

ADD

TP: Rs 425 | ▲ 6%

KAJARIA CERAMICS

Construction Materials

27 June 2020

Lockdown hits hard – downgrade to ADD

Kajaria Ceramics (KJC) posted a below-expected Q4FY20 with revenue down 20% YoY as tile volumes fell 19%. Operating margins contracted 75bps YoY to 14.3% due to negative operating leverage, causing EBITDA/PBT to decline 24%/36%. Management has not given FY21 guidance due to Covid-19 vagaries but expects cost rationalisation to cushion the margin impact. We cut FY21/FY22 earnings by 9%/1% and keep our Mar'21 TP unchanged at Rs 425. At current valuations of 24.9x FY22E EPS, we see limited upside. Cut from BUY to ADD.

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Lockdown erodes volume growth: KJC's Q4 revenue declined 20% YoY to Rs 6.5bn as realisations slipped 1.1% YoY and volumes dropped 19% YoY. As per management, volume growth was hit hard as the Covid-19 lockdown in the second half of March coincided with a seasonally busy period for the company. KJC has not provided any guidance for FY21 due to pandemic-related uncertainties, but stated that demand traction has improved post easing of the lockdown – revenues are back to ~25% of normal levels in May and 60-70% in June.

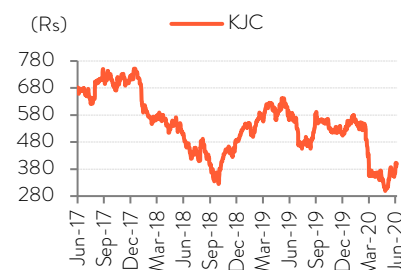
Operating margins decline: Despite a 270bps YoY increase in gross margin, operating margins contracted 75bps YoY to 14.3% (-70bps QoQ) as employee cost/other expenses increased 240bps/195bps YoY due to negative operating leverage. Consequently, EBITDA/PBT decreased 24%/36% YoY. KJC expects cost rationalisation to aid savings of Rs 750mn-900mn in FY21 and thus cushion the impact of lower sales on margins.

Downgrade to ADD: Given the below-expected Q4 performance, we prune FY21/FY22 PAT estimates by 9%/1%. We see limited upside potential and hence downgrade the stock to ADD with an unchanged Mar'21 TP of Rs 425.

Ticker/Price	KJC IN/Rs 401
Market cap	US\$ 843.6mn
Shares o/s	159mn
3M ADV	US\$ 2.2mn
52wk high/low	Rs 606/Rs 296
Promoter/FPI/DII	48%/23%/29%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
Total revenue (Rs mn)	27,106	29,562	28,080	22,857	28,158
EBITDA (Rs mn)	4,564	4,495	4,159	3,005	4,420
Adj. net profit (Rs mn)	2,342	2,314	2,553	1,551	2,565
Adj. EPS (Rs)	14.7	14.6	16.1	9.8	16.1
Adj. EPS growth (%)	(7.4)	(1.2)	10.3	(39.3)	65.4
Adj. ROAE (%)	18.5	15.8	15.5	8.7	13.3
Adj. P/E (x)	27.2	27.6	25.0	41.1	24.9
EV/EBITDA (x)	14.4	14.4	15.2	20.8	13.9

Source: Company, BOBCAPS Research

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FIG 1 – CONSOLIDATED QUARTERLY PERFORMANCE

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
Net Sales	6,520	8,153	(20.0)	7,413	(12.0)	28,080	29,562	(5.0)
COGS	3,822	5,002	(23.6)	4,404	(13.2)	16,655	17,625	(5.5)
Employee cost	869	888	(2.2)	930	(6.6)	3,569	3,455	3.3
Other expenses	896	1,034	(13.4)	967	(7.3)	3,698	3,987	(7.3)
EBITDA	934	1,229	(24.1)	1,113	(16.1)	4,159	4,495	(7.5)
EBITDA Margin (%)	14.3	15.1	(76bps)	15.0	(70bps)	14.8	15.2	(39bps)
Depreciation and amortization	283	217	30.7	278	2.0	1,081	891	21.4
EBIT	650	1,013	(35.8)	835	(22.2)	3,078	3,604	(14.6)
EBIT Margin (%)	10.0	12.4	(245bps)	11.3	(130bps)	11.0	12.2	(123bps)
Net Interest expenses	49	33	50.8	48	1.9	195	156	25.1
Other non-operating inc (exp), net	69	65	6.0	51	34.9	242	180	33.9
Earnings before tax	670	1,045	(35.9)	838.4	(20.1)	3,125	3,629	(13.9)
Income taxes	182	362	(49.8)	226	(19.4)	589	1,293	(54.4)
Earnings after tax	488	683	(28.5)	613	(20.3)	2,535	2,336	8.5
Extraordinary items	0	14	-	0	-	0	48	(100.0)
Minority interest (expense) income	(8)	9	(189.5)	(3)	175.0	(18)	22	(182.6)
Reported Net income (loss)	496	660	(24.9)	615.4	(19.4)	2,553	2,266	12.7

Source: Company, BOBCAPS Research

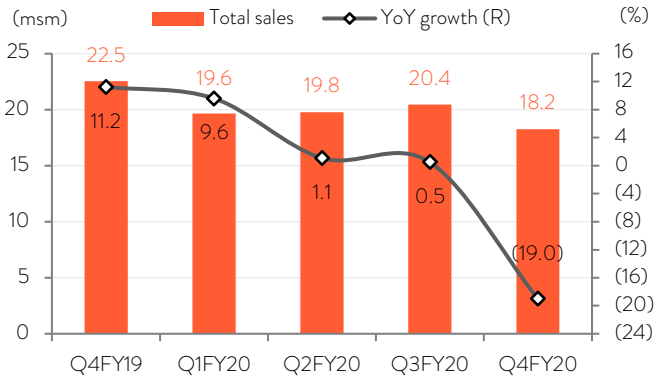
FIG 2 – SEGMENTAL RESULTS

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
Segment Revenues								
Tiles	6,051	7,552	(19.9)	6,837	(11.5)	26,049	27,545	(5.4)
Other	469	601	(22.0)	576	(18.6)	2,032	2,017	0.7
Total revenues	6,520	8,153	(20.0)	7,413	(12.0)	28,080	29,562	(5.0)
Segment Results								
Tiles	669.7	1,009.9	(33.7)	850	(21.2)	3,156.8	3,638.6	(13.2)
Other	(19.4)	2.7	NA	(14.5)	NA	(78.7)	(34.3)	NA
Total	650	1,013	(35.8)	836	(22.2)	3,078	3,604	(14.6)
Segmental Margins								
Tiles	11.1	13.4	(231bps)	12.4	(137bps)	12.1	13.2	(109bps)
Other	(4.1)	0.4	(458bps)	(2.5)	(162bps)	(3.9)	(1.7)	(217bps)

Source: Company, BOBCAPS Research

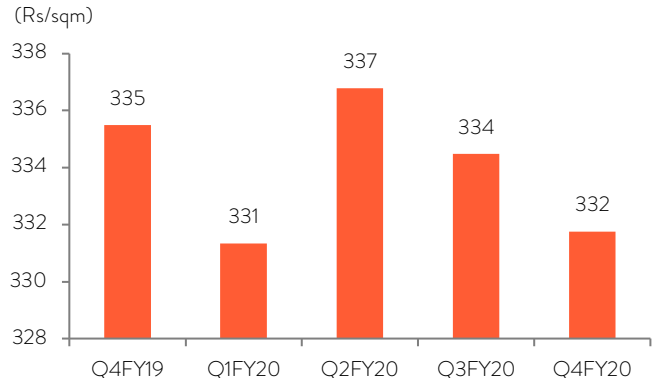
QUARTERLY TRENDS

FIG 3 – VOLUMES



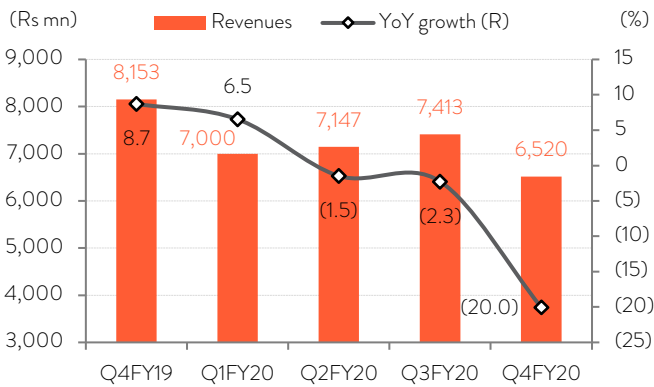
Source: Company, BOBCAPS Research

FIG 4 – NET REALISATIONS



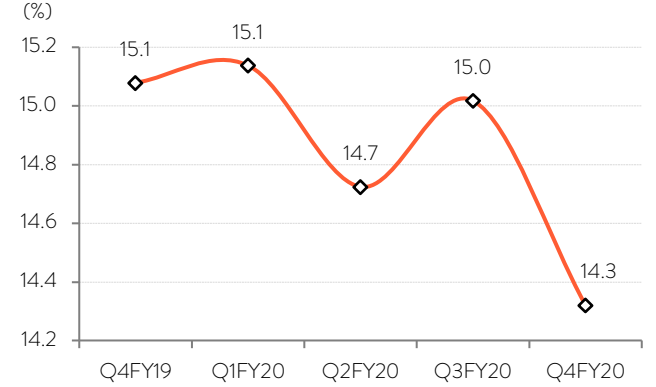
Source: Company, BOBCAPS Research

FIG 5 – REVENUES



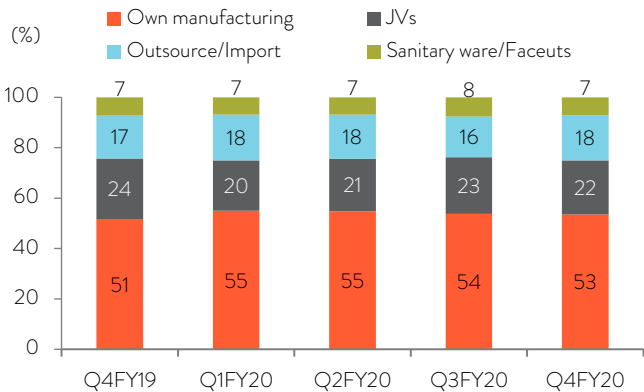
Source: Company, BOBCAPS Research

FIG 6 – EBITDA MARGIN



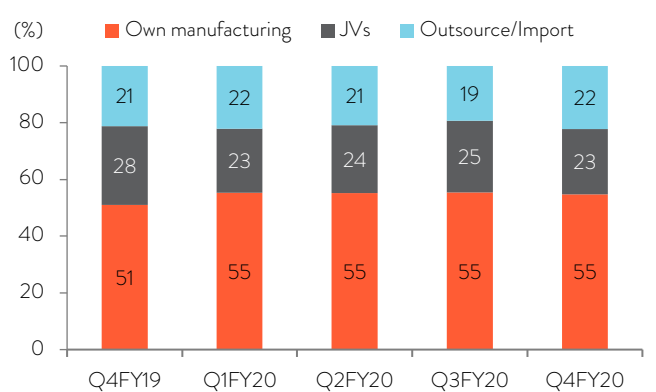
Source: Company, BOBCAPS Research

FIG 7 – REVENUE BREAKUP



Source: Company, BOBCAPS Research

FIG 8 – TILE VOLUME BREAKUP



Source: Company, BOBCAPS Research

Valuation methodology

KJC is the largest organised player in the Indian tiles market, with an organised market share of ~22% (~10.6% of the total market). Unorganised players currently comprise ~50% of the Rs 270bn tiles market. We expect the company to benefit from the gradual formalisation of demand post-GST and e-way bill implementation, given its strong brand, wide distribution reach and market leadership.

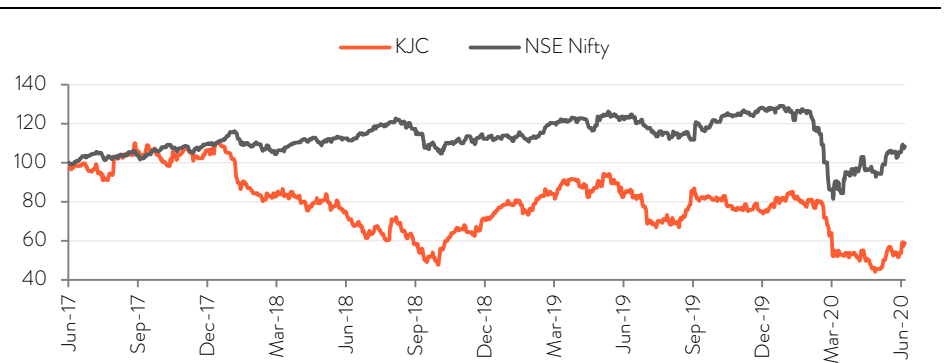
However, given the tepid FY20 performance and challenging demand climate, we prune FY21/FY22 earnings estimates by 9%/1%. Current valuations of 24.9x FY22E EPS offer limited upside, leading us to downgrade the stock from BUY to ADD. We retain our Mar'21 target price at Rs 425, set at an unchanged 26x FY22E P/E.

FIG 9 – REVISED ESTIMATES

(Rs mn)	New		Old		Change (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Revenue	22,857	28,158	24,838	30,464	(8.0)	(7.6)
EBITDA	3,005	4,420	3,398	4,685	(11.5)	(5.7)
PAT	1,551	2,565	1,702	2,578	(8.9)	(0.5)

Source: Company, BOBCAPS Research

FIG 10 – 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 this along could adversely affect KJC's profitability.
- **Increased competition from informal sector:** Higher competition from the informal sector primarily based out of Morbi, Gujarat, can hurt profitability.
- **Prolonged Covid-19 outbreak:** If pandemic fears 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
Total revenue	27,106	29,562	28,080	22,857	28,158
EBITDA	4,564	4,495	4,159	3,005	4,420
Depreciation	(885)	(891)	(1,081)	(1,113)	(1,182)
EBIT	3,678	3,604	3,078	1,892	3,237
Net interest income/(expenses)	(241)	(156)	(195)	(152)	(90)
Other income/(expenses)	108	180	242	249	268
Exceptional items	8	(48)	0	0	0
EBT	3,546	3,629	3,125	1,988	3,416
Income taxes	(1,267)	(1,293)	(589)	(457)	(861)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	64	(22)	18	20	10
Reported net profit	2,350	2,266	2,553	1,551	2,565
Adjustments	(8)	48	0	0	0
Adjusted net profit	2,342	2,314	2,553	1,551	2,565

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Accounts payables	2,398	2,890	2,105	1,863	2,003
Other current liabilities	2,153	2,211	2,311	2,154	1,753
Provisions	179	200	288	313	338
Debt funds	1,351	949	1,171	471	221
Other liabilities	1,151	1,073	731	746	771
Equity capital	159	159	159	159	159
Reserves & surplus	13,351	15,590	16,984	18,215	20,011
Shareholders' fund	13,510	15,749	17,143	18,374	20,170
Total liabilities and equities	21,403	23,732	24,386	24,538	25,864
Cash and cash eq.	824	2,524	2,350	4,376	4,379
Accounts receivables	4,507	4,751	3,967	3,632	4,320
Inventories	3,785	4,058	5,127	4,133	4,937
Other current assets	574	581	640	689	694
Investments	4	3	3	3	3
Net fixed assets	11,311	10,671	11,854	11,498	11,316
CWIP	176	934	257	0	0
Intangible assets	140	107	103	103	103
Deferred tax assets, net	82	103	85	105	112
Other assets	0	0	0	0	0
Total assets	21,403	23,732	24,386	24,538	25,864

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Net income + Depreciation	4,431	4,519	4,205	3,102	4,598
Interest expenses	241	156	195	152	90
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(1,251)	48	(943)	906	(1,733)
Other operating cash flows	(1,209)	(1,215)	(986)	(452)	(879)
Cash flow from operations	2,212	3,508	2,472	3,708	2,076
Capital expenditures	(657)	(976)	(1,213)	(500)	(1,000)
Change in investments	0	0	0	0	0
Other investing cash flows	(3)	1	0	0	0
Cash flow from investing	(660)	(975)	(1,213)	(500)	(1,000)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(355)	(402)	222	(700)	(250)
Interest expenses	(241)	(156)	(195)	(152)	(90)
Dividends paid	(572)	(570)	(1,150)	(320)	(770)
Other financing cash flows	(79)	314	(329)	(10)	36
Cash flow from financing	(1,248)	(813)	(1,452)	(1,182)	(1,073)
Changes in cash and cash eq.	304	1,720	(194)	2,026	3
Closing cash and cash eq.	824	2,544	2,350	4,376	4,379

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20P	FY21E	FY22E
Reported EPS	14.8	14.3	16.1	9.8	16.1
Adjusted EPS	14.7	14.6	16.1	9.8	16.1
Dividend per share	3.0	3.0	3.0	1.6	3.9
Book value per share	85.0	99.1	107.9	115.6	126.9

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20P	FY21E	FY22E
EV/Sales	2.4	2.2	2.3	2.7	2.2
EV/EBITDA	14.4	14.4	15.2	20.8	13.9
Adjusted P/E	27.2	27.6	25.0	41.1	24.9
P/BV	4.7	4.0	3.7	3.5	3.2

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20P	FY21E	FY22E
Tax burden (Net profit/PBT)	65.9	64.6	81.7	78.0	75.1
Interest burden (PBT/EBIT)	96.6	99.3	101.5	105.1	105.5
EBIT margin (EBIT/Revenue)	13.6	12.2	11.0	8.3	11.5
Asset turnover (Revenue/Avg TA)	129.7	131.0	116.7	93.4	111.7
Leverage (Avg TA/Avg Equity)	1.7	1.5	1.5	1.4	1.3
Adjusted ROAE	18.5	15.8	15.5	8.7	13.3

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

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
YoY growth (%)					
Revenue	6.5	9.1	(5.0)	(18.6)	23.2
EBITDA	(8.1)	(1.5)	(7.5)	(27.7)	47.1
Adjusted EPS	(7.4)	(1.2)	10.3	(39.3)	65.4
Profitability & Return ratios (%)					
EBITDA margin	16.8	15.2	14.8	13.1	15.7
EBIT margin	13.6	12.2	11.0	8.3	11.5
Adjusted profit margin	8.6	7.8	9.1	6.8	9.1
Adjusted ROAE	18.5	15.8	15.5	8.7	13.3
ROCE	15.9	14.0	13.8	7.6	12.0
Working capital days (days)					
Receivables	53	57	57	61	52
Inventory	72	68	83	101	83
Payables	43	39	38	36	30
Ratios (x)					
Gross asset turnover	1.6	1.7	1.5	1.1	1.4
Current ratio	1.8	2.0	2.1	2.7	3.3
Net interest coverage ratio	15.3	23.1	15.8	12.4	36.1
Adjusted debt/equity	0.0	(0.1)	(0.1)	(0.2)	(0.2)

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

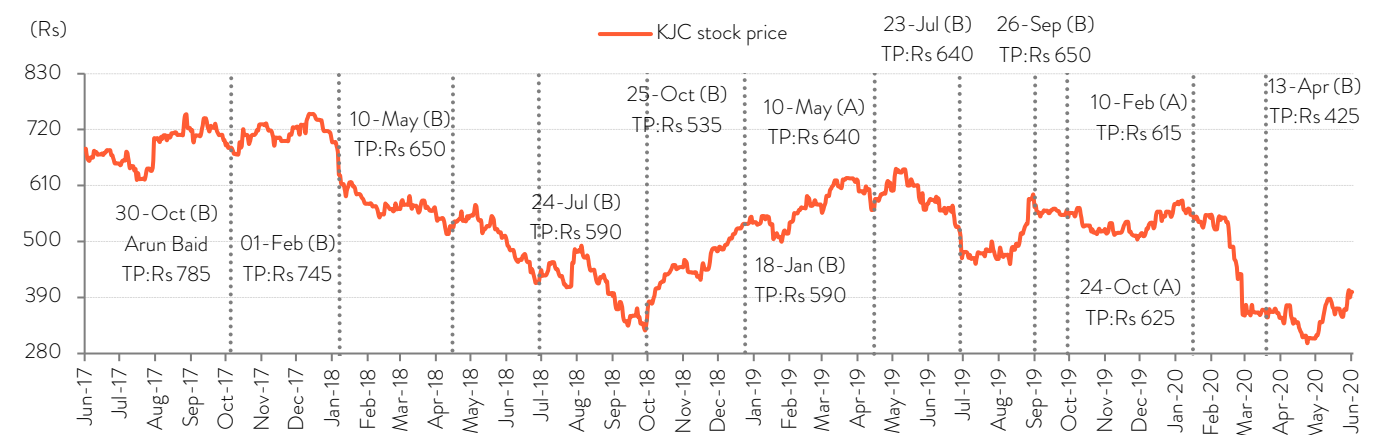
ADD – Expected return from >+5% to +15%

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: KAJARIA CERAMICS (KJC IN)



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

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