

## Margins to improve in H2FY23...

**About the stock:** Kajaria Ceramics is the largest manufacturer of ceramic/vitrified tiles in India with current annual capacity of 84.5 million square meters (MSM).

- Apart from completed capex of ₹ 250 crore on tiles, it is adding 3 MSM brownfield capex in Sikandrabad (~₹ 81 crore capex) and setting up a plant of 8 MSM in Nepal in JV with an investment of ~₹ 125 crore

**Update:** Kajaria is likely to witness an improvement in margins in H2FY23.

- The management has guided for ~15% YoY volume growth in the tiles segment during FY23, implying ~11% in H2FY23 with October, 2022 being relatively soft amid festivities. We believe while Q3 could witness modest volume growth, double digit growth is likely from Q4FY22 with underlying real estate demand remaining robust. Also, the company expects minimum 200 bps improvement in margin (to 14%+) in H2FY23 with relaxation in gas prices, use of alternate fuel and softening in raw material costs
- The company has started using LPG partly as an alternate to gas from November 2022 at Srikalahasti, Morbi and Gailpur plants in view of elevated gas prices. The company's average fuel price is likely to come down to ₹ 55/SCM in Q3FY23 (vs. ₹ 62/SCM in Q2FY23) with softening in gas prices and use of LPG as an alternate fuel

**What should investors do?** Kajaria's share price has grown at ~9% CAGR over the past five years.

- Kajaria with a net cash balance sheet and superior brand, is a solid play on the tiles sector with expanding reach to tier II/III cities. We maintain our **BUY** rating on the stock.

**Target Price and Valuation:** We value Kajaria at ₹ 1340/share, at 36x FY25 P/E.

### Key triggers for future price performance:

- We expect ~12% CAGR in tiles volume and realisations CAGR of ~3%, resulting in tiles revenues CAGR of ~16% over FY22-25 to ₹ 5237 crore
- The increased dividend payout (~45% vs. 20-25%, earlier) is likely to improve return ratios (RoCEs likely at 25%+ in FY25E vs. ~21% in FY22)

**Alternate Stock Idea:** Besides Kajaria, we like Century Ply in buildings materials.

- A play on leadership in the wood panel industry
- BUY with a target price of ₹ 695

### Key Financial Summary

(₹ crore)	FY20	FY21	FY22	5 yr CAGR (FY17-22)	FY23E	FY24E	FY25E	3 yr CAGR (FY22-25E)
Net Sales	2,808.0	2,780.9	3,705.2	7.8%	4,544.0	5,264.9	5,816.7	16.2%
EBITDA	415.9	508.8	610.8	4.2%	635.1	842.3	931.8	15.1%
EBITDA Margin (%)	14.8	18.3	16.5		14.0	16.0	16.0	
PAT	255.3	308.1	377.1	8.3%	377.5	532.6	591.1	16.2%
EPS (₹)	16.1	19.4	23.7		23.7	33.5	37.2	
P/E (x)	68.9	57.1	46.7		46.6	33.0	29.8	
P/B (x)	10.3	9.4	8.3		7.6	6.8	6.0	
EV/EBITDA (x)	42.0	33.9	28.3		27.6	20.7	18.5	
RoCE (%)	16.3	19.7	21.5		20.3	25.1	25.0	
RoE	14.9	16.5	17.8		16.3	20.5	20.1	

Source: Company, ICICI Direct Research

## Kajaria

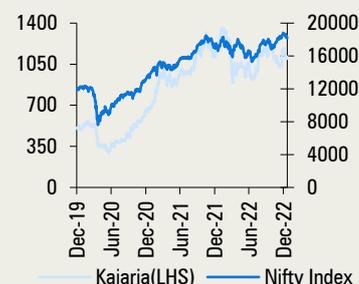
### Particulars

Particular	Amount (₹ crore)
Market Capitalization	17,589
Total Debt (FY22)	128
Cash (FY22)	424
EV	17,293
52 week H/L (₹)	1375 / 885
Equity capital	15.9
Face value (₹)	1.0

### Shareholding pattern

	Dec-21	Mar-22	Jun-22	Sep-22
Promoters	47.5	47.5	47.5	47.5
DII	16.8	19.7	21.8	22.2
FII	22.5	21.3	19.6	19.4
Other	13.3	11.5	11.2	10.9

### Price Chart



### Key Risks

**Key Risk:** (i) Slowdown in demand; (ii) Gas price rise

### Research Analyst

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## Q2FY23 business highlight and outlook

- Volume driver and current volume traction:** Kajaria's sales volume in the tiles segment improved merely by 0.5% (to 24.9 MSM) on a YoY basis during Q2FY23 mainly impacted by a subdued demand scenario and disruptions in natural gas supply followed by unprecedented increase in gas cost. However, revenue improved 11.5% YoY (to ₹ 983.9 crore) with better realisation and change in product mix (mix in volume terms: Ceramics - 46%; Vitrified - 26%; GVT - 28%). Further, higher gas prices and ad spends have impacted EBITDA margins in Q2FY23, which was at 12% (down 653 bps YoY; down 222 QoQ). Going forward, the management is confident of a gradual demand pickup during the post festive seasons with revived customer sentiments, continued traction in the real estate sector, upped re-construction/renovation and the government's focus on infrastructure spending in spite of high input costs and increasing interest rates
- Guidance:** The management has cautiously guided for ~15% YoY volume growth in the tiles segment during FY23, likely to be driven by a) expected rise in demand from Tier II and below cities, b) healthy capacity utilisation, c) expected increase in Kajaria's capacity, d) enhanced distribution network and e) strong brand recall. Also, the company expects minimum 200 bps improvement in margin (to 14%+) during H2FY23 compared to Q2FY23 with relaxation in gas prices, use of alternate fuel and softening in raw material costs
- Gas price rise and use of alternate fuel:** Gas prices for the industry continued to remain at elevated levels during Q2FY23. For Kajaria, average gas prices for Q2FY23 in its northern, southern and Morbi plants were at ~₹ 60/SCM, ~₹ 69/SCM and ₹ 69/SCM, respectively (vs. average gas prices in its northern, southern and Morbi plants during Q1FY23 at ~₹ 52/SCM, ~₹ 60/SCM and ₹ 67/SCM, respectively). Going forward, the management expects gas prices to soften as rates at current levels are unsustainable. The company has started using LPG partly as an alternate to gas from November 2022 at Srikalahasti, Morbi and Gailpur plants in view of elevated gas prices over past several quarters. LPG prices are currently hovering at ₹ 53-55/SCM at different locations. Thus, the company's average fuel price is likely to come down to ₹ 55/SCM in Q3FY23 (vs. ₹ 62/SCM in Q2FY23) with softening in gas prices and use of LPG as an alternate fuel
- Expansions:** Kajaria had commissioned 4.4 MSM of PVT capacity at its Morbi (Gujarat) plant during April 2022. The other two projects i.e. 4.2 MSM of ceramic floor tiles at Gailpur plant (Rajasthan) and 3.8 MSM of value added glazed vitrified tiles at Srikalahasti plant (Andhra Pradesh) were also commissioned during May 2022. Further, the company has announced expansion for glazed vitrified tiles capacity of 3 MSM/annum at Sikandrabad plant recently, which will increase the total capacity of the plant from 8.4 MSM/annum to 11.4 MSM/annum at the capex of ₹ 70 crore. The expansion is likely to be completed by September 2023. Additionally, the company is expected to invest ₹ 70 crore to set up a 6 lakh pieces per annum sanitaryware manufacturing facility in Gujarat (revenue potential: ~₹ 150 crore at full capacity utilisation). The expansion is expected to be completed by December 2023. Further, the company is adding new capacity of 6 lakh pieces/annum in its faucet plant at Gailpur, which will take the total capacity to 16 lakh pieces/annum. Estimated cost for this expansion is ~₹ 5 crore and is expected to be completed by November 2022
- Acquisition:** Kajaria has approved acquisition of 51% equity shares of South Asian Ceramic Tiles Pvt Ltd at a consideration of ₹ 28.5 crore and will have capital employed of ~₹ 60 crore. It has a facility at Balanagar, Telangana and manufactures 60 x 60 cm and 60 x 120 cm ceramic floor tiles (annual capacity of 4.8 MSM). The acquisition is mainly targeted to strengthen its foothold in South India thereby enlarging Kajaria's tiles markets to make more dealers, by reducing the transit time and by increasing the rotation of re-ordering by dealers of the company. Capex at the greenfield unit of such capacity would have been ~₹ 120 crore and would have taken 24 months

to commission the plant. The company is targeting revenue of ₹ 130 crore, ₹ 180 crore in FY23, FY24, respectively, from the plant

- **Investment in Nepal:** The board has approved an investment up to ₹ 125 crore (i.e. 50% of project cost of ₹ 250 crore) in a company to be incorporated in Nepal, by way of equity and/or loan, for establishing a tile manufacturing facility in Nepal, with annual capacity of 8 MSM/annum, on a JV basis between the company and various individuals affiliated with Ramesh Corp, Nepal. The plant is likely to get commissioned by March 2024. Kajaria expects tiles production at the Nepal plant to benefit it largely with a rise in market share backed by a) significant market size: Indian manufacturers export tiles worth ₹ 500 crore (25 MSM) to Nepal and b) higher 45% import duty for Indian producers. Margins are expected to be better compared to the Indian plant

**Kajaria with a net cash balance sheet and superior brand, is a solid play on the tiles sector with expanding reach to tier II/III cities.** We believe gas price uncertainty is fully built in and a recovery in margin is likely in H2. **We maintain BUY. We value it at a multiple at 36x FY25E P/E to ascribe a revised target price of ₹ 1340/share.**

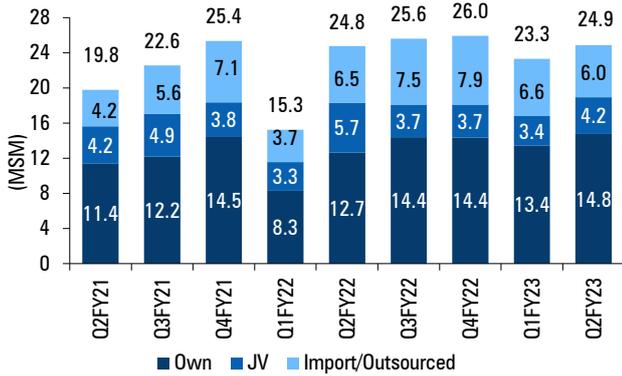
**Exhibit 1: Assumptions**

Volume in MSM	FY21	FY22	Current FY23E	Earlier	New FY24E	Earlier	New FY25	Comments
<b>Production</b>	<b>52.0</b>	<b>68.4</b>	<b>80.4</b>	<b>80.4</b>	<b>85.7</b>	<b>85.7</b>	<b>92.1</b>	
Own	37.7	50.4	62.7	62.7	67.3	67.3	69.0	
JV	14.3	17.9	17.7	17.7	18.5	18.5	23.1	
<b>Sales</b>	<b>75.4</b>	<b>91.7</b>	<b>103.6</b>	<b>103.6</b>	<b>119.2</b>	<b>119.2</b>	<b>129.1</b>	
Own	44.6	51.9	61.2	61.2	67.3	67.3	69.0	
JV	12.1	14.3	15.5	15.5	18.5	18.5	23.1	
Import/Outsourced	18.7	25.4	26.9	26.9	33.5	33.5	37.0	

Source: Company, ICICI Direct Research

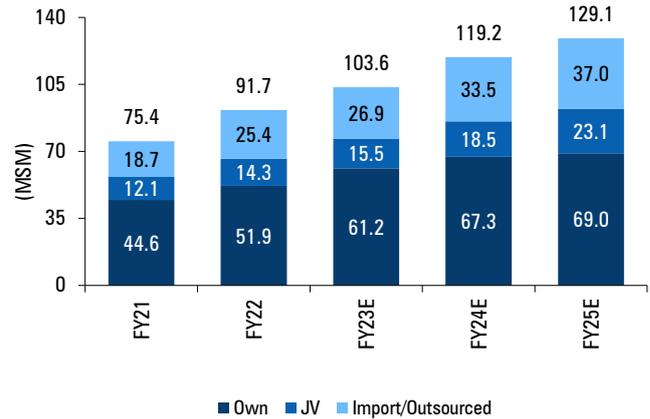
## Company Analysis

Exhibit 2: Quarterly sales volume trend



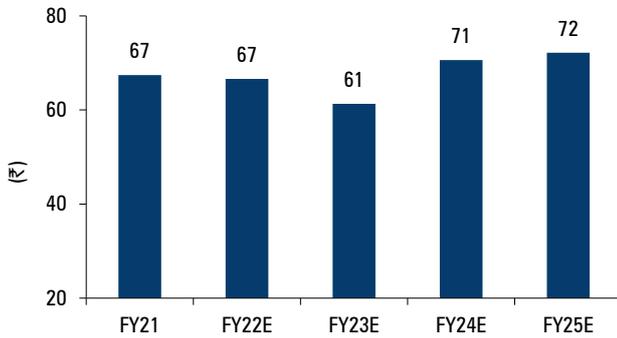
Source: Company, ICICI Direct Research

Exhibit 3: Annual sales volume trend



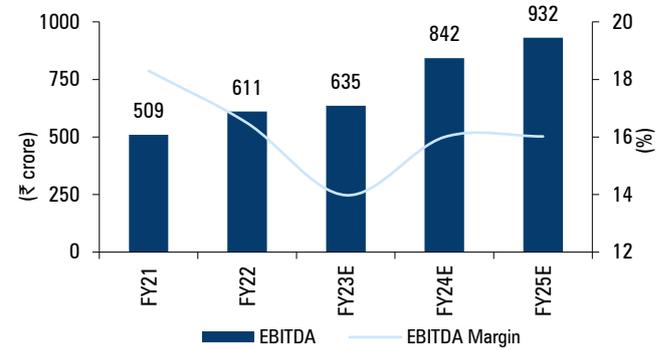
Source: Company, ICICI Direct Research

Exhibit 4: EBITDA/sq metre trend



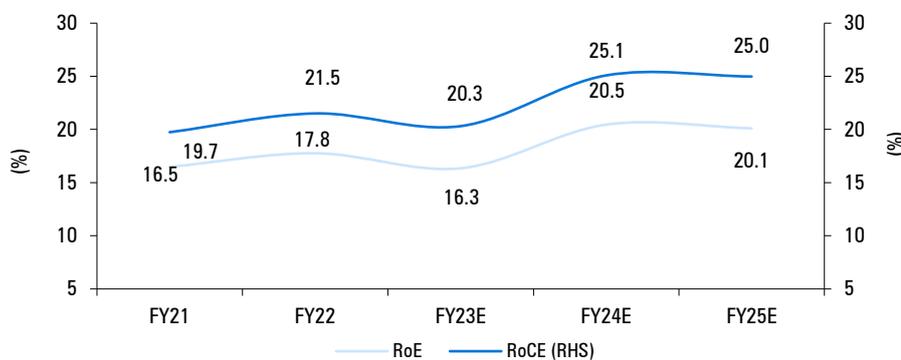
Source: Company, ICICI Direct Research

Exhibit 5: EBITDA and EBITDA margin trend



Source: Company, ICICI Direct Research

Exhibit 6: Return ratios trend



Source: Company, ICICI Direct Research

## Financial summary

Exhibit 7: Profit and loss statement				
	₹ crore			
(₹ Crore)	FY22	FY23E	FY24E	FY25E
<b>Net Sales</b>	<b>3,705.2</b>	<b>4,544.0</b>	<b>5,264.9</b>	<b>5,816.7</b>
Other Operating Income	-	-	-	-
Total operating income	3,705.2	4,544.0	5,264.9	5,816.7
Raw Material Expenses	730.3	817.9	921.4	1,017.9
Cost of Materials Consumed	824.8	1,067.8	1,216.2	1,337.8
Employee benefit expenses	407.7	463.5	526.5	587.5
Other Expenses	1,131.7	1,559.6	1,758.6	1,941.6
Total operating expenses	3,094.4	3,908.9	4,422.6	4,884.9
<b>EBITDA</b>	<b>610.8</b>	<b>635.1</b>	<b>842.3</b>	<b>931.8</b>
Interest	12.7	13.4	13.4	13.4
Depreciation	115.4	134.4	144.2	155.2
Other income	27.6	32.0	35.0	40.0
PBT	510.2	515.6	719.6	803.2
Taxes	127.4	134.1	181.1	202.1
PAT before MI	382.8	381.5	538.6	601.1
Minority Interest	5.8	4.0	6.0	10.0
<b>PAT</b>	<b>377.1</b>	<b>377.5</b>	<b>532.6</b>	<b>591.1</b>
Growth (%)	22.4	0.1	41.1	11.0
<b>EPS (₹)</b>	<b>23.7</b>	<b>23.7</b>	<b>33.5</b>	<b>37.2</b>

Source: Company, ICICI Direct Research

Exhibit 9: Balance sheet				
	₹ crore			
(₹ Crore)	FY22	FY23E	FY24E	FY25E
<b>Liabilities</b>				
Equity Capital	15.9	15.9	15.9	15.9
Reserve and Surplus	2,106.5	2,293.2	2,587.3	2,923.9
Total Shareholders funds	2,122.4	2,309.1	2,603.2	2,939.9
Minority Interest	64.8	68.8	74.8	84.8
Total Debt	127.9	127.9	127.9	127.9
Other Liabilities	98.5	98.5	98.5	98.5
<b>Total Liabilities</b>	<b>2,431.5</b>	<b>2,622.3</b>	<b>2,922.3</b>	<b>3,269.0</b>
<b>Assets</b>				
Gross Block	1,990.0	2,422.2	2,622.2	2,822.2
Less Acc. Dep	851.2	985.7	1,129.9	1,285.1
Net Block	1,138.8	1,436.5	1,492.3	1,537.1
Net Intangibles Assets	10.8	10.8	10.8	10.8
Capital WIP	263.4	263.4	263.4	263.4
Total Fixed Assets	1,413.0	1,710.7	1,766.5	1,811.3
<b>Investments</b>				
Inventory	465.9	572.7	663.5	733.1
Sundry Debtors	513.3	647.4	750.1	828.7
Loans & Advances	138.3	169.6	196.5	217.1
Cash & Bank Balances	424.4	170.8	302.6	518.4
Other Current Assets	31.8	31.8	31.8	31.8
Total Current Assets	1,573.6	1,592.2	1,944.4	2,329.0
Trade Payable	298.1	365.6	423.6	468.0
Other Current Liabilities	248.9	305.2	353.7	390.7
Provisions	8.0	9.8	11.3	12.5
Net Current Assets	1,018.6	911.5	1,155.8	1,457.7
<b>Total Assets</b>	<b>2,431.5</b>	<b>2,622.3</b>	<b>2,922.3</b>	<b>3,269.0</b>

Source: Company, ICICI Direct Research

Exhibit 8: Cash flow statement				
	₹ crore			
(₹ Crore)	FY22	FY23E	FY24E	FY25E
<b>Profit after Tax</b>	<b>377.1</b>	<b>377.5</b>	<b>532.6</b>	<b>591.1</b>
Depreciation	115.4	134.4	144.2	155.2
Interest	12.7	13.4	13.4	13.4
Others	99.9	102.1	146.1	162.1
Cash Flow before wc changes	605.0	627.5	836.3	921.8
Net Increase in Current Assets	(277.7)	(272.2)	(220.5)	(168.8)
Net Increase in Current Liabilities	174.6	125.6	108.0	82.7
<b>Net CF from operating activities</b>	<b>377.1</b>	<b>346.9</b>	<b>542.7</b>	<b>633.6</b>
(Purchase)/Sale of Fixed Assets	(321.0)	(432.2)	(200.0)	(200.0)
<b>Net CF from Investing activities</b>	<b>(288.4)</b>	<b>(400.2)</b>	<b>(165.0)</b>	<b>(160.0)</b>
Inc / (Dec) in Equity Capital	3.8	(0.0)	-	-
Dividend	(127.3)	(190.8)	(238.5)	(254.4)
Interest paid	(12.7)	(13.4)	(13.4)	(13.4)
Inc / (Dec) in Secured Loans	30.9	-	-	-
Inc / (Dec) in Unsecured Loans	(1.8)	-	-	-
<b>Net CF from Financing activities</b>	<b>(107.0)</b>	<b>(200.2)</b>	<b>(245.9)</b>	<b>(257.8)</b>
Net Cash flow	(18.4)	(253.6)	131.8	215.8
Opening Cash	442.7	424.4	170.8	302.6
<b>Closing Cash/ Cash Equivalent</b>	<b>424.4</b>	<b>170.8</b>	<b>302.6</b>	<b>518.4</b>

Source: Company, ICICI Direct Research

Exhibit 10: Key ratios				
	FY22	FY23E	FY24E	FY25E
<b>Per Share Data (₹)</b>				
EPS - Diluted	23.7	23.7	33.5	37.2
Cash EPS	31.0	32.2	42.6	46.9
Book Value	133.5	145.2	163.7	184.9
Dividend per share	11.0	14.0	15.0	16.0
<b>Operating Ratios (%)</b>				
EBITDA / Net Sales	16.5	14.0	16.0	16.0
PAT / Net Sales	10.2	8.3	10.1	10.2
Inventory Days	46	46	46	46
Debtor Days	51	52	52	52
Creditor Days	29	29	29	29
<b>Return Ratios (%)</b>				
RoNW	17.8	16.3	20.5	20.1
RoCE	21.5	20.3	25.1	25.0
RoIC	28.6	23.0	29.8	31.4
<b>Valuation Ratios (x)</b>				
EV / EBITDA	28.3	27.6	20.7	18.5
P/E (Diluted)	46.7	46.6	33.0	29.8
EV / Net Sales	4.7	3.9	3.3	3.0
Market Cap / Sales	4.7	3.9	3.3	3.0
Price to Book Value	8.3	7.6	6.8	6.0
Dividend Yield (%)	1.0	1.3	1.4	1.4
<b>Solvency Ratios (x)</b>				
Net Debt / Equity	(0.1)	(0.0)	(0.1)	(0.1)
Debt/EBITDA	0.2	0.2	0.2	0.1
Current Ratio	2.1	2.1	2.1	2.1
<b>Quick Ratio</b>	<b>1.2</b>	<b>1.2</b>	<b>1.2</b>	<b>1.2</b>

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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