January 30, 2017

# Kajaria Ceramics Limited

| Instruments* | Amount Rated (Rs. Cr.) | Rating Action |
|---|---|---|
| Fund Based Bank Facilities | 50.0 | [ICRA]AA(Stable) (Reaffirmed) |
| Non Fund Based Bank Facilities | 125.0 | [ICRA]A1+ (Reaffirmed) |
| Short Term Loan | 50.0 | [ICRA]A1+ (Reaffirmed) |

**Rating Action**
*Instrument details are provided in Annexure-1*

ICRA has reaffirmed the long term rating of [ICRA]AA (pronounced ICRA double A)[1] outstanding on the Rs. 50.0 Cr.[2] fund based bank facilities of Kajaria Ceramics Limited (Kajaria). ICRA has also reaffirmed the short term rating of [ICRA]A1+ (pronounced ICRA A one plus) outstanding on the Rs. 125.0 Cr. non fund based bank facilities and Rs. 50.0 Cr. short term loan of KCL. The outlook on the long term rating is 'Stable'.

**Rationale**

The ratings reaffirmation factor in Kajaria's dominant position in the Indian tile industry along with the company's healthy scaling up of operations over the past few years. Kajaria's operating income on a standalone basis over the period from 2011-12 to 2015-16 has increased at an annual CAGR of ~17%. Over the mentioned time period, the financial profile has strengthened as reflected by improvement in profitability margins, growth in return indicators, deleveraging of capital structure and strengthening of coverage indicators and debt protection metrics. One of the reasons for improvement in profitability margins is the declining share of outsourcing (Non JV) sale in the overall sales mix of the company.

The ratings continue to factor in the extensive experience of the promoters in the ceramic tile industry and Kajaria's established brand and strong market presence. Over the last few years, Kajaria has undertaken capacity expansions, both in-house as well as under JV's wherein the investments have been funded primarily through internal cash accruals. Over the last few years Kajaria has made acquisitions in Gujarat and Andhra Pradesh which have resulted in increase in installed capacity on a consolidated basis and improved its access to western and southern regions of the country. During Q4 2015-16, the company has even commenced operations at its 6.5 MSM (Million sq. meter) vitrified tile Greenfield facility at Malootana, Rajasthan taking the standalone capacity of the company to 40.8 MSM.

Over the last 12 months, Kajaria has also benefitted on account of decline in power and fuel cost on account of renegotiation of the gas price contract between RasGas (Saudi Arabia) and Petronet LNG (India). Despite the reduction in power and fuel price, the realizations of the company remained buoyant consequently resulting in improvement of profitability margins. However, gas prices have increased to a certain extent over the last few months. The ratings continue to be supported by the company's widespread distribution network.

However, the ratings continue to be constrained by the competitive nature of tile industry wherein there has been some moderation in the overall growth over the last year. Kajaria's profitability continues to remain vulnerable to any increase in the prices of raw materials and fuel as the combination of these two categories forms a major part of the cost structure. However, Kajaria continues to benefit on account of its strong brand, on account of which in the past, it has been able to pass on any increase in raw material and power and fuel costs to its customers. ICRA also notes that, there may be a short term impact on the offtake of Kajaria's products on account of recent demonetization of the Indian currency. However, such a move is expected to benefit the organized players in the long run.

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

Going forward, the operating income of the company is expected to report moderate growth and profitability margins are expected to remain healthy in line with the previous years. No further capacity additions are envisaged at the standalone level, however Kajaria may need to infuse funds to support some of its subsidiaries/JV. The ability of the company to increase its market share and maintain a healthy financial profile would be the key rating sensitivities.

**Key rating drivers**

**Credit Strengths**
- Established presence and extensive experience of the promoters in the tile industry
- Established brand and strong market presence which is well supported by the company's widespread dealer and distribution network
- Steady growth in realizations has aided in securing healthy profitability margins over the last few years
- Significant decline in contribution of outsourced sales in the overall sales mix on account of increase in installed capacity under JVs and commencement of operations in its new facility in Rajasthan; the inherent margins on the traded sales are lower and hence the overall profitability margins have increased
- Continuous capacity expansions, both in house as well as through JV's has aided in increased market share and growth in scale of operations wherein capex has been mainly funded through internal cash accruals
- Strong financial profile characterized by healthy growth in operating income, improvement in profitability margins, comfortable capital structure and strong debt protection metrics

**Credit Concerns**
- Vulnerability of the tile business to cyclical trends in the real estate sector – however, over the past years, slowdown in the real estate sector has not impacted the sales of the company due to its focus on retail segment
- High competitive intensity with presence of numerous un-organized players and several large players in the organized segment
- Vulnerability of profitability to any increase in the prices of key raw materials and fuel costs

**Description of key rating drivers highlighted above:**
Kajaria is the largest player in the Indian tile industry and accounts for approximately 8% of the Indian tile market wherein the share of the organized players is expected to be close to 50%. The promoters have been involved in this line of business since more than last three decades. The company has an installed capacity of 40.8 MSM on a standalone basis along with a capacity of 27.8 MSM under various JVs. Kajaria is adding another 5.7 MSM capacity under one of its JV's in Andhra Pradesh which is expected to become operational in FY18.

Own manufacturing contributes roughly 50% of the sales mix whereas the balance comprises sales in JVs and trading sales. Over the last few years, the contribution of trading sales has come down from 22% in FY14 to only 9% in H1FY17 which has consequently resulted in an improvement in profitability margins as trading/outsourced sales fetch lower profitability. Moreover, the profitability margins have been further supported by significant reduction in gas prices, which is a key fuel for the tile industry. On the other hand, the realization levels of the company have continued to remain buoyant. Subsequently the operating margins have improved and stood at 16.1% for FY16 and 18.5% for H1 FY17 as against 12.6% during FY14. The same has translated into better net profitability margins as well.

Despite, there being a significant capacity addition over the last few years, the capital structure has improved as Kajaria has funded a major proportion of its requirements through internal accruals and has relied on external debt to a very limited extent (mainly in JVs). As a result, the debt outstanding of its books remains very small in comparison to the company's net worth.

On account of the slowdown in the real estate sector which is the major consumer of building products, there was moderation in the growth rate of the tile industry. The same impacted Kajaria, as reflected by a 4% growth in operating income during H1FY17 over H1FY16. Moreover, the retail segment which is a key contributor towards Kajaria's top line is expected to be impacted on account of demonetization which may impact the scale of the company in the short run. The company continues to remain exposed to the high competitive intensity in the tile industry. Going forward, once GST would become applicable, organized segment players including

Kajaria are expected to benefit which may even lead to growth in their market share. The company's profitability continues to remain exposed to any increase in the prices of raw materials and power and fuel as both theses heads account for ~70% of the cost component.

**Analytical approach**
Not Applicable

**Links to applicable Criteria**
**Corporate Credit Ratings: A Note on Methodology**

**About the Company:**
Kajaria was incorporated in 1985 as a manufacturer and trader in ceramic tiles, by Mr Ashok Kajaria in technical collaboration with Todagres SA, Spain and it started its operations in 1988 with a capacity of 1 million sqm per annum at its ceramic tiles manufacturing facility at Sikanderabad (District Bulandshahr),UP. Since then the company has extended production capacities as well as the product range. The company is mainly engaged in manufacturing ceramic glazed wall and floor tiles and vitrified tiles. It also imports vitrified tiles from China and various high-end tiles from leading European brands, which are marketed under the brand name of 'Kajaria. Kajaria also imports sanitary-ware. The manufacturing facilities of the company are located in Sikanderabad (Uttar Pradesh), Gailpur (Rajasthan) and Malootana (Rajasthan) apart from five manufacturing facilities (JV's) of ceramic and vitrified tiles in Gujarat and one facility (JV's) in Andhra Pradesh and Kajaria has a majority stake in each of them. With these acquisitions and expansions carried out both in-house and in subsidiaries, the total tile manufacturing capacity of the company has increased to 68.6 million square meters (msm) on consolidated basis.

**Status of non-cooperation with previous CRA:** Not Applicable.

**Any other information:** Not Applicable

**Rating History for last three years:**
**Table: Rating History**

| S. No. | Name of Instrument | Current Rating | | | Chronology of Rating History for the past 3 years | | |
|---|---|---|---|---|---|---|---|
| | | Type | Rated amount (Rs. Crores) | Month - year & rating | Month - year & Rating in FY2016 | Month - year & Rating in FY2015 | Month - year & Rating in FY2014 |
| | | | | Jan 2017 | Jan 2016 | Nov 2014 | Jan 2014 |
| 1 | Fund Based Bank Facilities | Long term | 50 | [ICRA]AA (Stable) | [ICRA]AA (Stable) | [ICRA]AA- (Stable) | [ICRA]A+ (Stable) |
| 2 | Non Fund Based Bank Facilities | Short term | 125 | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ |
| 3 | Short Term Loan | Short term | 50 | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ |

**Complexity level of the 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 Instruments**

| Name of the instrument | Date of issuance | Coupon rate | Maturity Date | Size of the issue (Rs. Cr) | Current Rating and Outlook |
|---|---|---|---|---|---|
| Fund Based Limits | - | - | - | 50.00 | [ICRA]AA(Stable) |
| Non Fund Based Limits | - | - | - | 125.00 | [ICRA]A1+ |
| Short Term Loan | - | - | - | 50.00 | [ICRA]A1+ |

Source: Kajaria

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About ICRA Limited:

**ICRA Limited** was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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