

## RAK Ceramics (RAKCEC)

Ongoing geopolitical tensions and higher freight costs impacted profit

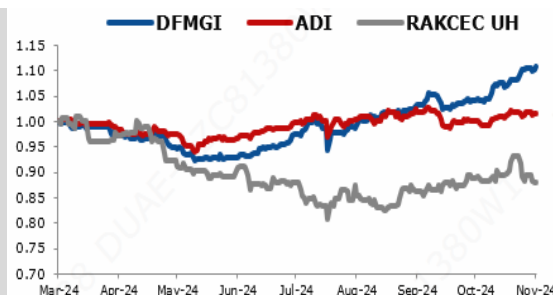
**Current Price**  
AED 2.45

**Target Price**  
AED 3.55

**Upside/Downside (%)**  
+45%

**Rating**  
BUY

- Revenue fell 4.1% YOY to AED 803 Mn in 3Q24 due to ongoing geopolitical tension, market volatility, higher interest rates, political unrest in Bangladesh and currency devaluation.
- Gross margins grew 247 bps YOY to 41.2% in 3Q24 due to favorable product mix.
- Company plans to invest in the production of large format tiles in UAE to produce differentiated premium products.
- The custom duty exemption in KSA on imports from UAE is expected to yield improvement in KSA revenues and profitability.
- Crises in the Red Sea impacted freight costs which impacted profit.
- Expect to incur a lower capex of AED 200 Mn in 2024 compared to AED 250 Mn estimated earlier.



### 3Q24 Net Profit lower than our estimate

RAK Ceramics PJSC (RAKCEC/"The Company") reported a 29.2% YOY decline in net profit to AED 54 Mn in 3Q24, falling short of our estimate of AED 60 Mn. The decline in net profit is primarily due to lower revenue resulting from ongoing geopolitical instability, supply chain disruptions and economic slowdown, lower other income along with higher freight costs, impairment loss and introduction of the corporate tax in UAE.

### P&L Highlights

RAKCEC's revenue declined 4.1% YOY to AED 803 Mn in 3Q24 mainly due to ongoing geopolitical tension, market volatility, high inflation and supply chain disruption which continued to affect export-driven industries. Tiles segment revenue dropped 1.5% YOY to AED 468 Mn in 3Q24, mainly driven by lower volumes across India, Bangladesh and European markets except the UAE. Sanitaryware segment revenue declined 4.5% YOY to AED 118 Mn in 3Q24, owing to a decline in revenue in Europe and Bangladesh markets. The Company major markets struggled with lower demand triggered from weak geopolitical conflicts. Furthermore, Tableware revenue fell 7.8% YOY to AED 85 Mn in 3Q24 due to overall slowdown in demand and a fall in new hotel projects owing to geopolitical conflicts. In addition, the supply chain issues along with currency depreciation in Egypt and Bangladesh also impacted the revenues of the segment. The Faucets segment's revenue decreased 5.3% YOY to AED 108.8 Mn in 3Q24, mainly attributed to a weak demand in Europe, slowdown in real estate sector in China and fall in employment rate in China along with new sanctions levied on Russia. The Company's direct costs declined faster than revenue and fell 8.0% YOY to AED 472 Mn in 3Q24, thereby resulting in 2.0% YOY increase in gross profit to AED 331 Mn. The decline in cost is mainly attributed to a decline in the cost of raw

### Stock Information

Market Cap (AED, mn)	2,434.57
Paid Up Capital (mn)	993.70
52 Week High	2.97
52 Week Low	2.23
3M Avg. daily value (AED)	792,776

### 3Q24 Result Review (AED, mn)

Total Assets	5,297
Total Liabilities	3,037
Total Equity	2,260
EBITDA	146
Net Profit	54

### Financial Ratios

Dividend Yield (12m)	8.16
Dividend Pay-out (%)	34.15
Price-Earnings Ratio(x)	10.37
Price-to-Book Ratio (x)	1.12
Book Value (AED)	2.18
Return on Equity (%)	10.77

### Stock Performance

5 Days	0.41%
1 Months	0.00%
3 Months	4.26%
6 Months	-2.39%
1 Year	-3.16%
Month to Date (MTD%)	-2.00%
Quarter to Date (QTD%)	2.08%
Year to Date (YTD%)	-8.24%

material consumer partially offset by an increase in an increase in repairs & maintenance and D&A expenses. Gross profit margin improved 247 bps YOY to 41.2% in 3Q24, primarily due to the combined impact of lower natural gas prices in the UAE and higher revenue in the UAE. Gross profit margins of the Tiles segment increased 350 bps YOY at 42.5% in 3Q24. Also, the Sanitaryware segment gross profit margin improved by 200 bps YOY to 33.8% in 3Q24 due to better cost efficiency and improved product mix. Tableware's margin also improved 270 bps YOY to 52.7% in 3Q24 due to product premiumization and change in product mix. Gross profit margin of the Faucets segment fell 350 bps YOY to 28.9% in 3Q24. Operating expenses increased 7.0% YOY to AED 246 Mn in 3Q24 due to higher variable expenses on freight rate and increased expenses on staff cost & advertisement expenses. The Company's operating profit declined 10.1% YOY to AED 85 Mn in 3Q24. RAK Ceramic's EBITDA fell 13.6% YOY to AED 146 Mn in 3Q24, with a 200 bps YOY decline in EBITDA margin to 18.2%. Impairments rose from AED 8 Mn in 3Q23 to AED 11 Mn in 3Q24. Other income decreased 39.5% YOY to AED 22 Mn in 3Q24 due to loss on disposal of PPE and nil write-back of unclaimed business. RAKCEC's income from investments and other sources rose from AED 2 Mn in 3Q23 to AED 5 Mn in 3Q24. Additionally, finance costs increased 15.1% YOY to AED 37 Mn in 3Q24. Tax expenses decreased from AED 8 Mn in 3Q23 to AED 5 Mn in 3Q24 mainly due to lower profit. Furthermore, the profit attributable to non-controlling interest holders fell from AED 7 Mn in 3Q23 to AED 1 Mn in 3Q24.

### Balance Sheet Highlights

RAKCEC's gross debt remained stable AED 1.75 Bn in 3Q24 compared to 2Q24. Net debt also remained marginally flat at AED 1.56 Bn in 3Q24 versus AED 1.55 Bn in 2Q24. The net debt to EBITDA ratio grew from 2.5x in 2Q24 to 2.6x in 3Q24 due to lower LTM EBITDA. Cash and cash equivalents including bank deposits fell to AED 184 Mn in 3Q24 from AED 202 Mn in 2Q24. The Company's capex reduced from AED 62 Mn in 2Q24 to AED 35 Mn in 3Q24 and the company has guided CapEx of AED 200 Mn for 2024. RAK Ceramic's net cash flow from operations decreased from AED 188 Mn in 3Q23 to AED 143 Mn in 3Q24 due to investment in working capital of AED 24 Mn in 3Q24 compared to positive cash generated from working capital in 3Q23. RAKCEC's working capital declined by AED 17 Mn to AED 1.54 Bn in 3Q24 due to an increase in payables.

### Target Price and Rating

We maintain our BUY rating on RAK Ceramics PJSC with a revised target price of AED 3.55. RAKCEC's performance was impacted in 3Q24 due to ongoing geopolitical challenges which impacted exports, however, the performance in UAE remained resilient backed by growth in the real estate sector and growing tourism. It also continued to face challenging business conditions in all markets except UAE. Despite all this, the Company's gross margin improved 250 bps YOY to 41.2% in 3Q24 due to a favourable product mix in the majority of the markets. While the EBITDA margin fell due to higher freight and salary costs. Rak Ceramics plans to introduce premium products to support retail and project channels allowing it to maintain margin and avoid engaging in the price war. The Company continues to focus on protecting market share by enhancing production capabilities, optimizing operations, strengthening retail presence, creating brand awareness in key markets, and accelerating digitization to make data-driven decisions. RAKCEC expects to invest in the production of differentiated large format tiles in UAE by converting some parts of its ceramic lines to higher demanded porcelain lines. In addition, it plans to enter into partnerships with reputed developers across the UAE to supply tiles, sanitaryware and faucets for their projects. The Company also plans to undertake similar initiatives in KSA by strengthening its sales team. It also plans to grow its retail presence across markets to showcase the products and boost the top line. Furthermore, the Company is also working towards establishing a greenfield production facility in KSA. In the European market, the company implemented initiatives to strengthen brand awareness among architects and designers through events and engagement activities along with the opening of new design centres in Germany and Spain in H1FY25. Besides, it aims to focus on increasing sales of premium products in KSA to maintain its margins. The company expects the recent exemption in customs duty on exports from UAE into KSA to positively impact the revenue of KSA. The recent rate cuts across its key markets are expected to improve the credit conditions positively benefitting the company. RAKCEC expect Faucets margin to improve in the next year owing to the relocation of the manufacturing footprint. It aims to incur a capex of AED 200 Mn during 2024. Thus, based on the above-mentioned reasons, we maintain our BUY rating on the stock.

**RAK Ceramics - Relative valuation**

(at CMP)	2019	2020	2021	2022	2023	2024F
PE (x)	14.8	NA	9.9	8.0	8.4	10.8
PB (x)	1.0	1.1	1.1	1.1	1.1	1.1
EV/EBITDA	8.4	10.9	7.2	6.7	6.2	7.6
Dividend yield	5.8%	3.1%	8.2%	8.2%	8.2%	8.2%

*FABS Estimates & Co Data*
**RAK Ceramics – P&L**

AED mn	3Q23	2Q24	3Q24	3Q24F	VAR	YOY Ch	QOQ Ch	2023	2024F	Change
Revenue	837	777	803	779	3.0%	-4.1%	3.3%	3,458	3,178	-8.1%
Direct costs	-513	-470	-472	-475	-0.7%	-8.0%	0.4%	-2,149	-1,903	-11.5%
<b>Gross profit</b>	<b>324</b>	<b>307</b>	<b>331</b>	<b>304</b>	<b>8.7%</b>	<b>2.0%</b>	<b>7.6%</b>	<b>1,309</b>	<b>1,275</b>	<b>-2.6%</b>
Selling & overhead exp.	-230	-227	-246	-221	10.9%	7.0%	8.0%	-930	-939	1.0%
<b>EBITDA</b>	<b>169</b>	<b>137</b>	<b>146</b>	<b>151</b>	<b>-3.2%</b>	<b>-13.6%</b>	<b>6.7%</b>	<b>647</b>	<b>538</b>	<b>-16.9%</b>
D&A charges	50	50	53	51	3.7%	6.8%	6.7%	195	202	3.5%
<b>Operating profit</b>	<b>95</b>	<b>80</b>	<b>85</b>	<b>83</b>	<b>2.6%</b>	<b>-10.1%</b>	<b>6.6%</b>	<b>379</b>	<b>336</b>	<b>-11.3%</b>
Impairment	-8	-7	-11	0	NM	<b>37.4%</b>	57.3%	-37	-24	-35.1%
Other income	36	17	22	19	10.7%	-39.5%	23.9%	119	76	-35.8%
Investment & other inc.	2	2	5	1	273.3%	NM	176.7%	7	19	178.6%
Financial charges	-32	-31	-37	-31	16.8%	15.1%	17.2%	-119	-134	12.9%
<b>Profit before tax</b>	<b>92</b>	<b>60</b>	<b>61</b>	<b>74</b>	<b>-17.3%</b>	<b>-33.8%</b>	<b>1.8%</b>	<b>345</b>	<b>266</b>	<b>-23.0%</b>
Tax expense	-8	-9	-5	-11	-54.9%	-38.8%	-44.0%	-25	-32	NM
<b>Profit before minorities</b>	<b>84</b>	<b>51</b>	<b>56</b>	<b>63</b>	<b>-10.7%</b>	<b>-33.3%</b>	<b>9.6%</b>	<b>321</b>	<b>234</b>	<b>-27.0%</b>
Minorities	7	1	1	3	-53.2%	-79.1%	93.8%	30	9	-68.9%
<b>Profit to shareholders</b>	<b>77</b>	<b>50</b>	<b>54</b>	<b>60</b>	<b>-8.5%</b>	<b>-29.2%</b>	<b>8.4%</b>	<b>291</b>	<b>225</b>	<b>-22.7%</b>

*FABS estimate & Co Data*
**RAK Ceramics - Margins**

	3Q23	2Q24	3Q24	YOY Ch	QOQ Ch	2023	2024F	Change
Gross margin	38.8%	39.6%	41.2%	247	167	37.9%	40.1%	227
Operating margin	11.3%	10.3%	10.6%	-70	34	11.0%	10.6%	-38
EBITDA margin	20.2%	17.6%	18.2%	-200	59	18.7%	16.9%	-179
Net profit margin	9.2%	6.5%	6.8%	-241	32	8.4%	7.1%	-134

*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	3.72	70.0%	2.60
Relative Valuation (RV)	3.16	30.0%	0.95
<b>Weighted Average Valuation (AED)</b>			<b>3.55</b>
Current market price (AED)			2.45
Upside/Downside (%)			+45%

### 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 8.0%. It is arrived after using cost of equity of 9.3% and after-tax cost of debt of 5.6% with a debt-to-equity ratio of 71.9%. Cost of equity is calculated by using 10-year government bond yield of 4.9%, beta of 1.00 and equity risk premium of 4.4%. Government bond yield is calculated after adding Abu Dhabi 10-year spread over 10-year US risk-free rate. Cost of debt of 5.6% is calculated after adjusting a tax rate of 12.0%. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (AED, Mn)	978
Terminal value (AED, Mn)	4,466
<b>FV to Common shareholders (AED, Mn)</b>	<b>3,697</b>
No. of share (Mn)	994
Current Market Price (AED)	2.45
<b>Fair Value per share (AED)</b>	<b>3.72</b>

### DCF Method

(All Figures in AED Mn)	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E
NOPAT	296	304	310	327	348
D&A	201	211	219	225	225
Change in working capital	-44	-104	-20	-17	-9
(-) Capex	-200	-275	-200	-200	-200
<b>Free Cash Flow to Firm (FCFF)</b>	<b>253</b>	<b>136</b>	<b>309</b>	<b>336</b>	<b>364</b>
Discounting Factor	0.99	0.92	0.85	0.79	0.73
<b>Discounted FCFF</b>	<b>63</b>	<b>125</b>	<b>262</b>	<b>264</b>	<b>265</b>

Source: FAB Securities

## 2) Relative Valuation:

We have used local and global peers to value Rak Ceramics, which is valued using the 2024 EV/ EBITDA multiple. It is valued at an EV/EBITDA of 9.1x compared to a peer median valuation of 13.0x. Historically, the Company traded at a forward 10-year average EV/EBITDA multiple of 7.5x.

Company	Market (USD Mn)	EV/EBITDA (x)		P/E (x)	
		2024F	2025F	2024F	2025F
Somany Ceramics Limited	303	11.5	9.5	24.1	17.2
Kajaria Ceramic Tiles	2,148	24.4	20.2	40.8	32.5
Dynasty Ceramic	486	9.3	8.8	14.8	13.7
Cera Sanitaryware Limited	1,060	27.6	23.0	36.6	31.6
Bawan Company	776	13.1	12.5	23.1	20.2
Brickworks Limited	2,585	12.9	11.8	20.4	15.9
<b>Average</b>		<b>16.4x</b>	<b>14.3x</b>	<b>26.6x</b>	<b>21.9x</b>
<b>Median</b>		<b>13.0x</b>	<b>12.1x</b>	<b>23.6x</b>	<b>18.7x</b>
<b>Max</b>		<b>21.5x</b>	<b>18.3x</b>	<b>33.5x</b>	<b>28.8x</b>
<b>Min</b>		<b>11.8x</b>	<b>10.1x</b>	<b>21.1x</b>	<b>16.2x</b>

Source: FAB Securities

### Research Rating Methodology:

Rating	Upside/Downside potential
BUY	Higher than +15%
ACCUMULATE	Between +10% to +15%
HOLD	Lower than +10% to -5%
REDUCE	Between -5% to -15%
SELL	Lower than -15%

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