

BUY

TP: Rs 3,900 | ▲ 16%

CERA SANITARYWARE

Construction Materials

03 February 2021

Supply disruptions hit Q3 but demand outlook strong – raise to BUY

Cera Sanitaryware (CRS) reported a 3% YoY decline in consolidated revenue for Q3FY21, with the sanitaryware segment down 5% due to production issues.

Operating margins were flattish at 13.7% with EBITDA down 4% YoY.

Management expects demand to outstrip supply for the next 2-3 quarters at least. We raise FY21-FY23 PAT estimates by 15-22% to bake in the swift demand recovery and reset our target P/E from 28x to 30x. Upgrade from ADD to BUY as we roll to a revised Mar'22 TP of Rs 3,900 (vs. Rs 2,910).

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Revenue declines due to sanitaryware supply issues: CRS reported a 3% YoY decline in consolidated revenue to Rs 3.2bn in Q3. The sanitaryware/tiles segments fell 5%/7% YoY and faucets grew ~8%. As per management, labour issues eroded sanitaryware segment revenue by ~Rs 650mn during the quarter – these issues were resolved at the end of Dec'20. The tiles segment declined as the company focused on cash-&-carry and premium products. Management expects improvement ahead as demand is robust.

Ticker/Price	CRS IN/Rs 3,359
Market cap	US\$ 598.7mn
Shares o/s	13mn
3M ADV	US\$ 0.6mn
52wk high/low	Rs 3,744/Rs 1,986
Promoter/FPI/DII	54%/15%/31%

Source: NSE

Weak product mix compresses margins: CRS's consolidated operating margins decreased 10bps YoY to 13.7% as gross margin shrinkage of 625bps neutralised lower employee/other expenses (-175bps/-440bps YoY) – this caused EBITDA to decline by 4% YoY. Gross margins contracted due to an adverse product mix from lower sales in the high-margin sanitaryware segment. Other expenses declined on the back of cost rationalisation measures. Management expects margins to improve as demand normalises.

STOCK PERFORMANCE



Source: NSE

Upgrade to BUY: Given the faster-than-expected demand recovery, we raise FY21-FY23 PAT estimates by 15-22%, reset our target P/E to 30x (from 28x), and upgrade the stock from ADD to BUY. On rolling valuations forward, we arrive at a revised Mar'22 TP of Rs 3,900.

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	13,491	12,220	12,034	14,392	16,135
EBITDA (Rs mn)	1,964	1,654	1,436	2,154	2,450
Adj. net profit (Rs mn)	1,010	1,013	909	1,476	1,691
Adj. EPS (Rs)	77.7	77.9	69.9	113.5	130.1
Adj. EPS growth (%)	4.1	0.3	(10.3)	62.4	14.6
Adj. ROAE (%)	15.5	13.8	11.3	16.4	16.7
Adj. P/E (x)	43.2	43.1	48.1	29.6	25.8
EV/EBITDA (x)	22.0	26.0	29.9	20.0	17.6

Source: Company, BOBCAPS Research

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



FIG 1 – CONSOLIDATED QUARTERLY PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Total revenues	3,158	3,252	(2.9)	3,241	(2.6)	7,859	9,258	(15.1)
Total raw material consumed	1,694	1,542	9.9	1,645	3.0	4,104	4,178	(1.8)
% of sales	53.7	47.4	625bps	50.7	291bps	53.3	45.6	767bps
Employee exps	357	424	(15.9)	374	(4.6)	1,053	1,257	(16.2)
% of sales	11.3	13.1	(175bps)	11.5	(24bps)	13.7	13.7	(5bps)
Other exp	675	837	(19.4)	812	(16.9)	1,822	2,592	(29.7)
% of sales	21.4	25.7	(438bps)	25.0	(368bps)	23.6	28.3	(465bps)
Total expenditure	2,726	2,804	(2.8)	2,831	(3.7)	6,979	8,027	(13.0)
% of sales	86.3	86.2	13bps	87.3	(101bps)	90.6	87.6	297bps
EBITDA	432	449	(3.8)	410	5.2	880	1,232	(28.6)
% of sales	13.7	13.8	(13bps)	12.7	101bps	11.4	13.4	(203bps)
Depreciation	100	96	4.1	99	0.8	295	282	4.7
Other income	94	50	87.0	45	111.1	209	130	60.6
Interest cost	23	25	(7.5)	23	(0.4)	69	74	(6.4)
PBT	403	378	6.5	333	21.1	724	1,005	(28.0)
Taxes	96	96	0.1	100	(4.4)	201	257	(21.6)
Effective tax rate (%)	23.8	25.4	(154bps)	30.2	(636bps)	27.8	25.5	230bps
PAT before minority interest/associates	307	282	8.7	232	32.2	522	749	(30.2)
Less: Minority interest	7.8	(0.7)	(1219.5)	(15.0)	(152.0)	(29.7)	(12.7)	133
Add: share of profit in associate	0.2	0.7	(0.7)	(1.1)	(119.9)	(2.0)	(1.4)	0.4
RPAT	299	284	5.5	246	22	550	760	(27.6)

Source: Company, BOBCAPS Research

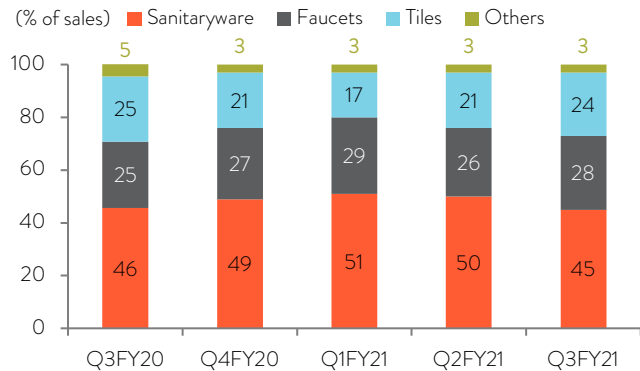
FIG 2 – STANDALONE QUARTERLY PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Total revenues	3,098	3,213	(3.6)	3,179	(2.5)	7,703	9,159	(15.9)
Total raw material consumed	1,801	1,635	10.1	1,668	7.9	4,195	4,461	(6.0)
% of sales	58.1	50.9	724bps	52.5	564bps	54.5	48.7	576bps
Employee exps	342	411	(16.8)	360	(5.0)	1,015	1,217	(16.6)
% of sales	11.0	12.8	(176bps)	11.3	(29bps)	13.2	13.3	(11bps)
Other exp	559	738	(24.3)	746	(25.1)	1,625	2,284	(28.8)
% of sales	18.0	23.0	(494bps)	23.5	(544bps)	21.1	24.9	(384bps)
Total expenditure	2,701	2,784	(3.0)	2,774	(2.6)	6,835	7,962	(14.2)
% of sales	87	86.6	54bps	87.3	(9bps)	89	86.9	180bps
EBITDA	397	429	(7.5)	405	(1.9)	868	1,197	(27.5)
% of sales	12.8	13.4	(54bps)	12.7	9bps	11.3	13.1	(180bps)
Depreciation	84	80	4.7	83	0.6	248	236	5.2
Other income	85	43	97.7	39	116.1	193	113	71.0
Interest cost	10	11	(10.6)	9	2.3	29	32	(11.0)
PBT	389	381	1.9	351	10.7	784	1,042	(24.7)
Taxes	98	98	0.1	88	10.7	201	267	(24.6)
Effective tax rate (%)	25.2	25.6	(46bps)	25.2	0bps	25.7	25.6	3bps
APAT	291	284	2.5	263	10.7	583	775	(24.8)

Source: Company, BOBCAPS Research

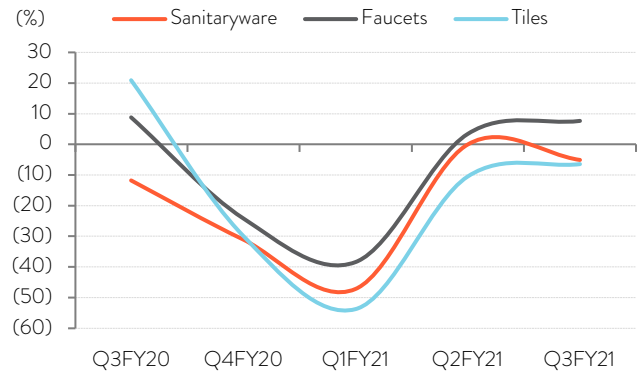
CONSOLIDATED QUARTERLY TRENDS

FIG 3 – REVENUE BREAKUP



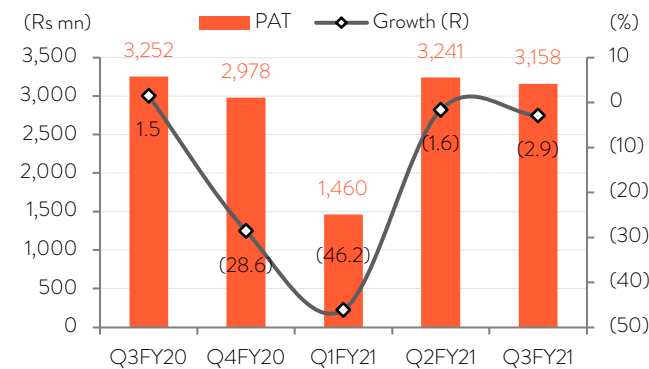
Source: Company, BOBCAPS Research

FIG 4 – SEGMENTAL GROWTH YOY



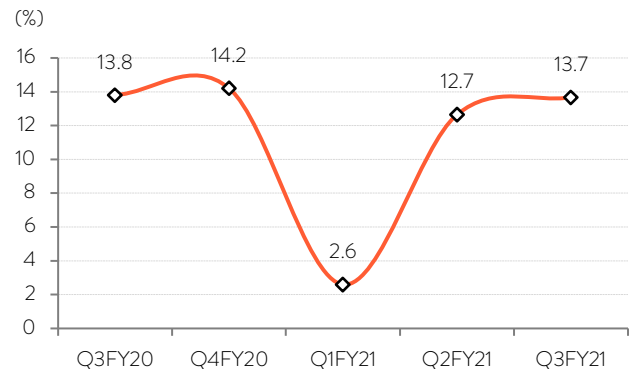
Source: Company, BOBCAPS Research

FIG 5 – CONSOLIDATED SALES & GROWTH



Source: Company, BOBCAPS Research

FIG 6 – CONSOLIDATED EBITDA MARGINS



Source: Company, BOBCAPS Research

Earnings call highlights

- CRS saw good demand across the sanitaryware and faucet segments in Q3FY21. Tier-2-and-below cities continued to show healthy demand momentum during the quarter.
- The company’s Kadi sanitaryware plant had some labour issues which affected production in Q3 and caused a loss of sales and EBITDA to the tune of Rs 650mn and Rs 100mn respectively. These issues were sorted out by end-Dec’20 and the plant is now running on three shifts. The last labour disruption occurred in 2002 and management does not expect a reoccurrence.
- As per management, the demand environment remains robust in both sanitaryware and faucets and could outstrip supply for the next few quarters. Segmental sales in January grew at a robust ~20% YoY, the first time since 2012 that demand has been so robust.

- The company has taken a 5-7% price increase in sanitaryware from Feb'20.
- Due to an increase in prices of raw material for faucets, CRS took an 8-10% price hike in the segment from Feb'20 which should help maintain margins.
- Capex planned for FY21 totals ~Rs 120mn. Cash & cash equivalents on the books stood at ~Rs 4.09bn as of 31 December 2020.

Valuation methodology

CRS is one of the largest organised sanitaryware players in India. 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 like CRS for its strong balance sheet and working capital discipline.

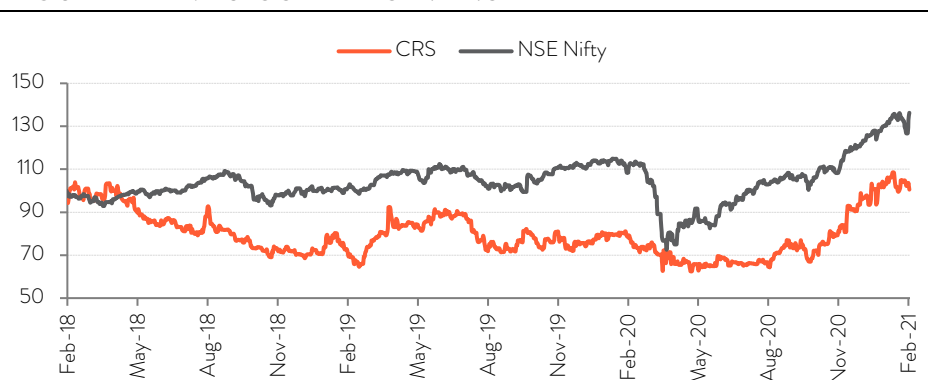
Given the faster-than-expected recovery in demand, we raise our FY21/FY22/FY23 earnings estimates by 15%/19%/22%, upgrade our target P/E from 28x to 30x – in line with the stock’s five-year average forward multiple – and upgrade our rating from ADD to BUY. On rolling valuations over, we move to a revised Mar’22 target price of Rs 3,900 (vs. Rs 2,910).

FIG 7 – REVISED ESTIMATES

(Rs mn)	Old			New			Change (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	11,628	13,278	1,4711	12,034	14,392	16,135	3.5	8.4	9.7
EBITDA	1,335	1,886	2,102	1,436	2,154	2,450	7.5	14.3	16.6
PAT	789	1,240	1,386	909	1,476	1,691	15.3	19.0	22.0

Source: 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.
- **Prolonged Covid-19 outbreak:** If pandemic fears prevail for a prolonged period of time, revenues will be adversely affected.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	13,491	12,220	12,034	14,392	16,135
EBITDA	1,964	1,654	1,436	2,154	2,450
Depreciation	(280)	(388)	(400)	(416)	(462)
EBIT	1,684	1,266	1,036	1,738	1,988
Net interest income/(expenses)	(85)	(101)	(92)	(61)	(58)
Other income/(expenses)	63	65	242	283	328
Exceptional items	141	119	0	0	0
EBT	1,662	1,230	1,186	1,960	2,259
Income taxes	(652)	(243)	(299)	(494)	(569)
Min. int./Inc. from associates	0	27	22	10	2
Reported net profit	1,151	1,133	909	1,476	1,691
Adjustments	(141)	(119)	0	0	0
Adjusted net profit	1,010	1,013	909	1,476	1,691

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	1,109	953	1,022	1,222	1,370
Other current liabilities	1,979	2,102	1,747	2,050	2,254
Provisions	365	136	181	201	226
Debt funds	906	919	620	600	500
Other liabilities	436	299	319	351	383
Equity capital	65	65	65	65	65
Reserves & surplus	6,944	7,642	8,370	9,484	10,667
Shareholders' fund	7,009	7,707	8,435	9,549	10,732
Total liabilities and equities	11,908	12,194	12,379	14,019	15,508
Cash and cash eq.	193	125	24	71	201
Accounts receivables	2,984	2,228	2,440	2,800	3,139
Inventories	2,158	2,430	1,879	2,326	2,608
Other current assets	747	737	725	828	928
Investments	1,779	2,283	3,100	3,800	4,300
Net fixed assets	3,845	4,373	4,194	4,177	4,315
CWIP	195	5	5	5	5
Intangible assets	9	12	12	12	12
Total assets	11,908	12,194	12,379	14,019	15,508

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	1,431	1,520	1,309	1,892	2,153
Interest expenses	85	101	92	61	58
Changes in working capital	(22)	33	111	(385)	(345)
Other operating cash flows	45	(137)	20	32	32
Cash flow from operations	1,540	1,517	1,532	1,600	1,899
Capital expenditures	(678)	(450)	(220)	(400)	(600)
Change in investments	(693)	(504)	(817)	(700)	(500)
Other investing cash flows	(9)	(45)	(22)	(10)	(2)
Cash flow from investing	(1,380)	(999)	(1,059)	(1,110)	(1,102)
Debt raised/repaid	(56)	13	(299)	(20)	(100)
Interest expenses	(85)	(101)	(92)	(61)	(58)
Dividends paid	(188)	(396)	(160)	(352)	(507)
Other financing cash flows	36	(103)	(22)	(10)	(2)
Cash flow from financing	(293)	(586)	(574)	(443)	(667)
Changes in cash and cash eq.	(134)	(68)	(101)	47	130
Closing cash and cash eq.	193	125	24	71	201

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	88.5	87.1	69.9	113.5	130.1
Adjusted EPS	77.7	77.9	69.9	113.5	130.1
Dividend per share	13.0	13.0	10.2	22.5	32.5
Book value per share	538.9	592.6	648.5	734.2	825.1

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	3.2	3.5	3.6	3.0	2.7
EV/EBITDA	22.0	26.0	29.9	20.0	17.6
Adjusted P/E	43.2	43.1	48.1	29.6	25.8
P/BV	6.2	5.7	5.2	4.6	4.1

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	56.0	75.1	76.7	75.3	74.9
Interest burden (PBT/EBIT)	107.1	106.6	114.5	112.8	113.6
EBIT margin (EBIT/Revenue)	12.5	10.4	8.6	12.1	12.3
Asset turnover (Revenue/Avg TA)	120.6	101.4	97.9	109.0	109.3
Leverage (Avg TA/Avg Equity)	1.7	1.6	1.5	1.5	1.5
Adjusted ROAE	15.5	13.8	11.3	16.4	16.7

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	14.5	(9.4)	(1.5)	19.6	12.1
EBITDA	15.5	(15.8)	(13.2)	50.0	13.7
Adjusted EPS	4.1	0.3	(10.3)	62.4	14.6
Profitability & Return ratios (%)					
EBITDA margin	14.6	13.5	11.9	15.0	15.2
EBIT margin	12.5	10.4	8.6	12.1	12.3
Adjusted profit margin	7.5	8.3	7.6	10.3	10.5
Adjusted ROAE	15.5	13.8	11.3	16.4	16.7
ROCE	14.2	12.4	8.7	13.5	13.9
Working capital days (days)					
Receivables	77	78	71	66	67
Inventory	123	152	140	117	122
Payables	33	36	34	33	35
Ratios (x)					
Gross asset turnover	2.6	2.1	1.9	2.2	2.3
Current ratio	1.5	1.5	1.5	1.6	1.7
Net interest coverage ratio	19.7	12.6	11.2	28.5	34.4
Adjusted debt/equity	0.1	0.1	0.1	0.1	0.0

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

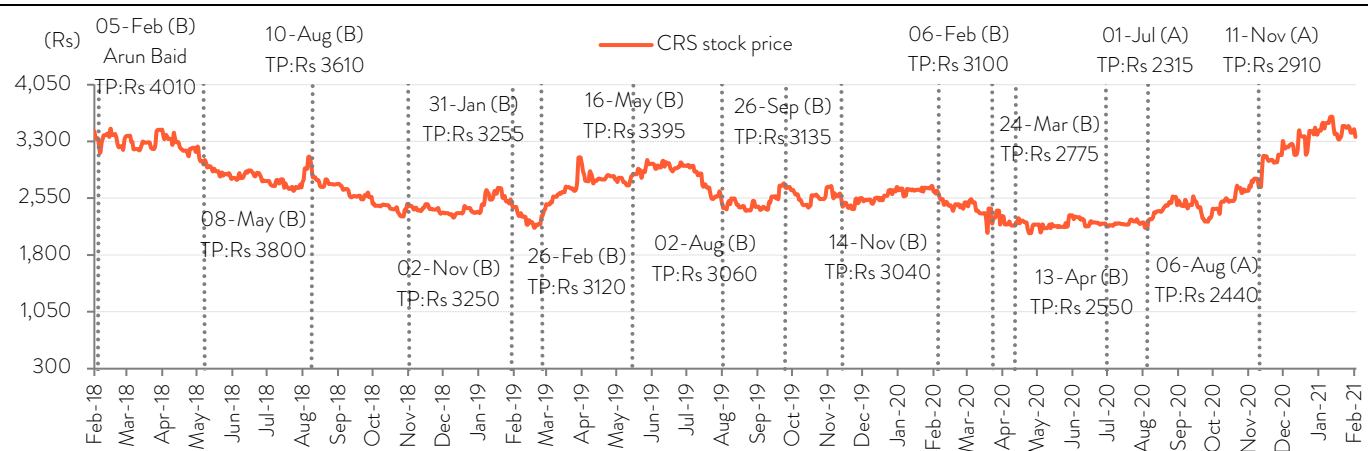
ADD – Expected return from >+5% to +15%

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)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): CERA SANITARYWARE (CRS IN)



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

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