Cera Sanitaryware Limited

September 26, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	56.00	CARE AA; Stable	Reaffirmed
Long-term / Short-term bank facilities	44.00	CARE AA; Stable / CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The ratings assigned to the bank facilities of Cera Sanitaryware Limited (CSL) continue to derive strength from its long track record of operations along-with strong market position in the Indian sanitaryware industry especially in the retail segment. The ratings also derive strength from its diversified product portfolio in the building product segment aided by the strong brand name of 'CERA', and its robust distribution network. Vast experience of its promoters in the sanitaryware and faucetware business and CSL's strong financial risk profile marked by consistent growth in total operating income (TOI) along with healthy profitability margins and return ratio, significantly low reliance on external dent and its strong liquidity further underpin the ratings.
The ratings are, however, constrained by susceptibility of its profitability to volatility in fuel prices, raw material cost and foreign exchange rate fluctuations. The ratings are also constrained by its linkages to the cyclical real estate sector along with presence of large number of unorganised players in the sanitaryware and faucetware industry, imparting high degree of competitive intensity.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Significant increase in its scale of operations with TOI growing at a compounded annual growth rate (CAGR) of 20% leading to significant increase in its market share, while achieving return on capital employed (ROCE) above 25% on a sustained basis, along with comfortable leverage and strong liquidity.

Negative factors

- Decline in the scale of operations marked by TOI at less than ₹1,200 crore.
- Decline in PBILDT margin below 12% on a sustained basis due to increased competitive intensity and/or adverse movement in raw material prices.
- Any large debt-funded capex/acquisition or significant stretch in working capital requirement leading to increase in total outside liabilities (TOL)/tangible net worth (TNW) (net of cash and liquid investments) beyond 0.5x.

Analytical approach: Consolidated

CARE Ratings Limited (CARE Ratings) has considered consolidated financials of CSL for its rating approach, as its subsidiaries/joint ventures (JVs) are either in similar line of business with geographic extension or in related diversification with operational linkages and have common management platform. The list of entities getting consolidated in CSL is placed at **Annexure-6.**

Outlook: Stable

The stable outlook reflects CARE Ratings' expectations that CSL's financial risk profile will be supported by its strong market position and favourable long-term demand prospects for the end-user industry. CSL is likely to maintain its strong credit profile with very minimum reliance on external debt while maintaining strong liquidity.

Detailed description of the key rating drivers:

Key strengths

Established presence of brand 'CERA' in the sanitaryware industry on the back of its strong distribution and marketing network

CSL has established presence in the sanitaryware industry through its brand, 'CERA', and is positioned amongst the top two largest players (around 25% market share) in the organised domestic sanitaryware industry. Its growth has been aided by its strong marketing and distribution setup. CSL has a PAN-India marketing and distribution network consisting of around 20,062 dealers and sub-dealers for retail market (increased from around 15,566 a year ago) in addition to direct institutional sales to various construction companies. CSL's revenue mix was dominated by retail segment contributing around 68% of sales in FY23 (refers to the period April 1 to March 31), while balance was from direct institutional sales. Furthermore, the company has setup centralised depots at 29 locations across India for efficient distribution of its products. Geographically, south India is the largest

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

contributor in CSL's revenues, while Tier-3 areas (semi-urban and rural areas) contributed around 60% of CSL's revenue in FY23. CSL normally incurs advertisement expenditure between 3% and 4% of its net sales, which it envisages to continue going forward.

Diversified product portfolio with beneficial mix of own and outsourced manufacturing

CSL has an established presence in the sanitaryware industry while its market share in the faucetware industry is also increasing gradually. CSL has nearly 10% market share in the organised domestic faucetware industry. CSL expanded its product offering to include bath accessories, kitchen sinks, mirrors, and modular kitchens, with an aim to establish the brand "CERA" as a one-stop solution for all household lifestyle products. CSL reserves its in-house capacity for manufacturing higher value-added products requiring complex processes and robotics, while lower value products are outsourced. The income from outsourcing includes sales of bathware, faucetware, ceramic tiles and sanitaryware products. CSL's sales mix during FY23 stood as follows: sanitaryware (49% of its TOI), faucetware (35% of its TOI), tiles (11% of its TOI) and bathware along with other household lifestyle products (5% of its TOI). Over the years, CSL has integrated its operations by venturing into manufacturing tiles, plastic products and packaging through its subsidiaries and joint venture (JV) for providing better quality and cost control. However, the company has served a legal notice to Milo Tile LLP (associate company) for non-compliance with the terms of agreement, consequently Milo Tiles LLP has stopped supplying to CSL. As against the total investment of ₹8.06 crore in Milo Tile LLP, the company has provided for an impairment loss of ₹5.00 crore in the books of accounts which has been disclosed as an "Exceptional Item" in the financial statements in FY23. CSL's tiles business is now largely reliant on other abundant outsourcing opportunities available in the market. To further expand its business, CSL has planned to undertake a capacity expansion project comprising a greenfield sanitaryware project at a cost of around ₹129 crore to be completed over a period of 24 months from 'zero date', and a brownfield expansion of its faucetware capacity entailing a cost of ₹69 crore, which is expected to be completed by Q4FY24. The entire capex is planned to be funded from its internal accruals/available liquidity.

Strong financial risk profile with comfortable leverage and debt coverage indicators

The TOI of CSL, at a consolidated basis, grew at compounded annual growth rate (CAGR) of around 9% in last 5 years ended FY23, while profit before interest, lease rentals, depreciation and taxation (PBILDT) and profit after tax (PAT) grew by 11% and 15%, respectively, during the same period. The TOI grew healthy at around 24% in FY23 over FY22 backed by strong replacement demand and accelerating real estate demand. The PBILDT margin also improved to 16.28% during FY23 vis-à-vis 15.79% during FY22 on the back of better economies of scale and various yield-improvement measures undertaken by the company. The PBILDT margins are expected to remain steady at around 16-17% in FY24-FY26. CSL has been maintaining healthy return of capital employed (ROCE) of over 20% except the COVID-19 impacted FY20 and FY21. ROCE stood strong at around 24% in FY23 and the same is likely to remain above 22% in FY24-FY26.

CSL's financial risk profile continued to remain strong with comfortable capital structure marked by an overall gearing of 0.04x as on March 31, 2023 (0.04x as on March 31, 2022). Debt coverage indicators also stood comfortable with PBILDT interest coverage of 50.73x and TDGCA of 0.22x during FY23. CARE Ratings notes that CSL's overall gearing and TOL/TNW (net of cash and liquid investments) is expected to remain comfortably below 0.10x during next 3 years ending FY26.

Liquidity: Strong

CSL's liquidity remained strong during FY23 marked by strong cash accruals against low debt repayment obligations and presence of unencumbered cash and bank balance/ liquid investments to the tune of around ₹656 crore as on March 31, 2023, which further increased to ₹755 crore as on June 30, 2023. CSL is likely to maintain unencumbered liquidity of more than ₹700 crore in the near to medium term in the absence of any major organic or inorganic expansion or diversification plan.

With an overall gearing of 0.04x as on March 31, 2023, CSL has sufficient gearing headroom to raise additional debt, if required, for its capex. CSL plans to incur a capex of around ₹50-75 crore per annum, which shall be entirely funded through internal accruals. Additionally, with its average working capital limit utilisation at around 22% for the trailing 12 months ended May 2023, its unutilised bank lines are more than adequate to meet its incremental working capital needs over the next one year. Its average collection period has further improved during FY23 to around 35 days (vs 47 days during FY22).

Key weaknesses

Susceptibility of profitability to volatility in fuel prices and raw material cost; albeit benefit from cheaper sources for meeting part requirement

CSL's profitability is susceptible to volatility in fuel prices (primarily natural gas) and other key raw materials (various types of clay, brass, and chrome plating). However, CSL has been largely able to pass on, though with some time lag, increase in raw material and other operating costs to the customers due to its strong brand name in the mid and mass market segment. It also has captive sources of renewable energy for meeting more than half of its power consumption apart from availability of natural gas at subsidised rates from nearby isolated fields for meeting around 60% of its total natural gas requirement which supports its operating profitability. CARE Ratings observes that CSL has also been taking various yield improvements measures to counter the cost inflation, if any, which allows the company to maintain its profitability margin.

Linkages to cyclical real estate sector and presence in a competitive building product industry
The demand for CSL's products is linked to the cyclical real estate sector. The sector is witnessing good momentum driven by new project launches across regions. Along with good replacement demand, the overall demand for sanitaryware and faucetware is expected to remain steady in the medium term. Furthermore, CSL has a major presence in Tier-III cities which experience less volatility in demand compared to Tier-I cities. Additionally, factors such as increasing urbanisation with the government's plan to develop at least 100 smart cities, renewed focus on infrastructure growth, better demographic profile and increasing awareness towards better sanitation facilities, etc., would be beneficial for the industry in the long term. The sanitaryware market is also witnessing shifting of consumer preference towards branded products thereby presenting growth opportunities for established players like CSL in the industry. However, there are many unorganised players in the ceramic sanitaryware products and faucetware market apart from well-established brands like 'Hindware', 'Roca', 'Parryware' in sanitaryware market, 'Kohler', 'Jaquar' in faucet ware and 'Kajaria', 'Somany' in tiles, thus putting competitive pressure on CSL and restricting its scale of operations. CARE Ratings believes that the company will thrive and continue to do better despite competition, going forward.

Environment, social, and governance (ESG) risks

Risk factors	
Environmental	• Sanitaryware and tile manufacturing is an energy-intensive process requiring substantial quantities of fuel, and thus, resulting in greenhouse gas emissions, waste generation and pollution. As such, the industry's (and CSL's) exposure to litigation/penalties arising from issues related to waste and pollution management remains relatively high. However, CSL has managed power costs by generating electricity through non-conventional sources (wind and solar) for captive use; as of FY23, its total installed non-conventional energy capacity stood at 10.325 MW. Around 60-80% of its energy needs are met through own renewable energy sources. Additionally, CSL uses the natural gas instead of coal to fire its kiln. • By successfully developing a fully functional rainwater harvesting system, CSL has managed to reduce dependence on ground water usage. • In its initiative to conserve biodiversity, the company has undertaken plantation of over 10,000 plus trees. • Under the initiative of 'Waste Minimization and Waste Utilization', the company has been undertaking numerous measures including recycling of solid and liquid and zero liquid discharge (ZLD), high energy-efficient-rated machines, compliance to pollution norms. The majority of the waste generated in the company's operations is recycled and the balance is disposed-off safely. The company has also installed an effluent treatment plant at both of its facilities. CSL's waste and emission remained within the prescribed limits of Central Pollution Control Board (CPCB) / Gujarat Pollution Control Board (GPCB) in FY23.
Social	• Social risks in the industry stem from the health and safety concerns of employees involved in management of clay, among other things. • The company at regular intervals provides necessary safety and skill up-gradation training to its permanent as well as its contractual employees. The company has systems in place to ensure no child labour, forced or involuntary labour at its facilities. • During FY23, the company has spent ₹3.00 crore towards CSR activities, mainly in the areas of education, healthcare, rural development, woman empowerment and eradicating hunger.
Governance	• CSL has adopted various best governance practices. Its policy relating to ethics, bribery and corruption serves as the guiding philosophy for its employees. • The company also has a whistle blower policy in place, which provides a platform to all employees, vendors, and customers to report any suspected fraud or error or confirmed incident of fraud / misconduct.

Applicable criteria

Policy on default recognition
Consolidation
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Short Term Instruments
Manufacturing Companies
Policy on Withdrawal of Ratings

About the company and industry

Industry classification

Macro-economic indicator	Sector	Industry	Basic Industry
Consumer Discretionary	Consumer Durables	Consumer Durables	Sanitary Ware

CSL was incorporated as Madhusudan Oils and Fats Ltd (MOFL) in 1998. MOFL was later acquired by Madhusudan Industries Limited under the scheme of arrangement in 2001, and subsequently its name was changed to CSL. It is promoted by Vikram Somany and has its manufacturing facility located at Kadi in Mehsana district of Gujarat. The company is mainly engaged in the manufacturing of ceramic sanitaryware (installed capacity of 33,750 metric tonnes per annum [MTPA]), faucet ware (installed capacity of 35 lakh pieces per annum [LPPA]) and trading of sanitaryware, faucet ware, ceramic tiles, kitchen sinks and bath wellness products (i.e., shower room, steam shower room, shower cubicles and bath-tubs). Most of its goods (including traded goods) are sold under the 'Cera' brand. Furthermore, CSL has wind-mills and solar power plant with installed power generation capacity aggregating 10.325 MW for meeting part of its power requirement.

(₹ crore)

Brief Financials - Consolidated	FY22 (A)	FY23 (A)	Q1FY24 (UA)
Total operating income	1,445	1,804	429
PBILDT	228	294	70
PAT	153	211	57
Overall gearing (times)	0.04	0.04	NA
Interest coverage (times)	48.14	50.73	52.95

A: Audited; UA: Unaudited; NA: Not available; Note: 'the above results are latest financial results available'

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating history for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Cash credit	-	-	-	-	56.00	CARE AA; Stable
Non-fund-based - LT/ ST-BG/LC	-	-	-	-	9.00	CARE AA; Stable/ CARE A1+
Non-fund-based - LT/ ST-BG/LC	-	-	-	-	35.00	CARE AA; Stable/ CARE A1+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Non-fund-based - LT/ ST-BG/LC	LT/ST*	35.00	CARE AA; Stable / CARE A1+	-	1)CARE AA; Stable / CARE A1+ (02-Sep-22)	1)CARE AA; Stable / CARE A1+ (23-Aug-21)	1)CARE AA; Stable / CARE A1+ (27-Aug-20)
2	Fund-based - LT-Cash credit	LT	56.00	CARE AA; Stable	-	1)CARE AA; Stable (02-Sep-22)	1)CARE AA; Stable (23-Aug-21)	1)CARE AA; Stable (27-Aug-20)
3	Non-fund-based - LT/ ST-BG/LC	LT/ST	9.00	CARE AA; Stable / CARE A1+	-	1)CARE AA; Stable / CARE A1+ (02-Sep-22)	1)CARE AA; Stable / CARE A1+ (23-Aug-21)	1)CARE A1+ (27-Aug-20)

** LT/ST - Long term/Short term*

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities: Not Applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT-Cash credit	Simple
2	Non-fund-based - LT/ ST-BG/LC	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Annexure-6: List of entities getting consolidated in CSL:

Sr. No.	Name of the entity	% stake of CSL as on March 31, 2023
1	Packcart Packaging LLP	51.00
2	Race Polymers Arts LLP	51.00

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:
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