

BUY

TP: Rs 280 | ▲ 23%

SOMANY CERAMICS

Construction Materials

06 November 2020

Good operational performance; sharp balance sheet improvement

Somany Ceramics (SOMC) reported above-expected consolidated revenue of Rs 4.2bn (flat YoY) in Q2FY21, aided by a 3% uptick in tile volumes. Operating margins expanded 105bps YoY to 11.7%, fuelling 10%/55% YoY growth in EBITDA/PBT. Consolidated debt reduced by ~Rs 1.2bn in FY21 YTD. Management expects a better Q3 and further balance sheet improvement, leading us to reset our target P/E to 15x (from 12x). We raise FY21-FY23 EBITDA estimates by 10-26% and roll forward to a revised Dec'21 TP of Rs 280 (from Rs 160).

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Healthy volume growth: SOMC reported a flat consolidated topline in Q2, with revenue from the tiles segment increasing 1.4% YoY (volumes up 2.9%, realisations down 1.4%), whereas sanitaryware & allied revenue declined 8.6% YoY due to availability issues. Management indicated that demand during the quarter was driven by tier-2 cities and below. The company expects a better Q3 as all plants are now operating at 100% capacity and sanitaryware availability has normalised.

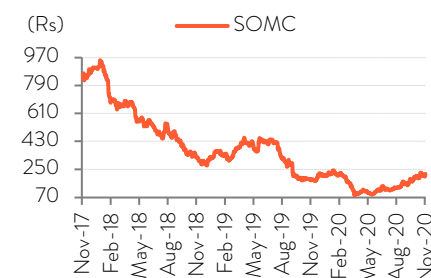
Operating margins expand: Though gross margins contracted 250bps YoY due to a weaker product mix, consolidated operating margins increased 105bps YoY to 11.7% due to lower employee/other expenses (-195bps/-160bps YoY). EBITDA/PBT for the quarter grew 10%/55% YoY. Management believes operating leverage would keep margins healthy despite some increase in gas cost.

Maintain BUY: SOMC has reduced consolidated debt by ~Rs 1.2bn YTD via better working capital control. We hike our FY21 PAT estimate four-fold (on a low base) and FY22/FY23 forecasts by ~30% each, accompanied by a reset in target one-year forward P/E multiple to 15x from 12x in light of the company's stronger balance sheet position. Maintain BUY as we roll forward to a revised Dec'21 TP of Rs 280.

Ticker/Price	SOMC IN/Rs 227
Market cap	US\$ 129.7mn
Shares o/s	42mn
3M ADV	US\$ 0.4mn
52wk high/low	Rs 253/Rs 77
Promoter/FPI/DII	55%/2%/44%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	17,110	16,030	15,093	17,862	20,025
EBITDA (Rs mn)	1,576	1,299	1,354	1,797	2,063
Adj. net profit (Rs mn)	490	220	311	636	836
Adj. EPS (Rs)	11.6	5.2	7.3	15.0	19.7
Adj. EPS growth (%)	(32.9)	(55.1)	41.5	104.3	31.4
Adj. ROAE (%)	8.2	3.6	5.0	9.6	11.4
Adj. P/E (x)	19.6	43.7	30.9	15.1	11.5
EV/EBITDA (x)	8.9	10.7	10.4	7.4	6.0

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)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
Net Revenue	4,239	4,223	0.4	1,694	150.2	5,933	8,178	(27.4)
CQGS	2,697	2,581	4.5	1,274	111.6	3,971	5,106	(22.2)
% of sales	63.6	61.1	250bps	75	(1,160bps)	66.9	62.4	450bps
Employee expenses	522	603	(13.3)	373	40.2	895	1,188	(24.6)
% of sales	12.3	14.3	(195bps)	22	(967bps)	15.1	14.5	56bps
Other Expenses	525	592	(11.2)	163	221.5	689	1,112	(38.1)
% of sales	12.4	14.0	(161bps)	10	275bps	11.6	13.6	(199bps)
EBITDA	494	448	10.4	(116)	(525.6)	378	773	(51.0)
EBITDA Margin	11.67	10.60	106bps	(6.86)	1,852bps	6.38	9.45	(307bps)
Depreciation/Amortisation	150	149	0.9	145	3.7	295	286	3.4
EBIT	344	299	15.2	(261)	(231.7)	83	487	(83.0)
EBIT Margin	8.1	7.1	104bps	(15.4)	2,353bps	1.4	6.0	(456bps)
Net Interest Expenses	98	132	(25.7)	115	(14.8)	214	255	(16.3)
Other Income	40	18	120.8	19	113.8	59	67	(10.8)
PBT	286	185	54.8	(358)	(180.1)	(71)	298	(123.9)
Tax Expenses	73	(165)	(144.3)	(94)	(178.1)	(21)	(123)	(83.3)
Net Income before minority interest & extraordinary items	213	350	(39.2)	(264)	(180.8)	(51)	422	(112.0)
Minority Interest and Income from associates	(8)	(24)	(66.8)	44	(118.0)	36	(21)	(272.6)
Exceptional items	(0)	(262)	(100.0)	0	NM	(0)	(262)	(100.0)
Reported Net Income	205	65	217.3	(220)	(193.2)	(15)	139	(110.7)
Adjusted PAT	205	243	(15.7)	(220)	(193.3)	(15)	509	(102.9)

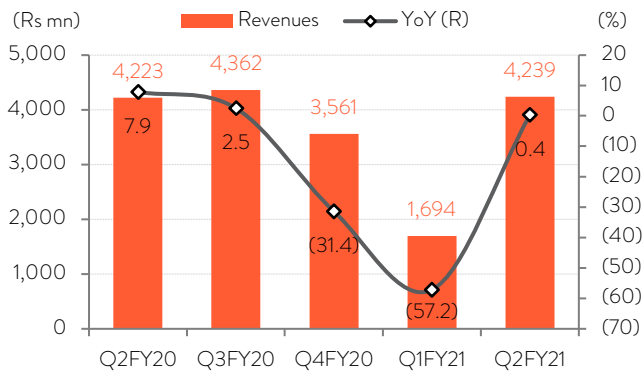
Source: Company, BOBCAPS Research

FIG 2 – STANDALONE QUARTERLY PERFORMANCE

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
Net Revenue	4,205	4,217	(0.3)	1,690	148.8	5,896	8,088	(27.1)
CQGS	3,067	3,032	1.2	1,359	125.7	4,426	5,813	(23.9)
% of sales	73	72	104bps	80	(748bps)	75	72	321bps
Employee expenses	359	436	(17.6)	293	22.4	652	869	(24.9)
% of sales	8.5	10.3	(179bps)	17.3	(881bps)	11.1	10.7	32bps
Other Expenses	407	470	(13.4)	138	195.5	545	897	(39.2)
% of sales	9.7	11.2	(147bps)	8.2	153bps	9.2	11.1	(184bps)
EBITDA	372	279	33.2	(100)	(472.4)	272	510	(46.6)
EBITDA Margin	8.85	6.62	222bps	(5.91)	1,476bps	4.62	6.30	(169bps)
Depreciation/Amortisation	108	109	(1.6)	103	4.9	210	206	1.8
EBIT	265	170	55.7	(202)	(230.7)	62	303	(79.5)
EBIT Margin	6.3	4.0	226bps	(12.0)	1,826bps	1.1	3.8	(270bps)
Net Interest Expenses	36	64	(44.5)	54	(34.5)	90	121	(25.7)
Other Income	42	29	41.6	27	53.1	69	89	(22.7)
PBT	271	135	100.1	(230)	(217.9)	41	271	(84.9)
Tax Expenses	69	(175)	(139.6)	(58)	(218.5)	11	(126)	(108.6)
Net Income before extraordinary items	201	310	(35.0)	(171)	(217.6)	30	397	(92.4)
Exceptional items	0	(262)	(100.0)	0	NM	0	(262)	(100.0)
Reported Net Income	201	48	319.6	(171)	(217.6)	30	135	(77.7)
Adjusted PAT	201	243	(17.2)	(171)	(217.6)	30	314	(90.4)

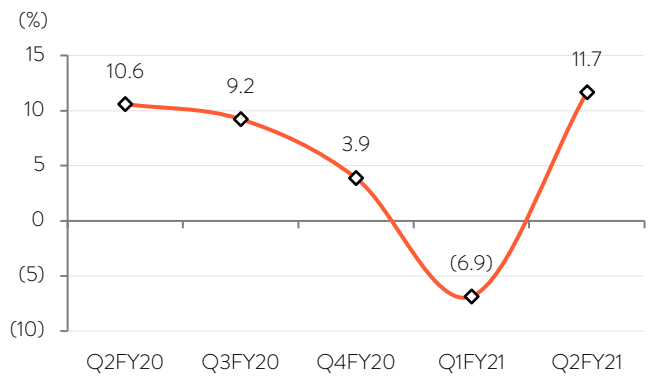
Source: Company, BOBCAPS Research

FIG 3 – CONSOLIDATED REVENUE GROWTH



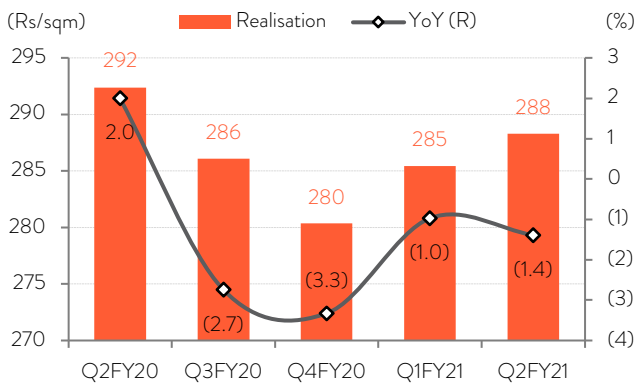
Source: Company, BOBCAPS Research

FIG 4 – CONSOLIDATED EBITDA MARGINS



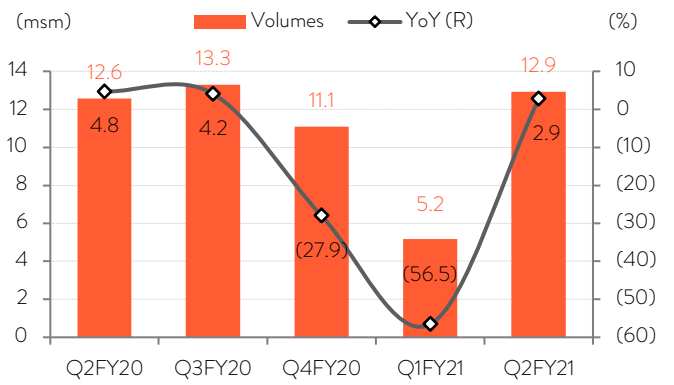
Source: Company, BOBCAPS Research

FIG 5 – TILE REALISATIONS



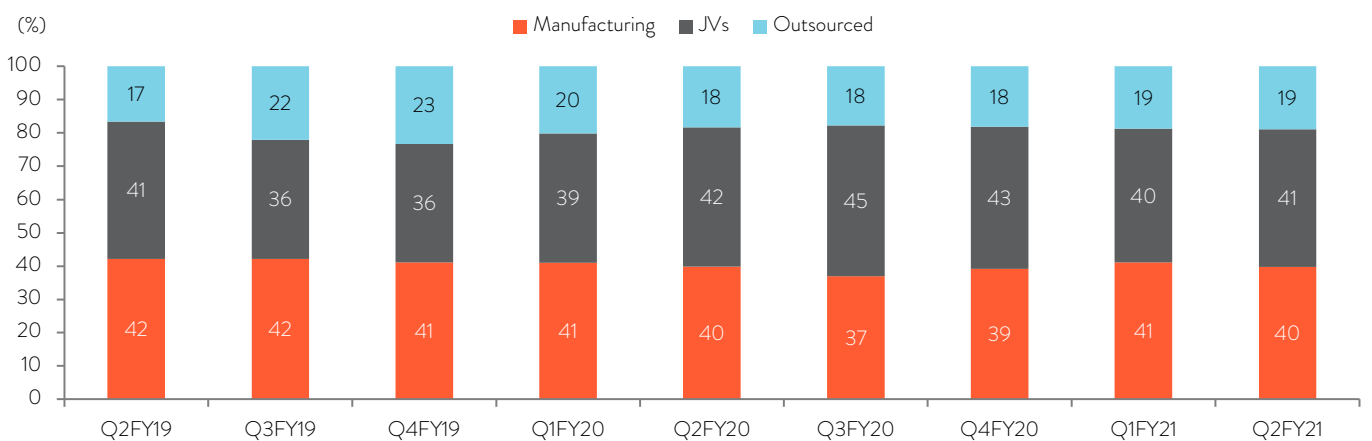
Source: Company, BOBCAPS Research

FIG 6 – TILE VOLUME GROWTH



Source: Company, BOBCAPS Research

FIG 7 – REVENUE BREAKUP



Source: Company, BOBCAPS Research

Earnings call highlights

- Demand for SOMC's products revived from August and continues to show improvement.
- Tier-2-and-below cities accounted for ~85% of revenues during the quarter (vs. 75% normally).
- Plant utilisation has now risen to 100% and thus the company expects a strong Q3 unless the pandemic worsens.
- Supply side-issues resulted in lower sanitaryware revenue in Q2. These issues have been ironed out and the company expects flattish Q3 sales (at least) in this segment.
- Gross margins in Q2 were affected by an adverse product mix. Management is hopeful of the mix normalising as bigger cities have now started to open up.
- Gas prices have increased marginally in Q3 but the company hopes to counter the impact via operating leverage as sales improve.
- Good cash collections and inventory reduction in H1 aided debt reduction of Rs 1.16bn YTD. Management reiterated its focus on further improving the balance sheet.
- Active dealers have risen to 1,500 in H1FY21 of a total of 2,200 dealers vs. 900 of a total of 1,900 in FY20. The company is planning net additions of 75-100 dealers every year going ahead.
- The top 350 dealers account for 60% of SOMC's sales and these are exclusive sellers of its products.
- Management believes that due to the pandemic, several dealers are shifting to organised players who can reliably supply material when required.
- Morbi exports remain robust which is aiding the sector. As per management, global players are looking to countries besides China as a secondary source of supply for tiles and India is a beneficiary of this.
- Exports are not a focus area for SOMC as they do not attract any brand premium. This segment would remain at 5-7% of the company's turnover.

Valuation methodology

SOMC is the third largest organised player in the Indian tiles market. We expect the company to be one of the prime beneficiaries of a shift in tiling demand from the unorganised segment (~50% of India's Rs 270bn tiles market) to the formal market given lower GST rates.

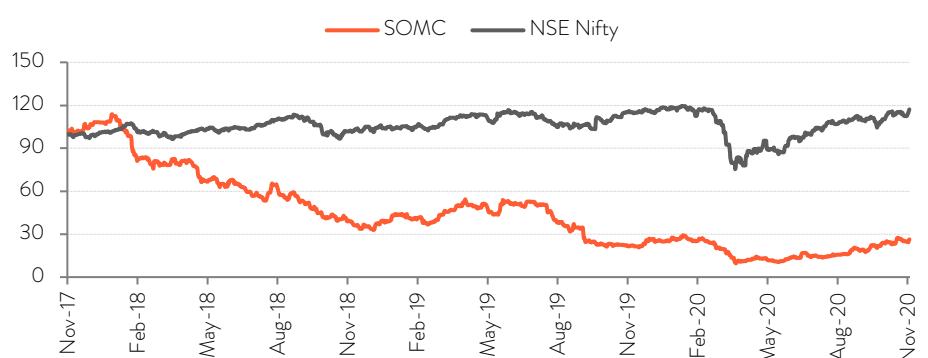
Factoring in the Q2FY21 performance, we raise FY21/FY22/FY23 EBITDA estimates by 26%/10%/11% and hike PAT forecasts 4x (on a low base)/31%/32%. We reinstate our target one-year forward P/E to pre-Covid levels of 15x (from 12x) given the stronger demand outlook and improving balance sheet. On rollover, we have a revised Dec'21 target price of Rs 280 (vs. Rs 160). Maintain BUY.

FIG 8 – REVISED ESTIMATES

(Rs mn)	New			Old			Change (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenues	15,093	17,862	20,025	13,859	16,485	18,396	8.9	8.4	8.9
EBITDA	1,354	1,797	2,063	1,073	1,638	1,864	26.2	9.7	10.7
PAT	311	636	836	71	485	632	338.5	31.2	32.2

Source: BOBCAPS Research

FIG 9 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Higher raw material prices:** Any abnormal increase in prices of key raw materials, such as gas, coupled with an inability to pass these along could adversely affect SOMC's profitability.
- **Increased competition from informal sector:** E-way bill implementation, if executed poorly as is currently the case, may allow competition from the unorganised sector to increase, thereby affecting growth prospects.
- **Housing market slowdown:** A slowdown in the housing market will hinder demand for the company's products.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	17,110	16,030	15,093	17,862	20,025
EBITDA	1,576	1,299	1,354	1,797	2,063
Depreciation	(443)	(589)	(613)	(632)	(663)
EBIT	1,134	709	741	1,165	1,400
Net interest income/(expenses)	(459)	(494)	(398)	(315)	(258)
Other income/(expenses)	149	125	102	100	105
EBT	824	339	445	950	1,248
Income taxes	(265)	112	(114)	(243)	(319)
Extraordinary items	(26)	(256)	0	0	0
Min. int./Inc. from associates	(69)	(45)	(20)	(71)	(93)
Reported net profit	463	150	311	636	836
Adjustments	26	70	0	0	0
Adjusted net profit	490	220	311	636	836

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	1,986	1,729	1,778	2,104	2,359
Other current liabilities	1,275	1,347	1,075	1,272	1,426
Provisions	59	98	75	89	100
Debt funds	5,731	4,981	3,400	2,900	2,250
Other liabilities	532	358	358	358	358
Equity capital	85	85	85	85	85
Reserves & surplus	6,045	5,980	6,264	6,874	7,675
Shareholders' fund	6,130	6,064	6,348	6,958	7,760
Total liabilities and equities	16,580	15,519	13,996	14,714	15,378
Cash and cash eq.	460	173	17	26	32
Accounts receivables	4,179	2,798	2,812	3,328	3,731
Inventories	2,545	3,282	2,481	2,789	3,127
Other current assets	1,366	1,085	910	1,077	1,207
Investments	683	341	400	400	400
Net fixed assets	7,048	7,726	7,264	6,982	6,768
CWIP	247	60	60	60	60
Intangible assets	52	52	52	52	52
Total assets	16,580	15,519	13,996	14,714	15,378

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	906	739	924	1,268	1,499
Interest expenses	459	494	398	315	258
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(174)	779	717	(454)	(451)
Other operating cash flows	(182)	(566)	20	71	93
Cash flow from operations	1,009	1,447	2,059	1,200	1,398
Capital expenditures	(1,028)	(664)	(150)	(350)	(450)
Change in investments	459	341	(59)	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(569)	(323)	(209)	(350)	(450)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	335	(750)	(1,581)	(500)	(650)
Interest expenses	(459)	(494)	(398)	(315)	(258)
Dividends paid	(138)	(204)	(47)	(97)	(127)
Other financing cash flows	96	38	20	71	93
Cash flow from financing	(167)	(1,411)	(2,007)	(841)	(942)
Changes in cash and cash eq.	274	(287)	(156)	9	6
Closing cash and cash eq.	460	173	17	26	32

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	10.9	3.5	7.3	15.0	19.7
Adjusted EPS	11.6	5.2	7.3	15.0	19.7
Dividend per share	2.0	2.0	1.0	2.0	2.6
Book value per share	144.6	143.1	149.8	164.2	183.1

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	0.8	0.9	0.9	0.7	0.6
EV/EBITDA	8.9	10.7	10.4	7.4	6.0
Adjusted P/E	19.6	43.7	30.9	15.1	11.5
P/BV	1.6	1.6	1.5	1.4	1.2

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	59.5	64.8	69.9	67.0	67.0
Interest burden (PBT/EBIT)	72.7	47.9	60.1	81.5	89.1
EBIT margin (EBIT/Revenue)	6.6	4.4	4.9	6.5	7.0
Asset turnover (Revenue/Avg TA)	103.8	99.9	102.3	124.4	133.1
Leverage (Avg TA/Avg Equity)	2.8	2.6	2.4	2.2	2.0
Adjusted ROAE	8.2	3.6	5.0	9.6	11.4

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	(0.1)	(6.3)	(5.8)	18.3	12.1
EBITDA	(16.0)	(17.6)	4.3	32.7	14.8
Adjusted EPS	(32.9)	(55.1)	41.5	104.3	31.4
Profitability & Return ratios (%)					
EBITDA margin	9.2	8.1	9.0	10.1	10.3
EBIT margin	6.6	4.4	4.9	6.5	7.0
Adjusted profit margin	2.9	1.4	2.1	3.6	4.2
Adjusted ROAE	8.2	3.6	5.0	9.6	11.4
ROCE	6.2	5.7	4.9	8.0	9.5
Working capital days (days)					
Receivables	98	79	68	63	64
Inventory	86	105	111	86	86
Payables	51	46	47	44	45
Ratios (x)					
Gross asset turnover	2.3	1.9	1.6	1.9	2.0
Current ratio	1.2	1.2	1.3	1.4	1.6
Net interest coverage ratio	2.5	1.4	1.9	3.7	5.4
Adjusted debt/equity	0.9	0.8	0.5	0.4	0.3

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

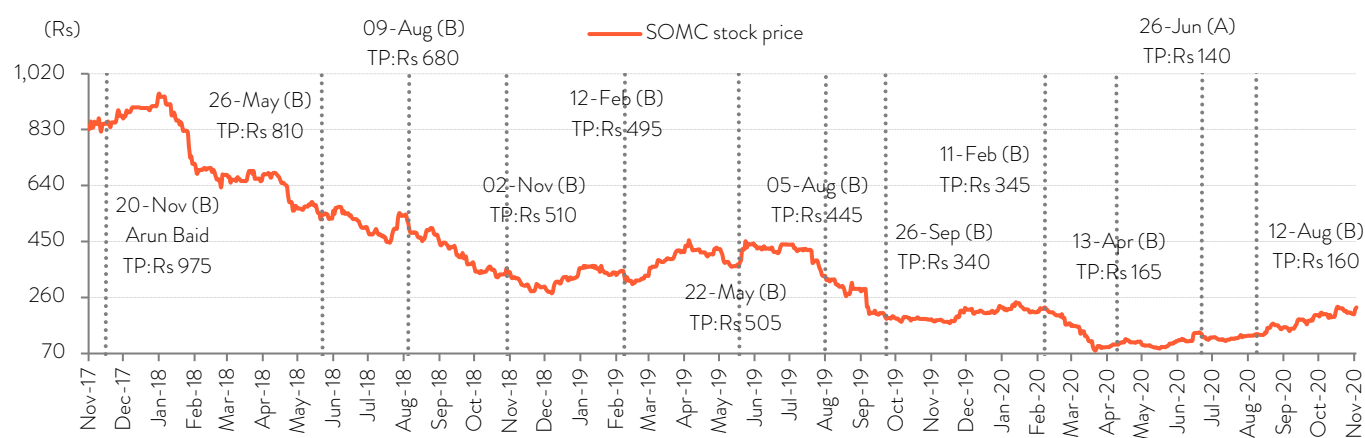
ADD – Expected return from >+5% to +15%

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)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): SOMANY CERAMICS (SOMC IN)



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

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