

WELSPUN INDIA

Industry headwinds mar FY18

India Equity Research | Midcap Textiles

Welspun India's (WLSI) Q4FY18 performance, as expected, was muted with revenues contracting 14% YoY impacted by currency, change in drawback rates and most importantly continued destocking by clients. To tackle an adverse year, the company had cut FY18 capex to INR3bn (earlier guidance was INR7bn), consequent to which net debt was stable at INR30bn. Company is increasing its investment in the flooring unit to INR11bn with capacity to double from earlier levels. Going ahead, WLSI expects the destocking issues to resolve and revenue/volume growth of 8-10% with margin at 19-20% for FY19E. Factoring in 8%/7% volume growth for FY19/20E, we maintain our target EV/EBITDA multiple of 7.0x, giving us a TP of INR84. Maintain 'BUY'.

Sector headwinds continue to impact; margin guidance of 19-20%

Q4FY18 revenue at INR15.1bn (Est.INR15.8bn) was down 14% YoY, the highest drop in FY18, impacted by client destocking and adverse currency. FY18 revenue fell ~9% on: a) lower volumes - ~5.0%; b) adverse currency - ~1.6%; and c) change in drawback rates - ~2.2%. Management stated industry scenario remains challenging, but things would start improving from Q1FY19 as they believe current share of online segment in home textiles in the US has peaked. The company is guiding for 8-10% revenue growth in FY19. On margin front, WLSI does not expect a sharp improvement despite the recent INR depreciation as certain costs, including cotton, will end up getting impacted. WLSI expects its margins to be between 19-20% for FY19E.

Debt stable YoY; capex pruned to INR3bn and flooring postponed

Capex incurred in FY18 was INR3bn (vs. guidance of INR7bn) and, majorly towards expanding towel capacity. Net debt at INR30.3bn was stable YoY. With WLSI shifting flooring facility from Gujarat to Telangana, expected investment has increased to INR11bn (~INR7bn earlier) as the degree of backward integration has increased and also doubled capacity from earlier stated levels. Commercial production at this unit is expected to start in Q3FY20. FY19 capex is expected to be INR9bn. Management is now targeting to become a net debt free by FY23E (from FY20E earlier).

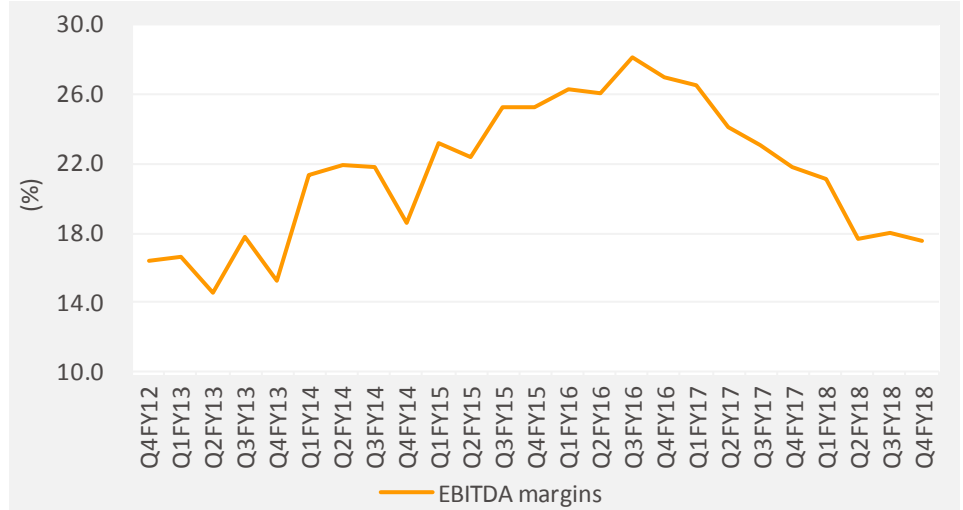
Outlook and valuations: Volumes to bounce back; maintain 'BUY'

We are building in 8% volume growth for FY19 and expect it to moderate to 7% in FY20. We maintain our target multiple of 7.0x EV/EBITDA with our target price of INR84. Maintain 'BUY'. At CMP, the stock trades at 10.7x FY20E EPS.

Financials	(INR mn)							
Year to March	Q4FY18	Q4FY17	YoY (%)	Q3FY18	QoQ (%)	FY18	FY19E	FY20E
Net Revenues	15,062	17,572	(14.3)	13,980	7.7	60,506	65,859	71,352
EBITDA	2,635	3,829	(31.2)	2,523	4.4	11,234	13,441	15,067
Adjusted Profit	866	1,530	(43.4)	774	11.9	3,982	5,381	6,129
Adj. Dil. EPS	0.9	1.5	(43.4)	0.8	11.9	4.0	5.4	6.1
Diluted P/E (x)						16.5	12.2	10.7
EV/EBITDA (x)						7.8	6.4	5.7
ROAE (%)						15.4	18.2	18.0

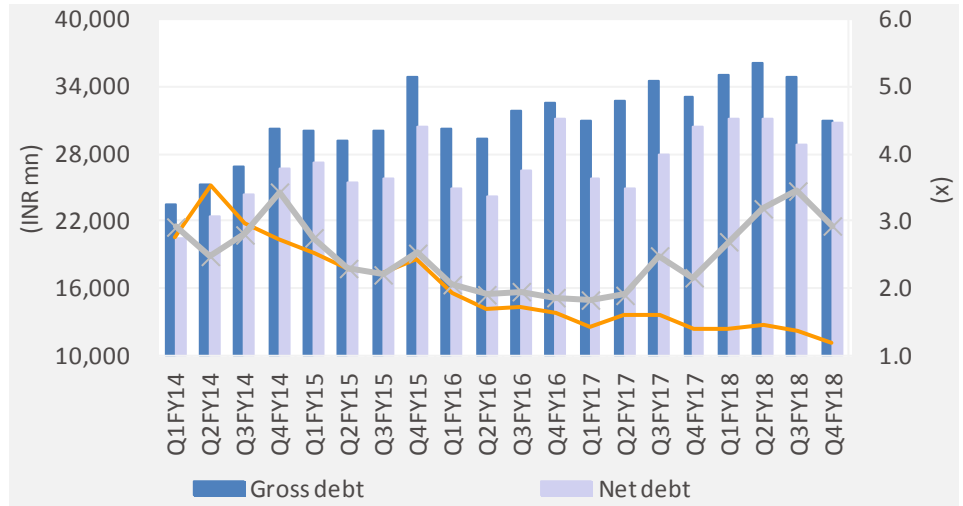
EDELWEISS RATINGS			
Absolute Rating	BUY		
Investment Characteristics	Value		
MARKET DATA (R: WLSP.BO, B: WLSI IN)			
CMP	: INR 65		
Target Price	: INR 84		
52-week range (INR)	: 93 / 50		
Share in issue (mn)	: 1,004.7		
M cap (INR bn/USD mn)	: 65 / 963		
Avg. Daily Vol. BSE/NSE ('000)	: 2,245.9		
SHARE HOLDING PATTERN (%)			
	Current	Q3FY18	Q2FY18
Promoters *	73.5	73.5	73.5
MF's, FI's & BKs	1.4	1.4	1.4
FII's	9.9	9.9	11.8
Others	15.2	15.2	13.3
* Promoters pledged shares (% of share in issue)	:	NIL	
PRICE PERFORMANCE (%)			
	BSE Midcap Index	Stock	Stock over Index
1 month	(3.9)	24.0	27.9
3 months	(2.8)	0.4	3.2
12 months	7.0	(26.7)	(33.7)
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May 17, 2018			

Chart 1: Margin improvement below expectation



Source: Company, Edelweiss research

Chart 2: Debt remained stable as capex plans have been pruned



Source: Company, Edelweiss research

Financial snapshot

(INR mn)

Year to March	Q4FY18	Q4FY17	% change	Q3FY18	% change	FY18	FY19E	FY20E
Net revenues	15,062	17,572	(14.3)	13,980	7.7	60,506	65,859	71,352
Staff costs	1,690	1,677	0.8	1,687	0.2	6,754	7,191	7,657
Direct costs	7,339	8,677	(15.4)	6,900	6.4	30,235	32,562	34,932
Other expenses	3,398	3,388	0.3	2,869	18.5	12,283	12,665	13,695
EBITDA	2,635	3,829	(31.2)	2,523	4.4	11,234	13,441	15,067
Depreciation	1,301	1,365	(4.7)	1,272	2.3	5,042	5,127	5,729
EBIT	1,335	2,464	(45.8)	1,252	6.6	6,192	8,314	9,338
Interest	381	430	(11.4)	345	10.3	1,408	1,143	1,153
Other income	287	156	84.5	164	75.5	812	714	821
Add: Exceptional items	-	9	(100.0)	-	-	-	-	-
Profit before tax	1,241	2,198	(43.6)	1,070	15.9	5,597	7,885	9,006
Provision for taxes	342	653	(47.7)	275	24.4	1,615	2,484	2,837
Minority interest	32	6	414.3	21	55.0	-	20	40
Reported net profit	866	1,539	(43.7)	774	11.9	3,982	5,381	6,129
Adjusted Profit	866	1,530	(43.4)	774	11.9	3,982	5,381	6,129
Diluted shares (mn)	1,005	1,005		1,005		1,005	1,005	1,005
Adjusted Diluted EPS	0.9	1.5	(43.4)	0.8	11.9	4.0	5.4	6.1
Diluted P/E (x)	-	-		-		16.5	12.2	10.7
EV/EBITDA (x)	-	-		-		7.8	6.4	5.7
ROAE (%)	-	-		-		15.4	18.2	18.0
Direct costs	48.7	49.4		49.4		50.0	49.4	49.0
Employee cost	11.2	9.5		12.1		11.2	10.9	10.7
Other expenses	22.6	19.3		20.5		20.3	19.2	19.2
EBITDA	17.5	21.8		18.1		18.6	20.4	21.1
Reported net profit	5.8	8.7		5.5		6.6	8.2	8.6
Tax rate	27.6	29.7		25.7		28.9	31.5	31.5

Change in Estimates

	FY19E			FY20E			Comments
	New	Old	% change	New	Old	% change	
Net Revenue	65,859	68,053	(3.2)	71,352	72,000	(0.9)	
EBITDA	13,441	14,247	(5.7)	15,067	15,330	(1.7)	
EBITDA Margin	20.4	20.9		21.1	21.3		
Adjusted Profit	5,381	5,701	(5.6)	6,129	6,247	(1.9)	
After Tax							
Net Profit Margin	8.2	8.5		8.6	8.8		
Capex	7,000	7,000	0.0	8,500	4,000	112.5	

Company Description

Established in 1985, Welspun India today, it is one of the top three home textile manufacturers globally and the largest home textile company in Asia. It has modern manufacturing facilities at Anjar and Vapi in Gujarat where it produces an entire range of home textiles for bed & bath category. The company has state-of-the-art completely vertically integrated plants, right from spinning to confectioning.

Welspun has been ranked No.1 among home textile suppliers in the US (Source: Home Textile Today). It has a distribution network in over 32 countries including US, UK, Europe, Canada and Australia.

In addition to manufacturing facilities, which predominantly supply to private labels, the company also maintains its own brands Christy, Hygrocotton, Welhome and Spaces - Home and Beyond; it also has a tie up with Nautica for North American markets.

Investment Theme

Innovation, diversified client and product base cement dominance: Welspun enjoys long standing relationships with top retailers in the US and Europe and supplies to 14 of the top 30 global retailers. It commands a lion's share of home textiles exported out of India. Increasing geographical and client diversification is improving the company's risk metrics. It has seven trademarks and has applied for six patents till date. Welspun derives ~30% of sales from innovative products.

Margin sustainability: WLSI has consistently improved its margin. While the rise is partially attributed to currency, it has been primarily driven by increase in share of innovative products. Driven by its confidence in sustaining these margins, it has upgraded its margin guidance from 20-22% to 23-24%.

Robust free cash flow & consistently lowering leverage: WLSI is at the end of its massive INR25bn capex programme it had undertaken in FY14, with only INR8bn to be spent in FY17. The company's confidence in generating free cash is also evident from its recently announced dividend policy of 25% payout ratio. Going forward, it is expected to generate strong free cash flows and lower its leverage further. Gross debt/equity has fallen from 2.1x at FY15 end to 1.3x as of FY16. We estimate this to fall below 1.0x by FY18E.

Key Risks

Raw material risk: Raw material costs, primarily cotton yarn, account for 50% of the overall expenses and are a prime driver of profitability. Volatility in cotton prices can impact the profitability adversely.

Currency fluctuations: Welspun exports more than 90% of its production. With a network spanning 50 countries, the company is exposed to currency fluctuations which can significantly impact profitability.

Egyptian cotton issue: Egyptian cotton products manufactured by WLSI came under the scanner when Target, cut ties with the company. Post the event, other major customers have however continued their regular sourcing of other products from WLSI. But, any further customer issues will be a negative for the company.

Financial Statements

Key Assumptions

Year to March	FY17	FY18	FY19E	FY20E
Macro				
GDP(Y-o-Y %)	6.6	6.5	7.1	7.6
Inflation (Avg)	4.5	3.8	4.5	5.0
Repo rate (exit rate)	6.3	6.0	6.0	6.5
USD/INR (Avg)	67.1	64.5	65.0	66.0
Company				
Raw Material (% net rev)	45.8	50.0	49.4	49.0
Other exp (% net rev)	20.8	20.3	19.2	19.2
Capex (INR mn)	7,003	2,565	7,000	8,500
Towel cap. (MT)	72,000	80,000	80,000	80,000
Bed-linen cap. (000 mts)	90,000	90,000	90,000	90,000
Rugs/carpets cap. (MT)	25,000	25,000	25,000	31,250
Towel utilis. (%)	97	76	81	85
Bed-linen utilis. (%)	73	80	84	88
Rugs/carpets utilis. (%)	72	65	78	72
Depreciation rate (%)	11.9	10.6	9.8	9.6
Dividend per share	0.7	0.7	1.0	1.2
Inventory % of costs	42.1	41.0	41.0	41.0
Debtors % of revenues	14.5	14.0	14.0	14.0
OCA % of revenues	10.9	10.9	11.0	11.0
Loans & adv (% net rev)	3.9	3.9	4.0	4.0
Incremental debt	636	(5,104)	(1,890)	1,623

Income statement

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Net revenue	66,405	60,506	65,859	71,352
Materials costs	30,396	30,235	32,562	34,932
Gross profit	36,009	30,270	33,297	36,419
Employee costs	6,373	6,754	7,191	7,657
Other Expenses	13,803	12,283	12,665	13,695
EBITDA	15,834	11,234	13,441	15,067
Depreciation	5,054	5,042	5,127	5,729
EBIT	10,780	6,192	8,314	9,338
Less: Interest Expense	1,583	1,408	1,143	1,153
Add: Other income	805.52	812.2	713.58	821.28
Profit Before Tax	5,355	5,597	7,885	9,006
Less: Provision for Tax	1,731	1,615	2,484	2,837
Less: Minority Interest	48	-	20	40
Add: Exceptional items	(4,648)	-	-	-
Reported Profit	3,576	3,982	5,381	6,129
Exceptional Items	(3,145)	-	-	-
Adjusted Profit	6,721	3,982	5,381	6,129
Shares o/s (mn)	1,005	1,005	1,005	1,005
Adjusted Basic EPS	6.7	4.0	5.4	6.1
Diluted shares o/s (mn)	1,005	1,005	1,005	1,005
Adjusted Diluted EPS	6.7	4.0	5.4	6.1
Adjusted Cash EPS	12.2	9.4	11.0	12.4
Dividend per share (DPS)	0.7	0.7	1.0	1.2
Dividend Payout Ratio(%)	22.0	19.7	20.0	20.0

Common size metrics

Year to March	FY17	FY18	FY19E	FY20E
Materials costs	45.8	50.0	49.4	49.0
Staff costs	9.6	11.2	10.9	10.7
S G & A expenses	20.8	20.3	19.2	19.2
Operating expenses	76.2	81.4	79.6	78.9
Depreciation	7.6	8.3	7.8	8.0
EBITDA margins	23.8	18.6	20.4	21.1
Interest Expense	2.4	2.3	1.7	1.6
Net Profit margins	10.2	6.6	8.2	8.6

Growth ratios (%)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	12.1	(8.9)	8.8	8.3
EBITDA	(0.6)	(29.1)	19.6	12.1
PBT	(50.2)	4.5	40.9	14.2
Adjusted Profit	(8.8)	(40.8)	35.1	13.9
EPS	(8.8)	(40.8)	35.1	13.9

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18	FY19E	FY20E	
Share capital	1,005	1,005	1,005	1,005	
Reserves & Surplus	22,967	26,163	30,467	35,371	
Shareholders' funds	23,971	27,167	31,472	36,375	
Minority Interest	355	355	375	415	
Long term borrowings	20,160	15,907	15,000	14,000	
Short term borrowings	12,954	12,102	11,119	13,742	
Total Borrowings	33,114	28,009	26,119	27,742	
Long Term Liabilities	2,354	2,520	2,522	2,524	
Def. Tax Liability (net)	1,466	1,855	2,404	3,031	
Sources of funds	61,260	59,907	62,893	70,088	
Gross Block	43,572	46,403	53,405	61,721	
Net Block	35,011	32,802	34,679	37,269	
Capital work in progress	564	298	296	479	
Intangible Assets	1,879	1,887	1,895	1,903	
Total Fixed Assets	37,454	34,987	36,870	39,651	
Non current investments	29	29	29	29	
Cash and Equivalents	2,857	6,424	5,569	8,359	
Inventories	12,810	12,396	13,350	14,322	
Sundry Debtors	9,601	8,471	9,220	9,989	
Loans & Advances	2,567	2,339	2,634	2,854	
Other Current Assets	7,265	6,619	7,244	7,849	
Current Assets (ex cash)	32,242	29,825	32,450	35,014	
Trade payable	7,517	7,424	7,744	8,327	
Other Current Liab	3,804	3,933	4,281	4,638	
Total Current Liab	11,321	11,357	12,025	12,965	
Net Curr Assets-ex cash	20,920	18,468	20,425	22,049	
Uses of funds	61,260	59,907	62,893	70,088	
BVPS (INR)	23.9	27.0	31.3	36.2	

Free cash flow		(INR mn)			
Year to March	FY17	FY18	FY19E	FY20E	
Reported Profit	3,576	3,982	5,381	6,129	
Add: Depreciation	5,054	5,042	5,127	5,729	
Interest (Net of Tax)	1,071	1,001	783	790	
Others	143	(16)	195	169	
Less: Changes in WC	1,522	(2,619)	1,955	1,622	
Operating cash flow	8,322	12,628	9,531	11,195	
Less: Capex	7,003	2,565	7,000	8,500	
Free Cash Flow	1,319	10,063	2,531	2,695	

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		EV / EBITDA (X)		ROAE (%)	
		FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Welspun India	963	12.2	10.7	6.4	5.7	18.2	18.0
Arvind	1,613	20.2	15.3	10.8	8.6	12.6	14.7
Himatsingka Seide	515	12.4	10.8	7.0	6.0	20.5	19.7
Median	-	12.4	10.8	7.0	6.0	18.2	18.0
AVERAGE	-	14.9	12.2	8.1	6.8	17.1	17.5

Source: Edelweiss research

Cash flow metrics		FY17	FY18	FY19E	FY20E
Year to March					
Operating cash flow		8,322	12,628	9,531	11,195
Financing cash flow		(990)	(7,298)	(4,089)	(716)
Investing cash flow		(7,124)	(1,763)	(6,296)	(7,689)
Net cash Flow		208	3,567	(854)	2,790
Capex		(7,003)	(2,565)	(7,000)	(8,500)
Dividend paid		(63)	(786)	(1,076)	(1,226)

Profitability and efficiency ratios

Year to March	FY17	FY18	FY19E	FY20E
ROACE (%)	21.1	12.4	15.9	16.6
ROAE (%)	30.5	15.4	18.2	18.0
Inventory Days	113	123	118	118
Debtors Days	50	55	49	49
Payable Days	85	90	85	84
Cash Conversion Cycle	77	88	82	83
Current Ratio	3.1	3.2	3.2	3.3
Gross Debt/EBITDA	2.1	2.5	1.9	1.8
Gross Debt/Equity	1.4	1.0	0.8	0.8
Adjusted Debt/Equity	1.4	1.0	0.8	0.8
Net Debt/Equity	1.2	0.8	0.6	0.5
Interest Coverage Ratio	6.8	4.4	7.3	8.1

Operating ratios

Year to March	FY17	FY18	FY19E	FY20E
Total Asset Turnover	1.1	1.0	1.1	1.1
Fixed Asset Turnover	1.9	1.7	1.8	1.9
Equity Turnover	3.0	2.3	2.2	2.1

Valuation parameters

Year to March	FY17	FY18	FY19E	FY20E
Adj. Diluted EPS (INR)	6.7	4.0	5.4	6.1
Y-o-Y growth (%)	(8.8)	(40.8)	35.1	13.9
Adjusted Cash EPS (INR)	12.2	9.4	11.0	12.4
Diluted P/E (x)	9.7	16.4	12.2	10.7
P/B (x)	2.7	2.4	2.1	1.8
EV / Sales (x)	1.4	1.4	1.3	1.2
EV / EBITDA (x)	6.1	7.8	6.4	5.7
Dividend Yield (%)	1.0	1.0	1.5	1.8

Additional Data

Directors Data

Mr. B K Goenka	Chairman	Mr. R. R. Mandawewala	Managing Director
Ms. Dipali Goenka	Executive Director	Mr. Arun Tadarwal	Independent Director
Mr. Ram Gopal Sharma	Independent Director	Pradeep Poddar	Independent Director
Arvind Kumar Singhal	Independent Director	Padma Betai	Nominee Director-IDBI Bank

Auditors -

**as per last available data*

Holding – Top10

	Perc. Holding		Perc. Holding
DSP Blackrock	4.87	FIAM Emerging Markets	3.82
Alliance Bernstein	1.55	Aditya Birla Asset Mgmt	1.30
Vanguard	1.30	Lazard Emerging Markets	1.06
Wasatch Advisors	0.79	Dimensional Fund Advisors LP	0.73
Birla Sun Life Insurance	0.51	L&T Mutual Fund	0.51

**as per last available data*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
10 Jan 2018	Dsp Blackrock Mutual Fund - Balanced Fund	Buy	7152682	72.70
10 Jan 2018	Dsp Blackrock Mutual Fund - Micro Cap Fund	Buy	16506190	72.70
10 Jan 2018	Mgn Agro Properties Pvt Ltd	Sell	48096381	72.71
10 Jan 2018	Dsp Blackrock Mutual Fund - Tax Saver Fund	Buy	6785420	72.70
10 Jan 2018	Dsp Blackrock Mutual Fund - Opportunities Fund	Buy	6800000	72.70

**as per last available data*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
11 Jan 2018	MGN Agro Proerties Private Limited	Sell	50236257.00

**as per last available data*

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Coverage group(s) of stocks by primary analyst(s): Midcap Textiles

Arvind, Himatsingka Seide, Trident Ltd, Welspun India

Recent Research

Date	Company	Title	Price (INR)	Recos
01-Feb-18	Arvind	Strong surge in brand margins; <i>Result Update</i>	406	Buy
09-Nov-17	Arvind	Brands strong, but textiles weak; demerger announced; <i>Result Update</i>	436	Buy
08-Nov-17	Himatsingka Seide	Margin blip due to one-offs; <i>Result Update</i>	360	Buy

Distribution of Ratings / Market Cap

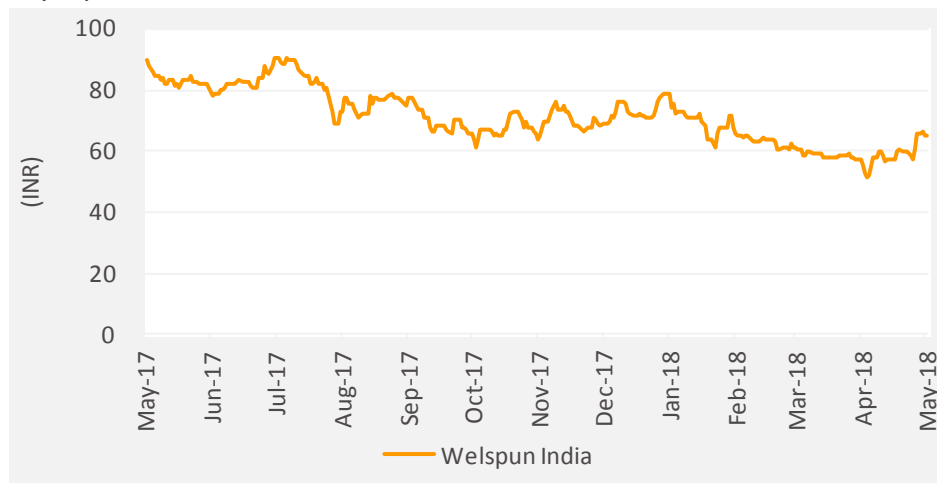
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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