

Pokarna Ltd (POKGRA)

₹ 150

Pokarna posted good Q1FY19 results given the low base as its quartz plant remained shut for 45 days in Q1FY18 owing to maintenance. Pokarna's topline grew by 23.4% YoY to ₹ 83.4 crore led by strong performance of quartz business. Quartz revenues grew robustly by 54.7% YoY to ₹ 51.2 crore. EBITDA margin slipped 32 bps YoY to 23.8% as granite margins contracted significantly by 860 bps YoY to 15%. However, PAT grew robustly by 69.5% YoY to ₹ 9.2 crore led by topline growth & lower effective tax rate (13.9% in Q1FY19 vs. 20.7% in Q1FY18).

Triggers

Quartz business prospects remain positive...

Pokarna's quartz division robust performance was led lower base as its quartz plant remained shut for maintenance purposes for 45 days in Q1FY18. On Quartz business front, the management indicated that demand environment remains strong and the US quartz market is expected to sustain its growth momentum. However, EBITDA margins have come under pressure (35.6% in FY18 vs. 46.2% in FY17) given the increasing competition and rising input costs. Furthermore, some media reports indicate that US may impose a tariff on Chinese Quartz imports which may offer Pokarna an opportunity to capture incremental share and also it would reduce the pricing differential between Pokarna and its Chinese counterparts. Currently, China accounts for ~60% US quartz market. However, given the capacity constraints at its current facility, the management has guided for a moderate growth in quartz division until its new quartz plant commissions.

Quartz Capacity addition to lead next leg of growth...

Currently, Pokarna has a quartz manufacturing unit in Visakhapatnam with a capacity of 6 LSM which is operating near optimum capacity utilization. Hence, given the strong opportunity in quartz business, it is setting up new quartz capacity of 7 LSM in Hyderabad on Bretonstone technology. The company has applied for requisite land approvals and expects to commence construction soon. It would take around 18 months to complete construction and commence operations. Total capex for the project will be ₹ 330 crore, which will be funded by ₹ 250 crore debt and ₹ 80 crore internal accruals. The plant is expected to be commissioned in Q4FY20E. This would lead to next leg of growth for the company.

Partners with Ikea to supply quartz countertops...

Pokarna has tied up with Ikea to serve as their exclusive quartz supplier and installation partner for the Indian market. Currently, Ikea has placed ~60-70 countertops in their newly opened store in Hyderabad which is being served by Pokarna's Visakhapatnam unit. The company would be supplying countertops to IKEA's upcoming two stores as well.

Granite division to remain muted amidst increasing competition...

The management indicated granite business performance has been declining due to rising competitive scenario. Consequently, it expects no growth coming from this segment in near term. Also, it added that China is selling cut-to-size granites (a customised high margin product) at very low prices, which are difficult to compete on the pricing front. We thus expect very low growth coming from this segment going forward.

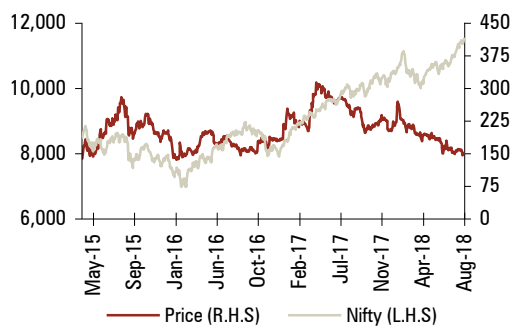
Valuation & Outlook

At the CMP, the stock is trading at 11x FY18 EPS. We like Pokarna, given its increasing focus on high margin quartz business, its owned quarries and sole manufacturer by superior BretonStone technology in India. We believe the new Hyderabad quartz facility will further help the company increase its share in the US market, going forward. We have a **BUY** rating with TP of ₹ 200(12x FY20E EPS of ₹ 17.1/share).

Rating Matrix		
Rating	:	Buy
Target	:	₹ 200
Target Period	:	18-24 months
Potential Upside	:	33%

Stock Data	
Particular	Amount
Market Capitalization	464.6
Total Debt	220.0
Cash & equivalent	20.9
EV	₹ 664 Crore
52 week H/L (₹)	141 / 275
Equity capital	6.2
Face value	₹ 2
FII Holding (%)	0.6
DII Holding (%)	4.3

Price Movement



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Conference call highlights

- **EBITDA Margins under pressure:** Recent increase in crude prices led to increase in prices of polyester resin-a key raw material to manufacture quartz. Rupee depreciation further led to higher cost of raw materials, putting pressure on margins
- **Quartz business:** The US remains a key export market for the company in this segment. The management indicated that Chinese quartz manufacturers offer their products at a 20-40% lower price than that of Pokarna. Also, China's share of quartz exports to the US rose to ~60% in the past 8 years because of their pricing power. However, the management is bullish on the US quartz market given the strong growth momentum it offers to cater to at least for medium term. Also there is possibility that the US government may impose tariff on Chinese quartz which will help Pokarna gain incremental share in the US quartz market
- **Granite business:** The management commented that realizations from granite business have been under pressure because of rising competitive environment. It expects low growth coming from this segment going ahead
- **Capacity addition:** The management has plans to add new capacity for its quartz business to cater to strong demand from the US market. It has obtained regulatory approval for purchase of 39 acres of land in Hyderabad. Furthermore, it has applied for requisite approvals for commencing work on new greenfield Engineered Stone Facility, which will be set up using the Breton Stone technology. Total investment for the project shall be to the tune of ~₹ 330 crore, which will be funded by ~₹ 250 crore debt and ₹ 80 crore internal accruals. The plant is expected to be commissioned in Q4FY20E
- **Supply to IKEA:** Pokarna has tied up exclusively with Ikea to supply and install quartz countertops. It has already placed ~60-70 countertops in the newly opened IKEA store in Hyderabad. The management has plans to supply to IKEA's upcoming two stores as well
- **Rupee loan conversion update:** The company has proposed to the consortium of banks to convert its domestic rupee loan to external commercial borrowing (ECB) loan. Out of ₹ 44 crore rupee loan, ₹ 30 crore is already confirmed for changing while, confirmation on loan of ₹ 14 crore from Bank of India is awaited
- **Apparel business update:** The company is still in process of finding a buyer to exit this business

Exhibit 1: Financials Performance

(Year-end March)	FY14	FY15	FY16	FY17	FY18
P&L					
Revenues (₹ crore)	230.6	326.4	393.9	367.4	328.2
EBITDA (₹ crore)	46.4	83.6	132.8	136.4	97.2
EBITDA Margins (%)	20.1	25.6	33.7	37.1	29.6
Net Profit (₹ crore)	11.7	31.4	51.2	70.3	42.1
Balance Sheet					
Equity (₹ crore)	6.2	6.2	6.2	6.2	6.2
Net worth (₹ crore)	25.8	53.0	96.8	164.2	191.3
Debt (₹ crore)	310.0	290.2	271.6	270.8	220.0
Ratios					
RoNW (%)	45.4	59.1	52.9	42.8	22.0
RoCE (%)	7.8	18.9	32.9	29.1	19.9
P/B	17.8	8.6	4.7	2.8	2.4
P/E	39.2	14.6	8.9	6.5	10.9
Earnings per share (₹)	3.8	10.1	16.5	22.7	13.6
Asset turnover (x)	0.7	0.9	1.1	0.8	0.8
EV/EBITDA (x)	16.4	8.8	5.4	5.1	6.8

Source: Company, ICICIdirect.com Research

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Strong Buy: > 15%/20% for large caps/midcaps, respectively, with high conviction;

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