

BUY
 TP: Rs 1,325 | ▲ 24%

KAJARIA CERAMICS

Construction Materials

02 November 2022

Demand sluggish; high gas cost weakens margins

- Q2 revenue grew 11% YoY aided by a 10% rise in tile realisations while volume growth stayed flat at ~25msm
- EBITDA margin contracted 650bps YoY to 12% due to higher power & fuel cost and other expenses
- We cut FY23/FY24 PAT estimates by 24%/9% and revise our TP to Rs 1,325 (vs. Rs 1,460); maintain BUY

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Flattish volumes offset by higher realisations: KJC's Q2FY23 revenue increased 11% YoY (7% QoQ) to Rs 10.8bn, backed by a 10% rise in realisations to Rs 391/sqm. Sale volumes remained flattish YoY at 24.9msm (+7% QoQ) owing to a demand slowdown in July-August. Revenue from the tiles business rose 10% YoY to Rs 9.7bn led by a 2% price hike, with KJC's own manufacturing, subsidiaries and outsourcing businesses contributing Rs 5.9bn (+14% YoY), Rs 1.3bn (-8.5%) and Rs 2.4bn (+15%) respectively. Sanitaryware and plywood revenue climbed 3.2% YoY to Rs 0.9bn.

Margins contract on higher gas cost: Gross margin contracted 520bps YoY and 220bps QoQ to ~23% owing to higher power & fuel cost (+825bps YoY) – mainly high gas cost averaging ~Rs 62/scm in Q2FY23 (vs. Rs 37/scm in Q2FY22 and Rs 55/scm in Q1FY23). EBITDA margin fell 650bps YoY and 320bps QoQ to 12%.

H2 margin guided to rise 200bps: Management now aims to achieve 15% volume growth in FY23 (vs. 15-20% guided earlier) and expects +200bps EBITDA margin improvement (to +14%) in Q3 and Q4 led by a shift to LPG feedstock in the Gailpur, Morbi and Srikalahasti plants. LPG is currently priced at Rs 55/scm.

Expansion on the cards: (a) Kajaria Bathware, Gailpur: Adding new capacity of 600,000 pieces p.a. by Nov'22 at Rs 50mn capex. (b) Kerovit Global, Gujarat: Investing Rs 700mn to make it a wholly owned subsidiary and to set up a sanitaryware facility for 600,000 pieces p.a. by Dec'23. (c) JV in Nepal: Investing Rs 1.25bn (50% of project cost of Rs 2.5bn) for 8msm of annual tile manufacturing capacity. (d) Sikandrabad plant: Expansion-cum-modernisation to add larger-sized glazed vitrified tiles (GVT) capacity of 3msm p.a. at a capex of Rs 800mn, which will raise total capacity at the plant to 11.4msm.

Long-term value play; maintain BUY: KJC is trading at attractive valuations of 29.2x FY24E P/E vs. its 5Y median of ~41x. We lower our PAT estimates by 23.8% for FY23 and 9.4% for FY24 to incorporate the H1FY23 performance and management's cautious demand outlook. This translates to a revised TP of Rs 1,325 (vs. Rs 1,460), set at an unchanged 40x FY24E P/E multiple – retain BUY.

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	KJC IN/Rs 1,068
Market cap	US\$ 2.1bn
Free float	53%
3M ADV	US\$ 2.5mn
52wk high/low	Rs 1,375/Rs 885
Promoter/FPI/DII	47%/19%/33%

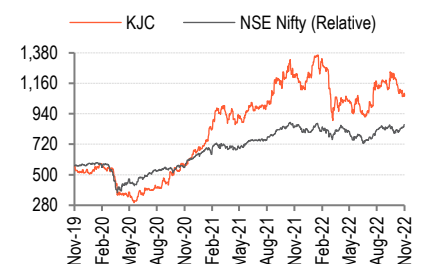
Source: NSE | Price as of 2 Nov 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	37,052	43,635	50,824
EBITDA (Rs mn)	6,107	6,116	8,472
Adj. net profit (Rs mn)	3,770	3,591	5,253
Adj. EPS (Rs)	23.7	22.6	33.1
Consensus EPS (Rs)	23.7	31.8	38.3
Adj. ROAE (%)	18.9	16.6	23.1
Adj. P/E (x)	45.0	47.3	32.3
EV/EBITDA (x)	27.4	27.2	19.9
Adj. EPS growth (%)	22.4	(4.8)	46.3

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Earnings call highlights

- **Demand:** July and August were difficult months for KJC with some revival witnessed in September. However, the month of October saw a renewed slowdown due to the festive season. Management is cautious on demand going forward.
- **Price hikes:** In order to offset the rise in gas price as well as higher transportation and packaging costs, KJC has increased prices of GVT and ceramics by ~2% in Q2FY23. The company has not taken any price hikes in sanitaryware and bathware (last raised in May'22).
- **Gas cost:** Average gas cost stood at ~Rs 62/scm in Q2FY23 vs. Rs 55/scm in Q1FY23. Further, gas availability reduced by 30% in Q2. Management is looking to incur gas cost of Rs 55/scm in Q3 due to a shift in plant feedstock composition to LPG, and also expects costs to come down starting Apr'23.

Fig 1 – Gas prices

Avg Price (Rs/scm)	Q2FY23	Q1FY23	Q4FY22	Q3FY22	FY22	FY21
North	60.0	52.0	45.5	43.0	41.0	26.0
South	69.0	60.0	60.0	55.5	44.0	12.5
West	69.0	67.0	62.0	58.2	49.0	28.5

Source: Company

- **JV realisation:** In Q2FY23, the JV earned realisations of Rs 324/tile vs. Rs 330/tile in Q2FY22.
- **Product mix:** Volume/value share during Q2 was at 46%/40% for ceramics, 28%/33% for GVT and 26%/37% for PVT. In comparison, value share for the year-ago quarter was at 38%/31%/31% for ceramics/GVT/PVT.
- **Sanitaryware and Plywood:** The segment reported a lower EBIT margin of 0.4% in Q2FY23 vs. 7.1% in Q2FY23 and 4.4% in Q1FY23.
- **Bathware:** Q2 revenue in bathware stood at Rs 744mn (flattish YoY, +4% QoQ). Management expects revenue of Rs 3.7bn in FY23 vs. Rs 2.75bn in FY22, ~35% YoY growth, on the back of expected demand revival in H2.
- **Other expenses:** A&P spend was at Rs 320mn in Q2FY23 vs. Rs 190mn in Q1FY23. For FY23, A&P is guided to be above Rs 1bn vs. Rs 800mn in FY22.
- **Channel inventory:** Channel inventory stands at 30-40 days.
- **Working capital:** The working capital cycle increased by 5 days QoQ to 62 days in Q2FY23 mainly due to a reduction in creditor days. KJC expects to have 57 working capital days by end-December.
- **Rationale for investment in Nepal:** India exports tiles worth Rs 50bn to Nepal and the country has a market size of 25msm p.a. Indian products currently attract ~45% import duty.
- **Industry exports:** Management estimates that industry-wide tile exports for FY23 will exceed Rs 170bn-180bn vs. Rs 127bn in FY22.

- **Domestic market growth:** Per KJC, the Indian market for tiles is estimated at Rs 210bn in FY22 and expected to grow by 5% to Rs 220bn in FY23.
- **Dealers:** KJC plans to add 400-450 dealers in the next three years (including 200 in FY23, of which 75 were added in H1FY23).

Fig 2 – Consolidated quarterly performance

(Rs mn)	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)	H1FY23	H1FY22	YoY (%)
Net Sales	10,778	9,736	10.7	10,082	6.9	20,860	15,352	35.9
COGS	7,191	5,999	19.9	6,425	11.9	13,616	9,258	47.1
Employee cost	1,138	1,020	11.6	1,144	(0.5)	2,282	1,953	16.9
Other expenses	1,154	912	26.6	978	18.1	2,132	1,532	39.2
EBITDA	1,294	1,805	(28.3)	1,536	(15.7)	2,830	2,610	8.4
EBITDA Margin (%)	12.0	18.5	(653bps)	15.2	(323bps)	13.6	17.0	(343bps)
Depreciation and amortization	337	282	19.5	324	4.0	660	547	20.7
EBIT	958	1,523	(37.1)	1,212	(21.0)	2,170	2,063	5.2
EBIT Margin (%)	8.9	15.6	(676bps)	12.0	(314bps)	10.4	13.4	(303bps)
Net Interest expenses	32	27	16.2	36	(12.5)	68	57	17.9
Other non-operating inc (exp), net	76	71	7.2	81	(5.7)	157	131	19.8
Earnings before tax	1,002	1,567	(36.1)	1,257	(20.3)	2,259	2,137	5.7
Income taxes	277	374	(26.0)	328	(15.5)	604	528	14.4
Earnings after tax	725	1,193	(39.2)	930	(22.0)	1,655	1,608	2.9
Extraordinary items	0	0	-	0	-	0	0	-
Minority interest (expense) income	37	32	15.1	(7)	(654.5)	30	16	89.9
APAT	689	1,161	(40.7)	936	(26.4)	1,625	1,592	2.1

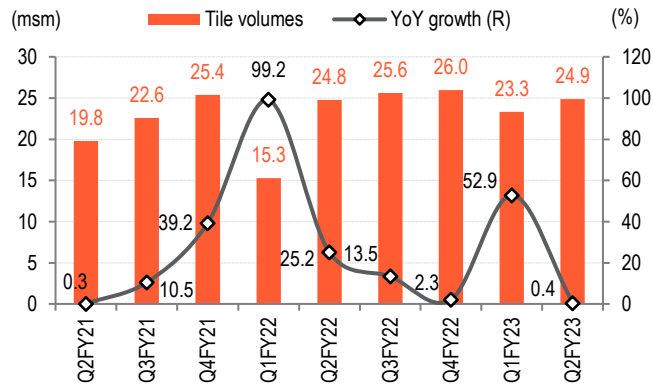
Source: Company, BOBCAPS Research

Fig 3 – Consolidated segmental performance

(Rs mn)	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)	H1FY23	H1FY22	YoY (%)
Segment Revenues								
Tiles	9,839	8,826	11.5	9,165	7.4	19,004	14,019	35.6
Other	938	910	3.2	917	2.3	1,856	1,333	39.2
Total revenues	10,778	9,736	10.7	10,082	6.9	20,860	15,352	35.9
EBIT								
Tiles	954	1459	(34.7)	1172	(18.7)	2126	1991	6.8
Other	4	64	(93.6)	40	(89.8)	44	71.4	(38.1)
Total	958	1,523	(37.1)	1,212	(21.0)	2,170	2,062	5.2
EBIT Margins (%)								
Tiles	9.7	16.5	(684bps)	12.8	(310bps)	11.2	14.2	(302bps)
Other	0.4	7.1	(663bps)	4.4	(394bps)	2.4	5.4	(297bps)

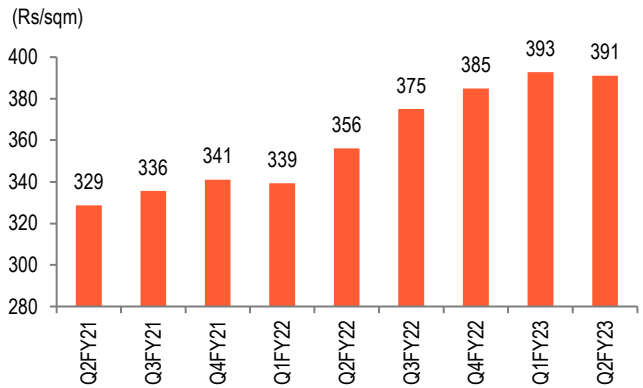
Source: Company, BOBCAPS Research

Fig 4 – Tile volumes



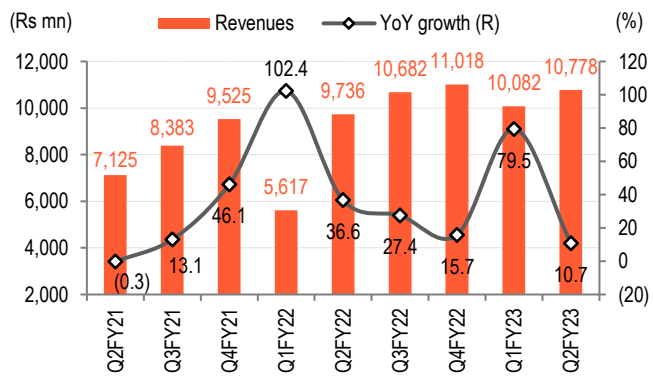
Source: Company, BOBCAPS Research

Fig 5 – Tile net realisations



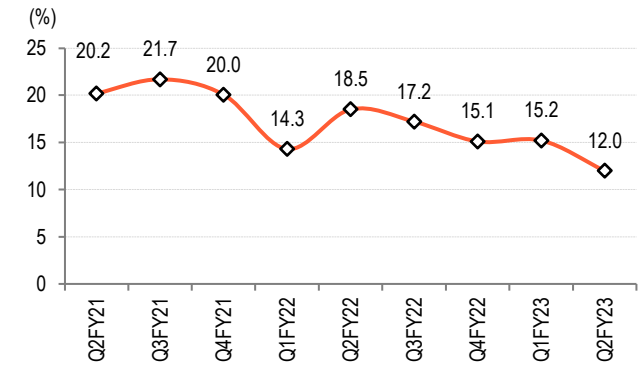
Source: Company, BOBCAPS Research

Fig 6 – Consolidated revenue trend



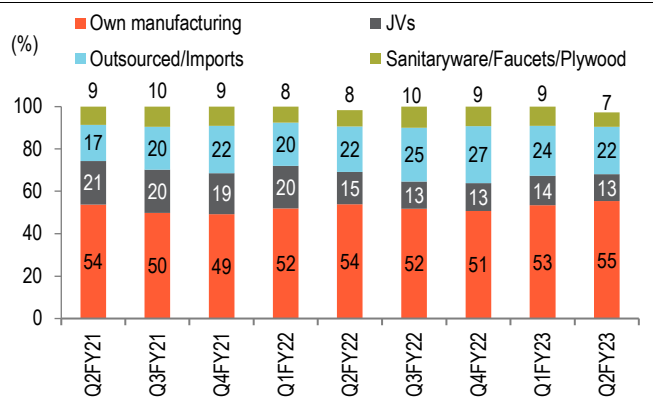
Source: Company, BOBCAPS Research

Fig 7 – Consolidated EBITDA margin trend



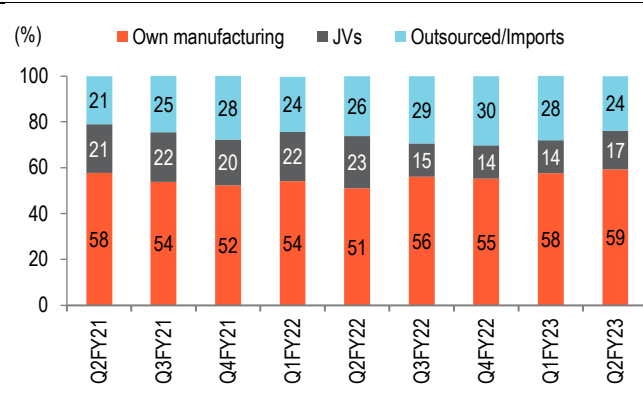
Source: Company, BOBCAPS Research

Fig 8 – Revenue breakup



Source: Company, BOBCAPS Research

Fig 9 – Tile volume breakup



Source: Company, BOBCAPS Research

Valuation methodology

We believe KJC has long-term structural growth drivers by way of improving real estate demand in tier-2-and-below towns, domestic market share gains captured from the Morbi ceramic cluster and an increasing export focus. The company remains the market leader in tiles and has strong brand recall, a high retail mix and expansive distribution across India, as well as robust cash flows and healthy return ratios. We believe ongoing capacity expansion coupled with improvement in realisations and product mix would spur growth ahead.

KJC is trading at attractive valuations of 29.2x FY24E P/E vs. its five-year median of ~41x. We lower our PAT estimates by 23.8% for FY23 and 9.4% for FY24 to incorporate the H1FY23 performance and management's cautious demand outlook. This translates to a revised TP of Rs 1,325 (vs. Rs 1,460), set at an unchanged 40x FY24E P/E multiple – retain BUY.

Fig 10 – Revised estimates

(Rs mn)	New		Old		Change (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Net Sales	43,635	50,824	43,635	49,791	0.0	2.1
EBITDA	6,116	8,472	7,643	9,225	(19.9)	(8.2)
EBITDA margin (%)	14.0	16.7	17.5	18.5	(350bps)	(180bps)
PAT	3,591	5,253	4,710	5,800	(23.8)	(9.4)

Source: BOBCAPS Research

Key risks

Key downside risks to our estimates are:

- sharp uptick in raw material prices and gas costs,
- substantial decrease in exports from Morbi players,
- increasing competition from the informal sector, and
- slowdown in economic revival and in housing demand.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Century Plyboards	CPBI IN	1.6	599	735	BUY
Cera Sanitaryware	CRS IN	0.9	5,431	5,225	HOLD
Greenpanel Industries	GREENP IN	0.6	372	595	BUY
Greenply Industries	MTLM IN	0.3	173	235	BUY
Kajaria Ceramics	KJC IN	2.1	1,068	1,325	BUY
Pidilite Industries	PIDI IN	16.2	2,634	1,870	SELL
Somany Ceramics	SOMC IN	0.3	543	830	BUY

Source: BOBCAPS Research, NSE | Price as of 2 Nov 2022

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Total revenue	28,080	27,809	37,052	43,635	50,824
EBITDA	4,159	5,088	6,107	6,116	8,472
Depreciation	(1,081)	(1,067)	(1,154)	(1,393)	(1,538)
EBIT	3,078	4,022	4,953	4,723	6,934
Net interest inc./(exp.)	(195)	(107)	(127)	(128)	(108)
Other inc./(exp.)	242	213	276	303	340
Exceptional items	0	0	0	0	0
EBT	3,125	4,127	5,102	4,898	7,166
Income taxes	(589)	(1,038)	(1,274)	(1,234)	(1,806)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	18	(9)	(58)	(73)	(107)
Reported net profit	2,553	3,081	3,770	3,591	5,253
Adjustments	0	0	0	0	0
Adjusted net profit	2,553	3,081	3,770	3,591	5,253

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Accounts payables	2,105	1,760	2,644	3,029	3,441
Other current liabilities	2,311	2,201	2,741	2,919	3,437
Provisions	288	313	338	363	388
Debt funds	1,171	971	1,279	1,079	879
Other liabilities	731	687	985	1,010	1,035
Equity capital	159	159	159	159	159
Reserves & surplus	16,984	18,530	21,065	21,962	23,276
Shareholders' fund	17,143	18,689	21,224	22,121	23,435
Total liab. and equities	24,386	25,266	29,858	31,243	33,443
Cash and cash eq.	2,350	4,477	4,244	1,300	615
Accounts receivables	3,967	4,317	5,133	6,575	7,658
Inventories	5,127	3,731	4,659	7,053	8,215
Other current assets	640	615	1,623	956	1,114
Investments	3	0	0	0	0
Net fixed assets	11,854	11,911	13,947	15,044	15,506
CWIP	257	50	70	80	80
Intangible assets	103	112	112	112	112
Deferred tax assets, net	15	13	0	0	0
Other assets	70	40	70	122	142
Total assets	24,386	25,266	29,858	31,243	33,443

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Cash flow from operations	2,472	4,963	3,524	2,630	5,555
Capital expenditures	(1,213)	(1,012)	(2,500)	(2,500)	(2,000)
Change in investments	0	0	0	0	0
Other investing cash flows	0	3	0	0	0
Cash flow from investing	(1,213)	(1,009)	(2,500)	(2,500)	(2,000)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	222	(201)	309	(200)	(200)
Interest expenses	(195)	(107)	(127)	(128)	(108)
Dividends paid	(1,150)	(1,591)	(2,827)	(2,693)	(3,940)
Other financing cash flows	(310)	72	1,389	(53)	8
Cash flow from financing	(1,433)	(1,827)	(1,257)	(3,074)	(4,239)
Chg in cash & cash eq.	(174)	2,127	(233)	(2,945)	(684)
Closing cash & cash eq.	2,350	4,477	4,244	1,300	615

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22A	FY23E	FY24E
Reported EPS	16.1	19.4	23.7	22.6	33.1
Adjusted EPS	16.1	19.4	23.7	22.6	33.1
Dividend per share	3.0	10.0	14.2	13.6	19.8
Book value per share	107.9	117.6	133.5	139.2	147.4

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22A	FY23E	FY24E
EV/Sales	6.0	6.1	4.5	3.8	3.3
EV/EBITDA	40.7	33.1	27.4	27.2	19.9
Adjusted P/E	66.5	55.1	45.0	47.3	32.3
P/BV	9.9	9.1	8.0	7.7	7.2

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22A	FY23E	FY24E
Tax burden (Net profit/PBT)	81.7	74.6	73.9	73.3	73.3
Interest burden (PBT/EBIT)	101.5	102.6	103.0	103.7	103.3
EBIT margin (EBIT/Revenue)	11.0	14.5	13.4	10.8	13.6
Asset turnover (Rev./Avg TA)	116.7	112.0	134.4	142.8	157.1
Leverage (Avg TA/Avg Equity)	1.5	1.4	1.4	1.4	1.4
Adjusted ROAE	15.5	17.2	18.9	16.6	23.1

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22A	FY23E	FY24E
YoY growth (%)					
Revenue	(5.0)	(1.0)	33.2	17.8	16.5
EBITDA	(7.5)	22.3	20.0	0.2	38.5
Adjusted EPS	10.3	20.6	22.4	(4.8)	46.3
Profitability & Return ratios (%)					
EBITDA margin	14.8	18.3	16.5	14.0	16.7
EBIT margin	11.0	14.5	13.4	10.8	13.6
Adjusted profit margin	9.1	11.1	10.2	8.2	10.3
Adjusted ROAE	15.5	17.2	18.9	16.6	23.1
ROCE	13.8	15.3	17.1	15.0	21.1
Working capital days (days)					
Receivables	57	54	47	49	51
Inventory	83	81	56	67	77
Payables	38	31	26	28	28
Ratios (x)					
Gross asset turnover	1.5	1.4	1.7	1.7	1.9
Current ratio	2.1	2.7	2.3	2.2	2.2
Net interest coverage ratio	15.8	37.5	38.9	36.9	64.3
Adjusted debt/equity	(0.1)	(0.2)	(0.1)	0.0	0.0

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

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

BUY – Expected return >+15%

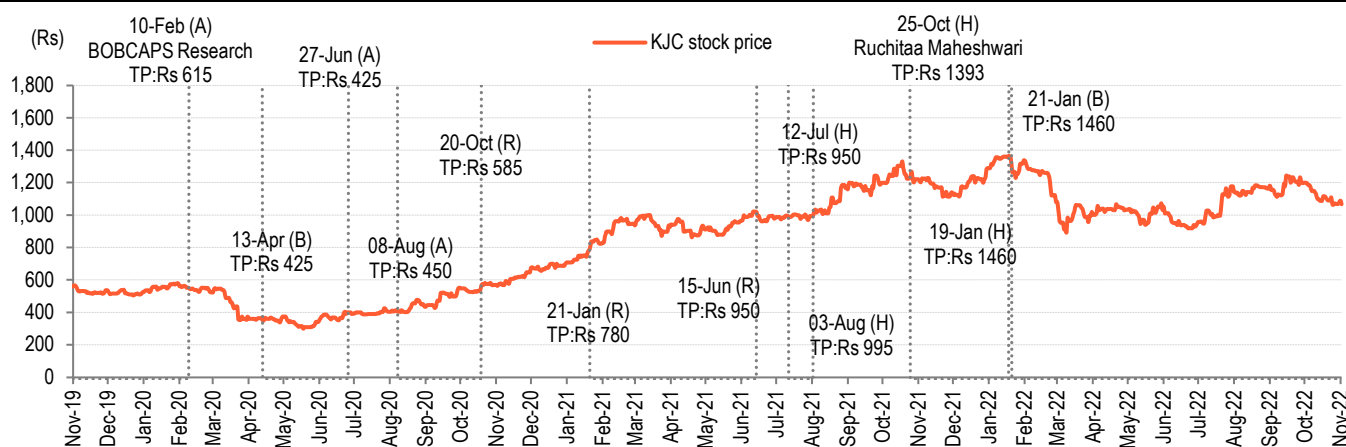
HOLD – Expected return from -6% to +15%

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): KAJARIA CERAMICS (KJC IN)



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

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