

Re-aligning focus on retail business...

Shankara's topline de-grew 18.6% YoY to ₹ 619.7 crore on account of sharp revenue de-growth in the channel & enterprise division. The EBITDA margin contracted 445 bps YoY to 2.7% mainly due to a sharp contraction in EBIT margins of the channel & enterprise division. Retail division EBIT margin was at 7.3% in Q4FY19 (10.8% in Q4FY18). PAT de-grew sharply by 92.5% YoY to ₹ 1.6 crore due to sharp EBITDA margin contraction.

Retail revenues de-grow 6.9% YoY in Q4FY19

Retail business revenues de-grew 6.9% YoY to ₹ 351.9 crore and contributed ~57% to overall revenues in Q4FY19. EBIT margins for this business contracted 350 bps YoY to 7.3% in Q4FY19 on account of volatility in steel prices. Shankara currently has 134 retail stores and is looking to close down six stores (~21,300 sq ft) mainly in Gujarat as the management does not see Gujarat as its strategic focus. Overall, the company reported same store sales (SSS) de-growth of <-10% in Q4FY19. Overall, in FY19, it reported 5% SSS growth. Going ahead, with Shankara aiming to increase focus on its core retail business, we expect retail revenues to grow at 15.9% CAGR to ₹ 1921.3 crore in FY19-21E.

Processing business to be partially sold

As a step towards reducing volatility in its business model through divestment in processing business, Shankara has proposed sale of partial assets (including land, building, equipment) at Chegunta unit (Hyderabad) for ₹ 69.1 crore to APL Apollo Tubes. Following this, Shankara will be left with 2.5 lakh TPA processing capacity. This will enable the company to increase its focus on its core business of retailing building products. The deal could lead to implied release of ~₹ 100 crore working capital in addition to proceeds from the sales transaction (₹ 69.1 crore). The funds are expected to be utilised partially towards debt reduction (₹ 195.1 crore as of FY19).

Valuation & Outlook

Currently, Shankara is in a correction mode. With the company consciously divesting its volatile margin processing business and increasing its focus on the high growth retail business, we believe Shankara is steadily aligning its business towards its core competency. It has also shown a marked improvement in balance sheet through improvement in WC. Its net debt to equity improved from 0.5x in FY18 to 0.38x in FY19. It should improve further with partial asset sale and release of working capital from that business. However, a recovery in the business could take a few more quarters. Hence, we have a **HOLD** recommendation on the stock with a target price of ₹ 485/share. We value its retail business at ₹ 466/share (11x FY20E EV/EBIT).



Particulars

Particulars	Amount (₹ crore)
Market Capitalization	1,119.7
Total Debt	195.1
Cash	17.5
EV	1,297.3
52 week H/L (₹)	1968 / 316
Equity capital	22.9
Face value (₹)	10.0

Key Highlights

- We expect retail revenues to grow at 15.9% CAGR to ₹ 1921.3 crore in FY19-21E
- As a step towards divestment in the processing business, Shankara has proposed sale of partial assets at Chegunta unit (Hyderabad) for ₹ 69.1 crore to APL Apollo Tubes
- Recommend **HOLD** with a target price of ₹ 485/share

Research Analyst

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Key Financial Summary

(₹ crore)	FY17	FY18	FY19E	FY20E	FY21E	CAGR FY19-21E
Net Sales	2,310.1	2,548.7	2,654.1	2,837.1	3,195.5	9.7%
EBITDA	154.4	175.2	119.4	95.5	120.1	0.3%
EBITDA Margin (%)	6.7	6.9	4.5	3.4	3.8	
Net Profit	60.3	73.8	32.7	37.3	62.8	38.5%
EPS (₹)	26.4	32.3	14.3	16.3	27.5	
P/E (x)	18.6	15.2	34.2	30.0	17.8	
EV/EBITDA (x)	8.2	7.7	10.9	13.2	9.4	
RoCE	22.9	22.7	15.1	11.8	16.0	
RoNW	15.3	16.2	6.8	7.1	10.7	

Source: Company, ICICI Direct Research

Exhibit 1: Variance Analysis

Year	Q4FY19	Q4FY18	YoY (%)	Q3FY19	QoQ(%)	Comments
Net Sales	619.7	760.8	-18.6	605.3	2.4	Topline de-grew on account of sharp revenue de-growth in channel & enterprise division
Other Income	2.2	0.0	NA	0.4	408.7	
Material Consumed	259.2	380.4	-31.9	317.5	-18.3	
Purchase of Stock in Trade	297.6	334.1	-10.9	197.6	50.6	
Other Expenses	25.4	39.9	-36.4	26.0	-2.5	
EBITDA	16.4	54.1	-69.6	23.0	-28.6	
EBITDA Margin	2.7	7.1	-446 bps	3.8	-115 bps	EBITDA margin contracted on account of sharp contraction in EBIT margins in channel & enterprise division
Depreciation	4.6	4.3	7.7	4.9	-4.7	
Interest	12.4	13.7	-9.6	15.2	-18.3	
Exceptional items	0.0	0.0	NA	0.0	NA	
PBT	1.6	36.0	-95.6	3.4	-53.4	
Taxes	0.0	14.6	-100.2	0.9	NA	
PAT	1.6	21.5	-92.5	2.5	-35.7	PAT de-grew sharply on account of sharp EBITDA margin contraction

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY18	FY19	FY20E		FY21E	Comments	
			Old	New	% Change		
Revenue	2,548.7	2,654.1	3,409.5	2,837.1	-16.8	3,195.5	We introduce FY21E estimates
EBITDA	175.2	119.4	201.9	95.5	-52.7	120.1	
EBITDA Margin (%)	6.9	4.5	5.9	3.4	-253 bps	3.8	
PAT	73.8	32.7	81.7	37.3	-54.3	62.8	
EPS (₹)	32.3	14.3	35.8	16.3	-54.3	27.5	

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

₹ crore	FY18	FY19	FY20E		FY21E	Comments
			Current	Earlier	Introduced	
Average store size (sq ft)	3,915	4,233	4,444	4,440	4,667	We introduce our FY21E estimates
Revenue per store (₹ crore)	9.5	10.7	11.8	12.8	13.0	

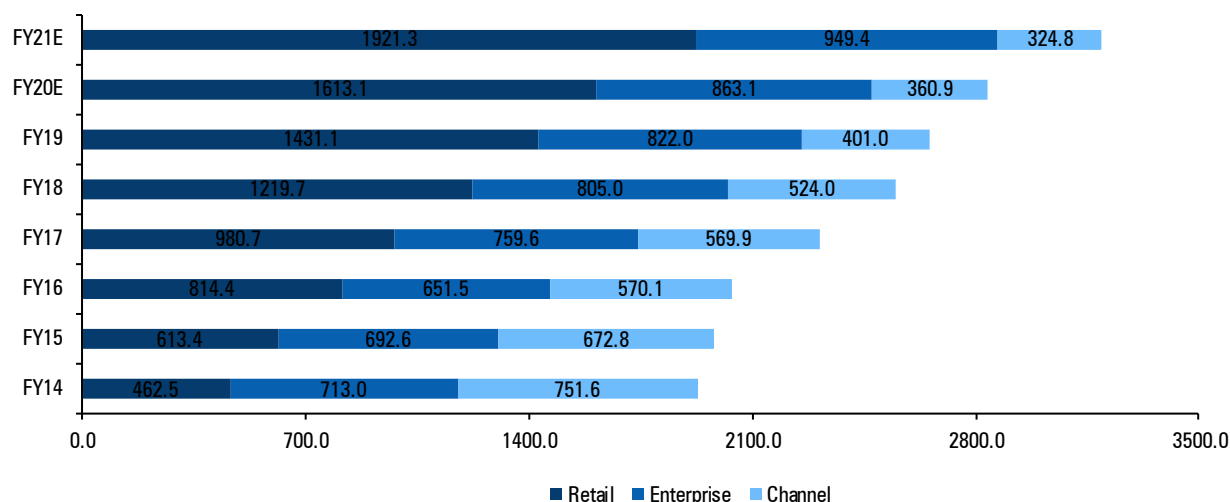
Source: Company, ICICI Direct Research

Conference Call Highlights

- **Business update:** The company has proposed a sale of partial assets (including land, building & equipment) at the Chegunta unit (Hyderabad) for ₹ 69.1 crore to APL Apollo Tubes. Upon completion of this proposed transaction, Shankara will be left with assets worth ~₹ 40 crore in Taurus. This deal will result in an implied release of working capital for the company to the tune of ~₹ 100 crore. In addition to the proceeds from the transaction (₹ 69.1 crore), this will be partially utilised towards debt reduction. This proposed transaction is in line with the company's strategy to increase focus on its core business of retailing building products that is a superior margin business with higher return on equity
- **Retail business:** Revenues from the retail business de-grew 6.9% YoY to ₹ 351.9 crore and contributed ~57% to overall revenues in Q4FY19. EBIT margins for the business segment contracted 350 bps YoY to 7.3% in Q4FY19. The management is not keen on undertaking expansion in the near term and has kept number of retail stores constant at 134 stores. Also, the company is planning to close down six stores spread over ~21,300 sq ft in Rajkot, Surat, Vadodara, Nizamabad, etc. This is because the management does not see Gujarat as its strategic focus. Going ahead, Shankara aims to focus on its core retail business that is a superior margin one with higher return on equity. The management has guided for 20% YoY growth in retail business, going ahead
- **Revenue break-up for retail business:** Construction materials contributed 60%, followed by interior & exterior products and new category business. In terms of geography, Tier-I cities contributed 45%, Tier-II cities 24% and Tier-III cities 31% in Q4FY19
- **Processing business:** In the processing business, the company clocked ₹ 7.6 crore EBITDA in Q4FY19 whereas for FY19, EBITDA was at ₹ 55.4 crore. Overall, processing margins declined 200 bps to 2.5% in Q4FY19. Following partial divestment from Taurus, the company will be left with 2.5 lakh TPA processing capacity
- **Capex:** The company has guided for ₹ 30 crore capex in FY20E
- **Same store sales growth:** The company reported same store sales (SSS) de-growth by <-10% in Q4FY19. Overall, in FY19, the company reported 5% SSS growth
- **Working capital & debt:** Net working capital days declined to 46 days in FY19 from 54 days in FY18. The company's net D/E was at 0.38 as of Q4FY19

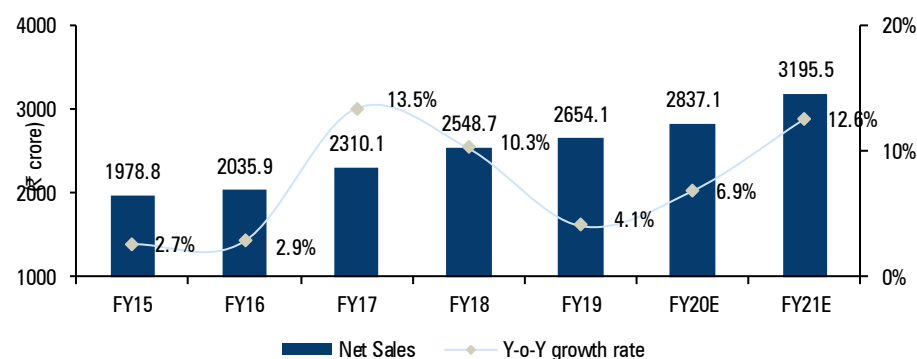
Company Analysis

Exhibit 4: Segmental revenue trend



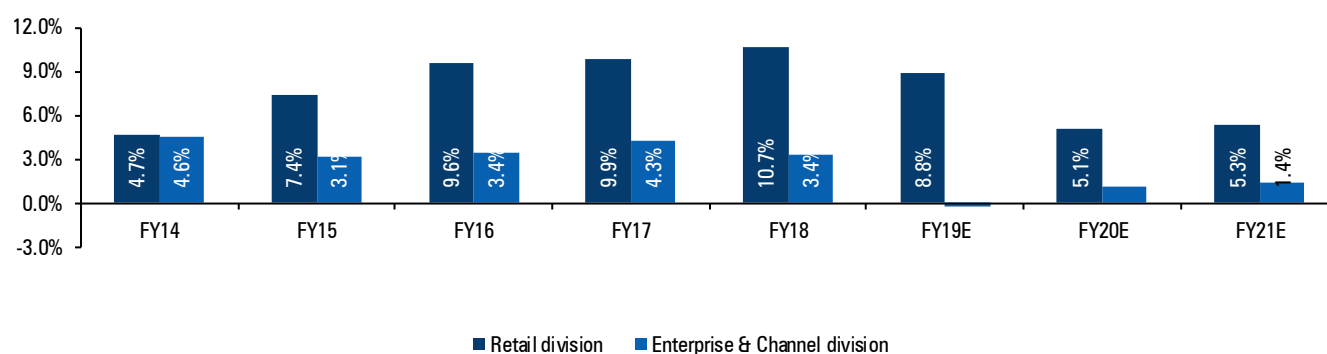
Source: Company, ICICI Direct Research

Exhibit 5: Overall revenue trend



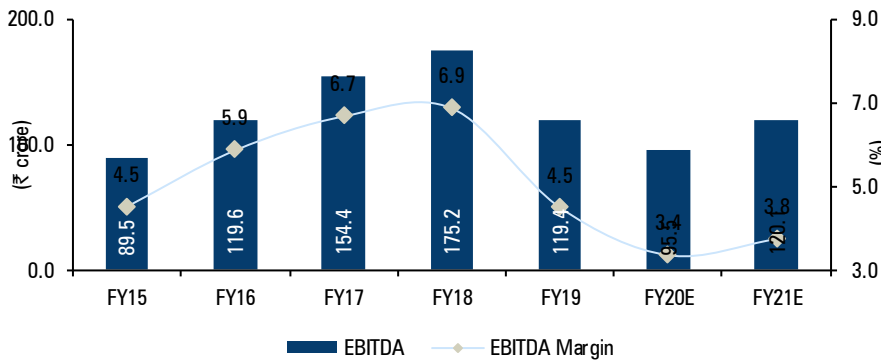
Source: Company, ICICI Direct Research

Exhibit 6: Segmental EBITDA trend



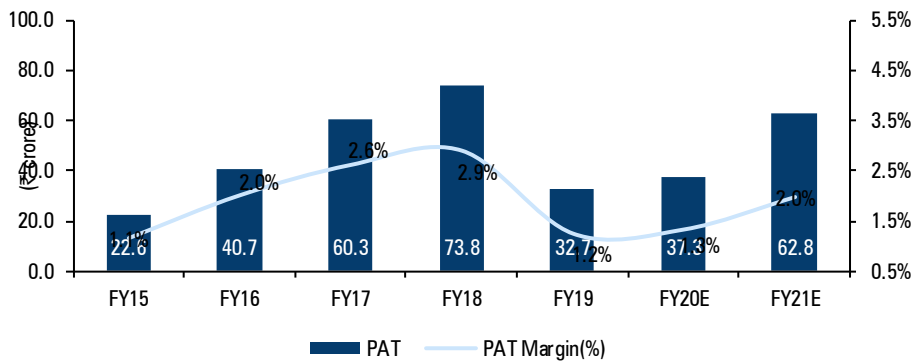
Source: Company, ICICI Direct Research

Exhibit 7: Overall EBITDA trend



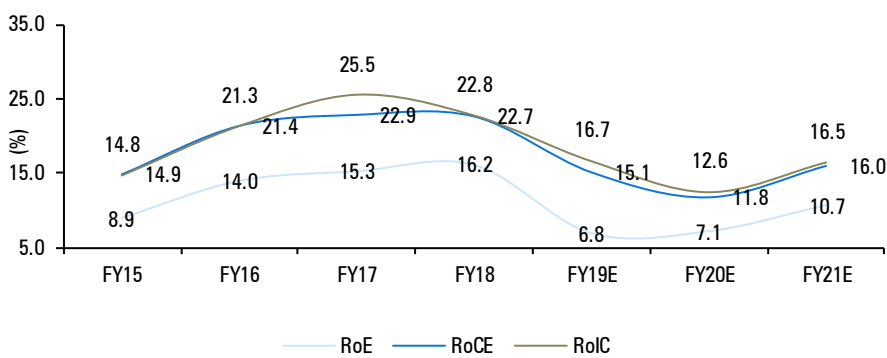
Source: Company, ICICI Direct Research

Exhibit 8: PAT trend



Source: Company, ICICI Direct Research

Exhibit 9: Return ratios trend



Source: Company, ICICI Direct Research

Valuation & Outlook

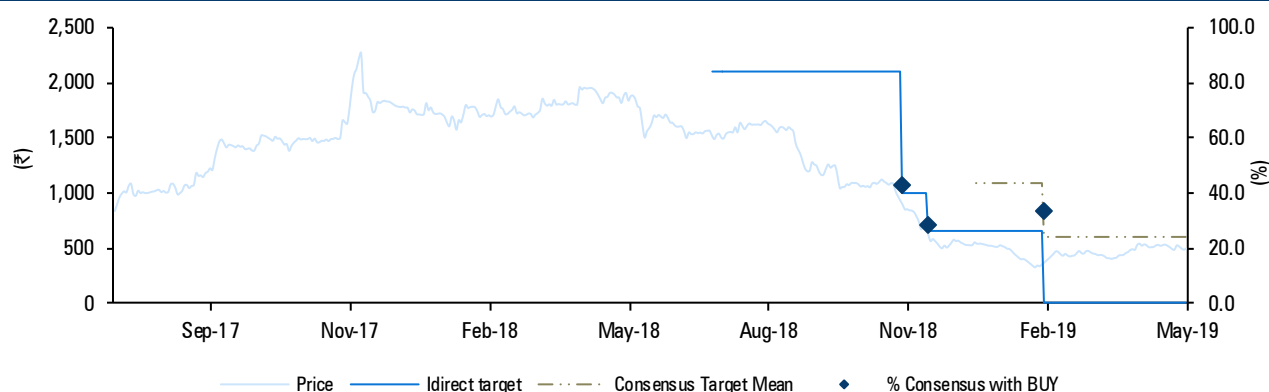
Currently, Shankara is in a corrective mode. With the company consciously divesting its volatile margin processing business and increasing its focus on the high growth retail business, we believe Shankara is steadily aligning its business towards its core competency. It has also shown a marked improvement in balance sheet through improvement in WC. Its net debt to equity improved from 0.5x in FY18 to 0.38x in FY19. It should improve further with partial asset sale and release of working capital from the business. However, recovery in the business could take a few more quarters. Hence, we have a **HOLD** recommendation on the stock with a target price of ₹ 485. We value its retails business at ₹ 466/share (11x FY20E EV/EBIT).

Exhibit 10: Valuation

Business	Method	Multiple	Basis	Valuation	₹/share
Retail	EV/EBIT	11.0	FY20E	1064.7	466
Channel & Enterprise	EV/EBIT	5.0	FY20E	183.6	80.4
Less: Net Debt				-143.6	-63
Target Valuation				1104.6	483.4
Rounded off target price					485

Source: Company, ICICI Direct Research

Exhibit 11: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 12: Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Srinivas (Sukumar)	28-Feb-19	54.8%	12.5	0.0
2	Amansa Holdings Pvt Ltd	31-Dec-18	7.5%	1.7	0.3
3	Ashoka Pte. Ltd.	31-Dec-18	7.5%	1.7	0.7
4	Franklin Templeton Asset Management (India) Pvt. Ltd.	31-Dec-18	4.2%	1.0	0.1
5	Mondrian Investment Partners Ltd.	31-Dec-18	2.3%	0.5	-0.1
6	Edelweiss Asset Management Ltd.	31-Dec-18	1.4%	0.3	0.0
7	Dimensional Fund Advisors, L.P.	31-Mar-19	0.3%	0.1	0.0
8	Ravikumar (C)	5-Jun-18	0.3%	0.1	0.1
9	Prasad (Siva)	1-Jun-18	0.3%	0.1	0.1
10	Van Eck Associates Corporation	31-Mar-19	0.3%	0.1	0.0

Source: Reuters, ICICI Direct Research

Exhibit 13: Recent Activity

Buys			Sells		
Investor name	Value (m)	Shares (m)	Investor name	Value (m)	Shares (m)
Ashoka Pte. Ltd.	5.3	0.7	Tata Asset Management Limited	-1.0	-0.1
Amansa Holdings Pvt Ltd	2.2	0.3	Mondrian Investment Partners Ltd.	-0.7	-0.1
Franklin Templeton Asset Management (India) Pvt. Ltd.	0.8	0.1	Morgan Stanley Investment Management Inc. (US)	-0.3	0.0
State Street Global Advisors (US)	0.2	0.0	India Infoline Asset Management Company Limited	-0.2	0.0
Edelweiss Asset Management Ltd.	0.1	0.0	Prusik Investment Management LLP	-0.1	0.0

Source: Reuters, ICICI Direct Research

Exhibit 14: Shareholding Pattern

(in %)	Sep-18	Dec-18	Mar-19
Promoter	56.2	56.2	56.2
Public	43.8	43.8	43.8
Others	0.0	0.0	0.0
Total	100.0	100.0	100.0

Source: Company, ICICI Direct Research

Financial summary

Exhibit 15: Profit and loss statement				
	₹ crore			
(₹ Crore)	FY18	FY19	FY20E	FY21E
Net Sales	2,548.7	2,654.1	2,837.1	3,195.5
Net Raw Material Cost	2,173.8	2,359.4	2,515.0	2,824.6
Employee benefit expenses	59.2	64.3	73.9	85.0
Power & Fuel	-	-	-	-
Consumption of stores and spares	-	-	-	-
Total operating expenditures	2,373.5	2,534.7	2,741.6	3,075.4
EBITDA	175.2	119.4	95.5	120.1
Interest	46.4	56.7	25.7	11.0
Depreciation	13.6	18.6	19.1	20.8
Other income	0.6	4.4	4.7	4.9
PBT	115.9	48.5	55.3	93.1
Taxes	42.1	15.8	18.0	30.3
Effective tax rate (%)	36.3%	32.5%	32.5%	32.5%
PAT	73.8	32.7	37.3	62.8
PAT Growth rate	22.4%	-55.6%	14.1%	68.3%
Adjusted EPS (Diluted)	32.3	14.3	16.3	27.5

Source: Company, ICICI Direct Research

Exhibit 16: Cash flow statement				
	₹ crore			
(₹ Crore)	FY18	FY19E	FY20E	FY21E
Profit after Tax	73.8	32.7	37.3	62.8
Depreciation	13.6	18.6	19.1	20.8
Interest	44.7	56.7	25.7	11.0
Taxes	42.1	15.8	18.0	30.3
Cash Flow before wc changes	176.2	119.4	95.5	120.1
Cash generated from operations	(86.0)	61.3	5.9	17.8
Income Tax paid	(49.3)	(15.8)	(18.0)	(30.3)
Net CF from operating activities	40.9	164.9	83.4	107.6
(Purchase)/Sale of Fixed Assets (Net)	(39.6)	(39.8)	(28.4)	(32.0)
Others	(35.4)	4.4	4.7	74.0
Net CF from Investing activities	(75.0)	(35.4)	(23.7)	42.0
Dividend	(7.6)	-	-	-
Interest paid	(45.9)	(56.7)	(25.7)	(11.0)
Inc / (Dec) in Loans	24.4	(47.7)	(50.3)	(100.0)
Net CF from Financing activities	33.6	(104.4)	(76.0)	(111.0)
Net Cash flow	(0.6)	25.1	(16.3)	38.6
Opening Cash	1.8	6.0	17.5	1.2
Closing Cash/ Cash Equivalent	1.2	31.1	1.2	39.7

Source: Company, ICICI Direct Research

Exhibit 17: Balance sheet				
	₹ crore			
(₹ Crore)	FY18	FY19E	FY20E	FY21E
Liabilities				
Equity Capital	22.9	22.9	22.9	22.9
Reserve and Surplus	432.9	456.2	503.0	565.8
Total Shareholders funds	455.7	479.0	525.8	588.6
Total Debt	242.8	195.1	144.8	44.8
Total Liabilities	716.1	695.3	688.4	651.2
Assets				
Gross Block	307.9	281.5	309.9	341.8
Less Acc. Dep	24.9	42.6	61.8	82.6
Net Block	283.1	238.9	248.1	259.2
Goodwill on consolidation	14.0	14.0	14.0	14.0
Total Fixed Assets	318.7	273.4	294.7	311.0
Investments	3.7	1.4	5.1	5.8
Inventory	415.7	383.0	425.6	415.4
Sundry Debtors	427.2	337.5	349.0	383.5
Loans & Advances	18.0	14.8	23.1	27.7
Cash & Bank Balances	6.0	17.5	1.2	39.7
Other Current Assets	45.1	31.5	0.1	0.1
Total Current Assets	894.0	769.5	791.7	856.6
Trade Payable	461.2	381.5	411.4	447.4
Other Current Liabilities	34.7	33.3	51.3	57.8
Provisions	0.7	2.0	10.2	17.1
Net Current Assets	397.4	352.8	318.9	334.4
Total Assets	716.2	695.3	682.6	645.4

Source: Company, ICICI Direct Research

Exhibit 18: Key ratios				
	FY18	FY19E	FY20E	FY21E
Per Share Data (₹)				
EPS - Diluted	32.3	14.3	16.3	27.5
Cash EPS	38.2	22.5	24.7	36.6
Book Value	199.4	209.6	230.1	257.6
Dividend per share	4.7	5.4	7.7	7.7
Operating Ratios (%)				
EBITDA / Net Sales	6.9	4.5	3.4	3.8
PAT / Net Sales	2.9	1.2	1.3	2.0
Inventory Days	59.5	52.7	54.8	47.5
Debtor Days	61.2	46.4	44.9	43.8
Creditor Days	66.1	52.5	52.9	51.1
Return Ratios (%)				
RoE	16.2	6.8	7.1	10.7
RoCE	22.7	15.1	11.8	16.0
RoIC	22.8	16.7	12.6	16.5
Valuation Ratios (x)				
EV / EBITDA	7.7	10.9	13.2	9.4
P/E (Diluted)	15.2	34.2	30.0	17.8
EV / Net Sales	0.5	0.5	0.4	0.4
Market Cap / Sales	0.4	0.4	0.4	0.4
Price to Book Value	2.5	2.3	2.1	1.9
Dividend Yield	1.0	1.1	1.6	1.6
Solvency Ratios (x)				
Net Debt / Equity	0.5	0.4	0.3	0.0
Debt / EBITDA	1.4	1.6	1.5	0.4
Current Ratio	1.8	1.8	1.7	1.6
Quick Ratio	1.0	0.9	0.8	0.8

Source: Company, ICICI Direct Research

Exhibit 19: ICICI Direct coverage universe (Tiles)

Sector / Company	CMP		M Cap (₹ Cr)	EPS (₹)			P/E (x)			V/EBITDA (x)			P/B (x)			RoE (%)			
	(₹)	TP(₹)		Rating	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
Shankara Building (SHABUI)	490	485	Hold	1120	14.3	16.3	27.5	34.2	30.0	17.8	10.9	13.2	9.4	2.3	2.1	1.9	6.8	7.1	10.7
Kajaria Ceramics (KAJCER)	590	680	Buy	9375	14.2	19.5	23.5	41.4	30.3	25.2	20.5	16.7	14.1	6.0	5.2	4.5	14.4	17.1	17.9
Somany Ceramics (SPLIND)	333	520	Buy	1412	26.4	18.3	18.3	18.4	26.7	26.6	10.2	13.3	12.4	3.9	3.6	3.2	21.4	13.3	12.1

Source: Company, ICICI Direct Research

RATING RATIONALE

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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