

BUY

TP: Rs 345 | ▲ 55%

SOMANY CERAMICS

Construction Materials

11 February 2020

Revenues in line, margins lower

Somany Ceramics (SOMC) reported in-line consolidated revenue growth of 2.5% YoY to Rs 4.4bn in Q3FY20, aided by a 4% uptick in tile volumes.

Consolidated operating margins expanded 100bps YoY to 9.2%, lower than estimates, with EBITDA rising 15% YoY. Management has guided for high single-digit or low double-digit growth in FY21 with improving margins. We cut FY20-FY22 PAT estimates by 4-7% and roll forward to a revised Mar'21 TP of Rs 345 (earlier Rs 340).

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Modest volume growth: SOMC reported 2.5% YoY consolidated topline growth, with revenue from the tiles segment increasing 1.3% (volumes up 4.2%, realisations down 2.7%) and sanitaryware & allied revenue rising ~5.7% YoY. Volumes were affected by the continued weak demand conditions and tight working capital discipline. Management expects the tiles segment to post volume growth in high single-digits/low double-digits in FY21. The company reiterated its continued focus on working capital discipline despite the tough market.

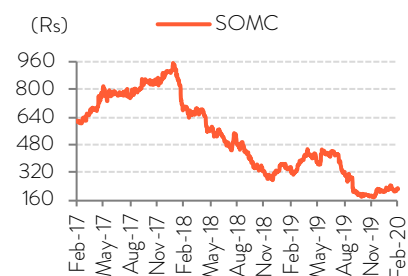
Operating margins increase: Despite a 40bps dip in gross margin, consolidated operating margins increased 100bps YoY (-135 bps QoQ) to 9.2% due to lower other expenses (-145bps YoY), aiding EBITDA growth of 15% YoY. Gross margins declined due to pricing pressure on PVT/GVT and a change in product mix. Management has indicated that operating margins should improve in FY21 over FY20 as capacity utilisation increases.

Maintain BUY: We trim FY20-FY22 EPS estimates by 4-7% due to continued tepid market conditions. Maintain BUY and roll forward to a Mar'21 TP of Rs 345 (earlier Rs 340), set at an unchanged P/E of 15x.

Ticker/Price	SOMC IN/Rs 223
Market cap	US\$ 132.5mn
Shares o/s	42mn
3M ADV	US\$ 0.3mn
52wk high/low	Rs 472/Rs 170
Promoter/FPI/DII	51%/3%/46%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	17,119	17,110	18,022	19,847	21,989
EBITDA (Rs mn)	1,878	1,576	1,847	2,064	2,298
Adj. net profit (Rs mn)	730	490	625	808	983
Adj. EPS (Rs)	17.2	11.6	14.7	19.1	23.2
Adj. EPS growth (%)	(24.7)	(32.9)	27.6	29.3	21.6
Adj. ROAE (%)	13.2	8.2	9.9	11.7	12.7
Adj. P/E (x)	13.0	19.3	15.1	11.7	9.6
EV/EBITDA (x)	6.6	8.8	7.5	6.6	5.6

Source: Company, BOBCAPS Research

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FIG 1 – STANDALONE QUARTERLY PERFORMANCE

(Rs mn)	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)	9MFY20	9MFY19	YoY (%)
Net Revenue	4,340	4,256	2.0	4,217	2.9	12,428	11,805	5.3
CQGS	3,233	3,059	5.7	3,032	6.6	9,047	8,490	6.6
% of sales	75	72	263bps	72	261bps	73	72	88bps
Employee expenses	414	417	(0.7)	429	(3.4)	1,270	1,258	0.9
% of sales	9.5	9.8	(25bps)	10.2	(63bps)	10.2	10.7	(44bps)
Other Expenses	464	540	(14.0)	477	(2.7)	1,374	1,438	(4.4)
% of sales	10.7	12.7	(199bps)	11.3	(62bps)	11.1	12.2	(112bps)
EBITDA	228	240	(4.9)	279	(18.4)	738	620	19.0
EBITDA Margin	5.3	5.6	(38bps)	6.62	(137bps)	5.9	5.3	68bps
Depreciation/Amortisation	103	79	30.2	109	(6.2)	309	231	33.7
EBIT	125	161	(22.1)	170	(26.2)	429	389	10.3
EBIT Margin	2.9	3.8	(89bps)	4.0	(114bps)	3.5	3.3	16bps
Net Interest Expenses	50	66	(23.8)	64	(21.3)	171	192	(11.0)
Other Income	42	53	(22.0)	29	42.0	130	156	(16.6)
PBT	117	148	(21.3)	135	(13.8)	388	353	9.9
Tax Expenses	17	66	(73.4)	(175)	(110.0)	(108)	141	(177.1)
Net Income before extraordinary items	99	83	20.0	310	(68.0)	496	212	133.8
Exceptional items	(12)	53	(122.9)	(262)	(95.3)	(274)	53	(615.0)
Reported Net Income	87	136	(36.0)	48	81.3	222	266	(16.2)
Adjusted PAT	97	106	(8.3)	216	(54.9)	573	233	145.4

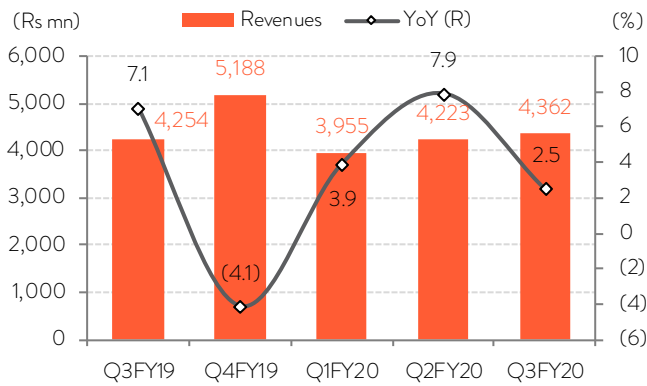
Source: Company, BOBCAPS Research

FIG 2 – CONSOLIDATED QUARTERLY PERFORMANCE

(Rs mn)	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)	9MFY20	9MFY19	YoY (%)
Net Revenue	4,362	4,254	2.5	4,223	3.3	12,540	11,962	4.8
CQGS	2,808	2,722	3.2	2,581	8.8	7,914	7,563	4.6
% of sales	64.4	64.0	39bps	61	325bps	63.1	63.2	(12bps)
Employee expenses	577	560	3.1	596	(3.1)	1,752	1,719	1.9
% of sales	13.2	13.2	8bps	14	(87bps)	14.0	14.4	(40bps)
Other Expenses	575	622	(7.7)	598	(4.0)	1,700	1,752	(3.0)
% of sales	13.2	14.6	(146bps)	14	(100bps)	13.6	14.6	(109bps)
EBITDA	403	350	14.9	448	(10.1)	1,175	929	26.5
EBITDA Margin	9.2	8.2	99bps	10.6	(137bps)	9.4	7.8	161bps
Depreciation/Amortisation	143	110	29.5	149	(4.3)	428	328	30.6
EBIT	260	240	8.2	299	(13.0)	747	601	24.3
EBIT Margin	6.0	5.6	31bps	7.1	(112bps)	6.0	5.0	93bps
Net Interest Expenses	124	115	7.9	132	(6.0)	379	343	10.7
Other Income	31	45	(30.7)	18	68.9	97	136	(28.1)
PBT	167	170	(1.8)	185	(9.9)	465	394	18.1
Tax Expenses	29	73	(60.1)	(165)	(117.5)	(94)	155	(160.9)
Net Income before minority interest & extraordinary items	138	97	41.7	350	(60.7)	559	239	133.8
Minority Interest and Income from associates	(21)	(10)	114.3	(24)	(11.8)	(42)	(21)	98.1
Exceptional items	(13)	4	(390.7)	(262)	(95.2)	(274)	4	(6479.1)
Reported Net Income	104	92	13.6	65	61.3	243	222	9.4
Adjusted PAT	112	89	26.2	229	(51.1)	573	220	160.7

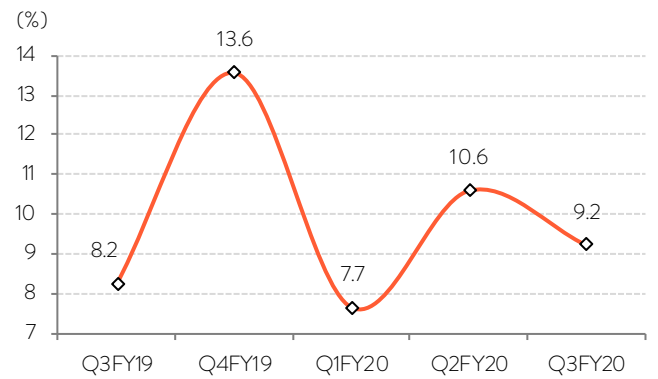
Source: Company, BOBCAPS Research

FIG 3 – CONSOLIDATED REVENUE GROWTH



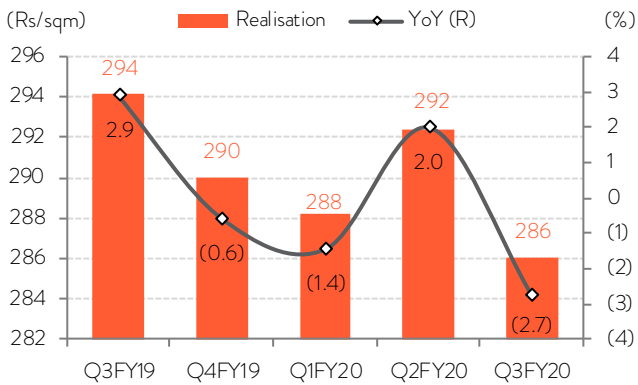
Source: Company, BOBCAPS Research

FIG 4 – CONSOLIDATED EBITDA MARGINS



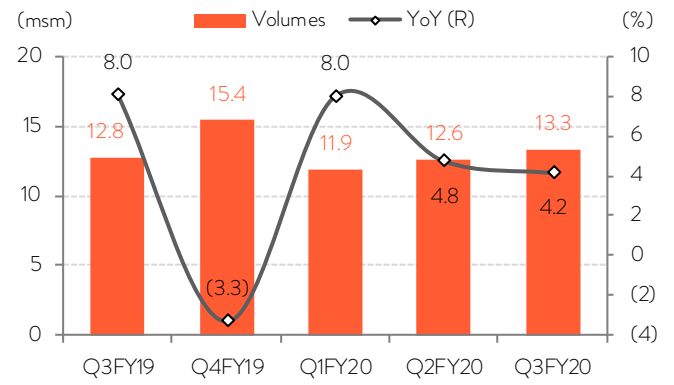
Source: Company, BOBCAPS Research

FIG 5 – TILE REALISATIONS



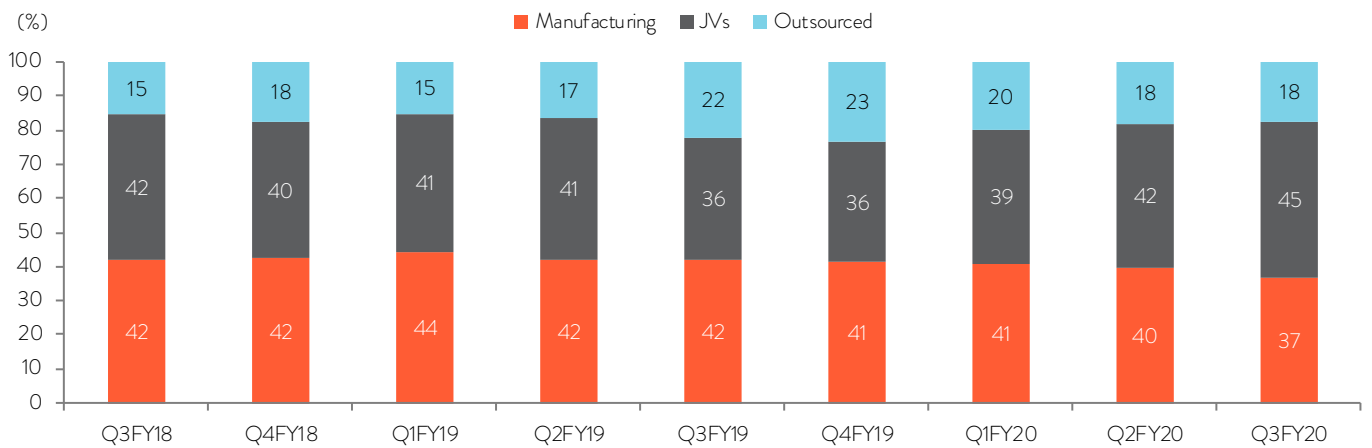
Source: Company, BOBCAPS Research

FIG 6 – TILE VOLUME GROWTH



Source: Company, BOBCAPS Research

FIG 7 – REVENUE BREAKUP



Source: Company, BOBCAPS Research

Earnings call highlights

- Soft demand conditions and the ban on construction activity in the NCR due to pollution adversely affected Q3FY20 sales.
- SOMC estimates that the tile industry declined by 5-10% in Q3 and expects demand to revive only post Diwali.
- GVT/PVT tile prices corrected during the quarter which affected profitability.
- GVT sales proportion in tiles increased by 2ppt YoY to 23% in Q3 due to commissioning of the South India plant.
- The company's average capacity utilisation stood at 77% in Q3 due to the slow market.
- Better utilisation of the South India plant and the newly refurbished Kadi (Gujarat) unit would aid high-single-digit/low-double-digit volume growth in tiles, as per management.
- SOMC expects to have consolidated margins of 11-12% at ~85% utilisation.
- Sanitaryware earns operating margins of 14-14.5% even now whereas the faucetware segment has 8-9% margins.
- Management has guided for sanitaryware segment revenue growth of ~20% in FY21.
- Average gas price for the quarter was ~Rs 31/scm; management expects some increase in Q4. Gas prices for the company will fall with a lag in Q1FY21 as it has three-month rolling pricing.
- Exports from the Morbi plant to GCC countries improved in December-January before India imposed anti-dumping duty. SOMC does not have a significant presence in exports.
- The company added ~100 net dealers in 9MFY20 and aims to add 150 more every year going ahead.
- SOMC has no significant capex plans for the next 18 months and has guided for Rs 350mn-400mn of outlay in FY21.
- The company has decided to use cash flows primarily for repayment of debt going ahead and will not undertake treasury operations.

Valuation methodology

SOMC is the third largest organised player in the Indian tiles market with ~15% organised market share. 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 post lower GST rates.

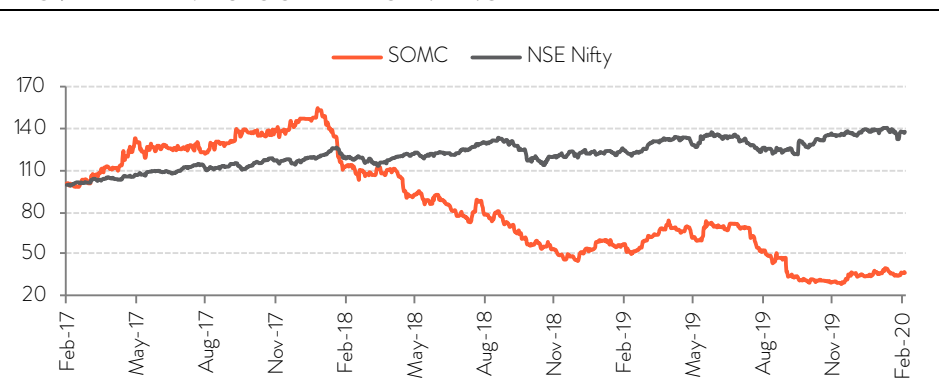
We cut FY20-FY22 PAT estimates by 4-7% due to continued slow market conditions. Maintain BUY as we roll forward to a revised Mar'21 target price of Rs 345 (earlier Rs 340), set at 15x one-year forward P/E. The stock is trading at a cheap 9.6x FY22E EPS and valuations could remain subdued pending better internal controls and usage of free cash flows for debt reduction. Maintain BUY.

FIG 8 – REVISED ESTIMATES

(Rs mn)	New			Old			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenues	18,022	19,847	21,989	18,195	20,313	22,653	(1.0)	(2.3)	(2.9)
EBITDA	1,847	2,064	2,298	1,865	2,133	2,390	(1.0)	(3.2)	(3.9)
PAT	625	808	983	649	870	1,060	(3.7)	(7.1)	(7.3)

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 continued to be executed poorly, may allow competition from the unorganised sector to increase, thereby affecting the company's 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)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue	17,119	17,110	18,022	19,847	21,989
EBITDA	1,878	1,576	1,847	2,064	2,298
Depreciation	(413)	(443)	(569)	(603)	(640)
EBIT	1,465	1,134	1,278	1,461	1,658
Net interest income/(expenses)	(399)	(459)	(501)	(406)	(352)
Other income/(expenses)	143	149	151	152	154
Exceptional items	0	0	0	0	0
EBT	1,209	824	927	1,207	1,460
Income taxes	(393)	(265)	(237)	(309)	(374)
Extraordinary items	(10)	(26)	(195)	0	0
Min. int./Inc. from associates	(87)	(69)	(65)	(90)	(104)
Reported net profit	720	463	430	808	983
Adjustments	10	26	195	0	0
Adjusted net profit	730	490	625	808	983

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	2,332	1,986	2,123	2,338	2,591
Other current liabilities	1,258	1,275	1,284	1,414	1,566
Provisions	116	59	90	99	110
Debt funds	5,396	5,731	4,600	3,950	3,300
Other liabilities	524	532	532	532	532
Equity capital	85	85	85	85	85
Reserves & surplus	5,722	6,045	6,431	7,206	8,143
Shareholders' fund	5,807	6,130	6,516	7,291	8,228
Total liabilities and equities	16,391	16,580	16,076	16,646	17,452
Cash and cash eq.	187	460	149	175	248
Accounts receivables	5,037	4,179	4,691	5,111	5,603
Inventories	2,597	2,545	2,568	2,773	3,072
Other current assets	667	1,366	691	761	843
Investments	1,142	683	800	800	800
Net fixed assets	6,429	7,048	6,879	6,726	6,586
CWIP	279	247	247	247	247
Intangible assets	52	52	52	52	52
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	16,391	16,580	16,076	16,646	17,452

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	1,133	906	1,000	1,411	1,623
Interest expenses	399	459	501	406	352
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(413)	(174)	318	(342)	(457)
Other operating cash flows	48	(182)	(130)	90	104
Cash flow from operations	1,167	1,009	1,689	1,565	1,620
Capital expenditures	(1,337)	(1,028)	(400)	(450)	(500)
Change in investments	44	459	(117)	0	0
Other investing cash flows	0	0	195	0	0
Cash flow from investing	(1,294)	(569)	(323)	(450)	(500)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	427	335	(1,131)	(650)	(650)
Interest expenses	(399)	(459)	(501)	(406)	(352)
Dividends paid	(134)	(138)	(110)	(123)	(150)
Other financing cash flows	106	96	65	90	104
Cash flow from financing	(1)	(167)	(1,677)	(1,089)	(1,048)
Changes in cash and cash eq.	(128)	274	(311)	26	73
Closing cash and cash eq.	187	460	149	175	248

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	17.0	10.9	10.2	19.1	23.2
Adjusted EPS	17.2	11.6	14.7	19.1	23.2
Dividend per share	2.7	2.0	2.2	2.5	3.0
Book value per share	137.0	144.6	153.7	172.0	194.1

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	0.7	0.8	0.8	0.7	0.6
EV/EBITDA	6.6	8.8	7.5	6.6	5.6
Adjusted P/E	13.0	19.3	15.1	11.7	9.6
P/BV	1.6	1.5	1.5	1.3	1.1

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	60.3	59.5	67.4	66.9	67.3
Interest burden (PBT/EBIT)	82.5	72.7	72.6	82.6	88.1
EBIT margin (EBIT/Revenue)	8.6	6.6	7.1	7.4	7.5
Asset turnover (Revenue/Avg TA)	111.1	103.8	110.4	121.3	129.0
Leverage (Avg TA/Avg Equity)	2.8	2.8	2.6	2.4	2.2
Adjusted ROAE	13.2	8.2	9.9	11.7	12.7

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

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
YoY growth (%)					
Revenue	(1.1)	(0.1)	5.3	10.1	10.8
EBITDA	(20.1)	(16.0)	17.2	11.7	11.3
Adjusted EPS	(24.7)	(32.9)	27.6	29.3	21.6
Profitability & Return ratios (%)					
EBITDA margin	11.0	9.2	10.3	10.4	10.5
EBIT margin	8.6	6.6	7.1	7.4	7.5
Adjusted profit margin	4.3	2.9	3.5	4.1	4.5
Adjusted ROAE	13.2	8.2	9.9	11.7	12.7
ROCE	8.5	6.2	7.7	8.9	9.9
Working capital days (days)					
Receivables	99	98	90	90	89
Inventory	83	86	83	78	78
Payables	48	51	46	46	46
Ratios (x)					
Gross asset turnover	2.7	2.3	2.2	2.3	2.4
Current ratio	1.1	1.2	1.3	1.4	1.6
Net interest coverage ratio	3.7	2.5	2.6	3.6	4.7
Adjusted debt/equity	0.9	0.9	0.7	0.5	0.4

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

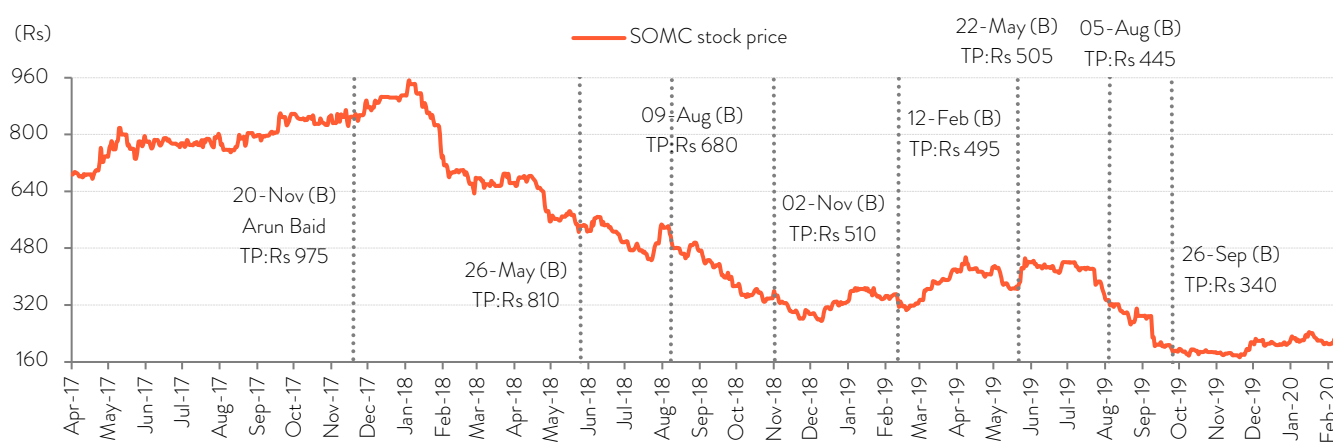
ADD – Expected return from >+5% to +15%

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: SOMANY CERAMICS (SOMC IN)



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

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