

**BUY**

TP: Rs 5,590 | ▲ 24%

**CERA SANITARYWARE**

Construction Materials

25 January 2022

## Healthy demand traction with positive outlook

- Q3 consolidated revenue grew 28% YoY with the sanitaryware/faucet segments increasing 51%/60%
- With ~95% of the RM basket stable and price hike benefits, operating margin expanded 280bps YoY to 16.5% and EBITDA grew 54%
- Maintain BUY with an unchanged TP of Rs 5,590 given strong growth prospects and improving return ratios

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**Healthy revenue growth led by strong demand traction:** CRS reported 28% YoY growth in Q3FY22 consolidated revenue to Rs 4bn as (a) the company 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 led by home upgrades and improvement.

**Operating margin expands:** A higher revenue contribution of sanitaryware and faucetware at 88% in Q3FY22 vs. 73% in Q3FY21 had a positive bearing on EBITDA margin. In addition, ~95% of raw material cost was largely stable. Gross margin thus expanded 820bps YoY to 54.5% which coupled with a better product mix and price hike benefits spurred EBITDA margin gains of 280bps YoY (+120bps QoQ) to 16.5%.

**Demand outlook healthy:** Demand has been robust and the sanitaryware/faucet segments ran at optimal capacity utilisation of 103%/99% in Q3. CRS expects to see strong demand traction in coming quarters led by (a) real estate demand, (b) demand for home improvement and upgrades, (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.

**Maintain positive view...:** CRS is in a sweet spot and continues to witness material volume growth in its bathroom solutions segment aided by (a) market share gains across the product portfolio led by import substitution in the sanitaryware and faucet segments, which has opened up untapped potential (besides market share gains, CRS is witnessing a sizeable shift from the unorganised to organised sector); (b) Morbi's intensified focus on exports in the tile segment; and (c) demand pickup in the housing sector (both new construction and replacement).

**...retain BUY:** CRS trades at a P/E of 28.2x on FY24E which is reasonable compared to its five-year median of 37.6x. We continue to value the stock at 35x FY24E EPS for a TP of Rs 5,590 and retain BUY given the company's strong growth prospects, improving balance sheet driven by stricter control on receivables and rising return ratios.

## Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	CRS IN/Rs 4,494
Market cap	US\$ 781.5mn
Free float	46%
3M ADV	US\$ 0.7mn
52wk high/low	Rs 6,450/Rs 3,315
Promoter/FPI/DII	54%/19%/27%

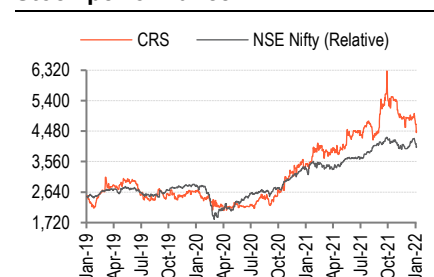
Source: NSE | Price as of 25 Jan 2022

## 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	113.5	141.2
Adj. ROAE (%)	12.3	15.4	16.9
Adj. P/E (x)	58.0	40.9	33.3
EV/EBITDA (x)	36.5	27.8	23.3
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. Management expects healthy sales trends to sustain in the medium term led by home upgrades and improvement given changing needs and trends, benign interest rates, government incentives and growing real estate sales.
- **Revenue share:** Sanitaryware contributed 53% of Q3FY22 revenue (45% in Q3FY21/52% in Q2FY22), faucetware 35% (28%/34%), tiles 10% (24%/12%) and wellness 2% (3%/2%). Sanitaryware and faucetware together formed 88% of the topline in Q3FY22 vs. 73% in Q3FY21. Management's objective is to increase the B2C contribution as the company can monetise its brand power and hike prices.

- **Value-added contribution rising:**

Segments (%)	Q3FY22	Q2FY22	Q3FY21
<b>Sanitaryware</b>			
Entry	29	34	27
Mid	31	11	10
Premium	57	55	63
<b>Faucetware</b>			
Entry	30	30	34
Mid	47	47	14
Premium	23	23	52

Source: Company, BOBCAPS Research

- **Reduced imports from China:** As per management, imports from China have reduced considerably as shipping cost has skyrocketed from US\$ 600 per container to US\$ 6,000 in Aug'21, US\$ 10,000 in Sep'21 and US\$ 7,000 in Jan'22. Many peers who were dependent on imports thus 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.
- **Price hikes in sanitaryware and faucetware:** CRS is highly dependent on outsourcing. Its vendors have been unable to absorb the increasing prices of gas, corrugated boxes (+5% YoY), and freight. Despite ~95% of raw material costs remaining stable, the company took a cumulative price hike of 26% in sanitaryware over Aug'20-Dec'21 (10% in Nov'21) and 27% in faucetware (5.5% in Dec'21). In addition, sanitaryware vendors raised prices by 8.5-9% and faucetware vendors by 5-6% in Oct-Nov'21.
- **SKU:** CRS currently has 350 SKUs in sanitaryware and 850 in faucetware. New SKUs contributed 20% to the topline.
- **Gas cost impact:** About 44% of CRS's gas requirement is met by GAIL where gas price stood at Rs 9.5/cbm in Sep'21 and Rs 13.3/cbm in Oct'21. The balance 56% of gas requirement is met via Sabarmati where prices climbed to Rs 70/cbm in Nov'21 from Rs 45/cbm in Sep'21. The company's gas cost thus increased from Rs 18.5mn/qtr to Rs 26mn for Q3 – though the impact on financials was minimal.

CRS also uses renewable energy (93% of requirement) such as wind and solar, keeping the cost basket stable.

- **Running at full utilisation:** CRS will continue to focus on outsourcing and will only make high-end, value-added products at its own facility. During Q3, the sanitaryware (103%) and faucetware (99%) plants ran at optimal capacity utilisation. Management expects to face capacity constraints in coming months owing to rising demand. It has acquired land for faucetware expansion in Q1FY22 but does not have a concrete plan for sanitaryware expansion due to a lack of skilled labour. Further, vendor availability in sanitaryware is low as the company demands stringent brand and quality standards.

- **Tile business to improve:** (a) CRS is looking to exit its stake in the Anjani Tiles joint venture but does not expect this to disrupt tile volume availability. As per the new scheme of arrangement, the company will have the option, but not an obligation, to buy tiles from the JV.

(b) Margins in CRS's tiles business are rising and should move closer to the overall margin at the company level in the next 2-3 years. Receivable days have also declined. Management expects the share of B2C business to increase and B2B to come down. Further, as this is a low-technology business with minimal differential, the company will manufacture 100% via outsourcing. Management's objective is to grow the bottomline and match the market leader's EBITDA margin going forward.

- **Distribution network:** The company has 8 Cera Style Studios, 150 Cera Galleries, 375 Cera Centres, 4,000 dealers and 11,000 retailers.
- **Working capital cycle:** Management expects the working capital cycle to increase in coming quarters due to growing demand and the need to rebuild inventory. Inventory days increased to 66.5 in Q3FY22 vs. 53.8 days in Q3FY21. Net working capital days stood at 60 vs. 64 in Q3FY21.
- **Capex:** Capex for FY21 was Rs 98mn with an outlay of ~Rs 172mn planned for FY22 broken up as follows: sanitaryware ~Rs 62mn, faucetware: ~Rs 50mn and logistics & IT enabled: ~Rs 55mn.
- **Cash and cash equivalents:** Dec'21: Rs 5.2bn, Sep'21: Rs 48bn, Dec'20: Rs 4.1bn.

**Fig 1 – Consolidated quarterly performance**

(Rs mn)	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)	9MFY22	9MFY21	YoY (%)
<b>Total revenues</b>	<b>4,045</b>	<b>3,158</b>	<b>28.1</b>	<b>4,033</b>	<b>0.3</b>	<b>10,359</b>	<b>7,859</b>	<b>31.8</b>
Total raw material consumed	1,839	1,694	8.5	1,881	(2.3)	4,655	4,104	13.4
% of sales	45.5	53.7	(820bps)	46.6	(119bps)	44.9	52.2	(728bps)
Employee exps	499	357	39.7	491	1.6	1,436	1,053	36.3
% of sales	12.3	11.3	102bps	12.2	16bps	13.9	13.4	45bps
Other exp	1,042	675	54.4	1,045	(0.3)	2,778	1,822	52.5
% of sales	25.8	21.4	439bps	25.9	(15bps)	26.8	23.2	364bps
Total expenditure	3,379	2,726	23.9	3,416	(1.1)	8,869	6,979	27.1
% of sales	83.5	86.3	(279bps)	84.7	(118bps)	85.6	88.8	(319bps)
<b>EBITDA</b>	<b>666</b>	<b>432</b>	<b>54.2</b>	<b>616</b>	<b>8.0</b>	<b>1490</b>	<b>880</b>	<b>69.4</b>
<b>EBITDA margin (%)</b>	<b>16.5</b>	<b>13.7</b>	<b>279bps</b>	<b>15.3</b>	<b>118bps</b>	<b>14.4</b>	<b>11.2</b>	<b>319bps</b>
Depreciation	95	100	(4.9)	92	2.6	276	295	(6.6)
Other income	53	94	(43.3)	79	(32.8)	198	209	(5.1)
Interest cost	19	23	(15.2)	20	(1.6)	61	69	(12.5)
<b>PBT</b>	<b>605</b>	<b>403</b>	<b>50.0</b>	<b>583</b>	<b>3.7</b>	<b>1351</b>	<b>724</b>	<b>86.7</b>
Taxes	157.1	96.1	63.5	143.2	9.7	348.6	201.4	73.1
Effective tax rate (%)	26.0	23.8	214bps	24.6	142bps	25.8	27.8	(203bps)
PAT before minority interest/associates	<b>448</b>	<b>307</b>	<b>45.8</b>	<b>440</b>	<b>1.7</b>	<b>1003</b>	<b>522</b>	<b>92.0</b>
Less: Minority interest	12.4	7.8	58.2	9.6	29.4	15.5	(29.7)	(152.2)
Add: Share of profit in associate	(2.6)	0.2	-	0.1	-	(2.4)	(2.0)	-
<b>RPAT</b>	<b>432</b>	<b>299</b>	<b>44.5</b>	<b>430</b>	<b>0.5</b>	<b>985</b>	<b>550</b>	<b>79.1</b>

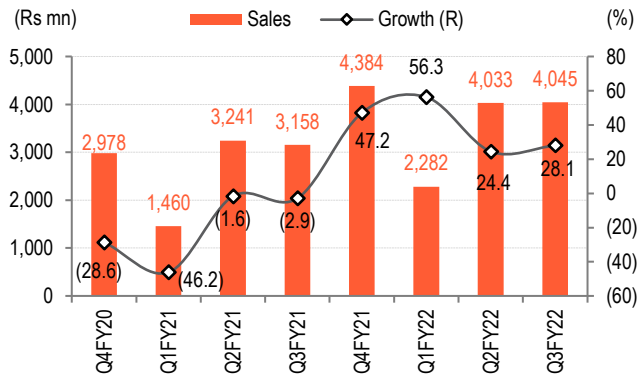
Source: Company, BOBCAPS Research

**Fig 2 – Standalone quarterly performance**

(Rs mn)	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)	9MFY22	9MFY21	YoY (%)
<b>Total revenues</b>	<b>3,870</b>	<b>3,098</b>	<b>24.9</b>	<b>3,932</b>	<b>(1.6)</b>	<b>10,031</b>	<b>7,703</b>	<b>30.2</b>
Total raw material consumed	1,839	1,801	2.1	1,944	(5.4)	4,769	4,195	13.7
% of sales	47.5	58.1	(1059bps)	49.4	(192bps)	47.5	54.5	(692bps)
Employee exps	482	342	40.9	474	1.6	1,386	1,015	36.6
% of sales	12.4	11.0	141bps	12.1	39bps	13.8	13.2	65bps
Other exp	938	559	67.9	935	0.4	2,487	1,625	53.0
% of sales	24.2	18.0	621bps	23.8	48bps	24.8	21.1	370bps
Total expenditure	3,259	2,701	20.7	3,353	(2.8)	8,642	6,835	26.4
% of sales	84	87	(297bps)	85	(106bps)	86	89	(257bps)
<b>EBITDA</b>	<b>611</b>	<b>397</b>	<b>53.8</b>	<b>579</b>	<b>5.5</b>	<b>1388</b>	<b>868</b>	<b>59.9</b>
<b>EBITDA margin (%)</b>	<b>15.8</b>	<b>12.8</b>	<b>297bps</b>	<b>14.7</b>	<b>106bps</b>	<b>13.8</b>	<b>11.3</b>	<b>257bps</b>
Depreciation	77.7	83.9	(7.3)	76.1	2.2	226.6	248.4	(8.8)
Other income	41.7	85.0	(51.0)	69.7	(40.2)	168.9	193.2	(12.6)
Interest cost	10.0	9.5	4.7	10.3	(2.9)	30.7	28.9	6.3
<b>PBT</b>	<b>565</b>	<b>389</b>	<b>45.3</b>	<b>562</b>	<b>0.4</b>	<b>1300</b>	<b>784</b>	<b>65.8</b>
Taxes	142.2	97.8	45.3	141.6	0.4	327.2	201.2	62.7
Effective tax rate (%)	25.2	25.2	0bps	25.2	0bps	25.2	25.7	(49bps)
APAT	<b>423</b>	<b>291</b>	<b>45.3</b>	<b>421</b>	<b>0.4</b>	<b>973</b>	<b>583</b>	<b>66.9</b>
Less: Extraordinary items	0	0	-	0	-	0	0	-
<b>RPAT</b>	<b>423</b>	<b>291</b>	<b>45.3</b>	<b>421</b>	<b>0.4</b>	<b>973</b>	<b>583</b>	<b>66.9</b>

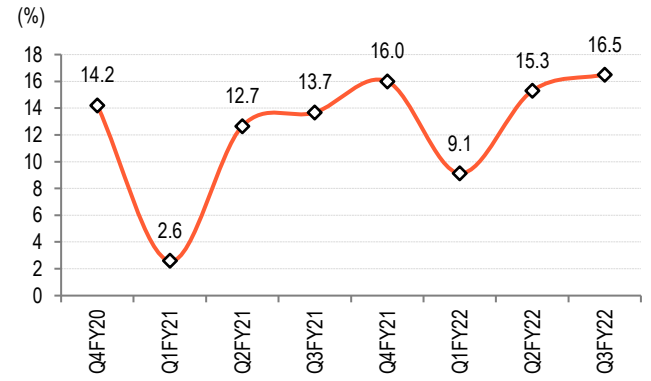
Source: Company, BOBCAPS Research

**Fig 3 – Consolidated revenue growth**



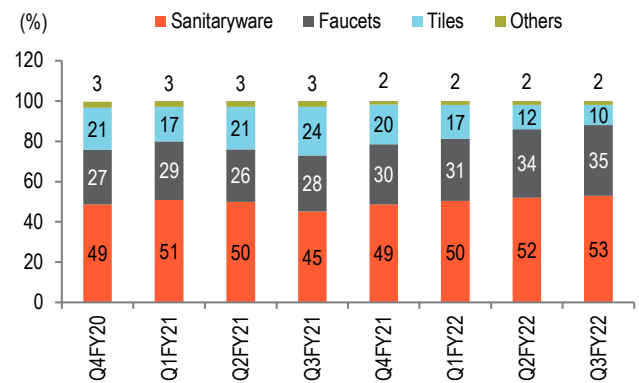
Source: Company, BOBCAPS Research

**Fig 4 – EBITDA margin trend**



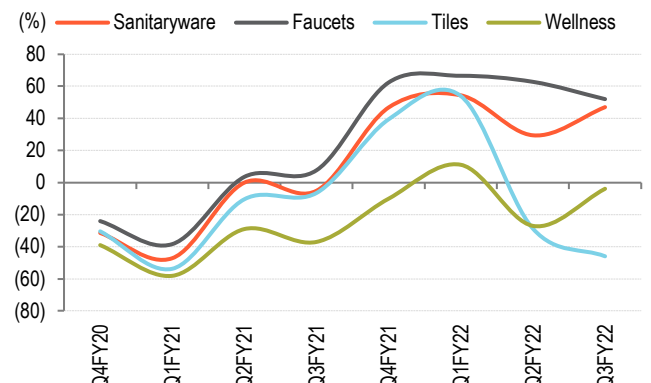
Source: Company, BOBCAPS Research

**Fig 5 – Segmental revenue contribution**



Source: Company, BOBCAPS Research

**Fig 6 – Segmental growth**



Source: Company, BOBCAPS Research

## Valuation methodology

CRS is in a sweet spot and continues to witness material volume growth in its bathroom solutions segment aided by (a) market share gains across the product portfolio led by import substitution in the sanitaryware and faucet segments, which has opened up untapped potential (besides market share gains, CRS is witnessing a sizeable shift from the unorganised to organised sector); (b) Morbi's intensified focus on exports in the tile segment; and (c) demand pickup in the housing sector (both new construction and replacement).

The stock is trading at a P/E of 28.2x on FY24E which is reasonable compared to its five-year median of 37.6x. We continue to value CRS at 35x FY24E EPS for a TP of Rs 5,590 and retain BUY given the company's strong growth prospects, improving balance sheet driven by stricter control on receivables, particularly in faucets and tiles (which is likely to continue in the near term), and rising return ratios.

**Fig 7 – 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 8 – 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	BUY	1,460	21.5	22.8	29.6	18.9	23.3	40
Somany Ceramics	SOMC IN	BUY	1,140	19.0	20.5	32.8	12.5	17.3	25
Greenply Ind	MTLM IN	BUY	260	18.0	7.7	10.2	19.7	21.4	22
Century Plyboard	CPBI IN	HOLD	735	23.8	13.6	16.7	22.1	22.1	35
Greenpanel Ind	GREENP	BUY	595	34.0	16.0	21.7	23.7	25.1	23
Cera Sanitaryware	CRS IN	BUY	5,590	17.1	109.8	134.9	15.4	16.9	35
Astral	ASTRA IN	HOLD	2,465	22.3	22.5	29.5	22.5	26.0	65
Finolex Ind	FNXP IN	HOLD	220	7.7	10.2	9.4	19.0	15.9	22
Supreme Ind	SI IN	BUY	2,535	15.7	74.7	80.7	28.0	26.7	30

Source: BOBCAPS Research

## Key risks

Key downside risks to our estimates are:

- higher input prices which may dent demand/profitability,
- decline in real estate demand,
- slowdown in economic revival, and
- resurgence of Covid-19 which might adversely affect sales in the short term.

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Total revenue</b>	<b>12,220</b>	<b>12,243</b>	<b>14,436</b>	<b>16,780</b>	<b>19,025</b>
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
<b>Reported net profit</b>	<b>1,133</b>	<b>1,008</b>	<b>1,427</b>	<b>1,754</b>	<b>2,077</b>
Adjustments	(119)	0	0	0	0
<b>Adjusted net profit</b>	<b>1,013</b>	<b>1,008</b>	<b>1,427</b>	<b>1,754</b>	<b>2,077</b>

### 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
<b>Total liab. and equities</b>	<b>12,194</b>	<b>13,777</b>	<b>14,717</b>	<b>16,303</b>	<b>18,192</b>
Cash and cash eq.	125	104	84	(28)	1,008
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
<b>Total assets</b>	<b>12,194</b>	<b>13,777</b>	<b>14,717</b>	<b>16,303</b>	<b>18,192</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Cash flow from operations</b>	<b>1,517</b>	<b>2,858</b>	<b>892</b>	<b>1,692</b>	<b>2,280</b>
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)
<b>Cash flow from investing</b>	<b>(999)</b>	<b>(2,595)</b>	<b>(367)</b>	<b>(1,112)</b>	<b>(415)</b>
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)
<b>Cash flow from financing</b>	<b>(586)</b>	<b>(283)</b>	<b>(545)</b>	<b>(692)</b>	<b>(828)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>(68)</b>	<b>(20)</b>	<b>(20)</b>	<b>(112)</b>	<b>1,036</b>
<b>Closing cash &amp; cash eq.</b>	<b>125</b>	<b>104</b>	<b>84</b>	<b>(28)</b>	<b>1,008</b>

### 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	4.7	4.7	4.0	3.4	3.0
EV/EBITDA	34.9	36.5	27.8	23.3	20.0
Adjusted P/E	57.7	58.0	40.9	33.3	28.1
P/BV	7.6	6.7	6.0	5.3	4.7

### 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	101.3	108.2	110.3
Leverage (Avg TA/Avg Equity)	1.6	1.6	1.5	1.5	1.5
Adjusted ROAE	13.8	12.3	15.4	16.9	17.7

### Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
<b>YoY growth (%)</b>					
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
<b>Profitability &amp; Return ratios (%)</b>					
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
<b>Working capital days (days)</b>					
Receivables	78	64	58	61	62
Inventory	152	129	123	125	126
Payables	36	43	43	36	36
<b>Ratios (x)</b>					
Gross asset turnover	2.1	2.0	2.2	2.5	2.6
Current ratio	1.5	1.2	1.4	1.5	1.7
Net interest coverage ratio	12.6	12.2	25.1	35.5	54.7
Adjusted debt/equity	0.1	0.1	0.1	0.0	(0.1)

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

## Disclaimer

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

**BUY** – Expected return >+15%

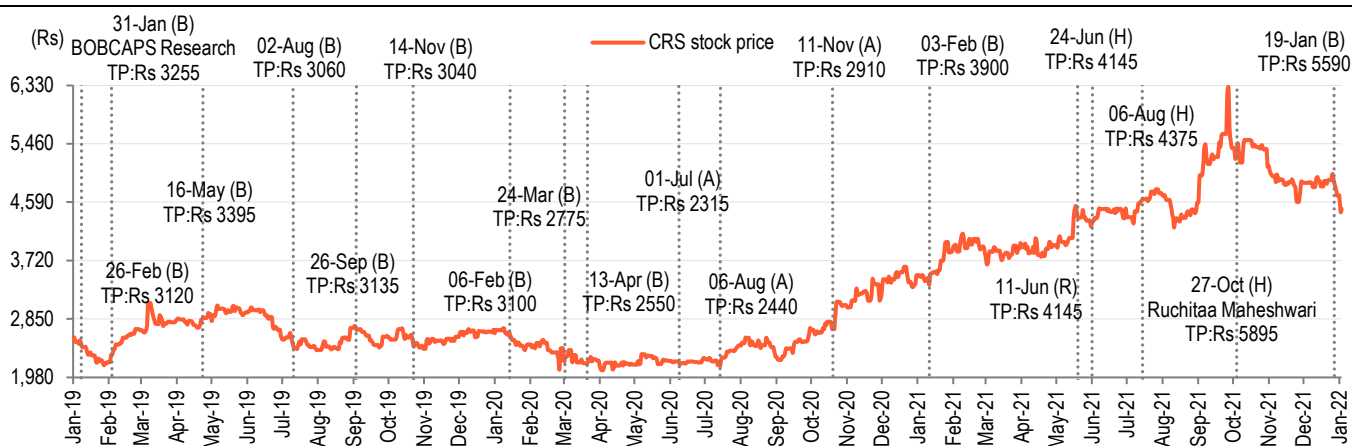
**HOLD** – Expected return from -6% to +15%

**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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