

**ADD**

TP: Rs 140 | ▲ 11%

**SOMANY CERAMICS**

Construction Materials

26 June 2020

## Disappointing performance – downgrade to ADD

**Somany Ceramics (SOMC) reported a dull Q4FY20 as consolidated revenue contracted 31% YoY to Rs 3.6bn, with tile volumes down 28% YoY. Consolidated operating margins shrank 970bps YoY to 3.9%, lower than estimates, and EBITDA slumped 80% YoY. Management did not provide any guidance for FY21 due to Covid-19 but indicated a possible 20-25% topline decline, despite which it expects to be profitable. We cut FY21-FY22 PAT estimates by 96%/18% and revise our Mar'21 TP to Rs 140 (vs. Rs 165). Downgrade from BUY to ADD.**

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**Sharp volume decline:** SOMC's consolidated topline decreased 31% YoY, with tiles segment revenue slipping 30% (volumes/realisations down 28%/3% YoY) and sanitaryware & allied revenue dropping 40% YoY. Management believes that but for sales losses incurred due to the lockdown in the second-half of March – historically a busy period – SOMC would have grown at 4.5-5% in Q4. FY21 revenue could decline 20-25%, per management, but a reworking of the cost structure should shield profitability. Post lockdown, sales in May returned to 45-50% of normal levels, rising to 55-60% in June.

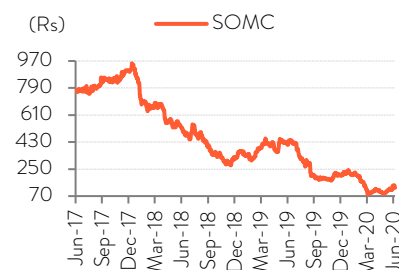
**Operating margins shrink:** SOMC's operating margins contracted 970bps YoY to 3.9% as gross margin declined 235bps, while other expenses/employee expense increased by 525bps/685bps due to negative operating leverage. This led to EBITDA slumping 80% YoY and a PBT loss of Rs 108mn.

**Downgrade to ADD:** SOMC's results has been lower than estimated and the demand outlook is far worse than earlier modelled. We thus scale back FY21-FY22 PAT estimates by 96%/18% and downgrade the stock from BUY to ADD – our revised Mar'21 TP of Rs 140 (earlier Rs 165) is set at an unchanged FY22E P/E multiple of 12x.

Ticker/Price	SOMC IN/Rs 126
Market cap	US\$ 70.4mn
Shares o/s	42mn
3M ADV	US\$ 0.2mn
52wk high/low	Rs 454/Rs 77
Promoter/FPI/DII	51%/2%/46%

Source: NSE

## STOCK PERFORMANCE



Source: NSE

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
Total revenue (Rs mn)	17,119	17,110	16,101	13,107	16,483
EBITDA (Rs mn)	1,878	1,576	1,314	994	1,638
Adj. net profit (Rs mn)	730	490	234	12	485
Adj. EPS (Rs)	17.2	11.6	5.5	0.3	11.4
Adj. EPS growth (%)	(24.7)	(32.9)	(52.2)	(95.0)	4027.3
Adj. ROAE (%)	13.2	8.2	3.8	0.2	7.7
Adj. P/E (x)	7.3	10.9	22.7	453.4	11.0
EV/EBITDA (x)	4.4	6.1	7.3	9.9	5.8

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 – CONSOLIDATED QUARTERLY PERFORMANCE**

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
<b>Net Revenue</b>	<b>3,561</b>	<b>5,188</b>	<b>(31.4)</b>	<b>4,362</b>	<b>(18.4)</b>	<b>16,101</b>	<b>17,151</b>	<b>(6.1)</b>
CQGS	2,219	3,355	(33.9)	2,808	(21.0)	10,132	10,918	(7.2)
% of sales	62.3	64.7	(235bps)	64	(206bps)	62.9	63.7	(73bps)
Employee expenses	619	546	13.2	577	7.2	2,391	2,275	5.1
% of sales	17.4	10.5	684bps	13	414bps	14.8	13.3	158bps
Other Expenses	585	581	0.7	575	1.8	2,264	2,312	(2.0)
% of sales	16.4	11.2	523bps	13	325bps	14.1	13.5	59bps
<b>EBITDA</b>	<b>139</b>	<b>707</b>	<b>(80.4)</b>	<b>403</b>	<b>(65.6)</b>	<b>1,314</b>	<b>1,645</b>	<b>(20.2)</b>
EBITDA Margin	3.9	13.6	(973bps)	9.2	(534bps)	8.2	9.6	(143bps)
Depreciation/Amortisation	161	115	40.8	143	13.0	590	443	33.2
<b>EBIT</b>	<b>(23)</b>	<b>592</b>	<b>(103.8)</b>	<b>260</b>	<b>(108.7)</b>	<b>724</b>	<b>1,203</b>	<b>(39.8)</b>
EBIT Margin	(0.6)	11.4	(1205bps)	6.0	(659bps)	4.5	7.0	(252bps)
Net Interest Expenses	115	117	(1.5)	124	(7.5)	494	459	7.6
Other Income	30	54	(44.6)	31	(2.9)	127	180	(29.1)
<b>PBT</b>	<b>(108)</b>	<b>530</b>	<b>NA</b>	<b>167</b>	<b>NA</b>	<b>358</b>	<b>923</b>	<b>(61.3)</b>
Tax Expenses	(17)	110	NA	29	(160.2)	(99)	265	(137.5)
<b>Net Income before minority interest &amp; extraordinary items</b>	<b>(90)</b>	<b>420</b>	<b>NA</b>	<b>138</b>	<b>NA</b>	<b>457</b>	<b>659</b>	<b>(30.7)</b>
Minority Interest and Income from associates	(3)	(48)	(93.4)	(21)	(84.8)	(45)	(69)	(35.2)
Exceptional items	0	(131)	(100.1)	(13)	(100.8)	(262)	(126)	107.4
<b>Reported Net Income</b>	<b>(93)</b>	<b>241</b>	<b>NA</b>	<b>104</b>	<b>NA</b>	<b>150</b>	<b>463</b>	<b>(67.6)</b>

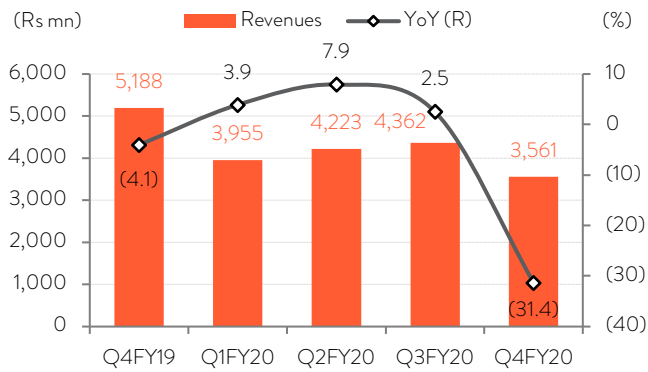
Source: Company, BOBCAPS Research

**FIG 2 – STANDALONE QUARTERLY PERFORMANCE**

Standalone Result Summary (Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
<b>Net Revenue</b>	<b>3,525</b>	<b>5,150</b>	<b>(31.6)</b>	<b>4,340</b>	<b>(18.8)</b>	<b>15,953</b>	<b>16,956</b>	<b>(5.9)</b>
CQGS	2,604	3,733	(30.3)	3,233	(19.5)	11,650	12,223	(4.7)
% of sales	74	72	137bps	75	(65bps)	73	72	94bps
Employee expenses	442	404	9.5	414	6.8	1,732	1,659	4.4
% of sales	12.5	7.8	470bps	9.5	300bps	10.9	9.8	107bps
Other Expenses	472	496	(4.8)	464	1.7	1,826	1,939	(5.8)
% of sales	13.4	9.6	376bps	10.7	269bps	11.4	11.4	1bps
<b>EBITDA</b>	<b>7</b>	<b>517</b>	<b>(98.6)</b>	<b>228</b>	<b>(96.8)</b>	<b>745</b>	<b>1,135</b>	<b>(34.4)</b>
EBITDA Margin	0.2	10.0	(983bps)	5.3	(504bps)	4.7	6.7	(202bps)
Depreciation/Amortisation	116	79	46.1	103	12.8	424	310	36.9
<b>EBIT</b>	<b>(108)</b>	<b>438</b>	<b>(124.7)</b>	<b>125</b>	<b>(186.3)</b>	<b>321</b>	<b>825</b>	<b>(61.1)</b>
EBIT Margin	(3.1)	8.5	(1,158bps)	2.9	(596bps)	2.0	4.9	(286bps)
Net Interest Expenses	47	69	(31.8)	50	(6.9)	218	261	(16.5)
Other Income	41	71	(42.5)	42	(2.4)	171	229	(25.3)
<b>PBT</b>	<b>(115)</b>	<b>440</b>	<b>(126.0)</b>	<b>117</b>	<b>(198.2)</b>	<b>273</b>	<b>793</b>	<b>(65.5)</b>
Tax Expenses	(25)	112	(122.1)	17	(242.0)	(133)	252	(152.7)
Net Income before extraordinary items	(90)	328	(127.4)	99	(190.5)	407	540	(24.8)
Exceptional items	0	(130)	(100.0)	(12)	(100.0)	(274)	(77)	254.9
<b>Reported Net Income</b>	<b>(90)</b>	<b>198</b>	<b>(145.4)</b>	<b>87</b>	<b>(203.2)</b>	<b>133</b>	<b>463</b>	<b>(71.4)</b>

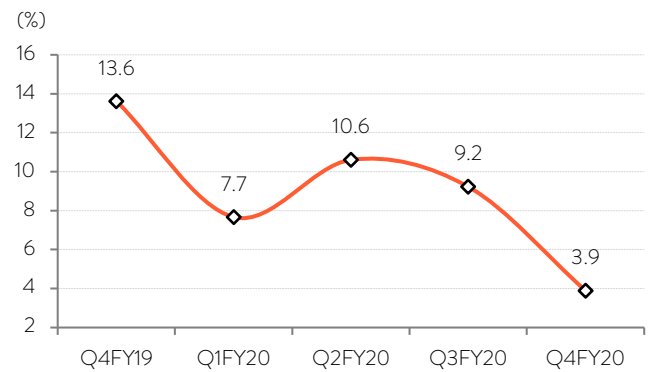
Source: Company, BOBCAPS Research

**FIG 3 – CONSOLIDATED REVENUE GROWTH**



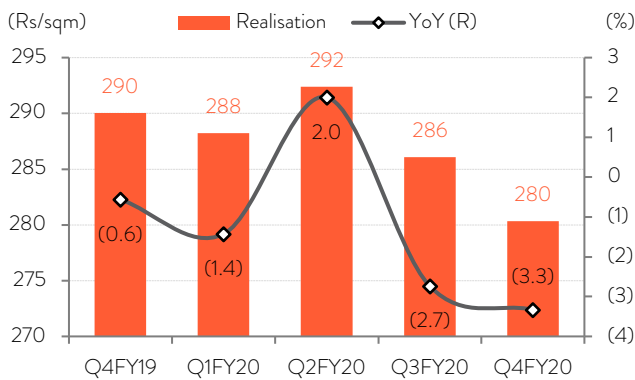
Source: Company, BOBCAPS Research

**FIG 4 – CONSOLIDATED EBITDA MARGINS**



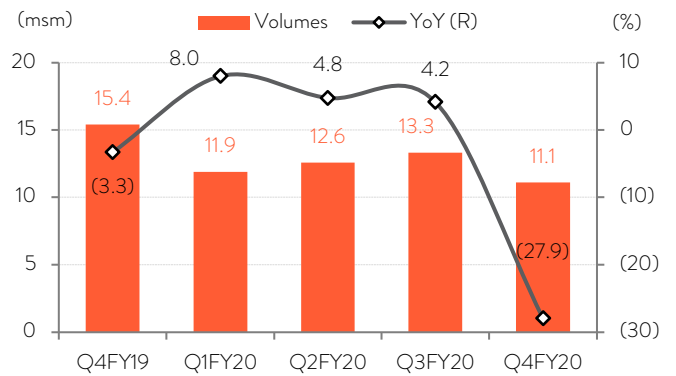
Source: Company, BOBCAPS Research

**FIG 5 – TILE REALISATIONS**



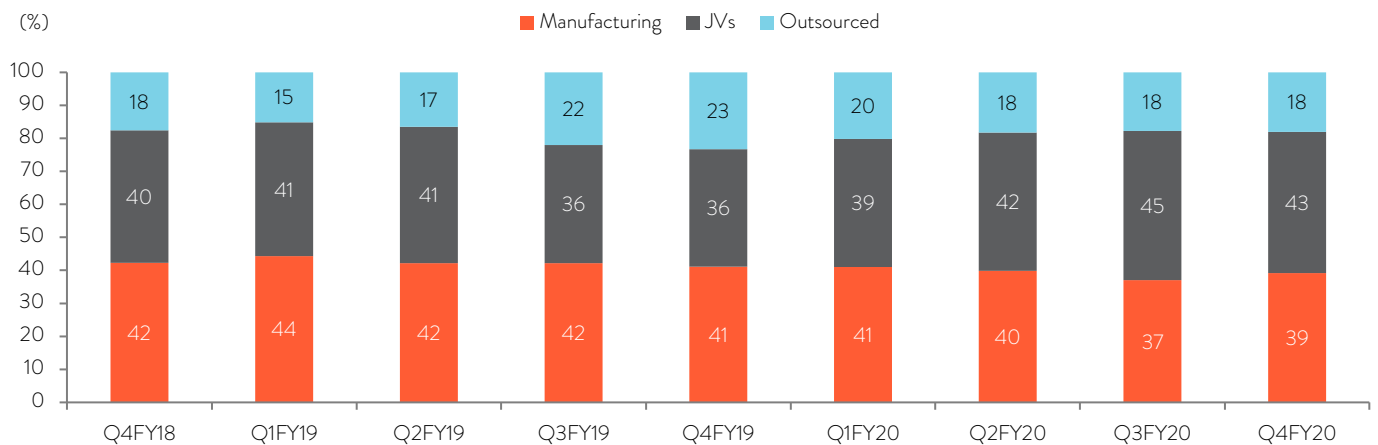
Source: Company, BOBCAPS Research

**FIG 6 – TILE VOLUME GROWTH**



Source: Company, BOBCAPS Research

**FIG 7 – REVENUE BREAKUP**



Source: Company, BOBCAPS Research

## Earnings call highlights

- Management estimates growth in the absence of the lockdown at 4.5-5% YoY for the quarter, ending FY20 with revenues of Rs 17.9bn-18bn in a normal situation.
- Revenue loss was substantial in Q4 as SOMC normally derives a bulk of its revenues in the last two weeks of any month/quarter, which coincided with the shutdown in late-March.
- While no guidance was proffered for FY21 due to Covid-19 volatility, SOMC alluded to a possible 20-25% topline decline, despite which it expects to be profitable. Management expects a demand pickup from H2FY21.
- The company has gradually restarted all its plants post lockdown and plans to ramp them up further in Q2FY21.
- Collections have improved substantially post easing of the lockdown.
- Channel inventory is low as stock filling which typically happens in end-March did not occur this year.
- Management stated that the focus on receivables continues and working capital discipline will not be sacrificed at the altar of sales.
- Gas prices have come down due to the correction in crude, which should benefit SOMC in the coming quarter.
- SOMC estimates that of the 900 unorganised ceramic tile factories in Morbi (Gujarat), ~100 will not resume operations due to liquidity issues post lockdown.
- Despite the GCC anti-dumping duty on Indian companies, SOMC believes exports of ceramic tiles would continue. GVT tile exports may become unviable but the industry is accessing new growth markets such as the US.
- A&P spend in FY20 stood at Rs 600mn.
- A total of ~130 new dealers were added in FY20.
- No material capex is planned for FY21 and only maintenance capex will be incurred.
- In FY20, SOMC received Rs 200mn of the outstanding ICDs of Rs 350mn. The balance is expected over the next 12-15 months.
- The company has taken an enabling resolution to raise NCDs because the new SEBI rules require a large corporate to raise 25% of long-term borrowings from this route. There are no plans to conduct this issue as of now.

## 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.

That said, SOMC's disappointing Q4FY20 results and strong demand headwinds have induced us to scale back FY21/FY22 PAT estimates by 96%/18%.

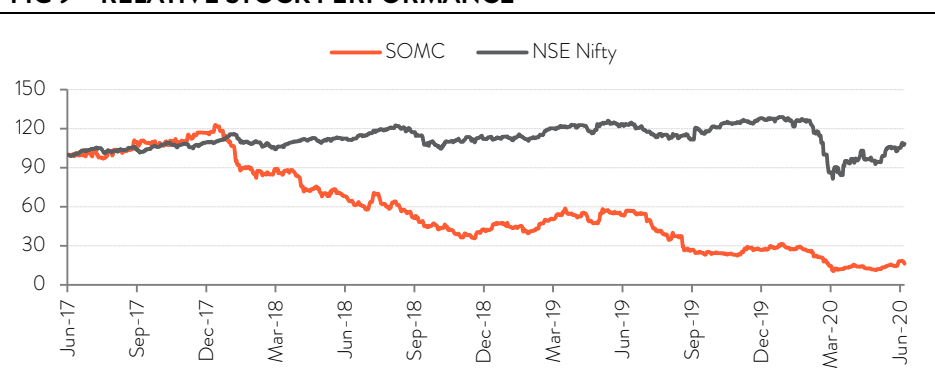
Downgrade from BUY to ADD with a revised Mar'21 target price of Rs 140 (earlier Rs 165), set at an unchanged one-year forward P/E multiple of 12x.

**FIG 8 – REVISED ESTIMATES**

(Rs mn)	New		Old		Change (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Revenues	13,107	16,483	15,164	18,036	(13.6)	(8.6)
EBITDA	994	1,638	1,372	1,804	(27.6)	(9.2)
PAT	12	485	304	590	(96.1)	(17.8)

Source: Company, 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.
- **Continued Covid-19 effect:** If pandemic fears continue to prevail for a prolonged period of time, revenues will be adversely affected.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
<b>Total revenue</b>	<b>17,119</b>	<b>17,110</b>	<b>16,101</b>	<b>13,107</b>	<b>16,483</b>
EBITDA	1,878	1,576	1,314	994	1,638
Depreciation	(413)	(443)	(590)	(613)	(632)
EBIT	1,465	1,134	724	381	1,006
Net interest income/(expenses)	(399)	(459)	(494)	(441)	(404)
Other income/(expenses)	143	149	127	102	100
Exceptional items	0	0	0	0	0
EBT	1,209	824	358	42	701
Income taxes	(393)	(265)	99	(11)	(177)
Extraordinary items	(10)	(26)	(262)	0	0
Min. int./Inc. from associates	(87)	(69)	(45)	(20)	(40)
<b>Reported net profit</b>	<b>720</b>	<b>463</b>	<b>150</b>	<b>12</b>	<b>485</b>
Adjustments	10	26	84	0	0
<b>Adjusted net profit</b>	<b>730</b>	<b>490</b>	<b>234</b>	<b>12</b>	<b>485</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Accounts payables	2,332	1,986	1,729	1,544	1,942
Other current liabilities	1,258	1,275	1,350	934	1,174
Provisions	116	59	96	66	82
Debt funds	5,396	5,731	4,981	4,300	3,950
Other liabilities	524	532	358	358	358
Equity capital	85	85	85	85	85
Reserves & surplus	5,722	6,045	5,980	6,010	6,461
Shareholders' fund	5,807	6,130	6,064	6,094	6,545
<b>Total liabilities and equities</b>	<b>16,391</b>	<b>16,580</b>	<b>15,519</b>	<b>14,257</b>	<b>15,053</b>
Cash and cash eq.	187	460	201	89	153
Accounts receivables	5,037	4,179	2,798	3,088	3,838
Inventories	2,597	2,545	3,282	2,514	2,574
Other current assets	667	1,366	1,058	790	993
Investments	1,142	683	341	400	400
Net fixed assets	6,429	7,048	7,727	7,264	6,982
CWIP	279	247	60	60	60
Intangible assets	52	52	52	52	52
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>16,391</b>	<b>16,580</b>	<b>15,519</b>	<b>14,257</b>	<b>15,053</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Net income + Depreciation	1,133	906	739	624	1,117
Interest expenses	399	459	494	441	404
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(413)	(174)	807	115	(359)
Other operating cash flows	48	(182)	(584)	20	40
<b>Cash flow from operations</b>	<b>1,167</b>	<b>1,009</b>	<b>1,457</b>	<b>1,200</b>	<b>1,202</b>
Capital expenditures	(1,337)	(1,028)	(664)	(150)	(350)
Change in investments	44	459	341	(59)	0
Other investing cash flows	0	0	0	0	0
<b>Cash flow from investing</b>	<b>(1,294)</b>	<b>(569)</b>	<b>(323)</b>	<b>(209)</b>	<b>(350)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	427	335	(751)	(681)	(350)
Interest expenses	(399)	(459)	(494)	(441)	(404)
Dividends paid	(134)	(138)	(204)	(2)	(74)
Other financing cash flows	106	96	56	20	40
<b>Cash flow from financing</b>	<b>(1)</b>	<b>(167)</b>	<b>(1,393)</b>	<b>(1,103)</b>	<b>(788)</b>
<b>Changes in cash and cash eq.</b>	<b>(128)</b>	<b>274</b>	<b>(259)</b>	<b>(112)</b>	<b>64</b>
<b>Closing cash and cash eq.</b>	<b>187</b>	<b>460</b>	<b>201</b>	<b>89</b>	<b>153</b>

**Per Share**

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20P	FY21E	FY22E
Reported EPS	17.0	10.9	3.5	0.3	11.4
Adjusted EPS	17.2	11.6	5.5	0.3	11.4
Dividend per share	2.7	2.0	2.0	0.0	1.5
Book value per share	137.0	144.6	143.1	143.8	154.4

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20P	FY21E	FY22E
EV/Sales	0.5	0.6	0.6	0.8	0.6
EV/EBITDA	4.4	6.1	7.3	9.9	5.8
Adjusted P/E	7.3	10.9	22.7	453.4	11.0
P/BV	0.9	0.9	0.9	0.9	0.8

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20P	FY21E	FY22E
Tax burden (Net profit/PBT)	60.3	59.5	65.4	27.7	69.1
Interest burden (PBT/EBIT)	82.5	72.7	49.4	11.1	69.7
EBIT margin (EBIT/Revenue)	8.6	6.6	4.5	2.9	6.1
Asset turnover (Revenue/Avg TA)	111.1	103.8	100.3	88.0	112.5
Leverage (Avg TA/Avg Equity)	2.8	2.8	2.6	2.4	2.3
Adjusted ROAE	13.2	8.2	3.8	0.2	7.7

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

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	(1.1)	(0.1)	(5.9)	(18.6)	25.8
EBITDA	(20.1)	(16.0)	(16.7)	(24.3)	64.8
Adjusted EPS	(24.7)	(32.9)	(52.2)	(95.0)	4027.3
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	11.0	9.2	8.2	7.6	9.9
EBIT margin	8.6	6.6	4.5	2.9	6.1
Adjusted profit margin	4.3	2.9	1.5	0.1	2.9
Adjusted ROAE	13.2	8.2	3.8	0.2	7.7
ROCE	8.5	6.2	5.9	2.4	6.6
<b>Working capital days (days)</b>					
Receivables	99	98	79	82	77
Inventory	83	86	105	129	90
Payables	48	51	46	49	43
<b>Ratios (x)</b>					
Gross asset turnover	2.7	2.3	1.9	1.4	1.7
Current ratio	1.1	1.2	1.2	1.3	1.4
Net interest coverage ratio	3.7	2.5	1.5	0.9	2.5
Adjusted debt/equity	0.9	0.9	0.8	0.7	0.6

Source: Company, BOBCAPS Research



## Disclaimer

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

**BUY** – Expected return >+15%

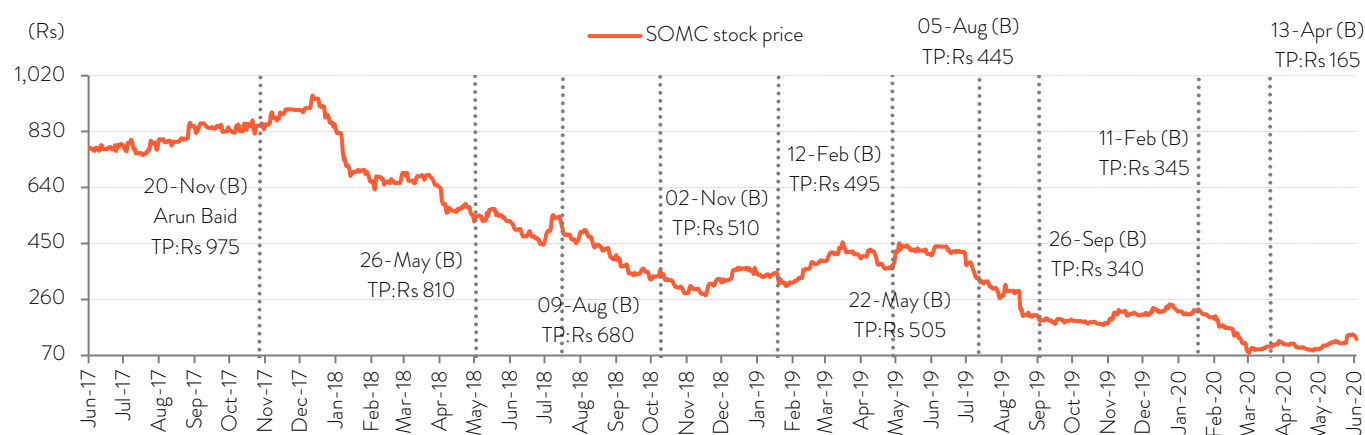
**ADD** – Expected return from >+5% to +15%

**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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