

Himatsingka Seide

STOCK INFO.	BLOOMBERG
BSE SENSEX: 9,465	HSS IN
	REUTERS CODE
S&P CNX: 2,884	HMSD.BO

23 January 2006

Neutral

Previous Recommendation: Neutral

Rs141

Equity Shares (m)	97.4
52-Week Range (Rs)	169/91
1,6,12 Rel.Per. (%)	1/14/-12
M.Cap (Rs. b)	13.8
M.Cap (US\$ b)	0.3

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
3/05A	1,498	446	4.6	-13.8	30.8	4.6	15.5	14.2	8.3	21.9
3/06E	1,690	521	5.3	16.8	26.4	2.3	11.7	8.9	5.8	15.9
3/07E	2,696	624	6.4	19.7	22.1	2.2	10.2	8.8	4.8	13.1

* Consolidated

- 3QFY06 results were below our expectations. Revenues increased by 3.9% YoY to Rs408m compared with our estimate of Rs449m, due to 12% YoY decline in fabric volumes.
- EBITDA margins declined by 670bp to 32.4% YoY owing to lower asset utilization. Operating margins were further negatively impacted by a one-time charge of Rs13.5m from revaluation of GDR proceeds, which was charged to administrative and sales expenses.
- PAT remained flat at Rs120m in 3QFY06 v/s our estimate of 19% YoY increase to Rs140m.
- A GDR issue of US\$60m (Rs2.7b) at Rs130/share was completed, diluting its equity capital by 27.4%. The company intends to utilize these funds to finance its overseas brand acquisitions.
- The stock trades at a PER of 22.1x FY07E and 11.2x FY08E earnings. We maintain **Neutral**.

QUARTERLY PERFORMANCE

(Rs Million)

Y/E MARCH	FY05				FY06				FY05	FY06E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Sales	311	346	392	330	342	381	408	375	1,380	1,505
Change (%)	5.8	-1.8	7.4	-4.0	9.8	9.9	4.0	13.8	1.8	9.1
EBITDA	131	153	153	121	132	147	132	182	559	594
Change (%)	4.8	9.0	6.7	-19.8	0.6	-3.9	-13.9	50.7	-0.2	6.2
As % of Sales	42.2	44.3	39.1	36.6	38.7	38.7	32.3	48.5	40.5	39.4
Depreciation	39	39	36	10	35	36	35	42	125	148
Interest	3	2	2	5	5	4	1	0	12	11
Other Income	18	11	14	22	32	29	25	19	65	105
Extra-ordinary Income	0	-8	0	-8	0	0	0	0	-8	0
PBT	107	123	129	128	124	136	121	159	496	540
Tax	6	16	12	-3	12	4	1	17	32	33
Effective Tax Rate (%)	5.6	13.2	9.3	-2.0	9.3	2.9	0.9	10.5	6.4	6.1
Reported PAT	101	115	117	130	113	132	119	142	464	507
Adj. PAT	101	107	117	130	113	132	119	142	456	507
Change (%)	-10.9	-11.7	-12.8	2.6	11.4	24.0	1.8	9.3	-9.8	11.3

E: MOST Estimates; Standalone

Revenue breakdown

During 3QFY06, fabric sales recorded a 12% YoY decline in volume terms, which was cushioned by an increase in realizations by 9.2% YoY. Thus the sales decline in value terms was limited to 1.6% YoY. Management attributed the fall in fabric sales to diversion of certain orders into 4QFY06 and discontinuation of a particular low margin apparel business present in the corresponding quarter, 3QFY05.

FABRIC PERFORMANCE

	3QFY06	3QFY05	% CHG.
Value (Rs m)	324.7	330.1	-1.6
Volume ('000 metres)	363.1	406.5	-11.9
Realization (Rs/meter)	894	812	9.2

Source: Company/Motilal Oswal Securities

Himatsingka Wovens

Himatsingka Woven, the retail arm of the company recorded a 12% YoY increase in revenues to Rs45m. We estimate total FY06 sales from the retail division to be around Rs180m. Performance of the retail division was negatively impacted due to closure of its retail showroom in Delhi as a result of legal issues.

RETAIL DIVISION PERFORMANCE

	3QFY06	3QFY05	% CHG.
Sales (Rs m)	45.48	40.01	12.0
Qty ('000 meters)	36.18	33.78	6.6
Realization (Rs/meter)	1,257	1,185	5.7

Source: Company/Motilal Oswal Securities

Has raised US\$60m through GDR issue

Himatsingka Seide (HSS) has raised US\$60m (Rs2.7b) through a GDR issue at US\$2.862/GDR (Rs130/share). The issue has led to an equity dilution of 27.4%, resulting in equity capital increasing from Rs382m to Rs487m. Management proposes to utilize these funds for an overseas acquisition and to fund its future capex plans. Several brand acquisitions in the EU and the US are being considered, which would allow HSS to forward integrate into branding and retailing.

Guidance of 72% sales CAGR over FY05-FY08

HSS has issued an aggressive sales guidance of Rs7b to be reached by FY08, a CAGR (FY05-FY08) of 72%. It expects the bed linen project to contribute around Rs4.8b in revenues by FY08 and benefit from its location in a SEZ unit. We believe this could lead to a substantial re-rating of the stock over the medium-to-long term as low growth has been one of the biggest concerns for the company.

Any acquisition to lead to re-rating

HSS has been catering to the premium home textile market in the developed countries. Any acquisition of a brand would allow it to forward integrate into branding and retailing and allow it to maximize margins. Hence, we believe that HSS is likely to be re-rated in the event of a successful acquisition.

Equity dilution of 27.4%

The GDR issue has led to an equity dilution of 27.4%, resulting in its equity capital increasing from Rs382m to Rs487m. In the event of a successful acquisition by the company, we believe this equity dilution would be earnings accretive, as margins would expand further.

Lowering revenue and net profit targets

For FY06 we are lowering our consolidated revenue estimates by 5% to Rs1,690m and that of our consolidated net profits estimate by 2% to Rs521m. The fall in net profit has been cushioned by higher other income, lower depreciation and tax provisioning for FY06.

REVISED ESTIMATES (RS M)

	FY06 OLD	FY06 (REVISED)	%
Sales	1,775	1,690	-5
PAT	533	521	-2

Source: Motilal Oswal Securities

Valuation and view

HSS stands out as a unique cash-rich textile company with one of the most robust knowledge-based business models in India. It is on the verge of a major re-rating once management implements its four-pronged growth strategy. Given management's strong credentials, we strongly believe

that the company would be able to achieve its growth plans and evolve into an international niche brand in the high-end home textile segment. The stock trades at a PER of 22.1x FY07E and 11.2x FY08E earnings. We have a **Neutral** rating on the stock.

Himatsingka Seide: an investment profile

Company description

Himatsingka Seide is the largest producer of silk and blended-silk fabrics and yarns in India and currently exports its entire production primarily to North America and Europe. It now plans to make a fresh foray into the cotton/silk bed linen segment, expand product offerings, further push its retail initiative and is also scouting for acquisitions in the global market. Once implemented, these initiatives have the potential to increase the company's sales to Rs7b by FY08.

Key investment arguments

- ✍ Himatsingka can be credited as being the only Indian textile company to build a sound business based on design-led competencies.
- ✍ The company has a sound financial position, with almost zero long-term debt and liquid cash of around Rs1.4b.
- ✍ Its top five customers account for 30% of turnover. Some of its client relationships date back to 15 years.

Key investment risk

- ✍ The company has not been able to effectively grow its topline in the past. As a result, its topline has been almost stagnant since FY01.

Recent developments

- ✍ It now plans to make a fresh foray into the cotton/silk bed linen segment.
- ✍ HSS has successfully raised US\$60m through a GDR issue

Valuation and view

- ✍ HSS has issued an aggressive guidance of Rs7b topline to be achieved by FY08, a CAGR (FY05-FY08) of 72%.
- ✍ It expects the bed linen project to contribute around Rs4.8b in revenues by FY08 and the unit to benefit from its location in the SEZ.
- ✍ The stock trades at 26.4x FY06E and 22.1x FY07E earnings. We have a **Neutral** rating on the stock.

Sector view

- ✍ Exports from China are likely to be severely constrained due to safeguarding measures adopted by the US and EU.
- ✍ India registered robust export growth rates to the US and EU in the post-quota era.
- ✍ Global buyers are focusing on building vendor partners that have high product development skills.
- ✍ The concern of industry overcapacity causing waves of deflation in prices is overblown.

COMPARATIVE VALUATIONS

		HIMATSINGKA	VARDHMAN	ARVIND MILLS
P/E (x)	FY06E	26.4	12.5	12.0
	FY07E	22.1	11.0	10.3
P/BV (x)	FY06E	2.3	2.1	1.3
	FY07E	2.2	1.8	1.1
EV/Sales (x)	FY06E	5.8	1.4	1.8
	FY07E	4.8	1.5	1.6
EV/EBITDA (x)	FY06E	15.9	8.5	7.9
	FY07E	13.1	8.5	7.0

SHAREHOLDING PATTERN (%)

	DEC.05	SEP.05	DEC.04
Promoters	48.3	61.2	61.2
Domestic Institutions	1.5	5.0	7.3
FII's/FDIs	26.9	11.0	11.8
Others	23.3	22.8	19.7

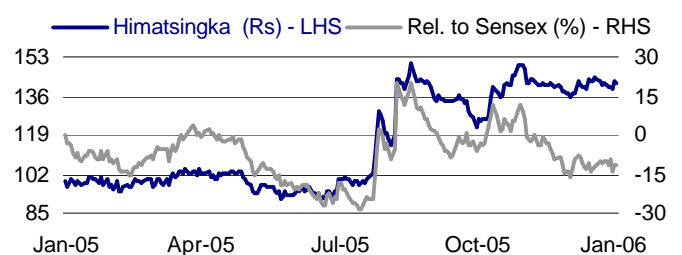
EPS: INQUIRE FORECAST VS CONSENSUS (RS)

	INQUIRE FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY06	5.3	-	-
FY07	6.4	-	-

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
141	-	-	Neutral

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					
(Rs Million)					
Y/E MARCH	2004	2005	2006E	2007E	2008E
Net Sales	1,356	1,498	1,690	2,696	6,054
YoY Growth (%)	8.0	10.5	2.9	59.5	24.6
Total Expenditure	786	933	1,077	1,701	4,282
EBIDT	570	565	614	995	1,772
Change (%)	3.3	-0.9	8.7	62.2	78.0
% of Net sales	42.0	37.7	36.3	36.9	29.3
Depreciation	147	134	148	330	429
EBIT	422	430	466	666	1,343
Int. & Finance Charges	1	12	11	54	60
Other Income	137	60	105	85	85
Profit before Tax	558	479	560	696	1,368
Tax	40	32	39	72	137
Effective Rate (%)	7.2	6.8	7.0	10.4	10.0
Profit after Tax	518	446	521	624	1,231
Adj. Profit after Tax	518	446	521	624	1,231
Change (%)	22.6	-13.8	16.8	19.7	97.3

BALANCE SHEET					
(Rs Million)					
Y/E MARCH	2004	2005	2006E	2007E	2008E
Share Capital	191	191	487	487	487
Reserves	2,587	2,804	5,427	5,774	6,675
Net Worth	2,778	2,995	5,914	6,261	7,162
Loans	138	420	420	2,170	1,720
Deferred Tax Liability	40	42	52	70	125
Capital Employed	2,955	3,457	6,386	8,501	9,007
Gross Fixed Assets	2,046	2,146	2,546	5,996	6,396
Capital WIP	0	0	0	0	2
Gross Block	2,046	2,146	2,546	5,996	6,396
Less: Depreciation	963	1,097	1,245	1,575	2,003
Net Fixed Assets	1,084	1,049	1,301	4,422	4,395
Investments	1,183	1,550	1,600	1,000	1,000
Curr. Assets, Loans & Advances					
Inventory	359	422	487	769	1,525
Sundry Debtors	217	246	278	443	829
Cash & Bank Balances	117	249	2,804	1,895	1,251
Others	371	371	400	520	651
Current Liab. & Prov.	374	429	484	548	644
Sundry Creditors	67	62	62	63	64
Other Liabilities	12	14	16	17	19
Current Liabilities	80	76	78	80	83
Provisions	295	354	407	468	561
Net Current Assets	689	858	3,485	3,079	3,612
Application of Funds	2,956	3,457	6,386	8,501	9,007

E: MOST Estimates

RATIO					
Y/E MARCH	2004	2005	2006E	2007E	2008E
Basic (Rs)					
EPS	5.3	4.6	5.3	6.4	12.6
Cash EPS	7	6	7	10	17
Book Value per Share	29	31	61	64	74
DPS	10.0	11.0	2.0	2.5	3.0
Payout (Incl. Div. Tax) %	42.7	52.2	42.6	44.5	0.3
Valuation (x)					
P/E		30.8	26.4	22.1	11.2
Cash PE		23.7	20.6	14.4	8.3
EV/EBITDA		21.9	15.9	13.1	7.5
EV/Sales		8.3	5.8	4.8	2.2
Price to Book Value		4.6	2.3	2.2	1.9
Dividend Yield (%)		7.8	14	1.8	2.1
Profitability Ratios (%)					
RoE	19.7	15.5	11.7	10.2	18.3
RoCE	18.9	14.2	8.9	8.8	15.9
Turnover Ratios					
Debtors (Days)	59	60	60	60	50
Inventory (Days)	167	165	165	165	130
Creditors (Days)	65	65	65	65	65
Working Capital (Days)	160	160	160	160	115
Asset Turnover (x)	0.5	0.4	0.3	0.3	0.7
Fixed Asset Turnover (x)	0.7	0.7	0.7	0.4	0.9
Leverage Ratio					
Debt/Equity (x)	0.0	0.1	0.1	0.3	0.2

CASH FLOW STATEMENT					
(Rs Million)					
Y/E MARCH	2004	2005	2006E	2007E	2008E
OP/(Loss) before Tax	558	479	560	696	1,368
Add: Depreciation & Amort.	147	134	148	330	429
Add: Interest Paid	1	12	11	54	60
Less: Direct Taxes Paid	32	30	29	54	82
Less: (Inc)/Dec in Wkg. Capital	-128	-37	-71	-504	-1,177
CF from Op. Activity	408	486	502	383	453
CF after EO Items	408	486	502	383	453
(Inc)/Dec in Fixed Assets & CW	-116	-100	-400	-3,450	-398
(Pur)/Sale of Invest.	-360	-363	-60	600	0
CF from Inv. Activity	-32	-102	-395	-3,450	-402
Inc / (Dec) in Debt	138	282	0	1,750	-450
Interest Paid	1	12	11	54	60
Dividends Paid	216	237	222	278	330
CF from Fin. Activity	-327	-251	2,448	2,158	-694
Inc / (Dec) in Cash	49	132	2,555	-909	-644
Add: Opening Balance	68	117	249	2,804	1,895
Closing Balance	117	249	2,804	1,895	1,251



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Himatsingka Seide

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| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |

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