

Somany Ceramics Ltd.

 BSE SENSEX
 27746

 S&P CNX
 8509

CMP: INR568 TP: INR700 (+23%) Buy

(INR CRORES)

Y/E MARCH	FY16	FY17E	FY18E
Revenue	1718	1976	2246
EBITDA	143	193	231
EBITDA Margin	8.3%	9.8%	10.3%
NP (Adj.)	68	98	123
EPS (Adj.)	16.0	23.1	29.0
EPS Growth	46%	45%	25%
BV/share	101	122	148
ROE (%)	16	19	20
ROCE (%)	18	23	25
P/E (x)	35.6	24.5	19.6
P/BV (x)	5.6	4.7	3.8

KEY FINANCIALS

Diluted Shares (cr)	4.2
Market Cap. (INR cr)	2408
Market Cap. (USD m)	354
Past 3 yrs Sales Growth (%)	28%

STOCK DATA

52-W High/Low Range (INR)	604/308
Shareholding (as of Mar 2016)	
Promoter	51.5
Non Promoter Corp Holding	16.4
Public & Others	32.1
Average Daily Turnover(6 months)	
Volume	17803
Value (Rs cr)	0.78
1/6/12 Month Rel. Performance (%)	1/54/39
1/6/12 Month Abs. Performance (%)	11/68/38

Maximum Buy Price :INR 590

Multiple triggers to drive 12% CAGR in organized tile industry:

(i) Government policy reforms like Swachh Bharat Abhiyaan, 100 smart cities, Housing for all by 2022, real estate bill, implementation of GST, (ii) Tile penetration is at just 11% in India with bulk of the houses having mud and cement flooring, (iii) shift towards value added vitrified tiles, (iv) Anti-dumping duty of USD 1.37/sq.m on imports from China, imposed in March 2016 is likely to get extended which shall translate to higher growth for domestic manufacturers. The growth of the tiles industry (size currently pegged at INR255bn) has decelerated from 20% CAGR in FY10-FY14 to 9% over FY14-16 largely due to the sustained slowdown in real estate, particularly in metros and tier-1 cities. However with structural drivers discussed above, we expect the organised tiles industry growth to accelerate to a CAGR of 12% over the next two years.

Increasing brand spends and improving product mix to aid 14%

revenue CAGR: Somany's brand equity has been on the surge led by increasing brand spend, which has expanded to INR 37cr (2.2% of revenues) in FY16 from INR 11cr (1.3%) in FY12, a CAGR of 35%. The management expects the same to further increase to 2.5-3% of revenues going forward. Revenue contribution from the vitrified tiles segment has substantially increased over the past five years to 55% of total revenues in FY16 from 30% in FY12. We expect the contribution to increase further to 63% by FY18E with the company aggressively adding capacities in this segment. With the recently commissioned 4mn-sq m GVT line at Kassar, Haryana, the recently acquired 4.3mn-sq m Somany Fine Vitrified in Morbi and the company's increasing focus on allied products (faucets and sanitaryware), we expect Somany to register 14% revenue CAGR over FY16-18E.

Levers in place for strong margin expansion: We expect Somany's EBITDA margins to improve by 200bps over FY16-18E to 10.3%, led by: i) higher focus on retail sales (currently 65%), ii) rising share of manufactured and subsidiary sales v/s outsourcing, iii) increasing mix of PVT & GVT from 55% in FY16 to 63% in FY18E, and iv) steep decline in LNG prices.

Valuations & View: Revenue CAGR of 14% over FY16-18E combined with strong expansion in margins and lower interest costs are expected to give a strong boost to profitability, leading to PAT CAGR of 35% over FY16-FY18E. We expect ROCE to improve by 730bp to 25% by FY18E. At CMP, the stock is trading at 19.6x its FY18E EPS. We value Somany at 24.2x FY18E earnings (a 15% discount to Kajaria) and arrive at a target price of INR 700.

Jehan Bhadha (jehan.bhadha@MotilalOswal.com); Tel: +91 22 33124915

Investors are advised to refer through important disclosures made at the last page of the Research Report.

Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

JV model leading to industry consolidation: The JV model is beneficial for both, the organized players as well as the unorganized players. The organized players benefit with - increased focus on branding & distribution, minimal gestation period, lower investment and higher ROI. The unorganized players benefit by way of assured optimum capacity utilization and assured receivables as the JV's organised counterpart is committed to buy the entire capacity without having to put in any efforts towards selling and marketing. The JV model gained momentum especially after the Gujarat Pollution Control Board banned the use of coal in tile manufacturing in October 2013 which eroded the cost advantage enjoyed by the unorganized players who avoided paying indirect taxes by under-reporting production. Further, switching to LNG increased their costs by 30%. Given the higher cost of operation and inability of unorganised players to push their products amid growing preference for branded products, they have been moving towards either forming JVs or being taken over by organised players.

Anti-dumping duty to lead to higher growth in FY17E: Anti-dumping duty of USD 1.37 per sq m was imposed on all vitrified tiles in March 2016 for a period of six months which will likely get extended post expiry of six months. Chinese imports stood at 55 mn sq m in FY16 and is likely to fall to 15 mn sq m in the current year, thereby adding about 5% of incremental growth for domestic players in FY17E. Thus we expect the industry to grow at 13% in FY17E as against 8% in FY16.

Allied products to complement growth: To complement its existing tiles portfolio and leverage its strong brand and distribution network, Somany has been intensifying its focus on allied products, viz. sanitaryware and faucets. These are typically procured from third-party suppliers and are also manufactured by one of Somany's 51% JV SSWPL, based out of Morbi. SSWPL currently has a capacity to manufacture 0.3mn sanitaryware pieces and is expanding its capacity to 0.9mn pieces at a capex of INR 35cr. The incremental capacity is expected to come onstream by April 2017 with a potential to generate INR 65cr revenues. Bath fittings are entirely sold on a trading model and the company is currently exploring opportunities in identifying a JV partner or putting up a greenfield project. This segment reported revenue of INR 112cr in FY16 and is expected to post revenue CAGR of 34% over FY16-18E.

Building scale to sustain growth momentum: Somany's capacity increased only marginally to 19msm in FY11 from 14msm in FY05. However, from FY12 the company started inking JVs with unorganised players to tap the growing opportunities in domestic tile market. As a result, by FY16 its overall capacity, including JVs, increased to 47 mn sq m. The company owns majority-26?51%-stakes in its JVs. Apart from this, Somany also has access to outsourced capacity of 9 mn sq m. Plans are afoot to further enhance capacity by 8mn sq m by FY18E, primarily in GVT/PVT (4 mn sq m each in own and JV plants).

CONCERNS:

Slowdown in real estate in tier2/3 towns: If the slowdown in real estate percolates down to tier2/3 towns (75% of revenue), offtake of incremental tile sales would be impacted thereby affecting the company's prospects.

Rise in fuel prices: Natural gas forms one of the key inputs for the company. Availability and pricing of natural gas remains a concern as increase in gas cost could increase operating costs and impact margins.

BACKGROUND:

Somany, established in 1971, is currently the third-largest player in the Indian tiles industry. It has an organised market share of 13% and overall market share of 7% as at FY16. It is present across the entire price and size range (value chain) ranging from affordable ceramic tiles, to mid-range polished vitrified tiles (PVT), to the upper-end glaze vitrified tiles (GVT). These are either manufactured in-house, in joint ventures, third-party outsourced or imported from overseas. The company operates through its own plants in Kadi (Gujarat) and Kassar (Haryana) and through the joint-venture model under which it has acquired stake in five companies in Morbi, Gujarat. Apart from this, the company also outsources commodity-based ceramic and vitrified tiles from various vendors in Morbi. The company is also present in the sanitaryware and faucet segment through the JV/outsourcing models and markets the same through brand Aquaware. As per the management, its current client mix comprises of 65% retail with the balance being shared equally by corporates, government and the builder category.

Somany Ceramics Ltd. Financials & Valuation

INCOME STATEMENT (INRCR)						RATIOS					
Y/E MARCH	FY14	FY15	FY16	FY17E	FY18E	Y/E MARCH	FY14	FY15	FY16	FY17E	FY18E
Revenues	1265	1543	1718	1976	2246	Adjusted EPS (INR)	6.8	10.9	16.0	23.1	29.0
Growth	20%	22%	11%	15%	14%	Book Value	58	66	101	122	148
COGS	780	939	1015	1157	1304	Div Per Share	1.5	2.0	2.3	2.6	3.0
Gross Profit	485	605	703	818	941	Dividend Payout	26%	20%	18%	13%	12%
GP Margin	38.4%	39.2%	40.9%	41.4%	41.9%	Net Debt / Equity	0.4	0.6	0.3	0.3	0.2
Employee Cost	83	101	123	148	174	P/E			35.6	24.5	19.6
Other Expenses	321	396	437	478	536	P/BV			5.6	4.7	3.8
EBITDA	81	108	143	193	231	EV/EBITDA			18.7	13.8	11.6
EBITDA Margin	6.4%	7.0%	8.3%	9.8%	10.3%	EV/Sales			1.6	1.4	1.2
Depreciation	22	27	28	30	33	Dividend Yield			0.4%	0.5%	0.5%
Other Income	3	8	9	7	7	ROCE	16%	19%	18%	23%	25%
PBIT	62	89	124	169	204	ROE	13%	18%	16%	19%	20%
E/O. Inc/(Loss)	0	0	(4)	0	0	PAT Margin	13%	18%	16%	19%	20%
Interest Cost	19	21	22	20	18	Asset Turnover	2.3	3.0	3.9	5.0	5.5
PBT	44	68	97	149	186	Leverage	3.2	3.4	2.5	2.7	2.7
Tax	17	22	31	48	61	Debtor days	62	61	67	67	67
Rate	39%	33%	32%	33%	33%	Inventory days	24	31	28	30	30
Adjusted PAT	29	46	68	98	123	Creditor days	49	53	56	55	54
Growth	-10%	61%	46%	45%	25%	W.Cap cycle	37	39	40	43	44
PAT Margin	2.3%	3.0%	3.9%	5.0%	5.5%						

BALANCE SHEET (INRCR)						CASH FLOW (INRCR)					
Y/E MARCH	FY14	FY15	FY16	FY17E	FY18E	Y/E MARCH	FY14	FY15	FY16	FY17E	FY18E
Share Capital	8	8	8	8	8	EBITDA	81	108	143	193	231
Reserves	216	250	420	507	617	Adjustments	0	0	0	0	0
Networth	223	258	428	515	626	(Inc)/Dec in W.Cap	4	(63)	(67)	(51)	(41)
Loans	171	191	252	194	160	Pre Tax OCF	86	44	76	142	190
Minority Interest	4	5	20	25	31	Tax Paid	(15)	(21)	(31)	(54)	(66)
SOURCES OF FUNDS	399	455	701	734	817	CF from Operations	71	23	45	88	123
Gross Fixed Assets	449	494	645	711	796	(Inc)/Dec in FA	(37)	(43)	(151)	(65)	(85)
Less: Depreciation	209	231	259	289	323	Invst in Bank Deposits	26	(8)	30	10	12
Net Fixed Assets	241	264	386	421	473	Interest Received	3	8	9	7	7
Capital WIP	3	1	1	0	0	CF from Investing act.	(8)	(43)	(112)	(48)	(66)
Investments	18	20	20	20	20	Inc/(Dec) in Sh. Prem.	0	0	104	0	0
Inventories	91	136	139	169	190	Inc/(Dec) in Debt	8	21	61	(58)	(34)
Debtors	215	259	317	365	415	Interest Paid	(19)	(21)	(22)	(20)	(18)
Cash & Investments	72	42	106	54	44	Divd Paid (incl Tax)	(7)	(9)	(12)	(13)	(15)
Loans & Advances	107	138	67	77	87	CF from Financing act.	(17)	(9)	131	(92)	(67)
Other Curr Assets	2	5	11	12	12	Inc/(Dec) in Cash	46	(29)	64	(53)	(10)
Curr. Assets	486	581	640	676	749	Add: Opening Balance	26	72	42	106	54
Creditors and Prov.	321	382	310	347	389	Closing Balance	72	42	106	54	44
Net Current Assets	165	199	330	328	360						
Less Net Def. Tax Liab	28	29	36	35	36						
APPLICATION OF FUNDS	399	455	701	734	817						

Disclaimer: This document has been prepared by Motilal Oswal Securities Limited (hereinafter referred to as Most) to provide information about the company(ies) and/sector(s), if any, covered in the report and may be distributed by it and/or its affiliated company(ies). This report is for personal information of the selected recipient/s and does not constitute to be any investment, legal or taxation advice to you. This research report does not constitute an offer, invitation or inducement to invest in securities or other investments and Motilal Oswal Securities Limited (hereinafter referred as MOST) is not soliciting any action based upon it. This report is not for public distribution and has been furnished to you solely for your general information and should not be reproduced or redistributed to any other person in any form. This report does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, investors should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice. The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur.

MOST and its affiliates are a full-service, integrated investment banking, investment management, brokerage and financing group. We and our affiliates have investment banking and other business relationships with a some companies covered by our Research Department. Our research professionals may provide input into our investment banking and other business selection processes. Investors should assume that MOST and/or its affiliates are seeking or will seek investment banking or other business from the company or companies that are the subject of this material and that the research professionals who were involved in preparing this material may educate investors on investments in such business. The research professionals responsible for the preparation of this document may interact with trading desk personnel, sales personnel and other parties for the purpose of gathering, applying and interpreting information. Our research professionals are paid on twin parameters of performance & profitability of MOST.

MOST generally prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, MOST generally prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover. Our salespeople, traders, and other professionals or affiliates may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing among other things, may give rise to real or potential conflicts of interest. MOST and its affiliated company(ies), their directors and employees and their relatives may; (a) from time to time, have a long or short position in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.; however the same shall have no bearing whatsoever on the specific recommendations made by the analyst(s), as the recommendations made by the analyst(s) are completely independent of the views of the affiliates of MOST even though there might exist an inherent conflict of interest in some of the stocks mentioned in the research report

Reports based on technical and derivative analysis center on studying charts company's price movement, outstanding positions and trading volume, as opposed to focusing on a company's fundamentals and, as such, may not match with a report on a company's fundamental analysis. In addition MOST has different business segments / Divisions with independent research separated by Chinese walls catering to different set of customers having various objectives, risk profiles, investment horizon, etc, and therefore may at times have different contrary views on stocks sectors and markets.

Unauthorized disclosure, use, dissemination or copying (either whole or partial) of this information, is prohibited. The person accessing this information specifically agrees to exempt MOST or any of its affiliates or employees from, any and all responsibility/liability arising from such misuse and agrees not to hold MOST or any of its affiliates or employees responsible for any such misuse and further agrees to hold MOST or any of its affiliates or employees free and harmless from all losses, costs, damages, expenses that may be suffered by the person accessing this information due to any errors and delays. The information contained herein is based on publicly available data or other sources believed to be reliable. Any statements contained in this report attributed to a third party represent MOST's interpretation of the data, information and/or opinions provided by that third party either publicly or through a subscription service, and such use and interpretation have not been reviewed by the third party. This Report is not intended to be a complete statement or summary of the securities, markets or developments referred to in the document. While we would endeavor to update the information herein on reasonable basis, MOST and/or its affiliates are under no obligation to update the information. Also there may be regulatory, compliance, or other reasons that may prevent MOST and/or its affiliates from doing so. MOST or any of its affiliates or employees shall not be in any way responsible and liable for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. MOST or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

This report is intended for distribution to institutional investors. Recipients who are not institutional investors should seek advice of their independent financial advisor prior to taking any investment decision based on this report or for any necessary explanation of its contents.

Most and its associates may have managed or co-managed public offering of securities, may have received compensation for investment banking or merchant banking or brokerage services, may have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past 12 months.

Most and its associates have not received any compensation or other benefits from the subject company or third party in connection with the research report. Subject Company may have been a client of Most or its associates during twelve months preceding the date of distribution of the research report

MOST and/or its affiliates and/or employees may have interests/positions, financial or otherwise of over 1 % at the end of the month immediately preceding the date of publication of the research in the securities mentioned in this report. To enhance transparency, MOST has incorporated a Disclosure of Interest Statement in this document. This should, however, not be treated as endorsement of the views expressed in the report.

Motilal Oswal Securities Limited is under the process of seeking registration under SEBI (Research Analyst) Regulations, 2014.

There are no material disciplinary action that been taken by any regulatory authority impacting equity research analysis activities

Motilal Oswal Securities Limited is registered as a Research Analyst under SEBI (Research Analyst) Regulations, 2014. SEBI Reg. No. INH000000412

A graph of daily closing g prices of securities is available at www.nseindia.com and <http://economicstimes.indiatimes.com/markets/stocks/stock-quotes>.

Analyst Certification

The views expressed in this research report accurately reflect the personal views of the analyst(s) about the subject securities or issues, and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations and views expressed by research analyst(s) in this report. The research analysts, strategists, or research associates principally responsible for preparation of MOST research receive compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors and firm revenues

Disclosure of Interest Statement	Somany Ceramics Ltd.
1. Analyst ownership of the stocks mentioned above	No
2. Served as an officer, director or employee	No

Regional Disclosures (outside India)

This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject MOST & its group companies to registration or licensing requirements within such jurisdictions.



Motilal Oswal Securities Ltd

Motilal Oswal Tower, Level 6, Sayani Road, Prabhadevi, Mumbai 400 025
 Phone: (91-22) 30894200 Fax: (91-22) 22885038. E-mail: info@motilaloswal.com