

BUY

TP: Rs 990 | ▲ 18%

SOMANY CERAMICS

Construction Materials

12 November 2021

Strong recovery, positive outlook

- Consolidated Q2 revenue grew 32% YoY to Rs 5.6bn with tile volumes up 25% and blended realisation up 6% YoY to Rs 306/msm
- EBITDA margin expanded 50bps YoY to 12.2% as lower employee & other expenses (-265bps) offset higher fuel cost (+295bps)
- Reiterate BUY with rollover to a revised TP of Rs 990 (vs. Rs 820) based on 27x Sep'23E P/E (vs. 22x) on improving business fundamentals

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Robust recovery: SOMC's revenue/EBITDA/PAT grew 15%/23%/100% vs. pre-Covid levels (Q2FY20) on the back of strong underlying demand and healthy real estate launches. Consolidated revenue increased 32% YoY to Rs 5.6bn and gross margin expanded 75bps YoY to 55%. Total fuel cost as a percentage of sales rose 295bps YoY to 20.8% due to rising gas prices, but EBITDA margin expanded 50bps YoY to 12.2% led by a decline in employee cost/other expenses of 80bps/185bps. EBITDA at Rs 682mn grew 38% YoY and adj. PAT was up 71% YoY to Rs 350mn.

Tiles – strong demand, healthy pricing: SOMC reported 25% YoY volume growth in tiles as the demand recovery that began at the end of Q1FY22 continued to firm up in Q2, led by strong offtake from real estate and individual housing. Healthy demand has buoyed the industry's pricing power amid rising fuel cost. Blended realisations rose 6% YoY from Rs 292 in Q1 to Rs 306 in Q2. Further, as Morbi players remained export-focused, the organised pan-India domestic players were able to hike prices to pass on the higher gas cost.

Demand momentum picking up: Management is highly optimistic on business momentum on the back of (a) strong underlying demand, (b) healthy real estate launches, (c) Morbi players' export focus once freight cost normalises, and (d) SOMC's new capacities coming onstream by Feb-Mar'22 which will improve the product mix and add to margins. Management has maintained guidance of 12-13% EBITDA margins in FY22 and expects a further 100-150bps increase in FY23 due to product mix and operating leverage benefits. The company has also guided for 15-20% volume growth and 35-40% growth in the bathware segment in FY22.

Maintain BUY: We lower our FY22/FY23/FY24 PAT estimates by 10%/8%/6% to factor in the higher fuel costs. At the same time, we raise our target P/E multiple from 22x to 27x (a discount to the 33x five-year median) and roll valuations over to Sep'23E. This yields a revised TP of Rs 990 (earlier Rs 820). Our multiple upgrade stems from an improving product mix, demand tailwinds, capital allocation towards the core business and better pricing power. BUY.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	SOMC IN/Rs 842
Market cap	US\$ 479.4mn
Free float	45%
3M ADV	US\$ 0.4mn
52wk high/low	Rs 896/Rs 232
Promoter/FPI/DII	55%/3%/42%

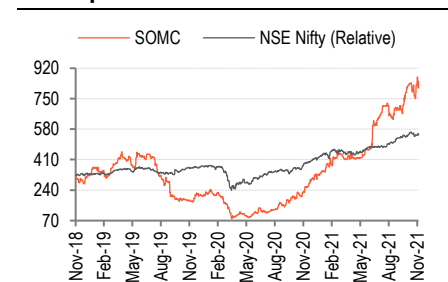
Source: NSE | Price as of 12 Nov 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	16,505	19,830	22,911
EBITDA (Rs mn)	1,908	2,179	2,893
Adj. net profit (Rs mn)	711	870	1,320
Adj. EPS (Rs)	16.8	20.5	31.2
Consensus EPS (Rs)	16.8	24.6	34.7
Adj. ROAE (%)	11.3	12.4	16.2
Adj. P/E (x)	50.2	41.0	27.0
EV/EBITDA (x)	21.1	17.8	13.2
Adj. EPS growth (%)	223.3	22.3	51.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Earnings call highlights

- Increased export-led demand for Morbi-based unorganised players has opened up more opportunities for organised players focusing on the domestic market.
- Management expects gas prices in the northern region to increase from ~Rs 42/sqm currently to ~Rs 48/sqm and in the western region from ~Rs 62/sqm to ~Rs 72/sqm in 3-4 months. In the south, prices have peaked at ~Rs 92/sqm and are expected to cool off in the next one month.
- SOMC has taken a price hike of 7-8% since Apr'21 and is planning another hike in 10-15 days to the tune of ~3%, which should offset the gas cost inflation. Management expects gas prices to soften by Jan'22 as global prices cool off.
- For every gas price hike of Rs 1.5-2/sqm, SOMC takes a 5-6% price increase to mitigate the impact. Gas costs have been increasing every 15 days and the company's price hikes have a lag effect of 15-20 days.
- Indian players cannot shift from LPG-based furnace manufacturing because of a lack of infrastructure and an unviable cost structure.
- Volume and value growth is guided at 15-20% for FY22. Management expects a 12-13% operating margin for FY22 with a further increase of 100-150bps in FY23 as new facilities manufacturing higher value-added products get commissioned. For bathware, management expects 30-40% revenue growth for the next two years and an EBITDA margin of 14-15%.
- SOMC is more focused on profitable exports and will maintain exports at 3-4% of the topline with no increase in share for the next 24 months at least.
- The earlier announced capex of Rs 1.8bn-1.9bn is on track and should be commissioned in Feb-Mar'22. This includes (a) Sudha Ceramics (brownfield capex of Rs 0.4bn, additional capacity of 3.6msm), (b) Kassar plant (brownfield capex of Rs 0.5bn, additional capacity of 3msm), and (c) Somany Piastrelle (greenfield capex of Rs 0.9bn, additional capacity of 3.48msm). The company expects incremental revenue of Rs 3bn from the additional capacities with 100-150bps margin improvement. These projects are expected to be fully operational in FY23 which will help improve the product mix and operating leverage, in our view.
- Capex post FY22 will be routine spends of ~Rs 400mn for a period of 18 months.
- A&P spends was almost nil in Q1FY22 and ~2% of sales in Q2FY22. For FY22/FY23, A&P is planned at 2.5-2.7%/2.75-3%.
- Capacity utilisation in Q2 was at 92% in tiles, 38% in sanitaryware and 90% in faucets. Sanitaryware has reached 100% utilisation at present.
- As per the company, upcoming plants in Morbi (50-60 large GVT plants with 12,000sqm capacity per day) should start operations by Nov-Dec'21. Though these plants will be focused on exports, there may be short-term pressure on tile pricing in the domestic market. However, the impact will be more visible in the private builders' market which is not a focus area for the company and leading industry players given credit concerns.

- There is a 14-15% pricing gap between Kajaria Ceramics (KJC) and SOMC, of which 5-7% is product pricing and the balance is due to product mix. KJC's margins are high on account of proximity to market (~55% of revenue comes from North India), strong brand-led price realisations, economies of scale (40% larger than SOMC) and a better product mix. SOMC's management is working to reduce the gap with KJC.
- SOMC has 2,700 active dealers (vs. ~2,200 in Q4FY21) and will add 300 dealers (net) in FY22 and 300 more in FY23. The additional dealers contributed 3-4% of the H1FY22 topline.
- Non-metros contribute ~80% of the company's revenue and SOMC remains focused on tier-2/3/4/5 towns.
- The domestic market size is Rs 250bn and exports Rs 100bn. As per management, the industry should double from Rs 350bn to Rs 700bn in 7-8 years.
- Tile exports from India currently form 20-21% and are expected to grow to 40-50% in the next decade.
- Replacement demand in India constitutes 15-18% of the market.

Fig 1 – Consolidated quarterly performance

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H1FY22	H1FY21	YoY (%)
Net Revenue	5,607	4,239	32.3	3,299	70.0	8,907	5,933	50.1
CQGS	3,689	2,697	36.8	2,031	81.6	5,720	3,971	44.0
% of sales	65.8	63.6	217bps	61.6	423bps	64.2	66.9	(271bps)
Employee expenses	645	522	23.5	601	7.4	1,246	895	39.2
% of sales	11.5	12.3	(81bps)	18.2	(670bps)	14.0	15.1	(109bps)
Other Expenses	591	525	12.4	437	35.2	1,028	689	49.2
% of sales	10.5	12.4	(186bps)	13.2	(270bps)	11.5	11.6	(7bps)
EBITDA	682	494	38.0	231	195.4	913	378	141.4
EBITDA Margin (%)	12.2	11.7	50bps	7.0	517bps	10.3	6.4	388bps
Depreciation/Amortisation	161	150	7.3	151	7.2	312	295	5.6
EBIT	521	344	51.4	80	548.0	601	83	625.5
EBIT Margin (%)	9.3	8.1	117bps	2.4	685bps	6.8	1.4	535bps
Net Interest Expenses	78	98	(20.8)	81	(3.7)	159	214	(25.7)
Other Income	38	40	(5.4)	56	(31.7)	94	59	58.7
PBT	481	286	68.1	56	767.4	537	(71)	(853.0)
Tax Expenses	128	73	74.1	16	682.8	144	(21)	(798.5)
Net Income before minority interest & extraordinary items	354	213	66.1	39	802.6	393	(51)	(875.1)
Minority Interest and Income from associates	(4)	(8)	(50.6)	10	(139.4)	6	36	(83.3)
Exceptional items	0	(0)	-	(4)	-	(4)	(0)	-
Reported Net Income	350	205	70.7	45	682.8	395	(15)	(2748.3)

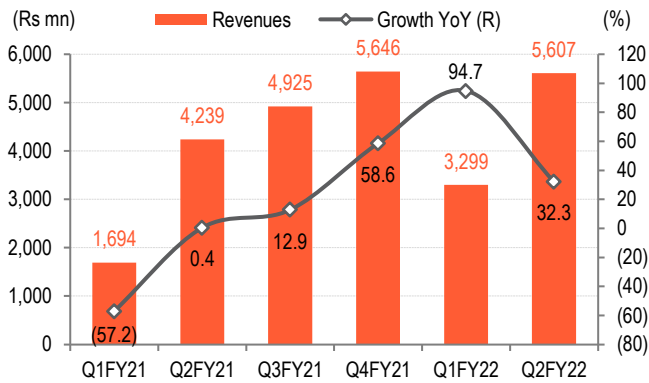
Source: Company, BOBCAPS Research

Fig 2 – Standalone quarterly performance

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H1FY22	H1FY21	YoY (%)
Net Revenue	5,575	4,205	32.6	3,255	71.2	8,830	5,896	49.8
CQGS	4,072	3,067	32.8	2,343	73.8	6,415	4,426	44.9
% of sales	73.0	72.9	11bps	72.0	109bps	72.6	75.1	(243bps)
Employee expenses	469	359	30.7	441	6.4	910	652	39.5
% of sales	8.4	8.5	(12bps)	13.5	(513bps)	10.3	11.1	(76bps)
Other Expenses	468	407	15.0	328	42.9	796	545	46.0
% of sales	8.4	9.7	(129bps)	10.1	(167bps)	9.0	9.2	(23bps)
EBITDA	565	372	51.9	144	291.7	710	272	160.7
EBITDA Margin (%)	10.14	8.85	129bps	4.43	571bps	8.04	4.62	342bps
Depreciation/Amortisation	119	108	10.2	108	9.3	227	210	8.0
EBIT	447	265	68.9	36	1144.3	483	62	677.1
EBIT Margin (%)	8.0	6.3	172bps	1.1	691bps	5.5	1.1	441bps
Net Interest Expenses	22	36	(37.7)	23	(2.2)	45	90	(50.2)
Other Income	54	42	30.1	65	(16.4)	119	69	72.9
PBT	479	271	76.9	78	514.4	557	41	1257.3
Tax Expenses	129	69	86.7	20	545.0	149	11	1279.6
Net Income before extraordinary items	350	201	73.6	58	503.8	408	30	1249.3
Exceptional items	0	0	-	0	-	0	0	-
Reported Net Income	350	201	73.6	58	503.8	408	30	1249.3

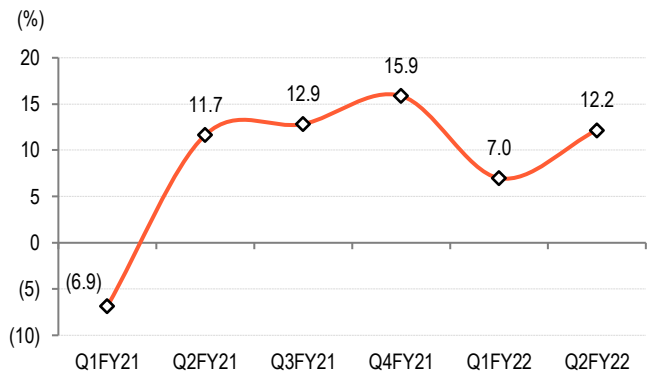
Source: Company, BOBCAPS Research

Fig 3 – Consolidated revenue growth



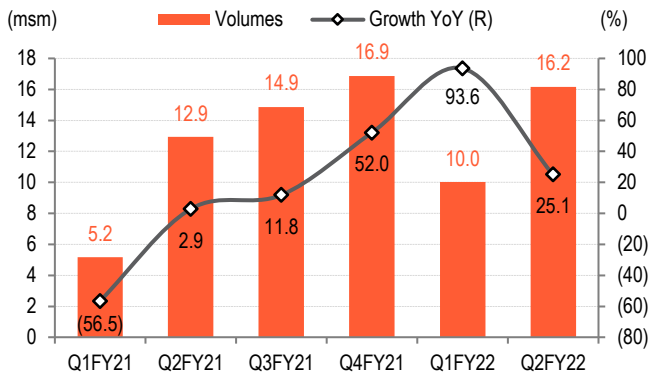
Source: Company, BOBCAPS Research

Fig 4 – Consolidated EBITDA margin



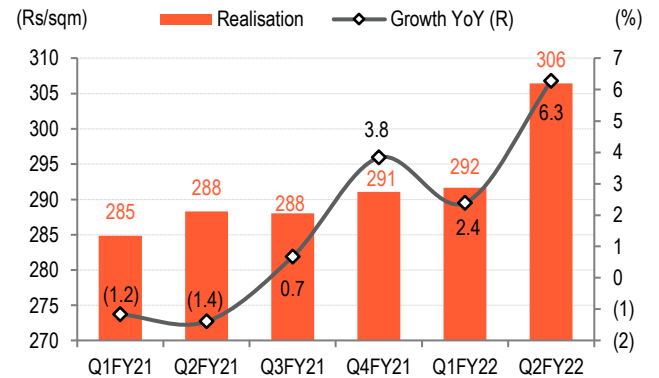
Source: Company, BOBCAPS Research

Fig 5 – Tile volume growth



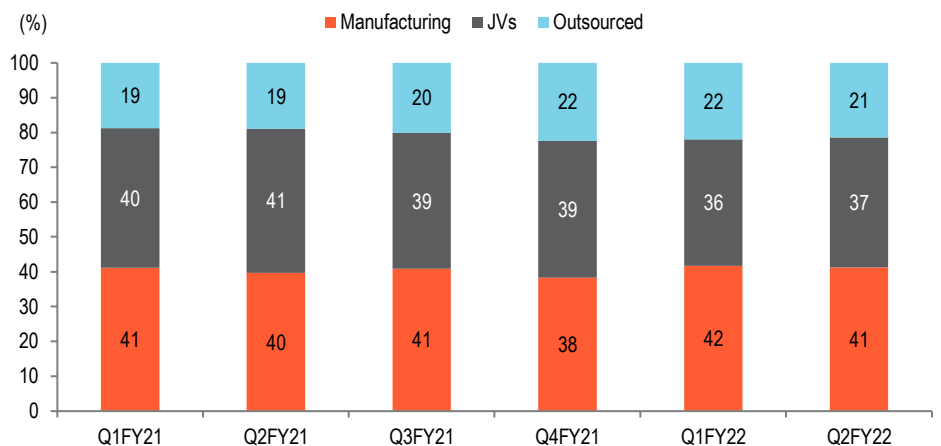
Source: Company, BOBCAPS Research

Fig 6 – Tile realisation growth



Source: Company, BOBCAPS Research

Fig 7 – Revenue breakup



Source: Company, BOBCAPS Research

Valuation methodology

We lower our FY22/FY23/FY24 PAT estimates by 10%/8%/6% to factor in the higher fuel costs. At the same time, we raise our target P/E from 22x to 27x (a discount to the 33x five-year median) with rollover to Sep'23E valuations, given an improving product mix, demand tailwinds, capital allocation towards the core business and better pricing power. Despite a higher capex outgo, we expect working capital discipline and healthy operating profits to keep the balance sheet in check during FY22-FY24.

SOMC is currently trading at 27x FY23E EPS and we believe it can sustain these multiples owing to its improving business fundamentals and operating leverage-led earnings growth. In addition, the new construction activity yet to kick-in and organized players like SOMC will be in the fore-front to benefit from the space vacated by the unorganized players. Maintain BUY.

Fig 8 – Revised estimates

(Rs mn)	New			Old			Change (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	19,830	22,911	26,506	19,467	22,781	26,374	1.9	0.6	0.5
EBITDA	2,179	2,893	3,564	2,315	3,031	3,781	(5.9)	(4.6)	(5.7)
EBITDA %	11.0	12.6	13.4	11.9	13.3	14.3	(90bps)	(70bps)	(90bps)
PAT	870	1,320	1,781	966	1,436	1,991	(9.9)	(8.1)	(5.7)
EPS	20.5	31.2	42.0	22.8	33.9	47.0	(10.1)	(8.0)	(10.6)

Source: BOBCAPS Research

Fig 9 – Key assumptions

Particulars	FY21	FY22E	FY23E	FY24E
Tile Volume (msm)	49.8	56.3	64.0	73.1
Growth (%)	2.0	13.0	13.7	14.1
Realisation (Rs/sqm)	288.9	303.7	304.2	307.3
Growth (%)	0.7	5.1	0.2	1.0
Tile Revenues (Rs mn)	14,397	17,111	19,482	22,48
Growth (%)	2.5	22.2	15.5	15.7
Bathware (Rs mn)	1,648	2,224	2,892	3,470
Growth (%)	(3.3)	35.0	30.0	20.0

Source: Company, BOBCAPS Research

Fig 10 – 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	990	17.8	20.5	31.2	12.4	16.2	27
Greenply Ind	MTLM IN	HOLD	230	18.7	9.2	11.3	23.0	22.9	20
Greenpanel Industries	GREENP IN	HOLD	395	27.6	14.1	18.3	21.1	22.1	20
Century Plyboard	CPBI IN	HOLD	630	19.5	12.1	15.1	19.9	20.5	37
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 downside risks to our estimates are:

- **Higher raw material prices:** Any abnormal increase in prices of key raw materials, such as gas, coupled with an inability to pass these along could adversely affect SOMC's profitability.
- **Increased competition from informal sector:** E-way bill implementation, if executed poorly as is currently the case, may allow competition from the unorganised sector to increase, affecting growth prospects.
- **Housing market slowdown:** A slowdown in the housing market will hinder demand for the company's products.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Century Plyboards	CPBI IN	2.0	679	630	HOLD
Cera Sanitaryware	CRS IN	0.9	5,415	5,895	HOLD
Greenpanel Industries	GREENP IN	0.7	399	395	HOLD
Greenply Industries	MTLM IN	0.4	230	210	HOLD
Kajaria Ceramics	KJC IN	2.5	1,194	1,393	HOLD
Pidilite Industries	PIDI IN	16.6	2,426	2,080	SELL
Somany Ceramics	SOMC IN	0.5	842	990	BUY

Source: BOBCAPS Research, NSE | Price as of 12 Nov 2021

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	16,030	16,505	19,830	22,911	26,506
EBITDA	1,299	1,908	2,179	2,893	3,564
Depreciation	(589)	(613)	(676)	(769)	(813)
EBIT	709	1,294	1,503	2,123	2,751
Net interest inc./(exp.)	(494)	(401)	(345)	(303)	(254)
Other inc./(exp.)	125	128	134	141	148
Exceptional items	0	0	0	0	0
EBT	339	1,021	1,292	1,961	2,645
Income taxes	112	(229)	(326)	(494)	(667)
Extraordinary items	(256)	(180)	0	0	0
Min. int./Inc. from assoc.	(45)	(36)	(97)	(147)	(198)
Reported net profit	150	577	870	1,320	1,781
Adjustments	70	134	0	0	0
Adjusted net profit	220	711	870	1,320	1,781

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	1,729	1,882	2,133	2,497	2,890
Other current liabilities	1,347	1,602	1,653	1,872	2,168
Provisions	98	120	136	159	185
Debt funds	4,981	4,120	3,720	3,020	2,620
Other liabilities	413	372	372	372	372
Equity capital	85	85	85	85	85
Reserves & surplus	5,980	6,469	7,395	8,772	10,681
Shareholders' fund	6,064	6,553	7,480	8,857	10,766
Total liab. and equities	15,573	15,646	16,599	18,041	20,485
Cash and cash eq.	173	1,491	217	516	1,805
Accounts receivables	2,798	2,307	2,933	3,433	3,974
Inventories	3,282	2,446	3,360	3,932	4,552
Other current assets	1,085	799	1,120	1,311	1,517
Investments	341	898	0	0	0
Net fixed assets	7,737	7,546	8,640	8,421	8,158
CWIP	60	86	86	86	86
Intangible assets	42	22	22	22	22
Deferred tax assets, net	54	50	50	50	50
Other assets	0	0	0	0	0
Total assets	15,573	15,646	16,429	17,771	20,165

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash flow from operations	1,447	3,634	456	1,895	2,415
Capital expenditures	(664)	(414)	(1,770)	(550)	(550)
Change in investments	341	(557)	898	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(323)	(970)	(872)	(550)	(550)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(750)	(861)	(400)	(700)	(400)
Interest expenses	(494)	(401)	(345)	(303)	(254)
Dividends paid	(204)	(102)	(147)	(218)	(303)
Other financing cash flows	38	17	107	160	221
Cash flow from financing	(1,411)	(1,347)	(785)	(1,062)	(735)
Chg in cash & cash eq.	(287)	1,317	(1,200)	283	1,129
Closing cash & cash eq.	173	1,491	290	500	1,645

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	3.5	13.6	20.5	31.2	42.0
Adjusted EPS	5.2	16.8	20.5	31.2	42.0
Dividend per share	2.0	2.4	3.0	4.4	6.1
Book value per share	143.1	154.6	176.5	209.0	254.0

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	2.5	2.4	2.0	1.7	1.5
EV/EBITDA	30.8	21.1	17.8	13.2	10.9
Adjusted P/E	162.2	50.2	41.0	27.0	20.0
P/BV	5.9	5.4	4.8	4.0	3.3

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	64.8	69.7	67.3	67.3	67.3
Interest burden (PBT/EBIT)	47.9	78.9	86.0	92.4	96.2
EBIT margin (EBIT/Revenue)	4.4	7.8	7.6	9.3	10.4
Asset turnover (Rev./Avg TA)	99.6	105.7	123.6	134.0	139.7
Leverage (Avg TA/Avg Equity)	2.6	2.5	2.3	2.1	1.9
Adjusted ROAE	3.6	11.3	12.4	16.2	18.1

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	(6.3)	3.0	20.1	15.5	15.7
EBITDA	(17.6)	46.9	14.2	32.7	23.2
Adjusted EPS	(55.1)	223.3	22.3	51.8	34.9
Profitability & Return ratios (%)					
EBITDA margin	8.1	11.6	11.0	12.6	13.4
EBIT margin	4.4	7.8	7.6	9.3	10.4
Adjusted profit margin	1.4	4.3	4.4	5.8	6.7
Adjusted ROAE	3.6	11.3	12.4	16.2	18.1
ROCE	5.7	8.5	9.4	12.5	14.7
Working capital days (days)					
Receivables	79	56	48	51	51
Inventory	105	99	83	91	91
Payables	46	45	42	42	43
Ratios (x)					
Gross asset turnover	1.9	1.8	1.9	2.0	2.2
Current ratio	1.2	1.1	1.2	1.4	1.7
Net interest coverage ratio	1.4	3.2	4.4	7.0	10.8
Adjusted debt/equity	0.8	0.4	0.5	0.3	0.1

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

Disclaimer

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

BUY – Expected return >+15%

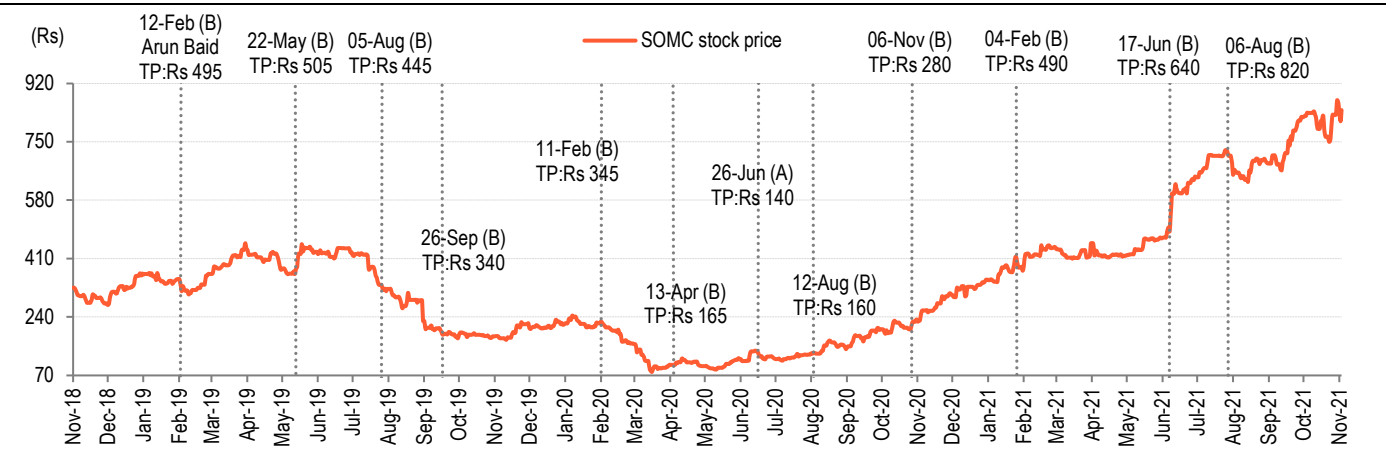
HOLD – Expected return from -6% to +15%

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): SOMANY CERAMICS (SOMC IN)



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

Rating distribution

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