

20 August 2023

India | Equity Research | Sector Update

## Tiles and Sanitaryware

### Margin uptrend to continue as input prices remain benign

Kajaria Ceramics (KJC) and Somany Ceramics (SOMC) have reported volume growth of 7.2% YoY and 8.1% YoY in Q1FY24 as tile revenues grew 5.4% and 5.8% YoY, respectively, due to modest demand. Consolidated EBITDA margin for KJC/SOMC was up 67bps/59bps YoY due to lower RM cost (including gas cost). With gas price now stabilising close to its 10-year average (after declining ~84% since Aug'22 peak), margins may normalise going forward. Volumes, too, are expected to improve in H2FY24 as the uptick in real estate market sustains and Morbi's focus remains on exports. In bathware segment, Cera Sanitaryware's (CRS) revenue grew 7.6% YoY, while KJC/SOMC's grew 17.3%/7.7% YoY. CRS' margin in Q1 was up 59bps YoY (due to lower RM cost) and we expect it to remain flat YoY in FY24 as RM pressures have abated. We believe, going forward, the tile industry has margin tailwinds due to lower RM cost and operating leverage, whereas bathware companies may continue to see healthy revenue growth with steady margins. We remain positive on the sector with **ADD** rating on KJC, **BUY** on SOMC and **HOLD** on CRS.

### Tiles volume to grow in double-digit in FY24 for KJC/SOMC

Tile companies under over coverage reported modest demand environment in Q1 as tile volume for KJC/SOMC grew 7.2%/8.1% YoY (4-yr CAGR 6.2%/6.7%) and tile revenue grew 5.4%/5.8% YoY, while realisation declined 1.8%/2.2% YoY (companies partially passed on lower RM cost benefit to dealers). Managements of both the companies remain optimistic of demand improvement in H2FY24. KJC has guided for 13-15% YoY volume growth, while SOMC guided for double-digit volume growth in FY24. We expect KJC/SOMC to have demand tailwinds due to a) continued uptick in real-estate market, b) higher preference for organised players due to strong branding, c) less domestic competitive pressures from Morbi due to its renewed focus on exports as freight rates have normalised and gas cost has also come down. We have modelled tile volume CAGR of 11.7%/11.4% for KJC/SOMC over FY23-26E (vs 7.2%/5.2% over FY18-23).

### Tile margins to continue improving due to lower gas cost

In Q1FY24, operating margins for KJC/SOMC increased 67bps/59bps YoY to 15.9%/8.6% due to lower RM cost (including power & fuel cost). With gas price declining ~84% from its peak in Aug'22 and stabilising close to its 10-year average, margins of organised tile players in FY24 are expected to normalise going ahead. KJC has guided for a consolidated EBITDA margin of 14-16% in FY24, while SOMC has guided for 9.5-10%. We have modelled FY24-FY26E operating margins of 16.4-16.6% for KJC and 10.1-10.4% for SOMC (in line with 10-year average EBITDA margin of 16.6% for KJC and 9.3% for SOMC).

### Bathware segment outlook remains healthy

Bathware revenues in Q1FY24 grew 7.6% YoY (-19.3% QoQ; 4-year CAGR of 15.5%) for CRS, and 17.3%/7.7% YoY for KJC/SOMC. CRS' EBITDA margin expanded 59bps YoY to 16.4% in Q1 due to lower RM cost. We expect demand for bathware to be healthy, driven by home renovation and continued uptick in real estate. CRS management stated it is on-track to achieve its guidance of doubling revenue to ~INR 29bn by Sept'25. It also indicated that current margins are sustainable with an upward bias led by better product mix and a benign raw material environment. We model margins of 16.3-16.5% for CRS over FY24-26E. In FY24, KJC management has guided for revenue growth of 30% YoY, while SOMC has guided for ~22% YoY revenue growth for its bathware segment.

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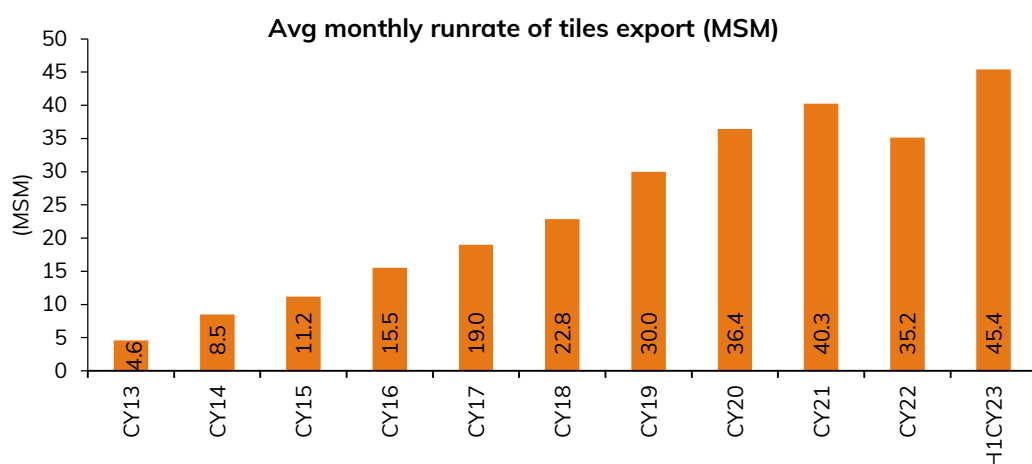
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## Tile exports remain on a strong footing

Exports value grew 26% YoY (as per Gol data) in Apr-Jun'23 quarter whereas domestic tile industry growth was flat YoY (source: KJC Q1FY24 concall). Tile exports continue on a strong footing with volume growth of ~27% YoY (flat QoQ) in Q2CY23 and is expected to remain buoyant in the near term, as per industry participants. Of the total volume exported in Q2CY23, GCC countries accounted for ~15% of exports, followed by USA with ~7% and Iraq accounting for ~5%. Average monthly tile exports are at their historical highest in H1CY23 and are likely to remain so going ahead (aided by normalised freight cost and lower gas prices). Higher exports may reduce the oversupply situation in the domestic tile market and thus moderate pricing pressures and normalise margins for organised players with domestic focus.

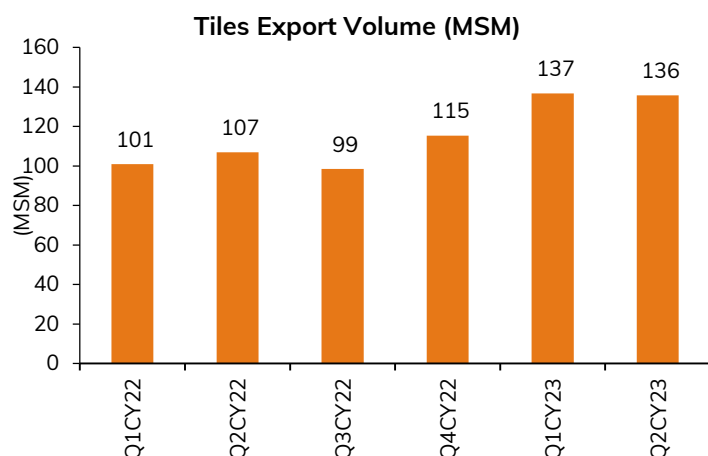
Average monthly tile exports are at their historical highest in H1CY23

### Exhibit 1: Average monthly tile export volumes from India



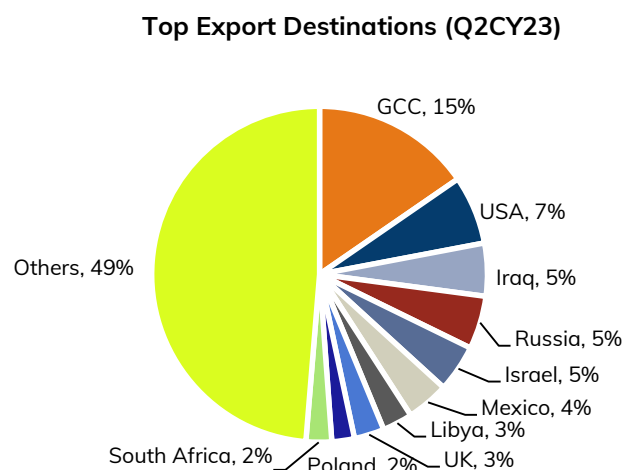
Source: Ceramic World Review, Gol, I-Sec research

### Exhibit 2: Quarterly tile export volumes



Source: Gol, I-Sec research

### Exhibit 3: Top tile export destinations from India



Source: Gol, I-Sec research

#### Exhibit 4: Q1FY24 for tiles and sanitaryware

	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)
<b>Kajaria Ceramics</b>					
<b>Segmental</b>					
<b>Revenue (INR mn)</b>					
Tiles	9,662	9,165	5.4%	10,956	-11.8%
Others (Bathware & plywood)	980	917	6.9%	1,092	-10.3%
<b>Total</b>	<b>10,642</b>	<b>10,082</b>	<b>5.6%</b>	<b>12,048</b>	<b>-11.7%</b>
<b>EBIT (INR mn)</b>					
Tiles	1,330	1,172	13.4%	1,350	-1.5%
Others (Bathware & plywood)	57	40	42.9%	66	-13.3%
<b>Total</b>	<b>1,387</b>	<b>1,212</b>	<b>14.4%</b>	<b>1,416</b>	<b>-2.1%</b>
<b>Tiles Sales Volume (MSM)</b>					
Self Manufactured	13.8	13.4	2.8%	15.2	-8.8%
Subsidiaries	4.8	4.2	13.5%	6.1	-20.9%
Outsourcing	6.4	5.7	13.1%	6.8	-5.7%
<b>Total</b>	<b>25.0</b>	<b>23.3</b>	<b>7.2%</b>	<b>28.0</b>	<b>-10.7%</b>
<b>Tiles Realisation (INR/sqm)</b>					
Self Manufactured	391	401	-2.5%	396	-1.3%
Subsidiaries	279	312	-10.6%	308	-9.2%
Outsourcing	442	421	5.0%	438	0.8%
<b>Blended</b>	<b>382</b>	<b>390</b>	<b>-1.8%</b>	<b>387</b>	<b>-1.2%</b>
<b>Consolidated (INR mn)</b>					
Revenue	10,642	10,082	5.6%	12,048	-11.7%
EBITDA	1,692	1,536	10.2%	1,759	-3.8%
margin (%)	15.9%	15.2%	67 bps	14.6%	130 bps
APAT	1,075	923	16.5%	1,115	-3.5%
<b>Somany Ceramics</b>					
<b>Segmental</b>					
<b>Revenue (INR mn)</b>					
Tiles	5,075	4,799	5.8%	5,835	-13.0%
Others (Sanitaryware & Allied)	699	602	16.2%	849	-17.7%
<b>Total</b>	<b>5,774</b>	<b>5,400</b>	<b>6.9%</b>	<b>6,684</b>	<b>-13.6%</b>
<b>Tiles Sales Volume (MSM)</b>					
Self Manufactured	6.5	5.7	13.7%	7.5	-13.4%
Subsidiaries	4.9	5.0	-1.0%	5.5	-10.0%
Outsourcing	4.0	3.6	12.1%	4.6	-13.9%
<b>Total</b>	<b>15.4</b>	<b>14.3</b>	<b>8.1%</b>	<b>17.6</b>	<b>-12.4%</b>
<b>Tiles Realisation (INR/sqm)</b>					
Self Manufactured	325	330	-1.6%	333	-2.3%
Subsidiaries	347	337	3.1%	341	1.6%
Outsourcing	315	348	-9.4%	318	-1.0%
<b>Blended</b>	<b>329</b>	<b>337</b>	<b>-2.2%</b>	<b>332</b>	<b>-0.6%</b>
<b>Consolidated (INR mn)</b>					
Revenue	5,865	5,591	4.9%	6,792	-13.6%
EBITDA	506	449	12.6%	610	-17.0%
margin (%)	8.6%	8.0%	59 bps	9.0%	-35 bps
APAT	196	205	-4.4%	250	-21.4%
<b>Cera Sanitaryware</b>					
<b>Segmental revenue (INR mn)</b>					
Sanitaryware	2,264	2,120	6.8%	2,805	-19.3%
Faucetware	1,478	1,365	8.3%	1,842	-19.8%
Tiles	449	406	10.6%	566	-20.7%
Wellness	81	67	21.4%	91	-10.5%
<b>Standalone (INR mn)</b>					
Revenue	4,272	3,958	7.9%	5,304	-19.5%
EBITDA	685	612	12.0%	851	-19.5%
margin (%)	16.0%	15.5%	58 bps	16.0%	-1 bps
APAT	564	396	42.2%	668	-15.6%
<b>Consolidated (INR mn)</b>					
Revenue	4,289	3,972	8.0%	5,325	-19.5%
EBITDA	704	628	12.0%	872	-19.3%
margin (%)	16.4%	15.8%	59 bps	16.4%	4 bps
APAT	563	395	42.5%	666	-15.5%

Source: I-Sec research, Company data

### Exhibit 5: Quarterly trend for tile and sanitaryware

Tiles Segment	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24
<b>Total Sales Volume (MSM)</b>								
Kajaria Ceramics	24.8	25.6	26.0	23.3	24.9	25.5	28.0	25.0
YoY Growth (%)	25.2%	13.5%	2.3%	52.9%	0.5%	-0.7%	7.9%	7.2%
Somany Ceramics	16.2	15.6	16.1	14.3	15.9	16.2	17.6	15.4
YoY Growth (%)	25.1%	4.8%	-4.5%	42.4%	-1.7%	3.7%	9.2%	8.1%
<b>Sales Volume Mix (%)</b>								
Kajaria Ceramics								
Self Manufactured	57%	56%	55%	58%	59%	55%	54%	55%
Traded goods (JV + Outcourced)	43%	44%	45%	42%	41%	45%	46%	45%
Somany Ceramics								
Self Manufactured	40%	39%	36%	40%	46%	44%	43%	42%
Traded goods (JV + Outcourced)	60%	61%	64%	60%	54%	56%	57%	58%
<b>Tiles Revenue (INR mn)</b>								
Kajaria Ceramics	8,826	9,616	9,999	9,165	9,839	9,929	10,956	9,662
YoY Growth (%)	35.6%	26.8%	15.5%	76.5%	11.5%	3.2%	9.6%	5.4%
Somany Ceramics	4,955	5,126	5,358	4,799	5,418	5,431	5,835	5,075
YoY Growth (%)	33.2%	19.9%	9.1%	64.3%	9.4%	6.0%	8.9%	5.8%
Cera Sanitaryware	486	400	496	406	388	547	566	449
YoY Growth (%)	-27.3%	-46.2%	-41.7%	8.7%	-20.2%	36.8%	14.2%	10.6%
<b>Tiles Revenue Mix (%)</b>								
Kajaria Ceramics								
Self Manufactured	59%	57%	56%	59%	61%	57%	55%	56%
Traded goods (JV + Outcourced)	41%	43%	44%	41%	39%	43%	45%	44%
Somany Ceramics								
Self Manufactured	41%	38%	36%	39%	46%	44%	43%	42%
Traded goods (JV + Outcourced)	59%	62%	64%	61%	54%	56%	57%	58%
<b>Sanitaryware Revenue (INR mn)</b>								
Kajaria Ceramics	744	817	827	714	744	795	904	837
YoY Growth (%)	40.6%	21.2%	15.9%	93.0%	0.0%	-2.7%	9.4%	17.3%
Somany Ceramics	530	576	627	540	545	580	742	582
YoY Growth (%)	31.0%	20.3%	10.0%	85.4%	2.9%	0.7%	18.4%	7.7%
Cera Sanitaryware	3,446	3,460	3,885	3,552	3,755	4,011	4,738	3,823
YoY Growth (%)	37.2%	46.9%	12.2%	91.4%	9.0%	15.9%	21.9%	7.6%
<b>Blended Tiles Realisation (INR/sqm)</b>								
Kajaria Ceramics	356	375	383	390	391	387	387	382
YoY Growth (%)	8.3%	11.7%	12.2%	14.5%	9.9%	3.1%	1.1%	-1.8%
Somany Ceramics	306	329	333	337	341	336	332	329
YoY Growth (%)	6.5%	14.4%	14.3%	15.4%	11.3%	2.2%	-0.3%	-2.2%
<b>Tiles Realisation (INR/sqm)</b>								
Kajaria Ceramics								
Self Manufactured	373	384	388	401	404	401	396	391
Traded goods (JV + Outcourced)	334	364	375	374	372	370	377	372
Somany Ceramics								
Self Manufacture	312	323	331	330	340	337	333	325
Traded goods (JV + Outcourced)	302	333	333	341	342	336	331	333

Source: I-Sec research, Company data

## Exhibit 6: Key highlights from Kajaria Ceramics' Q1FY24 earnings call

Kajaria Ceramics	
Demand	New real estate launches over the past one year are expected to translate into stable tile demand Sep,'23 onwards.
	Demand in Apr-May'23 was subdued but Jun'23 showed signs of improvement.
	<b>Industry</b>
	Exports out of India were INR 48bn in Q1FY24 (+23% YoY compared to INR 39bn in Q1FY23).
Guidance	In FY24, exports are estimated to be ~INR 210bn.
	Domestic industry is expected to have flattish growth in Q1FY24.
	<b>Volume</b> growth of 13-15% YoY in FY24.
	<b>Revenue</b> growth of 14-16% YoY in FY24, driven by volume growth and higher share of VAP.
Realisation	<b>EBITDA margin</b> of 14-16% in FY24.
	Sanitaryware revenue growth of ~30% YoY in FY24.
	<b>Adhesives</b> revenue of INR 650mn in FY24.
	KJC will not take any significant price cuts, but will pass on RM cost benefit via discount schemes to trade channel.
Capacity Expansion	Tile modernisation/expansion at Gailpur (capex of INR 510mn) and Sikandrabad (brownfield expansion of 2.6MSM) is expected to commission in Q2FY24.
	Greenfield JV capex in Nepal of INR 1.8bn (KJC's share of investment of INR 0.9bn) for a capacity of 5.1MSM is expected to commence production from Mar'24.
	Capex of INR 800mn for setting up a sanitaryware facility of 0.6mn p.a. pieces capacity by Mar'24.
	KJC has planned total capex of ~INR 3.7bn for FY24 (which also includes INR 0.3bn for maintenance activities and INR 0.5bn for setting up a new corporate office).

Source: I-Sec research, Company data

## Exhibit 7: Key highlights from Somany Ceramics' Q1FY24 earnings call

Somany Ceramics	
Demand	Management reported subdued demand conditions in Q1FY24 as SOMC's tile plants ran at 70% utilisation.
	Significant demand improvement in Q2-TD was observed as plants are now running near 100% utilisation.
	Demand is expected to improve post Diwali.
Guidance	Guidance for double-digit <b>volume</b> growth in FY24.
	<b>EBITDA margin</b> guidance of 9.5-10% for FY24.
	In FY24, <b>bathware revenue</b> guidance of INR 3bn.
Realisation	No price cuts were taken during Q1, but some discounts were given to dealers due to lower input costs.
	The ~4.5msm plant in Morbi, which will manufacture large format tiles, is expected to operationalise in early-Q3FY24.
Capacity Expansion	The 3.5MSM JV plant in Nepal is expected to operationalise in FY25.
	Management indicated a maintenance capex of INR 400mn-500mn for FY24.

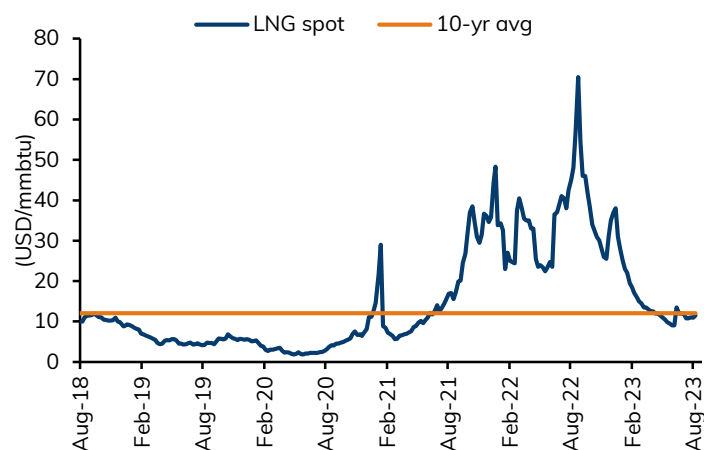
Source: I-Sec research, Company data

## Exhibit 8: Key highlights from Cera Sanitaryware's Q1FY24 earnings call

Cera Sanitaryware	
Demand	Demand remains healthy from replacement segment.
	Management foresees good demand for its new SKUs going forward.
Guidance	Guidance of achieving INR 29bn revenue by Sept'25 has been maintained.
	In FY24, CRS expects 17-19% YoY <b>revenue</b> growth.
Realisation	It indicated current margin is sustainable in the medium term with upward bias (supported by an improved product mix).
	No price hikes were taken in Q1FY24.
Capacity Expansion	Brownfield faucetware expansion (with total capacity of 0.4mn pieces per month) to commence operations in Aug'23 and CRS plans to ramp-up utilisation in a phased manner till Mar'24.
	Total capex for brownfield faucetware expansion has been revised downwards to INR 580mn vs earlier estimate of INR 690mn.
	For greenfield expansion of sanitaryware plant, CRS has finalised land parcel in Gujarat and its acquisition will be completed by Q2-Q3FY24 at a cost of INR 250mn, post which it will take 18-24 months for plant construction which will involve capex of INR 1,050mn.
	Maintenance capex of INR 350mn has been planned for FY24 of which INR 50mn has already been spent in Q1FY24.

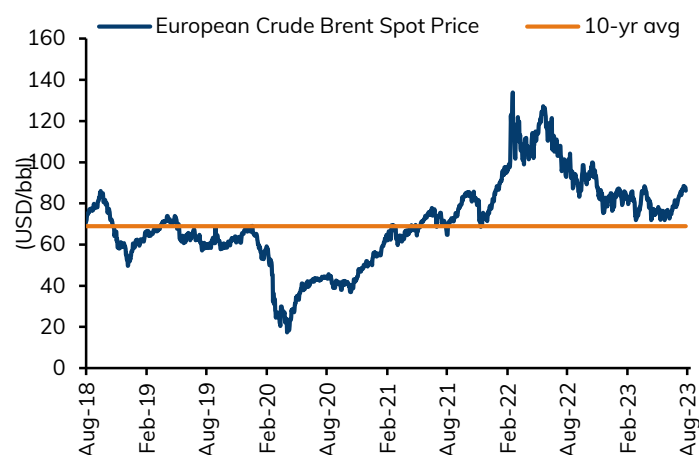
Source: I-Sec research, Company data

**Exhibit 9: Spot LNG price stabilising close to its 10-year average**



Source: Reuters, I-Sec Research

**Exhibit 10: European crude Brent's spot price declining**



Source: Bloomberg, I-Sec Research

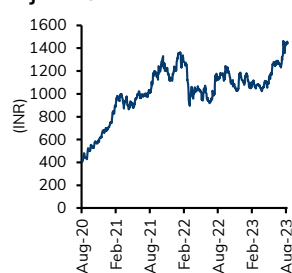
**Exhibit 11: Comparison table**

Company Name	Target Price (Rs)	Rating	CAGR % (FY23-26E)			PE (x)		EV/EBITDA (x)		ROE (%)	
			Revenue	EBITDA	APAT	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Kajaria Ceramics	1,487	ADD	12.3%	20.2%	23.5%	45.3	39.7	28.4	24.8	20.8%	21.2%
Cera Sanitaryware	7,928	HOLD	16.4%	16.8%	22.3%	42.7	37.2	30.0	25.2	20.4%	20.2%
Somany Ceramics	939	BUY	11.7%	23.8%	39.4%	20.5	17.1	11.1	9.5	16.8%	17.3%

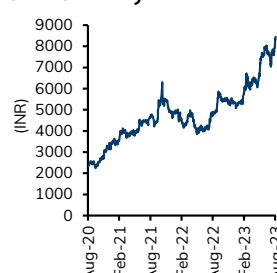
Source: I-Sec research, Company data

**Price chart**

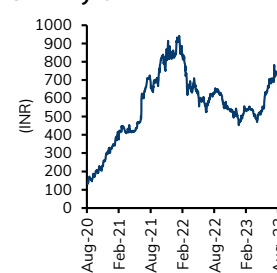
**Kajaria Ceramics**



**Cera Sanitaryware**



**Somany Ceramics**



Source: Bloomberg



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