

HOLD

TP: Rs 5,895 | ▲ 8%

CERA SANITARYWARE

Construction Materials

27 October 2021

Healthy demand traction but priced in

- Q2 consolidated revenue grew 24% YoY with the sanitaryware/faucet segments increasing 30%/63%
- With ~95% of the RM basket stable, operating margin expanded 260bps YoY to 15.3% and EBITDA grew 50%
- We raise our TP to Rs 5,895 (vs. Rs 4,375) on a higher multiple and rollover but retain HOLD as positives look priced in

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Healthy revenue growth led by strong demand traction: CRS reported 24% YoY growth in Q2FY22 consolidated revenue to Rs 4bn as (a) it filled the space vacated by peers who depend on imports from China which declined due to high shipping costs, and (b) it saw a revival in real estate demand and increasing retail consumption.

Operating margin expands: During the quarter, ~95% of RM cost was largely stable. Gross margin thus expanded 410bps YoY to 53.4% which coupled with a better product mix and benefits from price hikes spurred EBITDA margin gains of 260bps YoY (+615bps QoQ) to 15.3%.

Demand outlook healthy: Demand has been robust and the sanitaryware/faucet segments ran at optimal capacity utilisation of 97%/90%. CRS expects to see strong demand traction in coming quarters led by (a) a bounce back of real estate demand, (b) pent-up demand for home improvement post pandemic, (c) low interest rates, and (d) lower competition from peers who were dependent on sourcing from China and are now facing supply issues due to high freight cost. Management believes these positives can continue for the next two years.

Maintain positive view...: We expect CRS to witness healthy traction in ensuing years on the back of strong underlying demand and market share gains in sanitaryware (as peers face severe supply issues). The company will focus on replenishing channel inventory and ensuring product availability, leading to an increase in inventory days in FY22 (rise in debtor days also possible).

...but value priced in: We trim EBITDA margin assumptions to incorporate the H1 results, increasing contribution of outsourcing and management commentary. Though we lower FY22/FY23 EPS estimates by 5%/2% on reduced margins, we raise our target one-year forward P/E multiple from 30x to 40x (10% premium to the stock's five-year median of 36.4x) to factor in CRS's market share gains, extensive reach, healthy balance sheet and management pedigree. Positives, however, appear priced in at current valuations of 39x FY23E EPS – we retain HOLD, rolling over to a new Sep'22 TP of Rs 5,895 (vs. Rs 4,375).

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	CRS IN/Rs 5,472
Market cap	US\$ 948.3mn
Free float	46%
3M ADV	US\$ 2.0mn
52wk high/low	Rs 6,450/Rs 2,625
Promoter/FPI/DII	54%/18%/28%

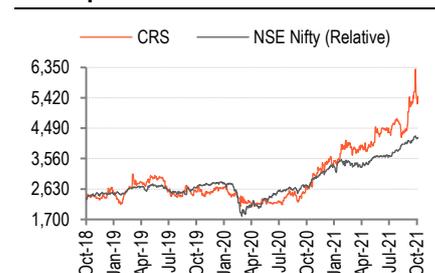
Source: NSE | Price as of 27 Oct 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	12,243	14,436	16,780
EBITDA (Rs mn)	1,581	2,080	2,482
Adj. net profit (Rs mn)	1,008	1,427	1,754
Adj. EPS (Rs)	77.5	109.8	134.9
Consensus EPS (Rs)	77.5	106.1	144.6
Adj. ROAE (%)	12.3	15.4	16.9
Adj. P/E (x)	70.6	49.9	40.6
EV/EBITDA (x)	44.5	33.9	28.5
Adj. EPS growth (%)	(0.6)	41.6	22.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Earnings call highlights

- **Healthy demand trends:** CRS is witnessing a positive demand trajectory, similar to Aug'20 levels. Management expects healthy sales trends to sustain for the rest of FY22.
- **Q2 revenue share:** Sanitaryware contributed 52% of Q2FY22 revenue, faucetware 34%, tiles 12% and wellness 2%. About 68% of total revenue comes from retail and 32% from the institutional segment. Management's objective is to increase the contribution of B2C as the company can monetise its brand power and hike prices.
- **SKU:** The company currently has 466 SKUs in sanitaryware and 911 in faucetware.
- **Value-added contribution rising:** (a) Sanitaryware (Q2FY22) – Entry: 34% (40% in Q2FY21), Mid: 11% (12%), Premium: 55% (48%). (b) Faucetware (Q2FY22) – Entry: 30% (31% in Q2FY21), Mid: 47% (16%), Premium: 23% (53%).
- **Reduced imports from China:** As per management, imports from China have reduced considerably due to rising shipping cost from US\$ 600 per container to US\$ 6,000 in August and US\$10,000 in September. Many peers who were dependent on imports have nothing to offer in the market. This has opened up untapped potential for CRS, and the company has been able to garner market share besides witnessing a sizeable shift from the unorganised to organised sector.
- **Next price hike in mid-November:** CRS is highly dependent on outsourcing and its vendors are unable to absorb the increasing prices of gas, corrugated boxes (up 15%; impact will be visible in Q3), and freight. Despite ~95% of RM costs remaining stable, the company is scheduling another round of price hikes to the tune of 8-12% mid-November.
- **Tile business to improve:** (a) CRS is looking to exit its stake in the Anjani Tiles joint venture and does not expect this to disrupt tile volume availability going ahead. As per the new scheme of arrangement, the company will have the option, but not an obligation, to buy from the JV. (b) Margins in CRS's tiles business are moving up and should move closer to the overall margin at the company level in the next 2-3 years. (c) Receivable days have also declined. (d) Management expects the share of B2C business to increase and B2B to come down.
- **Running a full utilisation:** CRS will continue to focus on outsourcing and will only make high-end, value-added products at its own facility. During Q2, the sanitaryware (97%) and faucetware (90%) plants were already running at optimal capacity utilisation. As of now, the company will face capacity constraints owing to rising demand. It acquired land for faucetware expansion in Q1FY22 but does not have a concrete plan for sanitaryware expansion due to lack of skilled labors.
- **Capex:** Capex planned for FY22 is ~Rs 172mn broken up as follows: sanitaryware ~Rs 67mn, faucetware: ~Rs 50mn and logistics & IT enabled: ~Rs 55mn.

Fig 1 – Consolidated quarterly performance

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H1FY22	H1FY21	YoY (%)
Total revenues	3,241	4,033	24.4	2,282	42.0	6,315	4,701	34.3
Total raw material consumed	1,645	1,881	14.4	936	75.8	2,817	2,410	16.9
% of sales	50.7	46.6	(410bps)	41.0	564bps	44.6	51.3	(665bps)
Employee exps	374	491	31.1	446	(16.1)	937	696	34.5
% of sales	11.5	12.2	62bps	19.5	(737bps)	14.8	14.8	2bps
Other exp	812	1,045	28.7	692	17.3	1,737	1,147	51.4
% of sales	25.0	25.9	86bps	30.3	(442bps)	27.5	24.4	311bps
Total expenditure	2,831	3,416	20.7	2,074	36.5	5,490	4,253	29.1
% of sales	87.3	84.7	(262bps)	90.9	(615bps)	86.9	90.5	(352bps)
EBITDA	410	616	50.2	208	97.0	824	448	84.0
% of sales	12.7	15.3	262bps	9.1	615bps	13.1	9.5	352bps
Depreciation	99	92	(6.6)	89	11.7	181	196	(7.4)
Other income	45	79	78.0	65	(32.0)	145	115	26.3
Interest cost	23	20	(14.2)	21	8.1	41	46	(11.2)
PBT	333	583	75.3	164	103.1	747	321	132.9
Taxes	100.5	143.2	42.6	48.3	108.1	192	105	81.9
Effective tax rate (%)	30.2	24.6	(564bps)	29.5	(492bps)	25.6	32.8	(719bps)
PAT before minority interest/associates	232	440	89.5	115	101.1	555	215	157.8
Less: Minority interest	(15.0)	9.6	(163.6)	(6.5)	132.9	3.1	(37.5)	(108.3)
Add: share of profit in associate	(1.1)	0.1	(107.3)	0.1	(927.9)	0.2	(2.2)	(109.5)
RPAT	246	430	74.9	122	102	553	251	120.3

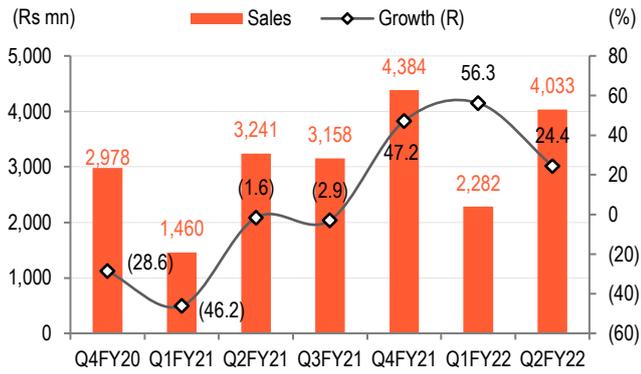
Source: Company, BOBCAPS Research

Fig 2 – Standalone quarterly performance

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H1FY22	H1FY21	YoY (%)
Total revenues	3,932	3,179	23.7	2,228	42.7	6,161	4,605	33.8
Total raw material consumed	1,944	1,668	16.5	985	69.3	2,930	2,395	22.3
% of sales	49.4	52.5	(303bps)	44.2	523bps	47.6	52.0	(445bps)
Employee exps	474	360	31.7	430	(16.4)	905	673	34.5
% of sales	12.1	11.3	73bps	19.3	(726bps)	14.7	14.6	7bps
Other exp	935	746	25.3	614	21.4	1,549	1,066	45.2
% of sales	23.8	23.5	30bps	27.6	(380bps)	25.1	23.2	198bps
Total expenditure	3,353	2,774	20.9	2,030	36.7	5,383	4,134	30.2
% of sales	85	87.3	(200bps)	91	(582bps)	87.4	89.8	(239bps)
EBITDA	579	405	43.1	198	103.9	777	471	65.1
% of sales	14.7	12.7	200bps	8.9	582bps	12.6	10.2	239bps
Depreciation	76.1	83.3	(8.7)	72.9	14.4	148.9	164.5	(9.5)
Other income	69.7	39.4	77.1	57.5	(31.6)	127.2	108.2	17.6
Interest cost	10.3	9.3	10.2	10.4	(10.7)	20.7	19.3	7.0
PBT	562	351	60.1	173	103.5	735	395	86.0
Taxes	141.6	88.4	60.1	43.4	103.5	185.0	103.3	79.1
Effective tax rate (%)	25.2	25.2	0bps	25.2	0bps	25.2	26.1	(97bps)
APAT	421	263	60.1	129	103.5	550	292	88.4
Less: extraordinary items	0	0	-	0	-	0	0	-
RPAT	421	263	60.1	129	104	550	292	88.4

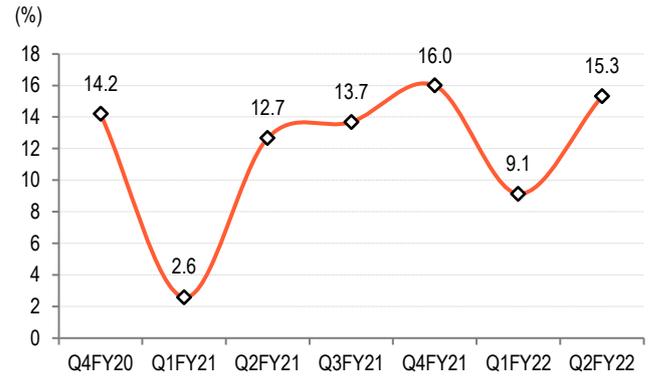
Source: Company, BOBCAPS Research

Fig 3 – Consolidated revenue growth



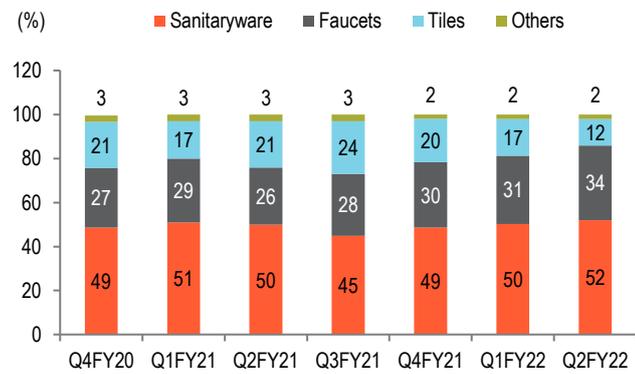
Source: Company, BOBCAPS Research

Fig 4 – EBITDA margin trend



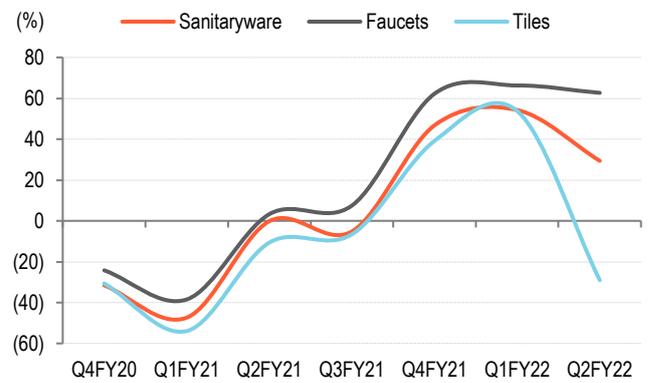
Source: Company, BOBCAPS Research

Fig 5 – Segmental revenue contribution



Source: Company, BOBCAPS Research

Fig 6 – Segmental growth



Source: Company, BOBCAPS Research

Valuation methodology

We expect CRS to witness healthy traction in ensuing years on the back of strong underlying demand and market share gains in sanitaryware (peers facing severe supply issues). The company will focus on replenishing channel inventory and ensuring product availability, leading to an increase in inventory days for FY22 (rise in debtor days also possible).

We have trimmed EBITDA margin assumptions after incorporating the H1 results, increasing contribution of outsourcing and management commentary on cost outlook. Though, we lower FY22/FY23 EPS estimates by 5%/2%, we raise our target one-year forward P/E multiple from 30x to 40x to factor in CRS's market share gains, extensive reach, healthy balance sheet and management pedigree. Our multiple is at 10% premium to the stock's five-year median of 36.4x. Positives, however, appear priced in at current valuations of 39x FY23E EPS – we retain HOLD, rolling over to a new Sep'22 TP of Rs 5,895 (vs. Rs 4,375).

Fig 7 – Revised estimates

(Rs mn)	New		Old		Change (%)	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Revenue	14,436	16,780	14,436	16,500	0.0	1.7
EBITDA	2,080	2,482	2,178	2,538	(4.5)	(2.2)
EBITDA margin (%)	14.4	14.8	15.1	15.4	(679bps)	(594bps)
PAT	1,427	1,754	1,501	1,796	(4.9)	(2.3)

Source: BOBCAPS Research

Fig 8 – Key assumptions

(Rs mn)	FY21	FY22E	FY23E	FY24E
Sanitaryware	5,830	6,995	8,185	9,249
Growth (%)	(0.4)	20.0	17.0	13.0
Faucets	3,398	4,127	4,746	5,368
Growth (%)	10.7	21.0	15.0	13.0
Tiles	2,500	2,924	3,363	3,800
Growth (%)	(6.4)	17.0	15.0	13.0
Wellness	288	389	487	608
Growth (%)	(34.9)	35.0	25.0	25.0

Source: Company, BOBCAPS Research

Fig 9 – 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	5,893	17.1	109.8	134.9	15.4	16.9	40
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:

- **Fall in raw material prices:** CRS's key raw material is natural gas; any sharp decrease in prices may positively affect near-term profitability.
- **Sharp increase in housing market:** A strong increase in housing activity may result in above-expected revenue growth

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	12,220	12,243	14,436	16,780	19,025
EBITDA	1,654	1,581	2,080	2,482	2,899
Depreciation	(388)	(396)	(410)	(432)	(457)
EBIT	1,266	1,185	1,670	2,050	2,442
Net interest inc./(exp.)	(101)	(97)	(66)	(58)	(45)
Other inc./(exp.)	65	252	291	337	360
Exceptional items	119	0	0	0	0
EBT	1,230	1,339	1,895	2,329	2,757
Income taxes	(243)	(340)	(478)	(587)	(695)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	27	9	10	12	15
Reported net profit	1,133	1,008	1,427	1,754	2,077
Adjustments	(119)	0	0	0	0
Adjusted net profit	1,013	1,008	1,427	1,754	2,077

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	953	1,554	1,345	1,471	1,668
Other current liabilities	2,102	2,186	2,334	2,621	2,971
Provisions	136	171	202	235	266
Debt funds	919	729	600	500	350
Other liabilities	299	303	335	367	399
Equity capital	65	65	65	65	65
Reserves & surplus	7,642	8,652	9,730	10,949	12,393
Shareholders' fund	7,707	8,717	9,795	11,014	12,458
Total liab. and equities	12,194	13,777	14,717	16,303	18,192
Cash and cash eq.	125	104	140	99	0
Accounts receivables	2,228	2,095	2,531	3,034	3,440
Inventories	2,430	1,997	2,413	2,804	3,180
Other current assets	737	670	831	965	1,095
Investments	2,283	4,743	4,800	5,500	5,500
Net fixed assets	4,373	4,147	4,037	4,006	3,949
CWIP	5	13	13	13	13
Intangible assets	12	8	8	8	8
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	12,194	13,777	14,773	16,429	17,184

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash flow from operations	1,517	2,858	892	1,692	2,280
Capital expenditures	(450)	(140)	(300)	(400)	(400)
Change in investments	(504)	(2,460)	(57)	(700)	0
Other investing cash flows	(45)	5	(10)	(12)	(15)
Cash flow from investing	(999)	(2,595)	(367)	(1,112)	(415)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	13	(191)	(129)	(100)	(150)
Interest expenses	(101)	(97)	(66)	(58)	(45)
Dividends paid	(396)	0	(340)	(523)	(619)
Other financing cash flows	(103)	5	(10)	(12)	(15)
Cash flow from financing	(586)	(283)	(545)	(692)	(828)
Chg in cash & cash eq.	(68)	(20)	(20)	(112)	1,036
Closing cash & cash eq.	125	104	84	28	1,135

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	87.1	77.5	109.8	134.9	159.7
Adjusted EPS	77.9	77.5	109.8	134.9	159.7
Dividend per share	13.0	13.0	21.8	33.5	39.6
Book value per share	592.6	670.3	753.1	846.9	957.9

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	5.8	5.8	4.9	4.2	3.7
EV/EBITDA	42.6	44.5	33.9	28.5	24.4
Adjusted P/E	70.2	70.6	49.9	40.6	34.3
P/BV	9.2	8.2	7.3	6.5	5.7

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	75.1	75.2	75.3	75.3	75.3
Interest burden (PBT/EBIT)	106.6	113.0	113.4	113.6	112.9
EBIT margin (EBIT/Revenue)	10.4	9.7	11.6	12.2	12.8
Asset turnover (Rev./Avg TA)	101.4	94.3	101.1	107.6	113.2
Leverage (Avg TA/Avg Equity)	1.6	1.6	1.5	1.5	1.4
Adjusted ROAE	13.8	12.3	15.4	16.9	17.7

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	(9.4)	0.2	17.9	16.2	13.4
EBITDA	(15.8)	(4.4)	31.6	19.3	16.8
Adjusted EPS	0.3	(0.6)	41.6	22.9	18.4
Profitability & Return ratios (%)					
EBITDA margin	13.5	12.9	14.4	14.8	15.2
EBIT margin	10.4	9.7	11.6	12.2	12.8
Adjusted profit margin	8.3	8.2	9.9	10.5	10.9
Adjusted ROAE	13.8	12.3	15.4	16.9	17.7
ROCE	12.4	9.7	12.5	13.9	14.9
Working capital days (days)					
Receivables	78	64	58	61	62
Inventory	152	129	123	125	126
Payables	36	43	43	36	36
Ratios (x)					
Gross asset turnover	2.1	2.0	2.2	2.5	2.6
Current ratio	1.5	1.2	1.4	1.5	1.5
Net interest coverage ratio	12.6	12.2	25.1	35.5	54.7
Adjusted debt/equity	0.1	0.1	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%

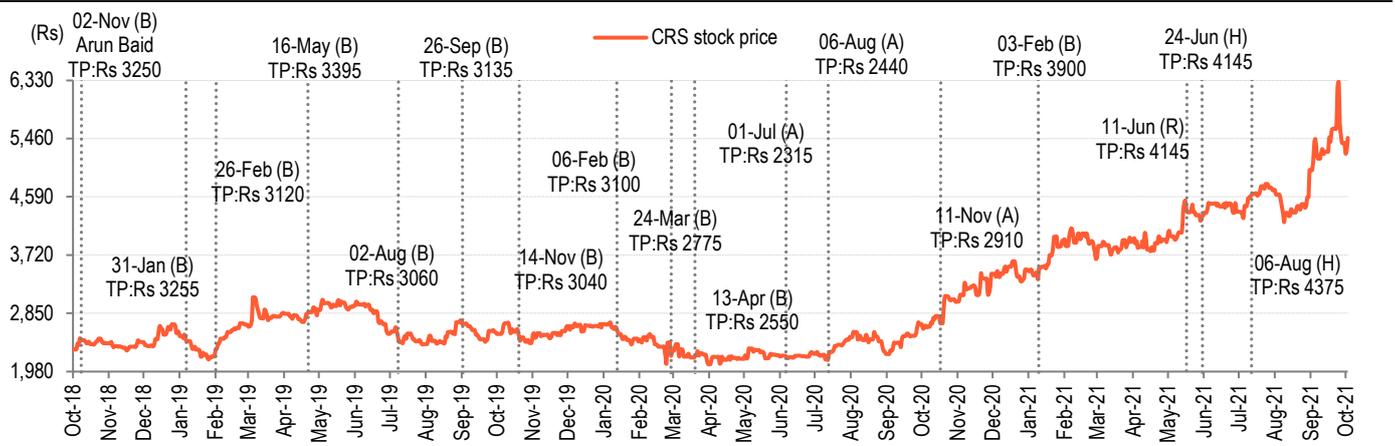
HOLD – Expected return from -6% to +15%

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): CERA SANITARYWARE (CRS IN)



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

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