

RAK Ceramics PJSC

Steady profitability despite challenging macroeconomic conditions

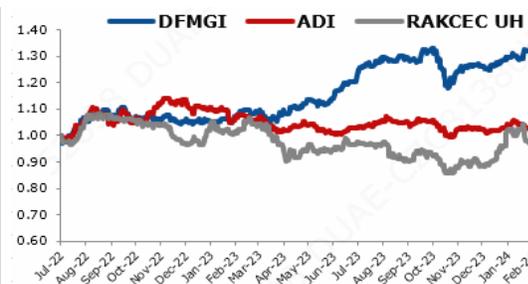
Current Price
AED 2.71

Target Price
AED 3.80

Upside/Downside (%)
+40%

Rating
BUY

- RAKCEC capex increased 33.4% to AED 273.4 Mn in 2023. While the 2024 capex guidance of the Company stood at AED 300-350 Mn
- RAKCEC EBITDA increased 20.7% YOY to AED 166 Mn in 4Q23, while the EBITDA margin rose 390 bps YOY to 19.2% in 4Q23
- RAKCEC borrowings declined from AED 1,736 Mn in 4Q22 to AED 1,699 Mn in 4Q23, while net debt increased 9.3% to AED 1,418 Mn in 4Q23
- The board proposed a cash dividend of 10 fils per share for 2H23 in addition to a dividend of 10 fils per share in 1H23 with an attractive dividend yield of 7.4% in 2023



4Q23 Net Profit lower than our estimate

Rak Ceramics PJSC (RAKCEC/"The Company") net profit marginally rose 1.4% YOY to AED 71 Mn in 4Q23, slightly lower than our estimate of AED 75 Mn. The increase in net profit is primarily attributable to a reduction in direct cost and operating expenses coupled with a rise in other income partially offset by a decline in revenue, higher tax expense, and NCI share.

P&L Highlights

RAKCEC revenue declined 3.8% YOY to AED 866 Mn in 3Q23 mainly due to challenging macroeconomic conditions, rising geopolitical tension, market volatility, currency devaluation, and rising interest rates across core markets. The Company's tiles revenue declined 6.6% YOY to AED 494 Mn in 4Q23 attributable to a rise in competition from local peers and increased imports from India that affected the growth in core markets of the Middle East and Saudi Arabia. The Company's sanitaryware revenue grew 2.9% YOY to AED 126 Mn in 4Q23, primarily due to UAE and the Middle East expansion. However, tableware revenue increased 12.3% YOY to AED 110 Mn in 4Q23 owing to enhanced production capacity and innovative product offerings. Faucets' segment revenue declined 9.8% YOY to AED 113 Mn in 4Q23 owing to a decline in sales from European markets mainly due to challenging macroeconomic conditions. The Company's direct cost declined 1.9% YOY to AED 532 Mn in 4Q23 mainly due to a decline in raw material cost and higher changes in inventories. As a result, gross profit declined marginally 6.7% YOY to AED 334 Mn in 4Q23. On the other hand, operating expenses declined 19.8% YOY to AED 245 Mn in 4Q23, mainly due to lower advertisement and staff cost. As a result, operating profit grew 69.5% YOY to AED 89 Mn in 4Q23. EBITDA increased 20.7% YOY to AED 166 Mn in 4Q23 whereas the EBITDA margin rose 390 bps YOY to 19.2% in 4Q23.

Stock Information

Market Cap (AED, mm)	2,692.94
Paid Up Capital (mm)	993.70
52 Week High	3.00
52 Week Low	2.37
3M Avg. daily value (AED)	1,784,987

4Q23 Result Review (AED, mm)

Total Assets	5,357
Total Liabilities	2,988
Total Equity	2,369
EBITDA	166
Net Profit	71

Financial Ratios

Dividend Yield (12m)	7.38
Dividend Pay-out (%)	34.15
Price-Earnings Ratio(x)	9.55
Price-to-Book Ratio (x)	1.23
Book Value (AED)	2.25
Return-on Equity (%)	13.23

Stock Performance

5 Days	1.88%
1 Months	-2.52%
3 Months	8.40%
6 Months	5.86%
1 Year	-4.91%
Month to Date (MTD%)	0.37%
Quarter to Date (QTD%)	1.50%
Year to Date (YTD%)	1.50%

Impairments grew from AED 4 Mn in 4Q22 to AED 15 Mn in 4Q23 due to impairment loss on other receivables. Other income rose 13.3% YOY to AED 47 Mn in 4Q23. Moreover, finance cost grew 5.2% YOY to AED 27 Mn in 4Q23 due to higher benchmark rates. Furthermore, tax expenses stood at AED 7 Mn in 4Q23 as compared to a reversal of AED 10 Mn in 4Q22. In addition, the share of profit attributable to non-controlling interest holders grew 33.8% YOY to AED 11 Mn in 4Q22.

Balance Sheet Highlights

RAKCEC borrowings declined from AED 1,736 Mn in 2022 to AED 1,699 Mn in 2023 while net debt increased 9.3% to AED 1,418 Mn in 2023. The Company maintained a net debt to EBITDA ratio of 2.2x in 2023 compared to 2.3x in 2022. Cash and cash equivalents along with bank deposits fell from AED 439 Mn in 2022 to AED 281 Mn in 2023. The Company's capex increased 33.4% to AED 273.4 Mn in 2023. Meanwhile, the 2024 capex guidance of the company stood at AED 300-350 Mn. The Company's net cash flow from operations marginally declined 0.5% to AED 507 Mn in 2023 mainly due to higher working capital.

Target Price and Rating

We maintain our BUY rating on RAK Ceramics PJSC with an unchanged target price of AED 3.80. Challenging macroeconomic conditions, market volatility, and currency devaluation mainly impacted the company's performance in 4Q23. Solid competition from local peers, coupled with increased imports from India in the Middle East affected the performance in core markets of KSA and the Middle East. High household prices and the slowdown of construction work in Europe in addition to volatile gas supply and currency devaluation in Bangladesh impacted the top line. However, RAKCEC took the initiatives to overcome these challenges by creating brand awareness, increasing dealer networks, new product launches, and leveraging brand enhancement. Furthermore, RAKCEC is upgrading its tiles production facility in India to add new designs and better production efficiency whereas the Company can now produce large format tiles in Bangladesh post the tiles plant upgrade. RAKCEC also successfully finished the Tableware expansion project and added 10 Mn pieces capacity. In addition, the approval for the Faucets Greenfield plant in Bangladesh is still pending and construction is expected to start in 2Q24. The Company aims to protect its market share, enhance production capabilities and diversify into new markets. Whereas the Company further aims to incur a capex of AED 300-350 Mn during 2024. The board proposed a cash dividend of 10 fils per share for 2H23 and 10 fils per share in 1H23, resulting in an attractive dividend yield of 7.4% in 2023. On a positive note, the Company maintained its margins despite challenging macroeconomic and business conditions. Thus, based on the above-mentioned factors, we maintain our BUY rating on the stock.

RAK Ceramics - Relative valuation

(at CMP)	2018	2019	2020	2021	2022	2023	2024F
PE (x)	14.7	16.4	NA	10.9	8.9	9.3	10.0
PB (x)	1.1	1.1	1.3	1.2	1.2	1.2	1.2
EV/EBITDA	9.8	8.9	11.6	7.8	7.1	6.6	7.5
Dividend yield	5.0%	5.3%	2.8%	7.4%	7.4%	7.4%	7.4%

FABS Estimates & Co Data

RAK Ceramics – P&L

AED mm	4Q22	3Q23	4Q23	4Q23F	Var.	YOY Ch	QOQ Ch	2022	2023	Change
Revenue	901	837	866	829	4.5%	-3.8%	3.5%	3,517	3,458	-1.7%
Direct costs	-542	-522	-532	-516	3.0%	-1.9%	1.9%	-2,196	-2,149	-2.2%
Gross profit	358	315	334	313	6.8%	-6.7%	6.1%	1,321	1,309	-0.9%
Selling & overhead exp.	-306	-220	-245	-215	14.1%	-19.8%	11.4%	-993	-930	-6.3%
EBITDA	138	169	166	140	18.5%	20.7%	-1.8%	577	647	12.2%
D&A charges	48	50	50	42	17.8%	3.9%	-0.5%	179	195	9.2%
Operating profit	52	95	89	98	-9.4%	69.5%	-6.3%	328	379	15.4%
Impairment	-4	-8	-15	-8	98.9%	274.7%	87.3%	-53	-37	-31.1%
Other income	41	36	47	31	52.5%	13.3%	31.8%	149	119	-20.3%
Investment & other inc.	2	2	-3	2	NM	NM	NM	7	7	-5.6%
Financial charges	-26	-32	-27	-31	-12.9%	5.2%	-15.1%	-93	-119	28.7%
Profit before tax	68	92	88	92	-4.0%	30.8%	-3.9%	372	345	-7.2%
Tax expense	10	-8	-7	-12	-45.8%	NM	-17.8%	-32	-25	-23.5%
Profit before minorities	78	84	82	80	2.3%	4.8%	-2.5%	340	321	-5.7%
Minorities	8	7	11	5	NM	33.8%	57.0%	37	30	-19.8%
Profit to shareholders	70	77	71	75	-4.8%	1.4%	-7.9%	303	291	-3.9%

FABS estimate & Co Data

RAK Ceramics - Margins

	4Q22	3Q23	4Q23	YOY Ch	QOQ Ch	2022	2023	Change
Gross margin	39.8%	37.6%	38.6%	-121	95	37.6%	37.9%	29
Operating margin	5.8%	11.3%	10.3%	444	-107	9.3%	11.0%	162
EBITDA margin	15.3%	20.2%	19.2%	390	-103	16.4%	18.7%	231
Net profit margin	7.8%	9.2%	8.2%	42	-101	8.6%	8.4%	-20

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	3.29	70.0%	2.31
Relative Valuation (RV)	4.97	30.0%	1.49
Weighted Average Valuation (AED)			3.80
Current market price (AED)			2.71
Upside/Downside (%)			+40%

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 8.3%. It is arrived after using cost of equity of 9.4% and after-tax cost of debt of 5.9% with a debt-to-equity ratio of 52.7%. Cost of equity is calculated by using 10-year government bond yield of 4.7%, beta of 1.00 and equity risk premium of 4.7%. Government bond yield is calculated after adding Abu Dhabi 10-year spread over 10-year US risk-free rate. Cost of debt is calculated using cost of 6.3% after adjusting a tax rate of 7.1%. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (AED, Mn)	774
Terminal value (AED, Mn)	4,152
FV to Common shareholders (AED, Mn)	3,273
No. of share (Mn)	994
Current Market Price (AED)	2.71
Fair Value per share (AED)	3.29

DCF Method

(All Figures in AED Mn)	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E
NOPAT	346	363	407	446	485
D&A	207	218	228	241	242
Change in working capital	-99	-192	-264	-216	-247
(-) Capex	-350	-275	-200	-200	-100
Free Cash Flow to Firm (FCFF)	92	114	171	270	379
Discounting Factor	0.93	0.86	0.79	0.73	0.68
Discounted FCFF	85	98	136	198	257

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 chose to value it in line with its multiple. It is valued at EV/EBITDA of 11.4x compared to a peer valuation of 13.4x.

Company	Market (USD Mn)	EV/EBITDA (x)		P/E (x)	
		2024F	2025F	2024F	2025F
Somany Ceramics Limited	343	13.4	10.5	28.5	20.1
Saudi Ceramic Company	596	13.2	NM	37.3	NM
Kajaria Ceramic Tiles	2,457	27.0	22.2	44.4	36.3
Dynasty Ceramic	496	8.3	7.4	13.9	13.0
Cera Sanitaryware Limited	1,292	30.2	25.0	42.8	35.7
Average		18.4x	16.3x	33.4x	26.3x
Median		13.4x	16.4x	37.3x	27.9x
Max		27.0x	22.9x	42.8x	35.9x
Min		13.2x	9.7x	28.5x	18.3x

Source: FAB Securities

