

OCTOBER 9, 2018

	8-Oct	% Chg		
		1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	34,474	0.3	(10.2)	(3.3)
NIFTY Index	10,348	0.3	(10.7)	(3.9)
NSEBANK Index	24,618	0.7	(10.4)	(7.1)
NIFTY 500 Index	8,603	(0.3)	(12.9)	(6.4)
CNXMcap Index	16,055	(1.5)	(18.0)	(11.9)
BSESMCAP Index	13,563	(2.0)	(19.7)	(15.6)

World Indices				
Dow Jones	26,487	0.2	2.2	6.9
Nasdaq	7,736	(0.7)	(2.1)	(0.3)
FTSE	7,233	(1.2)	(0.6)	(5.9)
NIKKEI	23,784	(0.8)	5.6	8.2
Hangseng	23,784	(0.8)	5.6	8.2
Shanghai	26,203	(1.4)	(2.7)	(8.5)

Value traded (Rs cr)	8-Oct	% Chg Day
Cash BSE	3,249	2.9
Cash NSE	39,123	(1.5)
Derivatives	794,667	3.2

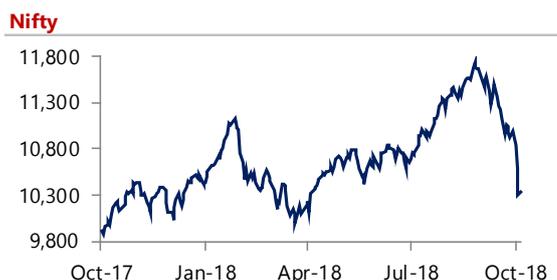
Net inflows (Rs cr)	5-Oct	MTD	YTD
FII	(5,010)	(10,405)	(25,467)
Mutual Fund	1,520	5,241	93,496

Nifty Gainers & Losers	Price	Chg	Vol
8-Oct	(Rs)	(%)	(mn)
Gainers			
HPCL	179	8.5	39.6
Yes Bank Ltd	221	7.4	62.4
Reliance Ind	1,109	5.8	24.7
Losers			
Vedanta Ltd	207	(10.8)	37.3
Hindalco Ind	223	(7.7)	25.2
Tech Mahindra	695	(2.7)	2.6

Advances / Declines (BSE)						
8-Oct	A	B	T	Total	% total	
Advances	128	216	47	391	100	
Declines	303	794	104	1,201	307	
Unchanged	-	14	20	34	9	

	8-Oct	% Chg		
		1 Day	1 Mth	3 Mths
Commodity				
Crude (US\$/BBL)	84.2	0.4	9.6	7.9
Gold (US\$/OZ)	1,188.2	(1.2)	(0.5)	(5.4)
Silver (US\$/OZ)	14.4	(1.9)	1.6	(10.7)

Debt / forex market	8-Oct	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	8.0	8.0	8.0	7.9
Re/US\$	74.1	73.8	72.4	68.7



Source: Bloomberg

News Highlights

- ▶ The International Monetary Fund (IMF) retained economic growth projection for India at 7.3% for FY19, lower than the government's and the Reserve Bank of India's (RBI's) forecasts. This is, however, noteworthy as the IMF cut global growth projections by 0.2% points. (BS)
- ▶ Bilateral trade of goods and services between India and the US has gone up by 119% since 2007, touching US\$126.2 bn, according to the United States Trade Representative. (BS)
- ▶ Despite the US pressuring India to cease oil imports from sanctions-hit Iran, the government is going ahead on negotiating greater oil purchases from the West Asian nation, along with Venezuela and Russia. However, this will be done with an aim to create a rupee-based trading mechanism with these nations, so as to reduce the exposure of the US dollar to India's largest import category. (BS)
- ▶ Gems and jewellery exports contracted by 0.75% to US\$13.18 bn in Apr-Aug FY19 as demand slowed down in major developed markets. According to the Gems and Jewellery Export Promotion Council (GJEPC) data, exports stood at US\$13.28 bn in Apr-Aug, 2017-18. (ET)
- ▶ Tamil Nadu has asked the Ministry of Finance to settle Rs 54.26 bn Integrated Goods and Services Tax for 2017-18 and the ad hoc settlement of IGST due for September 2018 immediately. Besides, the state also said that it should be compensated with a special assistance of Rs 20 bn for the unfair treatment that the state received under the 14th Finance Commission. (BS)
- ▶ **JSW Steel** is considering legal opinion on the possibility of a fresh bid for Essar Steel and would be interested in entering the fray with an independent offer if it is legally tenable in light of the recent Supreme Court order. (ET)
- ▶ **Tata Motors**, wholly owned subsidiary JLR's September sales were down 12.3% at 57,114 units, year-on-year basis. The company said that the monthly sales were impacted by the ongoing uncertainty in Chinese market as sales in China declined by 46.2% resulting from import duty changes and continued trade tensions which held back the consumer demand. (ET)
- ▶ A union of **Usha Martin** has raised concerns about irregular payment of salaries and sought government's intervention for sale of the company's wire rope manufacturing facility in Jharkhand to Tata Steel. (ET)
- ▶ **Federal Bank** said the Reserve Bank has approved proposal to sell up to 45% stake in NBFC arm Fedfina to private equity firm True North. (ET)
- ▶ **GMR Infrastructure** will give Rs 35.6 bn by way of cash and 5.86% stake in its airport holding company to three private equity (PE) investors, ending two years of litigation. (BS)
- ▶ **Suzlon**, is looking at monetising some of its assets, amid an anticipated rise in sales volume from the next financial year, both at home and abroad. (BS)

What's Inside

- ▶ **Company Update:** Kajaria Ceramics Ltd

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, IE = Indian Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange, MC = Moneycontrol

Company Update

Stock Details

Market cap (Rs mn)	:	53225
52-wk Hi/Lo (Rs)	:	765 / 328
Face Value (Rs)	:	1
3M Avg. daily vol (mn)	:	928,517
Shares o/s (mn)	:	159

Source: Bloomberg

Financial Summary

Y/E Mar (Rs mn)	FY18	FY19E	FY20E
Sales	27,106	30,639	33,127
Growth (%)	6.3	13.0	8.1
EBITDA	4,564	4,596	5,300
EBITDA margin (%)	16.8	15.0	16.0
Net profit	2,344	2,395	2,834
EPS (Rs)	14.7	15.1	17.8
Growth (%)	9.0	2.2	18.4
BVPS (Rs)	85.0	96.4	110.7
DPS (Rs)	3.0	3.0	3.0
ROE (%)	18.6	16.6	17.2
ROCE (%)	22.0	20.3	22.2
P/E (x)	22.9	22.4	19.0
EV/EBITDA (x)	12.2	12.0	10.3
P/BV (x)	4.0	3.5	3.1

Source: Company, Kotak Securities - PCG

Shareholding Pattern (%)

(%)	Jun-18	Mar-18	Dec-17
Promoters	47.6	47.6	47.6
FII	26.1	28.1	28.7
DII	9.6	9.2	7.4
Others	16.4	15.1	16.3

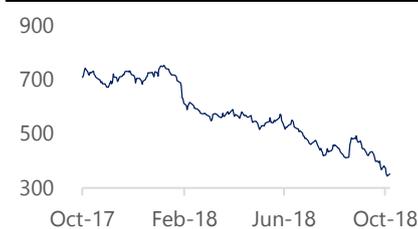
Source: Company

Price Performance (%)

(%)	1M	3M	6M
Kajaria Ceramics	(24.6)	(27.9)	(41.3)
Nifty	(10.7)	(3.9)	0.2

Source: Bloomberg

Price chart (Rs)



Source: Bloomberg

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KAJARIA CERAMICS LTD

PRICE Rs.338

TARGET Rs.500

BUY

Tile industry has continued to remain impacted by higher gas prices, rupee depreciation and lower than expected compliance towards GST. In our recent interaction with Kajaria Ceramics, company has mentioned that a significant shift of unorganized segment demand towards organized segment has not happened even after e-way bill implementation. Demand is coming from individual housing and renovation works but builder segment continues to remain weak. Prices seem to have largely bottomed out but margins can come under pressure due to higher power costs.

Key highlights about the company:

Demand improvement is being witnessed in select pockets

Demand environment for tiles segment is still subdued as the real estate segment demand particularly from mid-high end segment has not kicked off. The revival in real estate demand is kicking in only in pockets post RERA impact. However, individual housing segment demand mainly from Tier 2 and Tier 3 cities is driving the volumes. Also, low cost housing is also fueling demand for low-end tiles for various players. Post E-way bill implementation also, demand from unorganized segment has not moved towards organized segment as under-billing is still happening in the sector. We believe that improvement in compliance levels is likely to happen only after the elections get over.

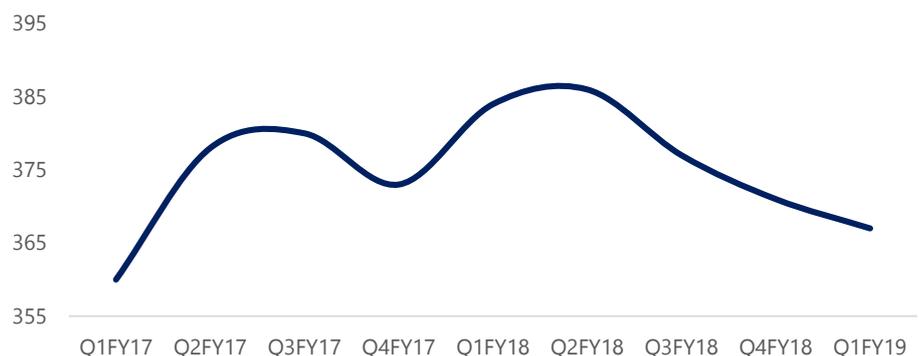
Several players in Morbi and western India are selectively focusing on exports and are likely to benefit from the recent fall in rupee. Thus, industry players expect demand improvement to be largely led by mid-housing segment, low cost housing and exports during FY19.

Prices seem to have bottomed out

Average realizations of the company had been continuously coming down since past few quarters led by increased competition from unorganized segment as well as commissioning of large number of units in GVT segment. We believe that prices have also largely bottomed out with most players operating at break-even level in the GVT category. Morbi players are also now working on thin margins due to increase in power costs and hence further decline in prices especially in the GVT segment is not expected.

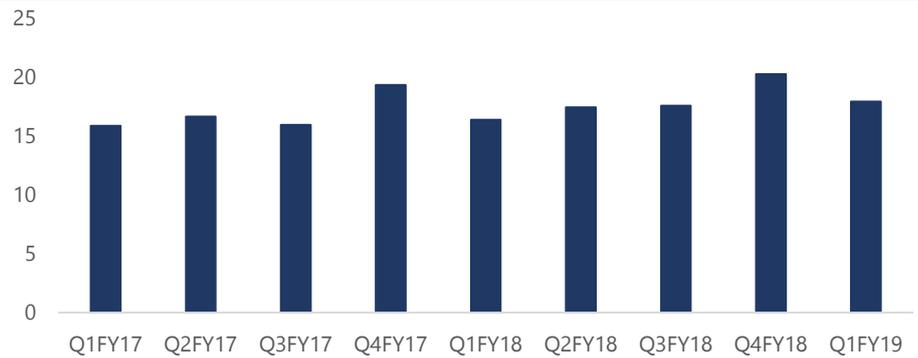
Company is also facing increased competition from various players like Varmora, Simpulo etc but being a diversified national player, Kajaria Ceramics will have an edge over other players once demand and pricing revival starts kicking in.

Kajaria Ceramics Average realization (Rs/msm)



Source: Company

Kajaria ceramics volumes (MSM)



Source: Company

Hike in gas prices

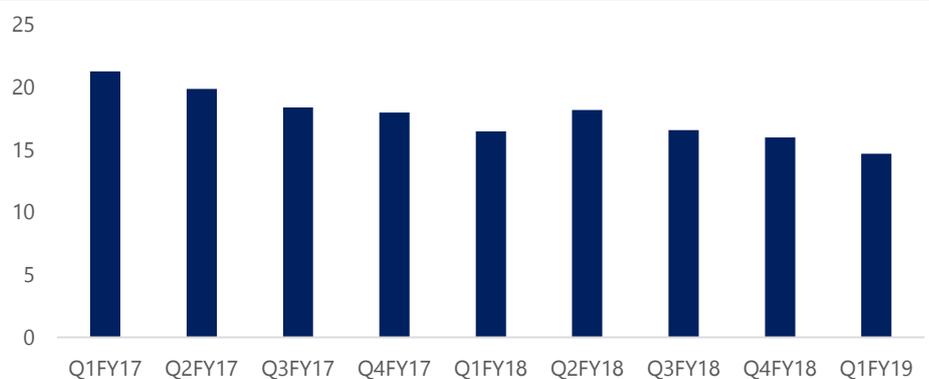
With increase in Brent crude prices, gas prices have also moved up sharply for the tile players thereby it can impact margins negatively as it was difficult to pass on the increase in gas prices in current scenario. Impact of rupee depreciation is also likely to be reflected in higher gas prices for the company. Kajaria Ceramics had hiked prices of ceramic tiles by 3% during July, 2018. Along with this, the correction seen in glazed vitrified tiles in past few quarters due to commissioning of large number of capacities in GVT category or conversion of ceramic plants to GVT plants, seems to be largely over. GVT prices were largely stable during Q2FY19.

Singapore Spot LNG (\$/mmbtu)



Source: Bloomberg

OPM (%)



Source: Company

Financials during Q2FY19 to be impacted by monsoons and higher power cost but JV performance is improving

Results of the company during Q2FY19 are expected to be impacted by floods in Kerala. Company sells nearly 12% of its volumes in Kerala and hence the impact of floods is likely to be reflected in lower volumes during the quarter. Along with this, there was a truckers' strike during July and festive season in Maharashtra during Aug-Sep, 2018 which can also impact volumes. Volumes are likely to improve from October onwards with demand improvement as well as redevelopment of Kerala post monsoons.

During Q2FY19, gas prices moved up further sequentially and on yearly basis. This is likely to put pressure on margins as full hike in the cost of power has not been passed on to the end users. However, the performance of JV's is improving slowly with loss making JVs having achieved break-even and are now expected to make profits going forward.

Capex target

The expansion plan of 5mn sq m in AP is progressing on time and is expected to commission by Q4FY19/Q1FY20. Kajaria ceramics plans to reach 100 mn sq m by 2021 through incremental additions and outsourcing. It can be through brown field or green field expansion in North while in south and western region, they can have a JV. It expects a capex of Rs 1.5 bn in FY19 and a branding spend Rs 1.1-1.15 bn in FY19.

Financial outlook

We revise our volume estimates downwards for FY19/20 to factor in slower than expected compliance towards e-way bill implementation. We thus expect revenues to grow at a CAGR of 10.6% between FY18-20. (as against CAGR of 11.7% estimated earlier).

Margins are likely to be impacted by higher power costs as the price hikes have been much slower than cost hikes. However, improvement in JV performance is likely to aid margins to some extent. We expect margins of 15%/16% for FY19/20 respectively. (16%/16% estimated earlier for FY19/20 respectively).

Post revising our estimates, we expect net profits to grow at a CAGR of 10% between FY18-20.

Valuation and recommendation

Stock is currently trading at valuations of 22.4x and 19.0x P/E on FY19 and FY20 estimates respectively. The challenges in the tile sector are likely to remain for another few quarters - lower realizations, higher gas prices are likely to have an adverse impact on projected financials as well as valuation multiples. There is still continued higher proportion of unorganized sales even after implementation of GST and e-way Bill. We revise our estimates to factor in slightly lower volumes and higher costs and arrive at a revised price target of Rs 500 based on 28x FY20 estimated earnings (Rs 551 earlier).

We believe that though the shift from unorganized to organized players post GST and e-way bill implementation has not happened to a large extent so far, but with improved compliance towards e-way bill implementation post elections, organized players like Kajaria Ceramics are likely to benefit with market leading position and wide offering of products. We remain positive on the company and maintain **BUY**.

About the company

Kajaria Ceramics is the largest manufacturer of ceramic/vitrified tiles in India and the 9th largest in the world. It has an annual capacity of 68.37 mn. sq. meters presently, distributed across eight plants - one in Sikandrabad (UP), one in Gailpur (Rajasthan), One in Malutana (Rajasthan), four in Morbi (Gujarat) and one in Vijaywada (AP).

Financials: Consolidated

Profit and Loss Statement (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Revenues	25,496	27,106	30,639	33,127
% change YoY	6.0	6.3	13.0	8.1
EBITDA	4,963	4,564	4,596	5,300
% change YoY	8.0	(8.1)	0.7	15.3
Other Income	154	116	100	100
Depreciation	814	885	964	1,088
EBIT	4,303	3,794	3,732	4,312
% change YoY	9.0	(11.8)	(1.6)	15.6
Net interest	340	241	191	105
Profit before tax	3,963	3,553	3,541	4,207
% change YoY	10.0	(10.3)	(0.3)	18.8
Tax	1,425	1,267	1,204	1,430
as % of PBT	36.0	35.7	34.0	34.0
Profit after tax	2,538	2,286	2,337	2,777
Minority interest and other CI	17	(58)	(58)	(58)
Net income	2,521	2,344	2,395	2,834
% change YoY	9.0	(7.0)	2.2	18.4
Shares outstanding (m)	158.9	159.0	159.0	159.0
EPS (reported) (Rs)	15.9	14.7	15.1	17.8
CEPS (Rs)	21.0	20.3	21.1	24.7
DPS (Rs)	3.0	3.0	3.0	3.0

Source: Company, Kotak Securities – Private Client Research

Cash flow Statement (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
EBIT	4,286	3,852	3,790	4,370
Depreciation	814	885	964	1,088
Change in working capital	(303)	(1,305)	71	(482)
Chg in other net current assets	39	(207)	325	-
Operating cash flow	4,836	3,226	5,149	4,976
Interest	(340)	(241)	(191)	(105)
Tax	(1,425)	(1,267)	(1,204)	(1,430)
CF from operations	3,071	1,718	3,754	3,441
Capex	(1,386)	(657)	(2,500)	(2,500)
(Inc)/dec in investments	-	-	-	-
CF from investments	(1,386)	(657)	(2,500)	(2,500)
Proceeds from issue of equity	-	0	-	-
Increase/(decrease) in debt	(991)	(173)	(1,000)	(1,000)
Proceeds from share premium	-	(12)	-	-
Dividends	(381)	(572)	(572)	(572)
CF from financing	(1,372)	(757)	(1,572)	(1,572)
Opening cash	199	520	824	506
Closing cash	512	824	506	(126)

Source: Company, Kotak Securities – Private Client Research

Balance sheet (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Cash and cash equivalents	520	824	506	(126)
Accounts receivable	3,389	4,507	4,463	4,825
Inventories	3,720	3,785	4,242	4,586
Loans and Adv & Others	795	574	621	648
Current assets	8,424	9,689	9,830	9,933
Other non-current assets	121	82	82	82
LT investments	1	4	4	4
Net fixed assets	11,856	11,627	13,163	14,575
Total assets	20,401	21,403	23,080	24,594
Payables	2,921	2,578	3,108	3,360
Others	655	580	580	580
Current liabilities	3,576	3,158	3,688	3,940
Provisions	308	248	572	572
LT debt	2,900	2,728	1,728	728
Min. int and def tax liabilities	1,866	1,759	1,759	1,759
Equity	159	159	159	159
Reserves	11,592	13,351	15,174	17,435
Total liabilities	20,401	21,403	23,080	24,594
BVPS (Rs)	74.0	85.0	96.4	110.7

Source: Company, Kotak Securities – Private Client Research

Ratio Analysis

(Year-end Mar)	FY17	FY18	FY19E	FY20E
EBITDA margin (%)	19.5	16.8	15.0	16.0
EBIT margin (%)	16.9	14.0	12.2	13.0
Net profit margin (%)	9.9	8.6	7.8	8.6
Receivables (days)	43.9	53.2	53.2	53.2
Inventory (days)	54.1	50.5	50.5	50.5
Sales/assets (x)	2.2	2.3	2.3	2.3
Interest coverage (x)	12.7	15.7	19.6	41.0
Debt/equity ratio(x)	0.3	0.2	0.2	0.1
ROE (%)	23.6	18.6	16.6	17.2
ROCE (%)	27.0	22.0	20.3	22.2
EV/ Sales (x)	2.2	2.1	1.8	1.6
EV/EBITDA (x)	11.3	12.2	12.0	10.3
Price to earnings (x)	21.3	22.9	22.4	19.0
Price to book value (x)	4.6	4.0	3.5	3.1
Price to Cash Earnings (x)	16.1	16.6	16.0	13.7

Source: Company, Kotak Securities – Private Client Research

RATING SCALE

Definitions of ratings

- BUY** – We expect the stock to deliver more than 12% returns over the next 12 months
- ACCUMULATE** – We expect the stock to deliver 5% - 12% returns over the next 12 months
- REDUCE** – We expect the stock to deliver 0% - 5% returns over the next 12 months
- SELL** – We expect the stock to deliver negative returns over the next 12 months
- NR** – **Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
- SUBSCRIBE** – We advise investor to subscribe to the IPO.
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- NA** – **Not Available or Not Applicable.** The information is not available for display or is not applicable
- NM** – **Not Meaningful.** The information is not meaningful and is therefore excluded.
- NOTE** – Our target prices are with a 12-month perspective. Returns stated in the rating scale are our internal benchmark.

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