RAK Ceramics Q1 2024 earnings call and webcast

Friday, May 10, 2024

Operator Hello, everyone, and welcome to the RAK Ceramics Q1 2024 earnings call and webcast. My name is Nadia, and I'll be coordinating the call today. If you would like to ask a question, please press star followed by one on your telephone keypad. If you have joined online, please use the Q&A chat box provided. I will now hand over to your host, Mohamad Haidar from Arqaam Capital, to begin. Mohamad, please go ahead.

Mohamad Haidar Hello, everyone, and welcome to the RAK Ceramics First Quarter 2024 Earnings Conference Call. This is Mohamad Haider from Arqaam Capital, and from RAK Ceramics, we are joined today by Mr Abdallah Massaad, Group CEO, and Mr PK Chand, Group CFO. Over to you, Abdallah.

Abdallah Massaad Thank you, Mohamad. Good afternoon, everyone, and thank you for joining us. Welcome to RAK Ceramics First Quarter 2024 Earnings Conference Call and Webcast.

Let me take you through the consolidated revenue split for the group across our key markets as well as the split between the product divisions. We continued to strengthen our position in the UAE, which is our largest market, as it contributes 36% of the total consolidated revenue for the group. This is followed by Europe, which contributes 24% of the consolidated revenue, supported by KLUDI offerings. Our revenue share from Saudi Arabia has declined to 9%, and I will shortly touch upon the challenges we face in Saudi.

Coming to the product segments, tiles division continues to contribute majority share of the revenue, followed by sanitaryware, faucets and then 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 the tiles and sanitaryware business continued its growth trajectory in the UAE, reporting year-on-year revenue growth of 6%. In Saudi Arabia, there is a surplus of cheap product from local manufacturers backed by Chinese investors, especially in tiles segment. This has led to a price war situation, mainly in the wholesale segment.

Additionally, the ongoing crisis in the Red Sea region has led to a rise in transportation costs and delay in delivery schedules. This has put substantial pressure on margin and the working capital management. Thus, we continue to invest and focus towards strengthening our project and retail presence in this market, as we are optimistic of future business growth, backed by government's substantial investment in infrastructure and real estate projects for the upcoming period.

The Red Sea crisis has also impacted our business in Europe due to increase in shipping cost and delay in delivery schedule. Moreover, the demand has seen a slowdown across wholesale and the retail segment as the European market is still struggling to recover from the recessionary pressure, thus reducing the consumer spending capacity. Also, several home renovations projects have been put on hold, mainly impacting our sanitaryware and faucet business in the UK and Italy.

In India and Bangladesh, markets continue to struggle with lower demand, mainly on account of a rising interest rate and tight liquidity. In Bangladesh, we are also facing shortage in gas supply, thus affecting production efficiencies. Our tableware division was also impacted, reflecting a 7.8% decline in revenue compared to the first quarter 2023. This slowdown in demand was mainly on account of decline in projects, hotel projects and reduced spending due to the ongoing regional conflicts.

As we closely monitor the ongoing macroeconomic and geopolitical challenges, we continue to innovate our approach to ensure that we stay ahead across all markets in which we operate. Our team is working on implementing several initiatives across our core market.

For instance, we are working towards brand enhancement through opening new showrooms and widening our dealer network in all core markets to strengthen and maintain our position. We are working with the architects' and designers' community to promote our new collection. We are focusing on premium product to mitigate the impact of our margin. We are also working on strengthening our retail and project business with differentiated products that will allow us to maintain a sustainable growth for revenue and margin going forward.

The upgradation of our tiles production facility in India is nearing its completion, which will allow us to produce slabs and large format tiles. In the UAE, we continue to invest in the latest deep digital technology and automation of our tiles production facility that will allow us to shift our production capabilities from ceramics to porcelain tiles and also 100% digital slabs. As we recall, we had a big capacity of ceramics servicing the market, especially Saudi and the GCC, with multiple differentiated sizes in ceramics, and the market has shifted to the demand in porcelain.

Therefore, what we are doing is shifting a majority of our existing kilns and facilities, with lower capex required, to be able to produce again differentiated as well as digital full lines from a small to the largest tiles available in the market, where we feel that this will give us a big advantage, as we are already known in the projects as well as the market with our quality and innovation.

We are also working towards setting up a production facility in Saudi in tiles, for tiles. In terms of KLUDI, I'm also pleased to update that the expansion which we started in UAE is already in production, the quality is by the highest standard, and our transformation of the factories which we closed in Austria as well shifted some capacity from Europe to UAE. And therefore, supplying a fully packed product out of Ras Al Khaimah allows us to improve our gross profit margin in KLUDI, and speeding the transformation.

I will now hand over to PK Chand, our CFO, to provide you with more detailed analysis of our financial performance.

PK Chand Yes. Thank you, Abdallah. Good evening, everyone, and thank you for joining us. Mr Abdallah has already briefed on business performance highlights for key markets, challenges and a strategy update for the first quarter of 2024. I will take you through the financial highlights for the first quarter, with details on revenue, gross profit margin and the balance sheet.

We will start from slide 11. Total revenue decreased by 11.4% year on year to AED 781.6 million, reflecting global geopolitical tensions, market volatility, higher interest rate and currency devaluation. Tiles and sanitaryware revenue is lower by 14.4% year on year to AED 556.5 million.

Tiles revenue decreased by 14.8% year on year to AED 443.6 million, impacted by lower sales volume, particularly in Saudi Arabia and Europe. Sanitaryware revenue experienced a decline of 12.7% year on year to AED 112.8 million due to economic pressures in Italy, UK and Bangladesh, which are our core markets. Tableware revenue saw a year-on-year decrease of 7.8% to AED 90 million, attributed to logistic challenges and currency depreciation.

Faucets revenue, however, has increased by 4.7% year on year to AED 116.9 million, driven by UAE and European markets. Revenue from other units decreased by 20.7% to AED 18.4 million, mainly due to a decrease in our ceramic raw material trading business.

Now let me go through slide 13 onwards, covering the end-market performance in the first quarter of 2024 for the tiles and sanitaryware segments. In UAE market, tiles and sanitaryware revenue increased by 6.2% year on year to reach AED 201.5 million, primarily driven by retail and project channels, backed by real estate market growth.

In Saudi Arabia, tiles and sanitaryware revenue witnessed a significant decline of 44.8% year on year due to continued price war and local competition. However, we have been able to maintain our gross margin by focusing on premium products and differentiation.

In India, the revenue declined by 3.5%, primarily as a result of persistent challenges, such as currency devaluation and reduced demand due to higher interest rate. To fortify our position in the dynamic Indian market, we strategically pursued upgrades to our facilities, expanded our market presence, implemented retail initiatives and introduced new product launches.

In Europe, revenue decreased by 19.5% year on year, with significant impact to our sanitaryware business. As Mr Abdallah mentioned, the Red Sea crisis has severely impacted our business in Europe, due to substantial increase in shipping costs and delay in delivery schedule. Moreover, the demand has seen a slowdown across wholesale and retail segments, as the European market is still struggling to recover from this recessionary pressure, thus reducing the consumers' spending capacity.

In Bangladesh market, the revenue declined by 15.5% year on year due to intense local competition, gas supply challenges and the currency devaluation. We have initiated actions to address these challenges by intensifying our marketing endeavours to enhance market penetration and elevate brand visibility.

In the Middle East, excluding UAE and Saudi market, we continued to face adverse effects due to ongoing geopolitical challenges in the region. Revenue has declined by 25.7% year on year to AED 26.3 million. Now we will turn to slide 14.

The total gross profit margin increased by 70 basis points year on year to 39.3% in the first quarter of 2024 due to lower natural gas price in UAE and improved efficiencies. Tiles margin increased by 50 basis points, at 39.4% compared to last year, supported by lower natural gas price and improved efficiencies.

However, sanitaryware margin decreased by 630 basis points year on year at 29.7% due to reduction in sales revenue resulting in shutdown costs. Tableware margin increased by 360 basis points year on year to 53.9% following the lower revenue and change in product mix. Faucets margin increased by 450 basis points at 31.1% due to rationalisation of costs, mainly in Europe.

Net profit before tax is AED 73.9 million compared to AED 85.1 million in last year, mainly due to a decrease in tiles and sanitaryware revenue. Margin is 9.5% compared to 9.6% in last year. Net profit after tax is AED 62.9 million compared to AED 80.1 million in last year. The impact of the newly introduced UAE corporate tax at the rate of 9%, effective 1 January 2024, is AED 8 million in the first quarter.

Net profit margin is 8% compared to 9.1% in the last year. EBITDA, however, decreased year on year by only 3.9% in the first quarter of 2024 to reach AED 151 million. The margin has improved by 150 basis points year on year to 19.3%. Now we will turn to balance sheet highlights on slide 16.

Overall working capital cycle decreased from 172 days in the fourth quarter of 2023 to 161 days in the first quarter of 2024, mainly due to accounting of dividend liability in the first quarter of this year, which has been paid in April 2024. In absolute terms, working capital decreased by AED 99 million to AED 1.38 billion in the first quarter of 2024. Excluding dividend liability, working capital remained stable quarter on quarter at AED 1.48 billion.

Inventory days increased from 221 days to 228 days compared to December 2023, only due to lower LTM sales. In absolute terms, inventory remained stable at AED 1.3 billion. Trade receivables decreased from 90 days in December 2023 to 88 days in March 2024. In absolute terms, trade receivables decreased by AED 39 million to AED 811 million. Trade payables marginally decreased from 59 days in December 2023 to 58 days in March 2024.

Net debt decreased by AED 54.3 million in March 2024, at AED 1.37 billion compared to December 2023. Net debt to EBITDA also decreased from 2.2 times in December 2023 to 2.13 times in March 2024. We continued to maintain an adequate liquidity position during the year. Capital expenditure during the first quarter of this year is AED 35 million, and CAPEX guidance for the full year of 2024 is AED 300 million.

Slide 18 shows the share price movement during the last 12 months. The shares are currently trading at a PE multiple of 10.5 times. Now I would like to turn back to Mr Abdallah for his final comments, before we answer your questions.

Abdallah Massaad Thank you, PK. It is evident that the ongoing geopolitical challenges and the crisis have impacted businesses across industries. While we also have seen a decline in our overall revenue, we have been more fortunate than a few others in successfully restricting any major impact to our profit margin.

In this complex scenario, we remain dedicated to serve our clients as we continue to position ourselves as a global preferred supplier. While we also remain cautiously optimistic about the outlook for the upcoming quarters, we will continue to invest and strengthen our presence across markets in which we operate.

We are committed to protecting our market share and solidifying our retail and project business through maintaining healthy competition and leveraging cross-product synergies. With digitalisation being the core of our growth strategy, we continue to invest in upgrading our facility with the latest technology to optimise productivity and increase efficiencies, thus driving improvement in our margin.

Also, we launched during this quarter the online sales for our retail business and tableware. We are ready to open our first showroom in Dubai Hills Mall also during this coming quarter. We already started the selling online, so we are also focusing on improving our specification, retail job, retail in general, as we did in UAE, in Saudi and in India, and then we roll it out.

And just thank you all for taking the time to join us for this presentation of our first quarter result of 2024. I would now like to hand over the call to the operator and open the line to questions.

Operator Thank you. If you would like to ask a question, please press star followed by one on your telephone keypad. If you have joined online, please use the Q&A chat box provided. If you would like to remove your question, please press star followed by two. When preparing to ask your question, please ensure your phone is unmuted locally. We ask you, please limit yourself to one question and one follow-up. Our first question goes to Sameer Kattiparambil of EFG Hermes. Sameer, please go ahead. Your line is open.

Sameer Kattiparambil Thank you, gentlemen, for the presentation. A couple of questions from my side. First, on the LPG and natural gas cost. Although you mentioned that the gas price has been decreased in UAE, but what I've noticed is that in your COGS segment, it has declined by 50% to 29 million from 59 million last year. So I just want to understand if that decline came just from the UAE cost adjustment, or is there any other markets, like India, Bangladesh, contributed to that decline?

Abdallah Massaad Sameer, thank you for your question. And this is what we were discussing, that the market, especially with the Red Sea, impacted the volume. And for us, we had less volume manufactured, and the consumption also reduced. It is a double impact of reducing the prices as well as reducing the volume utilised.

Sameer Kattiparambil Okay. So could you remind me, what was the price revision in UAE, what you are currently paying?

PK Chand $8.9/MMBTU.

Abdallah Massaad We were paying approximately $8.9/MMBTU. Now we are paying somewhere below six dollar per MMBTU.

Sameer Kattiparambil Got you. Got you. Maybe one more question from my side. Any recovery in sight for the Saudi market? Especially, we have seen some early signs of tile price improvement in the country from some of your peer companies. So anything you noticed in the Saudi market?

Abdallah Massaad Yes. Honestly, we are focusing… Saudi market is still strategic. But for us, strategically, we decided not to go into the price war and focus on projects, retail and be alert. We are selling the most quantity in ceramics, which the price has gone down. Yes, during last quarter, some notice from the government to stop reducing prices because it affected the overall ceramics market.

Yes, we saw a pick-up in the prices. But honestly speaking also, we see that the project is getting realised. As you know, when you invest in infrastructure, then the projects will come. We do have a target on the high-end, on the premium projects which we'll start. And that's why we're working very heavily in the specification in order to ensure a good market share in the high-end products.

Sameer Kattiparambil Okay, that's very clear, Abdallah. Thank you for that.

Abdallah Massaad Thank you.

Operator Thank you. We have a question via the chat. When do you plan to sell the land in Ras Al Khaimah? Thank you.

Abdallah Massaad Honestly, it is something where we'll consider when we get a good offer in order to liquidate, as we decided, as we declared earlier that this land will be for sale, and we are not going into any development ourselves.

Operator Thank you. And as a reminder, if you would like to ask a question, please press star followed by one on your telephone keypad. If you have joined online, please use the Q&A chat box provided. We'll pause for just a moment. We have a follow-up from Sameer from EFG Hermes. Sameer, please go ahead.

Sameer Kattiparambil Thank you. A few more questions. On the faucets segment, what I've noticed is that your revenue has improved year over year, and its EBITDA margin also now stands at almost 6% versus last full-year number of 1%. So it's really impressive to see the development in that segment.

So could you remind me, the development in this segment, what are the strategies for this segment and what's your target for this year? What kind of EBITDA margin and revenue are you looking at? And what kind of capacity has been shifted from Europe to UAE right now?

Abdallah Massaad Sameer, thank you for the question. KLUDI is a very important strategic initiative which we had, buying KLUDI, which is historically, 100 years, a German or European player. And this, we are working, as we already launched also in KLUDI the sanitaryware, KLUDI-branded. And we believe that this will help the overall sanitaryware division and RAK Ceramics by having categorised into RAK Ceramics product for mass, and KLUDI for the projects, which we are successfully addressing the high-end segment in the projects.

For us, we started first with the transformation of manufacturing, footprint transformation as we discussed. We reduced the production in Germany. We closed the factory in Austria. We did the first phase of expansion in UAE. And today in UAE, in which we were producing half a million pieces, we increased our capacity to almost a million pieces. Now we started with the third expansion to go up to 1.5 million, and then we'll have another expansion in the UAE.

What has happened was a shift of manufacturing the units from Europe to UAE. And when we supplied it, we saw that we had an advantage of 16-17% of cost advantage. And therefore, we also, as you saw, picked up in a way, even though Europe is still in recession.

And this is a good early sign, because with a recessionary environment, we are able to grow and we are able to improve our, as you said, gross profit margin, and the EBITDA also improved. We see that this will continue. I believe by next year, we should have a much, much, much better result, where it is a good initiative.

Now, going into the numbers, I can see if we have any numbers, or we can take it offline, anything you want in terms of details, because I don't have it honestly in detail, what will be the target of our EBITDA. But we have a very high expectation in this regard.

Sameer Kattiparambil Okay, got you. That's very clear. And maybe one last question from my side. So what's your overall outlook for the UAE market? It has been quite strong for quite some time. And how are you seeing this market? Will it continue with this growth, or any slowdown?

Abdallah Massaad Honestly, we do not have… It is our home market, and unfortunately, it is normal that it is difficult for us everywhere outside because of the logistics and the macro environment. One is a recession, as we discussed, and second is the Red Sea disruption which increased the transportation cost, which puts pressure on us in terms of profitability as well as competitiveness.

This always gives an advantage for a local manufacturer in his local market, and therefore, fortunately, the UAE. And you know that the projects continue to boom. We have a lot of projects around us. We are doing very well. The design hub which we opened in Dubai, we are ready now. As I said, in the next two months, we'll open our new showroom in Sheikh Zayed. It will be a very impressive showroom, the retail which we are opening also in Dubai Hills, the outlet concept which we launched.

So we have a good outlet, honestly, starting from the UAE, and we feel that we'll gain more market share also in the coming months, especially now, as I said, with the launching of KLUDI, where we are seeing a lot of acceptance and projects getting specified, our sanitaryware under the KLUDI brand. So we do have a positive outlook in the UAE market.

Sameer Kattiparambil Okay. Thank you so much, Abdallah. I wish you all the best.

Abdallah Massaad Thank you, Sameer.

Operator Thank you. It appears we have no further questions. I'll now hand back to CEO, Abdallah Massaad, for any closing comments.

Abdallah Massaad Thank you. Thank you very much.

Mohamad Haidar Thank you all, and hope to see you with us next quarter.

PK Chand Thank you. Thank you. Thank you.

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