

RAK Ceramics (Bangladesh) Limited

DSE: RAKCERAMIC; Bloomberg: RAKC:BD

Fair Value Estimate: **BDT 62.1**

Rating: **Overweight**

Valuation date: **22 April, 2015**

Analyst:

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Company Summary	
Current Price (BDT)	57.2
52-week price range (BDT)	40.4-71.1
Expected Capital Gain	12.1%
Market Cap (BDT mn)	18,627.8
3 Months Return	9.8%
3 Months Avg Turnover (BDT mn)	21.7
Market weight	0.8%
No. of Share Outstanding (in mn)	336.9
Free-float Shares	22.2%
Paid-up Capital (BDT mn)	3369.0
Sector	Ceramic

RAK Ceramics (Bangladesh) Limited, a UAE-Bangladesh joint venture company, is the largest, fastest-growing and most respected ceramics brand in Bangladesh. RAK Ceramics is the global market leader in ceramic tiles business. The company specializes in the manufacturing, branding and marketing of the broader range of tiles, bathroom sets and sanitary-ware products.

RAK's products include varieties of ceramic wall and floor tiles, sanitary wares, decors, listellos, pencils, cappings, border and corners. The company has over 1,000 models active in the ceramic and porcelain tile business and has over 30 models of sanitary ware of various bathroom utility and luxury products. The plant standard capacity is 22,000 square meter tiles per day & 8.03 mn square meter per annum and 3,400 pieces of sanitary ware per day & 1.10 mn pcs per annum.

As a part of expansion plan, the company is increasing its annual capacity by 3.5 million square meter of tiles from the current 8.03 mn square meter (43.58% escalation), and by 0.35 mn pieces of sanitary ware from 1.1 million (31.82% enhancement). For implementing these expansion plans RAK envisaged capital of BDT 1,800 mn for the tiles plant and BDT 270 mn for the sanitary ware facility.

However, to grow the core business, RAK group is giving priority to exit from all non-core businesses and returning to its roots. The company has recently divested one of its subsidiary and an associate in Bangladesh as part of global divestment plan from non-core businesses.

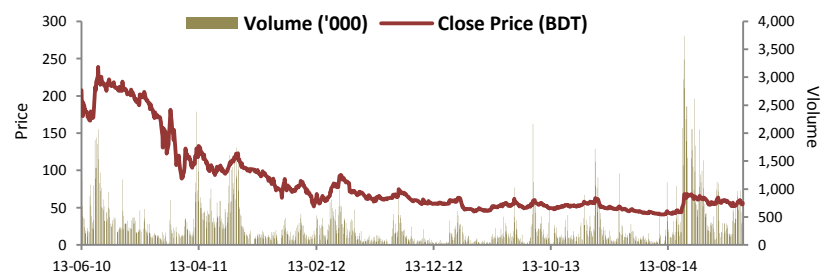
The company was listed in DSE and CSE in 2010 under Book building method.

We conducted a valuation on RAK Ceramics (Bangladesh) Limited based on both Discounted Cash Flow methods and Relative Valuation method while assuming next 5-Year CAGR of revenue will be 13.96%. Currently, RAKCERAMIC is traded at price of BDT 57.2 (as on 22 April, 2015). In our valuation, the fair value of RAKCERAMIC is determined at BDT 62.1.

	2014 A	2015E	2016E
Financial Information (BDT mn)			
Sales	5,047	6,110	7,310
Operating Profit	1,057	1,380	1,668
Net Profit*	612	985	1,131
Assets	9,477	10,162	11,360
Long Term Debt	0	0	0
Equity	5,919	5,631	5,741
Margin			
Gross Profit	39.1%	40.3%	40.6%
Operating Profit	20.9%	22.6%	22.8%
Pretax Profit	21.2%	22.2%	22.5%
Net Profit	12.9%	16.7%	15.9%
Growth			
Sales	6.8%	21.1%	19.6%
Gross Profit	6.9%	24.6%	20.2%
Operating Profit	-6.0%	30.5%	21.0%
Net Profit	-16.1%	61.0%	14.9%
Profitability			
ROA	6.6%	10.0%	10.5%
ROE	10.4%	17.1%	19.9%
Leverage			
Debt Ratio	3.4%	11.9%	13.2%
Debt-Equity	5.5%	21.4%	26.1%
Int. Coverage	136.3	68.6	60.1
Valuation**			
Price/Earnings	34.2	19.6	17.0
Price/BV	3.3	3.4	3.4
Miscellaneous			
Restated EPS	1.8	2.9	3.4
DPS	2.5	2.5	2.5
Payout Ratio	149.6%	85.5%	74.4%
NAVPS (BDT)	17.6	16.7	17.0

*Excluding Non-controlling Interest; **based on current market price; *** Based on continuing operation only

Price Volume Performance



The Ceramic Industry Review

The ceramics sector of Bangladesh can be categorized into two major subsectors: ceramic tableware and building materials

Bangladesh Ceramic industry took a formal start in this country in 1958. But it started to grow from the late 1990's. However, the industry has passed a long way and now became a huge potential sector for growth.

The ceramics sector of Bangladesh can be categorized into two major subsectors: ceramic tableware and building materials. The building materials segment is inclusive of tiles and sanitary ware. Bangladesh Tableware segment is mostly export oriented but the building materials segment mainly serves the domestic markets.

20 companies are producing Ceramic Tiles and 16 companies are producing Sanitary-ware products

According to Bangladesh Ceramic Wares Manufacturers Association (BCWMA), Currently 20 companies are producing Ceramic Tiles and 16 companies are producing sanitary-ware products on commercial basis in Bangladesh. However, A few ceramic manufacturers dominate the segment producing high quality products. State-owned enterprise Bangladesh Insulator and Sanitary ware Factory (BISF), which was set up by Bangladesh Chemical Industries Corporation, started producing ceramic tiles and sanitary ware for the first time in Bangladesh since 1977. Madhumati Ceramics Ltd. made the first private investment in this sector during 1993 followed by Taiwan based Fu-Wang Ceramics, UAE based RAK Ceramics. In FY 2013-14, total investment in the ceramic tiles sector was BDT 25 billion.

RAK Ceramics (Bangladesh) Ltd. brought a drastic change in the tiles industry and now owns one-fourth of the domestic market share. Other major players in the tiles segments are Great Wall Ceramics (7.5 million square meter annual capacity), Mir Ceramics (7.25 million square meter annual capacity), Star Ceramics (7.3 million square meter annual capacity), Akij Tiles (7.5 million square meter annual capacity), X-Ceramics (5.0 million square meter annual capacity), China-Bangla Ceramics (4.5 million square meter annual capacity), Fu-Wang Ceramics (4.37 million square meter annual capacity with 53% utilization), Hua-Thi Ceramics (3.0 million square meter annual capacity) etc.

Production and Consumption

Domestic producers dominate the market

In Bangladesh, currently about 54 tiles and sanitary ware and tableware ceramic manufacturers are now in operation. Investment in this sector by local as well as foreign investors already exceeded BDT 50 billion and the market size of ceramic industry currently worth BDT 20 billion.

Nearly 75,000 tons of ceramic wares and 40 million square meter tiles are produced annually by local manufacturers. Up to FY 2012, domestic table-ware industry had the capacity to serve the BDT 3.0 billion indigenous market. At present, total yearly production capacity of ceramic tableware manufacturing companies stands at 222 million pieces, for ceramic tiles it is 68.7 million square meters and for sanitary ware it is 114.0 thousand metric ton. The annual market growth rate is about 10% on average.

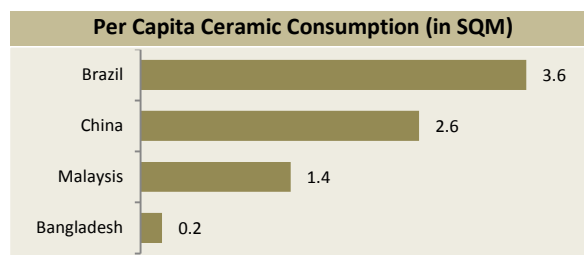
In Bangladesh, ceramic tiles manufacturers mainly cater to domestic demands but ceramic tableware manufacturers are mostly export oriented. As per the BCWMA

data, total sales of tiles were BDT 24.25 billion in 2013-14, within which BDT 18.5 billion (76.3%) were from domestic producers. Sales of imported tiles were BDT 5.75 billion which is 23.7% of total sales in the same financial year.

*Industry players expanding
production capacity*

On the face of robust growth in demand, all the major industry players in both segments like RAK Ceramics, Shinepukur, Monno Ceramic have been expanding their production capacity.

Globally, ceramic products comprising Stone, Porcelain and Bone China Tableware, Tiles and Sanitary ware worth more than USD 41.3 billion out of which Bangladesh possess only 0.97% share. Per capita consumption of ceramics tiles in Bangladesh is miniscule at 0.20 square



(Source: Ceramic World Review, WB and Credit Suisse, ILSL Research)

meter which is enormously low compared to 3.6 square meters in Brazil, 2.6 square meters in China, and 1.4 square meters in Malaysia.

However, in Bangladesh, the industry is considered to expand promptly in this global market with its skilled and creative human resource base, high quality products and low production cost ratio.

Export and Import Scenario

Though the country's entry into ceramic export market is not that old, it has already achieved a good name for its quality products with elegant outfit and design. Competitive advantage in production facility is pushing Bangladesh ahead in the export market. Bangladesh is now witnessing the industry as a vastly prospective sector for its growing export performances. Total ceramics export stood at USD 47.5 million (BDT 3.7 billion) in FY 2013-14. Whereas it was only USD 1.0 million in 1991 which means that ceramic products registered an average annual growth (CAGR) of 18.3% during the last two decades (from 1991 to 2014). However, the amount of export in the building materials sector i.e. tiles and sanitary ware is still very negligible.

*India, Nepal and Bhutan imports
ceramic tiles while UAE purchases
Sanitaryware from Bangladesh*

Ceramic Tableware mainly introduced the country to the international market as an exporter of ceramic products. Of the products manufactured, ceramic tableware are being exported to about 50 countries. Bangladeshi ceramic wares are exported to US, UK, Germany, Canada, France, Turkey, Italy, Sweden, Switzerland, Norway, U.A.E, India etc. The US and Canada mainly buys tableware, Nepal, Bhutan, India and other seven sisters states imports ceramic tiles while Middle East, specially the UAE purchases Sanitary-ware from Bangladesh.

Ceramic tiles and sanitary wares are imported mostly from China, Malaysia, Thailand and Europe.



Raw Materials for Ceramic Industry

Manufacturers are mostly dependent on imported raw materials

In ceramic manufacturing 35-40% of the total production cost is spent on raw materials. White clay and sand are the prime raw materials of ceramic products. Raw materials for ceramic ware also includes - China clay, ball clay, fire clay, feldspar, aluminum oxide, aluminum hydro oxide, zinc oxide, quarter's plaster of Paris, coloring items and liquid gold.

In Bangladesh, The largest deposit of white clay was first discovered in 1957 at Bijoypur of Mymensingh. Total reserve of white clay from this region is approximately 2.57 million tons. Clay was also found in Jaflong of Sylhet but there is no clay or sand treatment plant at these places.

There is an acute shortage of raw materials for ceramic goods in Bangladesh and the manufacturers are mostly dependent on import of raw materials from abroad. Other manufacturing countries have their own raw materials which work as a backward linkage to their local industry. Nearly 95% of required raw materials for producing quality and exportable ceramic products are imported. Raw materials are purchased mainly from Japan, Germany, South Korea, New Zealand, India, China, Rumania, Indonesia, Sweden, Finland, Spain, Italy, U.K, France and Germany.

Industry Characteristics

High capital expenditure required

- High capital expenditure is a critical feature of the industry. A medium scale ceramic plant needs around one billion BDT in initial investment, and this is why Bangladesh has only few such ceramic products manufacturers.
- 24 hours high voltage (380 degree temperature) uninterrupted power and gas supply is required in a ceramic factory. Temperature reduces in low power voltage or gas pressure. If the temperature falls it takes at least 12 hours to bring back to the preceding level. A low heat in any plant causes fault to color and quality.

Industry Prospect in Bangladesh

- **Cheap labor price drives the growth:** Labor intensive nature of the industry makes it difficult for the global economies to remain competitive in the ceramics industry due to rising labor cost and increasing financial instabilities. Bangladesh, with its positioning as a cheap labor-cost economy, is poised to grasp the growth potential among the emerging economies.
- **Availability of natural gas:** The country is enriched in gas. The natural gas that is used in the kilns (boilers for ceramics) of the Bangladeshi ceramic industry does not contain any Sulphur and that is why the country's ceramic products look brighter.
- **Demographic factors:** Bangladesh is a country of 160 million people. According to the World Bank data, the annual population growth of Bangladesh in 2013 was 1.2% and death rate per 1000 people was 5.7 as of 2012. Therefore, with the growth in population and their purchasing power the demand for every type of ceramics products are growing as well.

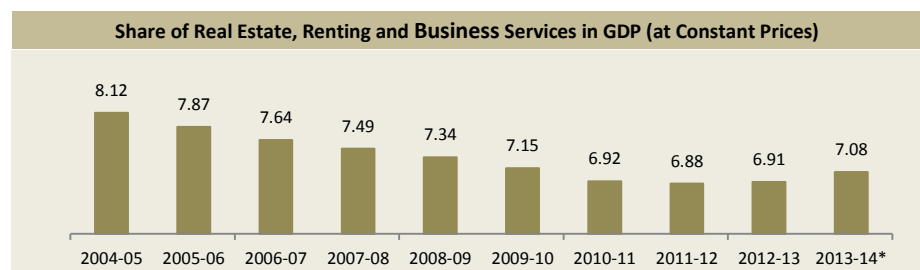
- **Export growth potential:** As demand for ceramic goods is going up globally, country's big players are now eyeing the export market. High quality of products has rewarded Bangladesh a niche market in the developed world. Ceramic units are having robust growth performances (12%-15% per year) belying all earlier speculations.

Bangladesh is rightly positioned to expand in ceramics business. Availability of skilled labor forces with cheap wages as well as gas supply is a blessing for Bangladesh. So, the country emerged as a perfectly placed one to be a strategic partner in the production and supply of ceramic ware products to the top branded companies in developed countries like Europe, USA etc.

Review of the Bangladesh Real-estate and Construction Sector

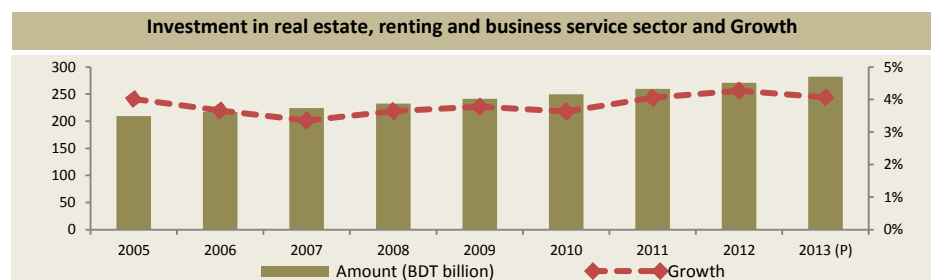
Bearish trend in the real estate sector have caused a declining growth in the ceramic tiles industry

Currently at least 1,300 flats are unsold in Dhaka city and 24000 unsold in the whole country, according to the local newspaper report and market players. Compared to overall GDP growth, this sector expanded in a slower rate since the last one decade. This sluggish condition will reduce the growth of the apartment business and in turn the consumption of ceramic tiles and sanitary-ware must also be reduced.



Source: Bangladesh Bureau of Statistics and ILSL Research; *Provisional

However, the real estate, renting and business service sector had a positive growth every year. But, compared to overall GDP growth, this sector expanded in a slower rate. That is why in overall GDP, the contribution of this sector has a downward trend.



The ceramic tiles consumption is closely linked with the growth of the country's real estate sector's performance. Earlier, the booming real estate had helped the ceramic tiles manufacturers to grow. Recent bearish trend in the real estate sector have caused a declining growth in the ceramic tiles industry. Investments in the housing sector by the private sector will drive demand for ceramic tiles and sanitary-ware products.



RAK Ceramics (Bangladesh) Limited

A UAE-Bangladesh joint venture company

RAK Ceramics (Bangladesh) Limited, a UAE-Bangladesh joint venture company, is the largest, fastest-growing and most respected ceramics brand in Bangladesh. The company specializes in the manufacturing, branding and marketing of the largest range of tiles, bathroom sets and sanitary-ware products. RAK has firmly established itself as the leading manufacturer of high quality ceramic wall, floor tiles, gres porcellanato and sanitary wares products in Bangladesh.

Largest Ceramic brand in Bangladesh

RAKCERAMIC was incorporated in Bangladesh on 26 November, 1998 and started commercial operation on 12 November, 2000. The company was thereafter renamed from RAK Ceramics (Bangladesh) Private Limited to RAK Ceramics (Bangladesh) Limited in 2009.

Grew at a 5 CAGR of 7.5% in Revenue & 11.6% in net profit after tax

RAKCERAMIC has demonstrated rapid growth since its inception. The company has achieved consistent growth in revenue and profits, its revenue and net profits grew at a 5 year Compounded Annual Growth Rate (CAGR) of 7.5% and 11.6% respectively as compared to 8.9% (2013 est.) per annum industrial production growth rate of Bangladesh.

The company was listed in DSE and CSE in 2010 under Book building method. At present, 77.82% of total shares of RAKCERAMIC are held by the sponsors/directors, 10.45% by institutional investors and rest 11.73% by general public as per the DSE website.

Business

Manufactures and sells tiles, bathroom sets and sanitary-ware products

The core business of RAK Ceramics (Bangladesh) Limited is to manufacture and sell of tiles, bathroom sets and sanitary ware products. The company has over 1,000 models active in the ceramic and porcelain tile business and regularly adds several new designs to the product portfolio. The company has over 40 models and an exclusive range of sanitary ware to offer. In sanitary ware, various models are produced in wash basins (mounted as well as pedestal), water closets, accessories and marble sets. Most of production is consumed in local market and balance gets exported to UAE.

Currently, RAK has one subsidiary and two associates

RAK Group has diversified its business portfolio to different strategic business segments to demonstrate its potential and explore the opportunities. As on 31 December 2013, RAKCERAMIC had two subsidiaries and three associates. However, the company has already divested one of its subsidiaries named RAK Pharmaceuticals Pvt. Ltd, where the company had 55% stake and an associate named RAK-Mosfly (Bangladesh) Pvt. Ltd. where the company had 20% stake. Current status of the group is as follows –

Particulars	Name of the Company	Ownership	Nature of Business
Subsidiary	RAK Power Pvt. Ltd	57.00%	Captive electricity generation
Associates	RAK Paints Pvt. Ltd.	47.00%	Manufacturing, sales and marketing of paints products
	RAK Security Services (Pvt.) Ltd.	35.00%	Security service



RAK Power Pvt. Ltd. (RAKPL), a 9 megawatt capacity (10 MW licensed) Natural Gas fired captive power plant was incorporated with a view to providing uninterrupted electricity supply to RAK group in Bangladesh. As on December 2013, RAK owns 57% ownership in RAKPL and rest 43% is owned by local investors. It has started operation in May, 2009. Capacity utilization of the plant was 83% in year 2013.

RAK Paints (Private) Limited produces solvent based and water based paints of premier quality. It is a 40% owned associated company of RAKCERAMIC.

RAK Security and Services Pvt. Ltd. is a 35% owned associated company of RAKCERAMIC. The company formally started supplying and training of security guards to different commercial establishments in May 2007. Services in the area of cleaning, termite, pest control, fumigation and setting up manpower technical training establishments for creation of skilled workers are also provided by the concern.

Parent Profile: RAK Ceramics PSC, UAE

*A USD 1 billion global conglomerate
in the ceramic industry*

RAK Ceramics is a USD 1 billion global conglomerate in the ceramic industry, offering a product portfolio comprising over 8,000 designs in ceramic tiles, gres porcelain, kitchen sink and several models in bathware.

*Global manufacturing capacity of
around 117 mn sqm of tiles per year
and over 4.5 mn pieces of sanitary
ware per year*

Ras Al Khaimah (RAK) Ceramics Public Shareholding Company, (RAKC, PSC) is a UAE based leading tiles and sanitary ware manufacturing company in the world. It was established in 1989 and commenced production in 1991, at its advanced facility at UAE location. RAKC, PSC has global manufacturing capacity of around 117 million square meters of tiles per year and over 4.5 million pieces of sanitary ware per year, which is recognized them as leader in ceramics world.

The founding shareholders include H.H. Sheikh Saud Bin Saqr Al Qassimi, the Crown Prince and Deputy Ruler of Ras Al Khaimah, one of the emirates of United Arab Emirates. Abdallah Massaad the present Chief Executive Officer of the company has devised global market strategy and implemented the company's global expansion plans. The company is highly regarded for its consistent performance, in stock market it is well noted as traditionally strong script for an average of over 20% dividend record.

*Manufacturing facilities in
Bangladesh, China, Iran and India*

RAK Ceramics PSC is having manufacturing facilities in in Bangladesh, China, Iran and India. Further, it has its own subsidiaries in Italy, Germany, United Kingdom, Saudi Arabia, Australia and few other countries. The company's international investment projects in China, Bangladesh, Iran and India were funded by International finance Corporation (IFC), a member of World Bank group. RAK-UAE's products are exported to more than 160 countries over five continents across the globe. The company was listed in Abu Dhabi Stock Market (ADX) in 2003.

*Products are exported to more than
160 countries*

Insights into RAK Ceramics PSC, UAE

Ras Al Khaimah (RAK) Ceramics is the world's largest makers of floor tiles and other ceramic products. RAK ceramic, PSC, UAE's domestic operations in UAE account for 66% of the group's revenues and has a plan to modernize at a cost of around 100



million U.A.E. dirhams (USD 27.2 million). RAK Ceramics has a lot of growth potential because of the construction boom in the Gulf and rising consumption in Africa and Asia.

Plans to invest about USD 80 million as it expands its production in the UAE, India and Bangladesh

Global Expansion Plans: In response to raising demand of tiles and ceramic products RAK Ceramics is pushing deeper into countries where it already has a presence but capacity need to enhance. The RAK ceramic envisaged a capital expenditure program of USD 80 million to expand its production in the UAE, India and Bangladesh as well as technology upgrades at other plants.

In India, RAK plans to invest up to Rs 5 billion (USD 81 million) over the next five years, which will include capacity expansion. Financing of the expansion could be raised mostly from internal accruals and with some assistance from the parent company. In Bangladesh, RAK Ceramics plans to increase annual capacity by 3.5 million square meters of tiles and by 350,000 pieces of sanitary. Besides, The Company is also upgrading technology at factories in the UAE and elsewhere.

The company's plan is to generate 1 billion U.A.E. dirhams (USD 270 million) out of divesting its non-core assets.

Divestment Plans from Non-Core Businesses: RAK ceramic, PSC, UAE decided to shift away from all the non-core businesses including construction as it now focuses on its main production operation i.e. tiles, sanitary ware, faucets- that helped grow the company into a global leader. Its main business accounted for 84.9% of revenue in 2013, compared to 78.1% in 2012. The company's plan is to generate 1 billion U.A.E. dirhams (USD 270 million) out of exiting these non-core assets.

As a part of these plans, the company already divested its stake in some non-core businesses in Bangladesh. The Abu Dhabi-listed firm is also in the process of selling its business in Sudan. RAK expects to receive more than USD 50 million from the sale of stake in RAK pharmaceuticals and its Sudan business.

RAK Ceramics PSC, UAE's profit fell 15% in the third quarter because of hyperinflation accounting in Sudan and Iran. The company's losses in Sudan reached Dh16.48 (USD 4.49) million at the end of September 2014. The divestment will help the company avoid operational issues regarding the import of raw materials and spares. The company is also selling its stake in a joint venture with U.S. firm RAK Laticrete, a joint venture between RAK Ceramics and Laticrete International, which manufactures tile installation systems and waterproofing products for distribution throughout the Middle East and Africa.

Samina Capital bought a 31% stake in RAK Ceramics in 2014

Stake Sale to Samina Capital: Investment firm Samena Capital, the principal investment group focused on the subcontinent, Asia, Middle East and North Africa, bought a 31% stake in RAK Ceramics in 2014. The acquisition was made through Samena Capital's subsidiary Samena Limestone Holdings and its consortium of international investors including two Gulf sovereign wealth funds. The shares were acquired from the ruling family of Ras Al Khaimah, who will continue to maintain a significant holding in the business. Under the terms of the transaction, Samina will be represented on the company Board and the two companies will work together to use private equity strategies to unlock new growth opportunities.

Samena Capital planned to hold its investment for between 3 to 5 years

Samina usually looks for between 25-30% on any investment

Samena Capital has regulated investment advisors based in London, Dubai, Hong Kong and an affiliated office in Mumbai, who collectively manage total capital



commitments of approximately USD870 million across three primary investment strategies – private equity, credit and hedge fund seeding. Samena Capital planned to hold its investment for between three and five years. Samina usually looks for between 25-30% on any investment.

Financial Strength of the RAK Ceramics PSC, UAE

Revenues & profits grew at a Compounded Annual Growth Rate (CAGR) of 14.7% & 8.1% respectively over period of 2001-2013

In FY2013, consolidated revenue of RAK Ceramics -PSC UAE reached to AED 3,514.8 million (USD 956.9 million). During last 13 years revenue and profits have shown consistent growth. Revenues and profits grew at a Compounded Annual Growth Rate (CAGR) of 14.7% and 8.1% respectively over period of 2001- 2013 as compared to about 6% per annum global industry growth rate. As of December 2013, asset base of the group reached to AED 5,679 million (USD 1546.2 million) with a CAGR of 13.8% over 2001-13 and net worth stood at AED 2473 million (USD 673 million) with a CAGR of 11% over 2001-13. Production and marketing capacity have increased at a CAGR of 13.4% since inception in 1991 to reach a position of world's largest ceramic manufacturer. The company has a well-diversified revenue base with 85% of revenues from exports outside UAE (of which 50% in GCC and other Asian region and 15% revenues generated in Europe) as part of Company's strategy to diversify market risks. The Group continues to remain satisfactorily levered, with debt-equity ratio of 1.22 times. Though tiles industry is highly capital-intensive, at 2013 RAK-Ceramics, PSC, UAE has generated handsome return on its capital employed.

Production and marketing capacity have increased at a CAGR of 13.4% since inception

Maintained satisfactory leverage with debt-equity ratio

(Source: RAK Ceramics PSC, UAE annual report, corporate profile and ILSL research)

Business Relation with RAK Ceramics PSC, UAE

Gets significant support from its parent company RAK Ceramics PSC, UAE under 'Technical Know-How and Assistance Agreement'

RAK Ceramics (Bangladesh) Ltd. gets significant support from its parent company RAK Ceramics PSC, UAE under 'Technical Know-How and Assistance Agreement'. Under this agreement, the parent company provides entire technical know-how and assistance in production, testing, safety and quality control. For any further expansion the parent company provides assistance and advisory in terms of technology, capital machineries, civil works support and pre-operating testing. The agreement also covers the areas to provide assistance by way of making available patented process and ensuring the right to avail of technical information resulting from Research and Development, providing technical assistance in management, marketing and assistance in all other technical matters. As per the agreement, RAKCERAMIC pays a recurring royalty fee and other expenses such as expenses for technical knowhow to RAK Ceramics PSC, UAE for each year subject to 2.5% calculated on the basis of net sales of the year.

Parent company also provides assistance regarding raw materials sourcing, business development, governance etc.

Other than the technical agreement, the parent company also provides assistance regarding raw materials sourcing, business development, governance and any other matter as and when needed. RAKCERAMIC has adopted business policy, innovation, quality control, diversification, expansion with similar vision of parent company. On quarterly basis Corporate Management Governance team from UAE visits for performance review and assessment. Every six month at corporate office, operational performance is reviewed by Corporate Board of Directors and Governance Body.

Products and Market Position

RAK's tiles has captured 1/4th share of market and sanitary ware has gained 2/3rd of the market through innovative product development initiatives

RAK Ceramics (Bangladesh) Ltd. produces a wide range of products in the ceramic tiles and sanitary ware. The company is continuously penetrating new markets and developing new products. RAKCERAMIC, a product driven company rather than market driven one, has captured over 1/4th share of market in tiles and 2/3rd of market in sanitary ware over the period.

In Bangladesh, the company has over 1,000 models in tiles and 40 models in Sanitaryware

In Bangladesh, the company has over 1,000 models active in the ceramic and porcelain tile business. The company has over 40 models of sanitary ware of various bathroom utility and luxury products. The company manufactures tiles in a very wide range of sizes in Bangladesh backed by variety of Gres Porcellanato (porcelain/fully vitrified tiles). Under "ceramic tiles" range, the company produces wall tiles, floor tiles, matching accessories listellos, pencils, cappings, border and décor tiles. In "Gres Procellanato" tiles category, it produces thousands sub-categories of glazed and unglazed porcelain, salt and pepper (mirror polished and unpolished), soluble salt (mirror polished) and double charge (mirror polished) tiles. Finishes such as Rustic, Slate, Brick Style and Wooden are some of the wide range of effects on offer. Under sanitary ware division, RAKCERAMIC produces wash basin (mounted and pedestal), water closets (WC), bidets, water tank, kitchen sinks and related accessories and decorated sets. Some of the popular sanitaryware models are- Amanda, Venice, Mistral, Shino, Jumeirah etc. In accessories the company introduced Soft Closing Seat and Cover and Hydraulic Hinges.

RAKCERAMIC has mostly professional and brand conscious clientele base. RAK Ceramics (Bangladesh) Ltd. targets mainly architects, project developers and retail clientele. A leading global tiles and sanitary ware producer RAK Ceramics distributes its products through company appointed dealers. Technology and product leadership, superior brand positioning, ability to deliver wide range of customer requirements at lower service costs and established infrastructure and delivery capabilities are the key competitive advantage of RAK Ceramics.

In order to maintain its competitiveness, in the highly competitive ceramics business, RAK Ceramics carries on innovative approaches which allow the company to reach a broader public base and ensures that the brand has distinctive points of values above the other players from the same category. Efforts in all these areas have resulted in increased revenues and market share.

Production Capacity and Capacity Utilization

Plant standard capacity of RAK Ceramics is 8.03 mn sqm tiles per annum and 1.10 mn pieces Sanitaryware per annum

As on 31 December, 2014 the plant standard capacity of RAK Ceramics is 22,000 square meter tiles per day and 8.03 million square meters per annum and 3,400 pieces of sanitary ware per day and 1.10 million pieces per annum. During the year 2014, 72.8% capacity has been utilized for tiles while it was 118.2% for sanitary ware segment.

In the year 2000, RAKCERAMIC instigated production with first tiles manufacturing plant having capacity of 2.92 million square meters (31.43 million sq. feet) per year. Later in 2004, it has approached second tiles plant of additional manufacturing



capacity of 2.56 million square meters (27.56 million square feet) per year. In the year 2008, it has approached third tiles plant with additional capacity of 2.56 million square meters (27.56 million square feet) per year.

In 2004, RAKCERAMIC approached 1st phase of sanitary wares plant with capacity of 300,000 pieces per year. In the year 2007, it has approached 2nd expansion phase with extending sanitary wares capacity with additional 400,000 pieces per day. Looking forward to market potential and demand in 2010, sanitary wares capacity was increased by another 400,000 pieces per year.

Particulars	2010	2011	2012	2013	2014
Tiles					
Installed capacity: (In mn sqm) yearly	8.00	8.00	8.00	8.03	8.03
Production (In mn sqm)	6.74	7.23	6.67	6.32	5.84
Capacity utilized (%)	84.3%	90.4%	83.4%	78.7%	72.8%
Sanitary ware					
Installed capacity: (In mn pieces) yearly	1.10	1.10	1.10	1.10	1.10
Production (In mn pieces)	1.15	1.23	1.26	1.29	1.30
Capacity utilized (%)	104.5%	111.8%	114.5%	117.3%	118.2%

The company is increasing its annual capacity by 3.5 mn sqm of tiles from the current 8.03 mn sqm (43.58% escalation), and by 0.35 mn pieces of sanitary ware from 1.1 mn (31.82% enhancement)

The company is planning to increase annual capacity by 3.5 million square meter of tiles from the current 8.03 million square meter (43.58% escalation), and by 0.35 million pieces of sanitary ware from 1.1 million (31.82% enhancement). These capacities are expected to come on stream within 2015. Additional allocation of gas supply has already been approved by the government for this enhanced capacity. The Bangladesh plant of the company is situated at Dhanua, Sreepur, Gazipur.

Raw Materials

Import 90% of raw material needs from overseas

The Company's key raw materials are Clays, Silica, Feldspar, Glaze Materials and Bonding agents. The company Import 90% of raw material needs from overseas, mainly from India, China, UAE, UK, Singapore, Thailand and few other European countries etc. Key suppliers include SACMI Imola, Gruppo B&T, Cerfrit, Hindalco, FERRO and local suppliers. Clay Local sand/ lime stone/ silica sand are sourced from various suppliers in Shepur, Sylhet. Most of the raw material prices witnessed on an average 14% increases during the year 2013, which is pushing the cost of production. However, it enjoys a diversified procurement base and leverages purchases through its parent company (RAK Ceramics Co. PSC), which ensures competitive pricing and hedging against adverse currency fluctuations.

Shareholding Structure and the Board of Directors

77.22% shares are held by the sponsors/ directors

Initially, 90% ownership of RAK Ceramics (Bangladesh) Limited were held by RAK Ceramics PSC and its nominees, a company incorporated under the laws of UAE and remaining 10% were owned by local investor Mr. S.A.K. Ekramuzzaman. Presently, RAK Ceramics PSC, UAE is presented by Mr. Abdallah Massaad as Chairman.



Shareholding Pattern			
Name	Position	%	No. of Shares held
RAK Ceramics PSC, UAE	Parent Company	72.41	243,910,021
S.A.K. Ekramuzzaman	Managing Directors	4.81	16,211,985
Abdallah Massaad	Chairman	0	14
General public (including EII & employee)		<u>22.78</u>	<u>76,728,591</u>
		<u>100</u>	<u>336,850,611</u>

Source: Company annual Report and DSE

The company became listed in DSE and CSE in 2010 under Book building method. At present, 77.22% of total shares of RAKCERAMIC are held by the sponsors/directors 10.29% by institutional investors and rest 12.49% by general public.

RAK ceramic has experienced board of directors consisting of six members including nominee from the parent company RAK Ceramics PSC, UAE and two independent directors.

Board of Directors	
Mr. Abdallah Massaad	Chairman (Nominee of RAK Ceramics PSC, UAE)
Mr. S.A.K. Ekramuzzaman	Managing Director
Mr. Khaled Abdulla Yousef Aal Abdulla Aal Abdulla	Director (Nominee of RAK Ceramics PSC, UAE)
Mr. Pramod Kumar Chand	Director (Nominee of RAK Ceramics PSC, UAE)
Mr. Rafique-ul Huq	Independent Director, Barrister-at-Law
Mr. Wassim Moukahhal	Independent Director

Dividend Trend

RAK ceramics maintains stable dividend policy. So far, the Company has paid handsome cash and bonus dividend conjointly. Since the listing in DSE, the company has declared stable 15% cash and 10% stock dividend for each of the successive years up to 2013. However, the company has announced 25% cash dividend for the year ended in December 2014.

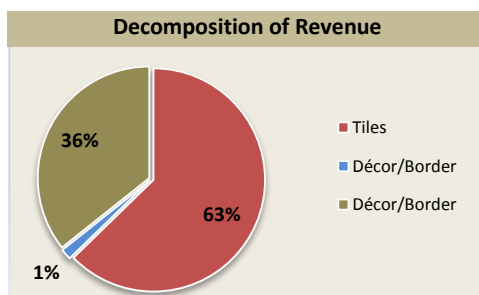


Revenue Decomposition

Ceramic and Gress Porcelain (GP) tiles are the key revenue sources generating around 67% of total revenue. Sanitary Wares contributes 38% while Décor/Border contributes 2% of the company's revenue as per the annual report 2014.

67% revenue comes from Ceramic and Gress Porcelain (GP) tiles

99.6% of the production is consumed in local market



Being a multinational entity and delivering quality products at affordable prices, RAK Ceramics has strong brand equity in the local market. About 99.6% of the production is consumed in local market and rest 0.4% is exported. Exposure to international market is

increasing day by day. The company primarily focuses on local market where it gained 25% of tiles and 67% of sanitary ware market share in Bangladesh. RAKCERAMIC export ceramic and GP (homogenous) tiles to India, Nepal and Sri Lanka. RAK Ceramics also exported a huge amount of sanitary ware to USA through UAE.

Financial Analysis and Performance

Sales revenue also experienced a steady growth with a CAGR of 7.5%

The overall business performance of RAKCERAMIC has been found to be good with increasing production capacity as well as high capacity utilization. The company utilized excess capacity in its Sanitaryware segment leaving the room for forthcoming expansion. However, Sales revenue also experienced a steady growth with a CAGR of 7.5% from 2009 to 2014. The revenue (including discontinued operation) grew at a 6.57% compared to previous year, a result of volume and value growth in existing businesses. Raw Materials cost decreased by BDT 60.14 million in 2014, due to production of bigger size tiles and increase in production volume.

Key Financials	2010	2011	2012	2013	2014
Turnover (In BDT million)	4,009	4,580	4,908	5,169	5,509
Cost of goods sold (In BDT million)	2,505	2,694	2,965	3,073	3,255
Net Profit (excluding non-controlling interest) (In BDT million)	606.5	757.0	608.1	682.4	562.8
COGS to sales	62.5%	58.8%	60.4%	59.4%	59.1%

**Source: Company Annual Reports and ILSL research

However, Cost of goods sold increased due to increase in turnover as well as labor cost. Marketing expenses increased by 21.07% (BDT 180.21 million) mainly due to increase in advertisement expenses, discount expenses, performance rebates, local freight cost and annual increment of 15% on staff cost. During the year Interest expenses decreased due to decrease in bank borrowings by the subsidiary/associate.

Particulars (In BDT million)	2010	2011	2012	2013	2014
Current Assets	3,962	4,768	4,948	5,965	7,123
Current Liabilities	1,923	2,078	2,490	3,032	3,538



Net Current Assets	2,039	2,691	2,458	2,933	3,585
Net Fixed Assets	3,079	2,973	3,342	3,022	2,354
Net Capital Employed	5,118	5,664	5,800	5,955	5,939

During the year 2014, the current assets has been increased, while the fixed assets decreased as the company sold one of its subsidiary; total assets value of the subsidiary has been presented in the current asset component as assets held for sale in the financial statement for the year 2014. However, there has been an addition of BDT 143.63 million in fixed assets during the year mainly to expand its capacity in tiles and Sanitaryware production. The Company also invested BDT 289.12 million in heavy equipment in its ceramic tiles and Sanitaryware facility which is expected to be commissioned within 2015.

Profitability

Divestment plan of non-core business is likely to reduce share of loss from associate companies

In 2013, the net profit after tax (net of non-controlling interest) experienced 12.2% growth in line with substantial decrease in non-operating expenses and decrease in share of loss of associated companies. However, it has reduced by 17.5% in 2014 mainly because of increase in selling and marketing expenses. Large investment in marketing expenses can increase the competitiveness of the company in future. Share of loss from associate company's equity holding has been reduced by 34.9% in 2013. However, the net loss from associate investment increased by 18.8% in 2014 due to adjustment from the loss on acquisition of the associates in the previous year. Recently the company has divested its one of the subsidiary RAK pharmaceuticals, which was a losing concern for the company. So, this divestment is likely to increase the company's future earnings with a larger contribution from its core business.

Key Financials	2010	2011	2012	2013	2014
Gross profit margin	37.51%	41.19%	39.60%	39.10%	39.14%
Operating profit margin	18.79%	21.72%	18.85%	23.80%	20.95%
Net profit margin	12.72%	14.01%	10.19%	12.48%	9.67%
Return on assets	8.02%	8.68%	6.24%	6.82%	5.29%
Return on equity	13.71%	12.54%	9.20%	10.37%	8.32%

Source: Company Annual Reports and ILSL research

RAK Ceramics enjoys handsome margin on its sales. Strong parent lineage and global experience enables the company easy access to latest technological advancement and thus reduce cost of sales. However, increased selling and distribution expense has been reducing the operating profit margin over the year.

Operating Efficiency

Operating efficiency of the company has increased in 2014 by reducing days in operating cycle. At the same time, increase in payables payment period helped the days in cash conversion cycle to drop. Meanwhile, total asset turnover remained almost same but fixed asset turnover increased due to accounting for divestment plan of subsidiary company.



Particulars	2010	2011	2012	2013	2014
Inventory Turnover Ratio	2.9	2.9	2.9	2.5	2.6
Receivable Turnover Ratio	11.6	10.0	8.5	8.0	8.9
Average Collection Period (Days)	31.0	35.9	42.4	45.2	40.6
Inventory Conversion Period(Days)	122.8	123.6	126.0	143.5	136.4
Operating Cycle (Days)	153.7	159.6	168.4	188.8	177.0
A/C Payable Turnover Ratio	3.9	6.5	10.8	11.3	9.7
Payables Payment Period (Days)	92.2	55.5	33.3	31.9	37.1
Cash Conversion Cycle (Days)	61.5	104.0	135.1	156.9	139.9
Total Asset Turnover	63.0%	62.0%	61.2%	54.7%	54.7%
Fixed Asset Turnover	138.0%	164.2%	171.4%	164.8%	212.6%

Liquidity Performance

RAKCERAMIC's liquidity position seems to be good enough. Within the current assets composition of the company, it appears that 28.9% of its current assets are in the form of inventory, 9.2% in the form of trade debtors, 4.58% in the form of advances, deposits and prepayments, 32.84% in advance income tax, 0.64% in loan top associated companies and rest 23.91% in the form of cash and cash equivalent assets. Inventory conversion period is too long which was 223 days in 2013 against 211 days in 2012. The average collection period seems an increasing trend over the year which was 36 days in 2011, 43 days in 2012 and 42 days in 2013 but average payable period follows a decreasing trend over the year.

Handsome liquidity position

Particulars	2010	2011	2012	2013	2014
Current Ratio	2.06	2.30	1.99	1.97	2.01
Quick Ratio	1.29	1.50	1.27	1.31	1.49

Because of long inventory holding period along with increasing gap between account receivables and account payable period, cash conversion cycle of the company stood at 236 days in 2013 against 220 days in 2012. From the cash flow statements of 2014 financial reports, it is revealed that the company has generated BDT 618.3 million cash flows from its operating activities up to December 2014.

Financial Strength and Solvency

RAKCERAMIC has been operating with an equity based capital structure which is composed of 62% equity capital and 38% liability as on December 2014. Among the debt capital, 2.2% is the long term debt and rest 97.8% is the short term debt. Therefore, the capital structure composition reveals that 9% of its total liability is composed of Bank loan, where 100% is the short term loan.

Equity based capital structure

Good debt servicing capacity

Less risky and more likely to get further debt financing

Particulars	2010	2011	2012	2013	2014
Total Debt to Equity (X)	2.4%	8.0%	7.3%	8.3%	5.5%
Debt to Total Assets (X)	1.7%	5.5%	4.9%	5.4%	3.4%
Interest coverage ratio (X)	18.3	29.8	64.7	86.2	136.3

Source: Company Annual Reports and ILSL research



*Less risky and more likely to get
further debt financing*

The equity pie of the RAKCERAMIC, net of non-controlling interest, is composed of 56.9% of equity capital, 24.9% share premium and 18.2% of retained earnings as on December, 2014. Consequently, the debt to equity ratio and debt to total asset ratio remained very low and reduced further in FY 2013. Due to less dependency on debt it also exhibited substantial strength to pay off its debt obligation. The interest coverage ratio has increased substantially in 2014, which has been possible with decrease in interest expense during the year in the continuing operation. This ratio reflects the fact that RAKCERAMIC affordability to pay interest expenses has increased and the company is now less risky and more likely to get further debt financing from lenders. Based on retained earnings position, effective use of borrowed capital, and payment of liability made the company more solvent over the year.

Investment Insights

- RAK Ceramics is pursuing an attractive expansion plan to grow its tiles and sanitary ware production capacity at round 45% and 33% respectively. However, 21% of tiles and 25% Sanitary ware expansion is expected to come on operation within 2015.
- No additional expenditure towards land, utility and ancillary infrastructure cost is needed for expansion as the new production is coming within the premises of existing plants.
- The company enjoys off-shore financing facility. As, the capital expenditure is being funded out of 70% USD denominated debt and 30% internal accruals, the cost of debt is significantly lower. Moreover, the debt has been structured at an attractive 1 year moratorium.
- The company has divested its stake in RAK Pharmaceuticals Pvt. Ltd, a losing concern for the company, to a Middle East Pharma giant. Even though the divestment has been conducted at a loss, this will increase the portability of the company in the coming years.
- In 2014, the Company invested BDT 144 million as capex towards establishing nano-polishing machine, striping machine, glaze tank, forklift and digital machines. This enabled the company to optimize resource consumption and deriving higher margin.
- RAK Ceramics has received approval of gas (fuel) connection for expanding unit and the company is now locked in 6.5 lac cubic meter/month of natural gas at attractive cost, which will ensure uninterrupted production.
- RAK enjoys strong parent lineage and global experience that enable them easy access to latest technological advancement.
- Due to ongoing political instability and the depressed trend in real estate business, a huge number of flats have remained unsold. According to the market players, 24,000 flats are currently unsold. This in other words reflects the probable decrease of demand for construction materials.

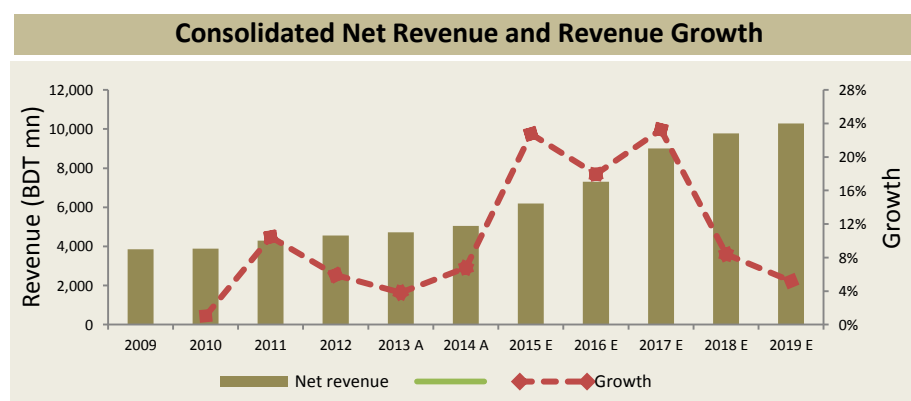
Valuation

Given the information available in the annual report and based on the company and industry analysis, our valuation for RAK Ceramics stands at **BDT 62.1** per share. With current market price of BDT 57.2 as on April 22, 2015, we perceive that the stock is **undervalued**.

Key assumptions underlying the valuation

Revenue: For RAK ceramic, installed capacity of tiles segment has been expected to increase by 21.2% within June, 2015 and that of sanitary ware by 25% from September, 2015. However, we assumed that full planned capacity i.e. capacity of tiles to 11.53 million square meter and that of sanitary ware to 1.45 million pieces per year will be installed within 2017.

Installed capacity of tiles segment is expected to increase by 21.2% within June, 2015 and that of sanitary ware by 25% from September, 2015



Source: RAK Ceramic's Annual Report and ILSL Research

Full planned capacity is expected to come on stream within 2017

Average capacity utilization of tiles production over the last five years was 82% and the company is in the process of upgrading its existing machineries. Considering all the facts, we assumed that capacity utilization for tiles will remain 82% over the next five years. The company is now utilizing its excess capacity in its Sanitaryware production. Capacity utilization in 2014 in this segment was 118.2% and 5 years average capacity utilization was 113.3%. After the completion of its capacity expansion we expect that its capacity utilization will decline over the next five years. However, per unit price of tiles is expected to grow at a rate of 6 to 8% and that of sanitary ware at 6.4% over the next 5 years.

As the power sector has limited growth opportunity, we assumed that revenue of RAK power will grow only at a rate of 2.5% to 3% over next 5 years.

Classified COGS items has been forecasted based on historical average as proportion to net sales

Cost of Goods Sold: Cost of sales for RAK Ceramics has been forecasted based on the detailed item wise forecast as a percentage on net sales based on historical average or company practices. However, summing up the detailed classified forecast COGS in next 5 year will be within 59.5% to 61.8% in next five years. Based on the average of last two years company practice, 94.1% of the depreciation on fixed asset is charged as cost of sales for the next five years.



Historical Cost of Goods Sold as percentage of sales for RAK Power reveals a declining trend. Last three years average CoGS as percentage of sales is 60.5%. We assumed that this declining trend will continue in future and will remain within the range of 58.0% to 60.5% in next five years.

Selling and Distribution Expenses: Five year's average selling and distribution expense as percentage of sales was 9.7%. Based on in-depth item wise forecast, in next five year this expenses are expected to remain within the range of 9.3 to 9.7%.

Administrative Expenses: AK ceramic's Historical 5 year average of administrative expense as percentage of net sales stands at 4.7%. However, we have analyzed detailed item wise expenses and forecasted based on historical average. Administrative expense also includes managing director's remuneration, which is 3% of net profit before tax. We assumed the same rate will be applied in future. However, 5.9% (calculated as an average of last two years) of depreciation on fixed asset is also charged as administrative expenses. Based on the historical data, RAK power's 5 year average administrative expense as a percentage of sales is 2.37% and we assumed that the cost will remain at same proportion in future.

*BDT 31.5 million net gains from
divestment of subsidiary and
associate in 2015*

Gain on Sale of Investment: RAK ceramic divested one of its subsidiary and an associate in 2015. The company is likely to avail BDT 600 million and BDT 19.9 million gains from the sale of its stake in RAK Pharmaceuticals and RAK-Mosfly (Bangladesh). However, The Company incurred BDT 589 million losses in the disposal of parent company loan to the discontinued subsidiary. Hence, the company might avail around BDT 31.5 million net gains from this divestment plans.

Effective rate of interest is 5.3%

Finance expenses: RAK ceramic maintains lower financial leverage. The company did not maintain any long term borrowing in from year 2010 to 2013. However, the company used short-term loan within these period. The company enjoys off-shore financing from HSBC, Standard Chartered Bank and Citibank, N.A. Interest rate for the company as on 2014 was Libor+ (2.75%-3.84%) and rate on short term bank loan (local currency) and bank overdraft was 12-13.5%. The planned capex of the company is being funded out of 70% USD denominated debt and 30% internal accruals. The debt has been structured at an attractive 1 year moratorium. However, we considered an effective interest rate to be 5.3%.

*Capex is being funded out of 70%
USD denominated debt and 30%
internal accruals*

RAK power also did not show any long term loan in last three year's financials. The company also not has taken any short term loan in last two financial years. We assumed this practice will be continued in future. So, no finance expense is likely to occur for RAK Power in next five years.

*Avails interest income from
investment in FDR, SND account,
loan to group companies and
foreign exchange gain*

Finance Income: Historically RAK ceramic earned finance income from investment in FDR, SND accounts, loan to different group companies and exchange gain. Last three years average interest rate on FDR is 10.5% and the FDR rate of the company was 6.4-8.25% as on December, 2014. We assumed that it will be 8% for the next five years. And effective interest rate on loan to group company stands at 14.9%. However, we assumed that a conservative 10% rate to be applied in this kind of loan.



However, based on 3 years historical average RAK power's interest income on FDR we expect that interest income on FDR in coming years will be 6% and on SND, it will be 1.6% on 2 years average balance.

Weighted Average Cost of Capital (WACC)

Expected cost of capital or discount rate is 13.4%

Cost of equity was calculated by using build-up Method. We considered RAKCERAMIC's operating and financial leverage to estimate operating and financial risk premium and added 1% as the country risk premium. Finally, we added this total risk premium with risk free rate. Last six years average cut off yield of 5-year T-bond is used as risk free rate.

Weighted Average Cost of Capital (WACC)				Calculation of Risk Free Rate	
		Weight	Amount (in BDT mn)		
Risk Free Rate	9.5%			5 year T-bond rate	
Equity Risk Premium	5.0%			Year	T- bond rate
Cost of Equity (Build-up)	14.0%	94.8%	5919.4	2009	7.80%
Cost of Debt	5.3%	5.2%	323.8	2010	8.11%
				2011	8.50%
WACC	13.4%			2012	11.52%
				2013	11.23%
				2014	9.60%
				Average	9.46%

Terminal Growth Rate

Terminal growth rate is assumed to be 4.5%

Average 4 year CAGR of the consolidated was 7.5% up to 2014. GDP growth rate of Bangladesh for the year 2013-14 was 6.1%. However, the country is significant impacted by political turbulence. Current growth in overall construction sector is also experiencing bearish vibe. The terminal growth rate of the company has been assumed as 4.5% considering all the macroeconomic and industry related factors.

Valuation Methods

Discounted Cash Flow Analysis

	(in BDT mn)	2014 E	2015 E	2016 E	2017 E	2018 E	2019 E	Terminal
Profit for the Year		612	962	1,113	1,550	1,555	1,569	
Add: Net Interest Expenses After Tax		5	14	19	32	50	67	
Add: Depreciation & Amortization		257	314	334	249	247	320	
Changes in NWC		-136	-21	-107	-301	-30	412	
CAPEX		-389	-1,438	-596	-225	-244	-257	
Free Cash Flow to the Firm		349	-169	763	1,305	1,579	2,111	24,728
Enterprise Value as on 22 April 2015		17,288						
Plus: Cash & Cash equivalent		1,474						
Plus: Cash proceeds from divestment		425						
Less: Interest bearing debt		324						
Equity Value		18,863						
No. of Share Outstanding		337						
Value per Share		56						



Our DCF analysis with a discount rate of 13.4% and terminal growth rate of 4.5% gives us Net Present Value (PV) of Free Cash Flow to Firm (FCFF) of BDT 17.3 billion as on April 22, 2015. In valuing RAK Ceramics, we also compared other ceramic companies that are listed on the DSE. After discounting, the fair value stands at BDT 56.0 per share respectively as on 22 April, 2015.

Sensitivity Analysis

We also checked the sensitivity analysis of DCF value per share on discount rate and terminal growth rate. We considered discount rate with a range of 12.5% to 14.5% and terminal growth rate with a range of 3.5% to 4.8%. As a result, we got a value range from BDT 46.23 to BDT 64.75.

Sensitivity Analysis						
Discount Rate						
Terminal Growth		12.5%	13.0%	13.4%	14.0%	14.5%
	3.5%	57.12	53.96	51.66	48.56	46.23
	3.8%	58.41	55.10	52.70	49.46	47.04
	4.0%	59.78	56.30	53.79	50.40	47.88
	4.5%	62.77	58.91	56.15	52.44	49.70
	4.8%	64.75	60.63	57.69	53.77	50.88

Relative Valuation Method

The peer group valuation is performed to compare the intrinsic value of RAK Ceramics arrived at using the DCF calculation. In order to value RAK CERAMIC using this method, we have used the average price-to-earnings (P/E) multiple for ceramic sector with a basket of comparable companies listed in the exchanges. The price-earnings multiple of a stock is a reflection of various factors, such as the expected profitability of the company, its growth potential as perceived by the market, predictability and sustainability of its revenues, the quality of its earnings and the quality of its management, among others.

Relative Valuation		
Method 1: Price/Earnings Multiple		
Particulars	Multiple	Value (in BDT)
Sector's F.P/E	34.3	100.4
Sector's Trailing P/E	31.2	52.11
Estimated Value (Average)		76.25
Method 2: Price/Book Value Multiple		
Particulars	Multiple	Value (in BDT)
Sector's P/B	1.5	27.5
Market's P/B	1.5	17.6
Estimated Value (Average)		22.5

To arrive at the peer-set P/E multiple, we have computed the average trailing and forward P/E of ceramic sector in DSE based on the current market prices.



Determination of Fair Value

The price-earnings multiple and price to book value multiples varies with time and is dependent on several factors, such as market sentiment and other qualitative factors, we have provided a lower weight of 30% to the PE based peer valuation method 0% weight on P/B based Valuation method, and 70% weight to the value arrived at using the DCF method.

Valuation Methods	Estimated Value	Weights
Discounted Cash Flow (FCFF)	56.00	70%
Price/Earnings Multiple	76.25	30%
Price/Book Value Multiple	22.52	0%
Fair Value	62.08	100%
Current Price (as on 16 March, 2015)		
		57.20
ILSL Fair Value		
		62.08
Expected Capital Gain		
		8.52%
Expected Dividend Yield		
		4.37%
Total Return		
		12.90%

At their current price, RAKCERAMIC's shares have a P/E multiple of 34.2 for 2014 earnings. With our recommended intrinsic value the stock gives at total of 12.9% expected return. We therefore recommend a 'Buy' on the RAK Ceramics Company's stock at its prevailing price levels.

Risks to our rating and price target

Changes in our assumptions on ceramic prices and volumes and country's overall macro-economic atmosphere are the main factors that could cause us to amend our estimate of RAK ceramic's future performance. Other risks include the slowdown in the overall construction activity coupled with potential competition from other players in the industry within the country may also hamper the expected growth of the company.



Annexure: 01
Consolidated Income Statement
(Based on Continued Operation)

(in BDT mn)	2013 A	2014 A	2015 E	2016 E	2017 E
Net Turnover	4,725	5,047	6,110	7,310	9,012
Cost of Goods Sold	2,878	3,072	3,649	4,353	5,202
Gross Profit	1,847	1,975	2,461	2,957	3,809
Other Income	7	4	30	11	12
Operating Expenses:	730	922	1,112	1,300	1,529
Selling and Distribution Expenses	487	665	812	933	1,085
Administrative Expenses	243	257	300	367	443
Profit From Operations	1,125	1,057	1,380	1,668	2,292
Financial Expenses	13	8	20	28	48
Interest Income	130	129	145	141	172
Gain on sale of investment	0	0	32	0	0
Share of Profit / (loss) of equity (associate companies)	(50)	(59)	(54)	(54)	(49)
Profit Before WPPF	1,192	1,119	1,481	1,727	2,368
Allocation for WPPF	59	49	67	81	111
Profit Before Tax	1,133	1,071	1,414	1,647	2,257
Income Tax Expenses	358	421	397	481	671
Provision for Income Tax	385	437	419	500	671
Provision for Deferred Income Tax	(27)	(16)	(23)	(19)	0
Profit After Tax	775	650	1,017	1,165	1,586
Profit (loss) on discontinued operation	(185)	(162)	0	0	0
Total Comprehensive Income for the Year	590	488	1,017	1,165	1,586
Non-controlling interest					
From continued operation	32	38	33	34	35
From discontinued operation	(125)	(113)	0	0	0
Profit Attributable to owners of the Company	682	563	985	1,131	1,550
From continuing operation	743	612	985	1,131	1,550
From discontinued operation	(60)	(49)	0	0	0
Earnings Per Share (EPS) - Restated (Continuing op)	2.21	1.82	2.92	3.36	4.60
EPS (including discontinued operation)	2.03	1.67	2.92	3.32	4.60



Annexure: 2
Consolidated Statement of Financial Position

(Figure in BDT mn)	2013 A	2014 A	2015 E	2016 E	2017 E
Assets:					
Non-Current Assets:	3,022	2,354	3,804	4,068	4,049
Property, Plant and Equipment-Carrying Value	2,734	2,014	3,285	3,709	3,834
Equity-accounted investee	87	28	27	25	24
Intangible Assets, net	106	5	4	5	6
Capital Work-in-Progress	35	289	473	313	163
Loan to associates	60	18	15	18	22
Current Assets:	5,965	7,123	6,357	7,292	9,199
Inventories	1,990	1,835	2,198	2,630	3,232
Trade & other Debtors	558	581	501	502	597
Loan to associates	36	41	36	36	45
Advances, Deposits and Prepayments	231	367	254	304	373
Advance Income Tax	1,656	2,014	2,365	2,777	3,331
Cash and Cash Equivalents	1,494	1,474	1,003	1,047	1,621
Assets held for sale	-	812	-	-	-
Total Assets	8,987	9,477	10,162	11,360	13,248
Shareholders' Equity and Liabilities:					
Shareholders' Equity:	5,816	5,919	5,631	5,741	6,271
Share Capital	3,062	3,369	3,369	3,369	3,369
Share Premium	1,473	1,474	1,474	1,474	1,474
Retained Earnings	1,280	1,077	789	899	1,429
Non-Controlling Interest	26	(59)	(26)	8	44
Non-Current Liabilities:	113	78	55	37	37
Borrowings	18	-	-	-	-
Deferred Tax Liability	94	78	55	37	37
Current Liabilities:	3,032	3,538	4,501	5,574	6,897
Borrowings	463	324	1,206	1,495	1,786
Employees benefits Payables	31	71	14	17	20
Trade Creditors	279	355	301	360	442
Accrued expenses	193	152	188	227	278
Provision for Income Tax	1,841	2,182	2,602	3,102	3,774
Provision for royalty and technical know-how fees	226	38	190	373	597
Liabilities held for sale	-	415	-	-	-
Total Shareholders' Equity and Liabilities	8,987	9,477	10,162	11,360	13,248
Net Asset Value Per Share (NAVPS)	17.27	17.57	16.72	17.04	18.62



Annexure: 03
Indicators (Consolidated based on Continuing Operations)

Particulars	2013 A	2014 A	2015 E	2016 E	2017 E
Liquidity Ratios:					
Current Ratio	2.0	2.0	1.4	1.3	1.3
Quick Ratio	1.3	1.5	0.9	0.8	0.9
Operating Efficiency Ratios					
Inventory Turnover Ratio	1.5	1.6	1.8	1.8	1.8
Receivable Turnover Ratio	8.0	8.9	11.3	14.6	16.4
Inventory Conversion Period (Days)	239.0	227.3	201.7	202.4	205.6
Average Collection Period (Days)	45.9	41.2	32.3	25.0	22.3
Operating Cycle (Days)	284.8	268.4	234.0	227.4	227.9
A/C Payable Turnover Ratio	11.3	9.7	11.1	13.2	13.0
Payables Payment Period (Days)	32.4	37.6	32.8	27.7	28.1
Cash Conversion Cycle (Days)	252.5	230.8	201.2	199.7	199.8
Total Asset Turnover	54.7%	54.7%	62.2%	67.9%	73.2%
Fixed Asset Turnover	164.8%	212.6%	230.6%	209.1%	239.0%
Operating Profitability Ratios					
Gross Profit Margin (GPM)	39.1%	39.1%	40.3%	40.5%	42.3%
Operating Profit Margin (OPM)	23.8%	20.9%	22.6%	22.8%	25.4%
Net Profit Margin (NPM)	16.4%	12.9%	16.7%	15.9%	17.6%
Return on Total Assets (ROA)	9.0%	7.0%	10.4%	10.8%	12.9%
Return on Equity (ROE)	13.6%	11.1%	17.6%	20.5%	26.4%
Leverage Ratios					
Total Debt to Equity	8.3%	5.5%	21.4%	26.0%	28.5%
Debt to Total Assets	5.4%	3.4%	11.9%	13.2%	13.5%
Times Interest Earned (TIE)	86.2	136.3	68.6	60.1	48.2
Valuation Ratios					
P/B (price to book) Ratio	3.3	3.3	3.4	3.4	3.1
EPS	2.0	1.7	2.9	3.4	4.6
P/E Ratio	28.2	34.2	19.6	17.0	12.4
Growth Rates					
EPS Growth Rate	-11.6%	-17.5%	75.0%	14.9%	37.0%
Sales Growth Rate	3.8%	6.8%	21.1%	19.6%	23.3%
Gross Profit Growth Rate	4.6%	6.9%	24.6%	20.2%	28.8%
Op. Profit Growth Rate	0.8%	-6.0%	30.5%	20.9%	37.4%
Net Income Growth Rate	-3.8%	-17.7%	61.0%	14.9%	37.0%
DUPONT ANALYSIS					
Net Profit AT/Sales	15.7%	12.1%	16.1%	15.5%	17.2%
Sales/Total Assets	54.7%	54.7%	62.2%	67.9%	73.2%
ROA	8.6%	6.6%	10.0%	10.5%	12.6%
Net Profit AT/Total Assets	8.6%	6.6%	10.0%	10.5%	12.6%
Total Assets/ Equity	1.52	1.57	1.70	1.89	2.05
ROE	13.1%	10.4%	17.1%	19.9%	25.8%



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Stock Status

Overweight: Expected to outperform the broader market averages;

Market weight: Expected to equal performance of broader market averages;

Underweight: expected to underperform broader market averages.

Not-Rated: Currently the analyst does not have adequate conviction about the stock's total return relative to the broader market average

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