HANUNG TOYS & TEXTILES LTD.

Q4 FY 2008 update BUY

PINC RESEARCH

Sector Toys & Textile | CMP Rs 239 | Target Rs 295

STOCK DATA

Market Cap	Rs6bn.
Book Value per share	Rs98
Eq Shares O/S (F.V. Rs.5)	25.2mn.
Median Vol (12 mths)	145,000 (BSE+NSE)
52 Week High/Low	Rs 300 / 121
Bloomberg Code	HATT@BO
Reuters Code	HTT.BO

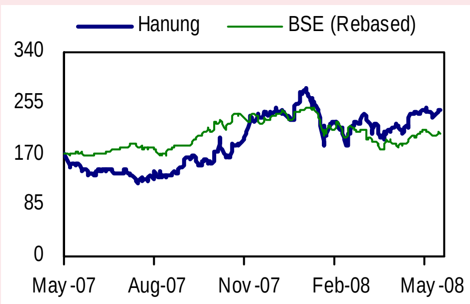
SHAREHOLDING PATTERN (%)

Qtr. Ended	Sep-07	Dec-07	Mar-08
Promoters	62.3	62.3	62.3
MFs / FIs	12.5	13.9	14.0
FIIs	7.9	8.6	9.2
PCB	5.8	6.3	6.6
Indian Public	11.4	8.9	8.0

STOCK PERFORMANCE (%)

	1M	3M	12M
Absolute	2.5	8.9	41.9
Relative	(0.4)	12.1	18.7

STOCK PRICE PERFORMANCE



KEY HIGHLIGHTS

Hanung Toys & Textile Ltd. (Hanung) posted an impressive 112% YoY growth in net sales to Rs1.6bn. While this was largely led by a 228% surge in textile revenues (to Rs1.1bn), toys segment also reported a 26% growth in sales to Rs556mn.

Exports contribution to total sales rose 1,550 bps to 88.8%, with textiles accounting for the bulk of it. Commissioning of the Roorkee facility in Jul'07 was the key reason for the upsurge in textile and export revenues.

- **Margins shrink 600 bps**

However, increasing contribution from low margin textiles segment resulted in overall margins declining 600 bps to 14.4%. Other income spiked 6.5x to Rs65mn on account of DEPB benefits. Lower effective tax rate on account of tax benefits enjoyed by its Roorkee facility helped net profits surge 143% to Rs211mn.

- **Strong order book**

Hanung's order book as on Mar'08 stands at Rs13bn, equally divided between toys and textiles and executable over four years. Of these, ~20% comprises of domestic orders, 50% from Europe and balance from USA.

- **MoU with Chinese toy manufacturer**

Hanung has entered into a MoU with a Chinese toy manufacturer for acquiring latter's soft toys business. The company achieved a turnover of USD7mn on a capacity utilisation of 35%.

VALUATIONS AND RECOMMENDATION

With aggressive capacity expansions and benefits from backward integration, Hanung should be able to capitalise on the growing demand for toys & textile, both in the domestic and export markets. Its limited exposure to the currency movements, after taking into account its natural hedge, ensures stability to margins with potential benefits coming from backward integration of textile operations. Hence, we maintain our 'BUY' recommendation on the stock with a price target of Rs295 on an investment perspective of 12 months.

KEY FINANCIALS (STANDALONE)

Rs mn	Quarter Ended			Yr Ended (March)				
	Sep-07	Dec-07	Mar-08	2006	2007	2008	2009E	2010E
Net Sales	1,138	1,281	1,636	1,467	2,751	4,907	6,950	8,750
YoY Gr. (%)	*79.3*	*60.4*	*112.3*	*83.3*	*87.5*	*78.4*	*41.6*	*25.9*
Op. Profits	187	206	235	229	475	781	1,128	1,443
Op. Marg. (%)	*16.5*	*16.1*	*14.4*	*15.6*	*17.3*	*15.9*	*16.2*	*16.5*
Net Profits	137	168	211	130	277	609	739	993
Eq. Capital	*252*	*252*	*252*	*157*	*252*	*252*	*252*	*252*

KEY RATIOS

	Yr Ended (March)				
	2006	2007	2008E	2009E	2010E
EPS (Rs)	8.3	11.0	24.2	29.3	39.4
ROCE (%)	26.7	26.9	27.9	21.9	21.1
RONW (%)	29.2	22.0	28.3	26.3	27.4
P/E (x)	28.9	21.7	9.9	8.2	6.1
EV/Sales (x)	3.0	2.4	1.7	1.2	1.0
EV/EBIDT (x)	19.3	14.1	10.7	7.3	5.9

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PERFORMANCE OVERVIEW

Hanung's Q4FY08 results in line with our expectations...

Hanung's performance for Q4FY08 was in line with our expectations, as it posted a 112% and 143% growth in net sales and profits to Rs1.6bn and Rs211mn respectively.

Revenues of toys segment grew by 26% to Rs556bn, whereas textiles division witnessed an increase of 228% to Rs1.1bn. Thus, the share of textiles in total revenues rose to 66% from 42.7% in Q4FY07. Realisations were also stable at Rs110/pcs for toys and Rs206/mtr for fabrics. Surge in textiles revenues can be attributed to the commissioning of processing capacity at Roorkee in Jul'07. Contribution from exports to total turnover also jumped 1,550 bps to 88.8%, as execution of long term orders from foreign clients were undertaken during the quarter.

Lower margins on account of increasing contribution from textiles...

Margins ebbed by 600 bps to 14.4%, on account of increasing contribution from low margin textiles segment. Accordingly, operating profits grew by 50% to Rs235mn. Other income spiked by 6.5x to Rs65mn on account of DEPB benefits. Capital charges rose marginally by 17% to Rs50mn whereas tax rate was lower by 1,450 bps to 15.5% as contribution from tax exempted Roorkee facility trickled in. This helped net profits grow 143% to Rs211mn.

Hanung's exposure to foreign currency movements is limited to only ~9%, as ~23% is from domestic sales, ~18% from rupee denominated IKEA order, ~30% from raw material imports and ~20% through hedging contracts.

As on Mar'08, the company has an order book of Rs13bn, divided equally between toys and textiles. Of the total orders, long term contracts account for ~Rs10.6bn which are executed over a four year period, whereas balance ~Rs2.4bn are short term orders. The yearly execution of long term contracts is given below:

Execution of long term contracts (Rs mn)

Particulars	FY08	FY09	FY10	FY11	Total
Toys (EUR108mn)	830	1,280	1,670	2,220	6,000
Home furnishings (USD65mn)	600	800	1,200	-	2,600
Home furnishings (USD50mn)	800	1,200	-	-	2,000
Total	**2,230**	**3,280**	**2,870**	**2,220**	**10,600**

EXPANSION PLANS

Hanung commissioned its fabric processing capacity (41mn mtrs) at Roorkee (Uttarakhand) in Jul'07. The weaving capacity (6.9mn mtrs), is expected to be commissioned Jun'08 and would enable Hanung to capture a greater share of total value addition. This would lead to margin expansion as currently the entire grey fabric requirement are sourced externally. However, it would continue to rely on procuring the fabric externally as its weaving capacity would still be significantly lower than annual processing capacity of 41mn mtrs. The toy manufacturing capacity currently stands at 20mn pcs with further expansion plan of 15 mn pcs by Q3FY09, taking the total capacity to 35mn pcs.

MoU WITH CHINESE TOY MANUFACTURER

Signs MoU with a Chinese toy manufacturer, having a capacity of 10 mn pcs...

Hanung has entered into a MoU with a Chinese toy manufacturer, with an annual capacity of 10 mn pcs, for acquiring latter's 100% stake. The existing infrastructure also enables it to further expand the capacity to 20 mn pcs. The company had achieved a turnover of USD7mn on a capacity utilisation of 35%, i.e. 3.5 mn pcs. The acquisition should strengthen Hanung's presence in the manufacture of low cost, mass production (standardised products) segment.

OUTLOOK

We expect the company to post a revenue growth of 42% and 26% to Rs7bn and Rs8.8bn in FY09 and FY10 respectively. This would be mainly due to capacity expansion in both, toys and textiles segment. We have not factored any benefits accruing from the acquisition of Chinese toy manufacturing company.

We expect revenues and profits of Rs8.8bn and Rs993mn in FY10…

Operating margins are expected to improve marginally by 30 bps to 16.2% in FY09 as it will benefit from full year operation of processing capacity and better capacity utilisation. In FY10, we expect margins to further improve by another 30 bps to 16.5%. Accordingly, operating profits should rise by 44% and 28% to Rs1.1bn and Rs1.4bn in FY09 and FY10 respectively.

Capital charges in FY09 should scale up by 92% to Rs360mn in FY09 on back of capacity expansions across both its segments. Tax rate is expected to be lower by 330 bps and 70 bps to 16.2% and 15.5% in FY09 and FY10 as a result of increasing contribution from Roorkee facility, which enjoys income tax benefits. Thus, net profits should grow by 21% and 34% to Rs739m and Rs993mn in FY09 and FY10 respectively.

VALUATIONS AND RECOMMENDATION

At the CMP of Rs239, the stock trades at a P/E of 8.2x and 6.1x discounting its FY09 & FY10 estimated EPS of Rs29.3 and Rs39.4 respectively. It trades at an EV/Sales & EV/EBIDTA of 1.2x and 7.3x its FY09E.

We maintain our 'BUY' recommendation…

With aggressive capacity expansions and benefits from backward integration, Hanung should be able to capitalise on the growing demand for toys & textile, both in the domestic and export markets. Its limited exposure to the currency movements, after taking into account its natural hedge, ensures stability to margins with potential benefits coming from backward integration of textile operations. Hence, we maintain our 'BUY' recommendation on the stock with a one year price target of Rs295.

Company description

HTTL, founded by Mr Ashok Bansal in 1990, commenced operations by manufacturing and exporting soft toys in technical collaboration with Hanung Industrial Co. Ltd (South Korea) in 1990. In FY03, it diversified into home furnishings and textiles and came out with an IPO in Oct'06, raising Rs902mn. HTTL has manufacturing facilities located at Noida SEZ and has set up greenfield plant for home furnishings / textiles at Roorkee (Uttarakhand).

Financial Results for the quarter & year ended 31 March 2008

Particulars (Rs Mn)	Quarter Ended			Year Ended		
	31/03/08	31/03/07	Gr %	31/03/08	31/03/07	Gr %
Net Sales	**1,636**	**771**	**112.3**	**4,907**	**2,751**	**78.4**
Total Expenditure	**1,401**	**614**	**128.2**	**4,126**	**2,274**	**81.4**
(Inc)/Dec in stock	(91)	(58)		(445)	(109)	
Raw Materials	1,199	584	110.3	3,846	2,094	71.4
Employee Cost	24	16	44.8	79	51	53.8
Other Expenses	270	71	280.9	646	238	171.3
Operating Profit	**235**	**157**	**49.9**	**781**	**475**	**63.8**
Other Income	65	10	553.9	164	60	172.1
PBIDT	**299**	**167**	**79.7**	**944**	**537**	**75.9**
Interest	34	32	8.8	136	95	43.5
Depreciation	15	11	38.8	51	30	72.3
PBT	**250**	**124**	**101.5**	**757**	**412**	**83.6**
Provision for current tax	39	37	4.2	148	134	10.2
Net Profits	**211**	**87**	**143.1**	**609**	**277**	**119.1**
Equity Capital (F.V Rs10 / share)	252	252		252	252	
Reserves (excl. revaluation reserves)	2,207	1,598		2,207	1,598	
EPS for the period (Rs)	8.4	3.4		24.2	11.0	
Book Value (Rs)	97.6	73.5		97.6	73.5	
OPM (%)	**14.4**	**20.3**		**15.9**	**17.3**	
NPM (%)	12.9	11.3		12.4	10.1	
Expenditure (% of Net Sales)						
Raw Materials (incl. stock adjustments)	67.7	68.3		69.3	72.1	
Employee Cost	1.5	2.1		1.6	1.9	
Other Expenses	16.5	9.2		13.2	8.7	

Segmentwise Results for the quarter & year ended 31 March 2008						
Particulars (Rs Mn)	Quarter Ended			Year Ended		
	31/03/08	31/03/07	Gr %	31/03/08	31/03/07	Gr %
Segment Revenue						
Toys	556	441	26.0	2,140	1,492	43.4
Textiles	1,080	329	228.0	2,767	1,259	119.8
Net Sales	**1,636**	**771**	**112.3**	**4,907**	**2,751**	**78.4**
PBIT						
Toys	116	96	21.5	434	300	44.6
Textiles	103	50	107.2	296	147	101.2
Total	**219**	**146**		**730**	**447**	
Less: Interest	34	32	8.8	136	95	43.5
Add: Net other unallocable income	65	10	553.9	164	60	172.1
PBT	**250**	**124**	**101.5**	**757**	**412**	**83.6**
Geographical Segment						
Exports	1454	566	157.1	3,938	2,077	89.6
Domestic	183	205	(11.0)	969	674	43.6
Total	**1,636**	**771**	**112.3**	**4,907**	**2,751**	**78.4**
Geographical Mix (%)						
Exports	88.8	73.4		80.3	75.5	
Domestic	11.2	26.6		19.7	24.5	
PBIT Margins (%)						
Toys	20.9	21.7		20.3	20.1	
Textiles	9.5	15.1		10.7	11.7	
Total	**13.4**	**18.9**		**14.9**	**16.3**	
Sales Mix (%)						
Toys	34.0	57.3		43.6	54.2	
Textiles	66.0	42.7		56.4	45.8	
PBIT Mix (%)						
Toys	53.1	65.9		59.5	67.1	
Textiles	46.9	34.1		40.5	32.9	

Year Ended March (Figures in Rs mn)

Income Statement	2006	2007	2008	2009E	2010E
Revenues	**1,467**	**2,751**	**4,907**	**6,950**	**8,750**
Growth (%)	*83.3*	*87.5*	*78.4*	*41.6*	*25.9*
Total Expenditure	**1,238**	**2,276**	**4,126**	**5,822**	**7,307**
Operating Profit	**229**	**475**	**781**	**1,128**	**1,443**
Growth (%)	*0.0*	*108.0*	*64.2*	*44.5*	*28.0*
Interest & dividend income	34	60	164	114	139
EBIDT	**263**	**535**	**944**	**1,242**	**1,582**
(-) Interest	54	95	136	209	238
(-) Depreciation	14	30	51	151	169
PBT	**195**	**411**	**757**	**882**	**1,175**
(-) Tax provision	66	134	148	143	182
Net Profits	**130**	**277**	**609**	**739**	**993**
Growth (%)	*205.6*	*113.7*	*120.0*	*21.2*	*34.4*
Fully diluted Eq. sh. O/s (mn no)	15.7	25.2	25.2	25.2	25.2
Book Value (Rs)	42.7	73.5	97.6	125.2	162.9
Basic EPS (Rs)	8.3	11.0	24.2	29.3	39.4
Diluted EPS (Rs)	**8.3**	**11.0**	**24.2**	**29.3**	**39.4**

Balance Sheet	2006	2007	2008E	2009E	2010E
Equity Share Capital	157	252	252	252	252
Reserves & Surplus	513	1,598	2,207	2,902	3,851
Net worth	**670**	**1,850**	**2,459**	**3,154**	**4,103**
Term Debt	726	1,294	2,550	2,812	3,372
Deferred Tax liability	29	53	73	75	81
Capital Employed	**1,424**	**3,196**	**5,082**	**6,041**	**7,556**
Fixed Assets	374	1,210	2,303	2,332	2,305
Net current assets	1,049	1,948	2,732	3,613	5,005
Investments	1	38	46	96	246
Total Assets	**1,424**	**3,196**	**5,082**	**6,041**	**7,556**

Year Ended March (Figures in Rs mn)

Cash Flow Statement	2006	2007	2008E	2009E	2010E
PBT & Extraord. items	**195**	**413**	**757**	**882**	**1,175**
Depreciation	14	30	51	151	169
Interest & dividend inc.	(1)	(2)	(164)	(114)	(139)
Interest paid	29	76	136	209	238
Tax paid	(7)	(98)	(128)	(141)	(176)
(Inc)/Dec in working capital	(644)	(410)	(1,190)	(516)	(1,257)
Cash from operations	**(413)**	**8**	**(537)**	**471**	**10**
Net capital expenditure	(297)	(866)	(1,144)	(180)	(142)
Net investments	1	(37)	(8)	(50)	(150)
Interest recd	-	-	164	114	139
Cash from investing activities	**(296)**	**(903)**	**(989)**	**(116)**	**(153)**
Issue of eq. shares	90	95	-	-	-
Share Premium	240	808	-	-	-
Change in debt	463	568	1,256	262	560
Dividend paid	(6)	(6)	(43)	(43)	(43)
Interest paid	(28)	(74)	(136)	(209)	(238)
Cash from financing activities	**759**	**1,390**	**1,076**	**10**	**278**
Inc/Dec. in cash	**50**	**496**	**(449)**	**365**	**135**

Key Ratios	2006	2007	2008E	2009E	2010E
EBIDT (%)	15.6	17.3	15.9	16.2	16.5
ROACE (%)	26.7	26.9	27.9	21.9	21.1
ROANW (%)	29.2	22.0	28.3	26.3	27.4
Sales/Total Assets (x)	1.0	0.9	1.0	1.2	1.2
Debt:Equity (x)	1.1	0.7	1.0	0.9	0.8
Current Ratio (x)	4.5	6.6	5.8	6.5	6.1
Debtors (days)	61.5	62.4	60.4	61.4	61.9
Inventory (days)	172.4	147.8	130.9	130.0	139.2
Net working capital (days)	187.6	170.3	157.8	158.1	164.2
EV/Sales (x)	3.0	2.4	1.7	1.2	1.0
EV/EBIDT (x)	19.3	14.1	10.7	7.3	5.9
P/E (x)	28.9	21.7	9.9	8.2	6.1
P/BV (x)	5.6	3.3	2.4	1.9	1.5

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