

## In line operating performance

- Welspun India, home textile player exporting largely to US, saw 14% 1Q sales growth with underlying volumes up 10%. Ebitda growth (15%) and in turn EPS growth (13%) was broadly in line with estimates.
- Management expects double-digit sales growth despite some weakness seen in the market, given strong relationship with retailers and healthy demand for product innovations such as Hygro.
- Further despite the sharp 30-40% increase in cotton prices seen over the last few months, Welspun remains confident of maintaining Ebitda margins as it passes on some of the input cost rise and gains from increasing share of sales of high margin products such as Hygro.
- Welspun expects the government to increase export incentives in the near term, aiding margins.
- Multiple growth tailwinds (entry into hospitality, healthcare channels, smart textiles category, rising share of innovative products) should drive 14% EPS Cagr over FY16-19.
- Further, ROCE should expand 300bps over FY16-19 as capex is largely in processing and maintenance (cRs8bn in FY17). Trading at 12x FY18 EPS; we maintain BUY (TP: Rs130 at 14x Jun-18 EPS).

## Result update

	Rs100	Price performance (%)			
		1M	3M	1Y	
<b>CMP</b>	<b>130 (30%)</b>				
<b>12-mth TP (Rs)</b>	<b>130 (30%)</b>				
<b>Market cap (US\$ m)</b>	<b>1,495</b>	Absolute (Rs)	(3.9)	0.1	24.5
<b>Enterprise value(US\$m)</b>	<b>1,868</b>	Absolute (US\$)	(2.9)	0.0	18.5
<b>Bloomberg</b>	<b>WLSI IN</b>	Rel. to Sensex	(9.9)	(7.5)	24.9
<b>Sector</b>	<b>Textiles</b>	<b>Cagr (%)</b>		<b>3 yrs</b>	<b>5 yrs</b>
<b>Shareholding pattern (%)</b>		EPS		45.4	165.0
Promoter	73.5	<b>Stock performance</b>			
FII	13.6	52Wk High/Low (Rs)			120/67
DII	2.3	Shares o/s (m)			1005
Others	10.6	Daily volume (US\$ m)			2
		Dividend yield FY17ii (%)			1.4
		Free float (%)			26.5

## Financial summary (Rs m)

Y/e 31 Mar, Consolidated	2QFY15	3QFY15	4QFY15	1QFY16	2QFY16	3QFY16	4QFY16*	1QFY17*	2QFY17ii	FY16	FY17ii	FY18ii
Gross margin	48.9	53.0	53.6	53.3	54.9	58.3	55.0	54.5	55.3	55.2	55.2	54.6
Employee costs as % of sales	8.1	8.4	8.6	8.9	9.0	9.5	8.5	9.7	8.8	9.0	9.2	9.2
<b>Revenues (Rs m)</b>	<b>14,135</b>	<b>13,459</b>	<b>13,658</b>	<b>13,885</b>	<b>14,723</b>	<b>14,904</b>	<b>16,294</b>	<b>15,926</b>	<b>17,078</b>	<b>59,795</b>	<b>67,615</b>	<b>76,463</b>
% change	22.0	22.0	15.3	21.1	4.2	10.7	NA	NA	16.0	12.8	13.1	13.1
<b>Ebitda (Rs m)</b>	<b>3,169</b>	<b>3,400</b>	<b>3,446</b>	<b>3,598</b>	<b>3,743</b>	<b>4,006</b>	<b>4,326</b>	<b>4,225</b>	<b>4,552</b>	<b>15,575</b>	<b>17,585</b>	<b>18,876</b>
<b>Ebitda Margins (%)</b>	<b>22.4</b>	<b>25.3</b>	<b>25.2</b>	<b>25.9</b>	<b>25.4</b>	<b>26.9</b>	<b>26.6</b>	<b>26.5</b>	<b>26.7</b>	<b>26.0</b>	<b>26.0</b>	<b>24.7</b>
Interest expense (Rs m)	(731)	(816)	(569)	(593)	(515)	(592)	(668)	(353)	(555)	(2,362)	(2,053)	(1,773)
Effective tax rate (%)	30.9	20.3	23.5	33.7	29.8	31.4	30.0	29.0	31.0	31.1	31.1	31.1
Reported PAT (Rs m)	1,299	1,436	1,614	1,632	1,724	1,741	1,994	2,019	2,120	7,029	8,097	8,718
<b>Pre-exceptional PAT (Rs m)</b>	<b>1,299</b>	<b>1,436</b>	<b>1,614</b>	<b>1,632</b>	<b>1,724</b>	<b>1,741</b>	<b>1,994</b>	<b>2,019</b>	<b>2,120</b>	<b>7,029</b>	<b>8,097</b>	<b>8,718</b>
% change	(168.7)	31.1	97.4	55.4	32.7	21.3	NA	NA	23.0	30.2	15.2	7.7

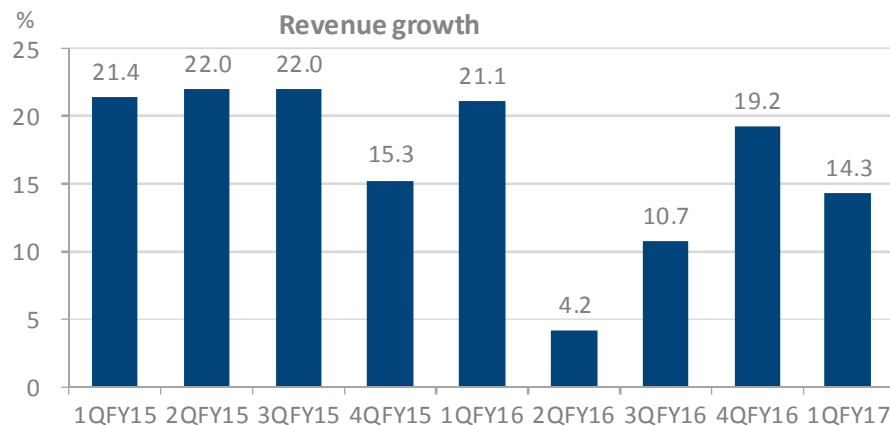
Source: Company, IIFL Research. Priced as on 26 July 2016. \* represents reporting as per Ind AS

## Key takeaways from the conference call

### Expect double digit revenue growth going forward

- Welspun remains confident of maintaining double digit revenue growth trajectory on back of growth across new categories such as fashion bedding, new geographies such as Europe, Japan and India, and new channels such as hospitality and health care.
- Welspun is working with major retailers in Europe and despite 8-9% duty disadvantage vs. Bangladesh and Vietnam has seen 24-25% growth in this segment.
- In Japan, it estimates two more years of business development before gaining a sizeable scale.
- The Indian market continues to grow 20%+ and management expects growth rates to improve going forward.

**Figure 1: Revenue growth has recovered after a blip in 2QFY16**



Source: Company, IIFL Research

### Maintain conservative margin guidance to factor in GST impact

- The company has maintained its Ebitda margin guidance of 22-24% over the medium term.
- It expects margins to remain flattish despite the increase in cotton prices recently. Management believes that it can successfully

negotiate to pass on some of the higher prices to its clients. It also plans to improve upon its product specifications and reduce costs to maintain its Ebitda margins.

### FY17 capex guidance at Rs8bn

- Management reiterated its FY17 capex guidance of Rs8bn.
- It intends to incur Rs3-4bn capex towards its capacity expansion in towels, sheets and rugs and Rs1.5bn capex on the carpets segment (still in research phase). The remaining capex is spill over capex from last year.

**Figure 2: Capacity addition plans in FY17**

Segment	Capacity in FY16	Planned Capacity in FY17	% increase in capacity
Towel	60,000	72,000	20%
Bed Linen	72m mts	90m mts	25%
Rugs/Carpets	8m sq mts	10m sq mts	25%

Source: Company, IIFL Research

**Figure 3: With only 18% of planned capex incurred in 1QFY17, the company is likely to miss its annual capex guidance**

Capex	1QFY16	1QFY17
Capex incurred (Rs bn)	2.2	1.4
As % of annual capex	21%	18%

Source: Company, IIFL Research

### Ancillarization plans on track

- A spinning unit has already become operational under the ancillarization mode. It has a planned production capacity of 45tonnes yarn per day)
- Welspun is in discussion with eleven such players to become supporting ancillaries.
- Welspun believes that through this model, it would be save two-thirds of its capex incurred traditionally and intends to utilize its saved funds towards investing in front end capabilities such as design, distribution, etc.

- Management clarified that this model is not a bottleneck for capacity addition as it always has the option to source yarn and fabric from the open market in case the ancillarization units don't come up in time.

**Others:**

- Growth potential in the US hospitality and health care channels remains immense as Welspun sales from hospitality channel at USD25-30m (vs market size of USD1.5bn across both these segments). Welspun is in business development phase in its healthcare segment.
- Working capital increased in 1QFY17 primarily due to decline in payables driving by maturing of payables.
- Gross debt has increased as the company has availed term loans to meet capex requirements.
- The government recently increased duty drawback rates for apparels by 5% and the company is confident of getting similar benefits in the home textiles space as well.

**Figure 4: Earlier grants were recognized on payment, under Ind-AS they need to be recognized based on depreciation and hence are front-ended**

Ind AS impact on profit	1QFY16	4QFY16	FY16
Net profit as per Indian GAAP	1,650	1,968	7,153
Add			
Effect of change in method of recognizing grants	87	89	353
Deferred tax impact on Ind AS adjustments	111	(46)	(13)
Others	1	19	33
<b>Net profit as per Ind AS</b>	<b>1,849</b>	<b>2,029</b>	<b>7,525</b>
% impact	12.0	3.1	5.2
Other comprehensive income, net of income tax	(107)	265	66
<b>Total comprehensive income as per Ind AS</b>	<b>1,742</b>	<b>2,295</b>	<b>7,591</b>

Source: Company, IIFL Research

**Figure 5: Sharp reduction in payables resulted in increase in working capital**

	FY14	FY15	FY16	1QFY17
Inventory Days	84	76	69	64
Debtor Days	34	31	36	34
Payable Days	51	48	62	45
<b>Total working capital days</b>	<b>67</b>	<b>59</b>	<b>43</b>	<b>53</b>

Source: Company, IIFL Research

**Figure 6: Net debt level has remained stable**

Rs mn	FY14	FY15	FY16	1QFY17
Gross Debt	30,293	30,851	26,661	30,911
Net Debt	26,635	26,554	25,275	25,731

Source: Company, IIFL Research

**Welspun 1QFY17: In Line operating performance**

Welspun India saw 14% sales growth with underlying volumes up 10% and 4% currency gains. Ebitda margin expansion was muted at 20bps as 120bps gross margin expansion was offset by higher employee costs and other expenses. Ebitda was up 15% driving 10% PAT growth. Excluding impact of Ind AS, profit growth stood at 15%, in-line with our estimates. Please note that 1Q financials are as per Ind-AS accounting standards and are not comparable to our estimates.

**Figure 7: Welspun India reported an in-line performance in 1QFY17**

Consolidated (Rs m)	1QFY16	1QFY17	% YoY
Net sales	12,456	13,865	11.3
Other op income	1,475	2,061	39.7
Total income	13,931	15,926	14.3
Total expenses	(10,262)	(11,701)	14.0
Ebitda	3,669	4,225	15.1
Ebitda margin (%)	26.3	26.5	19bps
Depreciation	(785)	(1,121)	42.9
Interest	(593)	(353)	-40.5
Other income	286	189	-33.9
<b>PBT</b>	<b>2,577</b>	<b>2,940</b>	<b>14.1</b>
Tax	(729)	(853)	17.1
% tax rate	28.3	29.0	74bps
<b>Adjusted PAT</b>	<b>1,849</b>	<b>2,087</b>	<b>12.9</b>
PAT margin (%)	13.3	13.1	-17bps
Minority Interest	(18)	(68)	271.2
Reported PAT	1,830	2,019	10.3

Source: Company, IIFL Research

**Figure 8: Gross margin expanded 120bps**

Consolidated Cost details	1QFY16	1QFY17	% YoY
RM	6,500	7,240	11.4
As % of sales	46.7	45.5	-120bps
Staff costs	1,239	1,539	24.2
As % of sales	8.9	9.7	77bps
Power & fuel	328	335	1.9
As % of sales	2.4	2.1	-26bps
Other expenditure	2,195	2,587	17.9
As % of sales	15.8	16.2	49bps

Source: Company, IIFL Research

**Figure 9: Standalone 1QFY17**

Standalone (Rs m)	1QFY16	1QFY17	% YoY
Net sales	11,254	12,979	15.3
Other op income	694	884	27.3
Total income	11,948	13,863	16.0
Total expenses	(8,529)	(10,305)	20.8
Ebitda	3,420	3,558	4.1
Ebitda margin (%)	28.6	25.7	-295bps
Depreciation	(671)	(1,025)	52.7
Interest	(368)	(184)	-50.1
Other income	301	193	-36.0
<b>PBT</b>	<b>2,681</b>	<b>2,543</b>	<b>-5.2</b>
Tax	(801)	(722)	-9.8
% tax rate	29.9	28.4	-146bps
<b>Adjusted PAT</b>	<b>1,881</b>	<b>1,821</b>	<b>-3.2</b>
PAT margin (%)	15.7	13.1	-261bps
Reported PAT	1,881	1,821	-3.2

Source: Company, IIFL Research

**Figure 10: Standalone 1QFY17 cost details**

Standalone Cost details	1QFY16	1QFY17	% YoY
RM	5,049	6,139	21.6
As % of sales	42	44	203bps
Staff costs	928.8	1,148.3	23.6
As % of sales	8	8	51bps
Power & fuel	933.5	1,067.9	14.4
As % of sales	8	8	-11bps
Other expenditure	1,617.3	1,949.0	20.5
As % of sales	14	14	52bps

Source: Company, IIFL Research

**Valuation summary (Rs m)**

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
Revenues (Rs m)	53,025	59,795	67,615	76,463	86,953
Ebitda margins (%)	24.0	26.0	26.0	24.7	24.8
Pre-exceptional PAT (Rs m)	5,398	7,029	8,097	8,718	10,416
Reported PAT (Rs m)	5,398	7,029	8,097	8,718	10,416
Pre-exceptional EPS (Rs)	5.4	7.0	8.1	8.7	10.4
Growth (%)	26.9	30.2	15.2	7.7	19.5
IIFL vs consensus (%)			(3.6)	(11.4)	(4.0)
<b>PER (x)</b>	<b>18.6</b>	<b>14.3</b>	<b>12.4</b>	<b>11.5</b>	<b>9.7</b>
ROE (%)	42.5	41.1	35.1	29.3	27.9
Net debt/equity (x)	1.8	1.2	0.9	0.5	0.3
EV/Ebitda (x)	10.0	8.1	7.1	6.3	5.3
Price/book (x)	7.0	5.1	3.8	3.0	2.4

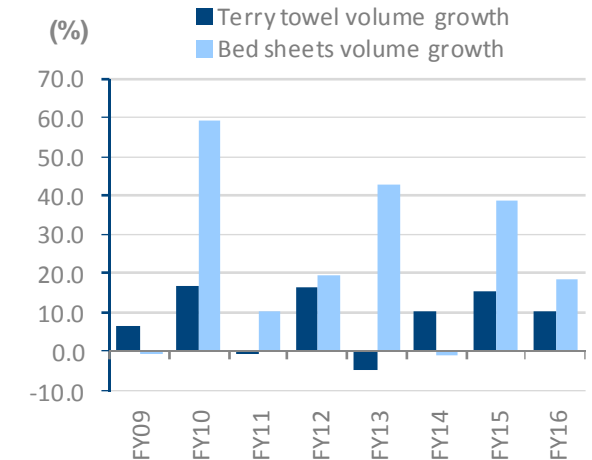
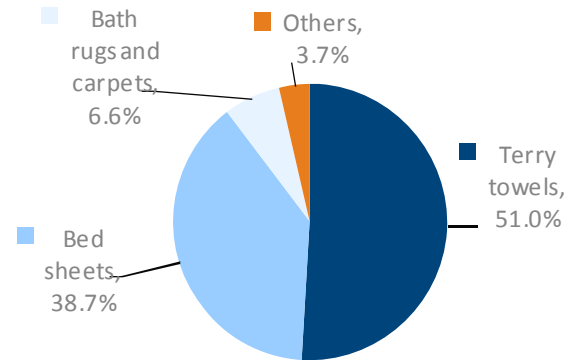
Source: Company data, IIFL Research

**Background:** Welspun India is India's leading exporter of home textiles with presence in bed-sheets, terry towels and rugs and carpets. The company was established as Welspun Winilon Silk Mills Pvt. Ltd in 1985, which subsequently became Welspun India in 1993. It is the largest exporter of towels and second largest exporter of bed-sheets and pillowcases to the US. Exports account for c95% of the company's sales with contribution from US alone at 65%. The company also has retail brands such as Spaces and Christy and c26 patents for its innovations.

## Management

Name	Designation
B K Goenka	Chairman
Dipali Goenka	CEO and joint MD
Rajesh Mandawewala	Managing Director

FY16 Revenue mix

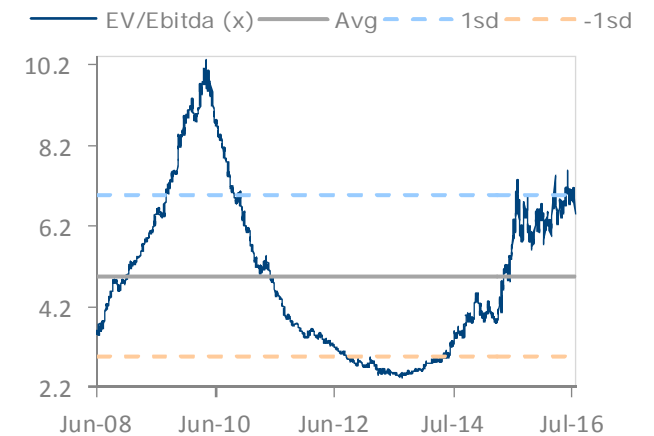


## Assumptions

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
Terry towel volume growth	15.1	10.0	7.9	8.4	8.9
Bed sheet volume growth	22.0	14.2	12.3	12.0	12.3
Bath rugs and carpets volume growth	5.5	33.2	9.8	10.4	10.8
Tax rate (%)	27.7	31.1	31.1	31.1	31.1
Capex (Rs bn)	5.2	10.5	8.1	5.1	7.1

Source: Company data, IIFL Research

EV/Ebitda



## Financial summary

### Income statement summary (Rs m)

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
<b>Revenues</b>	<b>53,025</b>	<b>59,795</b>	<b>67,615</b>	<b>76,463</b>	<b>86,953</b>
Ebitda	12,742	15,575	17,585	18,876	21,566
Depreciation and amortisation	(3,329)	(3,750)	(4,497)	(5,043)	(5,512)
Ebit	9,412	11,825	13,088	13,832	16,055
Non-operating income	949	915	911	807	612
Financial expense	(2,829)	(2,362)	(2,053)	(1,773)	(1,293)
PBT	7,533	10,378	11,946	12,866	15,374
Exceptionals	0	0	0	0	0
Reported PBT	7,533	10,378	11,946	12,866	15,374
Tax expense	(2,090)	(3,224)	(3,712)	(3,997)	(4,777)
PAT	5,443	7,153	8,234	8,868	10,597
Minorities, Associates etc.	(45)	(125)	(137)	(151)	(181)
<b>Attributable PAT</b>	<b>5,398</b>	<b>7,029</b>	<b>8,097</b>	<b>8,718</b>	<b>10,416</b>

### Ratio analysis

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
<b>Per share data (Rs)</b>					
Pre-exceptional EPS	5.4	7.0	8.1	8.7	10.4
DPS	10.5	1.3	1.4	1.5	1.7
BVPS	14.3	19.8	26.2	33.0	41.3
<b>Growth ratios (%)</b>					
Revenues	21.3	12.8	13.1	13.1	13.7
Ebitda	38.3	22.2	12.9	7.3	14.3
EPS	26.9	30.2	15.2	7.7	19.5
<b>Profitability ratios (%)</b>					
Ebitda margin	24.0	26.0	26.0	24.7	24.8
Ebit margin	17.8	19.8	19.4	18.1	18.5
Tax rate	27.7	31.1	31.1	31.1	31.1
Net profit margin	10.3	12.0	12.2	11.6	12.2
<b>Return ratios (%)</b>					
ROE	42.5	41.1	35.1	29.3	27.9
ROCE	23.5	27.1	27.7	27.2	30.0
<b>Solvency ratios (x)</b>					
Net debt-equity	1.8	1.2	0.9	0.5	0.3
Net debt to Ebitda	2.0	1.6	1.3	1.0	0.6
Interest coverage	3.3	5.0	6.4	7.8	12.4

Source: Company data, IIFL Research

### Balance sheet summary (Rs m)

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
Cash & cash equivalents	4,766	1,855	1,474	1,175	(396)
Inventories	11,006	11,046	12,491	14,126	16,064
Receivables	4,467	6,114	5,743	6,494	7,385
Other current assets	8,874	8,027	9,077	10,265	11,673
Creditors	6,910	10,080	9,262	10,474	11,911
Other current liabilities	3,855	4,222	5,381	5,985	6,799
<b>Net current assets</b>	<b>18,348</b>	<b>12,741</b>	<b>14,141</b>	<b>15,601</b>	<b>16,016</b>
Fixed assets	26,049	33,435	37,074	37,167	38,792
Intangibles	1,785	1,775	1,775	1,775	1,775
Investments	6	19	19	19	19
Other long-term assets	0	0	0	0	0
<b>Total net assets</b>	<b>46,188</b>	<b>47,970</b>	<b>53,010</b>	<b>54,562</b>	<b>56,602</b>
Borrowings	30,851	26,412	24,912	19,412	12,912
Other long-term liabilities	1,019	1,681	1,818	1,969	2,150
<b>Shareholders' equity</b>	<b>14,318</b>	<b>19,877</b>	<b>26,279</b>	<b>33,181</b>	<b>41,539</b>
<b>Total liabilities</b>	<b>46,188</b>	<b>47,970</b>	<b>53,010</b>	<b>54,562</b>	<b>56,602</b>

### Cash flow summary (Rs m)

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
Ebit	9,412	11,825	13,088	13,832	16,055
Tax paid	(1,767)	(2,393)	(3,712)	(3,997)	(4,777)
Depreciation and amortization	3,329	3,750	4,497	5,043	5,512
Net working capital change	(2,252)	2,754	(3,416)	(1,879)	(2,228)
Other operating items	668	602	0	0	0
Operating cash flow before interest	9,391	16,538	10,457	12,999	14,561
Financial expense	(3,127)	(2,573)	(2,053)	(1,773)	(1,293)
Non-operating income	237	430	911	807	612
<b>Operating cash flow after interest</b>	<b>6,501</b>	<b>14,394</b>	<b>9,315</b>	<b>12,032</b>	<b>13,881</b>
<b>Capital expenditure</b>	<b>(5,672)</b>	<b>(10,480)</b>	<b>(8,136)</b>	<b>(5,136)</b>	<b>(7,136)</b>
Long-term investments	(362)	925	0	0	0
Others	773	(870)	1,634	121	242
<b>Free cash flow</b>	<b>1,240</b>	<b>3,970</b>	<b>2,813</b>	<b>7,017</b>	<b>6,987</b>
Equity raising	4	0	0	0	0
Borrowings	568	(4,438)	(1,500)	(5,500)	(6,500)
Dividend	(711)	(2,443)	(1,695)	(1,816)	(2,058)
Net chg in cash and equivalents	1,100	(2,911)	(381)	(298)	(1,571)

Source: Company data, IIFL Research

**Disclosure : Published in 2016, © India Infoline Ltd 2016**

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**Key to our recommendation structure**

**BUY** - Absolute - Stock expected to give a positive return of over 20% over a 1-year horizon.

**SELL** - Absolute - Stock expected to fall by more than 10% over a 1-year horizon.

In addition, **Add** and **Reduce** recommendations are based on expected returns relative to a hurdle rate. Investment horizon for **Add** and **Reduce** recommendations is up to a year. We assume the current hurdle rate at 10%, this being the average return on a debt instrument available for investment.

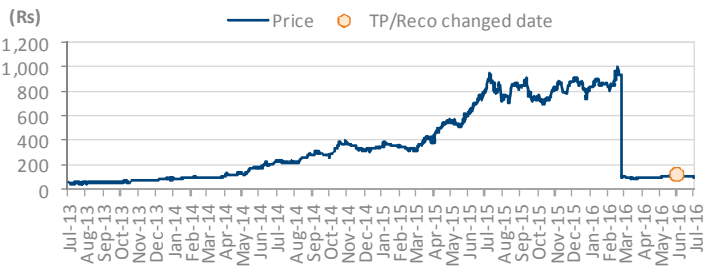
**Add** - Stock expected to give a return of 0-10% over the hurdle rate, i.e. a positive return of 10%+.

**Reduce** - Stock expected to return less than the hurdle rate, i.e. return of less than 10%.

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**Welspun India: 3 year price and rating history**



Date	Close price (Rs)	Target price (Rs)	Rating
24 Jun 2016	106	130	BUY