



# Cera Sanitaryware Limited

## Q4 FY23 Earnings Conference Call Transcript

May 11, 2023

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**Moderator:** Ladies and gentlemen, good day, and welcome to Q4 FY23 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 this 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, sir.

**Mayank Vaswani:** Thank you, Nirav. Good morning, everyone, and thank you for joining us on the earnings call for CERA Sanitaryware Limited to cover the Q4 and FY23 earnings, which were announced yesterday.

We have with us on the call today, the management team comprising: Mr. Ayush Bagla, Executive Director; and Mr. Vikas Kothari, CFO of CERA Sanitaryware.

We will start with brief opening remarks from the management, following which we will open the floor for Q&A. A quick disclaimer before we begin, some of the statements made in today's 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 would now like to 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> March, 2023, were adopted by the Board of Directors yesterday, 10 May, 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. CERA's product and design emphasis allowed it to focus on the B2C segment where it can truly exhibit pricing power. Over the last few years, all efforts have borne fruit to decouple CERA's revenue growth from fluctuations in interest rates and housing demand, thereby insulating it from cyclicalities.

We have reported strong topline growth. Financial year '23 revenues are higher by 24.6% on a Y-o-Y basis, and CERA's revenue growth has been 3x of the industry growth rate. More importantly, our focus on enhancing the quality of revenues is

reaping dividends. The topline increase is driven by a higher share of premium and high-margin products. Share of premium products in the incremental turnover is higher than the blended topline. This has aided in further expansion of margins.

The gross margin increased from 52.77% in FY22 to 54.25% in FY23, and the EBITDA margin has increased from 16.66% in FY22 to 17.59% in FY23. Our stated objective was to increase our annual EBITDA margin by 50 to 75 basis points each year. We have surpassed our stated objective as the increase in EBITDA margin in financial year '23 has been almost 100 basis points, despite advertising spend in the year increasing from INR 32 crore in FY22 to INR 57 crore in FY23.

The industry has traditionally followed an orientation of price increase as a regular response to overcome cost pressures. At CERA, we have responded differently, with the objective to deploy multiple levers to protect and enhance our margins. These include productivity and yield increases in the manufacturing processes, cost optimizations, product mix enhancement through higher share of new and higher value-added products, thereby limiting our reliance on price increases. As a result, we are well placed to capitalize on market share gains made over the last 2 years. At present, our manufacturing facility continues to function at high utilization levels. During the quarter, the sanitaryware plant capacity utilization was 115%.

In faucetware, the capacity utilization was at 118% during Q4 FY23. The faucetware expansion program to take capacity to 4 lakh pieces per month commenced from July 2022. The enhanced production is scheduled to go onstream in July 2023 and in a staggered manner, we'll increase monthly production to 4 lakh pieces per month by March 2024. We expect to complete the project in time and well within the cost of INR 69 crore. The product mix planned is coloured SKUs, water turn SKUs, PVD SKUs and a few more SKUs that can be taken in from outsourcing partners.

During FY22, China imports was INR 69 crore or 5% of sales. In FY23, China imports were INR 55 crore or 3% 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 imports to sales has been continuously declining. In a business which is brand-driven, the fulcrum of success is manufacturing quality and plant efficiency.

With regard to capacity expansion for manufacturing of sanitaryware, a fully aggregated land parcel in Gujarat, historically owned by a single owner has been shortlisted and the Company is currently undertaking due diligence. We expect title documents to be executed and other approvals over the next six months.

During Q4FY23, 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, which were all a demonstration of pricing power. Currently, we are capitalizing on the market share gains over the last

two years. In sanitaryware, the raw material like China clay, feldspar, POP and the glazing recipe did not have a material price movement. Zinc went down by 13%. In Faucetware, brass prices increased by 5% in Q4 and 10% during financial year '23. Despite changes in input costs, our increasing plant efficiency ensured stable gross margins in Q4 FY23 of 53.26% and in Q4 FY22 of 53.47%.

For the twelve months, gross margin has increased from 52.77% to 54.25% with no increase in product prices. 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 remained almost stable at around INR 35 per cubic meter in December 2022 and in March 2023, it was INR 36 per cubic meter. Normally, GAIL supplies 50% of CERA's gas needs. However, in Q4 FY23, GAIL provided 65% of the gas requirement of the sanitaryware business.

Sabarmati Gases pricing went down from INR 67 per cubic meter in December '22 to INR 58 per cubic meter in March '23, supplying 35% of the gas needs of the plant for Q4. Post April '23, a price reduction has been carried out by GAIL from INR 36 to INR 31 per cubic meter, and by Sabarmati from INR 58 to INR 41 per cubic meter. The Q4 weighted average cost of gas is INR 43, much lower than the industry. Gas costs constitute 2.68% of CERA's topline. The retailer loyalty program that was launched by CERA in Q1 FY23, which has now almost completed twelve months.

More than 14,000 retailers have uploaded 1.46 lakh invoices. The feedback we received from retailers has helped us in understanding the consumers' changing demands, geographical segmentation of SKUs, and evolution of the rewards program to retailers. Besides standardizing invoices, of the total retail sales of INR 1,042 crore in FY23, more than INR 339 crore of sales, which is 33% of overall 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 and ability to steer the direction of the dealer and retailer equation, have all undergone a sea change. We have also seen an improvement in multi-brand retailers who have undertaken various initiatives to sell CERA products.

After the success of the retailer loyalty program, a similar program was launched for plumbers across India. CERA had been conducting training workshops for many years now, imparting installation and product knowledge to plumbers. A new program where rewards are provided to plumbers who recommend and facilitate the sale of CERA products is now active from 1<sup>st</sup> May 2023. The program communications include program posters at retailers, and a mix of communication channels, which includes SMS, phone calls, creatives and in-person meetings by the sales and marketing team.

In Q4 FY22, 104 new products were introduced. New products launched in the past 3 years constitute 34% of CERA's topline in Q4. Our highest ever advertising spends were achieved in financial year '23 of INR 57 crore. CERA's share of voice was lower than its share of market, and now its increase in advertising spends, its share of

voice is getting closer to its share of market. Publicity spends, which was INR 7 crore in Q4 FY22 were increased to INR 24 crore in Q4 FY23. Despite a 340% increase in quarterly advertising and publicity expenses, there was no major impact on EBITDA and PAT margins.

Population centers of 17 lakhs and above which are Tier 1 cities have 31% of sales; population centers of 3 lakhs to 17 lakhs, which are Tier 2 cities have 22% of sales; and population centers below 3 lakhs of population are Tier 3 cities with 47% of sales.

We can now go over the financials. Revenues from operations in Q4FY23 was INR 530 crore versus INR 439 crore in Q4FY22, an increase of 21%. EBITDA, excluding other income was INR 85 crore in Q4FY23 versus INR 82 crore in Q4FY22, an increase of 3%. The gross margin has remained almost stable; it is currently at 53.26% in Q4FY23 against 53.47% in Q4FY22. PAT was at INR 63 crore in Q4FY23 versus INR 52 crore in Q4FY22, an increase of 21% Y-o-Y. EPS for Q4FY23 was 48.39% versus 40.04% in Q4FY22. For Q4 FY23, 53% of the topline was from sanitaryware; 35% from faucetware; tiles represented 11%; and wellness 1%. On a Y-o-Y basis, sanitaryware revenues registered an increase of 18%; faucetware revenues increased by 29%; tiles increased by 14%; and wellness increased by 15%.

The sanitaryware and faucetware verticals remain the backdrop of the business with the contribution of 88% to CERA's overall revenues. The classification of overall sales in Q4FY23 was 43% in the premium category; 31% in the mid category; and 26% in the entry category. Inventory days in Q4FY23 was 77 days compared to 73 days in Q4FY22. Receivable days in Q4 FY23 were 32 days versus 35 days. Payable days in Q4FY23 were 40 days against 49 days in Q4 of FY22. Therefore, net working capital days in Q4FY23 was 69 days versus 59 days in Q4 of FY22. This number is around the optimum number of inventory days that CERA has been making efforts to achieve for many quarters now.

In this quarter, availability of products ensured there was no element of lost sales. This is the eighth 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 expansion program is at INR 25 crore, of which INR 20 crore was spent in the last 12 months and INR 17 crore was spent in Q4. As on 31<sup>st</sup> March 2023, our cash and cash equivalents stood at INR 687 crore against INR 580 crore in March 2022, an increase of INR 107 crore or 18%. Positive cash flow for Q4 FY23 has been INR 62 crore as compared to INR 54 crore Y-o-Y. Positive cash flow for FY23 has been INR 219 crore versus INR 164 crore in FY22, an increase of 34%.

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

capacity expansions. The Board of Directors yesterday has recommended a dividend of INR 50 per share, which is 1,000% of the face value per share.

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 the macros of home improvement, CERA would be able to monetize all the growth drivers that present themselves. CERA growth plan remains intact as it plans to expand capacities and 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. In FY23, CERA has reached a topline of INR 1,796 crore, a growth of 24.5% over FY22, and a growth of 49.4% over FY21. This trajectory is 3x the industry growth. It increases CERA's market share and pricing power. Achieving the magic number of INR 1,796 crore has reaffirmed our confidence of achieving the targeted doubling of turnover within 40 months from March '22.

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

- Moderator:** The first question is from the line of Praveen Sahay from Prabhudas Lilladher.
- Praveen Sahay:** The first question is on the in-house and outsourcing contribution in the sanitary and the faucet segment. How much is that for the quarter?
- Ayush Bagla:** So for the quarter, in sanitaryware, outsourcing was 60% of overall sales and in-house manufacturing was 40%. In faucetware, the outsourcing was 49% and in-house was 51%. For the year, in sanitaryware outsourcing was 59% and in-house was 41%. And for the year, in faucetware outsourcing was 52% and in-house was 48%.
- Praveen Sahay:** Okay. The next question is related to the mid-segment contribution as well as your faucet contribution also on the increase in the last 6 quarters, I am continuously seeing. So is it fair to assume your faucet segment is largely in the mid-segment of product segment? And if you also give some indication on the margin differential in the sanitary and faucet?
- Ayush Bagla:** So Praveen, the thing is I'll just give you some statistics to add more color to the answer. In sanitaryware, our composition of sales is entry level, 25%; mid is 17%; and premium is 57%. In faucetware, entry is 26%; mid is 48%; and premium is 24%. But that's not the reason why you're seeing faucetware growing. The unorganized to organized shift in sanitaryware has more or less played out, whereas in faucetware where it is nowhere near played out. And the unorganized market in faucetware continues to be INR 5,000 crore. That market is fully available over the next many years. And the second aspect is CERA, let's say it's faucetware market share is double digit. It is the second largest player in the industry, but it's incremental market share. So the share of the growth that CERA is monetizing is 1.5x to 2x its incremental market share.
- Praveen Sahay:** Okay. So any margin differential between these two products?

**Ayush Bagla:** See normally, we don't split the margins between our various businesses. We just focus on the blended number. And the reason for that is we don't want to give out our pricing and margin strategy to the market.

**Praveen Sahay:** Right. Okay. And sir, the question on the growth way forward, because this year, you had delivered a very high growth in both the segments, around 27%-28% and overall addition of incremental sales in the range of around INR 350-odd crore. What's your guidance for '24-'25?

**Ayush Bagla:** See again, I'd like to focus on the overall larger picture that we had painted in March and April '22 of reaching a run rate of INR 2,900 crore by September '25. That required a CAGR of 17%, 18%. We have achieved much more than that. So now most of the investors and people in the financial community are calling us and telling us that, that aim of INR 2,900 crore by September '25 is a very conservative target. So, if you just work backwards from that number, we'll need to add about INR 350-odd crore of topline every year, which we have delivered this year. And going forward, that will be the trajectory.

**Praveen Sahay:** Great, sir. And the last question, sir, related to your advertisement budget. So this year, definitely, there is a good jump in that. So is there any one-off because you had a new brand ambassadors as well or that will continue on the yearly basis the way forward?

**Ayush Bagla:** Normally, the spend were 3.5% to 4% of topline. In the manner in which topline is increasing, that number will remain between 4% and 4.5% of topline. But the absolute number will increase in relation to the topline. And the benefits of this expense in Q4 and during FY23 is both in the short-term and in the medium-term. So, we are seeing a difference in pricing power and premiumization of our products.

**Praveen Sahay:** Okay. Great. And all the best.

**Moderator:** The next question is from the line of Vijay Kedia from Kedia Securities.

**Vijay Kedia:** Ayush ji, this is Vijay Kedia. Congratulations for this wonderful numbers. This has really surprised us, at least me. And I just want to understand one thing from you. One thing I would like to tell you that ever since you have joined the Company, the shape and size of the Company has really changed dramatically. And in various occasions, whenever I met your competitors, I was told that you have taken some really out of the box decisions in the last 2 years and your competitors and me both were skeptical whether they are going to bring positive results for the Company or not. But actually you have proved us wrong. And I hope in the future also you will prove us wrong.

So, whatever you have done differently than others, I just have one simple question. Maybe the deficiency of your competitors has also played an important role, if not a significant role, but a little bit of a role in your numbers or in your growth. So, I just want to understand from you that, of course, all of them are very strong,

capable and compatible. So, what would happen is they will also strike back, which I am sure because most of the problems like gas and all are behind us. So, they will also start recovering. So where would you stand out in that circumstance?

**Ayush Bagla:**

Thank you, Mr. Kedia for taking time to attend the call and also participating. You see this is an entirely a team effort by CERA. And right from the shop floor to absorbing new technologies, increasing new products. So I'll just give some background; new products in the industry are 10%-12% of sales for the industry as a whole and for CERA, they were 22%-24% of sales. Now they are 34% to 39%, depending on which quarter you look at. These are all new sales which were not previously available but are incremental sales at much higher margins. So, all around the CERA team has delivered, and it's a testimony to their execution skills.

So as far as competitive intensity is concerned, the competitive intensity, whether from the large Indian players or MNC players or large building material companies was always there. And we expect it to keep on getting fiercer. But we have both the bandwidth in terms of products, manufacturing capability, technological expertise to meet that challenge. And not only is the consumer evaluating us at every step, but even retailers, dealers, we get a lot of feedback from them, we execute accordingly, so those are some of the levers. And there were a few concerns about the Company 5, 6 years ago, but the governance level in the Company would be at par with the best companies of Corporate India, the really blue-chip companies. So those are things that I think the investors have really appreciated. And the Company's debt-free high-cash, decisions have all been ROCE accretive over the last many years. Those are the things which have made the Company perform in the way it has over the last few years. So other than that, I can only say that going forward, we want to maintain the same growth trajectory, both in topline and bottom line, as well as offerings to the consumer. So ultimately, the validation by the consumer results in all the financial metrics being met.

**Vijay Kedia:**

Yes. Okay. There is a last one point only, INR 687 crore line in the safe instrument, when are you going to utilize that fund in some lower risk and high return kind of investment?

**Ayush Bagla:**

So, we are currently just working on our brownfield expansion in faucetware and the greenfield expansion in sanitaryware, Other than that, there is no current capex that is lined up. If there's a good opportunity inorganic, the Company will definitely evaluate it. But other than that, this Company has been very conservative and that's one of the reasons for its success.

**Moderator:**

The next question is from the line of Akshay Chheda from Canara Robeco Mutual Fund.

**Akshay Chheda:**

Just one question. If we see the gross margin, so in Q2, it was a good number of around 55%, 55.5%. But then if you see the last two quarters, it has cooled off to around 53.3%. So, what is it that is, is it the raw material, which is hurting us, how

should we see it because on one side if we see, raw materials benign and even if we are improving the product mix. So then, how should we look at the gross margins going forward?

**Ayush Bagla:** If you were able to cherry pick 1 number from 1 quarter, then I could also give you the baseline of gross margin, which has always been between 48% and 50% of the last many years, we are 300 basis above that currently, both for the quarter and also for the year, we have 400 basis above that. So Company is operating at a much higher level in manufacturing efficiencies. And the baseline number of 48% to 50% has been surpassed. In one particular quarter, if it becomes 55%, that is not really, I wouldn't recommend that, that is the new benchmark.

**Akshay Chheda:** Okay, sir. And how should we look at it going forward?

**Ayush Bagla:** I think anything above 52% would be a very acceptable number. And that is a number that is optimal because that takes into account the high-capacity utilizations, spreading the fixed cost over a large number of products, management of both raw materials and all other costs associated with manufacturing.

**Moderator:** And the next question is from the line of Mihir Damania from Ambit Asset Management.

**Mihir Damania:** I have one question. It was, so we've seen other building material companies catering to a wider basket of products, including one of your closest competitors who has kind of ventured into the lighting front. So, since we have like a huge pile of cash of around INR 700 crore, are we looking to maybe look at hedges and these? Are you open to looking at it and can we see something on that front in the next couple of years or so?

**Ayush Bagla:** See, currently there are no plans or no proposal in front of the Board to diversify and especially diversification into unrelated areas, you know lighting and electrical goods or even whitegoods are all unrelated businesses. They are like a decision to be taken independent of the current business. And many of these sectors, I'm not talking about any particular Company or business, but are very crowded marketplaces, where margins are much lower than what we are used to in our current businesses. So, till any business achieves a certain ROCE threshold, even on paper, we don't want to even evaluate such an opportunity. So currently there is no such evaluation going on, but let's see if we keep on expanding our current two main businesses, first through a brownfield and a greenfield venture, and maybe there is some inorganic opportunities in those businesses as well.

**Moderator:** The next question is from the line of Pranav from Equirus Securities.

**Pranav Mehta:** Congratulations on a very good set of numbers. Sir, I wanted to understand on the incremental dealer and distributor addition that you have done in FY23 versus let's say 3 or 4 years before, so can you just share how the dealer and distributor addition has been a focus area for the Company?



**Ayush Bagla:** So I'll give you some numbers. The dealers in March '22 were 4,260 which in March '23 had become 5,462. And the retailers were around 11,300, which are now around 14,600. But at the same time, the size of large dealers have grown. So large dealers are anything between INR 20 crore to INR 40 crore in topline. That is the revelation of the last 2, 3 years. Being a dealer in sanitaryware is a very profitable business, allowing them cash flow to expand geographically, more salespeople increase opex and capex at their end, at the retail end and the dealer end. Some of our dealers have large warehouses, large inventory of their own. So what we are seeing is the large dealers will continue to expand and that is going to be our focus. So making sure a INR 5 crore dealer becomes a INR 15 crore dealer I think over the next 2, 3 years that is going to be the focus.

**Pranav Mehta:** Okay, sir. And sir, can we say that Tier 2 and 3 cities are seeing better growth for you versus, let's say, 3 or 4 years before?

**Ayush Bagla:** There are all different markets for different products and Tier 3 cities maybe 10, 15 years ago was a market for inexpensive products or affordable products, not anymore. So Tier 2 and Tier 3 towns are now consumers of also luxury products. So for us, we are not really that bothered about where our sales go, but I would tell you something that dealers in Tier 2 and 3 towns have a larger footprint. They have better relationships with plumbers, civil contractors, architects, and other influencers. So their ability to sway a customer in those towns is much higher than in a Tier 1 town. And in Tier 1 towns, MNCs are fully focused on Tier 1 markets. So our focus is across all 3 markets. As you can see, even our share of sales in Tier 1 markets is increasing.

**Pranav Mehta:** Right, sir. And sir, any guidance on EBITDA margins for next 2 years that is FY24 and FY25?

**Ayush Bagla:** See, we had predicted 50 to 75 basis over 1 year, and we are already at 103 basis for the year. So I think I would say we have achieved what was to be achieved in 2 years in 1 year. Even maintaining this INR 17.96 billion number would be a great number to have with other income and INR 15.88 billion without other income would be a great number to have for FY24.

**Moderator:** The next question is from the line of Dhananjai from ASK Investments.

**Dhananjai Bagrodia:** Just wanted to ask you, sir, what would be your market share in both faucetware and sanitary and our market position also?

**Ayush Bagla:** You see, Dhananjai, for us to give out any number which is anecdotal would not be correct because we don't have any third-party agency like a Technopak or someone making out a report on relative market share. So, we are the largest player in sanitaryware without doubt, and the second largest player in faucetware and growing much faster than all the players behind us in faucetware. So incremental

market share, which is a more relevant statistic, the highest is CERA's case in faucetware. And in sanitaryware, we are just guarding our #1 position.

**Dhananjai Bagrodia:** And just to have an idea, how far would the number 2, if you have to ballpark only, any idea what would number 2 be in that sense?

**Ayush Bagla:** See, it's difficult for me to talk about any other Company.

**Dhananjai Bagrodia:** Okay. And the good growth we've seen in our numbers, would this be an industrywide phenomenon, or are we seeing some market share gains there?

**Ayush Bagla:** If you remember during our Q3 call, there were a lot of questions on volatility of demand during Diwali and post Diwali. And we had said that we did not see that kind of volatility in our offtake. The same thing happened in Q4. So different industry players have different dynamics and pricing decisions that they make. In our case, the focus on B2C segment and just focusing on the product rather than any other intangibles has made our numbers work, and we have really come out of the typical housing and interest rate cyclicalities.

**Dhananjai Bagrodia:** Sure. Okay. And I guess then thirdly, last question, just any possible breakup between how much of your revenues come from, let's say, metros or Tier 1 versus Tier 2, Tier 3?

**Ayush Bagla:** Yes. I will give you that number. Tier 1 is 31% of sales, Tier 2 is 22% of sales, and Tier 3 is 47% of sales.

**Dhananjai Bagrodia:** Okay. And this is on a combined basis, right?

**Ayush Bagla:** Yes. And exports are for the quarter 1% of sales, and for the year it's between 1 and 2% of sales.

**Moderator:** The next question is from the line of Udit Gajiwala from Yes Securities.

**Udit Gajiwala:** Just following up on the previous participant. Given that the market you mentioned that the other players have taken price hikes for last two quarters now, so there could be an element that since it is volume driven for us, there could be some element of market share gain. Is it a possibility?

**Ayush Bagla:** Other players took price rises in October, November '22, which we did not at that time. And our manufacturing efficiencies has beaten the effect of both inflation and RM changes and changes in labor and any other costs. So that we were happy to pass on those benefits to the consumer. And, of course, we also knew that will increase our market share. So that's exactly what we followed. The last price hike we had was May '22, only 12 months ago.

**Udit Gajiwala:** Understood. And sir, secondly, your margins, you mentioned that even if at these levels, you will be comfortable. But given that the RM pressure is coming down and with our premiumization basket going up, could we see that you're being

conservative maybe in terms of maintaining your margin guidance or we might see some 50, 70 basis points uptick, is it a possibility?

**Ayush Bagla:** Well, we had expected 50 to 75 basis points. We delivered 103 basis points. So that is something that we have delivered for 2 years in 1 year. We'll be happy with these margins if they're stable. And what you said the RM is cooling off, margins may increase if INR 350 crore, INR 400 crore of sales are added this year as well. So we'll wait for those things to play out before guiding.

**Udit Gajiwala:** Okay. And just last question, if I may squeeze in. Sanitaryware, given that now we are moving more towards the outsourced with the capacity. Do we see some squeezing of growth in sanitaryware or outsource may increase and that's why even margins could be at your...

**Ayush Bagla:** So outsource, you see, we work with, let's say, there are 50, 60 plants in the country. We work with only 10, 12 who meet our quality parameters. So currently within those 10, 12, there is no capacity constraint and even our in-house manufacturing, the strategy we have adopted is to make sure all complicated products are made in-house and products which were previously made in-house are sent to outsourcing partners, freeing up fresh capacity to take in newer products. So it's a mix and it's an evolving mix of which product to make in-house and which product to take outside. Currently, there is no capacity constraint both in the in-house capacity and from our outsourcing partner. And the proof of that is the inventory days. The sector always had a problem of inventory and availability, and we've had eight straight quarters of no element of lost sales. So, the inventory levels are at optimum level right now.

**Udit Gajiwala:** Got it. And lastly on capex, you said that '24 will be how much, excluding your brownfield maybe?

**Ayush Bagla:** So I'll just give you some numbers. For FY23-24, a total of INR 34.78 crore is planned, of which INR 11 crore will be sanitaryware automation, INR 4 crore faucetware automation, INR 7 crore customer touchpoints, INR 7 crore land and building at the current manufacturing facility, and INR 4 crore in logistics and IT. And I can also give you what was achieved last year. We had a budget last year outside of the INR 69 crore for the faucetware brownfield of INR 24.7 crore, of which INR 20.49 crore was spent. And they were spent in INR 6 crore for sanitaryware automation, INR 3 crore for faucetware automation, INR 4 crore on customer touchpoints, INR 2.5 on crore on land and building in our current facility, and INR 5 crore on logistics and IT.

**Moderator:** The next question is from the line of Shrenik from LIC Asset Management.

**Shrenik Bachhawat:** So basically, I wanted to understand that we are expecting 17% to 18% revenue CAGR for the next 3 years. So, I understand the real driver for our sales, but we are already 1 of the best Company in terms of distribution, as our distribution is quite

deep in Tier 2, Tier 3, Tier 4 cities. So, what will be the key driver for growth from here? Like what has structurally changed for the industry and for us?

**Ayush Bagla:** At Cera we don't need to do anything differently. We just have to execute in the same manner that we have been doing for the past 7, 8 years. So that includes enhancing product technology, maintaining the same product quality, and at the price that it's made available, and this distributed logistics, distributed inventory availability. So, we have to continue to do the same things we have done and not do anything differently. The demand from all three Tiers, 1, 2, and 3 towns is available. The replacement demand, home improvement demand is for real, and the industry is expanding, in faucetware the conversion from unorganized to organized is taking place, in sanitaryware the industry size was so small, that size is increasing dramatically.

**Shrenik Bachhawat:** Okay, got it. And sir, can you throw some light on how the other large private players in the likes of Kohler, Parryware, Jaquar have performed relative to us? And say, on that, secondly, as they are increasing the penetration in smaller cities, are we facing increased competition from these brands?

**Ayush Bagla:** See, the competitive intensity was never low in this industry, whether you talk about the 4 large companies in India or 7, 8 MNCs, the competitive intensity for dealers, for retailers, and for customers was always very high, but for me to talk about any other Company will be very difficult. But you'll find that CERA has been outperforming all other players in the industry on any of the metrics, whether it's product, technology, pricing, placement and, of course, all that translates into investor return and financial metrics. And most importantly, free cash flow, that is one of the most important focuses of this Vcompany.

**Shrenik Bachhawat:** Got it, sir. And sir, basically again on the cash questions. Currently our ROCE is around 26% with such high cash on books, right. So, going ahead, do you have any plans to better utilize the capital that is available on our books around INR 650 crore in investments which can improve our ROCE and ROE?

**Ayush Bagla:** Currently they are parked in safe instruments, and you rightly said ROCE is already high. If you take away the liquid cash from the capital employed, then that ROCE number will dramatically increase. So, one of the steps that have been taken is to increase the dividend payments. So over the last 2 years, our average dividend payment which used to be 17%, 18% of PAT, is now 31%, 32% of PAT and PAT has also more than doubled. The average PAT of the last 10 years was between INR 100 crore and INR 110 crore. This year it's INR 209 crore. So, both the absolute number and the dividend payout ratio all have dramatically changed. And having this availability of cash has provided us additional flexibility, so both the brownfield and greenfield capex, we have been able to do without the need to raise any resources or without the need to change any of our business practices to bring in more cash flow.

- Moderator:** The next question is from the line of Sonali Salgaonkar from Jefferies India.
- Sonali Salgaonkar:** Sir, my first question is related to the industry. I understand you cannot share your market share data, but can you please give us the updated numbers of the market size and organized proportion of sanitaryware, faucets and tiles, please?
- Ayush Bagla:** Again, Sonali, it will be anecdotal data, the data we collect from our sales force and various offices. So again, that is not something that will be correct to give to any outside community.
- Sonali Salgaonkar:** No problem, sir. Understand. Sir, my second question is about the tile industry in Morbi. Any update on the competition emerging over there? So, are exports on track or are you seeing a slowdown in the exports? And are you seeing them coming with a higher competition in the domestic market.
- Ayush Bagla:** Sonali, you have been a regular on our calls for many years. You know the commentary we've been making about tiles, that the tile industry is going through very difficult phase, and it will continue to remain that way because of significant overcapacity in the industry and none of the players having any pricing power, so that remains. And the exports have not grown in the same pace that they were growing for the last 4, 5 years. That has resulted in a significant glut in the domestic industry and price is not moving upward, even demand is more or less stagnant. So, the number of plants kept on mushrooming. There is no barriers to entry for SME entrepreneurs to put up a plant for a very small amount. And that's over fragmentation of the industry, which will take a few years to sort out.
- Sonali Salgaonkar:** Understand. Sir, and my last question is, could you enumerate what is the approximate average price hike that CERA has taken in FY23 across sanitaryware, faucets, and tile segments separately, please?
- Ayush Bagla:** So I'll give you some numbers. In FY23, there was only one price hike and that was in May 2022, 3% in sanitaryware and 5% in faucetware. And before that, the last price hike was in November '21. So, in calendar year '22, there was only one price hike, and in the financial year '23, there was only one price hike. There was a price rationalization exercise earlier this year, in calendar year '23, which resulted in a 50 basis point increase in price hike because we went for a uniform MRP across all products and all states, irrespective of the freight costs.
- Sonali Salgaonkar:** Understand. Sir, and none in tiles, right?
- Ayush Bagla:** Tiles there are just too many products. I'll just give you some information on tiles. Now the soluble salt commoditized tile is only 4% of sales for CERA. The rest 40% is GVT, 21% is double charged, wall tiles are 24%, and other paving and outdoor tiles are 12%. So, there is a little bit of pricing power in GVT and double charge and the commoditized version we have restricted ourselves to just 4% of our overall tile sales where we have ongoing commitments.

- Moderator:** The next question is from the line of Akash from UTI Mutual Fund.
- Akash Shah:** Ayush, many congratulations on great set of numbers. Just had a few questions. One is, how much has been the decline in brass prices and are we planning to cut MRP or let's say the realization of faucetware to ensure that, I mean to stay ahead of competition. Would competition be taking price cut in faucetware?
- Ayush Bagla:** See, brass, I'll give you the RM behaviour of brass and ZAMAK for the full year first. There was a 10% increase in brass prices for twelve months FY23, of which 5.12% increased in Q4. And ZAMAK, which is used to make handles of single lever, there was a 24% increase for twelve months, of which 7% increased in Q4. Despite that, we didn't have to take any price hikes since May. So, you can understand that we're passing on all the gains made in efficiency to the consumer and also absorbing any changes in RM increases. So that was as far as the FY23 is concerned. Even if these prices cool off, which they most likely will, there is no proposal or there is no past history or trend of decreasing prices or decreasing MRP.
- Akash Shah:** Sure. And usually if, let's say, raw material price is correct, then usually discount increase or we take price cut in MRP terms?
- Ayush Bagla:** Normally, the brands like CERA, which have pricing power, don't have to change any behaviour with changes in RM. So, we don't have to increase discounts or decrease MRP. Yes, sometimes there are combo offers, but that is in the regular course of business, not related to changes in raw materials. So, the whole point of spending the kind of money we do on advertising, publicity, creating a brand, creating the technology, and spending so much on technology and the shop floor is to make sure that our MRP doesn't move along with any kind of RM or any other cost or demand factors.
- Akash Shah:** Sure. Our EBITDA margin this quarter reduced by about 270 to 280 bps as compared to last year same quarter. One factor was increase in ad spends. But any other factors that led to this decrease in margins?
- Ayush Bagla:** See, if you look at EBITDA without other income it's INR 16.04 billion versus INR 18.78 billion and the ad spend increase of INR 17 crore for the quarter is if you add that to the EBITDA numbers, it increases it to more than last year's EBITDA margin. Other than that, there was no other change. All other costs were in line with revenues.
- Moderator:** The next question is from line of Onkar from Shree Investments.
- Onkar Ghugardare:** You mentioned this to several participants, just wanted to know what's management's thinking on, say, a buyback in this regard, since you have lots of cash. Just wanted to know management's thinking on this.
- Ayush Bagla:** See, we recognize that a buyback is a very tax efficient way of distributing cash to shareholders, and we are alive to those possibilities, but we've not taken any kind

of proposal to the Board on buyback. However, the Board is always keen to distribute more to shareholders and that's why you're seeing a INR 18 crore distribution becoming INR 65 crore, INR 66 crore this year, and last year it was about INR 46 crore. So that's one of the ways of distributing cash. Other than that, buyback is not really been evaluated at the Board level so far.

**Onkar Ghugardare:** Correct. But is the management open to buyback or like what's the thinking, just wanted to know.

**Ayush Bagla:** See, that is a decision that I think after all the capex, brownfield, greenfield of the Company's play out, that is another decision that can be evaluated seriously. But currently there is no such proposal.

**Onkar Ghugardare:** Okay, alright. Another question was on the land acquisition which we're supposed to do, I guess, in the next six months. So just wanted to know when can the greenfield project it will be commenced and what would be the addition to the existing thing and how much it can contribute to the overall, like how much sales it can add once it starts up, it becomes operational and working at 100% capacity?

**Ayush Bagla:** So, the plan is to complete the land acquisition and approvals within this calendar year, and most likely by October-November. That will cost around INR 25 crore. Another INR 100 crore will be spent on plant, machinery, and technology in the sanitaryware facility which will take let's say 18, 20 months, post all land acquisition and approvals. And the initial capacity, it will be modular. Initial capacity could be 12 lakh pieces per year and the topline will be close to INR 300 crore. So, asset turns for that will be between 2.25 and 3x. As far as the faucetware facility is concerned, we are almost seeing the end of that brownfield expansion. The cost is INR 69 crore, the addition is 1 lakh pieces per month or 12 lakh pieces per year to take the capacity to 48 lakh pieces a year. And asset turns, because it was brownfield and there was no land cost, etc., will be around 3.5x.

**Onkar Ghugardare:** So as far as the sanitaryware is concerned, it will take another 2.5 to 3 years to commence the facility, right?

**Ayush Bagla:** No, 18 to 20 months after the zero date. And the zero date will be set after the land acquisition is over and approvals are in place. So, we'll wait for the zero date to be set by the end of the year.

**Onkar Ghugardare:** Okay. And till then whatever you are comfortable with the outsourcing level and whatever the capacity utilization around 115% to 118%, you're comfortable with that to meet the...?

**Ayush Bagla:** That's right. And that will lead to increase in our inventory days.

**Onkar Ghugardare:** Okay. And this is fine with you guys to meet the existing demand as well as the future demand.



**Ayush Bagla:** That is correct.

**Moderator:** Thank you very much. I'll now hand the conference over to the management for closing comments.

**Ayush Bagla:** Thank you very much. I would like to thank everyone for attending this call and for showing interest in CERA Sanitaryware. CERA remains positive that its strong positioning in the industry and improving macros would help it deliver steady and consistent growth going forward. Should you need any further clarifications 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 the time to join the call and see you all next quarter. Thank you very much.

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

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