Shankara Building Products (SHABUI)

CMP: ₹ 322 | Target: ₹ 320 (-1%) | Target Period: 12 months | HOLD

November 20, 2020

Balance sheet repair on course…now growth awaited!

Shankara Building Products' (Shankara) H1FY21 has been about balance sheet repair and cost rationalisation amid the Covid-19 shock. For H1FY21, the topline de-grew 34% YoY to ₹ 834 crore (decline of ~23% YoY for Q2, with a sharp sequential improvement) impacted by Covid-19. The EBITDA margin for H1FY21 declined 350 bps YoY to 1% (down 20 bps to 3.8% in Q2) mainly on account of negative operating leverage. Reported loss was at ₹ 19 crore for H1 while PAT for Q2 was at ₹ 6.3 crore, down 39% YoY.

Closure of loss making stores to improve profitability

For H1, retail business revenues de-grew ~30% YoY to ₹ 492 crore with Q2 witnessing ~18% YoY decline at ₹ 283 crore. The company, which reported EBIT losses in Q1, returned to the black with EBIT margins of 6% in Q2 (down 200 bps YoY. We highlight that Shankara has rationalised its stores with strong focus on higher revenue share and healthier margin. The process has reduced the store count (to 115 at the end of Q2FY21 vis-à-vis 129 at the end of Q2FY20) but increased the average ticket size (to ₹ 30,640 in Q2FY21 vis-à-vis ₹ 28,156 reported in Q2FY20). Post an expected decline of ~18% in FY21, we bake in ~25% growth on a depressed base in FY22, resulting in 1.2% CAGR in FY20-22E to ₹ 1476 crore. We highlight the retail margin improvement will be a function of pace of sales recovery.

Enterprise hit hard; channel relatively better

The channel and enterprise segment revenues were hard hit with H1FY21 revenues down 40% YoY at ₹ 342 crore (decline of ~28% in Q2). The segment also saw EBIT getting back in the black after losses in Q1. The company indicated that enterprise segment was hit hard while channel was relatively better. After its overall net debt + acceptances' reduction by 14% during H1FY20 to ₹ 292 crore, Shankara is targeting debt/EBITDA of <2.5x over the medium-term. It also said that the recovery continued in October 2020 and overall sales were at ~85% of October 2019 sales. The management expects 100% recovery on overall topline basis by Q4FY21.

Valuation & Outlook

With continued focus on the balance sheet, Shankara has been able to reduce its debtors by ₹ 172 crore and inventory by ₹ 108 crore in H1FY20. It was at ₹ 257 crore and ₹ 292 crore, respectively, as on September 2020-end. Also, its overall net debt + acceptances has reduced by 14% in H1FY20 and was at ₹ 292 crore as on September 2020-end. We believe Shankara steadily aligning its business towards its core competency is positive in the long term. Growth, however, is elusive. We would wait for the same before turning constructive. Hence, we maintain **HOLD** with a target price of ₹ 320/share. We value its retail business at ₹ 310/share (6x FY22E EV/EBIT).

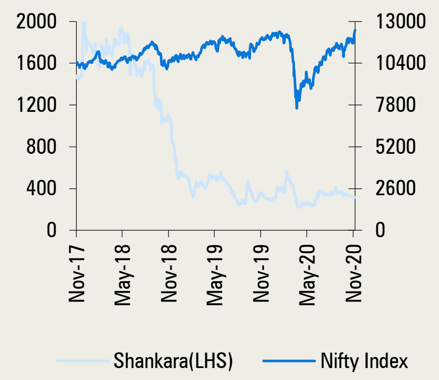
Particulars

Particulars	Amount (₹ crore)
Market Capitalization	735.9
Total Debt	239.1
Cash	20.8
EV	954.1
52 week H/L (₹)	580 / 214
Equity capital	22.9
Face value (₹)	10.0

Key Highlights

- Overall net debt + acceptances has reduced by 14% in H1FY20 and was at ₹ 292 crore as on September 2020 end
- Maintain HOLD with target price of ₹ 320 per share

Price performance



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Key Financial Summary

(₹ crore)	FY18	FY19	FY20	FY21E	FY22E	CAGR FY20-22E
Net Sales	2,548.7	2,546.3	2,639.7	2,153.0	2,439.1	-3.9%
EBITDA	175.2	99.5	117.1	72.1	107.3	-4.3%
EBITDA Margin (%)	6.9	3.9	4.4	3.3	4.4	
Net Profit	73.8	32.7	39.9	12.3	38.1	-2.3%
EPS (₹)	32.3	14.3	17.5	5.4	16.7	
P/E (x)	10.0	22.5	18.5	59.7	19.3	
EV/EBITDA (x)	5.6	9.2	8.1	11.6	7.7	
RoCE	22.7	12.8	12.2	6.4	10.2	
RoNW	16.2	6.8	7.9	2.3	6.6	

Source: Company, ICICI Direct Research

Company Update

ICICI Securities – Retail Equity Research

Business Highlights

- **Q2FY21 result highlight:** Despite partial lockdowns in some states during July 2020, Shankara witnessed a broad based recovery across its different verticals, largely aided by gradual unlocking of economy and uptick in demand in certain industries like automobile, infrastructure and construction. Also, demand in tier-II and III cities has picked up with good monsoons

- **Revenue breakup**: Shankara reported ₹ 488 of topline (up 41% QoQ) during Q2FY21 largely contributed by retail (58%), channel (21.9%) and enterprise (20.1%) businesses. Its revenue (as a percentage of last year sales) during July 2020, August 2020 and September 2020 have improved to 71%, 79% and 82%, respectively. Also, the recovery continued in October 2020 and was at ~85% of October 2019 sales. The management expects 100% recovery by Q4FY21

- **Retail business- product/geographical breakup:** Construction material contributed 65% to the retail business, followed by plumbing, sanitary ware and tiles (15%), interior exterior (15%), and agricultural products (5%). Own product retail sales were at ~25% while balance came from third party sales in Q2FY21. With regard to geographical contribution in retail business, Tier-I cities accounted for ~36% of revenues, Tier II (26%) and Tier III (38%)

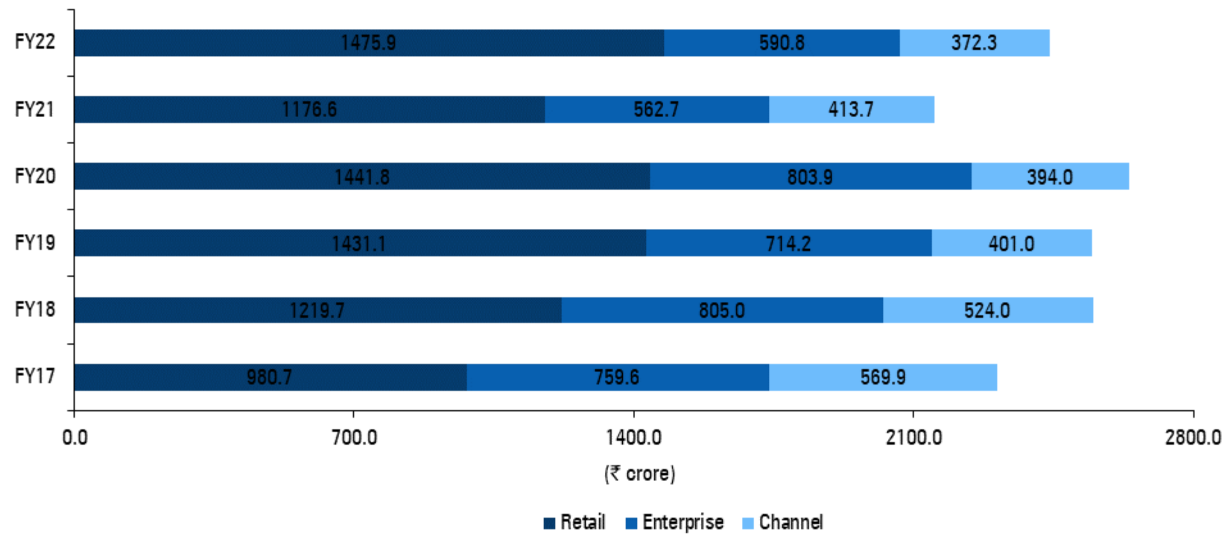
- **Stores count:** Shankara is rationalising its stores with strong focus on a) higher revenue share and b) healthier margin. The process has lowered the store count (to 115 at the end of Q2FY21 vis-à-vis 129 at the end of Q2FY20) but increased the average ticket size (to ₹ 30,640 during Q2FY21 vis-à-vis ₹ 28,156 reported in Q2FY20). Overall contribution of closed stores to total revenue was ~3%. The management has indicated towards almost completion of rationalising activity

- **EBITDA margin**: Shankara has managed to improve its EBITDA margin to 3.8% in Q2FY21 (vis-à-vis -3%, 4.2% reported in Q1FY21, Q2FY20, respectively) largely backed by cost cutting initiatives that were undertaken. Also, its average rental cost per sq ft has come down to ₹ 15.9 per month (from ₹ 20 per month reported in Q2FY20). Going forward, the management expects the rental cost to remain benign in Q3FY21. However, margins are likely to moderate from the current level with a change in product mix

- **Working capital & debt**: With continued focus on balance sheet, Shankara has been able to reduce its debtors by ₹ 172 crore and inventory by ₹ 108 crore during H1FY20. It was at ₹ 257 crore and ₹ 292 crore, respectively, as on September 2020 end. Also, its overall net debt + acceptances has reduced by 14% in H1FY20 and was at ₹ 292 crore as on September 2020 end. The company is targeting debt/EBITDA of <2.5x over the medium-term. H1FY21 operating cash flow was strong at ₹ 61 crore

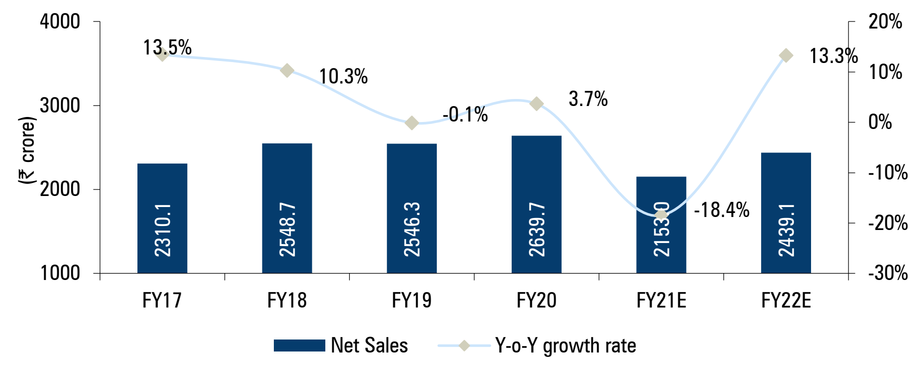
Company Analysis

Exhibit 1: Segmental revenue trend



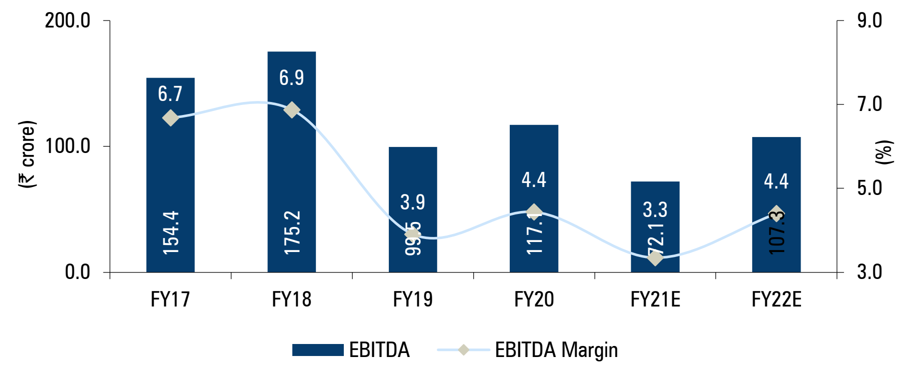
Source: Company, ICICI Direct Research

Exhibit 2: Overall revenue trend



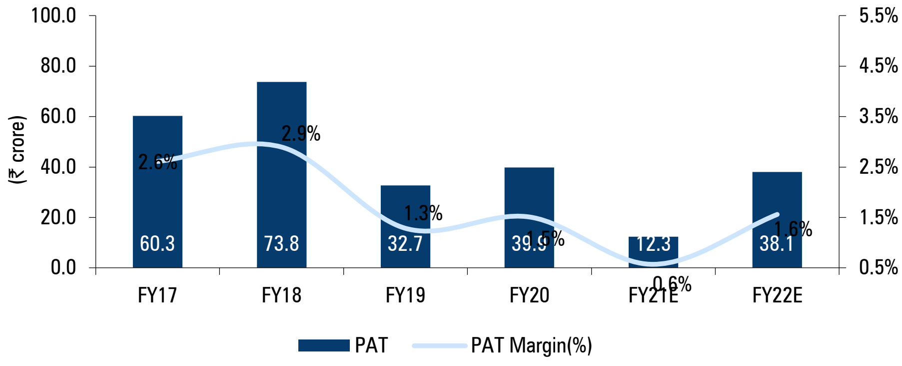
Source: Company, ICICI Direct Research

Exhibit 3: Overall EBITDA trend



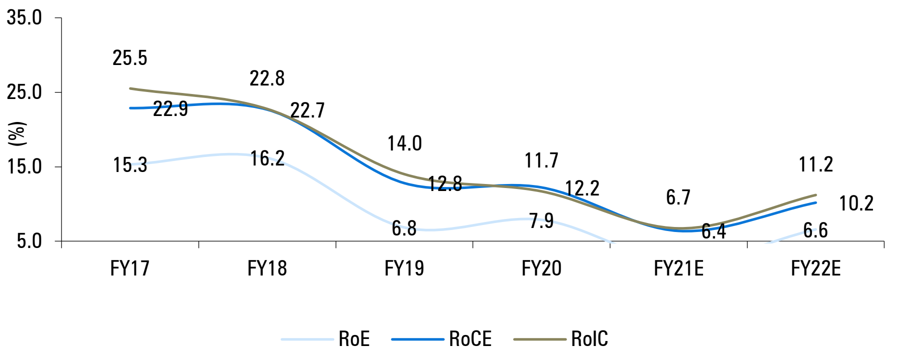
Source: Company, ICICI Direct Research

Exhibit 4: PAT trend



Source: Company, ICICI Direct Research

Exhibit 5: Return ratios trend



Source: Company, ICICI Direct Research

Valuation & Outlook

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Exhibit 6: Valuation

Business	Method	Multiple	Basis	Valuation	₹/share
Retail	EV/EBIT	6.0	FY22E	708.5	310
Channel & Enterprise	EV/EBIT	4.0	FY22E	115.6	50.6
Less: Net Debt				-91.1	-40
Target Valuation				732.9	**320.7**
Rounded off target price					**320**

Source: Company, ICICI Direct Research

Financial summary

Exhibit 7: Profit and loss statement ₹ crore

(₹ Crore)	FY19	FY20	FY21E	FY22E
Net Sales	**2,546.3**	**2,639.7**	**2,153.0**	**2,439.1**
Net Raw Material Cost	**2,312.0**	**2,398.2**	**1,949.5**	**2,202.5**
Employee benefit expenses	55.4	53.6	61.6	70.8
Power & Fuel	-	-	-	-
Consumption of stores and spares	-	-	-	-
Total operating expenditures	2,446.9	2,522.6	2,080.9	2,331.8
EBITDA	**99.5**	**117.1**	**72.1**	**107.3**
Interest	47.1	43.3	35.5	35.8
Depreciation	14.8	25.4	26.1	27.2
Other income	4.3	5.0	6.0	6.6
PBT	**41.8**	**53.4**	**16.5**	**50.9**
Taxes	13.4	11.2	4.2	12.8
Effective tax rate (%)	32.0%	21.0%	25.2%	25.2%
PAT	**32.7**	**39.9**	**12.3**	**38.1**
PAT Growth rate	-45.7%	21.8%	-69.1%	208.8%
Adjusted EPS (Diluted)	**14.3**	**17.5**	**5.4**	**16.7**

Source: Company, ICICI Direct Research

Exhibit 8: Cash flow statement ₹ crore

(₹ Crore)	FY19	FY19	FY21E	FY22E
Profit after Tax	**32.7**	**32.7**	**12.3**	**38.1**
Depreciation	14.8	14.8	26.1	27.2
Interest	47.1	47.1	35.5	35.8
Taxes	13.4	13.4	4.2	12.8
Cash Flow before wc changes	99.5	99.5	72.1	107.3
Cash generated from operations	61.3	61.3	85.5	(46.3)
Income Tax paid	(13.4)	(13.4)	(4.2)	(12.8)
Net CF from operating activities	**147.4**	**147.4**	**153.4**	**48.1**
(Purchase)/Sale of Fixed Assets (Net)	38.8	38.8	(10.8)	(12.2)
Others	(79.9)	(79.9)	13.2	6.6
Net CF from Investing activities	**(41.1)**	**(41.1)**	**2.4**	**(5.6)**
Dividend	-	-	-	-
Interest paid	(47.1)	(47.1)	(35.5)	(35.8)
Inc / (Dec) in Loans	(47.7)	(47.7)	(10.9)	-
Net CF from Financing activities	**(94.8)**	**(94.8)**	**(46.4)**	**(35.8)**
Net Cash flow	11.5	11.5	109.5	6.7
Opening Cash	6.0	6.0	20.8	130.3
Closing Cash/ Cash Equivalent	**17.5**	**17.5**	**130.3**	**137.0**

Source: Company, ICICI Direct Research

Exhibit 9: Balance sheet ₹ crore

(₹ Crore)	FY19	FY19	FY21E	FY22E
Liabilities				
Equity Capital	22.9	22.9	22.8	22.8
Reserve and Surplus	456.2	456.2	517.8	555.9
Total Shareholders funds	479.0	479.0	540.7	578.8
Total Debt	195.1	195.1	228.1	228.1
Total Liabilities	**695.3**	**695.3**	**813.8**	**851.9**
Assets				
Gross Block	271.5	271.5	303.3	315.5
Less Acc. Dep	32.6	32.6	70.5	97.6
Net Block	238.9	238.9	232.8	217.9
Goodwill on consolidation	14.0	14.0	14.0	14.0
Total Fixed Assets	273.4	273.4	300.1	289.5
Investments	1.4	1.4	35.7	35.7
Inventory	383.0	383.0	322.9	365.9
Sundry Debtors	337.5	337.5	347.6	393.8
Loans & Advances	14.8	14.8	17.4	21.8
Cash & Bank Balances	17.5	17.5	130.3	137.0
Other Current Assets	31.5	31.5	28.0	30.8
Total Current Assets	769.5	769.5	828.8	927.4
Trade Payable	381.5	381.5	293.9	333.0
Other Current Liabilities	33.3	33.3	17.0	19.3
Provisions	2.0	2.0	4.2	12.8
Net Current Assets	352.8	352.8	513.7	562.3
Total Assets	**695.3**	**695.3**	**813.8**	**851.9**

Source: Company, ICICI Direct Research

Exhibit 10: Key ratios

	FY19	FY19	FY21E	FY22E
Per Share Data (₹)				
EPS - Diluted	14.3	14.3	5.4	16.7
Cash EPS	20.8	20.8	16.8	28.5
Book Value	209.6	209.6	236.6	253.3
Dividend per share	5.4	5.4	-	7.7
Operating Ratios (%)				
EBITDA / Net Sales	3.9	3.9	3.3	4.4
PAT / Net Sales	1.3	1.3	0.6	1.6
Inventory Days	54.9	54.9	54.8	54.8
Debtor Days	48.4	48.4	58.9	58.9
Creditor Days	54.7	54.7	49.8	49.8
Return Ratios (%)				
RoE	6.8	6.8	2.3	6.6
RoCE	12.8	12.8	6.4	10.2
RoIC	14.0	14.0	6.7	11.2
Valuation Ratios (x)				
EV / EBITDA	9.2	9.2	11.6	7.7
P/E (Diluted)	22.5	22.5	59.7	19.3
EV / Net Sales	0.4	0.4	0.4	0.3
Market Cap / Sales	0.3	0.3	0.3	0.3
Price to Book Value	1.5	1.5	1.4	1.3
Dividend Yield	1.7	1.7	-	2.4
Solvency Ratios (x)				
Net Debt / Equity	0.4	0.4	0.2	0.2
Debt / EBITDA	2.0	2.0	3.2	2.1
Current Ratio	1.8	1.8	2.2	2.2
Quick Ratio	**0.9**	**0.9**	**1.2**	**1.2**

Source: Company, ICICI Direct Research

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Reduce: -15% to -5%;

Sell: <-15%

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