



UNEXPLORED MULTIBAGGER SMALL CAP STOCKS

EQUITY RESEARCH REPORT

CERA SANITARYWARE LTD.	BSE CODE: 532443 NSE CODE: CERA
Industry: Ceramics	CMP: Rs. 166.40 (24/12/2011)
Market Cap: 210.57 (Crores)	Target Price: Rs. 350
Date: December 24, 2011	Time Period: 12 – 18 months



Saral Gyan Capital Services
www.saralgyan.in
An Independent Equity Research Firm

TABLE OF CONTENT

S. No	Content	Page No.
1.	Company Background	03
2.	Recent Developments	07
3.	Financial Performance	09
4.	Charts & Graphs	11
5.	Peer Group Comparison	13
6.	Key Concerns	13
7.	Industry Overview	14
8.	Investment Rationale	17
9.	Saral Gyan Recommendation	18
10.	Disclaimer	19

1. Company Background



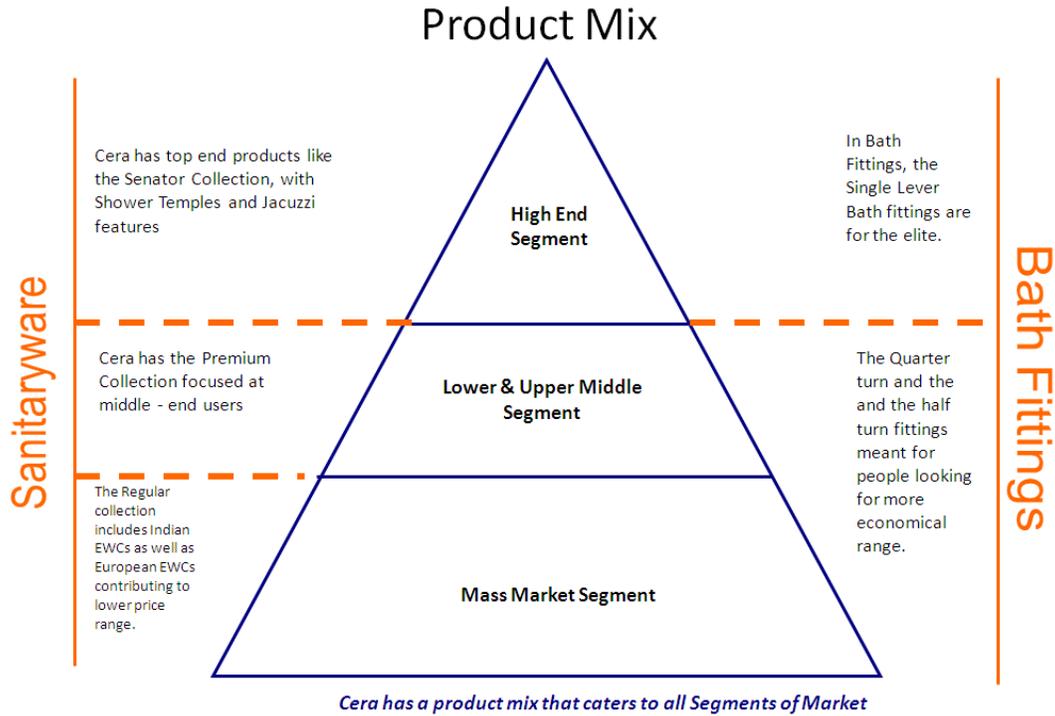
Launched in 1980, Cera is a pioneer in the sanitaryware segment in India. The first sanitaryware company to use natural gas, Cera has been on the forefront of launching a versatile colour range and introducing the bath suite concept. It also launched innovative designs and water-saving products. The twin-flush model launched in India by Cera for the first time, reduces the water needs of households considerably. WCs designed to flush in just 4 litres of water is another notable innovation by Cera.

Based in Kadi, Gujarat, Cera Sanitaryware Ltd. uses International technology, which has ensured Cera's superiority over others in quality. Established with an initial capacity of 3,600 MTPA, the plant has undergone several periodical upgradations and modernisations to expand to 25,000 MTPA.

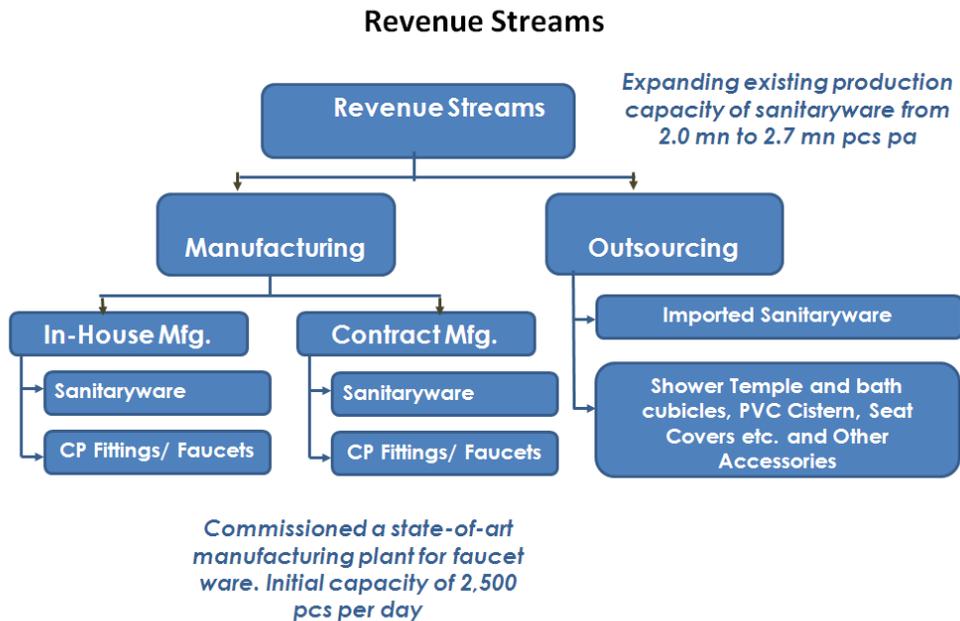
To achieve growth in the rapidly changing retail market in the country, Cera, has launched its one of a kind Cera Bath Studios in Ahmedabad, Bangalore, Chandigarh, Kolkata, Cochin and Hyderabad, Mumbai. With the opening of the Cera Bath Studios, the discerning consumers, architects and interior designers can have full view of the Cera's premium ranges of WC's, Wash Basins, Shower Panels, Shower Cubicles, Bath Tubs, Shower Temples, Whirlpools, CP fittings etc. Cera Bath Studios will complement its existing network of 600 dealers and 5000 retailers. Several Bathrooms are displayed live, so that the customers can get a feel of Cera's vast range of products.

Having shown a growth rate of more than 25% since last 3 years, Cera Sanitaryware Ltd. today is the fastest growing sanitaryware company in India. For its contribution towards the industrial growth, Cera's ED 'Mr. Vidhush Somany' received "The Nirman Ratna Award" in September 2010.

Products – Sanitaryware and Bath Fittings



Revenue Streams:



Revenue Streams

- For Cera there are two revenue streams. Manufacturing and Outsourcing. The company manufactures sanitary ware locally, while it outsources bath ware and faucet ware.
- The company has registered a good growth of 19% CAGR over the last 5 years in the Sanitaryware segment. This is well above 12-13% industry growth.
- In the Outsourced premium segment, the growth has been more spectacular at 33% CAGR over the last 5 years. Outsourcing doesn't require the company to set up a plant and therefore it's relatively easier to scale up and test market the products.

Strong Branding with Pricing Power

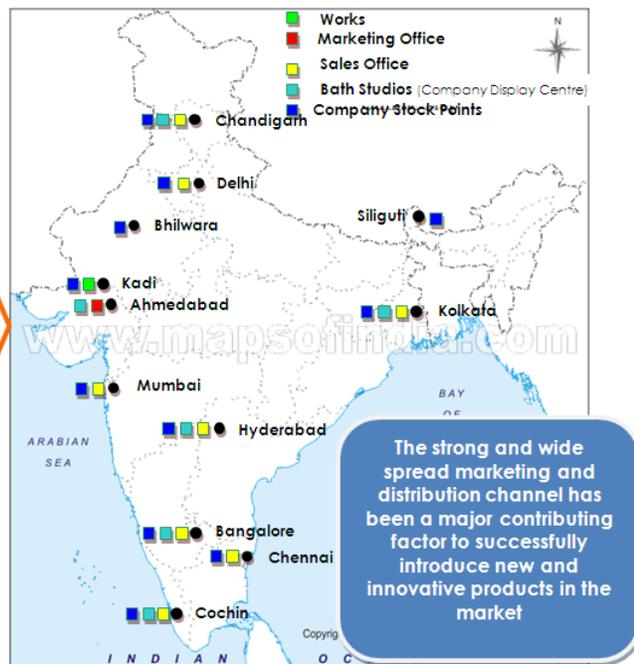
- In the Sanitary ware segment both the raw materials and the Power and fuel are the major inputs. Over the last 5 years, while the cost of raw materials has not increased much, the energy cost has gone up substantially.
- In case of Cera the company has been able to pass on any major increase in input price without much lag, while it doesn't have to reduce the prices in case the commodity prices go down. A sign of both the branding power and efficient management.

Strong Marketing and Distribution Network

Cera enjoys a strong distribution network with **500 Distributors / Dealers** (authorized stockiest) and **5000 retailers**.

To supplement the distribution network, the company has **12 major stock points** all over India. Cera also has **10 Zonal Sales, Service offices**, & **07 Bath studios** across the country.

A major marketing exercise of expanding dealer and retailer network is in progress. The company has also been sponsoring TV programs, arranging architect and plumber meets on regular intervals etc. to create its brand image in the market.



Cera Bath Studio and Bath Gallery



Cera pioneered the concept of Cera Bath Studios, the company owned company display centers, where architects, interior designers, builders, consultants, customers, etc. can touch and feel its range of sanitary wares, shower cubicles, steam cubicles, whirlpools, faucets, sinks, mirrors, sensors, etc.

2. Recent Developments

Cera embraces new Identity, Dia Mirza to Endorse, Nov 03, 2011

Cera Sanitaryware Ltd (CSL), has unveiled a new logo to capture the imagination of young and modern India. “Our new logo is the most sweeping transformation of the company’s corporate identity ever since it started its journey in 1980,” says Vidush Somany, executive director of the company. “Cera is one of the most preferred brands in the country, and the trust it generates from its customers is immeasurable. We are giving our logo a more contemporary look that is relevant for business today.”

Delving in to the semantics of the new logo, Somany explains, “Our new logo has been designed by the Ahmedabad-based creative agency Aakriti Promotions & Media Ltd, and has been infused with a sense of dynamism and openness. It is free from its boundaries, just as we are all set to become a total bathroom solutions provider. It aspires to evolve as a brand that provides style solutions to its core target group. Besides, the new and modern typeface indicates a strong sense of purpose and confidence in the brand’s ability.”

Somany believes that the new logo will connect seamlessly with the company’s customers, business associates and influencers. “Retaining the blue colour keeps Cera connected with its rich heritage of design and innovation for which it is immensely popular. While remaining rooted, it also aspires to adhere to core values of stability and sincerity.”

According to Somany, Cera has become a versatile brand by virtue of its expansion into new markets, creation of new businesses and strengthening of capabilities. “We are targeting those areas where our presence has been minimal. Soon our company will significantly scale up capacity from the current 75,000 pieces per month at the new faucet plant at Kadi. We will also aggressively increase the production of sanitaryware from 20 lakh pieces to 27 lakh pieces per annum to make it the largest plant in the country. Our new logo reflects this versatility.”

Along with the launch of the logo, CSL is also rejuvenating its marketing programmes. “We will kickstart our media campaign from December, which will spill over to the next financial year and span print, television and hoardings. We have signed up Bollywood actress Dia Mirza for endorsing the Cera brand. Our customers will get to see the new logo on all the products, packaging and signages within the next three to four months.” He adds that an array of new designs in sanitaryware and other products will also be launched in the coming year. “In our faucet vertical, we have launched four new ranges, and are planning to roll out some more shortly. Very soon, a new display centre will be thrown open in the western suburb of Mumbai.”

Cera Sanitaryware looks at acquisition in Italy, Oct 13, 2011.

Cera Sanitaryware Ltd, the third largest sanitaryware maker in India, is in talks with a number of companies to acquire a brand and a factory in Italy. Cera's board of directors is likely to take a decision on this by next year. Apart from this, the company is also in the process of expanding its manufacturing facility at Kadi in North Gujarat involving an investment of Rs 100 crore over the next couple of years.

With a view to catering to high end sanitaryware segment in India, we are looking at acquisition in Italy. This would be the first acquisition by Cera outside India," said Vidush Somany, executive director, Cera Sanitaryware Ltd. However, he did not disclose the size of the acquisition and the names of the Italian companies that Cera is in dialogue with.

According to Somany, the company is looking at acquiring either a brand or a factory or brand and factory both. Apart from this, the company may also buy out a research and development (R&D) studio. Cera has been scouting for a suitable company for almost a year.

Cera, which currently enjoys 21-22 per cent share in Rs 1500 to Rs 1800 crore organised sanitaryware market in India, is increasing the production capacity of its sanitaryware division at Kadi facility from current 2 million pieces to 2.7 million pieces. The expansion is slated to be completed by April 2012.

In addition to this, the taps manufacturing division will see its capacity going up almost three times to 2 million pieces from current 0.7 million pieces over the period of next 12 to 18 months.

"For sanitaryware division around Rs 60 crore will be infused, while for taps capacity increased Rs 40 crore would be pumped in," said Somany adding that the company is eyeing to capture 25 per cent market share by next year.

The company is also aggressively entering into luxury segment of shower enclosures, shower trays and equipped panels and cubicles. It has also tied-up with Italian company Novellini for this.

At present the company is the third largest player in Indian sanitaryware market with 21-22 per cent market share, while Hindustan Sanitaryware and Industries Ltd (HSIL) is on top with 41 per cent followed by Global giant Roca Bathroom Products Pvt Ltd with 26 per cent.

3. Financial Performance

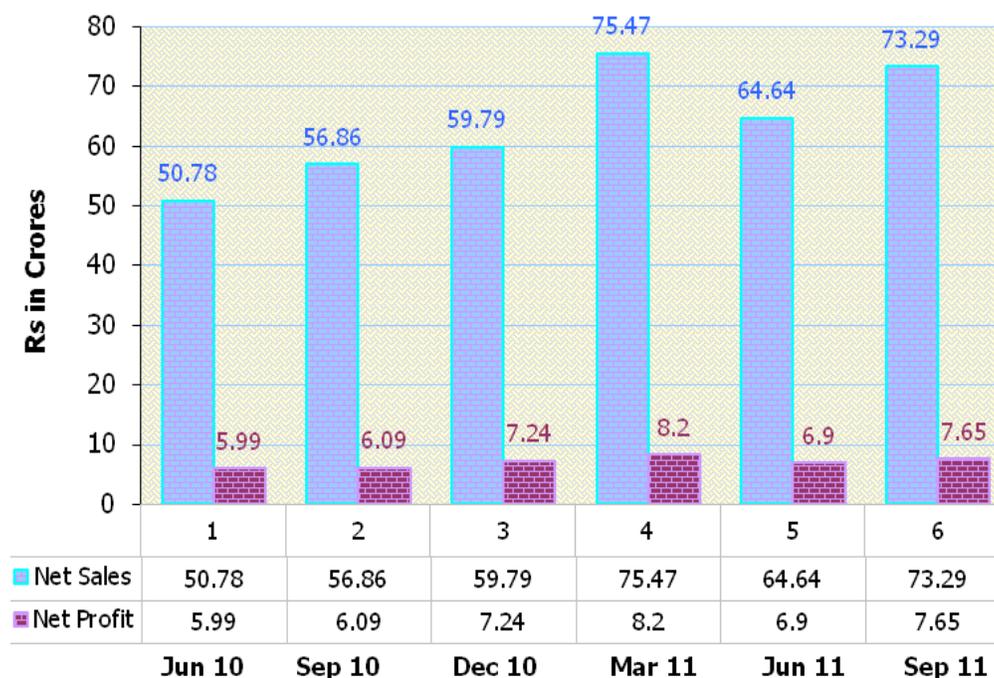
Cera Sanitaryware net profit rises 25.62% in the September 2011 quarter

Net profit of Cera Sanitaryware rose 25.62% to Rs 7.65 crore in the quarter ended September 2011 as against Rs 6.09 crore during the previous quarter ended September 2010. Sales rose 28.90% to Rs 73.29 crore in the quarter ended September 2011 as against Rs 56.86 crore during the previous quarter ended September 2010.

Cera Sanitaryware net profit rises 15.19% in the June 2011 quarter

Net profit of Cera Sanitaryware rose 15.19% to Rs 6.90 crore in the quarter ended June 2011 as against Rs 5.99 crore during the previous quarter ended June 2010. Sales rose 27.29% to Rs 64.64 crore in the quarter ended June 2011 as against Rs 50.78 crore during the previous quarter ended June 2010.

Last 6 Quarters Net Sales & Profit



Current & Expected Earnings:

Particulars (Rs. In Crores)	Dec '10	Mar '10	Jun '11	Sep '11	Dec '11 E	Mar' 12 E
Audited / Unaudited	UA	UA	UA	UA	UA	UA
Sales Turnover	59.79	75.47	64.64	73.29	71.89	86.76
Other Income	0.8	2.48	0.94	2.33	1.1	2.81
Total Income	60.59	77.95	65.57	75.61	72.99	89.57
Total Expenses	47.47	63.11	52.51	61.59	59.14	72.32
Operating Profit	12.32	12.36	12.13	11.7	12.75	14.44
Total Extraordinary Inc/Exp	--	--	--	--	--	--
Tax On Extraordinary Items	--	--	--	--	--	--
Net Extra Ordinary Inc/Exp	--	--	--	--	--	--
Gross Profit	13.12	14.84	13.07	14.03	13.85	17.25
Interest	0.76	0.72	0.72	0.82	0.80	0.98
PBDT	12.36	14.12	12.34	13.2	13.05	16.27
Depreciation	1.52	1.85	1.88	1.88	1.88	1.88
Depreciation On Assets	--	--	--	--	--	--
PBT	10.84	12.27	10.46	11.32	11.17	14.39
Tax	3.6	4.07	3.56	3.67	3.64	4.91
Net Profit	7.24	8.2	6.9	7.65	7.53	9.48
Prior Years Income/Expenses	--	--	--	--	--	--
Earnings Per Share	5.72	6.48	5.45	6.05	5.95	7.49
Equity	6.33	6.33	6.33	6.33	6.33	6.33
Reserves	--	--	--	--	--	--
Face Value	5	5	5	5	5	5
% of Public Share Holdings	45	45	45	45	--	--

Expected Earnings for 2nd and 3rd Qtr FY 2011-12:

CSL revenues may not deliver strong growth in next 2 quarters on account of high interest rates, raw material prices and slowdown in housing sector but can deliver robust growth in FY 2012-13.

Revenues are expected to increase significantly in FY 2012-13 considering higher volume sales on account of new manufacturing unit fully operational. Operating and profit margins will also improve with ease in raw material prices and interest rates. Increase in demand in housing and real estate sector will benefit the company.

4. Charts & Graphs

i) Share Price Moving Average:

CSL is currently trading below its 200 days price moving average and is having strong support at 150.

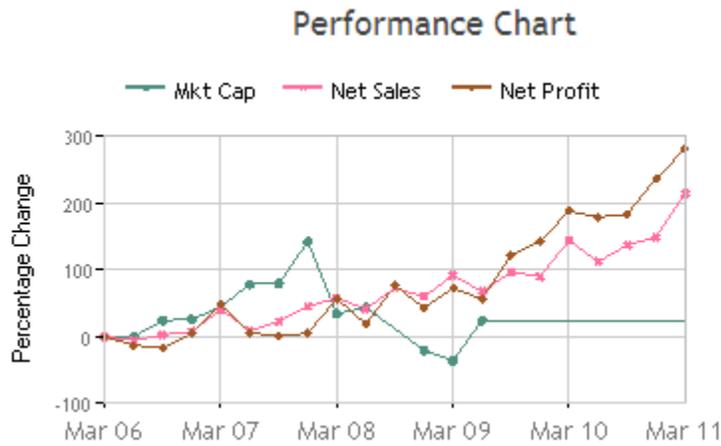


ii) Comparative Graph:

CSL has given returns of 411.05% in last three year. In last one year, CSL has outperformed giving returns of 7.31% against Sensex returns of -22.02%

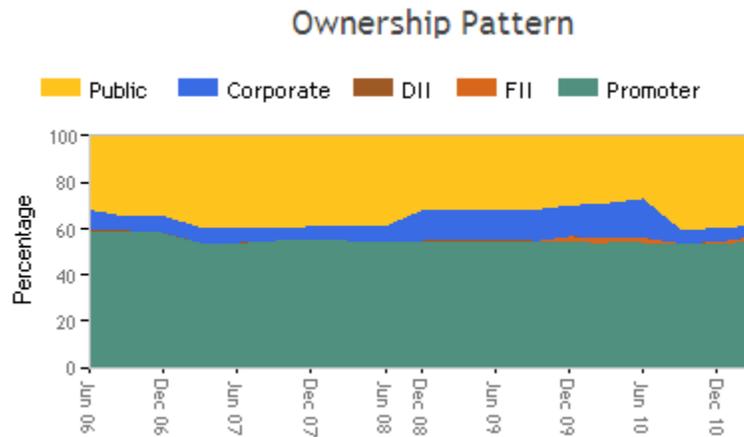


iii) Performance Chart:



iv) Share holding Pattern:

Promoters share holding is 55%. Promoters have increased their stake from 53.7% to 55% in last one year. FIIs holding have increased from minuscule 0.3% to 2.4% in last one year.



5. Peer Group Comparison

PEER GROUP	Cera Sanitaryware	Bell Ceramics	Euro Ceramics	Somany Ceramics	HSIL
CMP	166.40	10.69	10.15	32.70	122.50
52 W H/L	245.75/150.00	24.45/10.00	38.25/9.32	59.90/28.60	245.80/116.50
Mkt Cap	210.57	12.17	26.82	112.80	809.07
Results (in Crores)	Sep-2011	Se-2011	Sep-2011	Sep-2011	Sep-2011
Sales	73.29	42.70	53.65	207.66	299.05
PAT	7.65	-1.05	-20.88	5.75	23.00
Equity	6.33	12.17	26.43	6.90	13.21
EPS	23.70	0.84	0.00	7.16	16.87
P/E	7.02	11.90	-25.32	4.57	7.26

6. Key Concerns / Risks

- Over the last 1 year the raw material prices and the prices of other key inputs have increased, while on the same hand the global economy is slowing down. The company could be in for some tough times over the short term.
- In view of the inflationary environment, the RBI has continued with its monetary tightening. The same is hurting the growth and more specifically that of Real estate. The sale of Bath fittings is directly proportional to growth in real estate as replacement demand commands a very small share.
- Jaguar and other local and foreign brands are trying their hands at Indian Sanitary ware market. Jaguar has a very strong brand identity and distribution network. We believe it could come across as a major competitor to the established players.

7. Industry Overview

The Bathroom accessories and sanitary ware market in India has grown exponentially in the recent past. The current sanitary ware market size in India is approximately Rs 1700 crores while the Bathroom fittings market size is around Rs 3500 crores and are growing annually at a sustained rate of 15-16%. India is expected to become one of the largest consuming countries of sanitary ware in the near future.

The Sanitary ware and the bathroom fittings industry in India can be classified as follows:



Robust Growth Expected in next 3-5 years

The Indian sanitary ware industry has witnessed a seachange. With India emerging as the second largest in the baths and sanitary market in Asia Pacific, the sanitary ware market is poised to see strong growth in years to come.

The real estate and construction boom in India has helped in the increasing demand for bathroom products. Secondly, buying homes has become more 'affordable' to Indian customer with several housing finance companies offering attractive home loan packages.

The average age of an Indian youth buying his first house is in the early thirties or late twenties. They are willing to spend on their houses and demand the latest international trends and products for their new homes. Moreover, the 'replacement' market, comprising renovations, home improvements and refurbishments in bathrooms is growing significantly.

Competition Overview

Market is fragmented with many organized and unorganized players. Cera commands a market share of 21-22% in the organized sector.

- Share of unorganized sector is gradually declining.
- People are increasingly opting for branded bath fittings because of the guarantee in quality and after sales service.

Both domestic and the foreign manufacturers are supplying products in Indian Market

- Foreign players either have distribution partnerships with Indian players or have established their own subsidiaries.
- Companies are opening dedicated showrooms complete with concept bathrooms for providing better product demonstrations
- Companies operate both, through direct selling in the market and through retailers
- Companies also market directly to builders, architects and corporate without involving retailers.

Lack of Sanitation facilities in India

Sanitation Coverage in South-Asian Countries		
Country	Sanitation Coverage	
	Urban	Rural
India	58%	18%
Bhutan	65%	70%
Pakistan	92%	35%
Nepal	68%	20%

- India is a highly populated country with about 72% living in rural areas and the remaining 28% in urban areas.
- Around 58% of India's urban population has access to improved sanitation and in rural areas, the coverage is considerably lower at 18%.
- India's sanitation coverage in urban and rural areas is much less than other neighbouring South-Asian countries.
- Poor sanitation coverage in India reflects vast potential for growth opportunities for the sanitary ware industry.

Growth in Real Estate Sector

- The growth in sanitary ware industry is directly proportional to the growth in the real estate sector. The FY 2011-12 Union Budget has extended proposals with focus on affordable housing which are expected to benefit the sanitary ware industry in India.
- With robust growth in real estate sector, strong demand for sanitary ware products is expected from commercial and residential segments.

Increase in Life Style Spending

A customized bathing experience is fastly gaining momentum and presence of multiple International brands are making the market a competitive one.



In a developing market like India, these brands translate into more options for the luxury consumer. People are aspiring to a better life and they are spending money to get it.

An average household today is ready to invest more than Rs 15,000 on bathing luxuries. Three years ago, the average spend was just Rs 5,000.

The high-end products are targeted at the 3 million households and affordable products at segment of 6 million.

Today consumers are brand conscious and are aware of the fashion and changing trends, hence prefer branded products. They seek global brands for their kitchens or bathrooms for their flaunt value.

8. Investment Rationale

Strong Brand Equity – In the sanitary ware segment, there's strong brand identity against that in Tiles segment. At present there are only three major players i.e. HSIL, Parryware Roca and Cera. Cera's achievement of 20% + market share is commendable in the light of the fact that Cera started almost 20 years later than HSIL and 30 years later than Parryware.

Strong Marketing & Distribution network – Cera sells its products through a marketing network of 500 dealers and 5000 retailers spread across the country. It's difficult to replicate such a network and is one of the major business moats for Cera against the onslaught from foreign players and other local players.

Relatively slowly changing industry - It's a relatively slow changing business (makes it easier for us to hold it for long term in comparison to education or technology stocks where the trends change very fast and thus a company doing well today may end up on a losing side in a very short period of time).

No Institutional holding - There's no institutional holding in Cera, probably because of low liquidity. There is a very high probability the stock can get re-rated to higher PE multiples once it comes in sight of smart investors. At present the stock is quoting at 6.8 times trailing twelve months earnings.

Very attractive valuations – Murugappa group sold of their 47% stake in Parryware-Roca joint venture in 2008 for a sum of Rs 720 crore while the company had recorded a turnover of Rs 360 crore for FY 08, thus valuing the company at 4 times its annual turnover. Cera's market cap is approximately equal to its annual sales. Though not 4 times, however Cera can still get re-rated to twice the annual sales considering its efficiency and growth.

Regular Dividend Income – Since 2002, company has continuously rewarded its share holders paying regular dividend. Management has increased the dividend payouts every year from 2003. In last 8 years, dividend payout is increased by almost 9 times from Rs. 0.30 per share in year 2003 to Rs. 2.50 per share in 2011.

9. Saral Gyan Recommendation

i) Cera Sanitaryware net sales have grown at a rate of 26% on yearly basis during last 6 years whereas industry growth average is around 12-13%. Being into manufacturing sector, Cera commands higher margins, operating margins are at 20% and PAT margins are above 10%. PAT margins improved significantly from 4% in FY 2005 to 10.4% in FY 2011.

ii) Cera has achieved sales growth of 26% during last 6 years without any major equity dilution or debt funding and now it's a debt free company. Moreover, company is evaluating various parameters for an acquisition opportunity in Italy.

iii) For FY 2011, company has achieved 100% capacity utilization and in view of strong demand, it is increasing the production capacity of its sanitaryware division at Kadi facility from current 2 million pieces to 2.7 million pieces. The expansion is expected to be completed by April 2012. In addition to this, the faucetware manufacturing division will see its capacity going up almost three times to 2 million pieces from 0.7 million pieces over the period of next 12-18 months.

iv) Cera Sanitaryware Ltd is consistently paying dividends since 2002 to reward its shareholders. In last 10 years, dividend payout is increased by almost 9 times to Rs 2.5 per share in FY 2011 compared to Rs. 0.30 per share in FY 2002. Visibility of robust earnings in FY 2012-13 on account of increased production capacity, acquisition opportunity in Italy and increase in housing demand due to softening of interest rates makes CSL a good buy at current market price for investors who can hold it for period of 12-24 months.

v) At current market price of Rs 166.40, dividend yield works out to 1.5%. On equity of Rs. 6.33 crore the estimated annualized EPS for FY 2012-13 & FY 2013-14 works out to Rs. 32 and Rs. 44 respectively. Book value per share is Rs. 88.15 and at CMP of Rs. 166.40, stock price to book value is 1.89. Currently, the scrip is trading at 5.2X FY 2012-13 and 3.8X FY 2013-14 estimated earnings which make CSL an attractive bet at CMP.

Considering ongoing expansion, healthy operating margins with effective brand positioning and pricing power, better earning visibility on account of robust demand and strong marketing and distribution network, Saral Gyan Team recommends "BUY" on Cera Sanitaryware Ltd for a target price of Rs. 350 over a period of 12-18 months.

Buying Strategy:

- 50% at current market price of 166.40
- 50% at price range of 145-150 (if stock price falls during market correction)

10. Disclaimer

Important Notice: Saral Gyan Capital Services is an Independent Equity Research Company.

Disclosure: The author of this article does not hold shares in the recommended company.

© SARAL GYAN CAPITAL SERVICES

This document prepared by our research analysts does not constitute an offer or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. The information contained herein is from publicly available data or other sources believed to be reliable but we do not represent that it is accurate or complete and it should not be relied on as such. Saral Gyan Capital Services (www.saralgyan.in) or any of its affiliates shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. This document is provide for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision.