

HOLD

TP: Rs 1,393 | ▲ 14%

KAJARIA CERAMICS

Construction Materials

25 October 2021

Robust volume growth reflects strong underlying demand

- Q2 revenue grew 37% YoY (+73% QoQ) driven by 25% volume growth to 24.8msm
- EBITDA margin declined 160bps YoY to 18.5% on higher input cost (+140bps) and power & fuel cost (+130bps)
- We raise FY22/FY23 revenue 2%/3% to factor in higher tile volumes and realisations; retain HOLD with a new TP of Rs 1,393 (vs. Rs 995)

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Demand rebound buoys topline: KJC's Q2FY22 revenue growth surged 37% YoY to Rs 9.7bn (+73% QoQ), primarily led by a 25% rise in sale volumes to 24.8msm as urban demand rebounded to normal levels and smaller towns showed strong growth. Revenue from the tiles business rose 36% YoY to Rs 8.8bn, with the company's own manufacturing, subsidiaries and outsourcing businesses contributing Rs 4.6bn (+21% YoY), Rs 2.1bn (+42%) and Rs 2.1bn (+74%) respectively. Sanitaryware and plywood revenue climbed 48% YoY to Rs.0.9bn.

Gross margin down 277bps YoY; EBITDA margin fares relatively better: Due to higher gas (+130bps YoY) and other input costs (+140bps), gross margin contracted 280bps to 38.4%. EBITDA margin fared relatively better at 18.5%, down 160bps YoY.

Prudent balance sheet: KJC generated surplus cash of Rs 1.5bn, resulting in a net cash position of Rs 4.7bn. Working capital days improved to 56 vs. 88 in Q1FY22.

Guidance: Management has guided for H2FY22 volume and revenue growth of 15% and 20% respectively. In comparison, management expects industry volumes to grow 7-9% during the same period. KJC is targeting revenue of over Rs 5bn in bathroom fittings in the next two years.

Long-term value play; maintain HOLD: We believe KJC is in a sweet spot and should see improvement in operations and demand environment post easing of lockdowns in the domestic market. With demand recovering Q2 onwards, tiles prices have risen by ~4%, boosting cost pass-through and, hence, margin should rebound. KJC's upcoming capacities in FY22 at a capex of ~Rs 2.8bn will continue to support its market share, strengthening its leadership position in the domestic market.

We raise revenue estimates to incorporate the higher tiles volume and realisations and thus raise our target one-year forward P/E multiple from 34.5x to 47x – which is at 18% premium to the stock's three-year median of 40x. While we continue to like KJC, the stock has rallied >70% since Jan'21 and currently trades at ~54x FY22E EPS which looks expensive. We retain HOLD and roll over to a new Sep'22 TP of Rs 1,393.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	KJC IN/Rs 1,226
Market cap	US\$ 2.6bn
Free float	52%
3M ADV	US\$ 6.0mn
52wk high/low	Rs 1,355/Rs 554
Promoter/FPI/DII	48%/25%/27%

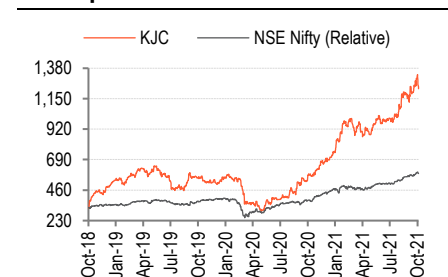
Source: NSE | Price as of 22 Oct 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	27,809	35,098	41,030
EBITDA (Rs mn)	5,088	6,006	7,604
Adj. net profit (Rs mn)	3,081	3,626	4,710
Adj. EPS (Rs)	19.4	22.8	29.6
Consensus EPS (Rs)	17.9	24.3	30.0
Adj. ROAE (%)	17.2	18.9	23.3
Adj. P/E (x)	63.3	53.8	41.4
EV/EBITDA (x)	38.0	32.1	25.4
Adj. EPS growth (%)	20.6	17.7	29.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Earnings calls highlights

- **Sales:** As per management, sales in tier I, II and III cities have resumed in full swing from June onwards.
- **Capacity utilisation:** Average capacity utilisation during Q2FY22 was at ~100% with the pickup in sales. Management expects utilisation to remain high given robust demand for tiles due to a resurgence in construction activities.
- **RM and gas price rise:** Raw material prices required for the tiles industry, including brass, gas, and packing boxes, have jumped over the past 6-9 months. Gas prices currently stand at Rs 38/scm in the northern region, Rs 60/scm in the south and Rs 50/scm in Morbi (Gujarat). KJC is anticipating a possible gas hike of Rs 15/scm in Morbi next month. Morbi and South India account for only 18% and 10% of KJC's sales respectively and the balance comes from the North.
- **Price hike:** In order to offset the rise in gas prices and higher transportation cost, the company has increased prices of all products three times in FY22 – by 1-1.5% in Apr'21, 2-3% in July and ~4% in October. The bathware segment would see 20-25% price increase in this fiscal. In sanitaryware, the 8-10% rise in gas cost has been a pass-through. Per management, the company takes a price increase with a lag effect of 15-30 days and is thus able to protect margins.
- **A&P spends:** A&P spends (under 'other expenses') stood at Rs 460mn in FY21, Rs 170mn in Q2FY22 and are guided to total Rs 700mn for full-year FY22.
- **Exports:** Exports currently stand at 2-3% of the topline which should increase to 5-8% in a couple of years. Management indicated that exports are not competitive and hence not a focus area for the company. Europe has seen a cost increase of EUR 1.5/sqm during Q2 which does make exports from India competitive, excluding high ocean freight rates
- **Imports:** Tiles have not been imported into India in the last 5-7 years. Bath fittings are not imported either and sanitaryware imports have halted due to high freight cost in China which has recently shot up from US\$ 1,500-2,000 per container to US\$ 7,000. In addition, post pandemic many countries have levied an anti-dumping duty on China for the next 3-5 years. India is the second largest producer of tiles in the world and highly cost competitive, which implies it stands to benefit the most.
- **Sanitaryware:** KJC is targeting Rs 2.8bn-3bn of revenue from sanitaryware in FY22. Over 2-3 years, the company expects the segment to cross Rs 5bn in revenue.
- **Capex plans:** (1) Gailpur plant – Rs 600mn capex, adding 4.2msm of capacity, (2) Srikalahasti plant – Rs 1.1bn, adding 3.8msm of capacity, and (3) Jaxx plant – Rs 800mn, adding 4.4msm of capacity. All the capex will be completed in FY22.

Fig 1 – Consolidated quarterly performance

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H2FY22	H2FY21	YoY (%)
Net Sales	9,736	7,125	36.6	5,617	73.3	15,352	9,901	55.1
COGS	5,999	4,193	43.1	3,259	84.0	9,258	6,133	50.9
Employee cost	1,020	779	31.0	933	9.4	1,953	1,387	40.8
Other expenses	912	717	27.3	620	47.1	1,532	1,019	50.3
EBITDA	1,805	1,437	25.6	805	124.3	2,610	1,361	91.7
EBITDA Margin (%)	18.5	20.2	(163bps)	14.3	421bps	17.0	13.7	325bps
Depreciation and amortization	282	274	2.9	265	6.1	547	526	4.0
EBIT	1,523	1,163	31.0	539	182.4	2,063	835	146.9
EBIT Margin (%)	15.6	16.3	(68bps)	9.6	604bps	13.4	8.4	500bps
Net Interest expenses	27	21	30.8	30	(9.9)	57	55	5.1
Other non-operating inc (exp), net	71	48	48.6	60	18.7	131	74	77.1
Earnings before tax	1,567	1,190	31.7	569	175.4	2,137	855	149.9
Income taxes	374	294	27.3	154	142.7	528	288	83.5
Earnings after tax	1,193	896	33.1	415	187.5	1,608	567	183.6
Extraordinary items	0	0	-	0	-	0	0	n.m.
Minority interest (expense) income	32	5	511.5	(16)	(298.8)	16	(53)	(129.7)
Reported Net income (loss)	1,161	891	30.3	431	169.5	1,592	620	156.8
APAT	1,161	891	30.3	431	169.5	1,592	620	156.8

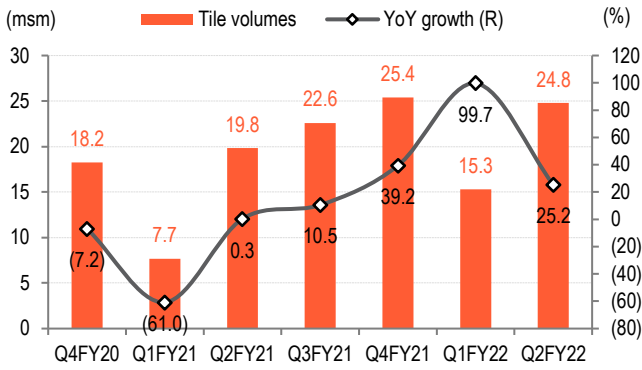
Source: Company, BOBCAPS Research

Fig 2 – Consolidated segmental performance

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H2FY22	H2FY21	YoY (%)
Segment Revenues								
Tiles	8,826	6,510	35.6	5,193	69.9	14,019	9,087	54.3
Other	910	615	47.8	423	114.9	1,333	814	63.8
Total revenues	9,736	7,125	36.6	5,617	73.3	15,352	9,901	55.1
EBIT								
Tiles	1459.1	1150.9	26.8	531.9	174.3	1991	889.1	123.9
Other	64.3	12.4	418.5	7.1	805.6	71.4	(53.7)	(233.0)
Total	1,523	1,163	31.0	539	182.6	2,062	835	146.9
EBIT Margins								
Tiles	16.5	17.7	(115bps)	10.2	629bps	14.2	9.8	442bps
Other	7.1	2.0	505bps	1.7	539bps	5.4	(6.6%)	1195bps

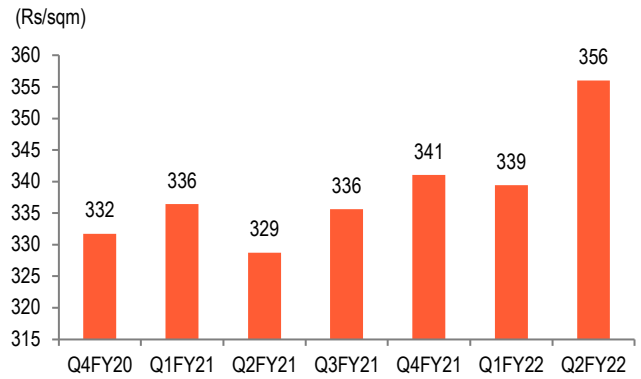
Source: Company, BOBCAPS Research

Fig 3 – Tile volumes



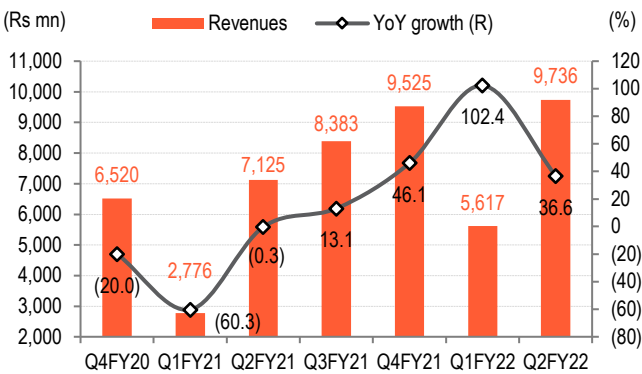
Source: Company, BOBCAPS Research

Fig 4 – Tile net realisations



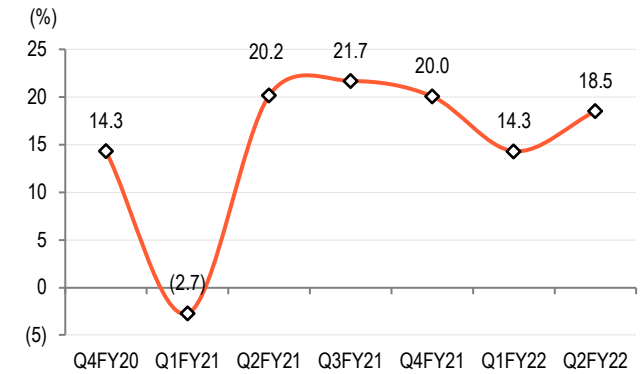
Source: Company, BOBCAPS Research

Fig 5 – Consolidated revenue trend



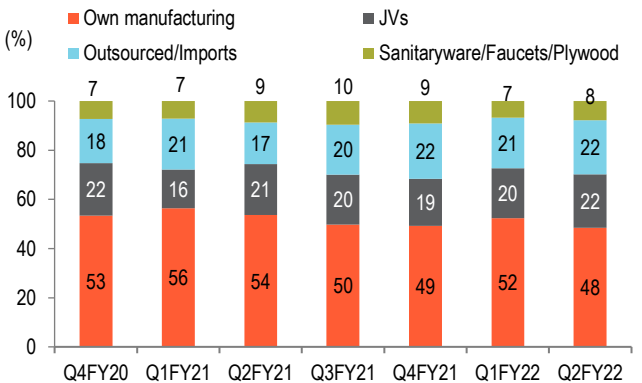
Source: Company, BOBCAPS Research

Fig 6 – Consolidated EBITDA margin trend



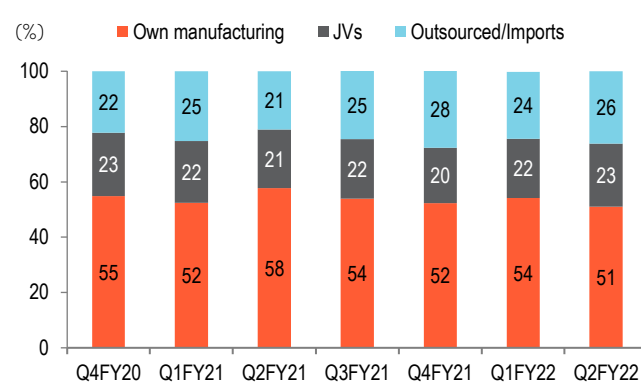
Source: Company, BOBCAPS Research

Fig 7 – Revenue breakup



Source: Company, BOBCAPS Research

Fig 8 – Tile volume breakup



Source: Company, BOBCAPS Research

Valuation methodology

We continue to like KJC for its superior margin in the tiles segment (a function of its robust distribution and cost controls) and fast expansion in the bathware and plywood businesses. Asset utilisation continues to improve, and management is optimistic of the demand environment in FY22. We believe the company will benefit from the recovery in demand given its healthy cash balance, resilient track record and superior brand presence.

Following the Q2FY22 results, we raise our revenue estimates to incorporate the higher tiles volumes and realisations. However, owing to the increase in input cost and gas price hike, we scale back our FY22/FY23 EBITDA margin assumptions to 17.1%/18.5% from 18.4%/19.3%.

At the same time, we increase our target one-year forward P/E multiple from 34.5x to 47x – an 18% premium to the stock's three-year median of 40x – as we continue to like KJC for its scale of operations, balance sheet strength, extensive distribution network and strong brand recall. However, the stock has rallied >70% since Jan'21 and currently trades at ~54x FY22E EPS which looks expensive. We thus retain HOLD and roll over to a new Sep'22 TP of Rs 1,393 (vs. Rs 995).

Fig 9 – Revised estimates

(Rs mn)	New		Old		Change (%)	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Revenue	35,098	41,030	34,273	39,720	2.4	3.3
EBITDA	6,006	7,604	6,308	7,648	(4.8)	(0.6)
PAT	3,626	4,710	3,848	4,743	(5.5)	(0.7)

Source: BOBCAPS Research

Fig 10 – Key assumptions

Parameter	FY21	FY22E	FY23E	FY24E
Tiles Volume	75.4	90.5	104.1	117.6
Growth (%)	(3.4)	20.0	15.0	13.0
Tiles revenue (Rs mn)	25,328	31,372	36,439	41,176
Growth (%)	(2.8)	23.9	16.2	13.0
Sanitaryware/Faucetware revenue (Rs mn)	2,090	2,926	3,511	4,213
Growth (%)	19.9	40.0	20.0	20.0
Plywood (Rs mn)	392	800	1,080	1,458
Growth (%)	35.4	104.3	35.0	35.0

Source: Company, BOBCAPS Research

Fig 11 – Peer comparison

Company	Ticker	Rating	Target Price (Rs)	Revenue CAGR FY21-23E (%)	EPS (Rs)		ROE (%)		Target P/E (x)
					FY22E	FY23E	FY22E	FY23E	
Kajaria Ceramics	KJC IN	HOLD	1,393	21.5	22.8	29.6	18.9	23.3	47
Somany Ceramics	SOMC IN	BUY	640	16.4	21.8	29.1	13.2	15.3	22
Greenply Ind	MTLM IN	HOLD	230	18.7	9.2	11.3	23.0	22.9	20
Century Plyboard	CPBI IN	SELL	370	19.5	11.9	14.7	19.1	19.6	25
Cera Sanitaryware	CRS IN	HOLD	4,145	16.1	115.4	138.1	16.2	17.1	30
Astral	ASTRA IN	SELL	1,210	16.3	20.2	25.2	20.3	22.6	48
Finolex Ind	FNXP IN	HOLD	185	4.2	7.3	7.5	13.9	13.2	24
Supreme Ind	SI IN	BUY	2,735	22.7	76.2	91.2	28.5	29.9	30

Source: BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- benign RM prices,
- lower competition from the informal sector, and
- sharp improvement in housing demand.

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	28,080	27,809	35,098	41,030	46,847
EBITDA	4,159	5,088	6,006	7,604	9,197
Depreciation	(1,081)	(1,067)	(1,186)	(1,352)	(1,497)
EBIT	3,078	4,022	4,820	6,252	7,700
Net interest inc./(exp.)	(195)	(107)	(97)	(72)	(52)
Other inc./(exp.)	242	213	224	246	271
Exceptional items	0	0	0	0	0
EBT	3,125	4,127	4,947	6,426	7,918
Income taxes	(589)	(1,038)	(1,247)	(1,619)	(1,995)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	18	(9)	(74)	(96)	(118)
Reported net profit	2,553	3,081	3,626	4,710	5,805
Adjustments	0	0	0	0	0
Adjusted net profit	2,553	3,081	3,626	4,710	5,805

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	2,105	1,760	2,292	2,659	3,016
Other current liabilities	2,311	2,201	2,191	2,765	3,232
Provisions	288	313	338	363	388
Debt funds	1,171	971	721	521	321
Other liabilities	731	687	712	737	762
Equity capital	159	159	159	159	159
Reserves & surplus	16,984	18,530	19,436	20,614	22,065
Shareholders' fund	17,143	18,689	19,595	20,773	22,224
Total liab. and equities	24,386	25,266	26,569	28,633	30,877
Cash and cash eq.	2,350	4,477	1,266	281	56
Accounts receivables	3,967	4,317	5,289	6,183	7,059
Inventories	5,127	3,731	5,770	6,632	7,573
Other current assets	640	615	769	899	1,027
Investments	3	0	0	0	0
Net fixed assets	11,854	11,911	13,205	14,343	14,846
CWIP	257	50	70	80	80
Intangible assets	103	112	112	112	112
Deferred tax assets, net	15	13	0	0	0
Other assets	70	40	95	115	132
Total assets	24,386	25,266	26,576	28,645	30,885

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash flow from operations	2,472	4,963	2,382	5,305	6,369
Capital expenditures	(1,213)	(1,012)	(2,500)	(2,500)	(2,000)
Change in investments	0	0	0	0	0
Other investing cash flows	0	3	0	0	0
Cash flow from investing	(1,213)	(1,009)	(2,500)	(2,500)	(2,000)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	222	(201)	(250)	(200)	(200)
Interest expenses	(195)	(107)	(97)	(72)	(52)
Dividends paid	(1,150)	(1,591)	(2,720)	(3,533)	(4,353)
Other financing cash flows	(310)	72	(26)	15	11
Cash flow from financing	(1,433)	(1,827)	(3,093)	(3,790)	(4,595)
Chg in cash & cash eq.	(174)	2,127	(3,211)	(985)	(225)
Closing cash & cash eq.	2,350	4,477	1,266	281	56

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	16.1	19.4	22.8	29.6	36.5
Adjusted EPS	16.1	19.4	22.8	29.6	36.5
Dividend per share	3.0	10.0	13.7	17.8	21.9
Book value per share	107.9	117.6	123.3	130.7	139.8

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	6.9	7.0	5.5	4.7	4.2
EV/EBITDA	46.7	38.0	32.1	25.4	21.2
Adjusted P/E	76.3	63.3	53.8	41.4	33.6
P/BV	11.4	10.4	9.9	9.4	8.8

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	81.7	74.6	73.3	73.3	73.3
Interest burden (PBT/EBIT)	101.5	102.6	102.6	102.8	102.8
EBIT margin (EBIT/Revenue)	11.0	14.5	13.7	15.2	16.4
Asset turnover (Rev./Avg TA)	116.7	112.0	135.4	148.6	157.4
Leverage (Avg TA/Avg Equity)	1.5	1.4	1.4	1.4	1.4
Adjusted ROAE	15.5	17.2	18.9	23.3	27.0

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	(5.0)	(1.0)	26.2	16.9	14.2
EBITDA	(7.5)	22.3	18.0	26.6	21.0
Adjusted EPS	10.3	20.6	17.7	29.9	23.2
Profitability & Return ratios (%)					
EBITDA margin	14.8	18.3	17.1	18.5	19.6
EBIT margin	11.0	14.5	13.7	15.2	16.4
Adjusted profit margin	9.1	11.1	10.3	11.5	12.4
Adjusted ROAE	15.5	17.2	18.9	23.3	27.0
ROCE	13.8	15.3	17.4	21.7	25.3
Working capital days (days)					
Receivables	57	54	50	51	52
Inventory	83	81	70	80	82
Payables	38	31	25	27	28
Ratios (x)					
Gross asset turnover	1.5	1.4	1.6	1.7	1.8
Current ratio	2.1	2.7	2.5	2.3	2.3
Net interest coverage ratio	15.8	37.5	49.7	86.8	147.9
Adjusted debt/equity	(0.1)	(0.2)	0.0	0.0	0.0

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

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

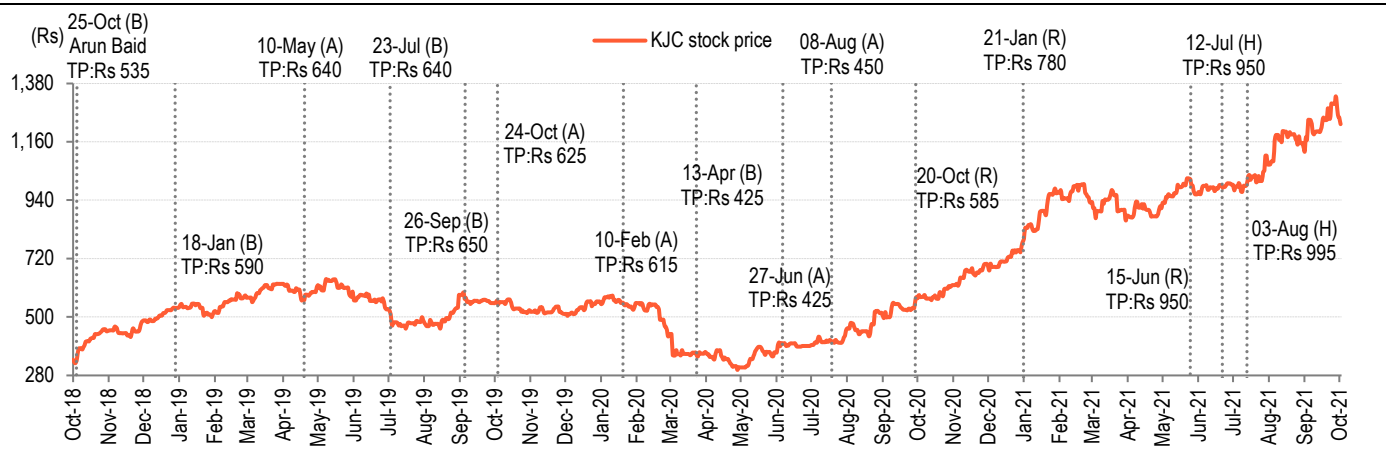
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): KAJARIA CERAMICS (KJC IN)



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

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