



3R MATRIX

	+	=	-
Right Sector (RS)	✓	■	■
Right Quality (RQ)	✓	■	■
Right Valuation (RV)	■	✓	■

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS	■	↔	■
RQ	■	↔	■
RV	■	↔	■

Reco/View	Change
Reco: Buy	↔
CMP: Rs. 1,178	
Price Target: Rs. 1,402	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

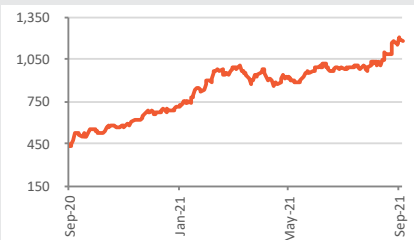
Company details

Market cap:	Rs. 18,737 cr
52-week high/low:	Rs. 1,228 / 425
NSE volume: (No of shares)	4.38 lakh
BSE code:	500233
NSE code:	KAJARIACER
Free float: (No of shares)	8.3 cr

Shareholding (%)

Promoters	48
FII	25
DII	15
Others	12

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	13.9	18.9	18.1	164.1
Relative to Sensex	6.7	7.5	2.6	112.3

Sharekhan Research, Bloomberg

Summary

- More than 180 companies in the Morbi ceramic cluster have shut down production since August 2021, which would create a favourable demand and pricing environment for Kajaria in Gujarat.
- Natural gas prices stay high in Morbi, while being stable outside Gujarat for Kajaria. Demand is upbeat since July 2021.
- Healthy demand and brownfield capacity expansion would drive earnings growth in the next three years.
- We retain a Buy on Kajaria Ceramics with a revised PT of Rs. 1402, as we believe the company is entering into a high growth phase led by structural demand drivers.

Kajaria Ceramics Limited (Kajaria) is expected to benefit from healthy demand & pricing environment in Gujarat region (15-20% exposure) after more than 180 companies in Morbi region shutting down production for double charged vitrified tiles and wall tiles from August 2021 end. Kajaria's gas price consumption rate outside Gujarat remains stable at Rs. 36/scm versus Morbi, which has seen a rise from Rs. 36/scm to Rs. 39.7/scm. Pan-India demand is also healthy since July 2021.

- Strong exports & muted imports of tiles till June 2021:** Indian tile exports had grown by 21% y-o-y in FY2021, but clocked a sharp 120% y-o-y rise in FY2022 (until June 2021). On the other hand, tile imports dipped 41% y-o-y in FY2021 and were up 13% y-o-y in FY2022 (until June 2021).
- Healthy pricing & supply shortage in Gujarat:** More than 180 companies in Morbi have entered a shutdown from August-end led by higher container rates, a rise in gas prices, increase in raw material and diesel prices. Kajaria, with a 15-20% exposure in Gujarat would benefit from supply shortage and pricing discipline.
- Gas prices outside Gujarat stable:** The Morbi cluster saw natural gas prices rise from 36/scm to 39.7/scm led by price hikes undertaken by Gujarat Gas. The company's gas consumption price outside Gujarat remains stable at 36/scm.

Our Call

**Valuation – Retain Buy with a revised PT of Rs. 1402:** Kajaria is expected to benefit from market share gains in Gujarat as more than 180 companies in Morbi have shut down production. Demand outside Gujarat remains buoyant since July 2021, while natural gas prices remain stable. Given the strong demand outlook for the next 2-3 years, the company has ventured into brownfield expansion which is expected to maintain strong earnings growth. We expect revenue/operating profit/net profit to rise at a 17%/20%/26% CAGR over FY2021-FY2024E. We retain a Buy rating on the stock with a revised price target (PT) of Rs. 1402.

Key Risks

A weak macro-economic environment, pressure on realisation, and increased gas prices are key risks to our call.

Valuation (Consolidated)

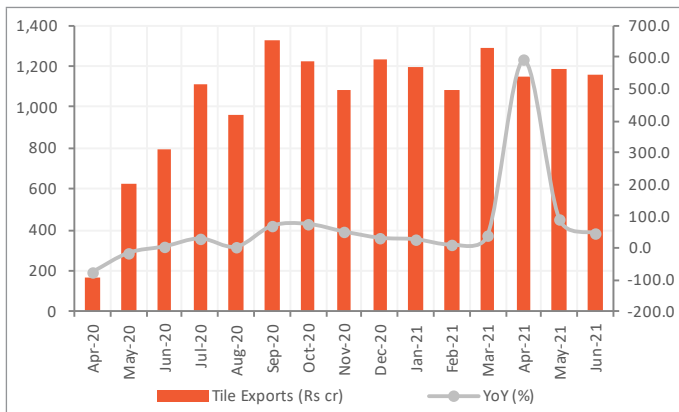
Particulars	Rs cr			
	FY21	FY22E	FY23E	FY24E
Revenue	2,780.9	3,343.2	3,868.6	4,481.3
OPM (%)	18.3	16.1	18.0	19.6
Adjusted PAT	308.1	326.6	450.7	610.5
% y-o-y growth	20.6	6.0	38.0	35.4
Adjusted EPS (Rs.)	19.4	20.5	28.4	38.4
P/E (x)	53.1	50.1	36.3	26.8
P/B (x)	8.7	8.1	7.2	6.1
EV/EBITDA (x)	31.1	29.3	22.8	18.0
RoNW (%)	17.2	16.9	21.1	24.7
RoCE (%)	16.6	16.5	20.6	24.1

Source: Company; Sharekhan estimates

### Healthy demand & pricing environment in & out of Gujarat

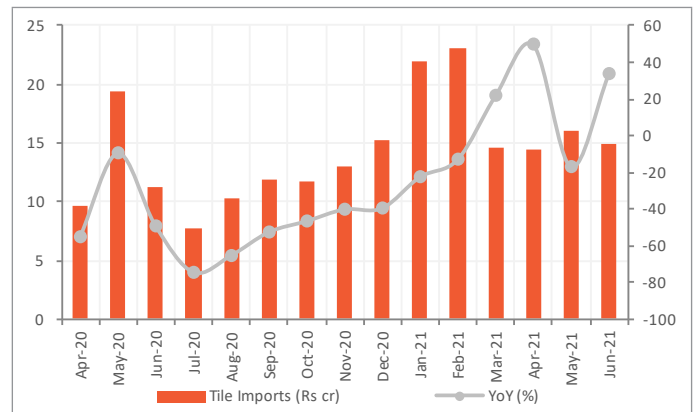
Indian tile exports had grown by 21% y-o-y in FY2021, but clocked a sharp 120% y-o-y rise in FY2022 (until June 2021). On the other hand, tile imports dipped 41% y-o-y in FY2021 and were up 13% y-o-y in FY2022 (until June 2021). During August-end, more than 180 tile companies in Morbi manufacturing double charged vitrified tiles and wall tiles stopped production and dispatches (dispatches resumed from September 5, 2021) led by multiple factors like 1) rise in export freight charges 2) rise in gas prices and 3) increase in diesel and other raw material prices. The same has led to supply shortage in the regional market while prices remained stable. Kajaria has 15-20% exposure in Gujarat, which is expected to see healthy pricing discipline amidst shortage of domestic supply.

**Tile Monthly Export trend (Rs cr)**



Source: Industry, Sharekhan Research

**Tile Monthly Import trend (Rs cr)**

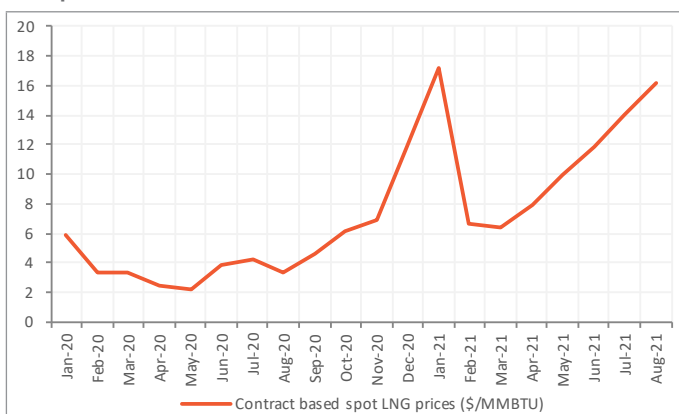


Source: Industry, Sharekhan Research

### Gas prices remain stable out of Gujarat for Kajaria

The Morbi tile industry saw natural gas prices rise from 36/scm to 39.7/scm due over a month's period led by price hike undertaken by Gujarat Gas (a predominant supplier to the Morbi cluster). The industry has been mulling to undertake price hikes but as mentioned earlier there has been a shutdown in manufacturing operations. Kajaria Ceramics had taken a 3% price hike in July 2021 post which it has not taken any price hike. The company's gas consumption price outside Gujarat remains stable at 36/scm versus Rs. 39/scm in Gujarat.

**LNG prices contract based**



Source: Industry, Sharekhan Research

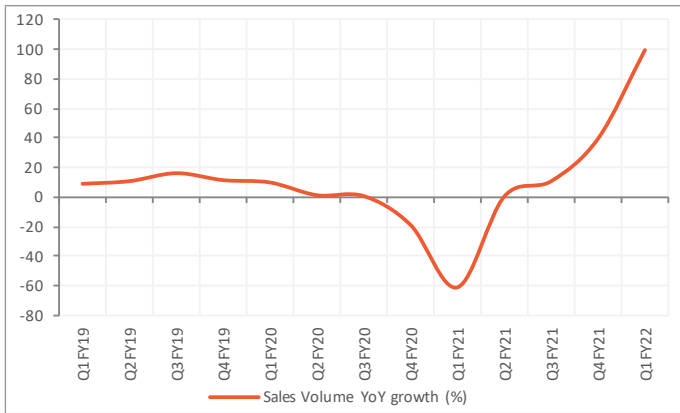
**Brent crude price trend**



Source: Industry, Sharekhan Research

**Financials in charts**

**Tile Volume Trend**



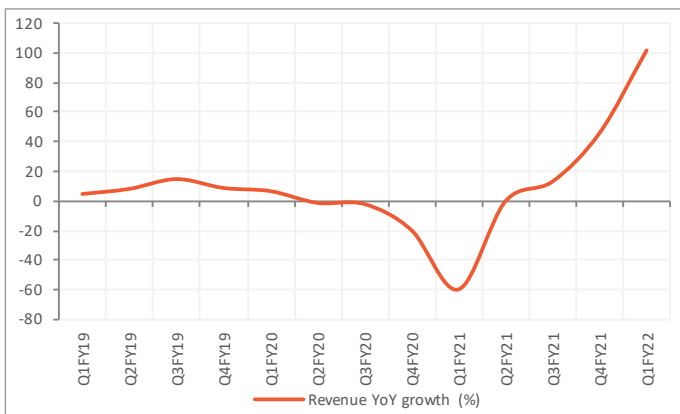
Source: Company, Sharekhan Research

**Tile Realisation Trend**



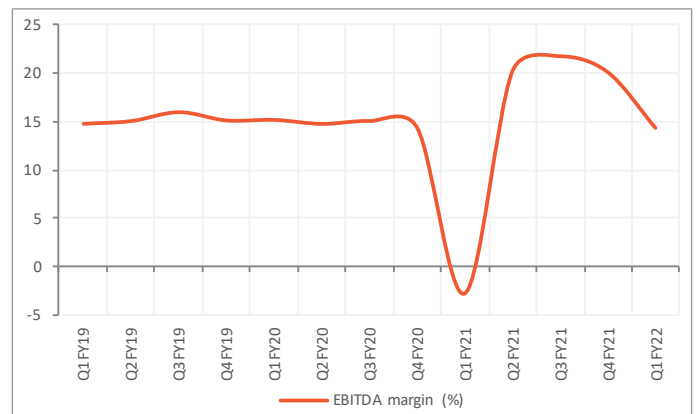
Source: Company, Sharekhan Research

**Revenue Trend**



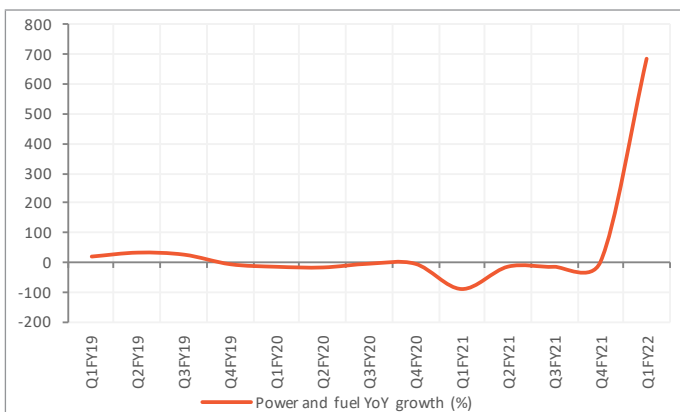
Source: Company, Sharekhan Research

**EBITDA margin Trend**



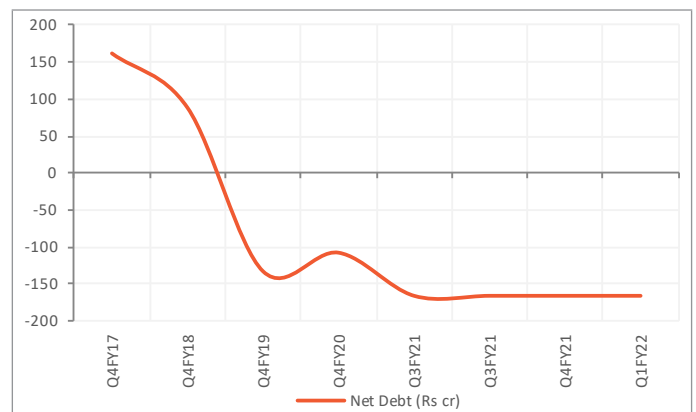
Source: Company, Sharekhan Research

**Power & fuel cost Trend**



Source: Company, Sharekhan Research

**Net Debt Trend**



Source: Company, Sharekhan Research

## Outlook and Valuation

### ■ Sector view – Strong recovery in operations to sustain

The building materials industry was severely affected by COVID-19 led lockdown during Q1FY2021, which had affected its peak sales period of the year. Additionally, its high fixed cost structure had affected OPM, dragging down net earnings. However, from June, the sector has been among the fastest to recover with easing of lockdowns domestically. The sector saw resumption of dealer and distribution networks and a sharp improvement in capacity utilisation. Most players have begun to see demand and revenue run-rate reaching 80-90% of pre-COVID levels. Scaling up of revenue is also expected to lead to better absorption of fixed costs going ahead, aiding a recovery in net earnings. The industry is expected to rebound with strong growth in FY2022 and FY2023.

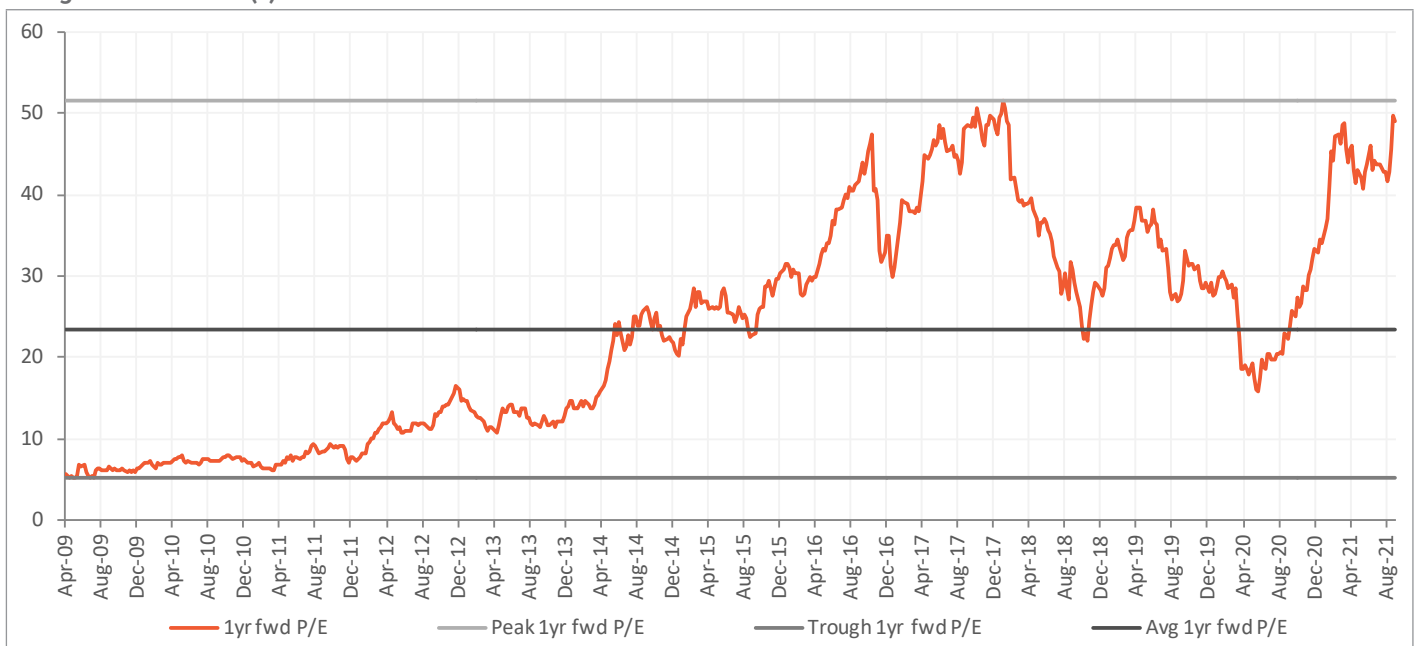
### ■ Company outlook – Demand environment to remain strong over next couple of years

Kajaria has seen operations and demand environment improve sharply m-o-m with the easing of lockdowns in India. The company's asset utilisation has been getting better and is expected to continue doing so. Further, anti-China sentiments in the US and European countries along with soft gas prices have boosted exports for the Morbi cluster, which houses around 850 manufacturing units. This has led to improved pricing environment for organised players such as Kajaria and driven up its domestic market share. The company expects strong 20-25% volume growth for FY2022 and 15%+ volume growth for FY2023 and FY2024. It expects OPM to be strong at 20% during FY2022. The confidence over demand revival has led to the company planning for brownfield expansion.

### ■ Valuation – Retain Buy with a revised PT of Rs. 1402

Kajaria is expected to benefit from market share gains in Gujarat as more than 180 companies in Morbi have shut down production. Demand outside Gujarat remains buoyant since July 2021, while natural gas prices remain stable. Given the strong demand outlook for the next 2-3 years, the company has ventured into brownfield expansion which is expected to maintain strong earnings growth. We expect revenue/operating profit/net profit to rise at a 17%/20%/26% CAGR over FY2021-FY2024E. We retain a Buy rating on the stock with a revised price target (PT) of Rs. 1402.

#### One-year forward P/E (x) band



Source: Sharekhan Research

## About company

Kajaria Ceramics is India's largest manufacturer of ceramic/vitrified tiles and the world's ninth largest tile manufacturer. The company has an annual capacity of 70.4 mn. sq. meters presently, distributed across eight plants - one in Sikandrabad in Uttar Pradesh, one in Gailpur, one in Malootana in Rajasthan, three in Morbi in Gujarat, one in Vijaywada, and one in Srikalahasti in Andhra Pradesh.

## Investment theme

Kajaria like other building material players is expected to witness benefits arising from improving demand from the housing sector. Further, anti-China sentiments in the US and European countries along with soft gas prices have boosted exports for the Morbi cluster, which has led to improved pricing environment for organised players such as Kajaria and increase in market share domestically. Given the strong demand outlook over next two to three years, the company is exploring the idea of brownfield expansion. Its rising free cash flow generation and low capex requirement is expected to reward shareholders through higher dividend payouts.

## Key Risks

- ◆ Increased crude oil prices followed by higher gas prices.
- ◆ Pressure on pan-India residential housing market leading to overall lower volume offtake for the industry.

## Additional Data

### Key management personnel

Mr. ASHOK KUMAR KAJARIA	Executive Director-Chairperson related to Promoter
Sanjeev Agarwal	Chief Financial Officer
R C Rawat	Company Secretary & Compliance Officer
Mr. CHETAN KAJARIA	Executive Director
Mr. RISHI KAJARIA	Executive Director

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	RISHI KAJARIA FAMILY TRUST	16.27
2	CHETAN KAJARIA FAMILY TRST	16.27
3	CK TRUSTEES PVT LTD	16.27
4	RK TRUSTEES PVT LTD	16.27
5	VERSHA KAJARIA FAMILY TRST	8.14
6	VK TRUSTEES PVT LTD	8.14
7	Norges Bank	4.73
8	GOVERNMENT PENSION FUND - GLOBAL	4.63
9	Mirae Asset Global Investments Co Ltd	4.24
10	Franklin Resources Inc	3.73

Source: Bloomberg

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## Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

# Sharekhan

by BNP PARIBAS

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