RAK Ceramics Q4&FY 2023 earnings call and webcast

Monday, 12 February 2024

Operator Welcome to RAK Ceramics fourth quarter and full year 2023 earnings call and webcast. My name is Lydia and I'll be your Operator today. If you'd like to ask a question at the Q&A, you can do so by pressing star followed by one on your telephone keypad. If you've joined online, you can type your question in the Q&A box provided. I'll now hand you over to your Arqaam host, Mohamad Haidar, to begin.

Mohamad Haidar Hello, everyone, and welcome to the RAK Ceramics fourth quarter and full year 2023 earnings call and webcast. This is Mohamad Haidar from Arqaam Capital. From RAK Ceramics we are joined today by the group CEO, Mr Abdallah Massaad, and the group CFO, Mr PK Chand. Over to you, Abdallah.

Abdallah Massaad Thank you, Mohamad. Good afternoon everyone and thank you for joining us. Welcome to RAK Ceramics fourth quarter and full year 2023 earnings conference call and webcast. I want to start off by talking about the presence of RAK Ceramics across our key markets, as well as the split between the different product divisions.

As you can see from the map on the screen, the UAE continued to be our largest market, contributing 31% of the total consolidated revenue for the group. Also, the revenue contribution share for Europe increased to 22%, supported by the addition of KLUDI offerings. As you will see on the right side, Tiles division continue to contribute the majority share of the revenue, followed by Sanitaryware, Faucets and Tableware. At the bottom you can see our production capabilities, where we continue to invest further to improve our capacity and bring in efficiencies.

Moving to the financial performance, I'm pleased to report that this year the business has continued its growth trajectory in the UAE, reporting year-on-year revenue growth of 22.3% across all product segments. Despite the strong performance in the UAE, we remain mindful of the ongoing macroeconomic challenges, increasing competition and geopolitical issues across several of our core markets.

Looking ahead, it's important to note that Saudi Arabia is currently making substantial investments in infrastructure and real estate projects, with numerous prestigious projects on the horizon. There will be a growing demand for a reputable brand and reliable supplier. Fortunately, RAK Ceramics is exceptionally well positioned in terms of our service excellence, diverse product offering and strong brand reputation. Thus, our outlook remains positive and we are well prepared to leverage these opportunities.

The Indian market continues to feel the adverse effects of rising interest rates and tight liquidity. However, we except the real estate sector to pick up momentum, as we invest in upgrading our facility and expand our dealer network. In Bangladesh our business sustained growth in local currency, despite several headwinds in the market, mainly currency devaluation and foreign currency availability.

The KLUDI products complement our product offering and provide differentiated German heritage quality to our customers, while Europe continues to be impacted from recession and slowdown in construction sector. We are optimistic to see improvement, as we continue to implement our value unlocking strategy. Our Tableware division continues to perform well, driven by factors including increased demand in and driving tourism.

We continue to monitor the recent issues in the region, specifically the ongoing situation in the Red Sea, which is affecting the supply chain dynamics. Despite these challenges, we are committed in turning these obstacles into opportunities, as we work towards brand enhancement through new showrooms and dealer network in our core market, to strengthen our revenue.

We continue to innovate our approach to ensure that we stay ahead across all the markets in which we operate. In light of the ongoing macroeconomic and geopolitical challenges, we believe these innovations are very important to allow us to stay ahead of the curve. In Europe, where high interest rates and inflation are continuing to squeeze household income, we are working with architects and designers to promote brand awareness. Similarly, in Saudi Arabia, India and Bangladesh, we are implementing several initiatives to create and enhance brand awareness.

We are pleased with the progress made so far in upgrading our Tiles production facility in both UAE and India. Also, we have finished the upgrading we are doing in Bangladesh in the Tiles sector. In the UAE we can already see the automation of some of our Tiles production facility that will allow us to shift our production capabilities from ceramic to porcelain tiles. In parallel, we continue to work towards setting up a production facility in Saudi. We are also working on increasing the production capacity in our Bangladesh plant, specifically to produce large format tiles. We have completed a significant expansion project that has added capacity for another 10 million pieces of tableware. The production scaling process will be implemented in phases.

I'm pleased to also mention that lately, we already installed a new kiln in our sanitary ware, which is considered to be the longest kiln in the industry, which will allow us to have a better quality, as well as improvement and efficiency in energy consumption. With this, I will now hand over to PK.

PK Chand Thank you, Mr Abdallah. Good evening everyone and thank you for joining us. Mr Abdallah has already briefed on the business performance highlights, key markets and strategy update for 2023. I will take you through the financial highlights for the fourth quarter of 2023 and also for the full year of 2023, with details on revenue, gross profit margin and the balance sheet. We will start from slide 11.

Total revenue experienced a marginal decrease of 1.7% to AED 3.45 billion in full year of 2023, while in the fourth quarter revenue registered a decline of 3.8% at AED 866.4 million going to macroeconomic factors. Tiles and Sanitaryware revenue is lower by 4.8% year-on-year at AED 620.6 million in the fourth quarter. In the full year of 2023 revenue decreased by 8% year-on-year to AED 2.5 billion.

Revenue in fourth quarter has been affected across all markets, except United Arab Emirates, Middle East, Bangladesh and Africa. However, the full-year revenue was impacted in all markets, except United Arab Emirates and the Middel East. Growth in UAE is largely driven by project and retail channels. Reduction in revenue in other markets is primarily attributable to continued recessionary fears and higher interest costs, which are affecting household savings and causing a deferment in major house renovation and development projects.

Tableware revenue struggled by 12.1% year-on-year at AED 110.1 million in the fourth quarter of 2023 and 11% year-on-year at AED 392 million in full year of 2023, primarily attributed to innovative product offerings and enhanced production capacity. Faucets revenue decreased by 9.8% year-on-year at AED 113.2 million in the fourth quarter of 2023. In full year of 2023 revenue is AED 456.2 million. In last year KLUDI Group consolidation was effective 1 June 2022. Revenue from other units decreased by 21.2% to AED 109.7 million in the full year of 2023, mainly due to decrease in our ceramic raw material trading business.

Now let me go through slide 14 onwards, covering the end market performance in the fourth quarter and for full year of 2023 for Tiles and Sanitaryware segments. In UAE market Tiles and Sanitaryware revenue in the fourth quarter increased by 8% year-on-year to reach 207 million, driven by the project and retail channel. In the full year of 2023 revenue grew by 17.8% year-on-year to AED 786.7 million. In Saudi Arabia Tiles and Sanitaryware revenue in the fourth quarter of 2023 witnessed a significant decline of 47% year-on-year to AED 71 million due to continued competition from local Chinese manufacturers, mainly impacting our wholesale business. However, we are well positioned in terms of our service excellence, diverse product offering and strong brand reputation. In full year of 2023 revenue decreased by 40.2% year-on-year to AED 350.3 million.

In India, revenue in the fourth quarter of 2023 decreased by 10.4% year-on-year to 91.3 million due to challenging market, mainly due to lower demand on account of increased interest rates and tight liquidity. In the face of these challenges we strategically engaged in upgrade of our facilities, market expansion, retail initiatives and product launches, to position ourselves to thrive in the dynamic Indian market. In full year of 2023 revenue decreased by 9.6% year-on-year at AED 360 million, while in local currency it decreased by 5.3% year-on-year.

In Europe revenue in the fourth quarter of 2023 decreased by 8.1% year-on-year to AED 79.2 million. This decrease is attributed to higher interest rates and persistent inflation, putting pressure on household income. However, our are under way to collaborate with architects and designers to enhance brand awareness. In full year of 2023 the revenue decreased by 6% year-on-year to AED 384.2 million.

In Bangladesh market revenue in the fourth quarter rebound by 20.3% year-on-year at AED 73.9 million. This growth was fuelled by various initiatives taken, including product differentiation and increased product awareness, and the strengthening of our retail presence through the expansion of our showroom network. In full year of 2023 the revenue decreased by 9.4% to AED 264.4 million, due to currency devaluation. However, in local currency the revenue has registered a growth of 4.8% year-on-year.

In Middle East, excluding United Arab Emirates and Saudi market, continued to face adverse effects due to ongoing geopolitical challenges. However, we have seen positive growth during the fourth quarter in projects channel. Revenue in the fourth quarter of 2023 increased by 19.8% year-on-year at AED 39.7 million. In the full year of 2023 revenue remained resilient at AED 153.6 million.

Now we will turn to slide 15. The total gross profit margin increased by 70 basis points year-on-year to 35.6% in the fourth quarter of 2023, due to higher sales in the UAE market with better margin and change in the product mix. In full year of 2023 the gross profit margin increased by 20 basis points year-on-year at 37.9% year-on-year. Tiles margin in the fourth quarter increased by 250 basis points compared to the fourth quarter in last year at 36.4%, mainly due to lower productivity on account of partial shut-down of plants in India and Bangladesh for upgrades. In full year of 2023 margin increased by 50 basis points to 38.4%.

Sanitaryware margin increased by 680 basis points year-on-year at 34% in the fourth quarter and in full year of 2023 it increased by 50 basis points at 34.2%, due to change in the product mix. Tableware gross margin increased by 140 basis points year-on-year to 47.8% in the fourth quarter, following top line increase and successful launch of new products. In the full year of 2023 the gross profit margin increased by 100 basis points year-on-year to 49.7%. Faucets gross margin increased by 480 basis points at 26% in the full year of 2023, following the results from cost optimisation initiatives.

Net profit before one-offs increased to AED 81.8 million in the fourth quarter, compared to AED 65.3 million in 2022. Last year reported net profit included a net one-off gain of AED 12.7 million towards sale of land in Australia. Margin is 9.4%, compared to 7.2% in the last year. In full year of 2023 net profit before one-offs increased by 3.7% to AED 320.9 million, compared to AED 309.3 million in the last year. Net profit margin is 9.3% compared to 8.8% in the last year. The EBITDA increased by 20.7% year-on-year to AED 166 million in the fourth quarter, compared to AED 137.5 million in the last year. EBITDA margin is 19.2% compared to 15.3% in last year. In full year of 2023 EBITDA increased by 12.2% at AED 647.4 million, compared to AED 577.2 million in last year. The margin is 18.7% compared to 16.4% in last year.

Now we will turn to balance sheet highlights on slide 18. Overall, working capital cycle increased from 146 days in the beginning of the year to 172 days in the end of 2023, mainly due to lower revenue. In absolute terms, working capital increased by AED 71 million to AED 1.48 billion in end 2023, mainly due to decrease in payables. Inventory days increased from 197 days in the beginning of the year to 221 days in the end 2023, mainly due to lower revenue. Trade receivable days increased from 84 days in the beginning of the year, to 90 days in the end of the year, mainly due to lower revenue. Net debt increased by AED 120.3 million to 1.42 billion in December 2023, compared to AED 1.30 billion in December 2022, mainly due to dividend payment of AED 221.7 million and Capex of AED 273 million. However, net debt to EBITDA decreased to 2.20 times in December 2023, compared to 2.26 times in December 2022. We continue to maintain adequate liquidity position during the year. Capital expenditure during the full year of 2023 has been AED 273 million and the Capex guidance for the full year of 2024 will be around AED 300 to 350 million.

Slide 19 shows the share price movement during the past 12 months. The shares are currently trading at P/E multiple of 8.9 times. Slide 20 shows the historical dividend payment in line with the dividend policy the board proposed to distribute semi-annual cash dividend of 10 fils per share for the second half of 2023, amounting to AED 99.4 million. This follows a previously approved and distributed semi-annual cash dividend of 10 fils per share, representing AED 99.4 million for the first half of 2023. Now I will turn back to Mr Abdallah for his final comments on 2024 priorities, before we answer your questions.

Abdallah Massaad Thank you, PK. These results reflect the hard work of our entire team and we are proud of what we have achieved in this challenging market environment. Looking ahead to 2024, we are cautiously optimistic and are closely monitoring the ongoing geopolitical scenario. We plan to build on our previous efforts, focusing on expanding our market share and we remain committed in delivering value to our customers, employees and shareholders.

With the rising competition across major markets, we are committed to protect our market share through maintaining health competition and leveraging on gross product synergies, embracing diversification and solidifying our retail business. We are also investing in our production capacity to boost productivity and efficiency, aiming for better margins. With regards to KLUDI, we continue building on a strong integration plan and transforming it into a global high-end faucet and sanitaryware brand. Thank you all for taking the time to join us for this presentation of our full year and fourth quarter results. I would like now to hand over the call to the Operator and open the line to questions.

Operator Thank you. Please press star followed by the number one if you would like to ask a question and ensure your device is unmuted locally when it's your turn to speak. If you've joined us online you can type your question in the chat box provided. Our first question comes from Sameer Kattiparambil of EFG Hermes. Please go ahead, your line is open.

Sameer Kattiparambil Thank you, PK and Abdallah, for the presentation. A couple of questions from my side. First, how do fuel and natural gas price increase in Saudi impact your operations there? Will it in any way influence your plan for a new plant?

Abdallah Massaad Sameer, as you mentioned that the gas prices in Saudi increased, for us it will not influence the decision because the Saudi market, as I mentioned, it is a big market, for sure. Today the main market is for the housing projects and the standard products, where we aim that with all the infrastructure and a lot of high-end projects which will come. 30% of Jeddah is getting prepared for rebuild and I believe with our brand and differentiating factor in terms of product offering and the brand perception, we are in the coming years a good opportunity to enter these projects. You know that the consent of Made in Saudi is very important and, therefore, it will not affect our decision.

Also, Sameer, we did not mention, but you know that we here in the UAE entered into a long-term contract and the gas prices reduced in a good way, where we have a long-term supply at a fixed price, where we will get a good saving in the UAE.

Sameer Kattiparambil Thank you, Abdallah. Just a follow-up on that. In Saudi, since your competitors are will that influence the pricing scenario in Saudi? That's the first one. Then the second one, could you remind me what's your average gas price in the UAE?

Abdallah Massaad Any increase today in prices and costs will push the market and the supplier to increase their prices. And with the increase of the prices, this will give us some, for sure. Because in this case, with our lower cost of production and the increase in gas, will reduce the delta, the difference in prices. For sure we'll not be as competitive as the prices we are offering, but we will be able to minimise the gap. In terms of our prices in gas, I cannot tell you the exact prices, but around. Last year our average cost was approximately $9 per million BTU and our existing prices will be a little less than $6 per million BTU.

Sameer Kattiparambil One more question from my side. Could you give some colour on your Faucet segment? What was its bottom line at the end of 2023? Is it breakeven level? Just want to get an update on that.

Abdallah Massaad Sameer, as you know, when we acquired KLUDI we have two operations. One, KLUDI Europe and one KLUDI Middle East. KLUDI Middle East, the sales have gone up and we have a good profitability in the operation. In Europe, unfortunately we acquired it and after two months, when we signed the contract, if I'm not mistaken in December 2021 and then in February 2022 the war in Ukraine started and the business had a big impact. So, we started with the restructuring programme. First we started with the manufacturing footprint. We closed one factory in Austria, we reduced the production in Hungary and we moved the high end into Germany, but this with the recession also followed, affected the top line. We end up in losses in 2023, combined operation today between UAE and Europe, Middle East and Europe combined as KLUDI Group, we are beta positive, as a net profit negative, but we are continuing with a turnaround plan and I believe we'll have a better result in 2024 and starting 2025, it will be a good operation in place.

Operator Thank you. We'll now move on to written questions online. The first question reads, if possible, could you provide segment-wide and country-wide utilisation level?

Abdallah Massaad We'll start with Tiles. In Tiles we have the converting from ceramics to porcelain. Therefore, a big part already converted, but still some existing capacity where we are converting, the demand in ceramics get reduced, so I can see the capacity utilisation is around 75 to 80% in terms of Tiles. Sanitaryware, where we also did a transformation in manufacturing in order to introduce the robot in production, as well as, as I mentioned, we put a big kiln, the longest kiln in the industry, with the purpose of having better quality and saving in energy. Where we have also the capacity utilisation is around 65% today. In terms of Tableware, we are approximately 95% in the utilisation. In terms of the Faucets with the transformation we have 100% capacity utilisation in the UAE and we are reducing the capacity in Europe, in order to have a better cost structure.

Operator Thank you. The next question reads hi and many thanks for this great set of results. We know with a lot of attention your increase in the EBITDA, despite the stagnation/reduction in revenues during the course of 2023. How sustainable is this operating improvement, assuming sales will stagnate for another quarter or two, until the interest rates start declining again, hence encouraging consumers to invest again, which will result in an increase in your sales again?

Abdallah Massaad I mentioned that all our focus is on differentiation, on working on the brand perception, on working on innovation. I believe with this difficult time, despite the revenue is down, there is pressure in our sector worldwide. We’re capped with launching of smart factories and working on efficiencies where we’re able to sustain and grow our EBITDA. I believe, as you mentioned, that we are all betting when the interest rate goes down and the demand increases, I believe during the tough times we are able to sustain it and in the good time we will for sure sustain our margin. Therefore, we are working for long term and for the interests of our shareholders, always.

Operator The next question is are you supplying the Saudi market from the UAE’s ability and, if so, do you incur any import fees?

Abdallah Massaad Yes, we are supplying the Saudi market from the UAE facility and we are paying 12% custom duty. As from today we are working very hard on providing all the documents, in order to waive this custom duty. As from today, we are still paying, yes.

Operator The next question is how much does the Red Sea problem affect percentage of your business and your share market, cover the demands through late deliveries, as well as cover your raw materials need through supply chain?

PK Chand No doubt, the Red Sea problem affects the supply chain and increases our cost of import and export of material. As from today, we do not have any shutdown or missing raw material where it's affecting our manufacturing capacity. We always maintain a minimum stock and with this minimum stock availability, we never had the issue that we need to shut down. Hopeful the situation will be improved in terms of market share and no doubt there are delays in supply and even non-availability, which is quite disturbing. But whatever is in our hands, we are trying to do our best in order to minimise the impacts which will come on us from that.

Operator The final question is can the management shed some light on the expected cost savings that will result from the decline in UAE's natural gas prices? And some details behind the agreement, when it will start, why is it happening, and whether the management will utilise the cost savings to maintain its market share through more competitive pricing?

Abdallah Massaad As we mentioned, the prices of our gas, first of all, we have a supply of gas. We don't have any interruption in terms of gas supply in our premises in the UAE. Fortunately, we already mentioned this agreement earlier, where it will start implementation of beginning of this year, which already started. This will reduce the prices from, as I mentioned, from approximately $9 per million BTU to a little below $6 per million BTU. Which according to the volume which we are doing today, it might give us around AED 70 million impact benefit.

Yes, as you mentioned, that today with the Red Sea impact, we cannot pass to the consumer immediately the impact, so we are subsidising at a part the increase of raw material and the supply to our clients, in order to maintain our market share.

Operator Thank you. We have a follow-up audio question from Sameer Kattiparambil of EFG Hermes. Please go ahead, your line is open.

Sameer Kattiparambil Thanks. One last question from my side. On your land bank, I can see that your land valuation has gone up in your recent evaluation, but I think you didn't account that in your balance sheet yet, and I appreciate your conservative stance. Any chance that you will add that valuation this year? That's the first part. The second part is we want to hear more from you, how the more realistic market looks like over the last one year and what's your expectation on the realistic market overall? If you can give some colour on that, that would be very helpful.

Abdallah Massaad Thank you, Sameer, for your question. First, as you mentioned, valuation came a little higher, but honestly speaking, as we are not into real estate work, we didn't want as management to go with a year-by-year increase and taking provision and reverse provision, and focus on our core business. Regarding the land, we will work to offload it. Our aim is to sell it and we will account the profit or the loss the moment we sell it. In terms of real estate, as you know, that honestly, you see the number of projects and the prices, as well as the demand is amazing over the last 20 years. To be honest, we've never noticed that many prestigious names, which really, it's amazing. I believe the infrastructure, you can look and you see the infrastructure, as well as the development in a fast mode. We, as RAK Ceramics, we did not yet benefit fully. When the construction starts, after at least one-and-a-half years, where we will get the impact on the demand in our products, as we hopefully will benefit from the boom that is happening in the real estate and hospitality sectors.

Sameer, also, if you allow me, I want to add that this year we will have the taxes, which has to be at least considered, that this year we have to pay taxes.

Sameer Kattiparambil Yes, sure. I just want to reconfirm on that. Your tax rate will be in the 9% bracket or is it 15%.

PK Chand In 24, Sameer, it is going to be 9%. Because as far as 15% global minimum tax is concerned, it is not yet effective in the UAE. As per the latest information, the public consultation document is likely to be issued in the first quarter, then hopefully it might get implemented from 2025. That's the latest situation.

Sameer Kattiparambil Got you, thank you. Appreciate it and thank you, Abdallah, for your reply, really appreciate it.

Abdallah Massaad Thank you, Sameer.

Operator Thank you. We have another text question, which reads could you please provide any update on gas issue in Bangladesh?

Abdallah Massaad Honestly, in Bangladesh during this year we have a supply of a natural gas, but from time to time we have lower pressure, which we cannot run the full capacity. Or we have some interruption on some hours, which is affecting our production. I cannot say that we do not have gas, but sometimes we have some interruption. Now the election has happened in the beginning of the year, I think that slowly this will be stabilised.

Operator And the final question is are you planning to increase the capital instead of a high-interest loan, to cover your working capital and Capex?

Abdallah Massaad As of now, this is a board decision and general assembly decision, but I didn't hear any discussion on this in our board meeting or from this perspective. In fact, as a company we declared two-and-a-half years back, I believe, a policy of distributing minimum 20 fils, 10 fils every six months. This is continuing and the board of directors also continue to propose a distribution of 10 fils, to be approved by the general assembly. I don't see even changes in our dividend policy, for sure, before six months another policy will be declared, so not as per my understanding.

Operator Thank you. As a final reminder, if you'd like to ask a question, press star one on your telephone keypad or you can submit your questions in the chat box provided. We have no further questions, so I'll turn the call back to the management for any closing remarks.

Abdallah Massaad Thank you very much.

Mohamad Haidar Thank you, Mr Abdallah and Mr PK Chand, and thank you everyone for joining. We look forward to hosting you again next quarter.

Abdallah Massaad Thank you, Mohamad.

Operator This concludes today's call. Thank you for joining. You may now disconnect your line.