July 17, 2017

Somany Ceramics Limited

Summary of rated instruments

Instrument*	Rated Amount (in Rs. crore)	Rating Action
Commercial Paper	90.00 (enhanced from 40.00)	[ICRA]A1+; assigned/outstanding

*Instrument details are provided in Annexure-1

Rating action

ICRA has assigned the short-term rating of [ICRA]A1+ (pronounced as ICRA A one plus) for the Rs. 90.00-crore[1] (enhanced from Rs. 40.00-crore) CP programme of Somany Ceramics Limited (SCL)[2].

Rationale

The rating action takes into account SCL's strong brand, established market position and strong financial profile that have resulted in a very strong credit profile over the years. Aided by equity infusion in the previous years and low debt levels, the company's gearing has remained less than 0.5 times in the last two years. Further, it is continually shifting its product mix towards value-added products and increasing its portfolio of high margin sanitaryware and fittings products, which should aid margin expansion in the coming years. The company's profitability is supported by a decline in power and fuel expenses owing to softening gas prices during FY2017. Notwithstanding the transient effects of the Goods & Services Tax (GST) implementation, which can impact demand for the industry as a whole in the near term, the favourable long-term demand prospects for flooring and wall tiles in the domestic market will help in sustaining the company's revenue growth in the long term. SCL's improved manufacturing presence post acquisitions in Morbi, Gujarat should also support the top line. The company's presence in the sanitaryware and bath fittings segments (though JV and outsourced sales) are expected to provide a fillip to the profitability as the segments increase in scale (installed JV capacity of sanitaryware has been more than tripled to 1.15 million pieces per annum).

Rating concerns emanate from the highly competitive nature of the tile industry, marked by the presence of both large and organised players as well as numerous small scale tile manufacturers (mostly in and around Morbi, which operate with a leaner cost structure). The company's margins will remain vulnerable to change in input costs, especially power and gas. Notably, the company has benefitted from a decrease in gas prices, especially since January 2016, which is expected to aid its profitability in the near term. The business also remains vulnerable to slowdown in the real-estate sector. However, the company's actual exposure to private builders segment, which is witnessing pressure, is limited. Weak industry demand and demonetisation have impacted revenue growth in FY2017. Strong brand and distribution network coupled with distributed manufacturing presence act as a buffer against these concerns.

Going forward, SCL's ability to counter the rise in input costs, competitive pressures and demand slowdown with its focus on value-added products and brand will remain the key rating driver. Small sized organic and inorganic investments should keep the long-term debt levels stable and also aid revenue growth.

[1] 100 lakh = 1 crore = 10 million
[2] For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications

Key rating drivers

Credit strengths

- Established position in the domestic tile market; brand name enjoys national recognition
- Presence of manufacturing facilities in the northern as well as western regions of India, reducing the vulnerability of its revenue base to the demand-supply dynamics in any particular region
- Through a series of investments, accessible capacity (includes own manufacturing, JV and outsourced capacities) increased from 33.9 million square metre (msm) in FY2012 to 62.06 msm, with stable debt levels
- Strong financial profile, marked by equity infusion, low debt levels, improvement in profitability, low gearing and improved coverage indicators
- Presence of cash and liquid investments of Rs 123.6 crore as on March 31, 2017.

Credit weaknesses

- Implementation of GST can potentially impact the industry demand in the medium term; however, SCL's strong financial profile and recognised brand would mitigate risks
- Challenges in maintaining position in markets beyond northern and southern India; however, tie ups with players in Gujarat, and focus on manufacturing high-end tiles are expected to increase Somany's market share across regions;
- Highly competitive business marked by the presence of big organised players; focus on high value tiles segment, and strong distribution network should help sustain profitability
- Vulnerability to slowdown in the real-estate sector; although institutional sales constitute only a third of the company's sales.

Description of key rating drivers

The credit strengths of SCL arise from its established position in the domestic tiles market in northern and southern India, favourable long-term demand prospects for flooring and wall tiles in the domestic markets and the presence of manufacturing facilities in northern and western India. This helps to insulate its revenue base against localised downturns. The company continues to focus on its value-added segment, which constituted 45% of total sales in FY2017 (as against 39% in FY2016). The shift towards the high-value segment in addition to increasing proportion of high margin sanitaryware segment (capacity more than tripled to 1.15 million pieces per annum) bode well for the top-line growth as well as margin expansion. Among customers, the retail segment dominates the company's revenue profile with a share of ~70%. Thus, SCL's business model, characterised by distributed manufacturing facilities, a wide product base (that includes manufactured as well as outsourced products), and a higher share of retail segment, lends strong support to its operational profile.

The company's financial profile continues to be strong and is characterised by low gearing, improving profitability, and presence of significant cash and liquid investments despite continued investments in modernisation and expansion of existing capacities. The existing term loan repayments are spread out over the next six years and the debt service coverage ratio was 2.92 times in FY2017. Moreover, the low gearing and high availability of liquid funds imparts considerable financial flexibility to the company. Strong operational and financial profile will help it in countering challenges such as demand slowdowns, rise in input costs and stiff competition.

Key Financial Indicators

	FY2016	**FY2017**
Operating income (Rs. crore)	1,730.7	1,838.4
PAT (Rs. crore)	61.1	86.1
OPBDIT/ OI (%)	7.1%	8.8%
RoCE (%)	19.8%	21.7%
Total Debt/ TNW (times)	0.45	0.43
Total Debt/ OPBDIT (times)	1.54	1.35
Interest coverage (times)	7.53	9.80
NWC/ OI (%)	10.4%	12.8%

Note: Amounts in Rs. crore; OPBDITA: Operating Profit before Depreciation, Interest, Taxes and Amortisation; PAT: Adjusted Profit after Tax; TNW: Tangible Net Worth; NWC: Net Working Capital.
Source: Financial statements of SCL and ICRA estimates

Analytical approach

For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria
Corporate Credit Rating Methodology

About the company

SCL was incorporated in 1969 as a manufacturer of ceramic tiles by Mr. H. L. Somany in collaboration with Pilkington's of the U.K as a widely-held company. Since then, the company has extended its production capacities as well as product range. It is involved in the manufacturing, outsourcing and trading of ceramic wall and floor tiles. The company has access to 62.06 msm capacity, which includes 25.55 msm per annum (pa) capacity at the company-owned production units at Kassar (Haryana) and Kadi (Gujarat), 27.51 msm pa through subsidiaries and associates, and 9.0 msm pa through outsourcing. In addition, the company acquired a majority stake in Somany Sanitaryware Pvt. Ltd., which has a capacity of 3.03 lakh pieces of sanitaryware pa. The same has been more than trebled to 11.5 lac pieces pa in April 2017. The company markets its tiles under established brand names like Somany, Durastone, Duragress, VC Shield, Somany Express etc.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years

Table

S.No	Name of Instrument	Current Rating			Chronology of Rating History for the past 3 years		
		Type	Rated Amount (Rs. Crore)	Month-year & Rating	Date & Rating in FY2017	Date & Rating in FY2016	Date & Rating in FY2015
				July 2017	Oct 2016	Dec 2015	Sep 2014
1	Commercial Paper	Short Term	90.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-
2	Term loans	Long Term	-	-	-	-	[ICRA]BBB+ (Stable)^
3	Fund-based Facilities	Long Term	-	-	-	-	[ICRA]BBB+ (Stable)^
4	Non-fund Based Facilities	Short Term	-	-	-	-	[ICRA]A2+^

Complexity level of rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1
Details of Instrument

Name of the instrument	Date of Issuance/ Sanction	Coupon rate	Maturity Date	Amount Rated (Rs. Crore)	Current Rating and Outlook
Commercial Paper	20 June 2017	6.55%	15 September 2017	40.00	[ICRA]A1+
Commercial Paper – Proposed	-	-	-	50.00	[ICRA]A1+

Source: Somany Ceramics Limited

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About ICRA Limited:

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