

Kajaria Ceramics

15 January 2015

Reuters: KAJR.BO; Bloomberg: KJC IN

Healthy Margins; Retain Buy

Kajaria Ceramics' (KCL) 3QFY15 revenue increased 30.5% to Rs5,562mn, in line with expectations, because of 39.1%/23.7% rise in production/sales volume, respectively, on a lower base and a 24.1% increase in capacity despite weak demand. With a better product mix and earlier price hikes, operating margin remained firm at 15.7%. Healthy operating profit growth and lower interest costs/tax rate led to a 55.2% rise in net profit to Rs456mn, 15.6%/12.7% above our/Bloomberg consensus estimates, respectively. With a fall in crude oil prices, spot prices of gas have started declining. As KCL's power and fuel costs increased 415bps over FY12-FY14, it will benefit the most going forward from lower gas prices, which we/street haven't factored in yet. The 55% increase in capacity, better product mix and lean working capital needs are likely to result in revenue/net profit CAGR of 20.7%/30.6%, respectively, leading to strong operating cash flow of Rs8bn and a decline in the D/E ratio from 0.4x to 0.1x, and a 385bps improvement in RoCE to 24.7% over FY14-FY17E. Based on 13.5x FY17E EV/EBITDA (from 14.5x average over FY16E-FY17E) and 24.9x P/E, we have retained Buy rating on KCL with a revised target price of Rs868 (Rs848 earlier).

Healthy revenue growth with better margins: With capacity expansion at Jaxx and Cosa in September 2014, KCL's capacity increased 24.1% in 3QFY15 from 6.9% in 1HFY15. New capacity at Jaxx/Cosa operated at 60%/~100%, respectively, in 3QFY15. Because of a low base (a mere 2.4% revenue growth) in 3QFY14, and higher capacity, production grew 39.1%/15.4% YoY/QoQ and sales volume rose 23.7%/2.4% YoY/QoQ, respectively, to 14.7msqm in 3QFY15 despite weak demand. Following a better product mix, and earlier price hikes, blended realisation rose 5.2% and, therefore, operating margin remained firm at 15.7%, 72bps above Bloomberg consensus estimate. With lower interest costs because of a reduction in debt from Rs2.23bn/Rs2.07bn YoY/QoQ, respectively, to Rs1.52bn and a lower tax rate, net profit grew 55.2% to Rs456mn, 14.7% above our estimate.

Key things to monitor: Earlier, KCL was booking freight costs in traded goods only. Following reclassification of accounting heads, consolidated gross sales, goods purchased for trading and other expenses were reclassified in 3QFY14. This reduced gross sales/traded goods by Rs18mn/Rs106mn, respectively, and increased other expenses by Rs88mn in 3QFY14. Post reclassification, gross margin improved 501bps versus a 271bps improvement earlier, although EBITDA stayed unchanged at Rs665mn. Following reclassification, gross margin is not comparable for the quarter. Despite better performance of joint ventures, whose combined EBITDA increased to Rs162mn from Rs142mn QoQ, minority interest fell to Rs15mn from Rs18mn because of other income loss of Rs25mn.

Lower power and fuel costs to drive margins: With rising cost of gas, power and fuel costs posted a 32.8% CAGR against a 18.4% revenue CAGR, up 415bps over FY12-FY14. With a fall in crude oil prices, spot prices of gas have started declining. If spot prices of gas remain low, KCL is expected to witness a strong improvement in its operating margin.

Y/E March (Rsmn) consolidated	3QFY14	2QFY15	3QFY15	Chg. (YoY)%	Chg. (QoQ)%	9MFY14	9MFY15	Chg. (%)
Net sales	4,261	5,394	5,562	30.5	3.1	13,288	15,989	20.3
Net RM costs and finished goods purchases	1,768	2,181	1,955	10.6	(10.4)	5,879	6,247	6.3
% of sales	41.5	40.4	35.1	-	-	44.2	39.1	-
Power, oil & fuel costs	846	1,159	1,310	54.8	13.0	2,695	3,583	33.0
% of sales	19.9	21.5	23.6	-	-	20.3	22.4	-
Other expenses	982	1,241	1,422	44.8	14.6	2,747	3,670	33.6
% of sales	23.1	23.0	25.6	-	-	20.7	23.0	-
Operating profit	665	813	875	31.5	7.5	1,967	2,489	26.5
OPM (%)	15.6	15.1	15.7	-	-	14.8	15.6	-
Interest costs	110	84	56	(49.3)	(33.8)	341	215	(36.9)
Depreciation	119	135	144	21.4	6.2	351	406	15.7
Other income	16	14	3	(82.9)	(81.0)	38	30	(21.2)
PBT	452	608	678	49.8	11.5	1,313	1,898	44.5
Provision for tax	152	193	207	35.9	7.3	446	605	35.5
Effective tax rate (%)	33.6	31.7	30.5	-	-	34.0	31.9	-
Minority interest	6	18	15	129.7	(16.0)	46	53	16.6
Adjusted PAT	294	398	456	55.2	14.7	821	1,239	51.0
NPM (%)	6.9	7.4	8.2	-	-	6.2	7.8	-
EPS (Rs)	3.9	5.3	6.0	55.2	14.7	11.0	16.4	48.4

Source: Company, Nirmal Bang Institutional Equities Research

BUY

Sector: Building Products

CMP: Rs636

Target Price: Rs868

Upside: 37%

Jignesh Kamani, CFA

jignesh.kamani@nirmalbang.com

+91-22-3926 8239

Ruchita Maheshwari

ruchita.maheshwari@nirmalbang.com

+91-22-3926 8023

Key Data

Current Shares O/S (mn)	79.5
Mkt Cap (Rsbn/US\$mn)	50.6/813.7
52 Wk H / L (Rs)	690/290
Daily Vol. (3M NSE Avg.)	187,866

Price Performance (%)

	1 M	6 M	1 Yr
Kajaria Ceramics	11.0	20.9	111.2
Nifty Index	0.6	11.0	32.6

Source: Bloomberg

Exhibit 1: Financial summary

Y/E March (Rsmn) consolidated	FY12	FY13	FY14	FY15E	FY16E	FY17E
Revenue	13,130	16,120	18,400	22,088	27,099	32,352
YoY (%)	37.7	22.8	14.1	20.0	22.7	19.4
EBITDA	2,062	2,446	2,808	3,511	4,307	5,177
EBITDA margin (%)	15.7	15.2	15.3	15.9	15.9	16.0
Adj. PAT	809	1,045	1,242	1,724	2,212	2,769
EPS (Rs)	11.0	14.2	16.4	21.7	27.8	34.8
YoY (%)	31.0	29.2	15.6	32.1	28.3	25.2
RoE (%)	32.1	32.5	27.9	27.7	27.6	27.7
RoCE (%)	21.3	21.8	20.9	22.4	23.4	24.7
RoIC (%)	19.2	19.6	18.8	20.5	21.5	22.8
P/E (x)	57.9	44.8	38.7	29.3	22.9	18.3
EV/ EBITDA (x)	24.0	20.4	18.0	15.0	12.1	9.9

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Production/sales/revenue details

Y/E March (Rsmn)	3QFY14	2QFY15	3QFY15	YoY (%)	QoQ (%)	9MFY14	9MFY15	YoY (%)
Production details (msqm)								
Own manufacturing units	6.95	7.58	8.03	15.5	5.9	20.19	23.09	14.4
JVs	2.77	4.14	5.49	98.2	32.6	9.90	13.53	36.7
Total	9.72	11.72	13.52	39.1	15.4	30.09	36.62	21.7
Sales volume (msqm)								
Own manufacturing units	6.57	7.51	7.17	9.1	(4.5)	19.80	21.90	10.6
JVs	3.09	3.77	4.85	57.0	28.6	10.11	12.47	23.3
Outsourced/imports	2.18	3.02	2.63	20.6	(12.9)	7.45	8.66	16.2
Total	11.84	14.30	14.65	23.7	2.4	37.36	43.03	15.2
Revenue								
Own manufacturing units	2,338	2,833	2,743	17.3	(3.2)	6,788	8,130	19.8
JVs	1,075	1,505	1,752	63.0	16.4	3,593	4,700	30.8
Outsourced/imports	844	1,039	1,043	23.6	0.4	2,898	3,114	7.4
Others	448	520	590	31.6	13.5	1,172	1,620	38.2
Total gross revenue	4,705	5,897	6,128	30.3	3.9	14,451	17,565	21.5
Blended realisation (Rs/sqm)	360	376	378	5.2	0.5	355	371	4.3

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Our estimates versus actual performance

(Rsmn)	3QFY14	2QFY15	3QFY15	YoY (%)	QoQ (%)	3QFY15E	Devi. (%)	3QFY15 BBE	Devi.(%)
Revenue	4,261	5,394	5,562	30.5	3.1	5,524	0.7	5,584	(0.4)
EBITDA	665	813	875	31.5	7.5	862	1.5	838	4.4
EBITDA (%)	15.6	15.1	15.7	12bps	65bps	15.6	12bps	15.0	72bps
Adjusted PAT	294	398	456	55.2	14.7	395	15.6	405	12.7

Source: Company, Nirmal Bang Institutional Equities Research

Key updates

- KCL has decided to set up 5msqm annual capacity for making polished vitrified tiles at a new location in Rajasthan. The project is likely to be completed by August 2015.
- KCL is setting up a 3msqm ceramic wall tile capacity at its existing unit in Bhiwadi, Rajasthan. Production is expected to commence by March 2015.
- Production at brownfield expansion facility for high-end polished vitrified tiles (PVT) at Jaxx Vitrified (4.5 msqm capacity) commenced on 6 September 2014. The company operated at full capacity in 3QFY15. KCL increased its stake in Jaxx Vitrified to 61% from 51% in June 2014 at a cost of Rs35mn.
- Cosa Ceramics commenced the process of setting up a 3msqm PVT capacity on 29 September 2014. It operated at full capacity in 3QFY15.

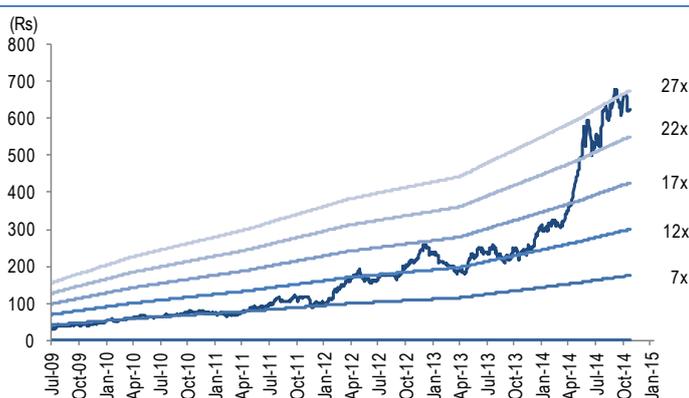
- Kajaria Sanitaryware, in which KCL holds a majority stake (64%), started the production of sanitaryware on 6 April 2014. Full utilisation of production capacity is expected to begin in FY16.
- KCL has initiated the process of setting up a faucet plant having a capacity of 1.5mn pieces in Gailpur, Rajasthan, at a cost of Rs500mn. The company has scaled down the project to 1.0mn pieces at a cost of Rs400mn. The project is likely to commence operations in March/April 2015.

Exhibit 4: Capacity addition of 23.9msqm over FY14-FY16E, up 55% from 43.6msqm in FY14

Company	Location	Tile types	Capacity addition (msqm)	Expected time of completion
Kajaria Ceramics	Sikandrabad, Uttar Pradesh	Glazed vitrified	3.4	Completed on 28 March 2014
Jaxx Vitrified	Morbi, Gujarat	Polished vitrified	4.5	Completed on 6 September 2014
Cosa Ceramics	Morbi, Gujarat	Polished vitrified	3.0	Completed on 29 September 2014
Greenfield unit of KCL	Rajasthan	Polished vitrified	5.0	August 2015
KCL	Rajasthan	Wall tiles	3.0	March 2015
Taurus Tiles	Morbi, Gujarat	Polished vitrified	5.0	March 2015
Total			23.9	

Source: Nirmal Bang Institutional Equities Research

Exhibit 5: One-year forward P/E band



Source: Nirmal Bang Institutional Equities Research

Exhibit 6: One-year forward median band

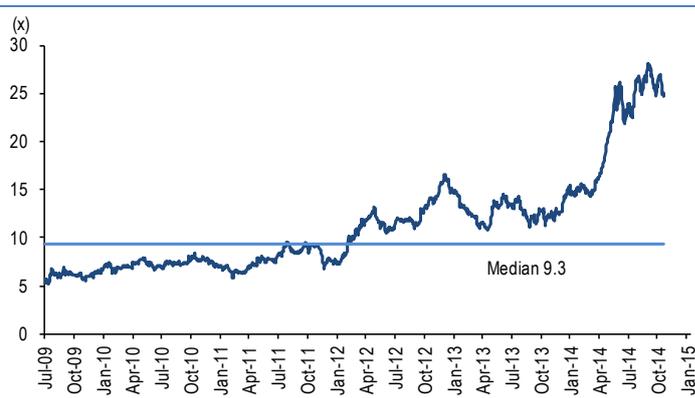
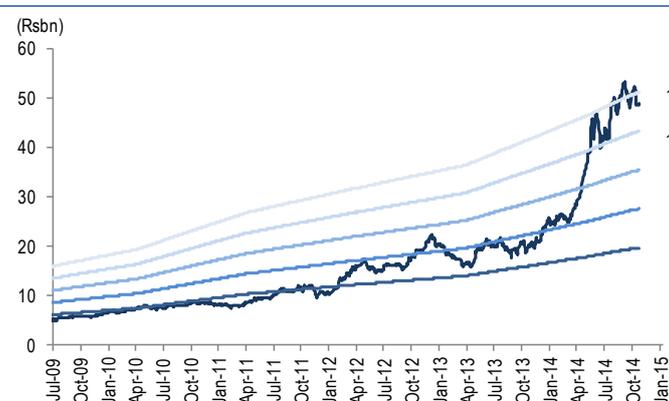
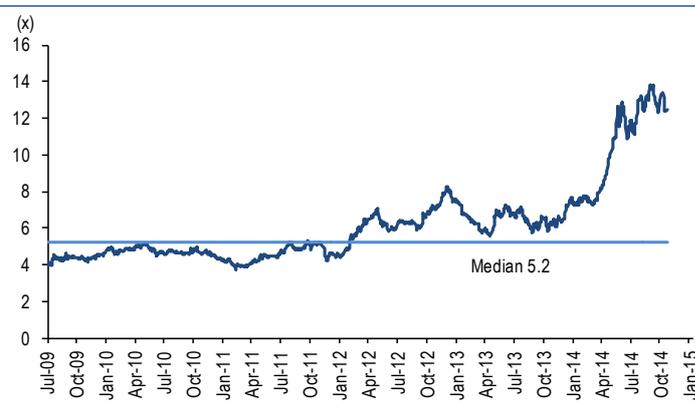


Exhibit 7: One-year forward EV/EBITDA band



Source: Nirmal Bang Institutional Equities Research

Exhibit 8: One-year forward median band



Financials (consolidated)

Exhibit 9: Income statement

Y/E March (Rsmn)	FY12	FY13	FY14	FY15E	FY16E	FY17E
Net sales	13,130	16,120	18,400	22,088	27,099	32,352
Growth (%)	37.7	22.8	14.1	20.0	22.7	19.4
Raw material costs	6,508	7,485	8,252	10,029	12,305	14,655
Staff costs	1,072	1,364	1,726	2,054	2,520	3,009
Power & fuel costs	2,107	3,066	3,717	4,241	5,149	6,147
Other costs	1,381	1,759	1,898	2,253	2,818	3,365
Total expenditure	11,068	13,673	15,593	18,577	22,792	27,175
EBITDA	2,062	2,446	2,808	3,511	4,307	5,177
Growth (%)	38.7	18.6	14.8	25.0	22.7	20.2
EBITDA margin (%)	15.7	15.2	15.3	15.9	15.9	16.0
Other income	15	30	63	53	81	109
Interest costs	485	454	408	294	249	189
Gross profit	1,592	2,023	2,462	3,270	4,139	5,096
Growth (%)	33.9	27.1	21.7	32.8	26.6	23.1
Depreciation	393	446	470	571	684	779
Profit before tax	1,199	1,577	1,992	2,698	3,455	4,317
Growth (%)	34.4	31.5	26.3	35.5	28.1	24.9
Tax	381	499	678	899	1,151	1,438
Effective tax rate (%)	31.7	31.6	34.0	33.3	33.3	33.3
Net profit	818	1,078	1,314	1,800	2,305	2,880
Growth (%)	34.9	31.8	21.9	37.0	28.1	24.9
Minority interest	10	33	72	76	93	111
Extraordinary items	-	-	-	-	-	-
Adjusted PAT	809	1,045	1,242	1,724	2,212	2,769
Growth (%)	31.0	29.2	18.8	38.9	28.3	25.2

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: Balance sheet

Y/E March (Rsmn)	FY12	FY13	FY14	FY15E	FY16E	FY17E
Equity	147	147	151	159	159	159
Reserves	2,674	3,462	4,890	6,986	8,734	10,946
Net worth	2,821	3,609	5,295	7,145	8,893	11,105
Minority interest	72	275	409	484	577	688
Short-term loans	1,865	2,309	1,513	1,413	1,263	763
Long-term loans	917	893	851	751	551	451
Total loans	2,782	3,202	2,364	2,164	1,814	1,214
Deferred tax liability	644	656	713	802	916	1,059
Liabilities	6,319	7,742	8,781	10,595	12,200	14,066
Gross block	7,752	9,113	10,180	12,086	14,498	16,512
Depreciation	2,605	2,988	3,319	3,890	4,574	5,353
Net block	5,148	6,126	6,861	8,196	9,924	11,159
Capital work-in-progress	24	78	405	512	14	17
Long-term Investments	1	1	1	1	1	1
Goodwill and other intangibles	62	74	55	55	55	55
Inventories	1,865	2,197	1,931	2,890	3,545	4,227
Debtors	1,189	1,436	1,649	1,963	2,409	2,876
Cash	72	55	61	142	133	360
Other current assets	550	508	794	691	848	1,012
Total current assets	3,676	4,197	4,434	5,686	6,935	8,475
Creditors	1,776	1,658	1,520	2,374	2,912	3,472
Other current liabilities	815	1,075	1,455	1,480	1,816	2,168
Total current liabilities	2,591	2,734	2,975	3,854	4,728	5,640
Net current assets	1,085	1,463	1,459	1,832	2,207	2,835
Total assets	6,319	7,742	8,781	10,595	12,200	14,066

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 10: Cash flow

Y/E March (Rsmn)	FY12	FY13	FY14	FY15E	FY16E	FY17E
EBIT	1,669	2,000	2,338	2,940	3,623	4,397
Inc./(dec.) in working capital	(274)	(395)	10	(292)	(384)	(401)
Cash flow from operations	1,395	1,605	2,348	2,647	3,240	3,996
Other income	15	30	63	53	81	109
Depreciation	393	446	470	571	684	779
Deferred liabilities	40	13	57	89	114	142
Interest paid (-)	(485)	(454)	(408)	(294)	(249)	(189)
Tax paid (-)	(381)	(499)	(678)	(899)	(1,151)	(1,438)
Dividend paid (-)	(214)	(257)	(309)	(371)	(464)	(556)
Minority interest (P&L)	(10)	(33)	(72)	(76)	(93)	(111)
Extraordinary items	-	-	-	-	-	-
Net cash from operations	754	852	1,470	1,721	2,163	2,733
Capital expenditure (-)	(693)	(1,479)	(1,533)	(2,012)	(1,914)	(2,017)
Net cash after capex	61	(626)	(63)	(291)	248	716
Inc./(dec.) in short-term borrowing	2	444	(796)	(100)	(150)	(500)
Inc./(dec.) in long-term borrowing	(100)	(24)	(41)	(100)	(200)	(100)
Inc./(dec.) in preference capital	-	-	-	-	-	-
Inc./(dec.) in borrowings	(98)	420	(838)	(200)	(350)	(600)
(Inc.)/dec. in investments	16	(12)	19	-	-	-
Minority interest	54	203	133	76	93	111
Equity issue/(buyback)	-	-	754	496	-	-
Cash from financial activities	(28)	610	69	372	(257)	(489)
Others	-	(1)	-	-	-	-
Opening cash	38	72	55	61	142	133
Closing cash	72	55	61	142	133	360
Change in cash	34	(17)	6	81	(9)	227

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: Key ratios

Y/E March	FY12	FY13	FY14	FY15E	FY16E	FY17E
Per share (Rs)						
EPS	11.0	14.2	16.4	21.7	27.8	34.8
Book value	38	49	70	90	112	140
Valuation (x)						
P/E	57.9	44.8	38.7	29.3	22.9	18.3
P/sales	3.6	2.9	2.6	2.3	1.9	1.6
P/BV	16.6	13.0	9.1	7.1	5.7	4.6
EV/EBITDA	24.0	20.4	18.0	15.0	12.1	9.9
EV/sales	3.8	3.1	2.7	2.4	1.9	1.6
Return ratios (%)						
RoIC	19.2	19.6	18.8	20.5	21.5	22.8
RoCE	21.3	21.8	20.9	22.4	23.4	24.7
RoE	32.1	32.5	27.9	27.7	27.6	27.7
Margins (%)						
EBITDA margin	15.7	15.2	15.3	15.9	15.9	16.0
PBIT margin	12.7	12.4	12.7	13.3	13.4	13.6
PBT margin	9.1	9.8	10.8	12.2	12.8	13.3
PAT margin	6.2	6.5	6.7	7.8	8.2	8.6
Turnover ratio						
Asset turnover ratio (x)	2.1	2.1	2.1	2.1	2.2	2.3
Avg. inventory period (days)	61	58	45	56	56	56
Avg. collection period (days)	33	32	32	32	32	32
Avg. payment period (days)	58	44	35	46	46	46
Solvency ratios (x)						
Debt-equity	1.0	0.8	0.4	0.3	0.2	0.1
Interest coverage	3.4	4.4	5.7	10.0	14.6	23.2
Growth (%)						
Sales	37.7	22.8	14.1	20.0	22.7	19.4
EBITDA	38.7	18.6	14.8	25.0	22.7	20.2
PAT	31.0	29.2	18.8	38.9	28.3	25.2

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
24 July 2012	Buy	177	227
4 October 2012	Hold	202	227
17 October 2011	Buy	210	252
5 December 2012	Buy	258	326
7 January 2013	Buy	235	326
22 January 2013	Buy	210	326
30 January 2013	Buy	211	284
9 April 2013	Buy	191	284
2 May 2013	Buy	207	284
7 May 2013	Buy	230	284
9 July 2013	Buy	234	284
31 July 2013	Buy	237	284
7 October 2013	Buy	244	284
11 October 2013	Buy	243	284
7 November 2013	Hold	242	266
7 January 2014	UR	294	UR
21 January 2014	Buy	307	385
11 April 2014	UR	376	UR
8 May 2014	Hold	483	522
4 July 2014	Hold	483	575
4 August 2014	Buy	625	767
10 October 2014	Buy	667	767
28 October 2014	Buy	610	848
15 January 2015	Buy	636	868

Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

This report is published by Nirmal Bang's Institutional Equities Research desk. Nirmal Bang has other business units with independent research teams separated by Chinese walls, and therefore may, at times, have different or contrary views on stocks and markets. This report is for the personal information of the authorised recipient and is not for public distribution. This should not be reproduced or redistributed to any other person or in any form. This report is for the general information for the clients of Nirmal Bang Equities Pvt. Ltd., a division of Nirmal Bang, and should not be construed as an offer or solicitation of an offer to buy/sell any securities.

We have exercised due diligence in checking the correctness and authenticity of the information contained herein, so far as it relates to current and historical information, but do not guarantee its accuracy or completeness. The opinions expressed are our current opinions as of the date appearing in the material and may be subject to change from time to time without notice.

Nirmal Bang or any persons connected with it do not accept any liability arising from the use of this document or the information contained therein. The recipients of this material should rely on their own judgment and take their own professional advice before acting on this information. Nirmal Bang or any of its connected persons including its directors or subsidiaries or associates or employees or agents shall not be in any way responsible for any loss or damage that may arise to any person/s from any inadvertent error in the information contained, views and opinions expressed in this publication.

Nirmal Bang Equities Private Limited (hereinafter referred to as "NBEPL") is a registered Member of National Stock Exchange of India Limited, Bombay Stock Exchange Limited. NBEPL is in the process of making an application with SEBI for registering as a Research Entity in terms of SEBI (Research Analyst) Regulations, 2014.

NBEPL or its associates including its relatives/analyst do not hold any financial interest/beneficial ownership of more than 1% in the company covered by Analyst.

NBEPL or its associates/analyst has not received any compensation from the company covered by Analyst during the past twelve months. NBEPL /analyst has not served as an officer, director or employee of company covered by Analyst and has not been engaged in market-making activity of the company covered by Analyst.

The views expressed are based solely on information available publicly and believed to be true. Investors are advised to independently evaluate the market conditions/risks involved before making any investment decision.

'Access our reports on Bloomberg Type NBIE <GO>'

Team Details:			
Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	-
Girish Pai	Head of Research	girish.pai@nirmalbang.com	+91 22 3926 8017 / 18
Dealing			
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 3926 8230, +91 22 6636 8833
Pradeep Kasat	Dealing Desk	pradeep.kasat@nirmalbang.com	+91 22 3926 8100/8101, +91 22 6636 8831
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 3926 8102/8103, +91 22 6636 8830
Umesh Bharadia	Dealing Desk	umesh.bharadia@nirmalbang.com	+91-22-39268226

Nirmal Bang Equities Pvt. Ltd.

Correspondence Address

B-2, 301/302, Marathon Innova,
 Nr. Peninsula Corporate Park,
 Lower Parel (W), Mumbai-400013.

Board No. : 91 22 3926 8000/1; Fax. : 022 3926 8010