



# Cera Sanitaryware Limited

## Q3 FY 2023 Earnings Conference Call Transcript

February 3, 2023

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**Moderator:** Ladies and gentlemen, good day and welcome to the Q3FY23 earnings conference call of Cera Sanitaryware Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing star, then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Mayank Vaswani from CDR India. Thank you and over to you Mr. Vaswani.

**Mayank Vaswani:** Thank you, Rutuja. Good morning, everyone and thank you for joining us on the earnings conference call of Cera Sanitaryware Limited to discuss the Q3FY23 earnings, which were announced yesterday.

We have with us today the management team comprising Mr. Ayush Bagla, Executive Director; Mr. Rajesh B. Shah, CFO and COO and Mr. Vikas Kothari, Deputy CFO at Cera Sanitaryware.

We will begin the call with brief opening remarks from the management, following which we shall open the call for Q&A. Some of the statements made in today's conference call may be forward-looking in nature and a detailed note in this regard is contained in the results documents that have been shared with all of you earlier.

I will now turn the call over to Mr. Ayush Bagla for his opening remarks.

**Ayush Bagla:** Good morning, everyone. The earnings for the quarter ended 31<sup>st</sup> December 2022 were adopted by the Board of Directors yesterday 2<sup>nd</sup> February 2023. The earnings documents have been released to the stock exchanges.

During the quarter gone by, we continued to witness strong demand for our products, as the overall replacement demand remained quite positive with consumers continuing to spend on home upgradation and improvement. The velocity of sales for newly built homes and for existing residential apartments continues to be very strong.

At present, our manufacturing facility continues to function at high utilization levels. During the quarter, the sanitaryware plant had a 15-day annual maintenance period, despite which capacity utilization for Q3FY23 for sanitaryware was at 105%.

In Faucetware, the capacity utilization was at 115% during Q3FY23 and all efforts are on to maintain these levels. Our current monthly production for December 2022 at the Faucetware plant was 3 lakh pieces, in FY 2022, it was an average of 2.18 lakh pieces per month. In FY21, it was an average of 1.25 lakh pieces per month. The current production is a 38% increase over the production level of FY22 and a 214% increase over FY21.

The Faucetware expansion program to take capacity to 4 lakh pieces per month commenced from July 2022, requisite approvals from Gujarat Pollution Control Board has been obtained. The enhanced production is scheduled to go on stream in July 2023 and in a staggered manner will result in an increase in monthly production to 4 lakh pieces per month by March 2024. The total cost of project is INR 69 crore to be entirely financed from annual operating cash flow. Building and civil work out of INR 69 crore is INR 37 crore, equipment and plant is INR 25 crore, electrical substation is INR 7 crore. We expect to complete the project in time and well within the cost of INR 69 crore. The product mix planned is coloured SKUs, quarter turn SKUs, PVD SKUs and a few more SKUs that can be taken in from outsource partners.

So far not a single day of disruption of current manufacturing at the faucetware plant has taken place. The market has been continuously fed with products from the existing plant. In April 2022, newer value-added SKUs in faucetware were introduced at the National Dealer Meet. SKUs in four ranges and in six colours were introduced to the trade. These value-added products included black matt finished faucets, red matt finished faucets and other PVD products. An extensive range of Rose Gold, French Gold and Yellow Gold products were part of the event. These new products are being gradually rolled-out with a grand display at 100 dealers outlets.

In FY22, China imports was INR 67 crore or 4.71% of sales. In nine months, FY23, China imports were INR 47 crore, 3.74% of sales. Cera was already one of the lowest users of products made in China and with availability of manufacturing infrastructure in-house, the percentage of Chinese import to sales have been continuously declining. In a business, which is brand-driven, the fulcrum of success is manufacturing quality and plant efficiency.

For fresh capacity for manufacturing sanitaryware, the Company has carried out extensive surveys of water, gas and labor availability for a greenfield facility. A land parcel in Gujarat has been short listed and the Company is currently undertaking due diligence. We expect title documents to be executed and land conversion procedures to take place over the next six to nine months.

As on 31<sup>st</sup> December 2022, our cash and cash equivalents stood at INR 597 crore against INR 523 crore in December 2021, an increase of INR 74 crore or a 14% increase. Positive cash flow for Q3FY23 has been INR 58 crore as compared to Q3 FY22 which was INR 48 crore. Therefore, going forward only internal accruals are

being used to fund the two capex programs and we would also retain the flexibility to use some part of cash and cash equivalents if required. No debt raising or equity dilution is planned or required for both the capacity expansions.

During Q3FY23, no price hikes were undertaken. Our peer group companies increased prices in October and November 2022, while Cera did not. During 2021 and 2022, many price hikes were undertaken by Cera which were all a demonstration of pricing power. Currently, we are capitalizing on the market-share gained over the last two years.

On the sanitaryware business, raw materials like China clay, Feldspar and Plaster of Paris had a moderate increase in pricing of between 5% and 7%. Within the glazing recipe, zinc moved down by 6% and glaze moved down by 9% during Q3. In faucetware, brass prices declined by 1.4% in Q3 and 10% over nine months of this financial year.

From 1<sup>st</sup> February 2023 a price rationalization exercise has been implemented. There is now a single MRP across the entire country. The impact on pricing for sanitaryware is an increase of 0.5% to 1% across some markets and in faucetware, a decrease of 0.5%. Due to availability of gas from isolated wells near our plant, the pricing of gas from GAIL continues to remain below market and will remain so in the future.

Price has increased from INR 26 per cubic meter in September 2022 to INR 35 per cubic meter in December 2022. Normally GAIL supplies 50% of Cera's gas needs. However, in Q3FY23, GAIL provided 67% of gas requirement for the sanitaryware business.

Sabarmati, a JV of BPCL and GSPC's pricing went down from INR 75 in September '22 to INR 67 per cubic meter in December 2022, supplying 33% of gas needs of the plant in Q3. In January '23, another round of reduction took place in Sabarmati from INR 67 to INR 59. The Q3 weighted-average cost of gas is INR 47, much lower than industry. Gas costs constitute 2.53% of Cera's topline. There have been no changes in the price of ancillary cost items like transportation. The cost of corrugated boxes have remained stable.

We launched a retailer loyalty program in Q1FY23 which has now almost completed nine months. More than 13,500 retailers have uploaded 1.1 lakh invoices. These retailers form the bulk of Cera's distribution reach. We expect the total number of retailers to be around 15,000 plus, who most likely will be part of this loyalty program by FY23. The feedback received from retailers has helped us in the understanding of consumers' changing demands, geographical segmentation of SKUs and evolution of the rewards program to retailers.

Of the total retail sales of INR 747 crore in nine months, more than INR 240 crore of sales which is 32% of retail sales in sanitaryware and faucetware have become eligible to receive rewards through this program. The Company's ability to tweak

trade practices, trade pricing, an ability to steer the direction of the dealer and retailer equation have all undergone a sea change. We also have seen an opportunity in multi-brand retailers who have undertaken various initiatives to sell Cera products.

This ties in very well with new product development, as product lifecycle reduces, new product offered at higher price points with dramatically new aesthetics and functionality are core to our topline and margin expansion. In Q3FY22, 67 new products were introduced. In Q3FY23, 614 products, including 496 of the Lustre series have been introduced. New products launched in the last three years constituted 39% of Cera's topline in Q3. Our highest ever advertising spends in FY 19 was INR 52 crore and in this financial year it is likely to be INR 55 crore. Cera's share of voice was lower than its market share and now with increase in advertising expenses, it's share of voice is getting closer to its share of market.

Publicity spends which were INR 5 crore in Q3FY22 were increased to INR 17 crore in Q3FY23. The ad campaign will continue into Q4FY23. In Q3, sales to Tier 1 markets were 27% of sales, Tier 2 were 11% of sales and Tier 3 was 62% of sales. We classify markets based on population. Population centers of above 25 lakhs are classified as Tier1 markets and population centers between 10 and 25 lakhs as Tier 2 markets and below 10 lakh, as Tier 3 markets. The large number of 62% in Tier 3 is more a function of this classification, rather than the Company's focus on Tier 3 markets. If we calculate population center of 17 lakhs and above as Tier 1, population centers of 3 lakh to 17 lakhs as Tier 2 and below 3 lakhs as Tier 3, then the ratio would be 32% of sales for Tier 1, 24% of sales for Tier 2 and 44% for Tier 3.

In that backdrop, we can go over the financials:

Revenue from operations in Q3FY23 was INR 456 crore versus INR 387 crore in Q3 FY22. EBITDA excluding other income was INR 73 crore in Q3FY23 versus INR 61 crore in Q3FY22. The gross margin has improved, is currently at 54% in Q3FY23 against 52% in Q3FY22. The EBITDA margin is higher by 20 basis points at 16% in Q3 FY23 versus 15.8% in Q3FY22. Profit after tax was INR 56 crore in Q3FY23 versus INR 42 crore in Q3FY22, an increase of 33.3% Y-o-Y. EPS for Q3FY23 was 43.34 versus 32.50 in Q3FY22.

In Q3FY23, 54% of the topline was from sanitaryware, 33% from faucetware, tiles represented 12% and wellness 1%. On a Y-o-Y basis, sanitaryware revenues registered an increase of 19%, faucetware revenues increased by 12%, tiles increased by 34% and wellness increased by 5%. The sanitaryware and faucetware verticals remains the bedrock of the business with contribution of 87% to our overall revenues. The classification of sales in Q3FY23 was 45% in the premium category, 28% in the mid category and 27% in the entry category.

Inventory days in Q3FY23 were 83 days compared to 67 days in Q3FY22. Receivable days in Q3FY23 were 30 days versus 30 days, payable days in Q3FY23 were 37 days

against 36 days in Q3FY22. Therefore, net working capital days in Q3FY23 was 76 days versus 61 days in Q3FY22. This number is around the optimum number of inventory days that Cera has been making efforts to achieve for many quarters.

In this quarter, availability of product ensured there was no element of lost sales. This is the seventh straight quarter with no element of lost sales. In the current year, the capex budget, other than the brownfield faucetware expansion and the proposed greenfield sanitaryware capacity expansion programs are INR 25 crore, of which INR 3 crore are spent in nine months of which INR 1 crore was spent in Q3.

In conclusion, I would like to say that due to the combination of internal factors, production throughput maximization, brand salience and design differentiation, as well as macros of home improvement, Cera would be able to monetize all the growth drivers that present themselves. Cera growth plans remain intact as it plans to expand capacity than to monetize rising demand. After taking a few years to break the INR 1,250 crore to INR 1,350 crore topline band, in FY22 Cera touched a topline of INR 1,446 crore. We also had the impact on EBITDA and PAT margins. Going forward, Cera is set on a new topline trajectory, which we can all witness in the nine-month numbers. Every decision made at Cera is from the shareholders point of view with ROCE, payback period and impact on EPS fully considered before being placed for deliberation amongst the Board of Directors.

I would now request the moderator to open the lines for Q&A. Thank you very much.

**Moderator:** Thank you very much. The first question is from the line of Achal Lohade from JM Financial. Please go ahead.

**Achal Lohade:** What I wanted to check was in terms of the outlook, how do you see FY24, given the capacity constraint on the sanitaryware part? So, if you can give some colour as to how you see FY24 in terms of the growth?

**Ayush Bagla:** See, currently capacity is not a constraint both in-house and outsourced. And if you can see from this year, in the current quarter outsourced in sanitaryware is 63%, in faucetware is 51%. So, a combination of internal and external resources are available first. Secondly, even within the internal resources, lot of capacity is being freed up to make higher-end SKUs. So, inventory days have been moving up and inventory days have been moving up because of this distributed inventory model that is unique to Cera. We would like to have all SKUs which are relevant for those markets available at all times in those markets. So that was the aim. We are not looking at any kind of constraints right now, as far as capacity is concerned, whether for the balance three months of this financial year or for FY24.

In faucetware, of course, the capacity is coming on stream in July and to reach 4 lakhs it might take a few months from July. And in sanitaryware, the land acquisition program is well underway, due diligence is currently on. So both due diligence and conversion and other approvals from the State Government, we expect all that to

get over within this calendar year. And then work to begin by the end of calendar year or latest by March 2024. But in any case, so there is no case made out for any kind of capacity constraints. At the same time, China imports are reducing. So, all these initiatives have been tackled in a multi-dimensional manner.

**Achal Lohade:** Any number you would like to, like can we do double-digit or high-single-digit, mid-teens any broad number?

**Ayush Bagla:** You can calculate based on this velocity of sales, what are FY23 numbers are going to be looking like. So other than that, that same 40 months doubling from 1,440 to 2,900, that remains intact, and investors and analysts should get the requisite confidence from these numbers in a market that was not maybe that conducive to these numbers that we'll achieve or beat those numbers.

**Achal Lohade:** And just in terms of the market share, any ballpark number you would like to share for sanitaryware and faucet?

**Ayush Bagla:** See we get more anecdotal return market share rather than any industry published report. So Cera is definitely the market-leader in sanitaryware and the number two player in faucetware. In sanitaryware, we are gaining from the next three players, the second, third and fourth player, that is one. In faucetware, we are capturing a larger share of the growth in the market. So, whatever our incremental market share number is, 1.5 times that.

**Achal Lohade:** Sir, if you could give a ballpark number for nine months or for FY22 or FY23 whatever you can best in terms of market-share would that be 20%, 15%, anything of that?

**Ayush Bagla:** So there is no authenticity of the data, so I'll be very careful before I give any data.

**Achal Lohade:** Yeah, I mean, at least your own estimate you may not call it as industry publication, but...

**Ayush Bagla:** We have never done it in the past, you've known this Company for so many years, it's never happened in the past that we gave out industry data or even market share data.

**Moderator:** The next question is from the line of Rakesh Wadhvani from Monarch AIF.

**Rakesh Wadhvani:** Sir, I wanted to understand, what is Cera doing differently or the things that they have done in the past that are benefiting them, because if you see the results of the peers, they have not grown, but Cera has grown in sanitaryware, faucetware and tiles also. So just want to understand what is Cera doing differently with respect to product, pricing, distributions, promotion. One point that you mentioned, you have now a new scheme for the retailers, if you can give your thought on what Cera is doing differently on the product, pricing point that is giving them edge in the market.

**Ayush Bagla:**

So the question you asked is very important and this is all a outcome of the efforts that have gone over the last five years. First of all, was manufacturing efficiency. Very few plants and especially we have the largest sanitaryware plant in the country, can operate at high 90s or 100 or even above 100% capacity utilization. So we tackle the industry-wide problem of product availability first, we ensured availability. That was one.

Second was, new product development. On an industry-wide basis, new products constitute 10% of sales for any Company. In Cera that number has always been around 20%, 22%, 24%. This quarter that number was 39%, last quarter that number was 36%. So new product development ensuring we are able to reduce product lifecycles and innovate on the basis of design differentiation and functionality. That was our second (inaudible). So 39% of sales are being captured or monetized that were not available, maybe to the industry and definitely not to the Company. Third, this retailer loyalty program that you mentioned. This industry had never practiced any kind of outreach beyond the dealer distributor. So now we have gone directly to the retailer. So, we get very granular data on consumer demand, consumer preferences, the equation between the dealer-retailer and what the retailer is looking for retailer rewards. So that is a direct program to the retailer, that is the absolute cracking of the last mile problem, which is there in most industries and definitely in the building material industry.

And you compared us to other peer companies, see the peer companies, they may be operating in more commoditized businesses, where slight changes in price and slight overcapacity in the industry have huge reflections and outcomes for companies. In sanitaryware and faucetware, it is a smaller industry, more dependent on quality, brand promise and those factors. So, Cera has clearly stood out, Cera is an outlier in each of those departments. On the financial front, topline growth, EBITDA growth, PAT growth and margin growth, on all the fronts we have delivered.

**Rakesh Wadhvani:**

One point just wanted to clarify on the retailer. So you said Cera has started a retailer that loyalty program. So, what was happening earlier, what used to happen in a channel like you, Cera will be selling the products to the dealer and distributor, dealer and distributors will be in touch with the retailers, so they will be having inventory in their own depots. Now Cera is directly going to the retailer and who will be stocking inventory – the dealer, distributor or the Cera?

**Ayush Bagla:**

There has been no change in business practices. We still sell to the dealers who sell to retailers. So, our equation with dealers has not changed. In fact, dealers have welcomed this program because Cera is rewarding their retailers. So, the stickiness between retailer and dealer has increased because of this program. So, no change in either stocking or inventory management or transactions between Cera and the dealers. This is just identification of all dealers, high-performing retailers and how to reward loyalty to Cera.

**Rakesh Wadhvani:** Just thought, like we have from 2010 we have adopted one strategy that in order to enter into any business, we will always start with outsourcing, the moment we think we are doing very good, we go in-house. But we've always maintained that strategy of 50% in-house and around 50% outsourced, that strategy has worked for us in the decade amazingly. Just wanted to understand, but if we do it in-house also, we will have a more profitability compared to like outsource will have a lesser profitability, your thoughts on that whether why because now we have a cash also, now we have understood the business very well. So just your thoughts on that?

**Ayush Bagla:** See, currently there are no plans to enter any new industry. And as far as sanitaryware and faucetware is concerned, many industry players have tried with fully in-house manufacturing and full outsourcing. So, those haven't worked, that business model requires the Company to have large-scale own manufacturing and make high-end pieces in-house and outsource products where vendors can do a better job in terms of price. So, this is a very delicate business model, that's why it's very difficult to succeed in sanitaryware and faucetware and that's why we say this business is completely mated. And if you remember over the last five, six quarters, there were lot of concerns that there are going to be so many new entrants in sanitaryware. They have not been able to put up capacities and they have not been able to achieve scale because dealers don't take them seriously and consumers transferability of a brand from a commoditized business to a completely brand-driven business is very difficult.

**Moderator:** Thank you. The next question is from the line of Sudarshan Mall from Dhunseri Investments. Please go ahead.

**Sudarshan Mall:** Ayushji, you said this you guys have very-high proportion of new inventory of 39% versus industry-standard of say around 10%, 12%. Just wanted to get some colour on how do you manage the old inventory? So, let's suppose my question is, if you have such high proportion of new innovative products, how do you deal with the older ones?

**Ayush Bagla:** The new products, it's not inventory, it's new sales, so the new products which were introduced in the last three years constitute 39% of sales. And most often you will find that new products which replace old products come with added design differentiation or functionality differentiation and also often at higher price points. So not only do we cannibalize our competitors SKUs, we are quite ready to cannibalize our own SKUs. And...

**Sudarshan Mall:** I was trying to understand, how do you manage this cannibalization from our own inventory?

**Ayush Bagla:** That is planned, well-planned exercise production, sales, inventory managed, management is all aligned to when a product will be suddenly phased down and a new product with a higher price point will be introduced. So, in the last seven quarters, you are seeing no element of lost sales, no element of sales where a dealer or a consumer or retailer was asking for a particular SKU and Cera couldn't



provide it. And as far as inventory management is concerned, you see this is a unique industry where the product is neither perishable nor the standard product, the high selling SKU's change due to change in consumer preferences. So, a high-level of inventory is one of the key to success in this business.

**Sudarshan Mall:** Sir, after having delivered such stupendous performance for last couple of quarters, you just now mentioned that you stick to your 40 months doubling of topline. Just I guess that you have been somewhat conservative, is that correct?

**Ayush Bagla:** See, if you look at the industry growth, the number I have mentioned is almost 1.8 times industry growth. So...

**Sudarshan Mall:** Certainly, certainly. I'm not saying on absolute basis that it is conservative, but in the backdrop of the stupendous performance that you guys have delivered in the last couple of quarters which is I feel taken away a lot of mistakes, so that's why, in that backdrop I wanted to understand that maybe I feel that you will play out some (inaudible) or something like that (inaudible) to grow in this industry in such a phenomenal way.

**Ayush Bagla:** See when I mentioned that 1,440 will become 2,900, it was met with some degree of scepticism and I'm glad to hear now that the financial community is saying that 2,900 is a conservative target. So that is a great achievement for the Company.

**Sudarshan Mall:** Does that mean you also agree that it's a conservative number?

**Ayush Bagla:** No, I think we will want to surpass any kind of guidance first and then look at fresh number or fresh target. So, this trajectory of sale has convinced everybody that 2,900 in 40 months is definitely achievable. We might surpass that. So I think that is a more immediate short-term goal after which newer benchmarks will be set.

**Moderator:** Thank you. The next question is from the line of Pranav Mehta from Equirus Securities. Please go ahead.

**Pranav Mehta:** Sir, firstly on the outsourcing mix I wanted to understand; till the stated expansion comes in, where do you see this mix going up for Cera?

**Ayush Bagla:** I think it will stay steady and this has been the normal number. Normally, it's 60:40 this quarter, it is 63:37 and in faucetware 51:49 which is almost fifty-fifty. So, this number will remain constant for the time being, because in value terms, the output from the factory is also increasing by taking in certain products which were either imported from China or made from even domestic partners, those are all being taken in the factory, which are in some cases, higher-value products as well. So, in value terms, the factory will not decline from 40%, even over the next 24 months or so till the new greenfield sanitaryware capacity comes on-stream.

**Pranav Mehta:** This is largely because of replacement of products manufactured at the factory, right, moving to higher-priced products or?

**Ayush Bagla:**

Yes, in any case the high-end products are made only in a manufacturing facility. And the low-end ones which vendors can do a better job at a lower-cost are given to outsourcing partners, that has always been the philosophy. But within these hundreds of SKUs now specific SKUs are being identified to be taken inward. And if any low-end products are being made in the manufacturing facility that are given to vendors, freeing up some capacity. So, as you can see, our inventory days target was between 80 and 90, that has been achieved, that was very important to get this growth correct and increase in topline it was very important to have requisite products available on a distributed model across the country.

**Moderator:**

Thank you. The next question is from the line of Aashish Uppanlawar from InvesQ Investment Advisors. Please go ahead.

**Aashish Uppanlawar:**

Ayush, I mean commendable with the way Cera is executing the plans that you've shared earlier. So just wanted to check I mean target that you shared are pretty good, but what risk do you see maybe in the external environment, especially I mean what can maybe soften these kind of growth that you are achieving therefore, I mean any risk that you see on the margin or the topline front?

**Ayush Bagla:** See, the numbers that you're seeing is outcome of the last five years effort in all spheres, whether it's marketing, brand positioning, getting the pricing right, increasing the number of SKUs and bringing down our overall cost structure dramatically by increasing productivity at the manufacturing facility. So, we kept the market abreast of all the activities that were going on over the last five years and it took some time for each of them to translate into numbers. Now going forward, we don't see any changes to this overall strategy, the brand will continue to be strengthened, brand salience will perform, the brand promise to the ultimate consumer will perform and the manufacturing facilities will continue to work at high productivity, newer designs in faucetware, you know the black matt faucets have been introduced this year, the PVD faucets have been introduced, production is being increased from 3 lakhs to 4 lakhs eventually, the overall infrastructure is being created for further capacity expansion up to 6 lakhs pieces per month. So on all these fronts there are enough initiatives being undertaken. I don't see any macro or internal risks to our targets. And we as a Company, we have never been dependent on real estate demand, we are more B2C Company, which is more focused on home-improvement rather than just a developer demand. So even the interest-rate cycle, now you see we are let's say at the highest end of the interest-rate cycle and this is our best Q3 ever. So if interest-rate cyclical would have impacted the Company, you would have not seen this result. And you heard the question earlier that other home-improvement companies have been saying that the demand has not been conducive, we never found any of those reasons in this quarter.

**Aashish Uppanlawar**

But I mean what would be the difference because then it would mean that others are not finding ways to grow, if you are growing, it means that most of the growth

is market share gain driven or value addition driven, I mean that will be the right way to look at it probably?

**Ayush Bagla:** It's a mix of industry, it's a mix of industry growth and market share gains, yes, you are absolutely correct. And others might find them, others doing more commoditized businesses. So that is why, sanitaryware and faucetware which is 87%, 88% of our sales is very different from tiles industry. Sanitaryware industry has not seen too many entrants which have been sizable in nature. If you look at the history of the industry over last 20 years, there is hardly any new entrant which has been sizable in nature maybe one or two names.

**Aashish Uppanlawar:** I don't know whether you shared the growth, I mean business wise on the faucets and sanitaryware etcetera, if you could let me know what growth rate was for this quarter?

**Ayush Bagla:** Sanitaryware grew by 18.95, so 19% and faucetware by 12% Y-o-Y.

**Aashish Uppanlawar:** Any reason that faucetware has grown lesser because that's been the most prominent business for us?

**Ayush Bagla:** Yes, faucetware over the last 1.5 years has seen price rise of 27% and now brass prices have come off 9% to 10% in nine months now things will change again.

**Aashish Uppanlawar:** So volume wise the growth would be there, but value wise that would be, this 12% is not representative figure for the volumes?

**Ayush Bagla:** The growth is both volume and value and again because more than one third sales is from new products. The pace of new product introductions in faucetware is very high. So this Lustre series, the Lustre series has almost 496 SKUs, which were launched this year. Normally, we launch 10, 15 or 20 SKUs per quarter. This time out of 614 total SKUs launched, 496 were Lustre, the bulk of which are faucetware.

**Moderator:** Thank you. The next question is from the line of Sangameswar Iyer from Consilium Investment. Please go ahead.

**Sangameswar Iyer:** I just wanted to clarify, in your endeavour to bring down the inventory levels at the Company level to 80, 90 days, how much is the current channel inventory at the retailers end, can you help us understand so that would help us to gauge how the incremental primary sales would look like going forward?

**Ayush Bagla:** See, Cera is a very unique player in the industry for the following reason. More than 55%, 60% of sales are cash and carry. So, the retailer and dealer keep a minimal inventory at their end because they've already paid for it, they want to have very short working capital cycles. So the bulk of the inventory is only at the Cera end, at the retailer dealer end because of the distributed warehousing model strategy, sometimes the dealer can go to the same depo owned by Cera or warehouse owned by Cera twice a day to pick-up material. So, at the retailer and dealer level, you will find minimal inventory. So, it is really just-in-time has been implemented by Cera

for the dealers. Otherwise, we could not have this 55%, 60% cash and carry model, that is something that every Company wants to achieve, but never gets there.

**Sangameswar Iyer:** Secondly, sir, you also mentioned about from February 1<sup>st</sup> onwards, competition is embarking on price rationalization. How much would be the price differential now given the fact that in Q3 we did not take any price hikes, while they took. So even post rationalization, what would be the differential, just to get a sense?

**Ayush Bagla:** Between Cera and the peer group?

**Sangameswar Iyer:** Yes because in Q3 we did not take any price hike, while they did, so when in February when they are taking a rationalization journey, we need not do anything, but still post that what would be the kind of discount, what would be the kind of differential that we would be at compared to the larger peers?

**Ayush Bagla:** From 1<sup>st</sup> February, Cera took a price rationalization exercise.

**Sangameswar Iyer:** Oh, we took is it, okay, I thought the industry is taking, yeah.

**Ayush Bagla:** And the rationalization exercise was aimed more at not at price increase or decrease, but to have a single MRP across the country. The result of that exercise was sanitaryware prices increased by 0.5% to 1% across some markets and faucetware decreased by 0.5%, so it was a negligible increase or decrease for the Company. But I am saying in Q3, most of the companies took a price rise which Cera did not and that was also one reason why market share was gained. So maybe those companies had cost pressures, which Cera did not and cost pressures come from the manufacturing end. Some Company is dependent on Chinese imports for large part of their high-end SKUs in sanitaryware. For them it is inevitable to keep on taking price rises. Now I'll give you example. Freight costs from China have gone down to \$900 to \$1,000 per container. Even with that container cost, there is no money to be made in Chinese imports.

**Sangameswar Iyer:** Is this because of the duty structure, is it because of the sequential pricing that come...

**Ayush Bagla:** Even the current freight duty, the changes in the Chinese currency and the cost of procurement from China. If you add those four factors, nobody is making any meaningful margin in Chinese imports. So for the financial community to worry that what will happen when freight rates go down; they have already gone down to 900 to 1,000, but the Indian market has not seen any impact.

**Moderator:** Thank you. The next question is from the line of Akash Shah from UTI Asset Management, please go ahead.

**Akash Shah:** So firstly, I have two bookkeeping questions. What would be the capex for FY23 and FY24 and what would be the ad spend for FY23 and FY24?

- Ayush Bagla:** Capex for FY23 is Rs. 24 crore, of which only Rs. 3 crore has been spent so-far.
- Akash Shah:** And FY24?
- Ayush Bagla:** And FY24, of the existing capacity it's worked out, of the new brownfield capacity the overall capex is INR 69 crore and that will get completed in July 2023, well within time and well within cost. As far as the land for sanitaryware is concerned, the current budget is about INR 25 crore, so there would be a 5%, 10% plus or minus in that number.
- Akash Shah:** And just one thing, so land acquisition, you said, we will be sort of acquiring that land within next about three to six months, right?
- Ayush Bagla:** Land acquisition, plus all approvals from the State Government will take between six to nine months.
- Akash Shah:** Yeah and ad spend...
- Ayush Bagla:** I think your voice was muffled.
- Akash Shah:** Yes, I was saying ad spend number, please.
- Ayush Bagla:** Ad spend this year is INR 55 crore, last year it was much lower, I can give you that number. Ad spend last year was, just taking a minute to dig out that number.
- Akash Shah:** Hello?
- Ayush Bagla:** We can get back to you offline.
- Akash Shah:** No problem. So just one last thing. So on faucetware, I mean in faucetware segment, we took a price increase of about 5% in Q1FY23 and about 6% in Q3FY22 and revenue growth in faucetware segment was about 11%, 12% on a year-on-year basis in this quarter. So roughly, it implies that volume growth in faucetware segment was I mean low-single digit. So would you please help us understand the reasons behind that?
- Ayush Bagla:** We took the last 5% increase in May '22 and before that was 5.5% in November '21. So very little of that, some part of that price increase also came in Q3FY22, November 2021, right. So, it's not as if the entire price increase 5.5 plus 5 has emerged in Q3.
- Akash Shah:** Right, but if I look at on a year-on-year basis, the price increase would be somewhere around 10-odd percent, so that implies that volume growth was low single digits.
- Ayush Bagla:** 10-odd percent if you consider the November increase which had some impact on the base of Q3FY22. If you don't consider that it was only 5% of May '22. That's why

the 12% consist of both price and volume. And I finally got that number of total ad spends 2021-2022 was INR 32 crore and this year will be INR 55 crore.

**Akash Shah:** And just this one last thing. So, in faucetware segment, are we planning to take some price cut given the fact that brass prices have corrected by 9%, 10% in last nine months?

**Ayush Bagla:** Currently, we are not planning to change the pricing upward or downward, but we'll wait for this quarter to pan-out and then decide.

**Moderator:** The next question is from the line of Deepak Lalwani from Unifi Capital. Please go ahead.

**Deepak Lalwani:** Firstly, can you please indicate the rough volume growth in our sanitaryware and faucetware segment, roughly how much would be the volume growth in this quarter? And can you please share the number for the tile revenues and the other segment?

**Ayush Bagla:** Yeah, those who know this Company well, they know that the number of SKUs are expanding at a very fast pace and looking at volume will not give a correct picture of what the Company has achieved, because the number of SKUs that are being launched are in most cases at higher price points. Manufacturing those SKUs take-up a larger share of labor input, gas input and overall manufacturing efficiency. So value is the only way because you know I'll give you first SKU introduction and total number of SKUs that will give you some colour.

So new launches in FY23 in sanitaryware was 72 products, in faucetware 573 products, a total of 673. So that's why, you know, unlike a typical Company which makes one product and therefore volume growth is easily indication of how the company is performing in this case is very different. Tiles, I'll give you the number one second, the tile number is increase of 34%. So last year it was INR 40 crore, this year is INR 53.71 crore topline. And the tile strategy is simple, tiles, I'll just give you what the Company has executed. The Company doesn't have any manufacturing capacity because they didn't want to deploy it's capital in a completely commoditized business. And now with a significant overcapacity in the tiles industry, it has access to low-cost product and available product of all designs. So in Q3, the vendors prices were stable and substantially declining also due to decline in gas costs at Morbi. So, neither did the Company have to take a price hike nor did any vendor ask for a price hike. And our overall strategy is to be a niche player in tiles, a boutique player not to compete with large tile companies in the commoditized titles, but to concentrate on GVT tiles, triple fired slabs and double charged and also wall tiles. So, our share of the commoditized soluble salt etcetera is only 6% of our tiles business.

**Deepak Lalwani:** And, sir, if you could communicate the revenue part you already said that doubling in 40 months is possible, but the margin expansion of 50 bps to 75 bps every year, if you could indicate what would be the drivers in this journey?

- Ayush Bagla:** Increase in productivity at the plant, product mix moving upward at the plant-level, slight changes in MRP every year and spreading on the fixed cost over a larger base, so these would be primarily the four factors. And overall, the Company has moved to a 80:20 mix, so 80% of all costs are variable in nature and less than 20% of costs are fixed in nature that 80% will keep on increasing and 20% will keep on reducing.
- Deepak Lalwani:** And sir any impairment do you access for the Milo agreement we had, with Milo...
- Ayush Bagla:** Yes, I'll give you the update. Milo again, we had taken a decision in 2015 never to have manufacturing capacity of tiles on our books. We invested INR 8 crore for a 26% share of equity in Milo and we were also their customer. So their governance standards and other standards were not according to Cera's liking and we served them a legal notice. All efforts are on for a resolution and to get our INR 8 crore invested back, in any case their plant is non-operational, so we have switched to other vendors to feed tiles requirement. So our entire risk in all the worst-case scenario is limited to our equity exposure.
- Moderator:** The next question is from the line of Hrishikesh Bhagat from Kotak Mutual Fund.
- Hrishikesh Bhagat:** I just wanted to check; you mentioned 24 months will be the timeline. So just it is fair to assume that the revenue from the new plant will largely flow, so 24 months is largely I guess is probably March 2025 assuming even if we start to work from March '23 or so and everything. So fair to assume that large part of this revenue will start flowing in 2026 from the new plant?
- Ayush Bagla:** Yes, but currently given what is happening in the Company, there is full access to availability. And our optimum level of inventory level has been reached, so we feel that till whatever March '25 or FY26, there is no need for this new capacity because capacity is being freed up in our current manufacturing facility. You saw what happened in faucetware, 1.5 lakhs of monthly production has already become 3 lakhs, 3 lakhs is now becoming 4 lakh, there is provision to go up to 6 lakhs. Similarly in sanitaryware, the productivity is increased and the product mix has increased dramatically. Otherwise, the Company would not have been able to reduce its imports from China. And we are probably the only Company to give out China import numbers. I have not seen any other Company in the peer group discuss their China import numbers.
- Moderator:** The next question is from the line of Mihir Damania from Ambit Asset Management.
- Mihir Damania:** So I have only one question. So, what is the Company's stance on utilizing cash in the books, so your cash equivalents of around INR 600 crore and considering your capex requirements for expansion should not exceed INR 200 crore. And as you already mentioned that they are going to be majorly funded by internal accruals. And there are also no plans to enter any newer segment, so do you not believe that excess cash in the books will be counter (inaudible) to ROE, ROCE metrics which set is hard to and what's the plan for the INR 600 crore of cash and cash equivalent in the books?

**Ayush Bagla:** See in March '19, we had INR 83 crore in the books of Cera, so only INR 83 crore were cash and the cash equivalents, now it's INR 600 crore. And not only is our two capex programs underway, last year the dividend to shareholders was increased dramatically from a normal 17%, 18% of PAT to it is the stated dividend policy on our website. We had a special dividend, so a total payout, INR 20 crore was INR 46 crore last year. So going forward, depending on how the Board deliberates on this topic, we could see more payouts. But other than that there is no other topic under discussion of any buyback or any other distribution. And as far as acquisitions or inorganic, growth is concerned, the Company is always willing to evaluate any capacity in sanitaryware as long as the capacity comes up with a facility which is similar to Cera's quality standards. If you look at other companies, our peer group, their diversifications have not resulted in ROCE accretion to the shareholders. They have been wealth destroyers.

**Mihir Damania:** So would it be fair to assume that post this we might see a revision in the dividend distribution policy?

**Ayush Bagla:** That is for the Board to decide after the annual results.

**Moderator:** Thank you. The next question is from the line of Alisha Mahawla from Envision Capital. Please go ahead.

**Alisha Mahawla:** Thank you for the opportunity. Just wanted to know for nine months FY23, what is the price hike we've taken in sanitaryware and faucets?

**Ayush Bagla:** I'll give you the numbers, the last price hike was 3% in May '22 and 5% in faucetware, 3% in sanitaryware in May '22, 5% in faucetware in May '22. Before that, the price hike was only in November '21. So in FY23, there was only one price hike.

**Alisha Mahawla:** And I missed the (inaudible) to an earlier participant in light of some softness in commodity prices and raw-material inflation also softening. As an industry, any signs that maybe some of this price hikes will be probably be rolled back?

**Ayush Bagla:** See, we cannot speak for other players, they have just taken a price hike in October, etcetera. So the softening of raw material that trend was visible throughout the year and definitely even more pronounced in Q3 despite that they took a price increase maybe there were other cost pressures like wages or any other input costs for them. For Cera, those factors didn't play out because wages didn't play out because our productivity increased, far exceeded inflation in wages. And RM, which is the other part of COGS decreased, gas price decreased.

**Alisha Mahawla:** My next question is, in sanitaryware the capacity, the greenfield will come by FY25 until then, the share of outsourcing will probably inch up a little bit like it has happened from 60% to 63% and probably a couple of points more. How will this impact our margins in the near-term?



- Ayush Bagla:** See margins are increasing because of plant productivity, the kind of product mix that is changing at the plant level and fixed costs spread over a larger base. So these are the three reasons and then the fourth reason is of course any change in MRP of the product.
- Alisha Mahawla:** A lot of these levers already well-executed or is there scope for more to ensure that it can negate the increase in outsourcing?
- Ayush Bagla:** See outsourcing, again you have to further go into granular data. Outsourcing of products which the factory will make at a higher-cost and low-end easy to make the vendors have adequate capacity and technology to make, only those products are outsourced. That dramatically increases profitability. And freeing up capacity at the own manufacturing level to make complicated products which vendors cannot make, that provides us an edge in terms of design differentiation in the market. So, it is not purely a financial decision, it is a mix of financial and innovation in terms of design differentiation and functionality of product. So that as you mentioned, it is not fully played out. There is tremendous room for that to continuously change.
- Alisha Mahawla:** What would be the share of the basic products versus the value-added products currently in our mix?
- Ayush Bagla:** I will give you that number, overall for the Company, in Q3, entry products were 27% of sales, mid products were 28% of sales and premium products were 45% of sales. And I can give you a further break-up in sanitaryware and faucetware. Sanitaryware entry-level products were 27% of sales, mid products 15%, premium products 58%. In faucetware, entry products were 28%, mid products 47% and premium products 25% of sales.
- Alisha Mahawla:** And overall, the consol number of 45% premium products, is there scope for this...
- Ayush Bagla:** Overall, the number is 45 for premium products yes, for the Company.
- Moderator:** The next question is from the line of Sanjaya Satapathy from Ampersand Capital. Please go ahead.
- Sanjaya Satapathy:** I have two questions, the first one, sir, you explained that, despite sharp reduction in freight rate from China, it is still not profitable to import and sell in India. Will that change through because of reopening of China now?
- Ayush Bagla:** As far as, the vendors are concerned, they have been open for quite some time and all the factors that the financial community was worried that China will flood the Indian market post COVID etcetera, those have not happened because it is not profitable to do that. No Chinese companies has tried to promote a brand in India, they were quite happy to remain as vendor to large Indian brands. Indian brands are discovering that without own capacity, sanitaryware is a very difficult industry to crack and importing from China, paying whatever dealing with the volatility of the Chinese currency, then the freight, then 11% import duty, all of that takes not

only too much time, but doesn't work out at the EBITDA level. So, for Cera again, this is not a decision that is a knee jerk reaction from five years we have been continuously sharing with the financial community that Chinese imports need to go down and we have bought it down to about less than 3.5% of sales.

**Sanjaya Satapathy:** And sir my last question is that, that I believe you have told TV channels that you will double your revenue from your fiscal '23 level in next three years. So can you just tell us like how will it be achieved and will it be through some new segment entry or something else and what would be your sustainable profit margin that you are looking at because on a quarter-to-quarter basis I have seen it been volatile from 12%, 15% to 19%. So what really is the sustainable margin?

**Ayush Bagla:** See, this number that you're saying even without other income 15.99% or 16%. That is all-time high number for Q3. Last year was 15.79%, so every quarter you are seeing higher-margin numbers and even gross margins which were always in that 48, 49 category are now 54 levels which were never the case. So margin expansion is taking place and even you'll see that in, I am not talking about any particular quarter, but on a full FY23 basis or FY24 basis and my comment to the TV channel was doubling of topline from 1,440 to 2,900 over 40 months, so 3.5 years. And we stand-by that number and this trajectory is higher than that.

**Sanjaya Satapathy:** Yeah, I agree, but will it be through same products, or you are entering some new segment, new categories?

**Ayush Bagla:** Currently it is same products. Currently, there are no plans there has been no discussion at the Board level to enter new categories. So, it will be with the three businesses that we currently have and out of which 87%, 88% is sanitaryware and faucetware.

**Sanjaya Satapathy:** So, what I'm trying to sir takeaway from here is that one is, that you are fairly confident of reaching that 2,900 crore and improve your margin consistently through productivity enhancement and product mix improvement, is that correct, sir?

**Ayush Bagla:** That's right and participate in the growth of the market and also move upward in-product mix and pricing.

**Moderator:** The next question is from the line of Akhil Parekh from Centrum Broking. Please go ahead.

**Akhil Parekh:** I just have one question. I probably would have missed from the last concall, could you please share more details of our retail loyalty program, the mechanism of it and what is the endeavour or the end goal of executing this program?

**Ayush Bagla:** This is a very simple program executed by Cera for the first time in the industry. All retailers have been asked to download a app, within the app, as and when they transact with their dealer, they simply upload the invoice to the Company, the

Company calculates their rewards based on volume and the complicated SKUs etcetera, they analyse the retailers on many parameters and declare rewards, which the Company distributes directly to a retailer. So that's why you're seeing 1.1 lakh invoices have already been uploaded, 13,500 retailers have already participated, and dealers are not feeling threatened by this program because the Company is paying their retailers something and their stickiness between the retailers and dealers are increasing. So this gives access of a lot of granular data to the Company, geographical SKU demand, relationship and pricing between a dealer, a retailer, their discount mechanisms, all of that, which the industry had no access to. As far as multi-brand retailers are concerned, this is one more edge that the Company has, they'll be encouraged to sell Cera products first.

**Akhil Parekh:** And this also helps keep the inventory levels lean across the channels, basically because since you have access to the data, you know which are the fast-moving SKUs and which are slow moving SKUs and accordingly try to sell those products to the distributors as retailers basically.

**Ayush Bagla:** That is very obvious aspect, but more than that since almost 40% of sales are from new products, it gives new product development a completely new direction on where to focus and where future revenues can be derived from.

**Moderator:** Thank you. Ladies and gentlemen, this was the last question for today. I would now like to hand the conference over to the management for closing comments.

**Ayush Bagla:** Thank you. I would like to thank everyone for attending this call and for showing interest in Cera Sanitaryware Limited. Cera remains positive that it's strong positioning in the industry and improving macros would help it to deliver steady and consistent growth going forward. Should you need any clarification or further information or would like to know more about the Company, please feel free to reach out to me or CDR India. Thank you once again for taking time to join the call and see you all next quarter. Thank you very much.

**Moderator:** Thank you. On behalf of Cera Sanitaryware Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.

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