FIRST LIGHT

04 July 2022

RESEARCH

India Strategy | Monthly Wrap

Valuations now in line with long term trends

Cera Sanitaryware | Target: Rs 5,225 | +27% | BUY

Consistent Performer

Crompton Greaves | Target: Rs 500 | +47% | BUY

Annual Report Analysis – Fortifying its market position

SUMMARY

India Strategy: Monthly Wrap

- Valuation will likely inch towards long term trend as market resets from an easy liquidity framework to a traditional valuation matrix, in our view
- Nifty 50 fell 4.5% in June, but still outperformed US and Europe. Nifty valuation is now at the bottom end of the five-year band
- India will likely gain from manufacturing resurgence in US, new outsourcing from Europe, and domestic market led growth

Click here for the full report.

Cera Sanitaryware

- We expect CRS to clock revenue CAGR of ~16.5% during FY22-24E aided by growth in sanitaryware and faucetware segments
- Price hike of 3% in sanitaryware and 5% in faucetware in Q1 and cumulative price hike in FY22, will enable CRS to maintain margins
- Retain BUY rating with a revised TP of Rs 5,225 (revised PER from 35x to 32x on FY24E) to factor in likely stress in real estate market

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Daily macro indicators

Indicator	28-Jun	29-Jun	Chg (%)
US 10Y yield (%)	3.17	3.09	(8bps)
India 10Y yield (%)	7.47	7.46	(1bps)
USD/INR	78.77	78.97	(0.2)
Brent Crude (US$/bbl)	118	116.3	(1.5)
Dow	30,947	31,029	0.3
Hang Seng	22,419	21,997	(1.9)
Sensex	53,177	53,027	(0.3)
India FII (US$ mn)	**27-Jun**	**28-Jun**	**Chg ($ mn)**
FII-D	(120.4)	(134.6)	(14.2)
FII-E	(139.5)	(108.4)	31.1

Source: Bank of Baroda Economics Research

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Crompton Greaves

- Leadership maintained in fans and pumps, while being a top player in lighting. BGAL acquisition to strengthen adjacency offerings
- It's cost savings program is one of its biggest margin shields, savings of Rs2 bn in FY22 (3.8% of sales); cumulatively Rs5 bn in last 3yrs
- Efforts towards brand building, R&D, scaling up distribution network should reinforce its market position. Maintain BUY with TP of Rs500

Click here for the full report.

MONTHLY WRAP | Volume #5 | 01 July 2022

Valuations now in line with long term trends

- **Valuation will likely inch towards long term trend as market resets from an easy liquidity framework to a traditional valuation matrix, in our view**
- **Nifty 50 fell 4.5% in June, but still outperformed US and Europe. Nifty valuation is now at the bottom end of the five-year band**
- **India will likely gain from manufacturing resurgence in US, new outsourcing from Europe, and domestic market led growth**

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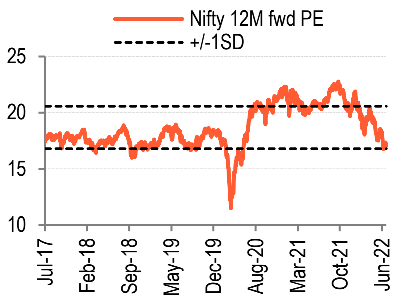
Extraordinary period of 2008-22 not a good valuation benchmark anymore: Central banks of majority of large economies unleashed a synchronised flood of liquidity, which may be a difficult precedence to follow. While there is only a tenuous consensus on whether this liquidity resulted in the massive extant inflation, central banks reverting to such an easy liquidity again is a low probability scenario in our view, given bloated balance sheets of many central banks and persistent inflation. Therefore, both investment hypothesis and valuation in our view will gradually get de-anchored from easy liquidity period and move more towards traditional matrices and valuation ranges (Fig 1 and Fig 2)

Currency resilience: Nifty 50 declined by 4.5% in June 2022 with small caps underperforming large caps. Except Auto (+1.2%), all the other sectors posted negative returns with Metals (-12.7%) underperforming most. RBI has been less hawkish than its global peers in raising rates. Even though INR is testing its all-time lows against USD, Indian currency has performed better than most of its Asian peers. On an average, Indian equity market trades at a ~50% premium to other emerging markets. Current premium of 70%, though higher than historical levels, can partly be justified on currency strength and robust earnings expectations.

Setback to climate activism. Latest decision by the Supreme Court of USA restraining Environment Protection Agency (EPA) from imposing emission norms on old power plants will likely have major implications on effecting large scale regulatory changes in US. The decision in a way shifts major environmental (or potentially other major) policy changes from bureaucrats to elected officials. This along with increased usage of coal in Europe does point to a setback to energy transition efforts. However, we believe these hurdles are largely short term, and energy transition will continue to get reinforced by annual Conference of Parties (COP).

Several levers for India's growth: As Chinese economy slows down, we believe India will gain from global supply chain realignments to countries like India, knock-on effect from manufacturing resurgence in US, high energy price led outsourcing from Europe, and underlying momentum in domestic demand. Please refer to our note of 11 Jan 22, **"India at Takeoff Point"** where we analysed building blocks for a faster underlying demand growth in India. A sharp demand destruction in western countries due to higher inflation remains the biggest near-term challenge for India.

Valuations are now in lower end of 5year historical range



Source: Bloomberg, BOBCAPS Research

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BUY
TP: Rs 5,225 | ▲ 27%

CERA SANITARYWARE | Construction Materials | 01 July 2022

Consistent Performer

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- **Price hike of 3% in sanitaryware and 5% in faucetware in Q1 and cumulative price hike in FY22, will enable CRS to maintain margins**
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We interacted with Cera Executive Director, Ayush Bagla to gain a perspective on the company's growth prospects and sector outlook. Key takeaways:

Gas cost impact: About 40% of CRS's gas requirement is met by GAIL where gas price increased to Rs 25/scm in Q1FY23 from Rs 11.13/scm in FY22. The balance 60% is met via Sabarmati Gas where prices climbed to Rs 65/scm in Q1FY23 from Rs 59.46/scm in FY22. As per management, the company is procuring gas at a much lower rate than the market. Gas cost is just 2.8% of overall raw material cost for the company.

Capex of Rs 2bn by FY24 from internal accruals: CRS is expanding capacity by 1.2mn pieces each in sanitaryware (greenfield; 24-30 months) for Rs 1.3bn and in faucetware (brownfield; by Q2FY24) for Rs 0.7bn.

Price hikes in sanitaryware and faucetware: CRS took a price hike of 3% in sanitaryware and 5% in faucetware segment in mid-May 2022.

Healthy demand outlook with stable margin: Management expects to double the revenues at a faster rate 18-20% CAGR in the next three-four years. In addition, management is confident of doubling revenue within the next 3.5 years from 5 years earlier. CRS has guided a 50-75bps rise in EBITDA margin each year.

Healthy demand traction; retain BUY: The recent capacity de-bottlenecking and capacity expansion by 40-50% announced (which would commence operations in the next 12-36 months) would lead the next leg of growth. CRS' timely capacity expansion plan, focus on improving product mix, extensive distribution network, healthy balance sheet and rising return ratios bode well for sustainable earnings growth. While we like the company's a) leadership position in sanitaryware, b) scale-up in faucetware/sanitaryware and c) robust return profile, we are concerned about likely stress in the real estate market due to higher inflation and rising interest rate. Hence, to factor-in, we have reduced our target multiple by ~10%. We retain BUY rating with a revised TP of Rs 5,225 (revised PER from 35x to 32x on FY24E).

Key changes

Target	Rating
▼	◄►

Ticker/Price	CRS IN/Rs 4,126
Market cap	US$ 678.9mn
Free float	46%
3M ADV	US$ 1.2mn
52wk high/low	Rs 6,450/Rs 3,515
Promoter/FPI/DII	54%/20%/26%

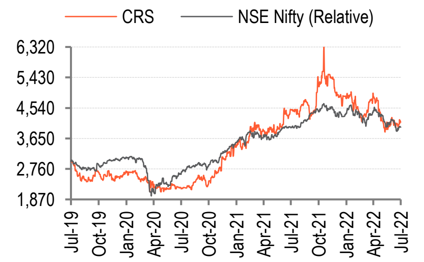
Source: NSE | Price as of 1 Jul 2022

Key financials

Y/E 31 Mar	FY22P	FY23E	FY24E
Total revenue (Rs mn)	14,458	16,850	19,634
EBITDA (Rs mn)	2,287	2,694	3,202
Adj. net profit (Rs mn)	1,568	1,802	2,124
Adj. EPS (Rs)	120.6	138.5	163.3
Consensus EPS (Rs)	116.2	135.4	158.4
Adj. ROAE (%)	16.6	16.7	17.5
Adj. P/E (x)	34.2	29.8	25.3
EV/EBITDA (x)	23.1	19.7	16.8
Adj. EPS growth (%)	55.6	14.9	17.9

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE

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BUY
TP: Rs 500 | ⮝ 47%

CROMPTON GREAVES | Consumer Durables | 01 July 2022

Annual Report Analysis: Fortifying its market position

- **Leadership maintained in fans and pumps, while being a top player in lighting. BGAL acquisition to strengthen adjacency offerings**
- **It's cost savings program is one of its biggest margin shields, savings of Rs2 bn in FY22 (3.8% of sales); cumulatively Rs5 bn in last 3yrs**
- **Efforts towards brand building, R&D, scaling up distribution network should reinforce its market position. Maintain BUY with TP of Rs500**

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Crompton was able to navigate FY22 well due to its cost-saving program, product mix improvement, and calibrated pricing. As a part of building its adjacent products, it acquired Butterfly Gandhimati (BGAL) in FY22. Its leadership position continued in fans segment, while lighting saw subdued demand in B2B lighting partly offsetting double-digit growth in B2C segment. Project Unnati aimed at aggressive cost cutting led to the savings of Rs2 bn (3.8% of FY22 revenue). Efforts towards brand building, R&D, scaling up distribution network should reinforce its market position in fans and pump division. Maintain BUY with a TP of Rs500.

BGAL to help increase presence in adjacency products – FY22 Crompton completed acquisition of 55% stake BGAL for Rs14 bn (subsequently hiked to 81% following its open offer in Q1FY23). Butterfly is amongst the top three kitchen and small domestic appliances players in India. Management has stated it would be focusing on prioritizing revenue growth over margin and anticipates operating leverage to drive EBIT margin. With this acquisition, Crompton is enhancing its offerings in adjacent products, with an advantage of leveraging its existing distribution network

5-dimesnional growth strategy: The company has devised a growth strategy to achieve its long-term strategic growth through Branding, Portfolio, Go-To-Market Reach, Operational and Organizational focus.

Project Unnati through its design optimization, commercial negotiation, and operational efficiency via in-house manufacturing has achieved a cost savings of Rs2 bn in FY22 (3.8% of revenue). Notably, company has achieved cost saving of Rs5bn over FY20-FY22.

Increase in Debt, mainly led by acquisition – The company's Net Debt increased to Rs6.9 bn from Net cash of Rs1.3 bn in FY21, primarily due to acquisition of Butterfly. Net Debt/equity stood at 0.3x. Pertinently, return ratios were impacted, but we believe that it should mean revert by FY24 as BGAL becomes earnings accretive.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	CROMPTON IN/Rs 340
Market cap	US$ 2.7bn
Free float	94%
3M ADV	US$ 7.0mn
52wk high/low	Rs 513/Rs 312
Promoter/FPI/DII	6%/38%/44%

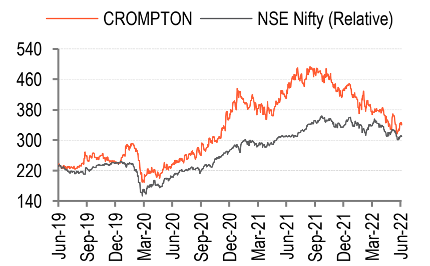
Source: NSE | Price as of 30 Jun 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	53,941	74,589	85,017
EBITDA (Rs mn)	7,694	10,057	11,922
Adj. net profit (Rs mn)	5,914	7,237	9,171
Adj. EPS (Rs)	9.3	11.1	14.1
Consensus EPS (Rs)	9.3	10.5	12.6
Adj. ROAE (%)	27.0	25.1	24.7
Adj. P/E (x)	36.4	30.5	24.2
EV/EBITDA (x)	27.6	21.4	18.3
Adj. EPS growth (%)	(4.1)	19.3	26.1

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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.

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