Somany Ceramics (SOMCER)

CMP: ₹ 668 | Target: ₹ 730 (9%) | Target Period: 12-18 months

HOLD

August 11, 2022

Result Update

Gas prices continue to weigh on margins…

About the stock: Somany Ceramics (SCL) is the second largest tiles manufacturers in the domestic tiles market having ~73 MSM capacity and sanitaryware, faucets capacity of 1.15 million (mn) pieces and 0.65 mn pieces, respectively.

- SCL's new capacity of 11 MSM has potential to generate ~₹ 250-300 crore worth of additional revenue (at full capacity) which will drive FY23 growth

Q1FY23 Results: SCL reported a soft performance on the margins front.

- The topline was up 69.5% YoY at ₹ 559.1 crore, on a washout base. Tiles revenues were up 64.4% YoY at ₹ 480 crore with volumes up 42.4% YoY and realisations up 15.5% YoY. QoQ volumes were down 11.5%
- EBITDA was at ₹ 44.9 crore, a decline of ~QoQ%, owing to higher input and gas prices leading to a decline of 20 bps in margins to 8%
- PAT was at ₹ 20.5 crore, up 19.7% QoQ given the lower depreciation, tax rate and higher other income

What should investors do? SCL's share price has declined ~12% over the past five years.

- Gas price uncertainty continues and there remains a risk of further global gas prices spike amid winters (H2) and continued geopolitical tensions. Thus, we downgrade from BUY to **HOLD**

Target Price and Valuation: We value SCL at ₹ 730/share at 22x FY24 P/E amid gas price uncertainty and as we cut margins estimates slightly further.

Key triggers for future price performance:

- New capacity of 11 MSM (with potential to generate revenue of ~₹ 250-300 crore has started contributing. Additionally, greenfield manufacturing facility of slab tile of ~4 MSM/annum in Gujarat is expected to commence production during Q1FY24 at capex of ~₹ 170 crore
- We expect 13% CAGR in tiles volume and realisations CAGR of ~3%, resulting in tiles revenues CAGR of 16.5% over FY22-24 to ₹ 2521 crore
- Any respite in gas price rise

Alternate Stock Idea: Besides SCL, we like Brigade in the real estate space.

- Quasi play on Bengaluru realty
- BUY with a target price of ₹ 595

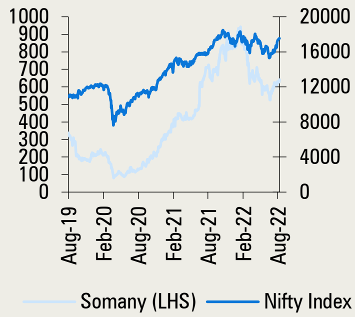
Particulars

Particular	Amount (₹ crore)
Market Capitalization	2,831
Total Debt (FY22)	511
Cash (FY22)	149
EV	3,193
52 week H/L (₹)	970 / 511
Equity capital	8.5
Face value	₹ 2

Shareholding pattern

	Sep-21	Dec-21	Mar-22	Jun-22
Promoters	54.8	54.8	54.8	54.8
DII	17.7	18.0	18.0	18.1
FIIs	2.9	2.5	2.5	2.4
Other	24.7	24.8	24.7	24.7

Price Chart



Key Risks

Key Risk: (i) Better demand; (ii) Continued high gas prices

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Key Financial Summary

₹ crore	FY20	FY21	FY22E	5 yr CAGR (FY17-22)	FY23E	FY24E	2 yr CAGR FY22-24E
Net Sales	1,600.2	1,641.4	2,082.7	9.8%	2,512.3	2,854.8	17.1%
EBITDA	131.4	190.2	206.5	-6.0%	238.1	300.3	20.6%
EBITDA Margin (%)	8.2	11.6	9.9		9.5	10.5	
PAT	15.0	57.0	88.7	-11.1%	94.9	141.1	26.2%
EPS (₹) *	3.5	13.5	20.9		22.4	33.3	
P/E (x)	188.7	49.6	31.9		29.8	20.1	
EV/EBITDA (x)	24.9	15.9	15.2		13.4	10.2	
RoNW (%)	2.5	8.9	12.2		11.7	15.3	
RoCE (%)	6.5	11.1	10.7		11.6	14.9	

Source: Company, ICICI Direct Research

Key business highlight and outlook

- **Q1FY23 performance**: SCL has witnessed a marked improvement in its performance during Q1FY23 wherein sales volume, revenue improved 42%, 67%, respectively, on a YoY basis to 14.25 MSM, ₹ 540 crore on a depressed base of Q1FY22, which was impacted by Covid second wave. Capacity utilisation remained elevated at 85% for tiles segment during Q1FY23. Overall tiles production was at 12.3 MSM (own plant: 6.5 MSM, JVs: 5.8 MSM). We note that QoQ volumes were down 11.5%. **Going forward, the management has guided for ~20% YoY revenues growth in FY23 to be driven by a) healthy product demand from real estate sector, b) no-major supply side constraint, and c) commencement of operation of new plants**
- **Margin guidance**: Operating margin remained under pressure and was at 6.9% during Q1FY23 (vs. 7.3% in FY22) primarily impacted by rise in gas and commodity prices and increased freight and packaging cost. **Going forward, the company is focusing more on value added sales and improving share of GVT to overall tiles segment' sales (30% in Q1FY23; 33-34% by FY23-end) in order to improve margin performance over medium to longer term**
- **Price hike**: SCL **undertook price hikes of ~2.5-3% during mid-April 2022 and mid-June 2022 across its major product** category in order to partially offset increase in input and gas prices. **The company may contemplate another price hike depending on gas prices and Morbi players (undertaking price hikes)**
- **Input prices**: After a drastic increase in gas prices over the past few quarters, it appears to have stabilised at an elevated level with minimum level of volatility witnessed over past few weeks. **For North-based Kassar plant, gas prices (linked to three month's average of crude) is currently at ~₹ 64/SCM (vs ~₹ 36 /SCM during Q1FY22; ~₹ 58 /SCM during Q1FY23).** Similarly, **for Kadi (Morbi plant), gas prices went up to ~₹ 67/SCM (vs ~₹ 39/SCM during Q1FY23; ~₹ 65/SCM during Q2FY23).** Also, **gas prices for southern plant have climbed up currently to ~90/SCM (vs ~₹ 34/SCM during Q1FY22; ~₹ 71/SCM during Q1FY23).** However, the **company has converted two of its plant at Morbi and transforming another one to use propane (₹ 7-8/SCM cheaper than gas)** by undertaking necessary permission from relevant authorities and incurring minimal required capex (of ~₹ 1 crore/plant)
- **Sanitaryware division**: In sanitaryware division, SCL witnessed robust 92.5% YoY growth in sales value (to ₹ 123.4 crore). Additionally, utilisation improved to 88% during Q1FY23 with better product demand (vs. 53% during Q4FY22) and the management expects utilisation to reach at optimum level by FY23-end. Overall, the management has guided for 30-35% YoY growth during FY23 (to ₹ 280-300 crore). The company may look for capacity expansion in FY24 post reaching of 100% utilisation
- **Update on Morbi players**: Inflated raw material costs, increased freight rates and shortage of containers have resulted in a fall in demand for tiles products. Therefore, **tiles makers located at Morbi have huge unsold inventory at their warehouses. With a view to clear that inventory, units in Morbi (except 50-60 plants out of 800 total units) have collectively decided to shut production for 30 days from August 10**. The **shutdown is also due to high gas prices and inadequate working capital**. However, **SCL's JVs manufacturing unit at Morbi would be operational.** Having said that, the company believes that **transporters may go on strike for 10-12 days at Morbi location very soon. This is likely to create logistical issues for operational plants**
- **A&D Spends:** SCL's A&D spends during Q1FY23 were at ~2-2.5% of overall sales, which is likely to improve ahead with ramping-up of brand building exercise, going ahead
- **Expansion plans:** SCL has successfully commissioned its three new plants in north, west and south (total capacity: 11 MSM). Additionally, the company has also announced set-up of greenfield manufacturing facility of large format/ slab tile of ~4.5 MSM/annum in Gujarat (capex: ~₹ 170 crore to be funded mainly via internal accruals; revenue potential: ~₹ 250 crore). The machineries have been orders and the management expects production to commence from Q1FY24-end. Also, the company has performed debottlenecking exercise for faucet plant located at Derabassi, Punjab which is likely to double its capacity to 1.3 mn pcs by Q2FY23-end.

The capacity additions are margin attractive with higher value added production

- **Dealers network**: SCL has built a strong distribution network consisting of 400+ showrooms, 2,900+ active dealers. The company added 70 dealers during Q1FY23 (vs. 200 dealers during FY22) mainly in the tier-II, III and IV cities as SCL's focused area remains non-metro regions. Overall, the company has guided for net addition of ~300 dealers during FY23E (50% likely to be exclusive dealers)
- **Working Capital**: Working capital days at the end of Q1FY23 have largely remained steady at 46 days (vs. 45 days at FY22-end) backed by better inventory and receivables management

Exhibit 1: Variance Analysis

Particular	Q1FY23	Q1FY22	YoY (Chg %)	Q4FY22	QoQ (Chg %)	Comments
Net Sales	559.1	329.9	69.5	616.8	-9.3	Tiles Revenues were up 64.4% YoY at ₹ 480 crore with volumes 42.4% YoY and realisations up 15.5% YoY. QoQ volumes were down 11.5%
Other Income	4.0	5.6	-29.0	1.5	173.8	
Raw Material Expense	148.1	91.0	62.9	127.7	16.0	
Purchase of Traded Goods	131.8	64.7	103.8	140.7	-6.3	
Power & Fuel	170.6	74.6	128.6	137.0	24.5	
Employee benefit expenses	71.2	60.1	18.5	66.0	7.9	
Other Expenses	56.2	43.7	28.6	67.2	-16.4	
EBITDA	44.9	23.1	94.5	50.6	-11.3	
EBITDA Margin (%)	8.0	7.0	104 bps	8.2	-17 bps	
Depreciation	15.4	15.1	2.3	17.1	-9.7	
Interest	7.3	8.1	-10.3	6.4	13.6	
PBT	26.3	5.5	373.2	28.7	-8.4	
Taxes	6.9	2.1	233.3	8.1	-14.9	
PAT	20.5	4.5	359.5	17.2	19.7	

Source: Company, ICICI Direct Research

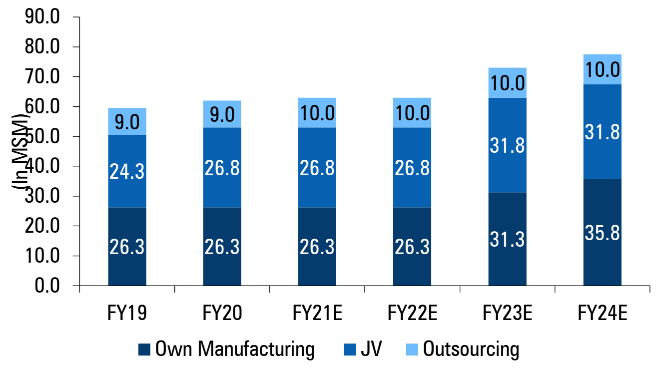
Exhibit 2: Change in estimates

Particulars	FY21	FY22	FY23E			FY24E			
			Old	New	Change	Old	New	Change	Comments
Revenue	1641.4	2082.7	2572.4	2512.3	-2.3	2824.0	2854.8	1.1	Realign estimates
EBITDA	190.2	206.5	256.1	238.1	-7.0	311.1	300.3	-3.5	
EBITDA Margin (%)	11.6	9.9	10.0	9.5	-48 bps	11.0	10.5	-49 bps	Lower the margins to account for elevated gas price
Adjusted PAT	57.0	88.7	109.2	94.9	-13.1	150.5	141.1	-6.2	
EPS	13.5	20.9	25.8	22.4	-13.1	35.5	33.3	-6.2	

Source: Company, ICICI Direct Research

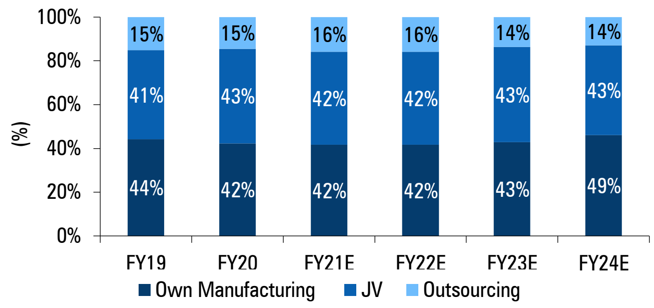
Company Analysis

Exhibit 4: Capacity break-up (in MSM)



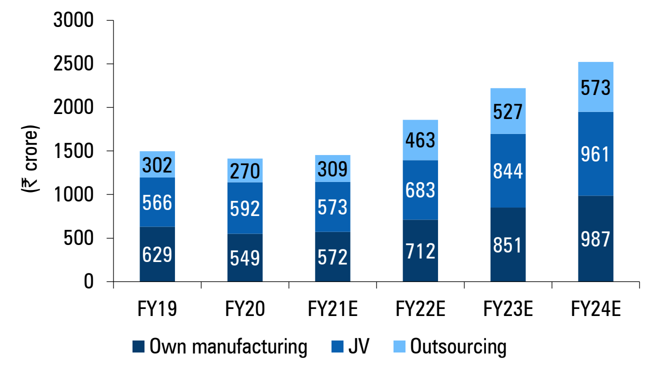
Source: Company, ICICI Direct Research

Exhibit 5: Capacity break-up (%)



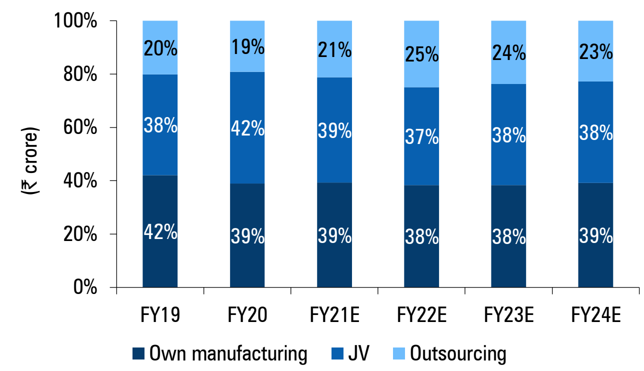
Source: Company, ICICI Direct Research

Exhibit 6: Revenue break-up (₹ crore)



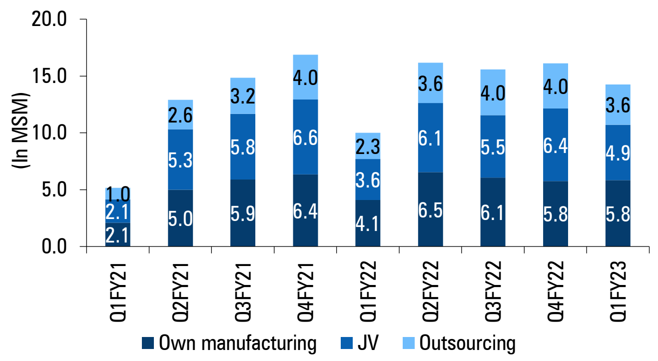
Source: Company, ICICI Direct Research

Exhibit 7: Revenue break-up (%)



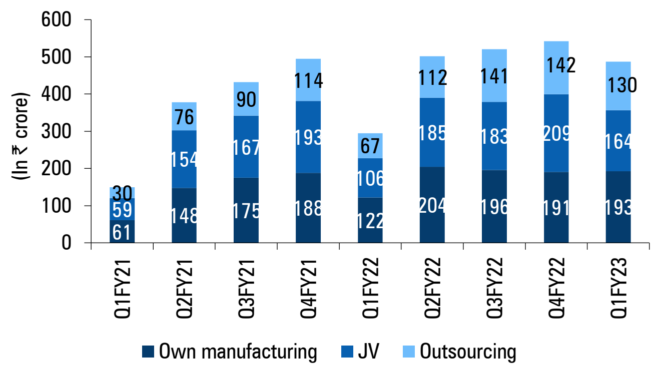
Source: Company, ICICI Direct Research

Exhibit 8: Quarterly standalone sales volumes (in MSM)



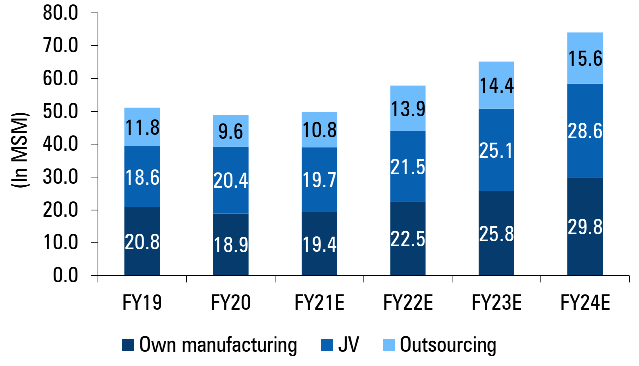
Source: Company, ICICI Direct Research

Exhibit 9: Quarterly standalone sales value



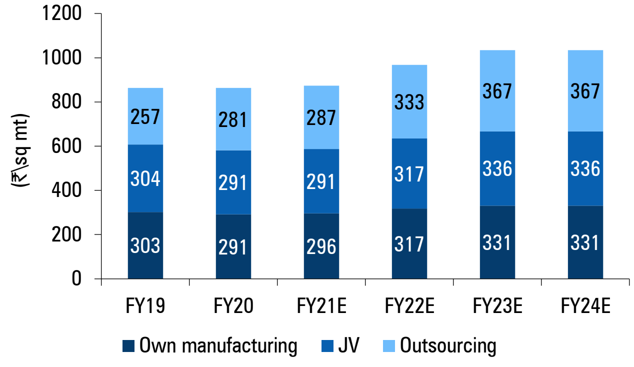
Source: Company, ICICI Direct Research

Exhibit 10: Model-wise standalone sales volumes break-up



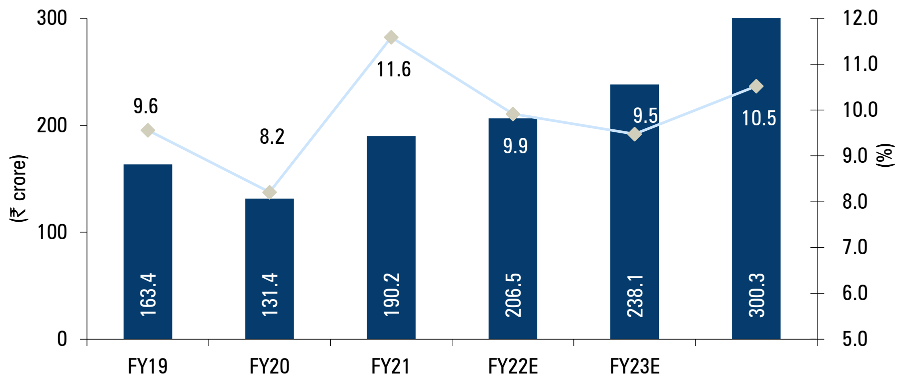
Source: Company, ICICI Direct Research

Exhibit 11: Average realisation break-up



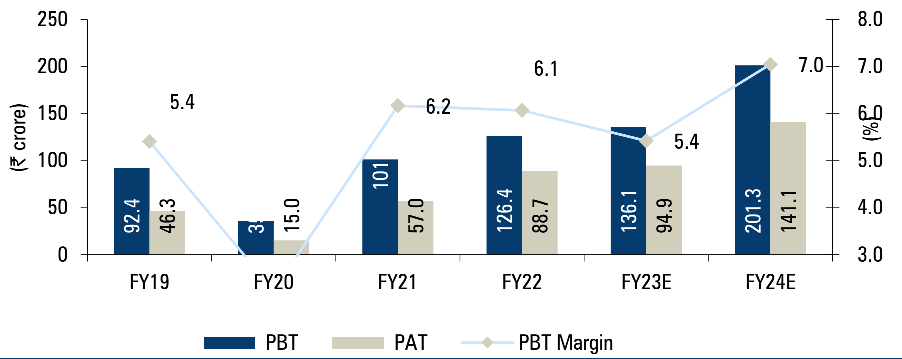
Source: Company, ICICI Direct Research

Exhibit 12: Consolidated EBITDA and EBITDA margin trend



Source: Company, ICICI Direct Research

Exhibit 13: Consolidated PBT, PAT margin trend



Source: Company, ICICI Direct Research

Financial summary

Exhibit 14: Profit and loss statement ₹ crore

(Year-end March)	FY21	FY22	FY23E	FY24E
Net Sales	1,641.4	2,082.7	2,512.3	2,854.8
Other Income	12.8	13.4	20.0	22.0
Total Revenue	**1,663.4**	**2,107.9**	**2,544.3**	**2,888.8**
Raw Material Expense	393.8	487.8	590.4	670.9
Purchase of Traded Goods	307.9	447.2	477.3	539.5
(Increase)/Decrease in Inventorie:	78.9	(14.4)	25.1	42.8
Employee benefit expenses	225.2	257.1	288.9	328.3
Other Expenses	177.4	229.3	263.8	299.7
Total Operating Expenditure	**1,460.4**	**1,887.9**	**2,286.2**	**2,566.4**
EBITDA	**190.2**	**206.5**	**238.1**	**300.3**
Interest	40.1	29.6	43.5	39.2
Depreciation	61.6	64.0	78.5	81.9
PBT	**101.2**	**126.4**	**136.1**	**201.3**
Total Tax	22.2	33.0	35.3	52.1
PAT before MI	60.6	93.4	100.9	149.1
Minority Interest	3.6	4.7	6.0	8.0
PAT	**57.0**	**88.7**	**94.9**	**141.1**
YoY growth	280.1%	55.6%	7.0%	48.8%
EPS (Diluted)	**13.5**	**20.9**	**22.4**	**33.3**

Source: Company, ICICI Direct Research

Exhibit 15: Cash flow statement ₹ crore

(Year-end March)	FY21	FY22	FY23E	FY24E
Profit after Tax	**57.0**	**88.7**	**109.2**	**150.5**
Depreciation	61.6	64.0	78.5	81.9
Interest Paid	40.1	29.6	43.5	39.2
Cash Flow before WC changes	**168.0**	**173.6**	**217.2**	**257.6**
Net Increase in Current Assets	169.4	(51.1)	(134.7)	(69.6)
Net Increase in Current Liabilities	33.4	56.2	82.7	41.1
Net CF from Op. Activities	**370.8**	**178.7**	**165.2**	**229.0**
(Purchase)/Sale of Fixed Assets	(62.6)	(266.4)	(170.0)	(50.0)
Others	(8.1)	41.1	20.0	22.0
Net CF from Inv. Activities	**(70.7)**	**(225.3)**	**(150.0)**	**(28.0)**
Proceeds/Repayment of Debt	(74.7)	87.8	(0.0)	(50.0)
Dividend and Dividend Tax	(10.2)	-	(10.2)	(30.1)
Interest Paid	(40.1)	(29.6)	(43.5)	(39.2)
Net CF from Fin. Activities	**(125.0)**	**58.1**	**(53.6)**	**(119.3)**
Net Cash flow	**129.0**	**(0.6)**	**(38.4)**	**81.7**
Opening Cash/ Cash Equivalent	20.1	149.1	148.6	110.2
Cl. Cash/ Cash Equivalent	**149.1**	**148.6**	**110.2**	**191.9**

Source: Company, ICICI Direct Research

Exhibit 16: Balance sheet ₹ crore

(Year-end March)	FY21	FY22	FY23E	FY24E
Liabilities				
Share Capital	8.5	8.5	8.5	8.5
Reserves & Surplus	632.3	717.8	802.5	915.4
Total Shareholders funds	640.7	726.3	811.0	923.9
Secured Loan	272.0	336.6	333.2	283.2
Unsecured Loan	151.4	174.6	178.0	178.0
Total Debt	423.5	511.2	511.2	461.2
Deferred Tax Liability	37.1	36.4	36.4	36.4
Minority Interest	99.7	107.6	113.6	121.6
Other Long Term Liabilities	66.9	63.2	63.2	63.2
Long Term Provisions	8.0	8.7	8.7	8.7
Liability side total	**1,276**	**1,453**	**1,544**	**1,615**
Assets				
Gross Block	932.0	991.1	1,161.1	1,211.1
Net Block	749.3	744.5	836.0	804.1
Capital WIP	8.6	226.7	226.7	226.7
Current Investments	89.8	60.0	60.0	60.0
Long-term loans and advances	4.6	-	-	-
Inventories	245.5	273.7	330.4	375.4
Sundry Debtors	221.1	236.8	285.7	324.6
Loans and Advances	10.9	3.0	3.6	4.1
Other Current Assets	48.9	63.9	75.7	86.0
Cash	149.1	148.6	102.7	166.6
Total Current Assets	765.2	786.0	858.1	1,016.8
Creditors	183.9	225.5	275.3	312.8
Provisions	1.6	1.7	1.7	1.7
Other Current Liabilities	97.2	111.7	134.7	153.1
Total Current Liabilities	282.7	338.9	411.8	467.7
Net Current Assets	482.5	447.1	446.3	549.1
Assets side total	**1,276**	**1,453**	**1,544**	**1,615**

Source: Company, ICICI Direct Research

Exhibit 17: Key ratios

(Year-end March)	FY21	FY22	FY23E	FY24E
Per Share Data				
EPS	13.5	20.9	22.4	33.3
Cash EPS	28.0	36.0	40.9	52.6
BV	151.2	171.4	191.4	218.0
Revenue per Share	387.3	491.4	592.8	673.6
Dividend per share	2.4	-	2.4	5.0
Operating Ratios				
EBITDA / Total Operating Income	9.5	8.2	11.5	9.9
PAT / Total Operating Income	2.7	0.9	3.5	4.2
Inventory Days	55	48	48	48
Debtor Days	49	42	42	42
Creditor Days	41	40	40	40
Return Ratios				
RoE	8.9	12.2	11.7	15.3
RoCE	11.1	10.7	11.6	14.9
RoIC	12.5	14.0	13.8	18.8
Valuation Ratios				
EV / EBITDA	15.9	15.2	13.4	10.2
P/E	49.6	31.9	29.8	20.1
EV / Net Sales	1.8	1.5	1.3	1.1
Market Cap / Sales	1.7	1.4	1.1	1.0
Price to Book Value	4.4	3.9	3.5	3.1
Turnover Ratios				
Asset turnover	1.3	1.4	1.6	1.8
Gross Block Turnover	1.7	2.1	2.2	2.4
Solvency Ratios				
Net Debt / Equity	0.3	0.4	0.4	0.3
Current Ratio	1.9	1.7	1.7	1.7
Debt / EBITDA	1.0	1.5	1.5	0.8
Quick Ratio	**1.0**	**0.9**	**0.9**	**0.9**

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%

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