

**BUY**

TP: Rs 3,100 | ▲ 18%

**CERA SANITARYWARE**

Construction Materials

06 February 2020

**Q3 marginally better than estimates**

Cera Sanitaryware (CRS) reported a dull Q3FY20 with standalone revenue growth of 1% YoY to Rs 3.2bn, as the sanitaryware segment declined ~11%. Operating margins contracted 105bps YoY to 13.4% despite a 305bps drop in other expense, as gross margins fell 375bps. EBITDA/PBT thus decreased 7%/13% YoY. Management expects the sanitaryware segment to return to growth in FY21. We broadly maintain estimates and roll forward to a revised Mar'21 TP of Rs 3,100 (earlier Rs 3,040).

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**Flattish revenue growth due to decline in sanitaryware segment:** CRS

reported a 1% YoY increase in standalone revenue to Rs 3.2bn in Q3. The sanitaryware segment fell 11% YoY whereas faucets/tiles grew 8.5%/22% YoY. As per management, revenue performance was undermined by a lacklustre demand climate. Management believes the sanitaryware segment will return to growth in FY21 due to the new SKU launches, demand from affordable housing and improving liquidity.

Ticker/Price CRS IN/Rs 2,626

Market cap US\$ 479.4mn

Shares o/s 13mn

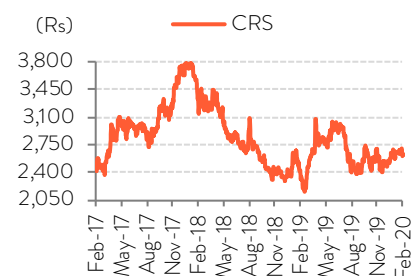
3M ADV US\$ 0.2mn

52wk high/low Rs 3,195/Rs 2,144

Promoter/FPI/DII 54%/8%/38%

Source: NSE

**Weak product mix takes a toll on margins:** CRS's standalone operating margins declined 105bps YoY to 13.4% due to lower gross margins (-375bps YoY) and higher employee expenses (+37bps YoY), which were only partly offset by lower other expenditure (-305bps YoY) – this caused EBITDA/PBT to contract 7%/13% YoY. Gross margin slippage stemmed from an adverse product mix, marked by a reduced share of high-margin sanitaryware products in the quarter (46% vs. 52% YoY). Other expenditure declined YoY aided by lower sales & marketing expenses.

**STOCK PERFORMANCE**

Source: NSE

**Maintain BUY:** Q3 was marginally better than expected. We broadly maintain estimates and roll to a revised Mar'21 TP of Rs 3,100 (earlier Rs 3,040), set at an unchanged 26x one-year forward P/E.

**KEY FINANCIALS**

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	11,776	13,444	13,451	14,798	16,419
EBITDA (Rs mn)	1,699	1,917	1,816	2,057	2,315
Adj. net profit (Rs mn)	970	1,010	1,162	1,352	1,548
Adj. EPS (Rs)	74.6	77.7	89.3	103.9	119.1
Adj. EPS growth (%)	0.9	4.1	15.0	16.4	14.5
Adj. ROAE (%)	17.2	15.5	15.5	15.9	16.0
Adj. P/E (x)	35.2	33.8	29.4	25.3	22.1
EV/EBITDA (x)	20.0	17.6	18.4	16.3	14.5

Source: Company, BOBCAPS Research

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

Important disclosures, including any required research certifications, are provided at the end of this report.



**FIG 1 – STANDALONE QUARTERLY PERFORMANCE**

(Rs mn)	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)	9MFY20	9MFY19	YoY (%)
<b>Total revenues</b>	<b>3,213</b>	<b>3,188</b>	<b>0.8</b>	<b>3,272</b>	<b>(1.8)</b>	<b>9,159</b>	<b>9,305</b>	<b>(1.6)</b>
Total raw material consumed	1,635	1,502	8.8	1,595	2.5	4,461	4,384	1.8
% of sales	50.9	47.1	376bps	48.8	212bps	48.7	47.1	159bps
Employee expense	411	396	3.8	407	1.1	1,217	1,177	3.4
% of sales	12.8	12.4	37bps	12.4	36bps	13.3	12.7	64bps
Other expense	738	830	(11.1)	854	(13.6)	2,284	2,476	(7.8)
% of sales	23.0	26.0	(307bps)	26.1	(313bps)	24.9	26.6	(167bps)
Total expenditure	2,784	2,729	2.0	2,856	(2.5)	7,962	8,037	(0.9)
% of sales	87	85.6	106bps	87.3	(65bps)	87	86.4	56bps
<b>EBITDA</b>	<b>429.2</b>	<b>459.5</b>	<b>(6.6)</b>	<b>415.9</b>	<b>3.2</b>	<b>1,197.3</b>	<b>1,268.1</b>	<b>(5.6)</b>
% of sales	13.4	14.4	(106bps)	12.7	65bps	13.1	13.6	(56bps)
Depreciation	80.1	55.9	43.3	79.3	1.0	236.2	161.7	46.1
Other income	43.0	40.6	6.1	40.8	5.4	113.0	99.6	13.4
Interest cost	10.7	6.5	64.0	10.3	3.1	32.4	17.4	85.9
<b>PBT</b>	<b>381.5</b>	<b>437.6</b>	<b>(12.8)</b>	<b>367.0</b>	<b>3.9</b>	<b>1,041.7</b>	<b>1,188.6</b>	<b>(12.4)</b>
Taxes	97.8	154.0	(36.5)	66.7	46.5	266.9	418.5	(36.2)
Effective tax rate (%)	25.6	35.2	(957bps)	18.2	745bps	25.6	35.2	(958bps)
<b>APAT</b>	<b>283.7</b>	<b>283.6</b>	<b>0.0</b>	<b>300.3</b>	<b>(5.5)</b>	<b>774.7</b>	<b>770.1</b>	<b>0.6</b>

Source: Company, BOBCAPS Research

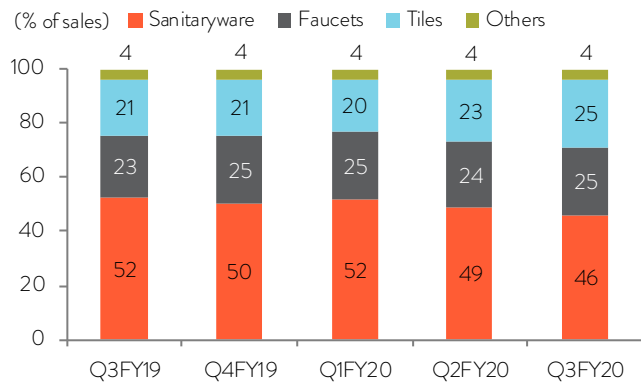
**FIG 2 – CONSOLIDATED QUARTERLY PERFORMANCE**

(Rs mn)	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)	9MFY20	9MFY19	YoY (%)
<b>Total revenues</b>	<b>3,252</b>	<b>3,203</b>	<b>1.5</b>	<b>3,294</b>	<b>(1.3)</b>	<b>9,258</b>	<b>9,346</b>	<b>(0.9)</b>
Total raw material consumed	1,542	1,409	9.4	1,491	3.4	4,178	4,069	2.7
% of sales	48.0	44.2	378bps	45.6	243bps	45.6	43.7	189bps
Employee expense	424	407	4.3	421	0.8	1,257	1,211	3.8
% of sales	13.2	12.8	44bps	12.9	34bps	13.7	13.0	70bps
Other expense	837	921	(9.1)	952	(12.0)	2,592	2,748	(5.7)
% of sales	26.1	28.9	(283bps)	29.1	(304bps)	28.3	29.5	(123bps)
Total expenditure	2,804	2,737	2.4	2,864	(2.1)	8,027	8,028	0.0
% of sales	87.2	85.8	140bps	87.5	(27bps)	87.6	86.3	136bps
<b>EBITDA</b>	<b>448.7</b>	<b>466.4</b>	<b>(3.8)</b>	<b>430.5</b>	<b>4.2</b>	<b>1,231.7</b>	<b>1,317.8</b>	<b>(6.5)</b>
% of sales	14.0	14.6	(66bps)	13.2	81bps	13.4	14.2	(71bps)
Depreciation	95.9	68.8	39.3	95.2	0.8	282.1	200.0	41.1
Other income	50.3	48.9	2.9	47.0	6.9	129.9	118.5	9.6
Interest cost	24.8	18.8	31.8	24.1	3.0	74.0	54.4	36.0
<b>PBT</b>	<b>378.3</b>	<b>427.6</b>	<b>(11.5)</b>	<b>358.3</b>	<b>5.6</b>	<b>1,005.5</b>	<b>1,181.8</b>	<b>(14.9)</b>
Taxes	96.0	156.0	(38.5)	63.4	51.4	256.7	417.5	(38.5)
Effective tax rate (%)	25.4	36.5	(1,111bps)	17.7	769bps	25.5	35.3	(980bps)
<b>APAT</b>	<b>282.3</b>	<b>271.6</b>	<b>3.9</b>	<b>294.9</b>	<b>(4.3)</b>	<b>748.8</b>	<b>764.3</b>	<b>(2.0)</b>
Less: Minority interest	(0.7)	(5.9)	(88.1)	(2.6)	(73.5)	(12.7)	(2.9)	345.4
Add: share of profit in associate	0.66	0.13	4.3	(2.05)	(132.2)	(1.36)	0.19	(8.2)
<b>RPAT</b>	<b>283.6</b>	<b>277.6</b>	<b>2.2</b>	<b>295.5</b>	<b>(4)</b>	<b>760.1</b>	<b>767.3</b>	<b>(0.9)</b>

Source: Company, BOBCAPS Research

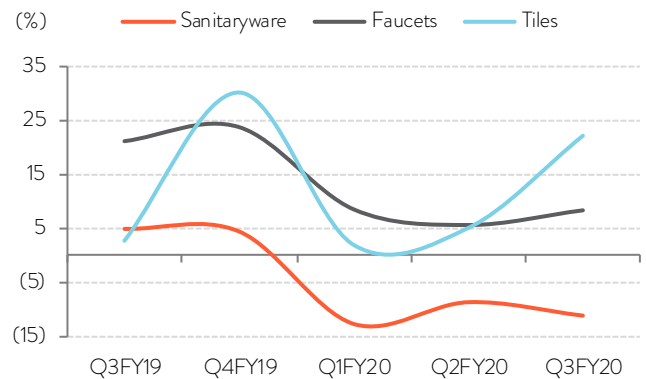
**STANDALONE QUARTERLY TRENDS**

**FIG 3 – REVENUE BREAKUP**



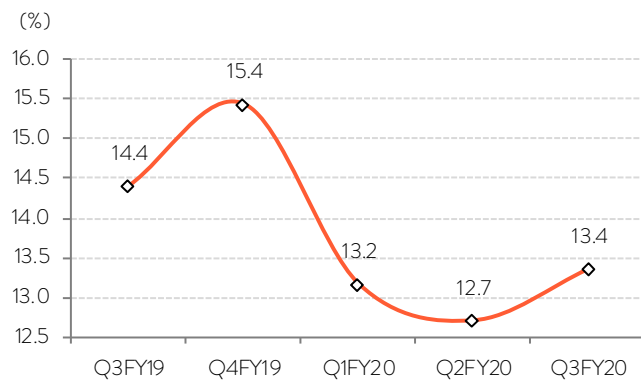
Source: Company, BOBCAPS Research

**FIG 4 – SEGMENTAL GROWTH YOY**



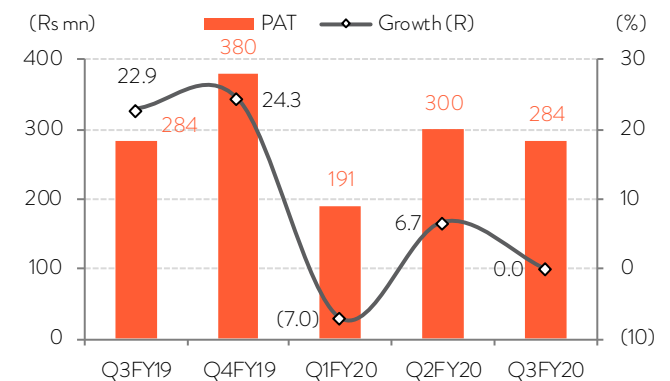
Source: Company, BOBCAPS Research

**FIG 5 – EBITDA MARGIN**



Source: Company, BOBCAPS Research

**FIG 6 – PAT GROWTH YOY**



Source: Company, BOBCAPS Research

**Earnings call highlights**

- Market demand conditions remained subdued in Q3FY20 as customers continued to postpone their purchases.
- CRS believes the sanitaryware market will remain flattish in FY20 and grow at 7-8% in FY21. Management expects growth in its business in FY21 to be driven by affordable housing sales, 50 new SKU launches by the company, and improving liquidity conditions.
- About 35% of CRS’s sanitaryware & faucet revenues come from the entry-level segment and ~50% from the premium segment.
- The company has observed that dealers are streamlining their businesses which will improve their liquidity going ahead.

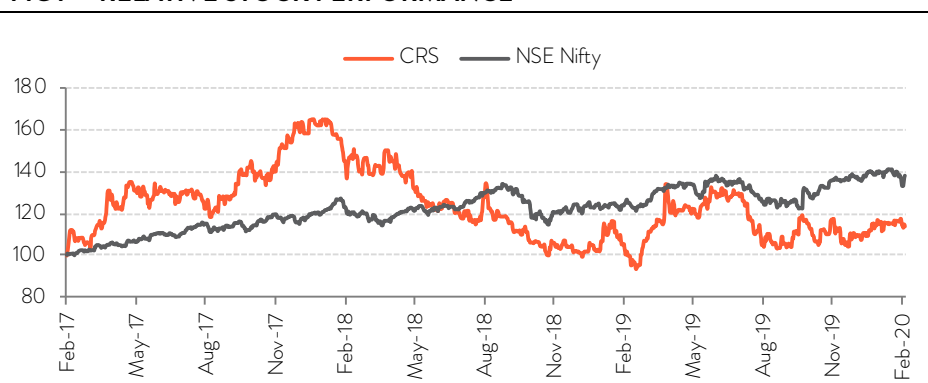
- About 75% of CRS's revenue was derived from the dealer network in Q3 and the balance from institutional sales. A total of ~170 dealers were added during the quarter.
- CRS used 58% of its gas requirement from APM gas and purchased the balance 42% from Sabarmati Gas.
- Raw material pricing was benign and thus the company did not take any price hikes in Q3. A 3-5% hike in the sanitaryware segment is planned for Apr'20.
- For 9MFY20, the company derived 43% of sales from South India, 30% from North India, ~17% from West India and ~10% from eastern states.
- Capex planned for FY20 totals ~Rs 560mn, of which ~Rs 318mn has been spent in 9MFY20. Cash & cash equivalents on the books totalled ~Rs 2.1bn as of 30 Dec 2019.

## Valuation methodology

CRS is the third largest organised sanitaryware player in India with 21-22% 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.

We broadly maintain estimates and roll forward to a revised Mar'21 target price of Rs 3,100 (earlier Rs 3,040), set at an unchanged 26x one-year forward P/E. Maintain BUY.

**FIG 7 – 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>13,451</b>	<b>14,798</b>	<b>16,419</b>
EBITDA	1,699	1,917	1,816	2,057	2,315
Depreciation	(271)	(280)	(375)	(408)	(451)
EBIT	1,428	1,637	1,441	1,649	1,864
Net interest income/(expenses)	(98)	(85)	(93)	(71)	(71)
Other income/(expenses)	129	110	187	202	244
Exceptional items	90	141	0	0	0
EBT	1,459	1,662	1,534	1,781	2,037
Income taxes	(488)	(652)	(387)	(449)	(513)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	(1)	0	14	20	25
<b>Reported net profit</b>	<b>1,061</b>	<b>1,151</b>	<b>1,162</b>	<b>1,352</b>	<b>1,548</b>
Adjustments	(90)	(141)	0	0	0
<b>Adjusted net profit</b>	<b>970</b>	<b>1,010</b>	<b>1,162</b>	<b>1,352</b>	<b>1,548</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	944	1,109	1,032	1,135	1,260
Other current liabilities	1,840	1,979	1,916	2,108	2,339
Provisions	201	365	202	222	246
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	7,885	8,977	10,227
Shareholders' fund	6,056	7,009	7,950	9,042	10,292
<b>Total liabilities and equities</b>	<b>10,461</b>	<b>11,908</b>	<b>12,216</b>	<b>13,713</b>	<b>15,267</b>
Cash and cash eq.	327	193	22	44	70
Accounts receivables	2,680	2,984	2,801	3,081	3,419
Inventories	1,935	2,158	2,045	2,270	2,519
Other current assets	782	747	774	851	945
Investments	1,086	1,779	2,300	2,950	3,550
Net fixed assets	3,584	3,840	4,065	4,307	4,556
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>12,216</b>	<b>13,713</b>	<b>15,267</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	1,537	1,759	2,000
Interest expenses	98	85	93	71	71
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(648)	(22)	(36)	(268)	(300)
Other operating cash flows	(3)	45	0	0	0
<b>Cash flow from operations</b>	<b>778</b>	<b>1,540</b>	<b>1,594</b>	<b>1,563</b>	<b>1,771</b>
Capital expenditures	(470)	(678)	(600)	(650)	(700)
Change in investments	(215)	(693)	(521)	(650)	(600)
Other investing cash flows	(64)	(10)	(14)	(20)	(25)
<b>Cash flow from investing</b>	<b>(749)</b>	<b>(1,381)</b>	<b>(1,135)</b>	<b>(1,320)</b>	<b>(1,325)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	124	(56)	(316)	110	(50)
Interest expenses	(98)	(85)	(93)	(71)	(71)
Dividends paid	(188)	(188)	(207)	(240)	(274)
Other financing cash flows	(107)	36	(14)	(20)	(25)
<b>Cash flow from financing</b>	<b>(268)</b>	<b>(293)</b>	<b>(629)</b>	<b>(221)</b>	<b>(420)</b>
<b>Changes in cash and cash eq.</b>	<b>(239)</b>	<b>(134)</b>	<b>(170)</b>	<b>22</b>	<b>26</b>
<b>Closing cash and cash eq.</b>	<b>327</b>	<b>193</b>	<b>22</b>	<b>44</b>	<b>70</b>

**Per Share**

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	81.5	88.5	89.3	103.9	119.1
Adjusted EPS	74.6	77.7	89.3	103.9	119.1
Dividend per share	12.0	13.0	13.2	15.4	17.6
Book value per share	465.7	538.9	611.3	695.3	791.3

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	2.9	2.5	2.5	2.3	2.0
EV/EBITDA	20.0	17.6	18.4	16.3	14.5
Adjusted P/E	35.2	33.8	29.4	25.3	22.1
P/BV	5.6	4.9	4.3	3.8	3.3

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	62.6	56.0	75.7	75.9	76.0
Interest burden (PBT/EBIT)	108.5	110.1	106.5	108.0	109.3
EBIT margin (EBIT/Revenue)	12.1	12.2	10.7	11.1	11.4
Asset turnover (Revenue/Avg TA)	116.2	120.2	111.5	114.1	113.3
Leverage (Avg TA/Avg Equity)	1.8	1.7	1.6	1.5	1.5
Adjusted ROAE	17.2	15.5	15.5	15.9	16.0

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	0.1	10.0	11.0
EBITDA	(1.1)	12.8	(5.3)	13.3	12.5
Adjusted EPS	0.9	4.1	15.0	16.4	14.5
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	14.4	14.3	13.5	13.9	14.1
EBIT margin	12.1	12.2	10.7	11.1	11.4
Adjusted profit margin	8.2	7.5	8.6	9.1	9.4
Adjusted ROAE	17.2	15.5	15.5	15.9	16.0
ROCE	14.7	13.8	12.9	13.4	13.4
<b>Working capital days (days)</b>					
Receivables	76	77	78	73	72
Inventory	121	123	125	117	117
Payables	32	33	34	31	31
<b>Ratios (x)</b>					
Gross asset turnover	2.5	2.6	2.4	2.4	2.4
Current ratio	1.6	1.5	1.6	1.6	1.7
Net interest coverage ratio	14.6	19.2	15.5	23.2	26.3
Adjusted debt/equity	0.1	0.1	0.1	0.1	0.1

Source: Company, BOBCAPS Research



## Disclaimer

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

**BUY** – Expected return >+15%

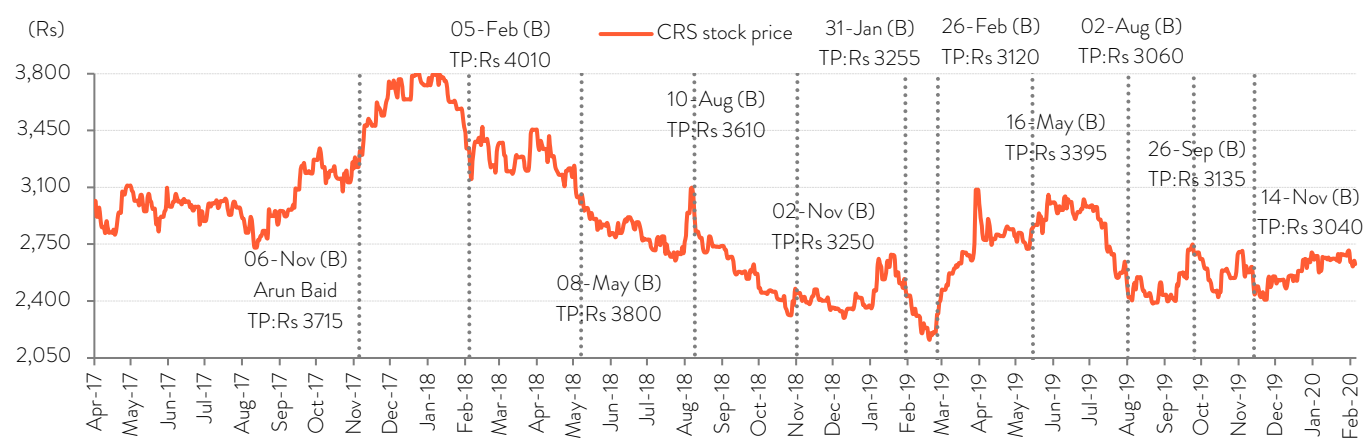
**ADD** – Expected return from >+5% to +15%

**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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As of 31 January 2020, out of 85 rated stocks in the BOB Capital Markets Limited (BOBCAPS) coverage universe, 50 have BUY ratings, 18 are rated ADD, 8 are rated REDUCE and 9 are rated SELL. None of these companies have been investment banking clients in the last 12 months.

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