	-	-	-	-
Current Assets	2,091	3,149	3,534	4,124	4,796
Cash	201	113	188	122	275
Current Liabilities	919	1,545	1,629	1,853	2,106
Working capital	1,172	1,604	1,905	2,270	2,689
Capital Deployed	**2,992**	**3,988**	**5,600**	**6,556**	**7,721**
Contingent Liabilities	-	3	-	-	-

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
EBIT (incl. other income)	260	334	874	1,111	1,426
Non-cash items	127	177	263	344	406
OCF before WC changes	387	511	1,137	1,455	1,832
Incr./(decr.) in WC	159	185	280	346	399
Others including taxes	(226)	(191)	181	252	327
Operating cash-flow	454	516	675	857	1,106
Capex	359	731	1,500	1,000	1,000
Free cash-flow	95	(215)	(825)	(143)	106
Acquisitions					
Dividend	53	64	53	64	80
Equity raised	-	-	-	-	-
Debt raised	50	360	1,100	300	300
Fin Investments	-	-	-	-	-
Misc. Items (CFI + CFF)	74	105	147	159	173
Net cash-flow	18	(25)	75	(66)	153

Source: Company, Systematix Institutional Research

Ratios @ Rs 565

YE: Mar	FY21	FY22	FY23E	FY24E	FY25E
P/E (x)	38.6	23.3	26.9	21.1	16.0
EV/EBITDA (x)	24.2	15.8	15.3	12.2	9.8
EV/sales (x)	5.1	3.4	2.8	2.3	1.9
P/B (x)	7.9	5.9	5.0	4.1	3.3
RoE (%)	20.4	25.5	18.4	19.3	20.6
RoCE (%)	22.2	27.4	18.4	18.6	20.5
ROIC	15.3	19.4	12.1	12.1	13.6
DPS (Rs per share)	2.0	2.4	2.0	2.4	3.0
Dividend yield (%)	0.4	0.4	0.4	0.4	0.5
Dividend payout (%)	13.6	9.9	9.5	9.0	8.5
Net debt/equity (x)	0.4	0.5	0.7	0.7	0.6
Receivables (days)	98	76	76	76	76
Inventory (days)	64	79	65	65	65
Payables (days)	49	60	50	50	50
CFO:PAT%	116	80	120	120	118

Source: Company, Systematix Institutional Research

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