

Q2FY21 result review
and reco change

Tiles

Target price: Rs700

Earnings revision

(%)	FY21E	FY22E
Sales	↑ 3.7	↑ 3.0
EBITDA	↑ 22.9	↑ 9.9
PAT	↑ 31.7	↑ 13.2

Target price revision

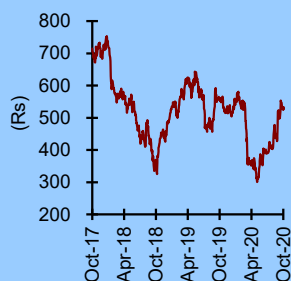
Rs700 from Rs530

Shareholding pattern

	Mar '10	Jun '10	Sep '10
Promoters	47.6	47.6	47.6
Institutional investors	38.0	38.8	40.0
MFs and others	14.5	16.5	15.0
FIs/Banks	0.0	0.0	0.0
Insurance	0.1	0.1	1.4
FII	23.4	22.2	23.6
Others	14.4	13.2	12.4

Source: NSE

Price chart



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INDIA

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Kajaria Ceramics

BUY

Upgrade from Hold

A roaring comeback; upgrade to BUY

Rs575

Kajaria Ceramics (KJC) makes a roaring comeback in Q2FY21 with 100%+ volume recovery (vs its guidance of 80%+ post Q1 result) and 20%+ EBITDA margin (vs 14-15% consensus estimates and I-Sec: 16.4%). This was largely driven by market share gains from Morbi players and aggressive cost control measures undertaken by KJC post Covid-19 outbreak. Key takeaways from Q2FY21 result conference call: a) Sustainance of double-digit growth in Oct'20 as well after 15% growth witnessed in Sep'20; and b) 18%+ EBITDA margin in the near term driven by operating leverage, superior product mix, stable product pricing and benign fuel costs, and certain cost-cutting initiatives are likely to sustain. With pricing and demand headwinds for branded tile players turning their heads around post Covid-19, we expect KJC's earnings momentum to sustain in the near term. Upgrade to BUY.

- **Valuations and risks:** Factoring in better than expected volume recovery and EBITDA margin in higher teens, we increase our revenue and earnings estimates by 3.7% / 3.0% and 31.7% / 13.2% for FY21/FY22, respectively. With this, we expect KJC to report 3.9%/12.5% revenue/PAT CAGR over FY20-FY22E. We upgrade the stock to **BUY** (from HOLD earlier) with a revised target price of Rs700 (earlier: Rs530) based on 35x FY22E earnings (from 30x earlier). We believe 35x P/E multiple is justifiable considering sustainable pricing and demand tailwinds on offer for top branded players in the near term and expected sharp improvement (by 820bps to 26%) in KJC's RoCEs (adjusted for cash) over the next two years.
- **Market share gains and stable pricing drive flat revenues YoY:** KJC posted mere 0.3% YoY decline in revenues in Q2FY21 to Rs7.13bn (I-sec: Rs6.58bn) driven by market share gains from Morbi players in tiles and 24% growth in bathware products. Tile realisations, however, were down 2.4% YoY due to adverse product (higher volumes of lower format tiles) mix in particular. Considering demand tailwind to sustain and realisations to improve in near term with expected higher penetration of GVT going forward, we model 1.6% / 3.9% volume / revenue CAGRs over FY20-FY22E, respectively.
- **Lower overheads and stable fuel costs push EBITDA margin to 4-year high:** KJC's EBITDA margin for the quarter surprised positively at 20.2% driven by operating leverage, superior product mix, stable product pricing, benign fuel costs, and cost cutting initiatives undertaken post Covid-19. Despite the expected reversal of recent salary cuts and likely higher A&P spends in H2FY21, KJC has guided for sustainable 18%+ margins in the near term. This, we believe, is achievable due to likely improvement in its product mix, expected higher utilisation of its South India plant, operating leverage and (certain) sustainable cost cutting measures. We model in 16.4%/17.6% EBITDA margin for KJC for FY21E / FY22E, respectively.
- **Cash on books piles up to Rs3.58bn:** Strong FCF generation driven by firm cash collections and muted capex in H1FY21 drives its cash and cash equivalents higher to Rs3.58bn as on Sep'20. The management expects this to be deployed partly by way of capex and balance by a one-time dividend or a buy-back in near-medium term.

Market Cap	Rs91bn/US\$1.2bn	Year to Mar	FY19	FY20	FY21E	FY22E
Reuters/Bloomberg	KAJR.BO/KJC IN	Revenue (Rs mn)	29,562	28,080	25,834	30,300
Shares Outstanding (mn)	159.0	Rec. Net Income (Rs mn)	2,297	2,553	2,410	3,180
52-week Range (Rs)	580/300	EPS (Rs)	14.6	14.3	15.2	20.0
Free Float (%)	52.4	% Chg YoY	(1.2)	(2.0)	6.2	32.0
FII (%)	23.6	P/E (x)	39.5	40.3	37.9	28.8
Daily Volume (US\$/'000)	2,802	CEPS (Rs)	19.9	22.9	22.2	27.7
Absolute Return 3m (%)	47.0	EV/E (x)	20.0	21.7	20.7	16.1
Absolute Return 12m (%)	4.7	Dividend Yield (%)	0.5	0.5	0.7	0.9
Sensex Return 3m (%)	8.5	RoCE (%)	21.2	17.3	15.8	19.2
Sensex Return 12m (%)	4.3	RoE (%)	15.1	13.3	12.9	15.5

Please refer to important disclosures at the end of this report

Table 1: Q2FY21 result review*(Rs mn, year ending March 31)*

Particulars	Q2FY21A	Q2FY21E	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
Net Sales	7,125	6,575	7,147	(0.3)	2,776	156.7	9,901	14,147	(30.0)
Total Op. Income	7,125	6,575	7,147	(0.3)	2,776	156.7	9,901	14,147	(30.0)
Expenditure	5,688	5,495	6,095	(6.7)	2,851	99.5	8,540	12,035	(29.0)
Raw Materials	1,999	1,590	1,723	16.0	1,185	68.7	3,184	3,401	(6.4)
Cost of traded goods	990	1,090.0	1,183	(16.4)	590.4	67.6	1,580	2,311	(31.6)
Staff Cost	779	750	888	(12.3)	608	28.0	1,387	1,771	(21.7)
Other Expenditure	1,921	2,065	2,300	(16.5)	467	311.1	2,388	4,553	(47.5)
Operating Profit	1,437	1,080	1,052	36.5	(76)	(1,998.2)	1,361	2,112	(35.5)
OPM (%)	20.2	16.4	14.7	550bps	(2.7)	NA	13.7	14.9	-120bps
Other Income	48	50	68	(29.8)	26.2	82.8	74	121	(38.8)
Interest	21	40	52	(60.2)	34	(38.5)	55	97	(43.9)
Depreciation	274	275	262	4.6	252	8.5	526	520	1.2
Exceptional income	0	0	0		0		0	0	
PBT	1,190	815	807	47.5	(336)	(454.8)	855	1,616	(47.1)
Tax	294	205	(124)	(337.3)	(6)	(4,919.7)	288	181	58.7
PAT	896	610	931	(3.7)	(329)	(372.1)	567	1,435	(60.5)
Minority Interest	5.2	(15.0)	(1)	(533.3)	(58.4)	(108.9)	(53)	(8)	609.3
Reported PAT	891	625	932	(4.4)	(271)	(428.9)	620	1,442	(57.0)
NPM (%)	12.5	9.5	13.0	-50bps	(9.8)	NA	6.3	10.2	-390bps

Source: Company data, I-Sec research

Table 2: Volume growth sourcing-wise*(mn-sqm)*

	Q2FY21A	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
Own manufacturing	11.4	11.1	3.0	4.0	185.0	15.4	22.0	-29.7
Joint ventures	4.2	4.5	-7.7	1.7	143.6	5.9	9.0	-34.1
Third-party outsourcing	4.2	4.1	1.7	1.9	116.6	6.1	8.5	-27.8
Total	19.8	19.8	0.3	7.7	158.5	27.5	39.4	-30.3

Source: Company data, I-Sec research

Table 3: Revenue growth sourcing-wise*(Rs mn)*

	Q2FY21A	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
Own manufacturing	3,823.9	3,977.3	(3.9)	1,564.0	144.5	5,387.9	7,819.4	(31.1)
Joint ventures	1,475.8	1,436.5	2.7	442.3	233.7	1,918.1	2,837.2	(32.4)
Third-party outsourcing	1,210.0	1,237.6	(2.2)	570.7	112.0	1,780.7	2,502.3	(28.8)
Sanitaryware/Faucets	529.5	425.5	24.4	173.9	204.5	703.4	837.3	(16.0)
Total	7,125.1	7,146.8	(0.3)	2,775.6	156.7	9,900.7	14,146.7	(30.0)

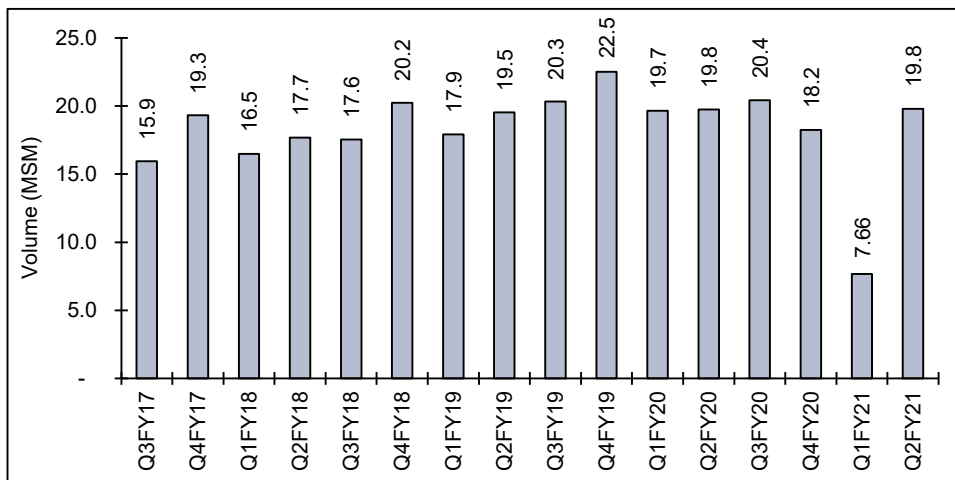
Source: Company data, I-Sec research

Table 4: Change in estimates*(Rs mn)*

	Old		New		% change	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Revenue	24914.2	29418.9	25834.4	30300.3	3.7%	3.0%
EBITDA	3442.9	4840.0	4229.9	5318.3	22.9%	9.9%
EBIDTA margins	13.8%	16.5%	16.4%	17.6%	260bps	110bps
PAT	1829.5	2809.2	2409.6	3179.9	31.7%	13.2%
EPS (Rs)	11.5	17.7	15.2	20.0	31.7%	13.2%

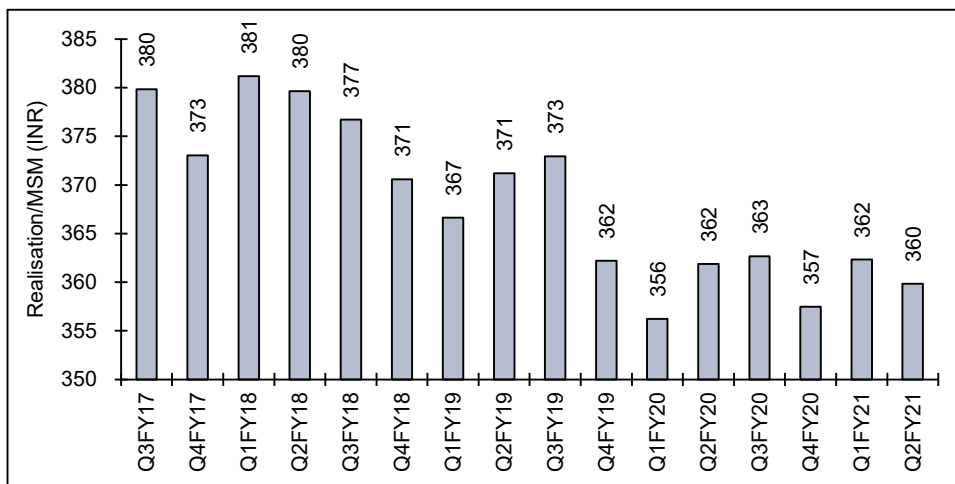
Source: Company data, I-Sec research

Chart 1: Volume trend over the past 16 quarters



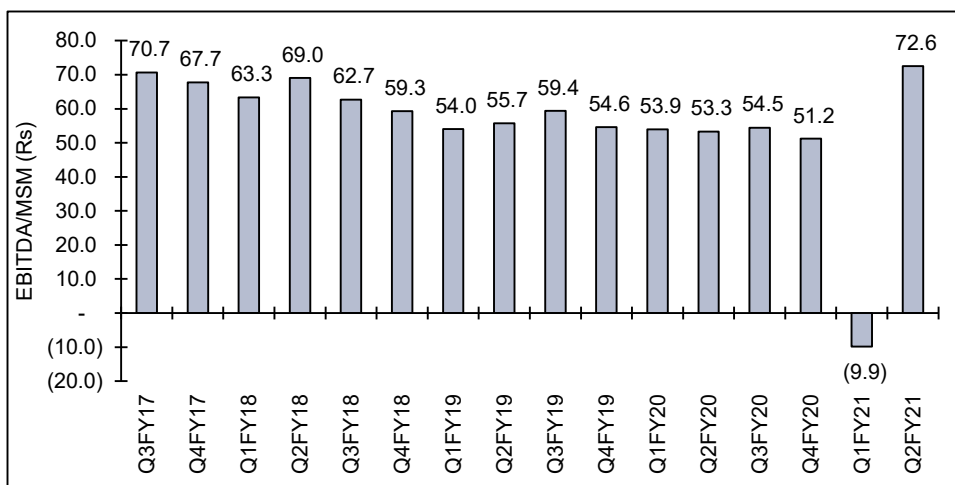
Source: Company data, I-Sec research

Chart 2: Realisation per mn-sqm over the past 16 quarters



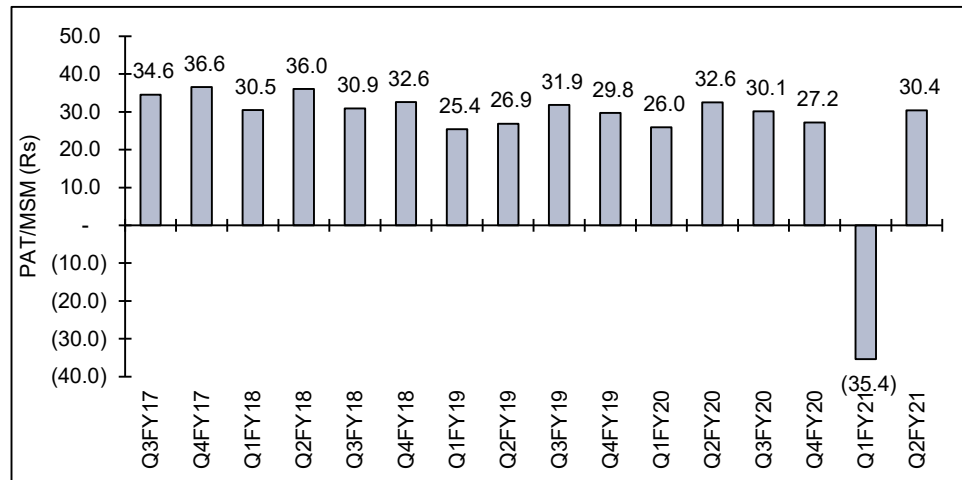
Source: Company data, I-Sec research

Chart 3: EBITDA per mn-sqm over the past 16 quarters



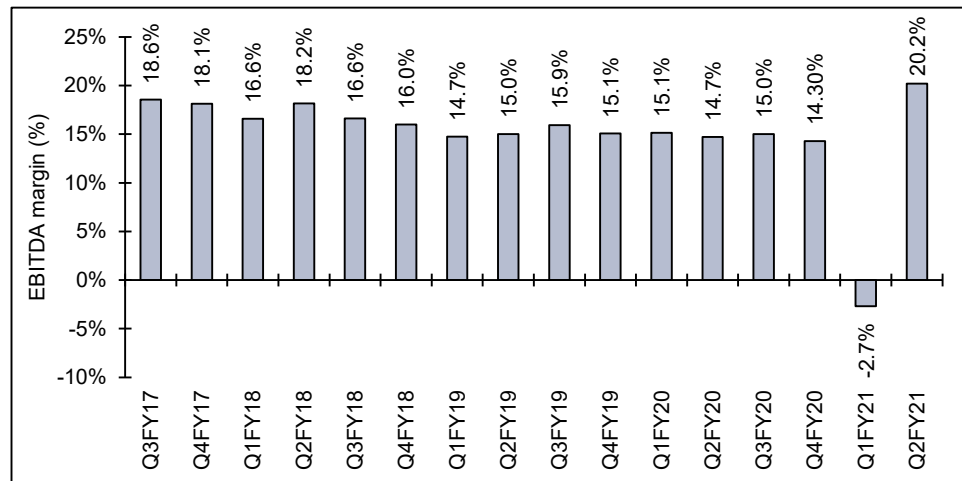
Source: Company data, I-Sec research

Chart 4: PAT per mn-sqm over the past 16 quarters



Source: Company data, I-Sec research

Chart 5: Trend in EBITDA margin (consolidated) over the past 16 quarters



Source: Company data, I-Sec research

Key takeaways from Q2FY21 conference call:

- **Near-term guidance:**
 - **Revenue:** Q3FY21 – flat volumes, Q4FY21 – 10% higher YoY. Post that KJC expects 15% volume growth over the next 2-3 years.
 - **EBITDA margin:** 18%+ consolidated EBITDA margin in H2FY21 and FY22.
- All top branded ceramic tile players have done well in terms of volume recovery in Q2FY21.
- **Q2FY21 revenue recovery:** KJC's revenue recovery month-wise YoY: Jul'20 – 85%, Aug'20 – 100% and Sep'20 – 115%
- The recovery was mainly led by 1) higher sales from tier-2 and below cities/towns (driven by higher sales from showrooms opened in FY20 in these places), 2) growth traction in GVT sales led by higher capacity utilisation at its newly commissioned south India plant, 3) market share gains from Morbi players with these players focusing more on exports and 4) bathware growth of 24.4% YoY due to showrooms addition and new high-end collection range launched during the quarter.
- Company is currently running at full utilisation at all its plants except for the Cosa JV (technology upgradation underway at the moment).
- **Q2FY21 EBITDA margin performance:** Sharp jump in EBITDA margin was mainly led by volume recovery, savings in salary, wages, branding, travelling and softer gas cost.
- While salary cost stands reversed from Oct'20, branding and ad spends are likely to gradually increase in H2FY21. Other savings in travelling and conveyance related costs may sustain in H2FY21 and FY22.
- **Gas cost:** Gas cost is likely to remain benign till Mar'21 as per its interaction with GAIL. KJC does not expect material increase in gas cost from hereon.
- **Pricing** has also remained stable and KJC does not expect prices to fall from here.
- **Revenue mix** – 40% from ceramics, 30% from PVT and 30% from GVT. GVT share is likely to increase to 32% in near term.
- 60% of KJC's sales is attributed to value-added tiles.
- Current market mix: 90% retail and 10% trade
- **Capex** is likely to be in the range of Rs1-1.5bn in FY22.
- **Bathware division** targets revenue of Rs5bn over the next 3-4 years
- **Morbi exports** expected to remain buoyant with shift of USA business from China to India with USA levying 220-300% anti-dumping duty post May'20.
- With regards to ADD imposed by GCC countries on Indian exports, Saudi Arabia and Bahrain have only levied anti-dumping duty so far while others are still importing without ADD from India. Hence, there is only a marginal decline in Morbi's export to GCC countries.
- **Working capital** situation has improved drastically with robust cash collection in H2FY21.

Financial summary

Table 5: Profit & loss statement

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Net Revenues	29,562	28,080	25,834	30,300
Operating Expenses	25,067	23,921	21,605	24,982
EBITDA	4,495	4,159	4,230	5,318
% margins	15.2%	14.8%	16.4%	17.6%
Depreciation & Amortisation	891	1,081	1,121	1,225
Gross Interest	156	195	118	124
Other Income	132	242	192	329
Recurring PBT	3,580	3,125	3,183	4,298
Less: Taxes	1,293	589	802	1,092
Less: Minority Interest	22	(18)	(29)	27
Net Income (Reported)	2,266	2,553	2,410	3,180
Extraordinaries (Net)	(32)	-	-	-
Recurring Net Income	2,297	2,553	2,410	3,180

Source: Company data, I-Sec research

Table 6: Balance sheet

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Assets				
Total Current Assets	12,017	12,071	15,139	17,364
of which cash & cash eqv.	2,524	2,252	5,887	7,547
Total Current Liabilities & Provisions	5,048	4,594	5,044	5,200
Net Current Assets	6,969	7,477	10,095	12,164
Investments	3	101	101	101
Net Fixed Assets	10,694	11,863	11,843	11,868
Capital Work-in-Progress	934	266	-	-
Goodwill	85	85	-	-
Total Assets	18,684	19,792	22,039	24,133
Liabilities				
Borrowings	1,203	1,281	1,850	1,700
Deferred Tax Liability	1,073	731	731	731
Minority Interest	659	637	676	702
Equity Share Capital	159	159	159	159
Face Value per share (Rs)	1	1	1	1
Reserves & Surplus*	15,590	16,984	18,624	20,842
Less: Misc. Exp. n.w.o.				
Net Worth	15,749	17,143	18,783	21,001
Total Liabilities	18,684	19,792	22,039	24,133

*Excluding revaluation reserves

Source: Company data, I-Sec research

Table 7: Quarterly trend

(Rs mn, year ending March 31)

	Dec-19	Mar-20	Jun-20	Sep-20
Net revenues	7,413	6,520	2,776	7,125
% growth (YoY)	-2.3%	-20.0%	-60.3%	-0.3%
EBITDA	1,113	934	(76)	1,437
Margin (%)	15.0	14.3	(2.7)	20.2
Other income	51	69	26	48
Extraordinaries (Net)	-	-	-	-
Net profit	615	496	(271)	891

Source: Company data, I-Sec research

Table 8: Cashflow statement

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Operating Cashflow	3,297	2,819	5,172	4,405
Working Capital Changes	73	(780)	1,017	(409)
Capital Commitments	(568)	(1,350)	(750)	(1,250)
Free Cashflow	2,802	689	5,439	2,746
Cashflow from Investing Activities	1	(98)	-	-
Issue of Share Capital	-	-	(1,641)	-
Inc (Dec) in Borrowings	(500)	78	569	(150)
Dividend paid	(577)	(599)	(731)	(935)
Change in Deferred Tax Liability	(26)	(342)	-	-
Chg. in Cash & Bank balance	1,700	(272)	3,635	1,660

Source: Company data, I-Sec research

Table 9: Key ratios

(Year ending March 31)

	FY19	FY20	FY21E	FY22E
Per Share Data (Rs)				
EPS	14.6	14.3	15.2	20.0
Cash EPS	19.9	22.9	22.2	27.7
Dividend per share (DPS)	3.0	3.0	4.0	5.0
Book Value per share (BV)	103.2	111.8	122.4	136.5
Growth (%)				
Net Sales	9.2	-5.0	-8.0	17.3
EBITDA	-1.5	-7.5	1.7	25.7
PAT	-1.2	-2.0	6.2	32.0
Cash EPS	-2.4	15.1	-2.8	24.8
Valuation Ratios (x)				
P/E	39.5	40.3	37.9	28.8
P/CEPS	29.0	25.2	25.9	20.8
P/BV	5.6	5.1	4.7	4.2
EV / EBITDA	20.0	21.7	20.7	16.1
EV / Sales	3.0	3.2	3.4	2.8
Operating Ratios				
Raw Material / Sales (%)	38.8	39.1	39.5	41.1
Employee cost / Sales (%)	11.7	11.4	14.0	11.6
SG&A / Sales (%)	5.1	10.5	10.0	9.6
Other Income / PBT (%)	0.1	0.1	0.1	0.1
Effective Tax Rate (%)	36.1	26.6	25.2	25.4
Working Capital (days)	70.6	87.1	78.0	65.0
Inventory Turnover (days)	50.1	66.6	58.0	55.0
Receivables (days)	58.7	51.6	60.0	50.0
Payables (days)	38.2	31.1	40.0	40.0
Net D/E Ratio (x)	-0.1	-0.1	-0.2	-0.3
Return/Profitability Ratios (%)				
Net Income Margins	7.8	8.1	9.3	10.5
RoACE	21.2	17.3	15.8	19.2
RoAE	15.1	13.3	12.9	15.5
Dividend Payout	25.4	22.6	31.9	30.3
Dividend Yield	0.5	0.5	0.7	0.9
EBITDA Margins	15.2	14.8	16.4	17.6

Source: Company data, I-Sec research

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