

India Midcap Discovery Series -----NOT COVERED*

Welspun India: Largest Indian home textile player

Anantha Narayan / Research Analyst / 91 22 6777 3730 / anantha.narayan@credit-suisse.com

Akhil Kalluri / Research Analyst / 91 22 6777 3747 / akhil.kalluri@credit-suisse.com

- Largest Indian home textile exporter: Welspun is the largest Indian exporter of towels and bedsheets to the US. According to management, it is benefiting from India's rising market share in the global cotton home textile trade and market share gains from some other domestic players.
- New categories and geographical expansion to drive growth, per management: It expects newer categories such as hospitality, geographies such as Europe, new products such as carpets and quilts, and new channels such as e-commerce to drive mid-teens sales growth. It expects margins to remain in the 22-23% range.
- FCF to remain positive, per management: Welspun incurred capex of Rs23 bn over FY14-16E, of which over 50% was spent on backward integration. Going forward, it is planning an asset-light model by having spinners have facilities at its 2,500-acre Anjar facility, similar to the auto ancillary model.
- The stock trades at 11x FY17E (consensus) P/E and 6.5x EV/E, at a premium to domestic textile players. It has better return ratios than peers and consensus is factoring in 17%+ EPS growth in FY16-18E.

Figure 1: Summary financials

Rs mn	FY11	FY12	FY13	FY14	FY15	9M FY16	9M growth
Revenue	21,132	32,205	36,473	43,730	53,025	43,511	10.5%
EBITDA	2,312	2,866	5,915	9,211	12,742	11,346	22.1%
Gross margins %	45.3%	50.3%	51.5%	48.2%	52.0%	60.8%	572 bp
EBITDA margin %	10.9%	8.9%	16.2%	21.1%	24.0%	26.1%	246 bp
PBT	438	496	3,017	1,059	7,558	7,585	41.1%
PBT margin %	2.1%	1.5%	8.3%	2.4%	14.3%	17.4%	378 bp
PAT	17	332	2,283	942	5,423	5,096	34.7%
EPS (Rs)	0.0	0.4	2.3	0.9	5.4	5.1	34.6%
RoE	0%	5%	26%	9%	43%	42%	
NWC days	66	52	60	67	59	57	
Net D/E (x)	2.6	2.5	1.9	2.7	2.0	1.4	

Source: Company data, Capitaline

Largest Indian home textile exporter

Welspun is the largest Indian home textile exporter of towels, sheets, and rugs and carpets. Home textiles is a US\$45 bn market, with US cotton home textiles accounting for ~US\$7.5 bn. The latter is dominated by China, India and Pakistan at 39%, 31% and 18% market shares, respectively. India's share increased from 20% in 2009 to 31% in 2015, mainly at the expense of China (44% market share in 2009), due to: (1) lower INR vs RMB, (2) rising wage and power costs in China, and (3) vendor rationalisation and increase in client focus on sustainability and labour regulations. India is dominant, however, in towels and sheets with 37% and 47% market share (up from 30% and 27% in 2009), respectively. Welspun is the largest Indian towel and sheet exporter with 16% and 10% market share, respectively, in the US. It has also gained from specific issues with a key Indian competitor. Welspun was established in 1985 as a yarn manufacturer and it moved into towels in 1993, sheets in 2006, and into rugs and carpets in 2010. Key clients of the company are retailers such as Walmart, and the client concentration is quite high (the top 5 customers account for 50% of the revenue and the largest one accounts for ~12% of the revenue).

Figure 2: Higher capacity for FY17

Category	Capacity			Peers	Mkt share in US	
	Current	1H FY17	Utilisation		India	Welspun
Towels	50k MT	60k MT	102%	Trident	37%	16%
Sheets	60 mn*	72 mn*	97%	IndoCount, Alok, Trident	47%	10%
Rugs	15k MT	20k MT	58%	Mohawk		

* mn meters; Source: Company data, Otxea

New categories and geographical expansion to drive growth, as per management

Welspun targets mid-teens revenue growth: growth was slower in FY16 mainly due to capacity constraints. While the market grows at a low single digit rate, it expects drivers such as: (1) newer segments such as hospitality (a US\$2 bn market) and healthcare, (2) increased presence in Europe (currently 17-18% of revenue) and Japan, (3) ramp-up in new products such as carpets and quilts (sheets form just 33% of bedding), and (4) e-commerce channel in India, the US and the UK. EBITDA margins improved from 16% in FY13 to 26% in 9M FY16 due to the closure of loss-making units in Mexico and Portugal and of retail stores' backward integration (it outsources 30% now, down from 45-50% earlier), and improving product mix (branded and innovative products form 11% and 31% of revenue) and it expects branded contribution to rise to 25% by 2020. Further, Welspun has 12 patented products such as Hygro and Flexifit. It expects 22-23% margins over the next three years. More than 5% fluctuation in input costs (such as cotton and fuel) and currency leads to re-negotiations every six months to protect the company's and the retailers' margins. However, margins can be impacted by 100-150 bp post GST due to the removal of duty drawback schemes.

FCF to remain positive, according to management

Capex was Rs23 bn over FY14-16E, and over 50% was on backward integration. This includes ~Rs10 bn spent in FY16 and Rs3.5 bn will be spent in 1H FY17. This will also increase the processing capacity by ~20%. It is looking at an auto-ancillary-type model wherein it is inviting entrepreneurs to set up dedicated spinning and weaving plants at its Anjar facility (with 2,500 acres of land). It believes lower freight costs and predictable demand will lead to higher utilisation, lower working capital and higher profits for spinners, while lower capex helps Welspun's returns. Typically, asset turn is 1x but as ~60-70% of capex is on backward integration, it targets 2.5x asset turns on incremental capex. Welspun generated FCF of Rs3.5 bn in FY15 and is confident of generating higher FCF from FY17.

Figure 3: Valuation comparables

Company	Mkt cap	ADTO	12M	EBITDA	Net debt/	P/E	EV/E	EPS
	US\$ mn		return	margin* RoE*	EBITDA* (x)	FY17E	FY17E	CAGR^
Arvind	1,062	8.2	-3%	13% 13%	3.1	15.6	8.3	28%
Himatsingka	282	1.5	122%	16% 18%	2.5	8.9	7.0	29%
Indo Count	593	1.1	110%	20% 49%	0.7	12.1	7.9	24%
KPR Mill	466	0.5	45%	18% 21%	1.5	10.4	6.8	24%
Raymond	368	0.5	-19%	8% 6%	2.5	16.8	6.4	49%
Trident	393	1.1	97%	20% 16%	3.4	8.7	5.4	28%
Vardhaman	825	0.6	25%	20% 16%	1.5	8.1	5.3	13%
Welspun	1,330	2.5	106%	26% 40%	1.7	11.2	6.5	17%

*Data for FY16E; ^CAGR over FY16-18E; Source: I/B/E/S

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