

## RAK Ceramics PJSC

Growth in margins despite challenging macroeconomic conditions

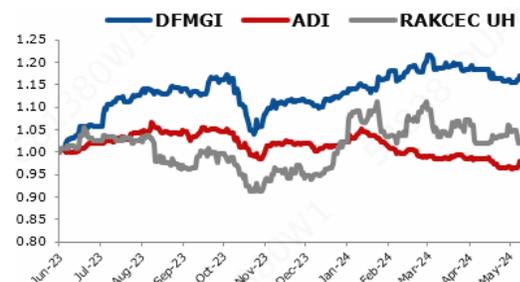
**Current Price**  
AED 2.52

**Target Price**  
AED 3.80

**Upside/Downside (%)**  
+51%

**Rating**  
BUY

- Gross and EBITDA margins grew 68 bps YOY and 151 bps YOY to 39.3% and 19.3% respectively in 1Q24.
- Net debt declined from AED 1,418 Mn in 4Q23 to AED 1,364 Mn in 1Q24. Net debt to EBITDA ratio also declined from 2.2x in 4Q23 to 2.1x in 1Q24.
- Capex declined from AED 90.9 Mn in 4Q23 to AED 35.2 Mn in 1Q24. RAKCEC further expects the capex to range between AED 300-350 Mn in 2024.
- In UAE, the Company successfully finished the Tableware expansion project and added 10 Mn of capacity.
- RAKCEC trades at an attractive dividend yield of 7.8% in 2024.



### 1Q24 Net Profit lower than our estimate

Rak Ceramics PJSC (RAKCEC/"The Company") net profit declined 21.5% YOY to AED 58 Mn in 1Q24, lower than our estimate of AED 87 Mn. The decline in net profit is primarily attributable to lower revenue owing to challenging macroeconomic conditions, rising geopolitical conditions, market volatility, currency devaluation, rising interest rates, and a decline in EBITDA, partially offset by a decline in direct costs, lower S&G expenses, and impairment charges.

### P&L Highlights

RAKCEC revenue declined 11.4% YOY to AED 782 Mn in 1Q24, mainly due to challenging macroeconomic conditions and lower sales in the Sanitaryware, Tiles and Tableware segments partially offset by growth in Faucets segment. The Company's tiles revenue declined 14.8% YOY to AED 444 Mn in 1Q24 mainly due to lower volumes in Europe and Saudi Arabia. Sanitaryware revenue declined 12.7% YOY to AED 113 Mn in 1Q24, primarily due to major challenges faced by the Company's key markets in the UK and Italy, such as recessionary pressure and inflation, impacting consumer spending. Tableware revenue also declined 7.8% YOY to AED 90 Mn in 1Q24, owing to a decline in sales volume attributed to currency devaluation and logistical challenges. However, Faucets segment revenue grew 4.7% YOY to AED 117 Mn in 1Q24. The Company's direct cost declined 12.4% YOY to AED 474 Mn in 1Q24. Thus, gross profit declined 9.9% YOY to AED 307 Mn in 1Q24. However, RAKCEC's gross profit margin grew 68 bps YOY to 39.3% in 1Q24, primarily due to the improved operational efficiency and lower gas prices in the UAE. Operating expenses declined 8.4% YOY to AED 218 Mn in 1Q24. The Company's operating profit declined 13.4% YOY to AED 89 Mn in 1Q24. EBITDA declined 3.9% YOY to AED 151 Mn in 1Q24, whereas the EBITDA margin rose 151 bps YOY to 19.3% in 1Q24. Impairments declined from AED 6 Mn in 1Q23 to AED 5 Mn in 1Q24 due to lower impairments

### Stock Information

Market Cap (AED, mm)	2,504.13
Paid Up Capital (mm)	993.70
52 Week High	2.97
52 Week Low	2.37
3M Avg. daily value (AED)	2,002,420

### 1Q24 Result Review (AED, mm)

Total Assets	5,342
Total Liabilities	3,026
Total Equity	2,317
EBITDA	151
Net Profit	58

### Financial Ratios

Dividend Yield (12m)	7.94
Dividend Pay-out (%)	34.15
Price-Earnings Ratio(x)	9.04
Price-to-Book Ratio (x)	1.14
Book Value (AED)	2.20
Return-on Equity (%)	12.77

### Stock Performance

5 Days	-1.56%
1 Months	-6.32%
3 Months	-10.32%
6 Months	0.80%
1 Year	-3.45%
Month to Date (MTD%)	-8.70%
Quarter to Date (QTD%)	-10.00%
Year to Date (YTD%)	-5.62%

loss on trade receivables. Other income grew from AED 15 Mn in 1Q23 to AED 19 Mn in 1Q24. Moreover, finance cost grew 24.8% YOY to AED 36 Mn in 1Q24. Furthermore, tax expenses grew from AED 5 Mn in 1Q23 to AED 11 Mn in 1Q24, mainly due to the introduction of UAE corporate tax. In addition, the share of profit attributable to non-controlling interest holders declined 20.9% YOY to AED 5 Mn in 1Q24.

### Balance Sheet Highlights

RAKCEC's gross debt declined marginally from AED 1,699 Mn in 4Q23 to AED 1,672 Mn in 1Q24. Net debt declined from AED 1,418 Mn in 4Q23 to AED 1,364 Mn in 1Q24. Net debt to EBITDA ratio also declined from 2.2x in 4Q23 to 2.1x in 1Q24. Cash and cash equivalents along with bank deposits grew from AED 281 Mn in 4Q23 to AED 308 Mn in 1Q24. The Company's capex declined from AED 91 Mn in 4Q23 to AED 35 Mn in 1Q24. However, the Company expects the capex to range between AED 300-350 Mn in 2024. The Company's net cash flow from operations grew from AED 38 Mn in 1Q23 to AED 139 Mn in 1Q24.

### Target Price and Rating

We maintain our BUY rating on RAK Ceramics PJSC with an unchanged target price of AED 3.80. Despite challenging macroeconomic conditions, market volatility, and high interest rates, the Company managed to maintain its gross and EBITDA margins in 1Q24. The Company's gross and EBITDA margins grew 68 bps YOY and 151 bps YOY to 39.3% and 19.3%, respectively, in 1Q24. The Company continues to focus on enhancing its brand positioning and customer experience by expanding its retail presence, increasing its distribution network, engaging in international exhibitions, and introducing distinct product offerings. In addition, along with refurbishing various showrooms in the UAE, the Company expanded its reach by establishing new outlets in India, Bangladesh, and Saudi Arabia while strengthening its network of dealers. In India, the upgrade to the Tiles plant in Gris has commenced, and is expected to start the production of GVT tiles from 2Q24. In Bangladesh, the Company has made substantial improvements to its tiles plant, focusing on increasing production capacity and introducing large-format tiles. In UAE, the Company successfully finished the Tableware expansion project and added 10 Mn of capacity. It intends to scale up production further in successive phases. The expansion and refurbishing of existing and new plants are anticipated to meet growing demand and help the Company boost its market share in key regions. The Company also plans to start its greenfield projects in Bangladesh and KSA. RAKCEC aims to incur a capex of AED 300-350 Mn during 2024, led by its expansion projects. The Company also trades at an attractive dividend yield of 7.9% in 2024. Thus, based on the above-mentioned factors, we maintain our BUY rating on the stock.

### RAK Ceramics - Relative valuation

(at CMP)	2019	2020	2021	2022	2023	2024F
PE (x)	15.5	NA	10.3	8.4	8.7	7.1
PB (x)	1.0	1.2	1.1	1.2	1.1	1.1
EV/EBITDA	8.6	11.2	7.5	6.9	6.3	5.7
Dividend yield	5.7%	3.0%	7.9%	7.9%	7.9%	7.9%

FABS Estimates & Co Data

**RAK Ceramics – P&L**

AED mm	1Q23	4Q23	1Q24	1Q24F	Var.	YOY Ch	QOQ Ch	2023	2024F	Change
Revenue	882	866	782	886	-11.8%	-11.4%	-9.8%	3,458	3,680	6.4%
Direct costs	-541	-539	-474	-545	-13.0%	-12.4%	-12.0%	-2,149	-2,321	8.0%
<b>Gross profit</b>	<b>341</b>	<b>327</b>	<b>307</b>	<b>341</b>	<b>-9.8%</b>	<b>-9.9%</b>	<b>-6.1%</b>	<b>1,309</b>	<b>1,359</b>	<b>3.8%</b>
Selling & overhead exp.	-238	-239	-218	-211	3.5%	-8.4%	-8.5%	-930	-857	-7.8%
<b>EBITDA</b>	<b>157</b>	<b>166</b>	<b>151</b>	<b>182</b>	<b>-17.0%</b>	<b>-3.9%</b>	<b>-9.1%</b>	<b>647</b>	<b>708</b>	<b>9.3%</b>
D&A charges	50	50	51	52	-2.2%	0.1%	2.0%	195	207	6.0%
<b>Operating profit</b>	<b>103</b>	<b>89</b>	<b>89</b>	<b>130</b>	<b>-31.5%</b>	<b>-13.4%</b>	<b>0.4%</b>	<b>379</b>	<b>501</b>	<b>32.3%</b>
Impairment	-6	-15	-5	-9	-41.5%	-12.5%	-66.3%	-37	-32	-11.8%
Other income	15	47	19	22	-12.6%	28.7%	-58.8%	119	110	-7.1%
Investment & other inc.	2	-3	7	1	NM	NM	NM	7	4	-38.1%
Financial charges	-29	-27	-36	-26	37.5%	24.8%	32.1%	-119	-104	-13.0%
<b>Profit before tax</b>	<b>85</b>	<b>88</b>	<b>74</b>	<b>118</b>	<b>-37.1%</b>	<b>-13.1%</b>	<b>-16.3%</b>	<b>345</b>	<b>477</b>	<b>38.0%</b>
Tax expense	-5	-7	-11	-19	-43.0%	120.7%	67.3%	-25	-77	NM
<b>Profit before minorities</b>	<b>80</b>	<b>82</b>	<b>63</b>	<b>98</b>	<b>-35.9%</b>	<b>-21.5%</b>	<b>-23.1%</b>	<b>321</b>	<b>400</b>	<b>24.6%</b>
Minorities	7	11	5	11	-50.7%	-20.9%	-51.1%	30	43	43.5%
<b>Profit to shareholders</b>	<b>73</b>	<b>71</b>	<b>58</b>	<b>87</b>	<b>-34.1%</b>	<b>-21.5%</b>	<b>-18.8%</b>	<b>291</b>	<b>357</b>	<b>22.7%</b>

FABS estimate & Co Data

**RAK Ceramics - Margins**

	1Q23	4Q23	1Q24	YOY Ch	QOQ Ch	2023	2024F	Change
Gross margin	38.7%	37.8%	39.3%	68	155	37.9%	36.9%	-93
Operating margin	11.7%	10.3%	11.4%	-26	115	11.0%	13.6%	266
EBITDA margin	17.8%	19.2%	19.3%	151	15	18.7%	19.2%	51
Net profit margin	8.3%	8.2%	7.4%	-95	-82	8.4%	9.7%	129

FABS estimate & Co Data

## Valuation:

We use Discounted Free Cash Flow (DCF) and Relative Valuation (RV) to value RAK Ceramics. We have assigned 70% weight to DCF and 30% to RV.

Valuation Method	Target	Weight	Weighted Value
DCF Method	3.36	70.0%	2.35
Relative Valuation (RV)	4.83	30.0%	1.45
<b>Weighted Average Valuation (AED)</b>			<b>3.80</b>
Current market price (AED)			2.52
Upside/Downside (%)			+51%

### 1) DCF Method:

Rak Ceramics is valued using free cash flow to the firm. We have discounted the cash flow using the weighted average cost of capital of 8.2%. It is arrived after using cost of equity of 9.2% and after-tax cost of debt of 5.9% with a debt-to-equity ratio of 53.6%. Cost of equity is calculated by using 10-year government bond yield of 5.3%, beta of 1.00 and equity risk premium of 3.9%. Government bond yield is calculated after adding Abu Dhabi 10-year spread over 10-year US risk-free rate. Cost of debt of 5.9% is calculated after adjusting a tax rate of 7.1%. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (AED, Mn)	816
Terminal value (AED, Mn)	4,121
<b>FV to Common shareholders (AED, Mn)</b>	<b>3,342</b>
No. of share (Mn)	994
Current Market Price (AED)	2.52
<b>Fair Value per share (AED)</b>	<b>3.36</b>

### DCF Method

(All Figures in AED Mn)	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E
NOPAT	465	363	407	446	438
D&A	207	218	228	241	242
Change in working capital	-118	-192	-264	-216	-218
(-) Capex	-350	-275	-200	-200	-100
<b>Free Cash Flow to Firm (FCFF)</b>	<b>128</b>	<b>115</b>	<b>171</b>	<b>271</b>	<b>362</b>
Discounting Factor	0.95	0.88	0.81	0.75	0.69
<b>Discounted FCFF</b>	<b>121</b>	<b>101</b>	<b>139</b>	<b>203</b>	<b>251</b>

Source: FAB Securities

## 2) Relative Valuation:

We have used local as well as international peers to value Rak Ceramics and it is valued using the 2024 EV/EBITDA multiple. We have applied a discount to the peer valuation as there is only one regional peer listed and we choose to value it in line with its multiple. It is valued at EV/EBITDA of 9.0x compared to a peer valuation of 12.9x.

Company	Market (USD Mn)	EV/EBITDA (x)		P/E (x)	
		2024F	2025F	2024F	2025F
Somany Ceramics Limited	355	9.3	10.7	25.1	22.0
Saudi Ceramic Company	790	12.9	10.5	26.2	17.5
Kajaria Ceramic Tiles	2,370	26.3	24.0	43.7	39.6
Dynasty Ceramic	498	8.9	8.1	14.1	13.2
Cera Sanitaryware Limited	1,100	30.0	24.9	36.9	34.3
<b>Average</b>		<b>17.5x</b>	<b>15.6x</b>	<b>29.2x</b>	<b>25.3x</b>
<b>Median</b>		<b>12.9x</b>	<b>10.7x</b>	<b>26.2x</b>	<b>22.0x</b>
<b>Max</b>		<b>26.3x</b>	<b>24.0x</b>	<b>36.9x</b>	<b>34.3x</b>
<b>Min</b>		<b>9.3x</b>	<b>10.5x</b>	<b>25.1x</b>	<b>17.5x</b>

Source: FAB Securities

