

STOCK DATA

Market Cap	Rs18bn.
Book Value per share	Rs79
Eq Shares O/S (F.V. Rs.10)	630mn.
Median Vol (12 mths)	441,500 (BSE+NSE)
52 Week High/Low	Rs401 /150
Bloomberg Code	BRFL@IN
Reuters Code	BRFL.BO

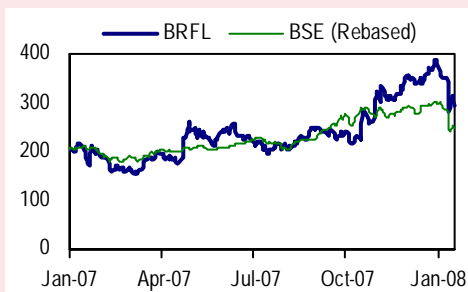
SHAREHOLDING PATTERN (%)

Qtr. Ended	Jun-07	Sep-07	Dec-07
Promoters	43.4	43.4	43.4
MFs/FIs	8.2	12.5	15.3
FIIIs	25.7	28.1	26.7
PCBs	12.6	8.8	8.3
Indian Public	10.0	7.2	6.2

STOCK PERFORMANCE (%)

	1M	3M	12M
Absolute	(17.1)	31.2	42.2
Relative	(4.5)	41.1	16.5

STOCK PRICE PERFORMANCE



KEY HIGHLIGHTS

Bombay Rayon Fashions Ltd. (BRFL) reported an impressive growth of 81% YoY in revenues to Rs2.4bn for Q3FY08. This was on the back of a healthy volumes growth in both garments and fabrics.

While garment volumes rose by ~113% to 3.9 mn pcs, fabric volumes grew ~61% to 11 mn mtrs with fabric realisations improving 2% to Rs112/mtr. However, garments witnessed a YoY decline of ~7% to Rs274/pcs, but improved 5% on a QoQ basis on account of increasing share of organic cotton garment sales and express deliveries orders.

● **Margins expand by 130 bps**

Garments, which has higher OPM as compared to fabrics, witnessed a 500 bps increase in share of revenues to 45% and the same resulted in a 130 bps improvement in OPM to 22.2%.

● **Net profit spurts**

Increase in OPM resulted in a 93% increase in operating profit to Rs529mn. This along with a ~5.8x increase in other income to Rs66mn and lower effective tax rate propelled net profits by ~2.5x to Rs346mn.

● **Aggressive capex plans**

BRFL is expanding its standalone fabric capacity from the current 55 mn mtrs to 235 mn mtrs and garment capacity from 30 mn pcs to 60 mn pcs. It has also acquired the garmenting unit of RSWM, which has a capacity of ~6k pcs/day, for Rs255mn.

VALUATION AND RECOMMENDATION

BRFL, with its aggressive capacity expansion, is well poised to capitalise on the growing garment demand from EU. Also, its new initiatives like express deliveries and sales of organic cotton garments should enable it to counter rupee appreciation to a large extent. Increasing scale, stable realisation trend coupled with incentives from Maharashtra government for its capex have the potential to result in substantial cost savings and margin expansion. Hence, we upgrade our recommendation to 'BUY' from 'HOLD' with a price target of Rs360.

KEY FINANCIALS (STANDALONE)

Rs mn	Quarter Ended			Yr Ended (March)				
	Jun-07	Sep-07	Dec-07	2005	2006	2007	2008E	2009E
Net Sales	2,012	2,246	2,388	1,039	1,990	4,888	9,602	18,340
YoY Gr. (%)	147.8	117.5	81.4	-	91.6	145.7	96.4	91.0
Op. Profits	396	492	529	114	332	911	1,992	3,875
Op. Marg. (%)	19.7	21.9	22.2	10.9	16.7	18.6	20.7	21.1
Net Profits	220	307	346	73	179	540	1,086	2,006
Eq. Capital	630	630	630	330	490	630	691	691

KEY RATIOS

	Yr Ended (March)				
	2005	2006	2007	2008E	2009E
Dil. EPS (Rs)	1.1	2.6	7.8	15.7	29.0
ROCE (%)	17.1	28.7	17.8	18.0	18.1
RONW (%)	15.8	17.9	16.7	18.3	25.6
P/E (x)	104.6	79.4	33.8	18.5	10.0
EV/Sales (x)	9.5	7.5	4.0	2.7	1.7
EV/EBIDT (x)	71.6	43.2	19.7	11.7	8.0

PERFORMANCE OVERVIEW

BRFL's Q3FY08 performance was in line with our expectations on the revenue front. However, the 130 bps improvement in margins to 22.2% positively surprised us. For the quarter its revenues grew 81% to Rs2.4bn, and profits surged by 2.5x to Rs346mn.

Increasing volumes of fabrics and garments helps in revenue growth...

Revenue growth was mainly led by volume growth in both fabrics and garments. Volumes of the former grew 61% to 11 mn mtrs whereas those of the latter rose 113% to 3.88 mn pcs. Fabric realisations improved by 2% to Rs112/mtr whereas garment realisations declined by ~7% to Rs274/mtr. On a QoQ basis, garment realisations have improved by 5% from Rs262/pc in Q2FY08 as a result of higher share of organic cotton garment sales and sales of garments on faster deliveries. It enjoys higher realisations to the tune of 15-25% on these sales.

BRFL's export consists primarily of garments and the same is exported to EU and USA. The balance fabrics is sold in the domestic market. Exports currently accounts for ~45% of BRFL's total revenues and of this over three fourths is Euro denominated (including GBP). Thus, it has to hedge only 25% of its exports and it has accordingly done so at a Rs/USD rate of over Rs40/USD.

Operating margins for the quarter expanded 130 bps to 22.2% for Q3FY08 largely due to the increasing contribution in revenues from garments (45% in Q3FY08 v/s 41% in Q3FY07) which traditionally have higher OPM. Accordingly, op. profits grew 93% to Rs529mn.

While other income grew by ~5.8x to Rs66mn as a result of higher interest income and forex gains, capital charges doubled to Rs153mn on back of its capacity expansions. Thus, net profits rose 151% to Rs346mn.

Minimising the impact of appreciating rupee against dollar

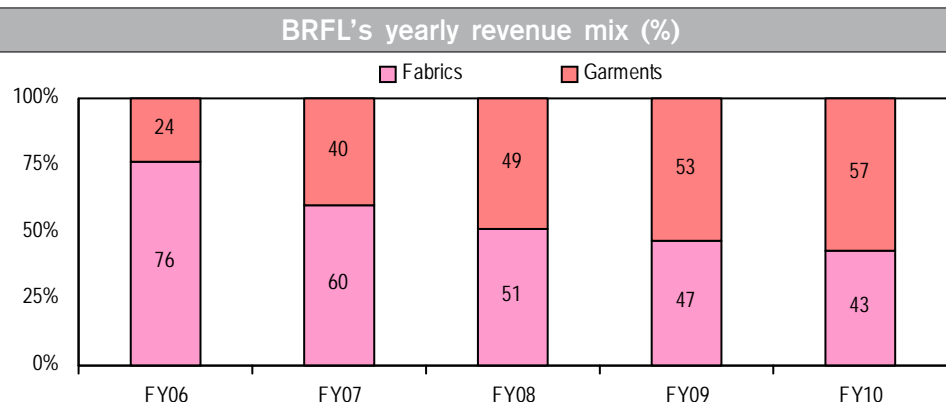
Focussing on high value products and lower lead time deliveries to minimise the currency impact...

BRFL exports, which consists mainly of garments, accounts for ~45% of its total revenues, with bulk of it being to EU. The share of exports in total revenues is expected to increase going forward as BRFL is constantly ramping up its garmenting capacity. To minimise the impact of appreciating rupee, it is now focusing more on the EU market and has started quoting in rupee for new orders. However, benefits from the rupee quotations would be limited as buyers are usually not willing to share the currency risks.

Strategically the company has also started focusing on orders which entail early delivery schedules. It charges an additional USD1/pcs over and above its average garment realisation of ~USD7/pcs for delivery within 30 days against the industry average of 80-90 days.

Another area of focus has been exports of garments made from organic cotton. This helps in improving realisations by 40-50%, with the associated cost increasing by ~20%.

Thus, BRFL enjoys EBIDTA margins in excess of ~30% from express deliveries and sales of organic cotton garments. BRFL is targeting to raise the share from the same to 20% as against the current 9-10% for FY09.



Source: Company, PINC Research

Expansion Plans

BRFL is aggressively expanding its fabric and garmenting capacities to meet the growing demand of its clients. Fabric capacity expansion is being undertaken through organic route, whereas it has followed both organic as well as inorganic route for expanding its garmenting capacities. It plans to increase its standalone capacities for fabrics from ~55 mn mtrs to 235 mn mtrs and from ~28 mn pcs to 60 mn pcs for garments.

BRFL plans to set up an additional fabric capacity of 180 mn mtrs and garment capacity expansion (100k pcs per day) at Maharashtra. To cater to the power requirement of this facility, it is also setting up 40 MW bagasse based cogen power plants. As these units will be located in the sugarcane belt of the state, bagasse will be procured from the nearby sugar mills. Of the 40 MW, 50% will be capitively consumed whereas balance will be sold to the state grid. The above capacities will be fully operational from Q3FY09 onwards.

For the above expansion, BRFL has signed an MoU with the Maharashtra government, under which it will receive number of incentives as the units will be set up in the backward regions and will create employment of ~30k jobs. The incentives available to the company are as follows:

- 1) Interest rate subsidy of 4%. This is over and above the 5% available under TUFS.
- 2) Reimbursement of employer's contribution to statutory employees benefit
- 3) Exemption from stamp duty and electricity duty
- 4) Exemption from VAT on sales in the domestic market
- 5) Support in infrastructural facilities

It is incurring a capex of Rs11bn on its Maharashtra facilities, funded in the debt equity ratio of 1.75x. Of this, Rs9bn would go towards fabric expansion and Rs2bn on garment expansion. The equity portion of Rs4bn would be raised from the proceeds of the QIP issue, warrants issued to the promoters and internal accruals, while the balance would be funded through debt.

Past Acquisitions

DPJ Clothing: BRFL acquired 70% stake in DPJ Clothing Ltd., a U.K. based wholesaler and distribution company for USD2.9mn. This will help BRFL to capitalise on the existing client base of DPJ, leverage its position in the global markets and also reduce its dependence on the USA market.

Leela Scottish Lace: Bombay Rayon Apparel, wholly owned subsidiary of BRFL, acquired the assets of Leela Scottish Lace (LSL) in Aug'07 for Rs1.6bn. LSL is into the garment manufacturing with facilities located at Chennai, Bangalore, Kochi and Thiruvanthapuram. It has a capacity of 50k pcs per day and employs ~16k people and for FY07 reported sales of Rs4bn, with operating margins of ~10%.

BRFL has infused ~Rs380mn (25% of acquisition cost) whereas balance 75% would be infused by its subsidiary. BRFL expects LSL to add ~Rs1.5-1.7bn to the topline. Going forward, we expect margins to improve substantially as LSL units will start sourcing fabrics from BRFL's existing fabric capacities.

LNJ Apparels: BRFL acquired LNJ Apparels, a garmenting unit of RSWM for a consideration of Rs255mn. The unit has a capacity of manufacturing of ~6k trousers per day and is located at Bangalore. The legal procedures of the acquisition are expected to be completed by Dec'07. BRFL, which is predominantly a shirt manufacturer, would foray into trouser manufacturing post acquisition of this unit.

The unit was set up by RSWM in Jan'06 and is currently a loss making unit as it was operating at a very low capacity utilisation of ~20%. BRFL, by ramping up the production, can turnaround the operations and post profits. On an annual basis, this unit can contribute ~Rs500mn.

Investing Rs11bn in Maharashtra to increase its fabric and garment capacities...

Acquires LNJ Apparels at a cost of Rs255mn...

OUTLOOK

We expect the company (on a standalone basis) to post a revenue growth of 96% and 91% to Rs9.6bn and Rs18bn for FY08 and FY09 respectively. This would be driven by increasing volumes of fabrics and garments resulting from its capex. Also, share of garment revenues to total revenues is expected to increase to 42% in FY08 and to 50% in FY09 from the current 41% in 9MFY08. Contribution from exports should also increase in line with the increase in garment sales, as exports mainly consist of garments.

Operating margins in FY08 are expected to expand by 210 bps to 20.7% as a result of increasing contribution from the high margin garment sales. Impact of rupee appreciation should be partially offset by high value products and express delivery orders. Additional cushion would be there from the benefits from Maharashtra government and that has the potential to improve margins by 40 bps to 21.1% in FY09. Accordingly, operating profits should increase by 119% and 95% to Rs2bn and Rs3.9bn in FY08 and FY09 respectively.

Capital charges should increase by 150% and 83% to Rs590mn and Rs1.1bn in FY08 and FY09 due to the capex being undertaken. This is being contained to a large extent due to the interest rate subsidy on loans borrowed for Maharashtra expansion. Thus, net profits should grow by 101% and 85% to Rs1.1bn and Rs2bn in FY08 and FY09 respectively.

VALUATION

At the CMP of Rs290, the stock trades at a P/E of 18.5x and 10x discounting its FY08 & FY09 estimated EPS of Rs15.7 and Rs29 respectively. It trades at an EV/Sales & EV/EBIDTA of 1.7x and 7.7x its FY09E.

BRFL, with its aggressive capacity expansions, is well poised to capitalise on the growing garment demand from EU. Also, its new initiatives like express deliveries and sales of organic cotton garments should enable it to counter rupee appreciation to a large extent. Increasing scale, stable realisation trend coupled with incentives from Maharashtra government for its capex have the potential to result in substantial cost savings and margin expansion. Hence, we upgrade our recommendation to 'BUY' from 'HOLD' with a price target of Rs360.

Risks and Concerns

- 1) Strengthening of the rupee against dollar and euro would continue to remain as a major overhand on the profitability of the company.
- 2) Slowdown in the consumer countries like EU and USA would severely impact the future performance as it aggressively expands its capacities factoring robust demand.
- 3) BRFL is in the midst of executing an ambitious expansion projects. Any delay in the project execution can adversely impact future performance.
- 4) Post expansion at Maharashtra units, BRFL's manufacturing workforce will be in excess of 60k people. The company might face difficulties in managing such a mammoth workforce due to its inexperience in handling the personnel on such a large scale.

Company description

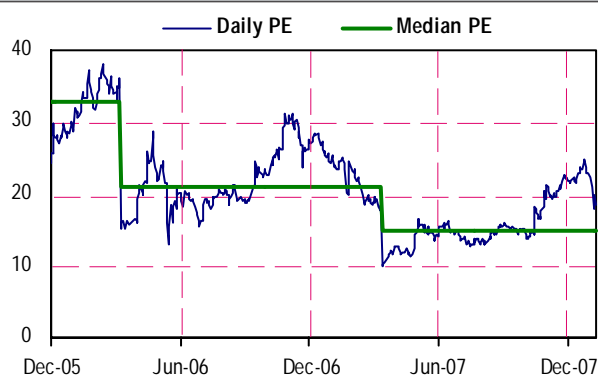
Bombay Rayon Fashions Limited (BRFL) is one of the largest exporters of shirts for men in India. It is ramping up its fabric and garmenting capacities through organic as well as inorganic route. As a result of the above expansion, the product mix of the company will move in favour of garments going forward.

Revenue mix to change in favour of garments...

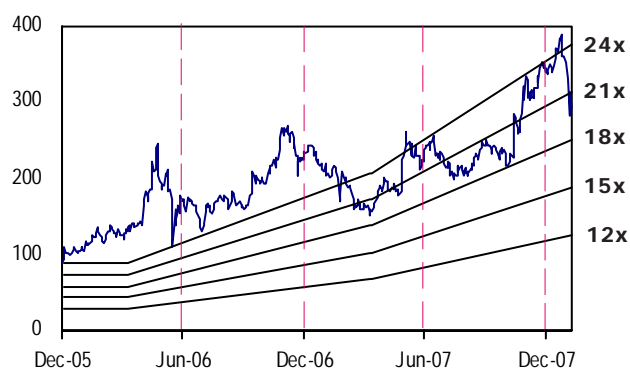
Financial Results for the quarter & nine months ended 31 December 2007 (Standalone)

Particulars (Rs Mn)	Quarter Ended			Nine Months Ended			Year Ended
	31/12/07	31/12/06	Gr %	31/12/07	31/12/06	Gr %	31/03/07
Net Sales	2,388	1,316	81.4	6,646	3,161	110.3	4,888
Total Expenditure	1858	1042	78.4	5229	2534	106.4	3978
(Inc.) / Dec. Stock-in-trade	(78)	(85)		(391)	(257)		(500)
Raw Material consumption	1,542	882	83.8	4535	2,165	117.2	3,469
Staff Cost	181	90	101.0	407	247	64.8	336
Job Work Charges	-	77	(100.0)	51	181	(71.9)	286
Other expenditure	214	79	172.2	628	199	216.2	387
Operating profit	529	274	92.8	1,417	627	126.0	911
Other Income	66	11	478.7	200	27	633.7	79
PBDIT	595	286	108.2	1,617	654	147.1	991
Interest	77	43	80.8	198	94	110.3	131
Depreciation	76	35	116.7	207	62	231.8	105
PBT & extra-ordinary items	442	208	112.3	1,213	498	143.5	754
Provision for current tax	112	50		356	95		90
Provision for deferred tax	(16)	20		(18)	73		119
Provision for FBT	-	1		3	2		4
Net Profits	346	138	151.3	873	329	165.6	540
Equity Capital (F.V. Rs 10/share)	630	490		630	490		630
Reserves (excl. revaluation reserves)	-	-		-	-		4,200
EPS for the period (Rs)	5.5	2.8		13.9	6.7		8.6
Book Value (Rs)	-	-		-	-		79
OPM (%)	22.2	20.9		21.3	19.8		18.6
NPM (%)	14.5	10.5		13.1	10.4		11.1
Expenditure (% of Net Sales)							
Raw materials (incl. stock adj.)	61.3	60.5		62.3	60.4		61.5
Staff Cost	7.6	6.8		6.1	7.8		6.7
Job Work Charges	0.0	5.8		0.8	5.7		5.8
Other expenses	9.0	6.0		9.5	6.3		7.2

Median PE v/s Daily PE



PE Band



Income Statement	2005	2006	2007	2008E	2009E
Revenues	1,039	1,990	4,888	9,602	18,340
<i>Growth (%)</i>	-	91.6	145.7	96.4	91.0
Total Expenditure	925	1,657	3,978	7,610	14,465
Operating Profit	114	332	911	1,992	3,875
<i>Growth (%)</i>	-	192.6	174.0	118.8	94.5
Interest & dividend income	24	14	79	210	120
EBIDT	137	346	990	2,202	3,995
(-) Interest	26	65	131	285	440
(-) Depreciation	19	30	105	305	640
PBT & extraordinary items	92	252	754	1,612	2,915
(-) Tax provision	19	73	213	526	909
Net Profits	73	179	540	1,086	2,006
<i>Growth (%)</i>	-	146.5	202.1	101.0	84.8
Fully diluted Eq. sh. O/s (mn no)	329.6	489.8	630.0	691.0	691.0
Book Value (Rs)	14	31	79	101	127
Basic EPS (Rs)	2.2	3.7	8.6	15.7	29.0
Diluted EPS (Rs)	1.1	2.6	7.8	15.7	29.0

Balance Sheet	2005	2006	2007	2008E	2009E
<i>Equity Share Capital</i>	330	490	630	691	691
<i>Reserves & Surplus</i>	129	1,044	4,319	6,257	8,061
Net worth	459	1,534	4,949	6,948	8,752
Total Debt	273	950	3,345	7,240	12,895
Deferred Tax liability	3	15	135	410	848
Capital Employed	735	2,498	8,428	14,598	22,495
Fixed Assets	294	1,202	3,645	8,490	13,700
Net current assets	436	1,196	3,560	5,358	8,253
Investments	1	100	1,222	750	542
Misc exp.	4	-	1	-	-
Total Assets	735	2,498	8,428	14,598	22,495

Cash Flow Statement	2005	2006	2007	2008E	2009E
PBT & Extraord. items	92	252	753	1,612	2,915
Depreciation	19	30	105	305	640
Interest & dividend inc.	-	(8)	(48)	(210)	(120)
Interest paid	26	65	131	285	440
Misc Exp W/off	3	(1)	-	-	-
Tax paid	(5)	(68)	(117)	(251)	(472)
(Inc) / Dec in working capital	(387)	(697)	(1,670)	(1,965)	(3,245)
Cash from operations	(252)	(427)	(846)	(223)	158
Net capital expenditure	(263)	(942)	(2,546)	(5,150)	(5,850)
Net investments	0	(95)	(1,124)	472	208
Interest / Dividend recd	1	8	48	210	120
Cash from investing activities	(263)	(1,029)	(3,622)	(4,468)	(5,522)
Issue of shares	313	952	2,971	1,072	-
Change in debt	232	677	2,417	3,895	5,655
Dividend paid	-	-	(56)	(158)	(201)
Interest paid	(26)	(65)	(131)	(285)	(440)
Cash from financing activities	519	1,565	5,201	4,525	5,014
Inc/Dec. in cash	4	109	733	(166)	(350)

Key Ratios	2005	2006	2007	2008E	2009E
EBIDTA (%)	10.9	16.7	18.6	20.7	21.1
ROACE (%)	17.1	28.7	17.8	18.0	18.1
ROANW (%)	15.8	17.9	16.7	18.3	25.6
Sales/Total Assets (x)	1.2	0.7	0.5	0.6	0.8
Debt:Equity (x)	0.6	0.6	0.7	1.0	1.5
Current Ratio (x)	2.7	4.1	5.1	4.7	5.6
Debtors (days)	83.8	70.4	83.8	87.5	70.5
Inventory (days)	149.4	181.0	166.2	148.1	121.7
Net working capital (days)	185.0	236.9	232.0	187.5	159.2
EV/Sales (x)	9.5	7.5	4.0	2.7	1.7
EV/EBIDT (x)	71.6	43.2	19.7	11.7	8.0
P/E (x)	104.6	79.4	33.8	18.5	10.0
P/BV (x)	20.8	9.3	3.7	2.9	2.3

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