

India

**ADD** (no change)

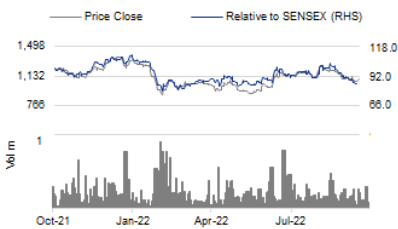
Consensus ratings\*: Buy 25 Hold 4 Sell 0

Current price:	Rs1,089
Target price:	Rs1,227
Previous target:	Rs1,331
Up/downside:	12.7%
InCred Research / Consensus:	-8.8%
Reuters:	KAJR.BO
Bloomberg:	KJC IN
Market cap:	US\$2,096m
	Rs173,357m
Average daily turnover:	US\$2.7m
	Rs226.3m
Current shares o/s:	159.2m
Free float:	52.5%

\*Source: Bloomberg

**Key changes in this note**

- FY23F/24F revenue cut by 1.1%/2.2%.
- FY23F/24F EBITDA cut by 12.4%/6.6%.
- FY23F/24F PAT cut by 15.3%/8.9%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(9.3)	(4.7)	(10.1)
Relative (%)	(14.8)	(9.4)	(11.7)

Major shareholders	% held
Promoters	47.5
Government Pension Fund Global	4.7
Kotak Small Cap Fund	3.8

**Analyst(s)**



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# Kajaria Ceramics

## Energy cost peaks; better days ahead

- 2QFY23 revenue and EBITDA miss was due to weak sales volume (flat yoy) and higher gas cost (+13% qoq). Repeated price hikes reduced demand in 1H.
- Propane gas to cut energy cost in 2HFY23F. Management gave FY23F sales volume growth guidance of +15% yoy and 2HFY23F EBITDA margin of 14%.
- We believe demand recovery is a bigger risk vs. energy cost in 2HFY23F. FY24F-25F to be much better. Retain ADD rating with a lower TP of Rs1,227.

### Inflation led to weak tile demand while higher energy cost hit 2QFY23

Kajaria Ceramics (KCL) reported weak 2QFY23 sales volume of 24.9msm, flat yoy and +7% qoq vs. our estimate of 26msm. Consolidated net sales stood at Rs10.8bn, +10.7% yoy/+7% qoq, largely pricing-led and missed our/Bloomberg consensus estimates by 1-5%. Old high-cost raw material inventory led to lower gross margin of 58%, +144bp yoy and down 480bp qoq. Blended natural gas price rose further to Rs62/scm, +13% qoq leading to a multi-year low EBITDA margin of 12%, down 650bp yoy and 320bp qoq. Hence, EBITDA/PAT were at Rs1.3bn/Rs735m, down 28%/37% yoy, respectively, missing estimates by 15-25%. Sales volume of tiles manufactured in-house was at 14.8msm, +17% yoy, improving its revenue share to 59% vs. 51% yoy. Bathware (sanitaryware and faucets) revenue was at Rs744m, flat yoy, while plywood revenue was at Rs291m, +76% yoy. EBIT margin of the non-tiles segment was close to zero vs. 7% yoy and 4.4% qoq.

### Management cautious on demand; energy cost may fall in 2HFY23F

Management indicated softening demand trend for tiles/bathware in 1H and is cautiously optimistic of meeting its sales volume guidance of +15% yoy for FY23F. At a few existing units (Srikalahasthi, Gailpur, & Morbi), KCL has started using propane gas (~15-20% cheaper than natural gas) besides natural gas from last month which will cut blended energy cost in 2HFY23F. Management gave guidance of ~10% savings in gas cost (~Rs55/scm) and EBITDA margin of at least 14% for 2HFY23F. Given the rising mix of bigger slab tiles, KCL plans to expand its tile adhesive/grout business (1HFY23 sales: Rs173m; FY23F guidance: Rs500m). Capex will be ~Rs5.5-6bn over FY23F-24F including Nepal greenfield plant (8msm, Rs1.25bn) and Indian brownfield expansions (~15msm).

### Change in our estimates; valuation and risks; retain ADD rating

We incorporate 1HFY23 actuals, capacity changes, new capex plans for FY23F/24F and also introduce FY25F estimates. Our revenue estimates largely remain unchanged (cut by 1-2%) while we cut our EBITDA margin estimates to 14%/16% from 15.8%/16.7% for FY23F/24F, respectively. We view demand recovery as a bigger risk vs. energy cost in 2HFY23F. We expect FY24F/25F to be much stronger as tile prices as well as cost cool-off. We estimate revenue/EBITDA/PAT CAGR of 15%/25%/28%, respectively, over FY23F-25F. We retain ADD rating on KCL with a lower target price of Rs1,227 (Rs1,331 earlier) retaining exit P/E of 38x (five-year mean). Downside risks: Slowing demand, higher gas prices, and low new business margins.

### Financial Summary

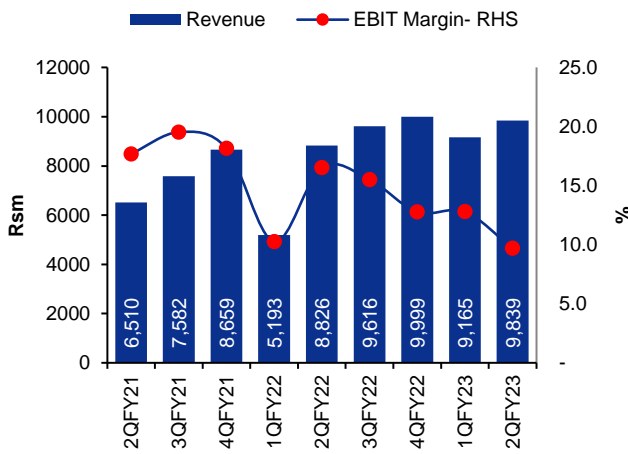
	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Revenue (Rsm)	27,809	37,052	44,897	51,162	59,069
Operating EBITDA (Rsm)	5,088	6,107	6,263	8,160	9,717
Net Profit (Rsm)	3,081	3,770	3,746	5,139	6,165
Core EPS (Rs)	19.4	23.7	23.7	32.3	38.7
Core EPS Growth	20.6%	22.3%	0.1%	36.2%	20.0%
FD Core P/E (x)	56.21	45.96	46.27	33.73	28.11
DPS (Rs)	10.0	11.0	12.0	15.0	18.5
Dividend Yield	0.92%	1.01%	1.10%	1.38%	1.70%
EV/EBITDA (x)	33.47	27.99	27.43	20.97	17.43
P/FCFE (x)	94.61	(188.15)	85.42	63.65	23.34
Net Gearing	(18.1%)	(13.6%)	(9.2%)	(10.8%)	(15.8%)
P/BV (x)	9.27	8.16	7.52	6.72	5.97
ROE	17.2%	18.9%	17.0%	21.0%	22.5%
% Change In Core EPS Estimates			(15.49%)	(8.99%)	
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

## 2QFY23 earnings-call highlights

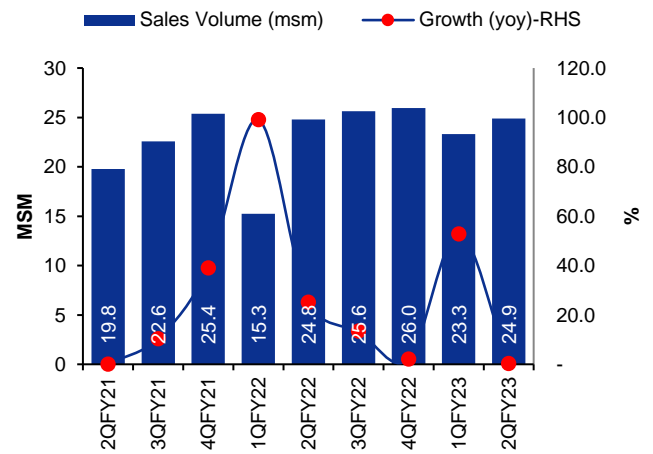
- **Volume and revenue mix:** Sales volume mix in the tiles segment was as follows: ceramics 46%, PVT 26%, and GVT 28%. In terms of revenue, ceramics accounted for 40%, PVT 27% and GVT 33% during 2QFY23.
- **Price hikes:** The company took a price hike of 2% in the tiles segment in Sep 2022. This was lower than the proportionate cost increase during 2QFY23, impacting margins. Owing to gas prices declining marginally along with the plan to blend propane gas for tile production, no more product price hikes are planned going ahead.
- **Distribution network:** KCL had a dealer network comprising 1,700 dealers as at end-Mar 2022. It plans to add nearly 400-450 dealers over the next three years. 1HFY23 saw an addition of 75 dealers. The plan is to add nearly 125 dealers in 2HFY23F and 125 each in FY24F/25F.
- **Gas prices:** The average gas price in North India was Rs60/scm while in South and West India plants it averaged at Rs69/ scm in 2QFY23 for KCL. The overall average gas price for the company during the quarter was Rs62/scm. KCL expects average gas price to decline to Rs55/scm in 3QFY23F.
- **Use of propane:** KCL has started using propane as an alternative fuel in addition to natural gas at three plant locations – Srikalahasthi, Gailpur and Morbi. Propane is currently 15-20% cheaper than natural gas and would reduce the overall energy cost for the company going ahead. The capex for creation of propane infrastructure at these plants was minimal, as per management.
- **Update on Nepal joint venture:** KCL entered into a manufacturing joint venture (50:50) in Nepal with a local partner (Ramesh Corp) for a total capacity of 8msm (ceramic: 4msm + GVT: 4msm) at a total capex outlay of Rs2.5bn. KCL's capex share would be Rs1.25bn (FY23F: Rs300m; FY24F: Rs950m). Nepal has domestic consumption of 25msm of tiles with nearly 100% being met through imports. Imports attract a duty of 40-50% in Nepal. KCL expects higher tile pricing and lower energy cost (will use coal for tile firing) as compared to India and sees a higher return on invested capital in the project compared to its Indian units. KCL plans to start production from Apr 2024F and achieve full capacity utilization in two years. The company currently exports Rs250m worth of tiles annually to Nepal.
- **Partial shutdown at Morbi unit:** KCL shut down and sold one unit having 3.1msm capacity based at Morbi in Gujarat, leading to a reduction in annual production capacity to 8.9msm at Kajaria Vitrified Pvt. Ltd. The company incurred a loss on sale of investment of Rs37m in 2QFY23, recognized as extra ordinary expense in the P&L statement.
- **Non-tile business update:** Bathware (sanitaryware and faucets), plywood and adhesives are three major revenue streams part of the 'Others' segment reported as segment financials. KCL plans to scale up its tile adhesive and grout business further as demand for the same has increased consistently, given the higher share of sales of large-sized tiles for KCL. The company plans to achieve adhesive revenue of nearly Rs500m in FY23F.
- **Capex:** KCL has approved expansion cum modernization plan for bigger size GVT capacity of 3msm with latest technologies at its Sikandrabad plant, which will increase the total capacity of the plant from 8.4 msm to 11.4 msm p.a at a capex of Rs800m (FY23F: Rs500m; FY24F: Rs300m). KCL incurred gross capex of Rs1bn in 1HFY23 and plans total capex of Rs4-5bn over the next 18 months.
- **Cash flow:** OCF and FCF stood at Rs513m and -Rs299m, respectively, in 1HFY23.
- **Net working capital and cash:** Net working capital stood at 58 days of TTM sales as at end-Sep 2022 (vs. 53 days as at end-Mar 2022). Net cash stood at Rs1.5bn as at end-Sep 2022 (vs. Rs3bn as at end-Mar 2022).

Figure 1: Tiles revenue and EBIT trend



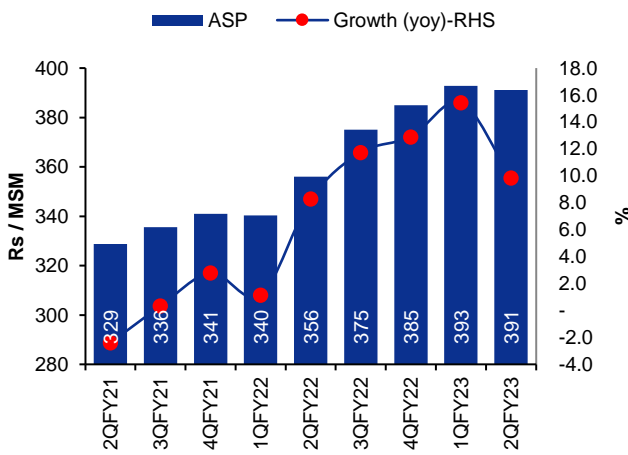
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Tiles volume trend



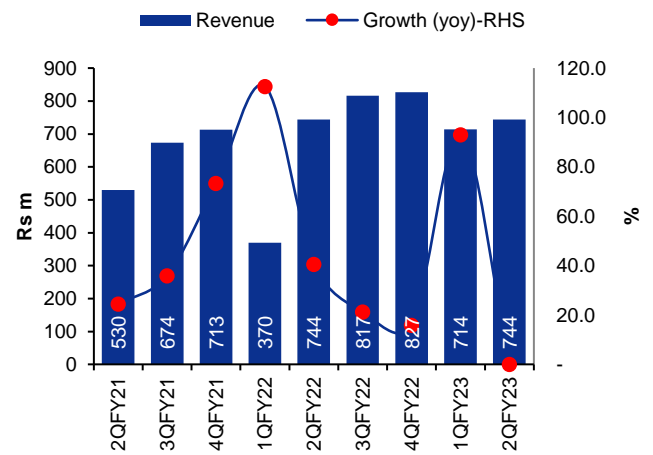
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 3: Tiles ASP trend



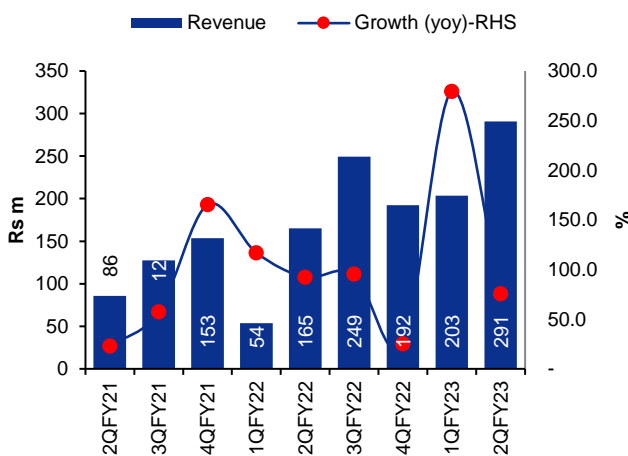
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 4: Sanitaryware revenue trend



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 5: Plywood revenue trend



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 6: 2QFY23 results snapshot

YE Mar (Rs m)	2QFY23	2QFY22	yoy (%)	1QFY23	qoq (%)	H1FY23	H1FY22	yoy (%)
Revenue	10,778	9,736	10.7	10,082	6.9	20,860	15,352	35.9
EBITDA	1,294	1,805	(28.3)	1,536	(15.7)	2,830	2,609	8.5
EBITDA margin (%)	12.0	18.5	-653 bp	15.2	-323 bp	13.6	17.0	-343 bp
Adj. PAT	735	1,161	(36.7)	923	(20.3)	1,658	1,592	4.2
Diluted EPS (Rs)	4.6	7.3		5.8		10.4	10.0	

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 7: 2QFY23 segment-wise results snapshot

YE Mar (Rs m)	2QFY23	2QFY22	yoy (%)	1QFY23	qoq (%)
<b>Revenue</b>					
Tiles	9,839	8,826	11.5	9,165	7.4
Others	938	910	3.2	917	2.3
<b>Total</b>	<b>10,778</b>	<b>9,736</b>		<b>10,082</b>	
<b>EBIT</b>					
Tiles	954	1,459	(34.7)	1,172	(18.7)
Others	4	64	(93.6)	40	(89.8)
<b>Total</b>	<b>958</b>	<b>1,523</b>		<b>1,212</b>	
<b>EBIT margin (%)</b>					
Tiles	9.7	16.5	-684 bp	12.8	-310 bp
Others	0.4	7.1	-663 bp	4.4	-394 bp

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 8: Actuals vs. our estimates

Rs m	2QFY23A	2QFY23F	Var (%)
Revenue	10,778	11,331	(4.9)
EBITDA	1,294	1,629	(20.5)
EBITDA margin (%)	12.0	14.4	-237 bp
Adj. PAT	735	976	(24.7)

SOURCE: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 9: Actuals vs. Bloomberg consensus estimates

Rs m	2QFY23A	2QFY23C	Var(%)
Revenue	10,778	10,949	(1.6)
EBITDA	1,294	1,553	(16.7)
EBITDA margin (%)	12.0	14.2	-218 bp
Adj. PAT	735	954	(23.0)

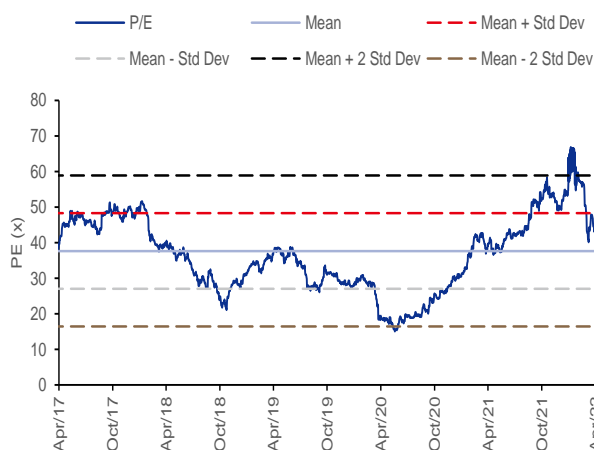
SOURCE: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 10: Revision in our earnings estimates

	New estimates			Old estimates			Change (%)		
	FY23F	FY24F	FY25F	FY23F	FY24F	FY25F	FY23F	FY24F	FY25F
Revenue	44,897	51,162	59,069	45,397	52,328	NA	-1.1	-2.2	NA
EBITDA	6,263	8,160	9,717	7,150	8,739	NA	-12.4	-6.6	NA
Adjusted consol. PAT	3,783	5,139	6,165	4,465	5,643	NA	-15.3	-8.9	NA
EPS	23.8	32.3	38.7	28.0	35.4	NA	-15.3	-8.9	NA
EBITDA margin (%)	14.0	16.0	16.5	15.8	16.7	NA	-180 bp	-75 bp	NA

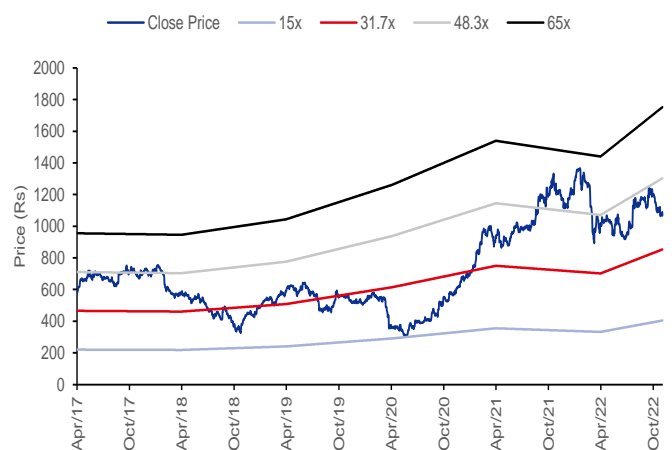
SOURCE: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 11: P/E SD (five-year mean P/E)



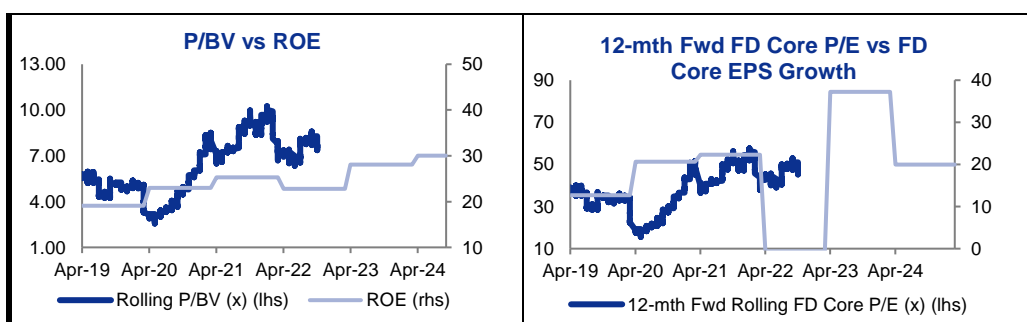
SOURCE: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 12: P/E band



SOURCE: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG

BY THE NUMBERS



Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
<b>Total Net Revenues</b>	<b>27,809</b>	<b>37,052</b>	<b>44,897</b>	<b>51,162</b>	<b>59,069</b>
<b>Gross Profit</b>	<b>15,340</b>	<b>21,501</b>	<b>26,153</b>	<b>30,441</b>	<b>35,589</b>
<b>Operating EBITDA</b>	<b>5,088</b>	<b>6,107</b>	<b>6,263</b>	<b>8,160</b>	<b>9,717</b>
Depreciation And Amortisation	(1,067)	(1,154)	(1,348)	(1,438)	(1,716)
<b>Operating EBIT</b>	<b>4,022</b>	<b>4,953</b>	<b>4,915</b>	<b>6,722</b>	<b>8,001</b>
Financial Income/(Expense)	73	125	93	110	201
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	33	23	50	53	55
<b>Profit Before Tax (pre-EI)</b>	<b>4,127</b>	<b>5,102</b>	<b>5,058</b>	<b>6,885</b>	<b>8,258</b>
Exceptional Items			(37)		
<b>Pre-tax Profit</b>	<b>4,127</b>	<b>5,102</b>	<b>5,021</b>	<b>6,885</b>	<b>8,258</b>
Taxation	(1,038)	(1,274)	(1,255)	(1,724)	(2,069)
Exceptional Income - post-tax					
<b>Profit After Tax</b>	<b>3,089</b>	<b>3,827</b>	<b>3,766</b>	<b>5,161</b>	<b>6,189</b>
Minority Interests	(9)	(58)	(20)	(22)	(24)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
<b>Net Profit</b>	<b>3,081</b>	<b>3,770</b>	<b>3,746</b>	<b>5,139</b>	<b>6,165</b>
Recurring Net Profit	3,081	3,770	3,774	5,139	6,165
<b>Fully Diluted Recurring Net Profit</b>	<b>3,081</b>	<b>3,770</b>	<b>3,774</b>	<b>5,139</b>	<b>6,165</b>

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
<b>EBITDA</b>	<b>5,088</b>	<b>6,107</b>	<b>6,263</b>	<b>8,160</b>	<b>9,717</b>
Cash Flow from Invt. & Assoc.					
Change In Working Capital	868	(621)	(1,128)	(413)	
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	179	165	107	163	
Net Interest (Paid)/Received	(67)	(111)	(93)	(110)	
Tax Paid	(980)	(1,285)	(1,255)	(1,724)	
<b>Cashflow From Operations</b>	<b>5,088</b>	<b>4,255</b>	<b>3,893</b>	<b>6,076</b>	<b>9,717</b>
Capex	(1,127)	(2,687)	(2,860)	(3,116)	(2,122)
Disposals Of FAs/subsidiaries	115	53			
Acq. Of Subsidiaries/investments	(2,119)	(491)	250		(500)
Other Investing Cashflow	176	215	246	263	329
<b>Cash Flow From Investing</b>	<b>(2,955)</b>	<b>(2,910)</b>	<b>(2,364)</b>	<b>(2,852)</b>	<b>(2,292)</b>
Debt Raised/(repaid)	(302)	(2,266)	500	(500)	
Proceeds From Issue Of Shares	53	52			
Shares Repurchased					
Dividends Paid	(1,591)	1,273	(1,910)	(2,388)	(2,945)
Preferred Dividends					
Other Financing Cashflow	(68)	(92)	(153)	(153)	(128)
<b>Cash Flow From Financing</b>	<b>(1,908)</b>	<b>(1,032)</b>	<b>(1,563)</b>	<b>(3,041)</b>	<b>(3,073)</b>
Total Cash Generated	224	313	(35)	182	4,351
<b>Free Cashflow To Equity</b>	<b>1,830</b>	<b>(921)</b>	<b>2,029</b>	<b>2,723</b>	<b>7,425</b>
<b>Free Cashflow To Firm</b>	<b>2,025</b>	<b>1,218</b>	<b>1,376</b>	<b>3,070</b>	<b>7,425</b>

SOURCE: INCRED RESEARCH, COMPANY REPORTS

**BY THE NUMBERS...cont'd**

<b>Balance Sheet</b>					
<b>(Rs mn)</b>	<b>Mar-21A</b>	<b>Mar-22A</b>	<b>Mar-23F</b>	<b>Mar-24F</b>	<b>Mar-25F</b>
Total Cash And Equivalents	4,477	4,244	3,959	4,141	5,992
Total Debtors	4,317	5,133	6,150	7,008	8,092
Inventories	3,731	4,659	6,150	7,008	8,092
Total Other Current Assets	402	478	686	782	903
<b>Total Current Assets</b>	<b>12,927</b>	<b>14,513</b>	<b>16,946</b>	<b>18,940</b>	<b>23,078</b>
Fixed Assets	11,552	11,022	13,918	15,596	17,152
Total Investments					
Intangible Assets	85	85	85	85	85
Total Other Non-Current Assets	703	4,245	2,862	2,862	1,712
<b>Total Non-current Assets</b>	<b>12,339</b>	<b>15,352</b>	<b>16,864</b>	<b>18,542</b>	<b>18,948</b>
Short-term Debt	658	1,041	1,190	855	855
Current Portion of Long-Term Debt					
Total Creditors	2,072	2,981	3,936	4,906	5,664
Other Current Liabilities	1,748	2,441	3,075	3,504	4,046
<b>Total Current Liabilities</b>	<b>4,478</b>	<b>6,464</b>	<b>8,201</b>	<b>9,266</b>	<b>10,565</b>
Total Long-term Debt	313	238	589	424	424
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	454	559	559	559	559
<b>Total Non-current Liabilities</b>	<b>767</b>	<b>797</b>	<b>1,148</b>	<b>983</b>	<b>983</b>
Total Provisions	687	733	733	733	733
<b>Total Liabilities</b>	<b>5,931</b>	<b>7,994</b>	<b>10,083</b>	<b>10,982</b>	<b>12,281</b>
Shareholders Equity	18,689	21,224	23,060	25,811	29,030
Minority Interests	646	648	668	690	714
<b>Total Equity</b>	<b>19,335</b>	<b>21,872</b>	<b>23,727</b>	<b>26,501</b>	<b>29,744</b>

<b>Key Ratios</b>					
	<b>Mar-21A</b>	<b>Mar-22A</b>	<b>Mar-23F</b>	<b>Mar-24F</b>	<b>Mar-25F</b>
Revenue Growth	(1.0%)	33.2%	21.2%	14.0%	15.5%
Operating EBITDA Growth	22.3%	20.0%	2.6%	30.3%	19.1%
Operating EBITDA Margin	18.3%	16.5%	14.0%	16.0%	16.4%
Net Cash Per Share (Rs)	22.05	18.63	13.69	17.98	29.60
BVPS (Rs)	117.50	133.36	144.85	162.13	182.35
Gross Interest Cover	37.55	38.91	32.14	43.96	62.55
Effective Tax Rate	25.2%	25.0%	25.0%	25.0%	25.1%
Net Dividend Payout Ratio	38.6%	34.7%	37.9%	34.8%	35.8%
Accounts Receivables Days	54.36	46.54	45.86	46.94	46.65
Inventory Days	129.64	98.45	105.24	115.90	117.37
Accounts Payables Days	65.36	59.31	67.35	77.88	82.16
ROIC (%)	22.4%	29.2%	24.3%	29.4%	32.1%
ROCE (%)	20.7%	23.2%	20.6%	25.5%	27.6%
Return On Average Assets	16.3%	18.1%	15.6%	19.0%	20.3%

SOURCE: INCRED RESEARCH, COMPANY REPORTS



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