



## 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	✗	↔	✗

## ESG Disclosure Score NEW

ESG RISK RATING 23.98  
Updated July 08, 2022

Medium Risk				
NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

## Company details

Market cap:	Rs. 17,083 cr
52-week high/low:	Rs. 1,379/886
NSE volume: (No of shares)	4.4 lakh
BSE code:	500233
NSE code:	KAJARIACER
Free float: (No of shares)	8.4 cr

## Shareholding (%)

Promoters	48
FII	20
Institutions	22
Public & others	11

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	16.6	2.1	-12.4	9.8
Relative to Sensex	9.1	4.8	-9.2	4.5

Sharekhan Research, Bloomberg

## Kajaria Ceramics Ltd

## Building on market share gains

## Building Materials

Sharekhan code: KAJARIACER

Reco/View: Buy

↔

CMP: Rs. 1,073

Price Target: Rs. 1,300

↑

↑

Upgrade

↔

Maintain

↓

Downgrade

## Summary

- We retain a Buy rating on Kajaria Ceramics with a revised PT of Rs. 1300 on account of strong earnings growth led by market share gains.
- The company reported a strong beat on net earnings for Q1FY2023 led by higher-than-expected revenue growth and operating margins.
- The management retained 15-20% y-o-y volume growth guidance for FY2023 although reframed from giving guidance on OPM due to volatility in gas prices.
- It acquired 51% stake in South Asian Ceramics having 4.8msm ceramic floor tiles capacity which would strengthen its presence in South.

Kajaria Ceramics Limited (Kajaria) reported a strong beat on net earnings for Q1FY2023 led by higher-than-estimated revenues and OPM. The consolidated revenues at Rs. 1008 crore (up 79.5% y-o-y) in Q1FY23, was led by a strong tile volume growth of 52.9% y-o-y (led by low base, down 10.2% q-o-q) while blended tile realizations were up 17.4% y-o-y (up 1.9% q-o-q). Revenues from the bath ware and plywood segments rose by 93% y-o-y and 279.5% y-o-y. Consolidated OPM at 15.2% (up 92 bps y-o-y) surprised positively led by better-than-expected gross margins although power & fuel costs remained at elevated levels. Overall, consolidated operating profit/net profit was up 91%/114% y-o-y. The management retained 15-20% tile volume growth for FY2023 although continued to reframe from guiding on OPM due to volatility in gas prices. It acquired a 51% stake in South Asian Ceramics for Rs. 28.5 crores having 4.8msm ceramic floor tile capacity, which would strengthen its presence in Southern India.

## Key positives

- Tile volumes rose 52.9% y-o-y for Q1FY2023. Operating margins were ahead of estimates despite elevated power & fuel costs.
- Acquisition of stake in Southern region which would strengthen its presence in South India.

## Key negatives

- Power & fuel costs remained at an elevated level at 26.6% of net revenues for Q1FY2023 as against 20.7% in Q4FY2022.
- Working capital days increased by 5 days q-o-q to 57 days due to building of stocks with the commissioning of three new plants.

## Management Commentary

- The management retained tile volume growth guidance of 15-20% y-o-y for FY2023 versus industry growth expectation of 6-7% y-o-y. Post that, the company expects to grow at 15%+ y-o-y in terms of volume for two years.
- The company took a 2% price hike in May 2022 in tiles.
- South Asian Ceramics is expected to generate revenues of Rs. 130 crore and Rs. 180 crores in FY2023 and FY2024 respectively. The EV of the plant is Rs. 120 crores comprising debt of Rs. 60 crores and equity value of Rs. 60 crores.

**Revision in estimates** – We have revised our estimates downwards for FY2023 factoring in lower OPM although broadly retained our FY2024 estimates.

## Our Call

**Valuation – Retain Buy with a revised PT of Rs. 1,300:** Kajaria is expected to be a beneficiary of the strong domestic demand from the housing sector and market share gains from unorganized players. Its increased capacity along with the acquisition of a stake in the Southern plant would aid in healthy volume growth over the next two to three years. The morbid cluster taking a month's shutdown from August 10, 2022 to September 10, 2022 would aid in correcting oversupply and help gain market share for organized players like Kajaria. Outpacing industry growth rates along with normalization of gas prices are strong growth tailwinds for the company over the next two to three years. We have introduced our FY2025E earnings estimates in this note. We retain a Buy rating on the stock with a revised price target (PT) of Rs. 1300.

## Key Risks

Weak macro-economic environments, pressure on realisations and increased gas prices are key risks to our call.

## Valuation (Consolidated)

Particulars	FY22	FY23E	FY24E	FY25E
Revenue	3,705.2	4,599.8	5,351.4	6,196.7
OPM (%)	16.5	14.5	16.5	17.0
Adjusted PAT	377.0	409.9	568.7	697.2
% y-o-y growth	22.4	8.7	38.7	22.6
Adjusted EPS (Rs.)	23.7	25.7	35.7	43.8
P/E (x)	45.3	41.7	30.0	24.5
P/B (x)	8.0	7.2	6.3	5.3
EV/EBITDA (x)	27.0	24.7	18.6	15.6
RoNW (%)	18.9	18.4	22.5	23.5
RoCE (%)	18.3	17.8	21.8	22.8

Source: Company; Sharekhan estimates

## Strong beat on net earnings led by higher than expected revenues and OPM

Kajaria Ceramics Limited (Kajaria) reported a strong beat on net earnings for Q1FY2023 led by higher-than-estimated revenues and OPM. The consolidated revenues at Rs. 1008 crore (up 79.5% y-o-y) in Q1FY23, were led by strong tile volume growth of 52.9% y-o-y (led by a low base, down 10.2% q-o-q) while blended tile realizations were up 17.4% y-o-y (up 1.9% q-o-q). Revenues from the bathware and plywood segments rose by 93% y-o-y and 279.5% y-o-y. Consolidated OPM at 15.2% (up 92 bps y-o-y) surprised positively led by better than expected gross margins although power & fuel costs remained at elevated levels. Hence, consolidated operating profit rose by 91% y-o-y to Rs. 154 crores. Strong operating performance led to a 114% y-o-y rise in consolidated net profit at Rs. 92 crores.

## Capacity additions and expansion plans

The company acquired a 51% stake in South Asian Ceramics Tiles, Telangana by making an investment of up to Rs. 28.50 crores. The annual production capacity of South Asian Ceramics is 4.79msm ceramic floor tiles. The acquisition would strengthen its presence in the Southern region. The plant manufactures two sizes of tiles viz. 50x60 metre and 60x120 metres. It has LPG connection. The plant was started two years back and had been suffering losses due to covid. It expects to generate revenues of Rs. 130 crore and Rs. 180 crore in FY2023 and FY2024 respectively. Additionally, it commissioned 4.20 MSM of ceramic floor tiles capacity at its Gailpur location and 3.80 MSM capacity of value-added glazed vitrified tiles at the Srikalahasti location in the month of May 22. The company also commissioned 4.40 MSM of polished vitrified tiles capacity at Kajaria Vitrified plant at Morbi, Gujarat in the month of April 22.

## Key Conference call takeaways

- ♦ **Guidance:** The management retained tile volume growth guidance of 15-20% y-o-y for FY2023 versus industry growth expectation of 6-7% y-o-y. Post that, the company expects to grow at 15%+ y-o-y in terms of volume for two years. The management continued to reframe from giving guidance on OPM due to uncertainty regarding availability of gas and the geopolitical situation.
- ♦ **Morbi shutdown:** The Morbi cluster would be taking shutdown from 10th August 2022 to 10th September 2022 with 85% of the units to be closed. The company's all JVs and 70% of the outsourced plants will be working. As per management, the development is positive for the organised players as it would correct supply and help in gaining market share.
- ♦ **Exports:** Exports are expected to rise to over Rs. 16,000 crores in FY2023 as against Rs. 12,700 crore in FY2022.
- ♦ **Domestic market:** The domestic market size is expected to grow to Rs. 32,000 crores in FY2023 from Rs. 21,000 crore in FY2022. The metros are having replacement-led demand while tier II and below cities are having real construction-led demand.
- ♦ **Gas prices:** The gas prices during the Q1FY2023 region wise is as follows North – Rs. 52/scm, South – Rs. 60/scm, West – Rs. 67/SCM. The average gas price for the company for Q1FY2023 was Rs. 55/SCM.
- ♦ **Acquisition:** The company acquired a 51% stake in South Asian Ceramics, Telangana having an annual production capacity of 4.79msm ceramic floor tiles for Rs. 28.5 crore. The acquisition would strengthen its presence in the Southern region. The plant manufactures two sizes of tiles viz. 50x60 metre and 60x120 metres. It has an LPG connection. The plant was started two years back and had been suffering losses due to COVID. It expects to generate revenues of Rs. 130 crore and Rs. 180 crores in FY2023 and FY2024 respectively. The EV of the plant is Rs. 120 crore comprising debt of Rs. 60 crores and equity value of Rs. 60 crores.

- ♦ **Capex:** The company would be incurring Rs. 200-250 crores capex each year which will be financed through internal accruals. The company has a dividend policy of 40-50% payout from earnings.
- ♦ **A&P spends:** The A&P spending during Q1FY2023 was Rs. 19 crore. It expects to spend Rs. 100 crores plus during FY2023 as against Rs. 80 crores incurred in FY2022.
- ♦ **Working capital:** The working capital increased by 5 days q-o-q to 57 days on account of building of stocks with the commissioning of three new plants.
- ♦ **Distribution:** It added 50 exclusive showrooms last year. Currently, there are 1700 operative distributors.

Results (Consolidated)

Particulars	Q1FY2023	Q1FY2022	y-o-y%	Q4FY2022	q-o-q%
<b>Net sales</b>	<b>1008.2</b>	<b>561.7</b>	<b>79.5%</b>	<b>1101.8</b>	<b>-8.5%</b>
other income	8.1	6.0	34.8%	7.0	15.1%
Total income	1016.3	567.7	79.0%	1108.8	-8.3%
Total expenses	854.6	481.2	77.6%	935.8	-8.7%
<b>Operating profit</b>	<b>153.6</b>	<b>80.4</b>	<b>91.0%</b>	<b>165.9</b>	<b>-7.4%</b>
Depreciation	32.4	26.5	22.0%	32.6	-0.8%
Interest	3.6	3.0	19.5%	4.0	-9.3%
Exceptional items	0.0	0.0		0.0	
<b>Profit Before Tax</b>	<b>125.7</b>	<b>56.9</b>	<b>121.0%</b>	<b>136.4</b>	<b>-7.8%</b>
Taxes	32.8	15.4	112.4%	39.1	-16.3%
Minority Interest	0.7	-1.6		1.5	
PAT	92.3	43.1	114.4%	95.8	-3.6%
<b>Adjusted PAT</b>	<b>92.3</b>	<b>43.1</b>	<b>114.4%</b>	<b>95.8</b>	<b>-3.6%</b>
EPS (Rs.)	5.8	2.7	114.4%	6.0	-3.6%
<b>Margins</b>					
OPM (%)	15.2%	14.3%	92 bps	15.1%	17 bps
NPM (%)	9.2%	7.7%	149 bps	8.7%	46 bps
Tax rate (%)	26.1%	27.1%	-106 bps	28.7%	-265 bps

Source: Company; Sharekhan Research

## Outlook and Valuation

### ■ Sector View – Expect operations to recover faster

The building materials industry was severely affected by the COVID-19-led lockdown during Q1FY2021, which affected its peak sales period of the year. Additionally, its high fixed cost structure affected OPM, dragging down its net earnings. However, from June, the sector has been one of the fastest in recovery with the easing of lockdowns domestically. The sector has witnessed a 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% as compared to 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.

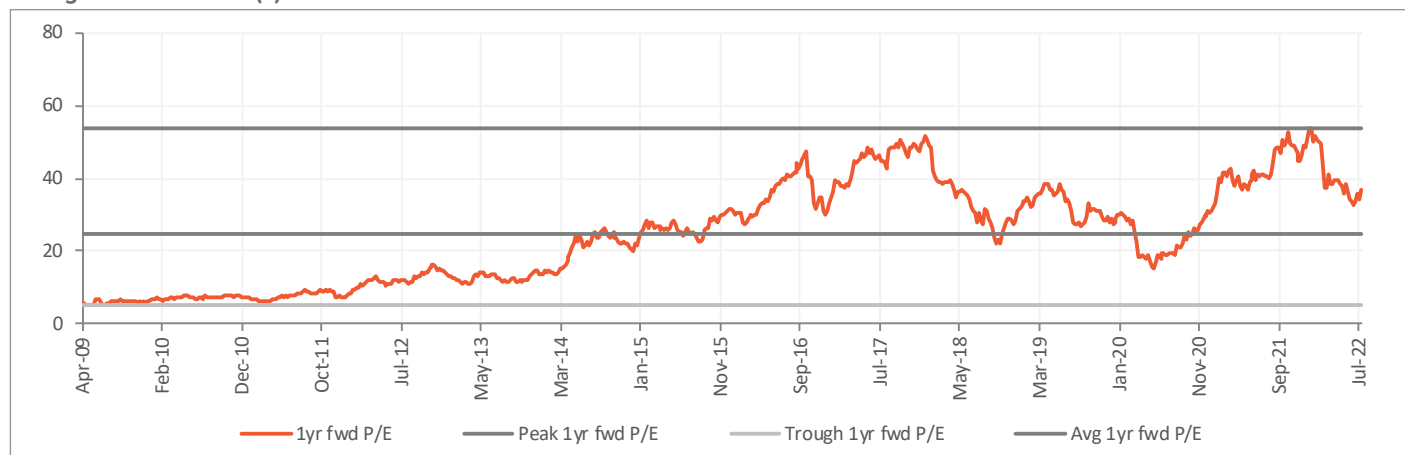
### ■ Company Outlook – Demand environment to remain strong over next couple of years

Kajaria is expected to see an improvement in operations and demand going ahead. The company's asset utilisation has been improving and is expected to grow further. Anti-China sentiments in the US and European countries have boosted exports for the Morbi cluster, which houses ~850 manufacturing units. This has led to an improved pricing environment for organised players such as Kajaria and an increase in market share domestically. The management has guided for 15-20% y-o-y volume growth for FY2023 although reframed from guiding on OPM due to current volatility in gas prices. The company would be investing close to Rs. 200-250 crore per annum capital expenditure over the next three years in augmenting its capacities.

### ■ Valuation – Retain Buy with a revised PT of Rs. 1,300

Kajaria is expected to be a beneficiary of the strong domestic demand from the housing sector and market share gains from unorganized players. Its increased capacity along with the acquisition of a stake in Southern plant would aid in healthy volume growth over the next two to three years. The morbid cluster taking a month's shutdown during August 10, 2022 to September 10, 2022 would aid in correcting oversupply and help gain market share for organized players like Kajaria. Outpacing industry growth rates along with normalization of gas prices are strong growth tailwinds for the company over the next two to three years. We have introduced our FY2025E earnings estimates in this note. We retain a Buy rating on the stock with a revised price target (PT) of Rs. 1300.

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 eighth largest tile manufacturer. The company has an annual capacity of 82.8 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 in 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 an improved pricing environment for organised players such as Kajaria and an increase in market share domestically. Given the strong demand outlook over the next two to three years, the company is undertaking brownfield expansion. Its rising free cash flow generation and high cash surplus would aid in expansion plans without leveraging the balance sheet.

## 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

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by BNP PARIBAS

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