

**BUY**

TP: Rs 3,060 | ▲ 26%

**CERA SANITARYWARE**

Construction Materials

02 August 2019

## Inspid quarter

**Cera Sanitaryware (CRS) reported subpar Q1FY20 standalone revenue of Rs 2.7bn, down 4.8% YoY, with the sanitaryware segment declining 12.7%. Operating margins were up 60bps YoY to 13.2% on lower other expenses (-188bps), resulting in flat EBITDA. Despite a tepid Q1, management retained guidance of 14-15% revenue growth and 14.5-15% margins in FY20. We cut FY20/FY21 estimates by ~6% each, pare our target P/E to 26x in a tough demand climate, and roll over to a new Jun'20 TP of Rs 3,060 (vs. Rs 3,395).**

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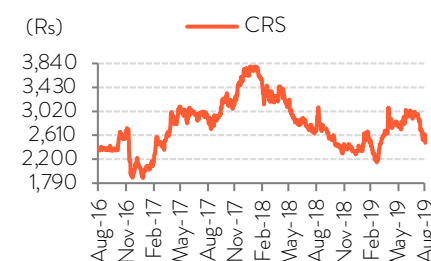
**Revenue slippage led by sanitaryware segment:** CRS reported a 4.8% YoY decrease in standalone revenue to Rs 2.7bn in Q1, with the sanitaryware segment down 12.7% whereas faucets/tiles grew 9%/2%. As per management, revenue performance was undermined by a lacklustre demand environment during the recent general elections. A dull Q1 notwithstanding, CRS expects to achieve earlier guided topline growth of 14-15% in FY20.

Ticker/Price	CRS IN/Rs 2,424
Market cap	US\$ 453.2mn
Shares o/s	13mn
3M ADV	US\$ 0.3mn
52wk high/low	Rs 3,195/Rs 2,144
Promoter/FPI/DII	55%/8%/38%

Source: NSE

**Standalone operating margins expand 60bps:** CRS's standalone operating margins rose 60bps due to lower other expenses (-188bps YoY), partially offset by higher employee cost (+115bps YoY), which translated to flat EBITDA YoY. Adj. PAT declined 7% YoY due to higher interest/depreciation (+94%/+54%) which nullified the 51% rise in other income. Management retained its operating margin guidance of ~14.5-15% for FY20.

## STOCK PERFORMANCE



Source: NSE

**Maintain BUY:** CRS's Q1 results have sharply underperformed expectations, prompting us to cut FY20/FY21 PAT estimates by ~6% each. We also reset our target one-year forward P/E multiple down from 28x to 26x amid a challenging demand climate. Rolling valuations forward, we have a revised June'20 TP of Rs 3,060 vs. Rs 3,395 earlier.

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	970	1,010	1,274	1,478	1,678
Adj. EPS (Rs)	74.6	77.7	98.0	113.6	129.0
Adj. EPS growth (%)	0.9	4.1	26.1	16.0	13.6
Adj. ROAE (%)	17.2	15.5	16.9	17.1	16.9
Adj. P/E (x)	32.5	31.2	24.7	21.3	18.8
EV/EBITDA (x)	18.4	16.1	14.1	12.5	11.0

Source: Company, BOBCAPS Research

**BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda**

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**FIG 1 – STANDALONE QUARTERLY PERFORMANCE**

(Rs mn)	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
<b>Total revenues</b>	<b>2,674</b>	<b>2,807</b>	<b>(4.8)</b>	<b>4,131</b>	<b>(35.3)</b>
Total raw material consumed	1,231	1,289	(4.5)	2,073	(40.6)
% of sales	46.0	45.9	12bps	50.2	(416bps)
Employee expenses	399	387	3.2	387	3.1
% of sales	14.9	13.8	115bps	9.4	556bps
Other exp	692	779	(11.2)	1,033	(33.0)
% of sales	25.9	27.7	(188bps)	25.0	87bps
Total expenditure	2,321	2,454	(5.4)	3,493	(33.5)
% of sales	87	87.4	(60bps)	84.6	227bps
<b>EBITDA</b>	<b>352.2</b>	<b>352.9</b>	<b>(0.2)</b>	<b>637.9</b>	<b>(44.8)</b>
% of sales	13.2	12.6	60bps	15.4	(227bps)
Depreciation	76.8	49.7	54.4	66.8	14.9
Other income	29.2	19.4	50.6	56.8	(48.6)
Interest cost	11.4	5.9	93.5	14.9	(23.6)
<b>PBT</b>	<b>293.2</b>	<b>316.6</b>	<b>(7.4)</b>	<b>613.0</b>	<b>(52.2)</b>
Taxes	102.5	111.5	(8.1)	232.6	(56.0)
Effective tax rate (%)	34.9	35.2	(28bps)	37.9	(300bps)
<b>APAT</b>	<b>190.8</b>	<b>205.1</b>	<b>(7.0)</b>	<b>380.4</b>	<b>(49.9)</b>

Source: Company, BOBCAPS Research

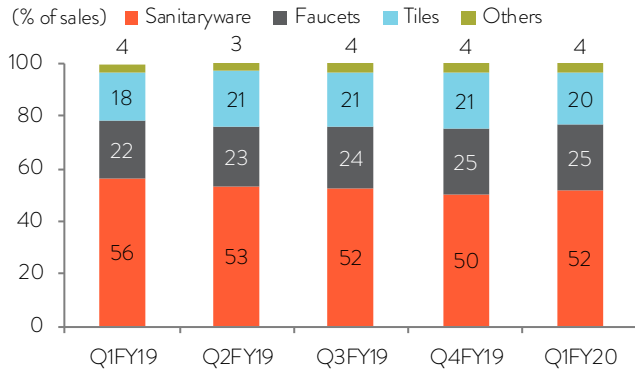
**FIG 2 – CONSOLIDATED QUARTERLY PERFORMANCE**

(Rs mn)	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
<b>Total revenues</b>	<b>2,712</b>	<b>2,818</b>	<b>(3.8)</b>	<b>4,156</b>	<b>(34.8)</b>
Total raw material consumed	1,146	1,181	(3.0)	1,982	(42.2)
% of sales	42.8	42.1	79bps	48.0	(512bps)
Employee expenses	411	398	3.3	397	3.7
% of sales	15.4	14.2	120bps	9.6	578bps
Other expenses	803	866	(7.3)	1,116	(28.1)
% of sales	30.0	30.9	(84bps)	27.0	301bps
Total expenditure	2,359	2,445	(3.5)	3,494	(32.5)
% of sales	88.3	87.1	115bps	84.6	366bps
<b>EBITDA</b>	<b>352.5</b>	<b>373.2</b>	<b>(5.5)</b>	<b>662.1</b>	<b>(46.8)</b>
% of sales	13.2	13.3	(11bps)	16.0	(284bps)
Depreciation	91.1	62.4	46.1	79.8	14.2
Other income	32.6	23.4	39.4	69.3	(53.0)
Interest cost	25.1	18.0	39.3	31.0	(19.1)
<b>PBT</b>	<b>268.9</b>	<b>316.2</b>	<b>(15.0)</b>	<b>620.6</b>	<b>(56.7)</b>
Taxes	97.3	112.2	(13.3)	234.3	(58.5)
Effective tax rate (%)	36.2	35.5	69bps	37.8	(157bps)
<b>APAT</b>	<b>171.6</b>	<b>203.9</b>	<b>(15.9)</b>	<b>386.3</b>	<b>(55.6)</b>
Less: Minority interest	(9.4)	(0.6)	1532.7	2.9	(424.5)
Add: Share of profit in associate	0.03	0.00	NA	0.3	(88.3)
<b>RPAT</b>	<b>181.0</b>	<b>204.5</b>	<b>(11.5)</b>	<b>383.7</b>	<b>(53)</b>

Source: Company, BOBCAPS Research

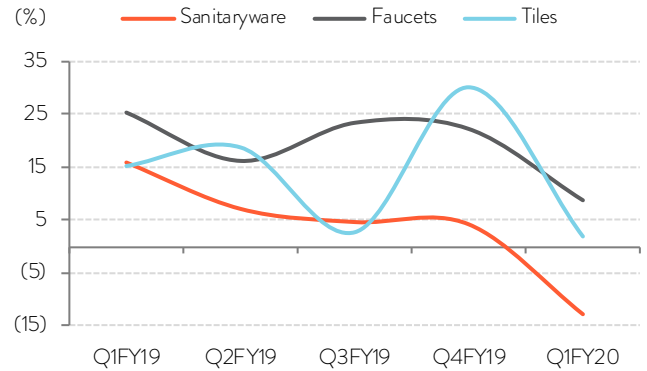
## STANDALONE QUARTERLY TRENDS

**FIG 3 – REVENUE BREAKUP**



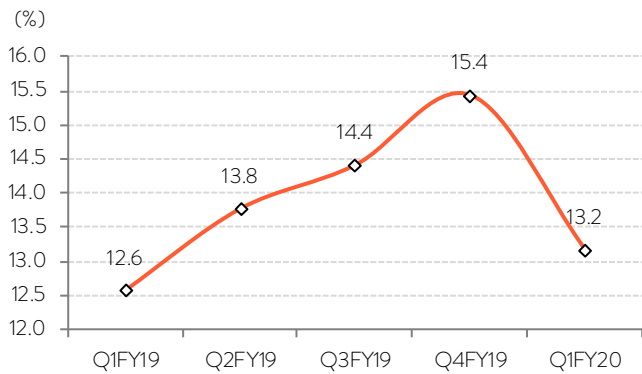
Source: Company, BOBCAPS Research

**FIG 4 – SEGMENTAL GROWTH**



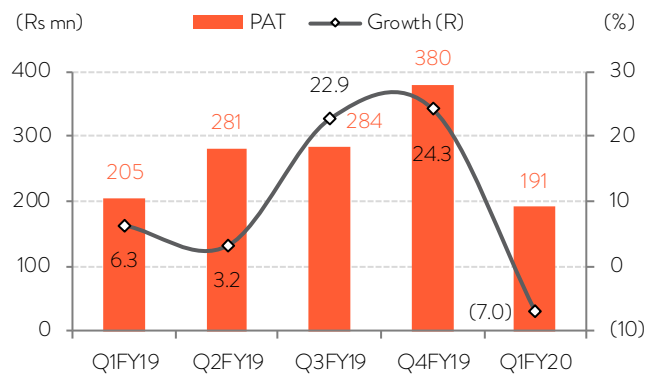
Source: Company, BOBCAPS Research

**FIG 5 – EBITDA MARGIN**



Source: Company, BOBCAPS Research

**FIG 6 – PAT GROWTH YOY**



Source: Company, BOBCAPS Research

## Earnings call highlights

- Demand conditions have been difficult with customers postponing purchases during the quarter. CRS saw revenue headwinds from channel destocking, general election-related uncertainty and tight liquidity.
- As per management, the company could have increased sales had it resorted to looser credit terms which it was not willing to do. Debtor days were flat YoY at ~55 days during the quarter.
- CRS expects a demand pickup from H2FY20 and has maintained its guidance of ~15% revenue growth and ~14.5-15% operating margins for FY20. The company is already seeing green shoots of growth from markets beyond tier-I and tier-II cities. Affordable housing continues to do well and hence remains a focus area.
- The faucetware range has been expanded to 850 SKUs, enabling topline and margin gains in the segment. Faucetware margins have now moved closer to those of sanitaryware. CRS has 27 sub-brands under brand CERA in sanitaryware and 24 sub-brands in faucetware.
- About 72% of revenues are derived from the dealer network and the rest from institutional sales.
- The company has 10.8MW of solar and wind power plants which ensures captive generation of ~90% of the electricity required for its factories.
- Natural gas is purchased from GAIL and Sabarmati Gas. The gas from GAIL is 35-40% cheaper as it is supplied from an isolated well. In FY19, over 50% of the natural gas requirement was met from GAIL supplies.
- Capex planned for FY20 totals ~Rs 560mn. CRS had ~Rs 1.9bn of cash & cash equivalents on the books as of 30 June.
- Ind-AS 116 implementation has had no material impact on financials.

## Valuation methodology

CRS is the third largest organised sanitaryware player in India with ~24% organised market share. Over the years, the company has expanded its product portfolio from sanitaryware to tiles, faucets and wellness goods, to become a one-stop bathroom solution provider.

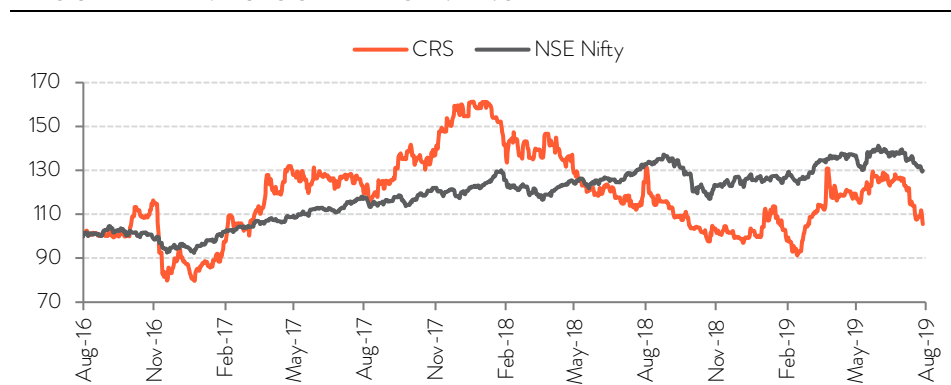
Following a disappointing Q1, we cut FY20/FY21 PAT estimates by ~6% each and now expect CRS to deliver a 11%/21% revenue/earnings CAGR over FY19-FY21, backed by its comprehensive portfolio, wide distribution reach and strong brand focus. Resetting our target one-year forward P/E multiple from 28x to 26x in light of the tough demand environment and rolling valuations over, we arrive at a revised June'20 target price of Rs 3,060 (from Rs 3,395). Maintain BUY.

**FIG 7 – REVISED ESTIMATES**

(Rs mn)	Old		New		Change (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	15,189	17,299	14,806	16,537	(2.5)	(4.4)
EBITDA	2,278	2,621	2,191	2,481	(3.8)	(5.4)
PAT	1,355	1,578	1,274	1,478	(6.0)	(6.3)

Source: Company, BOBCAPS Research

**FIG 8 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

- **Sharp rise in raw material prices:** CRS's key raw material is natural gas; any sharp increase in prices may affect near-term profitability.
- **Increased competition from unorganised players:** All of CRS's business segments have a large unorganised presence (~50% of the total market). An inability to compete effectively may affect the company's profitability.
- **Prolonged slowdown in housing market:** A continued slowdown in the housing market would hit growth prospects.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Total revenue</b>	<b>11,776</b>	<b>13,444</b>	<b>14,806</b>	<b>16,537</b>	<b>18,772</b>
EBITDA	1,699	1,917	2,191	2,481	2,816
EBIT	1,428	1,637	1,884	2,135	2,423
Net interest income/(expenses)	(98)	(85)	(75)	(61)	(64)
Other income/(expenses)	129	110	147	184	208
Exceptional items	90	141	0	0	0
EBT	1,459	1,662	1,956	2,259	2,567
Income taxes	(488)	(652)	(684)	(790)	(898)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	(1)	0	3	10	10
<b>Reported net profit</b>	<b>1,061</b>	<b>1,151</b>	<b>1,274</b>	<b>1,478</b>	<b>1,678</b>
Adjustments	(90)	(141)	0	0	0
<b>Adjusted net profit</b>	<b>970</b>	<b>1,010</b>	<b>1,274</b>	<b>1,478</b>	<b>1,678</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	944	1,109	1,136	1,269	1,440
Other current liabilities	1,840	1,979	2,150	2,401	2,726
Provisions	201	365	222	248	282
Debt funds	962	906	590	700	650
Other liabilities	391	436	436	436	436
Equity capital	65	65	65	65	65
Reserves & surplus	5,991	6,944	7,986	9,190	10,558
Shareholders' fund	6,056	7,009	8,052	9,255	10,623
<b>Total liabilities and equities</b>	<b>10,461</b>	<b>11,908</b>	<b>12,686</b>	<b>14,400</b>	<b>16,237</b>
Cash and cash eq.	327	193	67	131	312
Accounts receivables	2,680	2,984	3,083	3,443	3,909
Inventories	1,935	2,158	2,272	2,537	2,880
Other current assets	782	747	933	1,042	1,183
Investments	1,086	1,779	1,890	2,450	2,750
Net fixed assets	3,584	3,840	4,232	4,587	4,994
CWIP	52	195	195	195	195
Intangible assets	13	13	13	13	13
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>10,461</b>	<b>11,908</b>	<b>12,686</b>	<b>14,400</b>	<b>16,237</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	1,332	1,431	1,582	1,823	2,071
Interest expenses	98	85	75	61	64
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(648)	(22)	(345)	(325)	(419)
Other operating cash flows	(3)	45	0	0	0
<b>Cash flow from operations</b>	<b>778</b>	<b>1,540</b>	<b>1,311</b>	<b>1,559</b>	<b>1,716</b>
Capital expenditures	(470)	(678)	(700)	(700)	(800)
Change in investments	(215)	(693)	(111)	(560)	(300)
Other investing cash flows	(64)	(10)	(3)	(10)	(10)
<b>Cash flow from investing</b>	<b>(749)</b>	<b>(1,381)</b>	<b>(814)</b>	<b>(1,270)</b>	<b>(1,110)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	124	(56)	(316)	110	(50)
Interest expenses	(98)	(85)	(75)	(61)	(64)
Dividends paid	(188)	(188)	(229)	(264)	(300)
Other financing cash flows	(107)	36	(3)	(10)	(10)
<b>Cash flow from financing</b>	<b>(268)</b>	<b>(293)</b>	<b>(623)</b>	<b>(226)</b>	<b>(424)</b>
<b>Changes in cash and cash eq.</b>	<b>(239)</b>	<b>(134)</b>	<b>(126)</b>	<b>64</b>	<b>182</b>
<b>Closing cash and cash eq.</b>	<b>327</b>	<b>193</b>	<b>67</b>	<b>131</b>	<b>312</b>

**Per Share**

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	81.5	88.5	98.0	113.6	129.0
Adjusted EPS	74.6	77.7	98.0	113.6	129.0
Dividend per share	12.0	13.0	14.7	16.9	19.2
Book value per share	465.7	538.9	619.1	711.6	816.8

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	2.7	2.3	2.1	1.9	1.6
EV/EBITDA	18.4	16.1	14.1	12.5	11.0
Adjusted P/E	32.5	31.2	24.7	21.3	18.8
P/BV	5.2	4.5	3.9	3.4	3.0

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	62.6	56.0	65.2	65.4	65.4
Interest burden (PBT/EBIT)	108.5	110.1	103.8	105.8	105.9
EBIT margin (EBIT/Revenue)	12.1	12.2	12.7	12.9	12.9
Asset turnover (Revenue/Avg TA)	116.2	120.2	120.4	122.1	122.5
Leverage (Avg TA/Avg Equity)	1.8	1.7	1.6	1.6	1.5
Adjusted ROAE	17.2	15.5	16.9	17.1	16.9

Source: Company, BOBCAPS Research | Note: TA = Total Assets

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	17.0	14.2	10.1	11.7	13.5
EBITDA	(1.1)	12.8	14.3	13.2	13.5
Adjusted EPS	0.9	4.1	26.1	16.0	13.6
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	14.4	14.3	14.8	15.0	15.0
EBIT margin	12.1	12.2	12.7	12.9	12.9
Adjusted profit margin	8.2	7.5	8.6	8.9	8.9
Adjusted ROAE	17.2	15.5	16.9	17.1	16.9
ROCE	14.7	13.8	14.6	14.8	14.7
<b>Working capital days (days)</b>					
Receivables	76	77	75	72	71
Inventory	121	123	122	119	118
Payables	32	33	32	31	31
<b>Ratios (x)</b>					
Gross asset turnover	2.5	2.6	2.6	2.6	2.6
Current ratio	1.6	1.5	1.6	1.7	1.7
Net interest coverage ratio	14.6	19.2	25.2	34.8	37.8
Adjusted debt/equity	0.1	0.1	0.1	0.1	0.0

Source: Company, BOBCAPS Research



## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

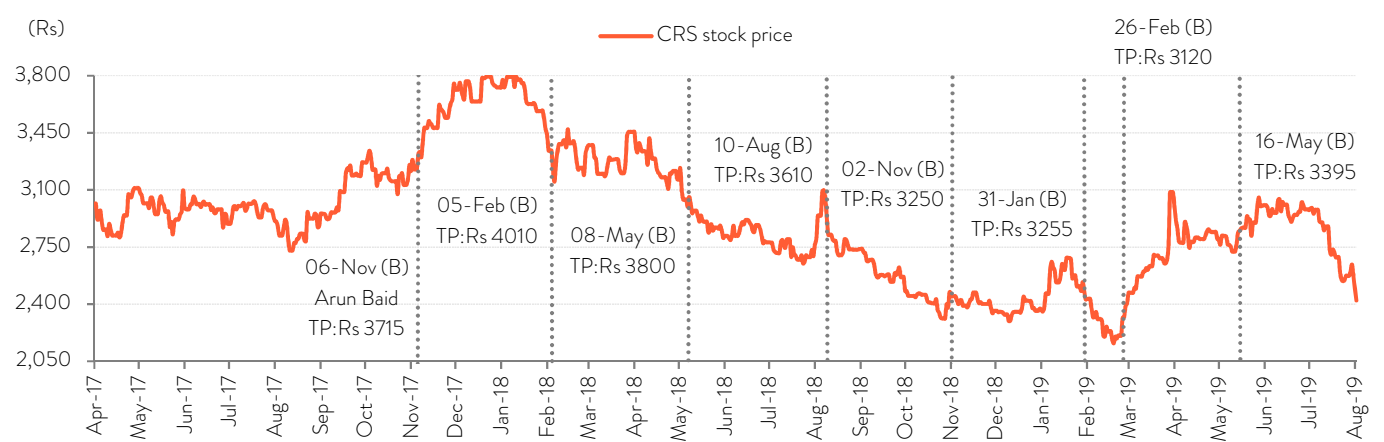
**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### HISTORICAL RATINGS AND TARGET PRICE: CERA SANITARYWARE (CRS IN)



B – Buy, A – Add, R – Reduce, S – Sell

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