Industry In-Depth

17 November 2006 | 64 pages

Indian Textiles

A Laggard With Business and Earnings Momentum

Ashish Jagnani[1]

Supriya Gupte[1**]

Paul Chanin[2]

- What's new — 1) India's textile export growth has remained at high levels post-quotas; 2) the thrust on value addition is differentiating India from its regional peers and is driving higher prices and better margins; 3) significant operational capex suggests strong earnings growth visibility; and 4) the government continues to respond favorably to industry requests.

- Export growth continues; domestic demand is up too — Exports grew 14% YoY for Apr-Jul'06 despite a high base on increased outsourcing by global retailers and a mix shift towards garments (53% of 1QFY07 exports vs. 49% in FY04). We think this trend could gain momentum as more capacity becomes operational. Increased domestic demand on rising incomes would be an additional trigger.

- Earnings CAGR of 25% to exceed revenue CAGR of 16% for FY06-09E — Our industry CAGR forecasts are driven by richer product mix, soft raw material prices, low labor costs and higher operating leverage.

- The sector has significantly lagged the Sensex — This has likely been due to near-term volatility in earnings from initial hiccups in production ramp-up and high overhead for expansion, but we think the sector's relative PE to the Sensex to weak 2002-03 levels is unjustified. With above-market earnings growth and improving ROCE, we see re-rating potential to the sector's 10x Sept'07E PE.

- Top picks — Our top picks are Raymond, Gokaldas Exports and Alok Industries. We have downgraded our rating on Arvind and made some target price changes following valuation methodology changes for Vardhaman and JCT.

Figure 1. Statistical Abstract of Key Indian Textile Companies

			M Cap	Price	Target	EPS (Rs.)		PE (x)		2-yr CAGR	ROCE
Stocks	RIC	Rec	(US$m)	(Rs.)	Rs.	FY07E	FY08E	FY07E	FY08E	(%)	(%)
Alok Industries	ALOK.BO	1M	316	68.45	100	8.1	10.8	8.5	6.3	45	7.3
Arvind Mills	ARMI.BO	2M	261	52.85	64	2.4	4.6	22.2	11.7	8	7.8
Gokaldas Exp	GOKL.BO	1M	239	598.3	800	48.5	57.7	12.3	10.3	28	16.2
Raymond Ltd	RYMD.BO	1L	607	438.6	570	30.1	39	14.6	11.2	33	10.5
Vardhaman	MHSP.BO	1L	357	286.3	350	31.9	38.6	9	7.4	15	9.5
Welspun India	WLSP.BO	2M	156	91.85	110	8.1	10.6	11.4	8.7	36	7.2

Prices as of 16 November 2006

Source: Company Reports and Citigroup Investment Research estimates

See page 61 for Analyst Certification and important disclosures.

Contents

Investment Thesis

Growth fundamentals intact

India's textile industry appears ready for strong growth post-quota regime. Sustained high growth in exports, focus on enriching product mix, and growth in domestic branded apparel are key drivers. India's strength across the textile value chain, role as an alternative supplier to China, favorable reforms and significant capex becoming operational suggest improved earnings visibility. We think India is a good proxy on the regional textile outsourcing theme.

Key positive developments

With quotas dismantled for more than a year, the sector has witnessed encouraging trends: 1) Exports are up 14% YoY in Apr-Jul'06 despite a high base (18% growth of FY06) on growing order book and changing mix in favor of garments (53% of 1QFY07 exports vs. 49% in FY04); 2) re-imposition of quotas on China by the US and EU led large global retailers to increase outsourcing from India; 3) thrust on value addition differentiates India from its regional peers, drives higher prices and better margins; 4) significant capex that has become operational suggests strong earnings growth visibility; and 5) the government continues to respond favorably to industry requests. The surge in domestic demand, particularly branded apparels given rising incomes and growing penetration of malls, is an additional trigger, in our view.

We forecast earnings a 25% CAGR for FY06-09E

We expect growth in exports and increased domestic demand to drive revenue by a 16% CAGR and forecast an even stronger earnings CAGR of 25% for FY06-09E. This is based on richer product mix, soft outlook for raw material prices, improved productivity on low costs, and higher operating leverage with large-scale capacity expansion becoming operational.

Why the sector has significantly lagged the Sensex

High volatility in near-term earnings due to initial hiccups in production ramp-up, margin pressure due to higher overhead on newly commissioned expansion and the adverse impact of market-to-market provisions due to forex fluctuations are likely reasons. However, the sector's relative PE to the Sensex is down to 2002-03 levels, which is when the industry had a high degree of uncertainty. At the current level, we believe this is unjustified. Given our forecast for the sector is well above market earnings growth, the improvement of 2Q FY07 to 1Q FY07 earnings and improving capital efficiency, we see re-rating potential for the sector's valuation of 10x Sept'07E PE.

Top picks – Raymond, Gokaldas Exports and Alok Industries

We like vertically integrated companies that offer scale, a strong brand, have a thrust in exports and value addition, enjoy a close relationship with global retailers, and have healthy earnings growth visibility at reasonable valuations. Our top sector picks with these attributes include Raymond (Buy/Low Risk, 1L), Gokaldas Exports (Buy/Medium Risk, 1M) and Alok Industries (Buy/Medium Risk, 1M). We have downgraded Arvind Mills to Hold/Medium Risk (2M) on continued denim woes. We also made some target price changes on changes to our valuation methodology. We maintain our buy ratings on Vardhaman Textiles (Buy/Low Risk, 1L) and JCT (Buy/High Risk, 1H); hold rating on Welpsun India (Hold/Medium Risk, 2M); and sell ratings on S Kumars (Sell/High Risk, 3H) and Abhishek Industries (Sell/Medium Risk, 3M).

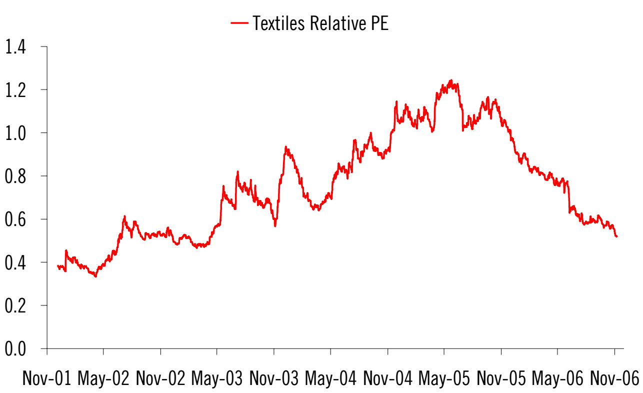
Valuations – Potential to Re-Rate

Sector's relative PE has declined to 2002-03 levels. With growth fundamentals intact, we see re-rating potential

The Indian textile sector has markedly lagged the Sensex due to volatility in near-term quarterly earnings when new expansion got commissioned and some concerns on stock liquidity hindered share price performances; the sector's PE relative to the Sensex has declined to 2002-03 levels – a period of high uncertainly for the industry. We believe this is unjustified. With strong earnings growth visibility, operating leverage likely to kick in on newly commissioned expansion and improving capital efficiency, we think there is potential for upward re-rating to sector's current valuation of 10x Sept'07E PE.

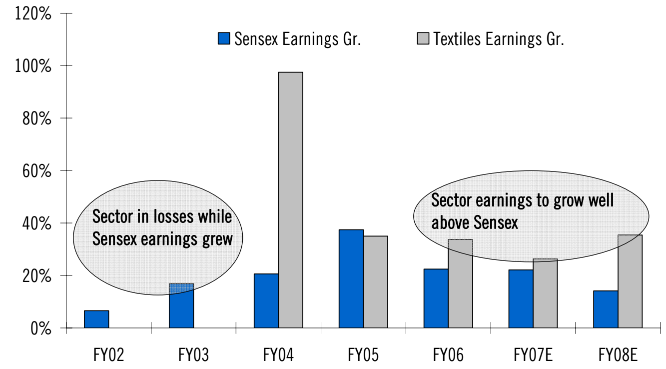
Despite intact growth fundamentals, the textile sector trades at 10x 12-month forward PE, close to the mean of its three-year historical range of 7-13x. With our forecast of higher earnings CAGR for the sector relative to the overall market, we think the Indian textile sector offers a good investment opportunity to tap the textile outsourcing theme. Even factoring in the commodity nature of the industry and taking in liquidity concerns, we still see upside potential to current valuations of 10x Sept'07E PE.

Figure 2. Indian Textile Sector PE Relative vs. Sensex



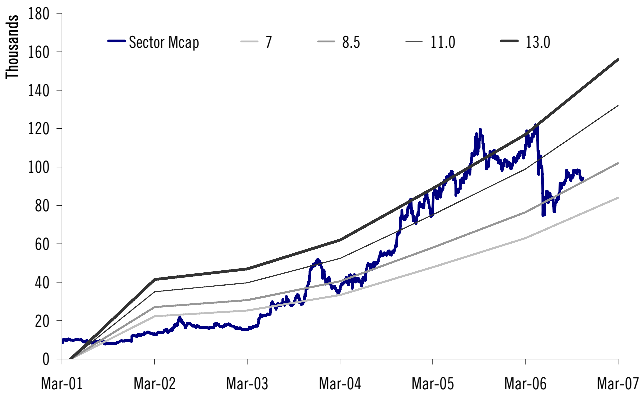
Source: Citigroup Investment Research

Figure 3. Citigroup Textile Universe Earnings Growth vs. Sensex Growth



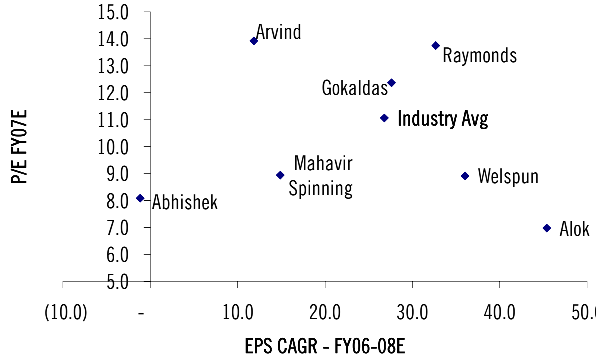
Source: Citigroup Investment Research estimates

Figure 4. Indian Textile Sector P/E Bands – 1yr forward



Source: Citigroup Investment Research estimates

Figure 5. 2-yr EPS CAGR v/s FY07E PE



Source: Citigroup Investment Research estimates

Top Picks and Rating Changes

Raymond offers 31% estimated total return

- **We reiterate our Buy/Low Risk (1L) rating on Raymond** — The company is a vertically integrated player with a strong brand that offers a robust business model for growth, in our view. We believe the stock offers multiple triggers including an earnings CAGR of 28% for FY06-09E, a strong brand-store network offering a proxy to the domestic retailing story, cash reserves of Rs4bn and potential unlocking of real estate assets. We reiterate our rating but have lowered our target price to Rs570 based on 16.5x Sept'07E PE that we ascribe to the sector leaders. Although this multiple is more conservative than our previous valuation metric of 2x EV/Sales, it still suggests a 31% estimated total return.

Gokaldas Exports – The best proxy to the garment outsourcing theme

- **We maintain a Buy/Medium Risk (1M) rating on Gokaldas Exports** — We think it offers the best proxy to the garment outsourcing theme. Large capacity, a wide product range with a thrust in enriching its product mix, close ties with global brands and new expansion going on-stream should drive growth. With global reforms favoring India post-quotas (after the US and EU re-imposed quotas on China), an earnings CAGR of 22% for FY06-09E, strong ROCEs (15%) vs. the sector (9%) and the likelihood of better liquidity following the company's announced 1:2 split, we maintain our rating and target price of Rs800 based on 15x Sept'07E (expected total return of 34%).

Alok – Significant operating leverage should drive rapid earnings CAGR of 38% for FY06-09E

- **We maintain a Buy/Medium Risk (1M) rating on Alok** — We forecast strong earnings growth visibility following Alok's major expansion in weaving-processing capacities of bed linen and its apparel fabric business has become operational. Significant operating leverage should drive rapid earnings CAGR of 38% for FY06-09E. With a thrust to diversify into a richer product mix, a growing order book for exports and compelling valuations of 7.3x Sept'07E PE, we maintain our rating and target price of Rs100 based on 10x Sept'07E PE (expected total return of 48%).

Arvind Mills – Continued weakness in the denim business prompts our rating downgrade

- **We have downgraded Arvind Mills to Hold/Medium Risk (2M)** on: 1) continued weakness in the denim business with supply growth likely to still exceed demand both domestically and regionally – we think, denim prices are unlikely to recover in the near term; 2) adverse impact on branded apparels profits following the company's JV with VF Corporation, US; 3) our downward revision in earnings. While the stock's laggard performance does discount some of this, its valuation of 11.9x FY08E does not offer much upside following our target price cut to Rs64, which is based on 14x FY08E earnings.

Vardhaman Textiles – We have lowered our lower target price to Rs350

- **Other picks**: Vardhaman Textiles is a leader in yarn, has a thrust in vertical integration and has strong management quality. We rate the stock as Buy/Low Risk (1L) on attractive valuations of 8x Sept'07E PE but have lowered our lower target price to Rs350 as we roll over to Sept'07E PE based on 10x PE – at par with the sector.

JCT – We have lowered our lower target price to Rs10

For JCT, we maintain our Buy/High Risk (1H) rating but have reduced our target price to Rs10 based on 10x FY08E PE. While delay in the company's expansion and modernization of plants have tempered its pace of turnaround – we have cut our earnings estimates for FY07-08E – we still forecast robust EPS CAGR of 77% for FY06-09E.

Welspun India – Hold/Medium Risk (2M) rating on moderate upside potential to our target price

For Welspun India – a fully integrated player in home textiles – we rate the stock Hold/Medium Risk (2M) in view of the company's high volatility in earnings due to margin pressure. We see only moderate upside to our target price of Rs110.

- **Our Sells:** We rate S Kumars Nationwide as Sell/High Risk (3H) on rich valuations and Abhishek Industries as Sell/Medium Risk (3M) on muted earnings growth and likely weakened price performance prospects following its large-scale paper expansions.

Scoring our universe on eight key criteria

In selecting our top picks, we look principally at eight key factors that address both qualitative and quantitative factors. Our top picks: Raymond, Gokaldas Exports and Alok Industries have the highest scores among our nine-stock universe.

Figure 6. Citigroup Indian Textile Universe: Eight Point Scorecard

	Global Scale	Integrated Capacities	Export Thrust	Value Addition	Brand Strength	Relationship with Global Retailers	Earnings Growth	Valuation	Total Score
Raymond	3	4	4	4	5	3	4	3	30
Alok Industries	3	3	3	3	3	4	5	5	29
Gokaldas Exports	3	2	5	4	4	5	3	2	28
Vardhaman Textiles	3	4	2	3	4	3	2	5	26
Welspun India	2	3	5	3	3	4	4	2	26
Arvind Mills	3	4	3	4	4	4	1	1	24
JCT	2	4	2	3	1	2	5	4	23
S Kumars Nationwide	1	2	1	3	2	2	5	1	17
Abhishek Industries	1	2	3	2	1	2	1	3	15

Source: Citigroup Investment Research

Figure 7. Valuation Summary of Citigroup Indian Textile Universe and Regional Peers

		Price (lcy)	Rating	Country	Yr End	Mkt Cap (US$m)	Sales (US$m)	PE (x) FY06	PE (x) FY07E	PE (x) FY08E	2-yr CAGR (%)	EBITDA Margin (%)	Price/ Sales (x)	ROCE (%)	P/BV (x)
ABHISHEK INDS	ABHP.BO	23.55	3M	India	Mar	105	132	8.2	9.1	8.4	-1	20.1	0.8	7.9	1.3
ALOK INDUSTRIES	ALOK.BO	68.45	1M	India	Mar	316	316	13.8	8.8	6.5	45	20.8	1.0	5.1	1.7
ARVIND MILLS LTD	ARMI.BO	52.85	2M	India	Mar	261	473	14.5	19.6	11.6	12	20.3	0.6	7.8	0.8
GOKALDAS EXPORTS	GOKL.BO	598.30	1M	India	Mar	239	194	17.5	12.8	10.7	28	9.0	1.2	15.0	3.1
JCT LTD	JCTL.BO	7.49	1H	India	Mar	59	117	28.1	22.1	7.7	91	4.5	0.5	6.4	2.0
RAYMOND LTD	RYMD.BO	438.60	1L	India	Mar	607	380	20.2	14.9	11.5	33	14.4	1.6	7.3	2.2
S KUMARS NATION	SKMK.BO	78.60	3H	India	Mar	290	395	30.6	18.9	13.0	53	16.4	0.7	5.9	4.8
VARDHAMAN TEXTILES	VART.BO	286.30	1L	India	Mar	357	421	9.4	8.6	7.1	15	18.4	0.8	10.5	1.7
WELSPUN INDIA	WLSP.BO	91.85	2M	India	Mar	156	145	15.8	11.2	8.5	36	18.2	1.1	5.1	1.3
FOUNTAIN SET HLD	0420.HK	2.32	3M	China	Aug	231	852	6.2	6.9	5.3	9	7.5	0.3	4.5	0.7
GLORIOUS SUN ENT	0393.HK	3.39	NR	China	Dec	459	489	14.2	13.1	11.6	11	11.3	1.0	15.6	2.2
TEXWINCA HLDG	0321.HK	5.10	NR	China	Mar	886	937	14.4	10.7	8.9	27	9.7	1.0	14.6	2.6
VICTORY CITY INT	0539.HK	2.61	1L	China	Mar	206	308	6.1	5.6	4.7	15	15.4	0.7	12.5	1.0
WEIQIAO TEXTI-H	2698.HK	10.06	NR	China	Dec	1,587	1,658	7.9	8.4	7.6	2	18.4	0.9	9.6	1.2
TOP FORM INTL	0333.HK	1.73	NR	Hong Kong	Jun	238	188	16.1	11.0	9.5	30	17.9	1.0	44.0	3.5
FAR EASTERN TEXT	1402.TW	26.60	1L	Taiwan	Dec	3,546	4,229	12.4	10.9	11.7	3	26.4	0.7	8.8	1.3
NIEN HSING TEXT	1451.TW	18.70	NR	Taiwan	Dec	339	384	8.2	6.0	5.7	20	13.7	0.8	11.9	1.0

Source: Bloomberg Estimates for non-rated (NR) stocks, Citigroup Investment Research;
Note Financials of companies with year end Dec'05 has been included as FY06.
Price as of 16 November 2006

Industry Macro Outlook Looks Strong

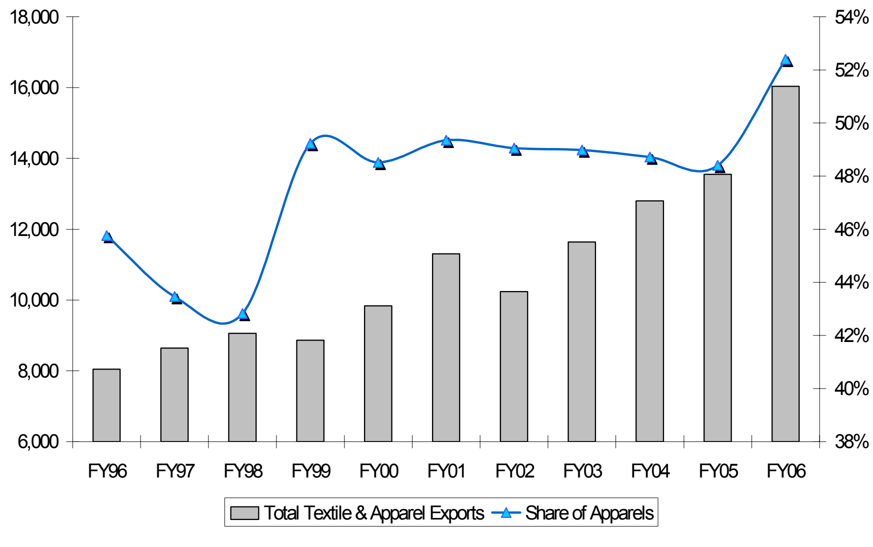
The Indian textile industry has started to benefit in a quota-free regime with: a) export growth sustaining at high levels post-quotas and India gaining market share; b) changing product mix in favor of higher value-added products to improve profitability; and c) thrust on value addition has differentiated India from regional peers and contributed towards higher price realizations and better margins. With a significant portion of the sector's large-scale capacity expansions now becoming operational (in phases), we expect operating leverage to drive earnings growth. The rise in domestic demand, particularly branded apparel – and considering the growing penetration of malls and rising income levels – are additional triggers, in our view.

Enriching the export mix

India's share of garments has increased to 51% in 1QFY07 vs. 49% for FY04. The trend appears to be gaining momentum

Exports are up 14% YoY in Apr-Jul'06 despite a high base (18% growth of FY06) on a growing order book. Traditionally, India has exported yarn and fabric (51% of FY04 exports) but this is fast changing in favor of higher value-added products such as garments. The increasing share of garments (c53% of 1QFY07 exports) is an early sign of this change in trend, in our view. We see this trend gaining momentum as more garmenting capacities become operational. Quotas on China by the US and EU have also led global retailers to diversify their outsourcing strategy, especially to India. We forecast higher exports growth of 18-20% for FY07E.

Figure 8. Total Indian Textile Exports (LHS – US$ m) vs Share of Garment Exports (%)

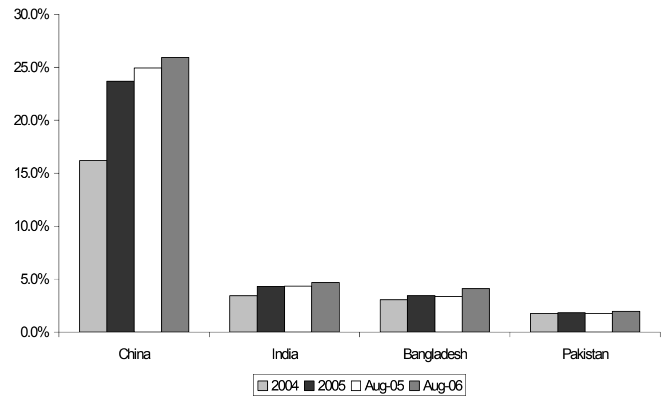


Source: Citigroup Investment Research

Value addition – A differentiating factor

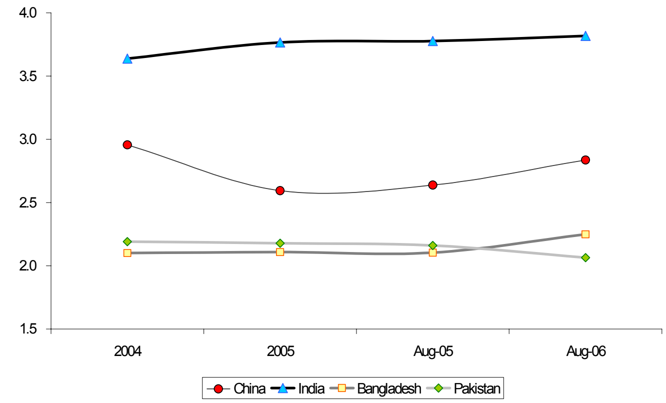
Focus on higher value addition and thrust on enriching product mix is India's attempt to differentiate from regional peers such as China and Pakistan; India's higher price realizations and increased market share of exports to the US in 1H06 vs. peers are early signs of this trend, in our view. We think this should mean better margins and healthier profitability in the future.

Figure 9. Exports to the US - Apparels Market Share by Country



Source: OTEXA

Figure 10. Realization for Apparel by Country



Source: OTEXA

Significant expansion becoming operational

We see high operating leverage improving earnings growth visibility

The sector expanded rapidly (4-5x) across the textile value chain in the past two year to take advantage of emerging growth opportunities. Significant parts of large-scale capacity expansion are now becoming operational in phases, which should help provide the sector with high operating leverage and improved earnings growth visibility. The expanded capacity would help meet bulk orders.

Domestic demand and textile production on the rise

Rising income levels and growing penetration of malls has led to a rise in domestic demand, particularly for branded apparel that has grown at 20%+. With domestic companies scaling up, global brands are queuing to enter India since the sector opened up to FDI. We expect growth rates to strengthen. Textile production is also growing on back of this growth. With more capacity becoming operational in phases, we expect sustained growth in textile production.

FDI in retail to trigger increased outsourcing

FDI in the domestic retail sector should lead global retailers to source more domestically, as was the experience for auto components

Entry of global giants making FDI into India's domestic retail markets should lead them to source more domestically. This would provide the industry with an opportunity to work with global retailers on quality standards and delivery schedules, and give retailers comfort about the manufacturing and designing capabilities of Indian vendors. This in turn should boost the outsourcing opportunity for India. We have already witnessed this in the Indian auto component sector with global automotive giants having entered the sector. We forecast a similar trend in the Indian textile and apparel industry for the next 3-5 years. The increasing number of retailers establishing "buying operations" in India an early sign of this trend, in our view.

Indian government continues to respond favorably to industry requests

The government recognizes the sector's potential to spur economic growth, generate employment and drive exports

The Indian textile industry, which employs more than 35m people, is the second-largest employment generator after the agriculture industry. The government recognizes the sector's potential to spur economic growth, generate employment opportunities and drive exports, thus it continues to respond favorably to industry requests to boost growth prospects, encourage further investment and enhance the global competitiveness of the textile sector. Specific measures include the following:

- Plan to extend the 5% interest subsidy via Technology Upgradation Fund (TUF) scheme, which was previously slated to expire in March 2007.
- Fast progress on relaxing labor laws to improve sector productivity. With textile SEZs offering flexible labor laws, we think a national rollout is not far.
- Establishment of Integrated Textile Parks for scaling manufacturing capabilities in India. Nine parks have already received permission by the Textile Ministry; the target is for 25.

2QFY07 performance improved from 1QFY07

2QFY07 was a good quarter, largely in line and better than 1QFY07

With more capacity expansion having become operational, revenue growth has picked up. EBITDA margins have expanded on richer product mix and some benefits from higher operating leverage, but the initial impact of higher overhead from the expansion, and increased depreciation and interest costs have resulted in muted earnings growth – yet it was still better than 1Q. Other income fell due to forex losses from foreign exchange rate volatility. With strong growth momentum and capacity utilization ramping up, we expect higher operating leverage to drive earnings and believe that growth rates can accelerate in the coming quarters.

Figure 11. Citigroup Indian Textile Universe 1HFY07 Quarterly Earnings Summary

Rs m	1QFY06	1QFY07	YoY	2QFY06	2QFY07	YoY	1HFY06	1HFY07	YoY
Net Sales	22,028	24,715	12%	24,858	28,798	16%	46,886	53,513	14%
EBITDA	3,881	4,453	15%	4,496	5,292	18%	8,377	9,744	16%
Margin	17.60%	18.00%		18.10%	18.40%		17.90%	18.20%	
Interest	994	1,093	10%	1,012	1,227	21%	2,006	2,320	16%
Other Income	485	203	-58%	489	296	-39%	974	500	-49%
Depreciation	1,437	1,643	14%	1,497	1,703	14%	2,934	3,345	14%
PBT	1,935	1,920	-1%	2,476	2,659	7%	4,411	4,579	4%
PAT before Ext.	1,540	1,506	-2%	1,961	2,151	10%	3,501	3,657	4%

Source: Citigroup Investment Research

Soft outlook on cotton prices

Cotton prices in India have started to decline on expectations of another bumper crop of 26-27m bales

The outlook on cotton prices remains soft in India given expectations of another bumper crop of 26-27m bales (vs. 24.4m bales last year) with increasing yields (460 Kgs/hectare) following higher usage of higher quality seeds of BT cotton. The outlook for global cotton prices is similar on expectations of higher cotton production of 147m bales. India cotton prices have already started to decline, and we think the trend will continue. This should provide the industry with access to low-cost cotton supply and give it a competitive cost advantage.

Rising concerns faced by regional peers

Increasing costs and deteriorating product mix in exports are some of the concerns of regional peers

Increasing costs of energy, labor and higher interest charges with falling price realization are growing concerns for countries such as China and Pakistan, which focus on volume growth for market share in exports to the US and EU. Pakistan started to see export growth tapering off after a surge in 2005 post-quotas and deterioration in its product mix with the decline in share of value-added products. China faces similar cost increases and its exports to the US declined in 1H06 for the first time due to the re-imposition of quotas in key garment categories. India too faces some of these cost pressures, but we believe the thrust on value addition should help it absorb these pressures. We believe growth concerns for core competitors such as China and Pakistan will enhance India's growth potential and market share in the global market.

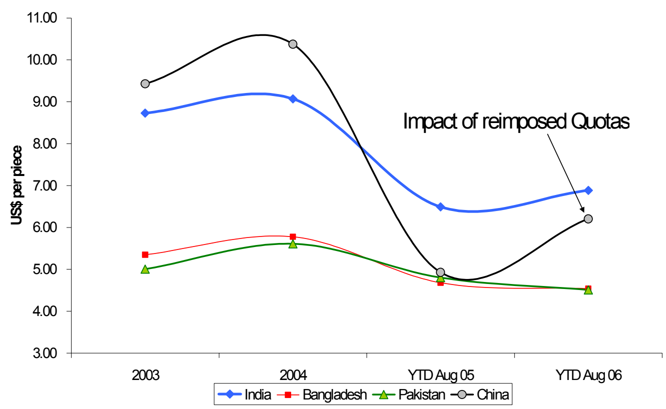
Key Growth Segments

Apparel exports enter a different growth orbit

Apparel exports grew 28% YoY in the first year post-quota versus a pre-quota growth CAGR of 4% for FY01-05

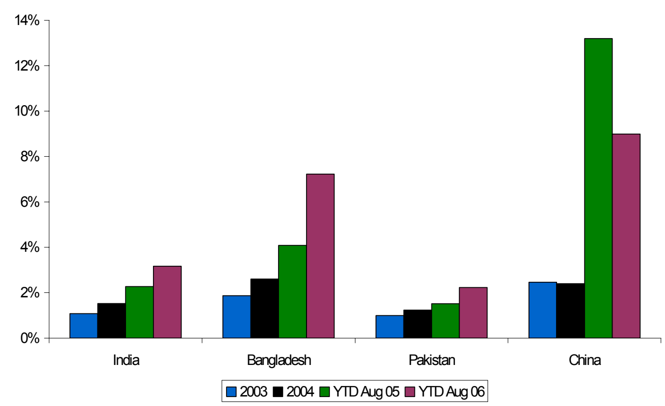
With the dismantling of quotas and new capacity expansions becoming operational, apparel exports have entered a different growth orbit. Apparel exports (US$8.4bn) grew 28% YoY in FY06 in first year post-quota compared with pre-quota growth of 4% CAGR for FY01-05. Exports were up 15% YoY in Apr-Jul'06 despite coming off a high base. With new capacities coming on-stream, we expect growth to pick up. Re-imposition of quotas on China by the US and the EU across key garment categories and rising quota costs in China provides India a relatively comfortable pricing scenario. Volumes have grown rapidly, particularly in cotton trousers and some shirt categories. Interestingly, while India's volume growth was lower than its peers' in the region, it still gained significant market share – largely benefiting from higher price realizations as compared with peers. This data point complements our view on Indian textile companies' focus on value addition for gaining market share rather than concentrating just on volume growth.

Figure 12. Export Realizations of Trousers to the US (US$ per Piece)



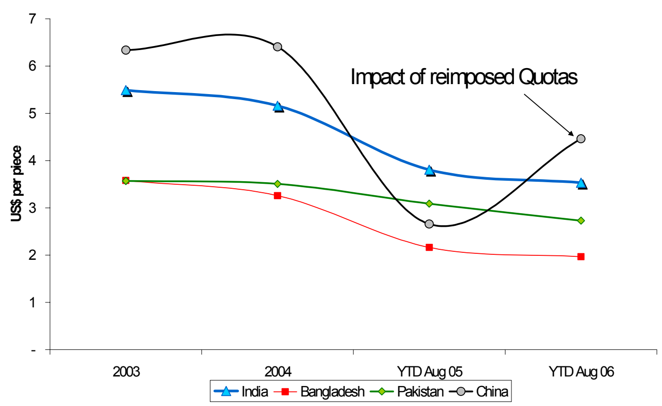
Source: OTEXA

Figure 13. Market Share by Value of Trouser Exports to the US



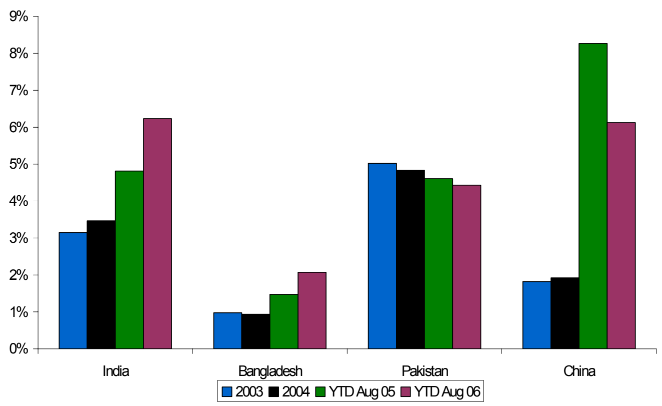
Source: OTEXA

Figure 14. Export Realizations of Shirts to the US (US$ per piece)



Source: OTEXA

Figure 15. Market Share by Value of Shirt Exports to the US



Source: OTEXA

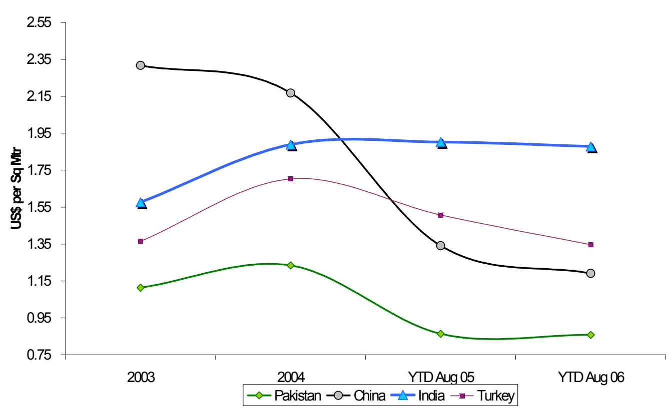
Home textiles in a growth zone

While India lost some market share to peers on low pricing, it is growing at a healthy pace in value-added segments with higher prices. This should benefit profitability

India is the largest supplier of terry towels (25% market share) and the third-largest supplier of bed linen (17% share) to the US. Indian home textile exports are in a growth zone. Although India has lost some market share to Pakistan and China due to aggressive shipments at low prices, it continued to grow at a healthy pace in higher value-added segments with high realizations compared with peers. Its greater presence in the decorative bed set segment has also been a step forward in India's strategy to enrich its product mix.

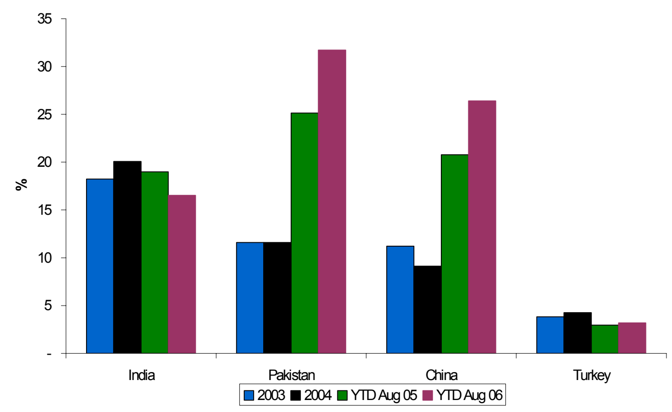
Terry towels is the fastest-growing segment, despite some pricing pressure, with exports to the US up 40%, followed by bed linen and decorative bed-set exports growing at 20% YTD Aug'06, respectively. With a significant part of new capacities now operational, growth rates are likely to pick up, particularly in bed linen and the decorative bed-set segments. We see higher operating leverage improving earnings growth visibility ahead.

Figure 16. Export Realizations of Bed Linen to the US (US$ per sqm)



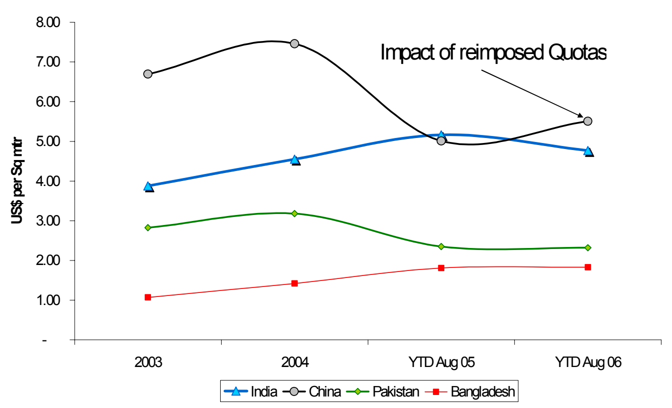
Source: OTEXA

Figure 17. Market Share by Value of Bed Linen Exports to the US



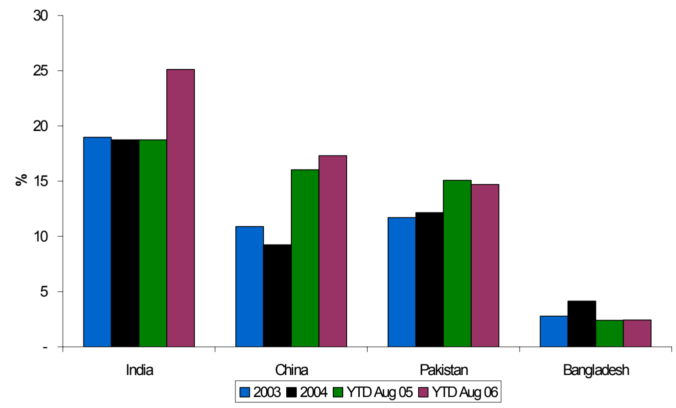
Source: OTEXA

Figure 18. Export Realizations of Terry Towels to the US (US$ per sqm)



Source: OTEXA

Figure 19. Market Share by Value of Terry Towel Exports to the US



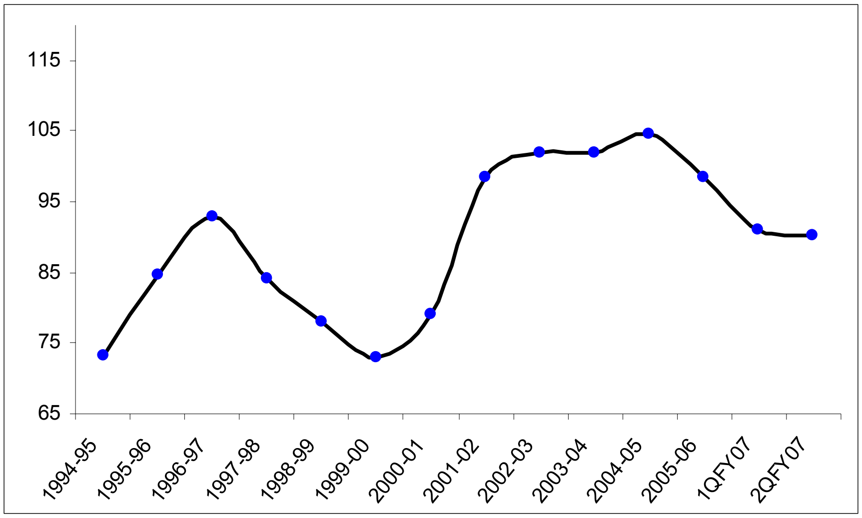
Source: OTEXA

Denim outlook remains subdued

With supply growth likely to still exceed demand domestically and regionally, denim prices are unlikely to recover in the near term, in our view

The denim segment continues to suffer from a sluggish environment, with continued pressure on denim prices. Although exports have shown some signs of recovery, the current decline in denim prices will likely arrest with supply growth expected to exceed demand both domestically and regionally. We think denim prices are unlikely to recover in the near term. Our channel checks (with domestic wholesalers and other denim players) suggest the key trends are: 1) the likelihood of cooling demand this quarter after good domestic demand in the festive season; 2) denim prices have bottomed but are unlikely to recover due to continued increases in supply – garment capacities for jeans remain insufficient; and 3) exports of value-added denim have picked up but growth in commodity denim capacities remains an overhang.

Figure 20. Arvind's Denim Price Realization Trend (Rs per Meter)



Source: Citigroup Investment Research

Figure 21. Indian Textile Exports to the US Versus Key Regional Peers

Description	India's value share (%)		India's Gr. (YTD Aug 06)		India's rank	Key Regional competitors			Value Gr. (%)
	YTD Aug 05	YTD Aug 06	Value (%)	Volume (%)		Country	Share (%)	Rank	
Bed Linen	19	17	20	21	3	Pakistan	31.7	1	73.65
						China	26.4	2	74.86
						China	18.3	2	10.75
Terry Towels	18.7	25.1	40.2	51.9	1	Pakistan	17.3	3	22.78
						Turkey	9.8	4	(14.28)
Decorative Bed sets	9.7	9.3	20.7	45.3	3	China	51.3	1	56.15
						Pakistan	22.4	2	26.53
Shirts						Pakistan	8.3	3	0.72
M/B Shirts*	7.5	8.5	21.3	26.6	2	Bangladesh	2.9	13	65.66
						China	4.8	7	(22.16)
						Pakistan	1.5	18	25.12
W/G Shirts*	2.7	4.5	83.4	96.1	9	Bangladesh	1.4	19	35.92
						China	7.1	3	(18.08)
Trousers						China	6.7	3	(36.68)
M/B Trousers*	2.6	3.4	31.7	26.6	8	Bangladesh	10.0	2	84.69
						Pakistan	2.8	12	29.53
						China	10.8	2	(30.84)
W/G Trousers*	2.0	3.0	43.4	32.4	12	Bangladesh	5.0	7	59.89
						Pakistan	1.8	16	69.65

Source: OTEXA, Citigroup Investment Research

*M/B – Men and Boys; W/G – Women and Girls

Paul Chanin[2]
+65-6432-1153
paul.chanin@citigroup.com

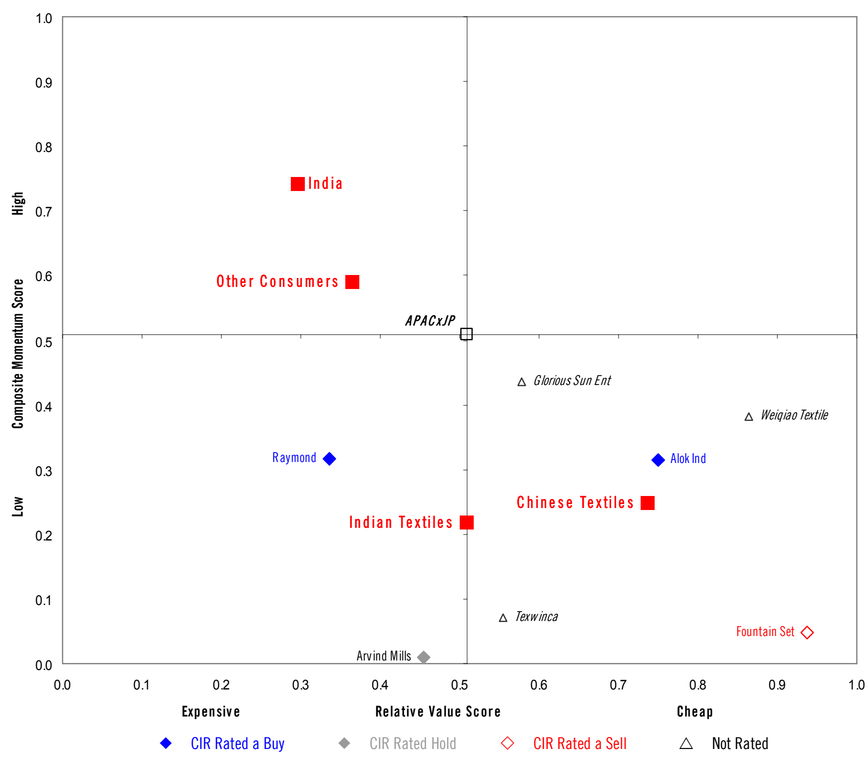
Quant View

Indian textiles lie on the border of the Contrarian and Unattractive quadrants for November. Although relatively less expensive than the Indian market and Other Consumers sector, compared with Chinese textile companies, the stocks appear expensive. The sector has weak composite momentum, ranking lower than the Indian market and Other Consumers sector on both price momentum and earnings estimates revision. It ranks better than the Chinese textiles sector on earnings estimates revision but has relatively weaker price support.

Rader Screen Quadrant Definitions

Glamour *Poor relative value but superior relative momentum*	**Attractive** *Superior relative value and superior relative momentum*
Unattractive *Poor relative value and poor relative momentum*	**Contrarian** *Superior relative value but poor relative momentum*

Figure 22. Radar Quadrant Plot



Source: Factset; IBES; Worldscope; Citigroup Investment Research

Arvind Mills (ARMI.BO)

Downgrade to Hold; Denim Woes Continue

Hold/Medium Risk	**2M**
from Buy/Low Risk	
Price (16 Nov 06)	Rs53.50
Target price	Rs64.00
from Rs90.00	
Expected share price return	19.6%
Expected dividend yield	0.0%
Expected total return	**19.6%**
Market Cap	Rs11,202M
	US$250M

Price Performance (RIC: ARMI.BO, BB: ARVND IN)

- Target price at Rs64 (14x FY08E EPS) — Our downgrade is premised on (1) increased supply exerting pressure on denim prices, (2) an adverse impact on branded apparel profits following a JV with VF, and (3) lower estimates to factor in the above pressures and forex losses.

- Denim outlook still subdued — Denim continues to suffer in a sluggish environment, but exports have shown some signs of recovery. With supply exceeding demand domestically and regionally, denim prices will likely remain subdued. Arvind's strategy to relocate some denim capacity to Bangladesh should be positive only in the long term.

- Branded apparels turnaround delayed — With Arvind's key premium brands, Lee and Wrangler, transferred to the 60:40 JV with VF Corp, we forecast a decline in sales and lower profitability of mass brands to delay turnaround of the branded apparel business (100% subsidiary, now merged) by a year, to FY09.

- Garment scale-up remains encouraging — We expect a revenue CAGR of 46% over FY06-09, contributing 23% of FY09E sales vs. 9% in FY06. Utilization of the jeans plant picked up to 70% in 2Q FY07, with export orders booked until April 2007. The company plans to increase capacity from 4m to 16m units by Dec 2007. Knits and Shirts are also showing good improvement.

- Conclusion — The stock's 16% decline over the past month likely discounts the denim woes. The company's thrust on vertical integration and growing share of garments should reduce its earnings sensitivity to denim over the next two years.

Consolidated Statistical Abstract

Year to 31-Mar	Net Profit (Rs M)	FD EPS (Rs)	EPS Growth (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	ROCE (%)
2005	1,046	5.4	31.2	10.1	0.9	7.1	8.7
2006	815	3.9	-27.3	13.9	0.8	7.6	7.8
2007E	505	2.4	-38.0	22.4	0.8	7.7	5.7
2008E	955	4.6	88.9	11.9	0.7	6.6	6.8
2009E	1,393	6.7	45.9	8.1	0.7	5.6	8.1

Source: Company Reports and Citigroup Investment Research estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	10.0	13.7	22.2	11.7	8.0
EV/EBITDA adjusted (x)	6.8	7.4	8.0	6.7	5.7
P/BV (x)	0.9	0.8	0.7	0.7	0.7
Dividend yield (%)	1.9	1.9	0.0	0.0	0.0
Per Share Data (Rs)					
EPS adjusted	5.35	3.89	2.41	4.56	6.65
EPS reported	5.35	3.89	2.41	4.56	6.65
BVPS	59.76	69.88	71.52	75.08	80.24
DPS	1.00	1.00	0.00	0.00	0.00
Profit & Loss (RsM)					
Net sales	19,608	21,304	21,139	22,654	25,027
Operating expenses	-17,164	-18,987	-19,112	-20,291	-22,215
EBIT	**2,444**	**2,317**	**2,027**	**2,363**	**2,812**
Net interest expense	-1,437	-1,718	-1,500	-1,400	-1,350
Non-operating/exceptionals	114	332	65	55	50
Pre-tax profit	**1,122**	**930**	**592**	**1,018**	**1,512**
Tax	-20	-106	-30	-51	-151
Extraord./Min.Int./Pref.div.	-56	-9	-57	-13	32
Reported net income	**1,046**	**815**	**505**	**955**	**1,393**
Adjusted earnings	1,046	815	505	955	1,393
Adjusted EBITDA	4,259	4,318	4,089	4,590	5,217
Growth Rates (%)					
Sales	24.8	8.6	-0.8	7.2	10.5
EBIT adjusted	8.8	-5.2	-12.5	16.6	19.0
EBITDA adjusted	3.7	1.4	-5.3	12.3	13.7
EPS adjusted	31.2	-27.3	-38.0	88.9	45.9
Cash Flow (RsM)					
Operating cash flow	**-2,091**	**4,042**	**1,523**	**2,403**	**2,443**
Depreciation/amortization	1,815	2,001	2,061	2,226	2,404
Net working capital	-4,070	-2,253	1,355	-569	-998
Investing cash flow	**-61**	**-7,903**	**-140**	**-943**	**-804**
Capital expenditure	-470	-6,919	-1,188	-1,023	-1,036
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	**2,182**	**4,189**	**-1,488**	**-1,324**	**-1,514**
Borrowings	2,377	2,765	-1,326	-1,115	-1,200
Dividends paid	-195	-209	-209	-209	-314
Change in cash	**30**	**327**	**-104**	**135**	**125**
Balance Sheet (RsM)					
Total assets	**34,572**	**40,787**	**39,485**	**39,002**	**38,777**
Cash & cash equivalent	205	240	136	271	396
Accounts receivable	2,020	1,673	1,797	1,926	2,002
Net fixed assets	18,689	23,237	22,364	21,161	19,793
Total liabilities	**21,646**	**24,856**	**23,425**	**22,241**	**20,830**
Accounts payable	1,744	1,552	1,961	1,806	1,585
Total Debt	18,971	21,736	20,410	19,295	18,095
Shareholders' funds	**12,926**	**15,932**	**16,060**	**16,761**	**17,947**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	21.7	20.3	19.3	20.3	20.8
ROE adjusted	9.5	6.2	3.4	6.2	8.6
ROIC adjusted	8.3	6.4	5.5	6.6	7.7
Net debt to equity	145.2	134.9	126.2	113.5	98.6
Total debt to capital	59.5	57.7	56.0	53.5	50.2

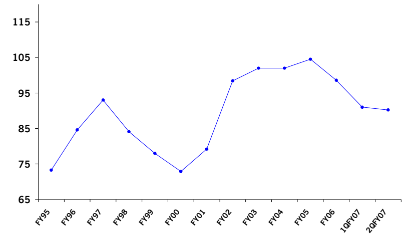
For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com
or +852-2501-2791

Powered by: dataCentral

Key Points

Denim outlook still subdued

Arvind Mills Denim Realz per mtr (Rs.)



Source: Citigroup Investment Research

Denim continues to suffer in a sluggish environment, which continues to pressure denim prices. Although exports have shown some signs of recovery, supply growth is likely to still exceed demand domestically and regionally. Our channel checks (with domestic wholesalers and other denim players) suggest the following: (1) after strong domestic demand from the upcoming festive season, demand is set to cool in the coming quarter; (2) denim prices have bottomed out but are unlikely to recover due to continued increase in supply, and garment capacities for jeans are still insufficient; (3) exports of value-added denim have picked up, but growth in commodity denim capacities remains an overhang.

Arvind's focus on higher-value-added segments and its strategy to relocate excess denim capacity to Bangladesh to capture growth in garment exports, while India scales up in garmenting capacities, are long-term positives. But we do not see any benefits next year given the gestation period for relocating plants and the time needed to stabilize production in a new operating environment. Given that denim is still 41% of consolidated revenues, Arvind's earnings in the near term remain highly sensitive to denim prices.

JV to push back turnaround for branded apparel business

Arvind Brand (was a 100% subsidiary of Arvind Mills earlier, now merged) has entered into a 40:60 joint venture with VF Corp for branded apparels. VF Corp will pay a one-time US$33m to Arvind Mills for a 60% stake in the new joint venture. Arvind, however, will transfer (1) existing marketing licenses for key premium apparel brands (c40% of branded apparel sales), Lee, Wrangler, Nautica, Jansport and Kipling from 1st Sept 2006, and 2) designing, sourcing rights of these brands and marketing rights for new brands from VF's brand portfolio in the future to the new venture. The existing retailing and store infrastructure with a 40% stake in the new JV will remain with Arvind Mills.

Although this will provide Arvind with upfront cash flow of Rs1.5bn, we see it adversely impacting branded apparel profitability long-term. With key premium brands growing at 20%-plus, we forecast a drop in sales and lower profitability of mass brands (EBITDA margin of 3-4%) — pushing back turnaround of the branded apparel business by a year, to FY09E. Factoring this, we forecast an 8% CAGR decline in sales vs. 22% growth assumed earlier for FY07-08E and profit of Rs30m in FY09E vs. our earlier estimate of Rs128m for FY08.

Earnings estimates, target price reduced

We are reducing our revenue and net profit estimates for Arvind by 8-14% and 24-46% respectively over FY06-08 to account for (1) sluggish growth in denim for a longer period than expected, (2) declines in sales and profitability following transfers of key premium brands to a new JV, (3) higher interest costs, and (4) an unexpected forex loss.

Lowering of estimates was triggered by (1) continued weakness in denim prices, (2) loss of sales following the transfer of rapidly growing profitable brands to the new JV, which we believe would push back the turnaround of the branded apparel business, and (3) an unexpected forex loss of Rs140m in 1H FY07 due to rupee volatility. Further, increased power cost due to shortage of gas and higher interest costs due to increased cotton inventory have increased pressure on earnings. We had earlier factored in a denim revenue CAGR of 5% over

FY06-08 and branded apparel business turning around with profits of Rs128m in FY08. We are now assuming a denim revenue CAGR decline of 8% over FY06-08E and expect branded apparel turnaround to be pushed back to FY09E with lower profits of Rs30m.

Factoring in our new assumptions and improved visibility for FY09E, we expect revenue and earnings CAGRs of 6% and 20% respectively over FY06-09E, with much of the growth being back-ended. In our view, Arvind's efforts to diversify to higher-value-added segments and increase contribution from the garmenting business will lower the sensitivity of Arvind's consolidated earnings to denim prices. We cut our target price to Rs64, based on 14x FY08E P/E (lower than the 15x assumed earlier because of poorer prospects for denim).

Earnings Revision (Rupees in Millions, Percent)

Year to	FY07E			FY08E		
31-Mar	New	Old	% Chg	New	Old	% Chg
Revenue	21,139	23,069	-8.4	22,654	26,205	-13.5
EBITDA	4,089	4,622	-11.5	4,590	5,482	-16.3
Net Profit	505	941	-46.3	955	1,246	-23.4
EPS	2.4	4.5	-46.4	4.6	6.0	-24.0

Source: Citigroup Investment Research estimates

Garment scale-up encouraging

After initial hiccups in the scale-up, garment operations are now showing rapid growth. With new capacities coming on stream in phases, productivity levels are on the rise. Thanks to increased export demand, garment export revenues are on the rise. Encouraging response from buyers, thrust on the middle-top end garment market, new product development and strong vendor relationships with a spectrum of global retail brands are resulting in healthy order flows. Management has aggressive expansion plans in garments, and targets to have capacities of 42m pieces by FY09. We believe the garment exports business is at an inflection point and see rapid growth over the next two years. This would de-risk the company’s dependence on fabric (72% of consolidated FY06 revenues) and, on our projections, garment’s share of revenues will increase from 9% in FY06 to 23% by FY09E.

Arvind Mills

Company description

Arvind Mills is one of the world’s largest denim manufacturers and one of India’s largest textile exporters. Aside from leadership in denim (a 72% market share) in India, Arvind Mills has a presence in shirting, knits, khakhis, voiles fabrics and a wide range of garments. it is an integrated player with a presence across the textile value chain — global capacity of 154m meters in fabrics, vertical integration to garments, strong brand franchise and a distribution network for branded apparels. Arvind’s wide product range, scaleable capacities and ability to offer specialty fabrics and high-end garments make it a preferred vendor in the domestic market and to global brands. It is the flagship company of the Lalbhai Group, which owns a 34% stake.

Investment thesis

We rate Arvind Mills as Hold/Medium Risk (2M). While poor prospects for denim are dampening sentiment toward the stock, we believe the company's vertically integrated business model across cotton textiles, focus on a richer product mix and close ties with global retailers are positives. We see Arvind's thrust on garments and efforts to relocate denim capacities overseas will reduce earnings sensitivity to denim fabric prices over the long term.

Valuation

Our target price of Rs64 is based on 14x FY08E P/E, at a discount to the 16.5x we ascribe to the top-tier textile companies in India. We ascribe a discount due to the weak prospects facing the denim business. However, we still believe it will trade at a premium to our India textile universe valuation of 9x FY08E P/E. The premium is attributable to Arvind's initiatives to vertically integrate and move up the value chain, its domestic leadership, close relationship with global retailers and presence in branded apparel retailing in the domestic market. We use P/E as our primary valuation tool because it captures growth potential.

Risk

We rate Arvind Mills as Medium Risk, as opposed to the Low Risk rating based on our quantitative risk-rating system, which tracks 260-day share-price volatility. The key reasons for our Medium Risk rating include high earnings volatility due to the pressure on denim prices and an adverse impact from forex fluctuations. The main upside risks to our target price include: (1) Strong up-tick in denim prices would significantly improve earnings growth visibility. An increase in denim prices of more than 5% would impact Arvind's profitability. (2) Large tie-ups with global retailers for sourcing garments would put our assumptions at risk. (3) Stronger-than-expected turnaround for its branded apparel division would contribute towards higher growth.

The main downside risks to our target price include: (1) Changes in fashion could hurt denim demand; (2) any sharp decrease in cotton prices from its existing inventory cost of Rs42.5/kg; (3) delay in the ramp-up of garment capacities; and (4) rupee depreciation from Rs46/US$1 (average rate at which forex exposures are hedged) would lead to forex losses.

Raymond Ltd (RYMD.BO)

Buy: Poised for Sustained Growth

Buy/Low Risk	**1L**
Price (16 Nov 06)	Rs438.60
Target price	Rs570.00
from Rs625.00	
Expected share price return	30.0%
Expected dividend yield	1.3%
Expected total return	**31.2%**
Market Cap	Rs26,922M
	US$595M

Price Performance (RIC: RYMD.BO, BB: RW IN)

- Reiterate Buy — With growth fundamentals intact, expanding store network offering a proxy to play domestic retailing story, and the company's strong balance sheet with cash reserves of Rs4bn, we reiterate Buy with a lower target price of Rs570 based on 16.5x Sept 07E P/E ascribed to leaders, which is more conservative than the 2x EV/Sales assigned earlier; implied 31% ETR.

- Improved earnings growth visibility — With most expansions in worsted fabric, denim, shirting-carded woolen fabric and garmenting commissioned – we see improved earnings growth visibility due to focus on richer product mix and higher operating leverage; we forecast earnings CAGR of 28% over FY06-09E.

- Thrust on branded retailing — The company plans to expand its premium brand portfolio and existing network of around 400 retail outlets by adding 75 new stores. We estimate revenue growth of 15% over FY06-09E and higher EBITDA margins of 14% (vs. 6-7% for peers) given its premium positioning, which should contribute towards earnings growth.

- Garment operations in ramp-up mode — We see rapid growth in export garment operations of suits, trousers, jeans and shirts (all 100% subs), after initial hiccups, to account for 13% of total revenues by FY09E from 4% in FY06. Healthy order flow in exports and improving capacity utilization to drive earnings of Rs316m for FY09E vs. an Rs183m loss in FY06.

- Other catalysts — 1) Leadership and strong brand franchise in domestic branded retail market; 2) Management's focus on inorganic initiatives for growth; and 3) any developments on unlocking of real estate assets.

Consolidated Statistical Abstract

Year to 31-Mar	Net Profit (Rs.Mn)	FD EPS (Rs)	EPS Gr. (%)	P/E (x)	EV/EBITDA (x)	P/BV (x)	ROCE (%)
2005	906	14.8	(34.2)	29.7	17.0	2.3	6.1
2006	1,361	22.2	50.2	19.8	12.0	2.1	7.3
2007E	1,847	30.1	35.7	14.6	9.0	1.9	9.0
2008E	2,396	39.0	29.7	11.2	7.3	1.7	10.5
2009E	2,823	46.0	17.8	9.5	6.2	1.4	11.4

Source: Company Reports and Citigroup estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	29.7	19.8	14.6	11.2	9.5
EV/EBITDA adjusted (x)	16.7	11.7	9.3	7.5	6.4
P/BV (x)	2.3	2.1	1.9	1.7	1.4
Dividend yield (%)	0.9	1.1	1.3	1.3	1.4
Per Share Data (Rs)					
EPS adjusted	14.76	22.17	30.09	39.03	45.99
EPS reported	14.76	22.17	30.09	39.03	45.99
BVPS	191.42	207.52	232.11	265.64	305.63
DPS	4.00	5.00	5.50	5.50	6.00
Profit & Loss (RsM)					
Net sales	14,401	17,106	19,862	22,921	25,012
Operating expenses	-13,530	-15,518	-17,487	-19,783	-21,183
EBIT	**871**	**1,588**	**2,376**	**3,138**	**3,828**
Net interest expense	-307	-390	-380	-365	-350
Non-operating/exceptionals	869	826	684	751	761
Pre-tax profit	**1,432**	**2,024**	**2,680**	**3,524**	**4,240**
Tax	-277	-610	-833	-1,128	-1,417
Extraord./Min.Int./Pref.div.	-250	-54	0	0	0
Reported net income	**906**	**1,361**	**1,847**	**2,396**	**2,823**
Adjusted earnings	906	1,361	1,847	2,396	2,823
Adjusted EBITDA	1,578	2,463	3,281	4,148	4,888
Growth Rates (%)					
Sales	14.3	18.8	16.1	15.4	9.1
EBIT adjusted	18.2	82.4	49.6	32.1	22.0
EBITDA adjusted	11.3	56.1	33.2	26.4	17.8
EPS adjusted	-34.2	50.2	35.7	29.7	17.8
Cash Flow (RsM)					
Operating cash flow	**1,721**	**1,961**	**1,758**	**2,681**	**2,636**
Depreciation/amortization	707	875	905	1,010	1,060
Net working capital	108	-274	-994	-725	-1,247
Investing cash flow	**-2,895**	**-4,707**	**-1,212**	**-2,060**	**-1,519**
Capital expenditure	-2,887	-5,120	-1,574	-3,129	-1,892
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	**1,345**	**2,852**	**-619**	**-614**	**-1,143**
Borrowings	1,433	3,002	-361	-302	-800
Dividends paid	-246	-307	-338	-338	-368
Change in cash	**170**	**107**	**-73**	**7**	**-26**
Balance Sheet (RsM)					
Total assets	**21,906**	**27,191**	**28,018**	**30,549**	**30,921**
Cash & cash equivalent	494	576	415	422	201
Accounts receivable	2,645	3,022	3,377	4,011	4,252
Net fixed assets	6,904	11,196	11,865	13,984	14,816
Total liabilities	**10,033**	**14,230**	**13,477**	**13,909**	**11,876**
Accounts payable	1,525	2,296	2,156	2,441	2,415
Total Debt	6,411	9,413	9,052	8,750	7,950
Shareholders' funds	**11,873**	**12,961**	**14,541**	**16,640**	**19,045**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	11.0	14.4	16.5	18.1	19.5
ROE adjusted	7.9	11.1	13.7	15.7	16.1
ROIC adjusted	5.2	6.7	8.6	9.9	10.6
Net debt to equity	49.8	68.2	59.4	50.0	40.7
Total debt to capital	35.1	42.1	38.4	34.5	29.5

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

Powered by: dataCentral

Key Points

Branded retailing the focus

Raymond is among the few highly profitable players in the domestic branded apparel business. Management has aggressive plans to expand its premium brand portfolio and widen its existing distribution network of around 400 retail outlets (10% are owned, which should increase). This retail build-out is positive, however, with most peers in branded retailing scaling up, new international brands queuing up to enter India, and real-estate prices spiraling, risk of delays in rolling out new stores is high. Additionally, consumer stickiness will be critical for growth, a challenge for retailing business in general.

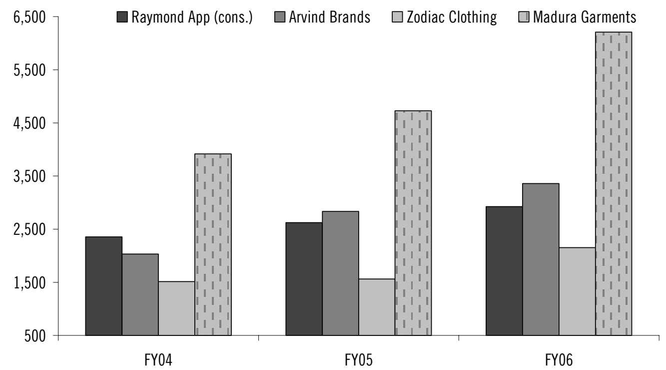
Raymond's strong brand penetration across India would help it tide over these challenges giving it an edge over peers. The company is considering widening its portfolio of brands to focus more on jeans and women's wear, which we believe should enhance customer base. It recently entered into a 50:50 joint venture with Grotto S.p.A of Italy to launch the 'GAS' brand in casual apparels and accessories, particularly jeans wear. The company has also recently acquired the remaining 25.9% stake in Colorplus Fashions, making it a wholly owned subsidiary. It plans to add 75 new stores in FY07 investing Rs450m and is targeting revenue CAGR of 25% over next two years. We forecast healthy revenue growth of 15% over FY06-09E and higher EBITDA margins of c.14% (vs. 6-7% for peers) given its premium positioning, which should contribute towards earnings CAGR of 28%.

Brand Portfolio & Exclusive Store Network of Key Branded Apparel Retailers in India

Company	Key Brands	No of Exclusive Stores
Raymond Apparels	Park Avenue, Parx, Colorplus, Manzoni	75
	Raymond (Fabric retail outlets)	300
Arvind Brands - Intl Brands	Arrow, Lee, Wrangler, Tommy Hilfiger	173
- Own Brands	Flying Machine, Newport, Ruf & Tuf, Excalibur	38
Zodiac Clothing	Zodiac, Zod	50
Madura Garments	Louis Philippe, Allen Solly, Van Heusen, SF Jeans, Peter England	59

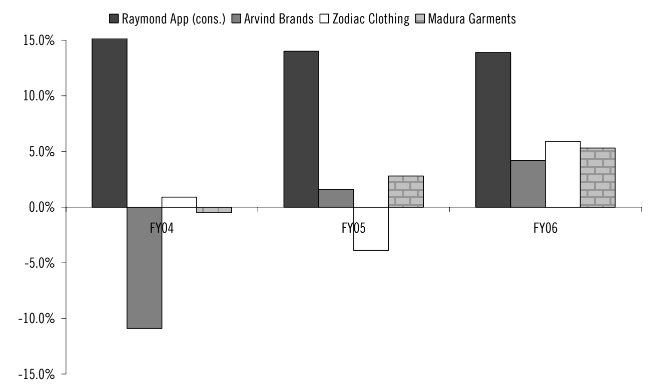
Source: Citigroup Investment Research

3-yr Revenues of Key Indian Branded Apparel Players



Source: Company, Citigroup Investment Research

3-yr EBITDA Margins of Key Indian Branded Apparel Players

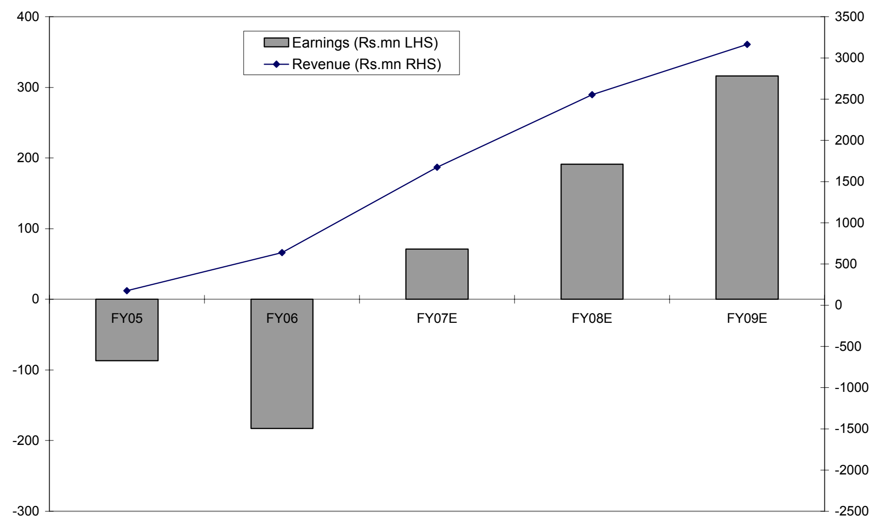


Source: Company, Citigroup Investment Research

Rapid growth prospects in garment exports

We see rapid growth in export garment operations of suits, trousers, jeans and shirts (all 100% subs) after initial hiccups. On our forecasts, garment exports' share of total revenues will rise from 4% in FY06 to 13% by FY09E. With export orders picking up and capacity utilizations expected to increase from 29% in FY06 to 60%-plus levels by FY08E (the company recently renewed its formal men's suits outsourcing arrangement for 150,000 suits per annum with Konaka & Co, largest menswear retailer in Japan), we expect garment operations to turn around and contribute earnings of Rs316m for FY09E vs. a Rs183m loss in FY06.

Garment operations turning around



Source: Company, Citigroup Investment Research estimates

Most of the expansion is operational

Most of expansion in worsted fabric (3m mtrs), denim (10m mtrs), shirting (11.7m mtrs) – carded woolen fabric (1m mtrs) and files has been commissioned. We believe timely scale up of production will be the key growth driver. In addition, the company has announced additional expansion of 3m meters in worsted fabric at VAPI (due 1QFY08) with investment of Rs2bn and plans to further ramp up garmenting capacities. Management is also exploring inorganic growth opportunities

Raymond Ltd

Company description

Raymond is among the top three worsted fabric players in the world, with capacity of 28m meters per annum. In India it is a leader with 60% market share, strong brand equity and a distribution network of 400 retail outlets. It also has a presence in denim and branded apparel garments, which it is looking to ramp-up. In files & tools, a non core engineering business, it is one of the largest producers with a 30% share, and dominates the domestic market with a 70% share. Its thrust on garmenting is a step toward vertically integrating its business model, leveraging off its fabric capacity. It is the flagship company of the Singhania Group, which owns a 35% stake in the company.

Investment thesis

We maintain a Buy (1L) rating on Raymond with lower target price of Rs570 based on 16.5x Sept 07E P/E at premium to sector valuations of 10x. This implies total return of 31% over a 12-month horizon. The premium is attributed to: 1) robust business model with strong brand; 2) a play on domestic branded retailing with wide network of stores; and 3) sustained earnings CAGR of 28% over FY06-09E.

With most of new expansions now operational, its JV in denim set to significantly scale up business, its thrust on vertical integration into garments, and partnerships with global players post quota removals, we believe Raymond offers a robust business model for growth. With growth fundamentals intact, cash reserves of Rs4bn, and potential unlocking of real estate value, we believe Raymond offers multiple growth triggers – and hence is our top sector pick.

Valuation

We are lowering our target price from Rs625 to Rs570. Our revised target price is based on 16.5x Sept 07E P/E. We believe P/E is a suitable valuation tool and more conservative compared to 2x EV/Sales assumed earlier, because it best captures the company's strong earnings growth potential. Our target multiple still places the stock at significant premium to our India textile universe valuations of 10x building for: 1) robust business model with strong brand; 2) a play on domestic branded retailing (45% of FY06 revenues) with wide network of stores; and 3) sustained earnings CAGR of 28% over FY06-09E

The stock is trading at 12.7x Sept 07E P/E towards the lower end of last 2-years trading band of 12-17.5x, which in our view does not completely discount its robust business model. With its premium brand positioning allowing some pricing power, improved earnings growth visibility, we believe the stock offers a re-rating potential and expect valuations to appreciate.

Risks

We rate Raymond Low Risk based on our quantitative risk rating system that measures the stock volatility over a 260-day period. The main company-specific risks are detailed below.

- High priced acquisitions to dilute cash reserves and adversely impact ROCE's. Acquisitions in non-core business would hinder re-rating;

- Delay in ramp up of production at export garment operations would adversely impact our earnings growth estimates;

- Sharp increase in cotton prices by 10-12% from current levels of Rs52/kg and any decline in denim price realization would impact profitability of the denim business (17% of FY06 sales), with cotton costs constituting (43% of denim revenues);
- Strong appreciation of over 5% in Rupee from levels of Rs45.4 would lower export price realizations (18% of FY06 revenues); and
- Any large VRS costs for reducing the work force would reduce its cash surplus of Rs4bn and the returns generated.

If any of these risk factors plays out, Raymond's share price will likely have difficulty attaining our target price.

Buy/Medium Risk	1M
Price (16 Nov 06)	Rs598.30
Target price	Rs800.00
Expected share price return	30.5%
Expected dividend yield	0.5%
Expected total return	**31.0%**
Market Cap	Rs10,535M
	US$233M

Price Performance (RIC: GOKL.BO, BB: GEXP IN)

Gokaldas (GOKL.BO)

Buy: Best Proxy to Garment Outsourcing

- Reiterate Buy/Medium Risk — Gokaldas' large capacities, wide product range and close ties with global brands make it poised for growth. We think it offers the best proxy to the garment outsourcing theme; our target of Rs.800 implies 33% upside.

- Growth catalysts — 1) Growing order books in exports, orders worth Rs.2.6bn in hand for 3Q07; 2) focus on diversifying customer base; 3) expansions going on-stream to accelerate export growth; and 4) any relaxation on labor laws would enhance growth potential.

- Enriching product mix further — Plans to enter the structured suits market for men and women (suits fetch higher prices and superior margins) – setting up a new facility in Bangalore by Dec'06. This apart, exploring export opportunities in new products like 1) industrial work-wear 2) innerwear and sleepwear products and 3) garments made from technical textiles.

- Expansions progressing at fast pace — Started operations at Chennai SEZ plant in Oct'06, production to ramp up by 4Q. Expects to expand capacity by 30% at two plants in Bangalore, commission suits facility and new plant in Mysore by Apr'07 – this will increase capacity by 15% yoy to 30mn pieces p.a. Capex of Rs.1.2bn over the next two years will be funded by internal accruals and existing IPO funds.

- Valuations to appreciate – Stock is trading at 11.2x Sept'07E P/E, with global reforms favoring India, company's healthy earnings CAGR of 22% over FY06-09E, superior ROCEs vs. sector and stock likely to offer better liquidity given recent announcement of 1:2 split, we expect valuations to appreciate.

Statistical Abstract

Year to 31-Mar	Net Profit (Rs)	FD EPS (Rs)	EPS Gr. (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	ROCE (%)
2005	396	23	nm	25.8	5.0	22.0	18%
2006E	609	35.4	54	16.8	3.0	15.0	15%
2007E	834	48.5	37	12.3	2.4	10.7	15%
2008E	991	57.7	19	10.3	2.0	9.1	16%
2009E	1,104	64.2	11	9.3	1.7	8.2	16%

Source: Company Reports and CIR Estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	26.6	17.3	12.6	10.6	9.5
EV/EBITDA adjusted (x)	22.0	15.5	10.8	9.3	8.3
P/BV (x)	5.2	3.0	2.5	2.1	1.7
Dividend yield (%)	0.3	0.5	0.8	1.0	1.0
Per Share Data (Rs)					
EPS adjusted	23.03	35.42	48.52	57.68	64.24
EPS reported	23.03	35.42	48.52	57.68	64.24
BVPS	118.22	201.00	244.51	296.19	354.43
DPS	2.00	3.00	5.00	6.00	6.00
Profit & Loss (RsM)					
Net sales	7,242	8,713	10,449	12,364	13,595
Operating expenses	-6,816	-8,109	-9,528	-11,269	-12,382
EBIT	**425**	**605**	**921**	**1,096**	**1,213**
Net interest expense	-47	-100	-83	-75	-70
Non-operating/exceptionals	58	175	89	81	70
Pre-tax profit	**437**	**679**	**927**	**1,102**	**1,213**
Tax	-41	-71	-93	-110	-109
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	**396**	**609**	**834**	**991**	**1,104**
Adjusted earnings	396	609	834	991	1,104
Adjusted EBITDA	541	786	1,126	1,316	1,448
Growth Rates (%)					
Sales	1,751.8	20.3	19.9	18.3	10.0
EBIT adjusted	1,397.9	42.2	52.3	18.9	10.8
EBITDA adjusted	1,509.4	45.2	43.3	16.8	10.1
EPS adjusted	1,247.7	53.8	37.0	18.9	11.4
Cash Flow (RsM)					
Operating cash flow	**-1,321**	**-160**	**429**	**694**	**632**
Depreciation/amortization	116	181	205	220	235
Net working capital	-1,522	-917	-643	-517	-707
Investing cash flow	**-556**	**-1,457**	**-14**	**-558**	**-526**
Capital expenditure	-556	-867	-604	-558	-386
Acquisitions/disposals	0	-590	590	0	-140
Financing cash flow	**-728**	**869**	**251**	**-68**	**-105**
Borrowings	-700	-418	337	36	-2
Dividends paid	-28	-52	-86	-103	-103
Change in cash	**-2,605**	**-747**	**665**	**69**	**2**
Balance Sheet (RsM)					
Total assets	**4,135**	**6,304**	**6,512**	**7,408**	**8,400**
Cash & cash equivalent	204	70	47	55	61
Accounts receivable	577	562	679	866	952
Net fixed assets	916	1,602	2,001	2,339	2,490
Total liabilities	**2,472**	**2,850**	**2,309**	**2,317**	**2,308**
Accounts payable	246	209	233	276	304
Total Debt	1,905	2,190	1,830	1,803	1,810
Shareholders' funds	**1,662**	**3,455**	**4,203**	**5,091**	**6,092**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	7.5	9.0	10.8	10.6	10.7
ROE adjusted	44.2	23.8	21.8	21.3	19.7
ROIC adjusted	16.9	12.6	15.0	15.5	15.4
Net debt to equity	102.3	61.4	42.4	34.3	28.7
Total debt to capital	53.4	38.8	30.3	26.2	22.9

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

Powered by: dataCentral

Garmenting capacity (Million pcs pa)

Company	Capacity
Gokaldas Exports	26.0
Kitex Garments	18.2
Celebrity Fashion.	14.0
SPL Industries	13.2
Arvind Mills	12.7
Bombay Rayon Fash	12.0
Raymonds	6.1

Source: Citigroup Investment Research

Key Points

Large capacities the strength

Gokaldas Exports enjoys a significant lead over domestic peers with existing capacities of 26m pieces per annum. This in our view is a significant competitive advantage over other domestic garment companies, which are now ramping up capacities. This apart, the company's expertise in managing multiple orders and wide product range in value-added garments make it a preferred vendor to many fashion brands and retailers around the world - continuous customer additions reflects this. Given the growing order flows, management has further plans to ramp up capacities to 30mn pieces by Mar'07 and 36mn by FY08E.

Increasing focus on value addition

Gokaldas plans to further enrich its product mix to stay ahead of the competition. It plans to enter structured suits market for men and women, which fetch higher price realizations of c$40/piece (vs. current average of c$9/pc) and superior margins. The company is setting up a new facility in Bangalore, which is scheduled to commission by Dec'06. Additionally, it recently commissioned a state-of-the-art large Laundry in Bangalore for offering special washes on garments as a value-added service to customers – this will improve realizations further and give it an edge over peers. This apart, it is also exploring export opportunities in new products like 1) industrial work-wear, 2) innerwear and sleepwear products, and 3) garments made from technical textiles.

Expansions progressing at fast pace; commissioning in phases

The company's garment capacity expansions are on course. It has recently started operations at Chennai SEZ plant in Oct'06, production to ramp-up by 4Q. Expects to expand capacities by 30% at two plants in Bangalore, commission suits facility and new plant in Mysore by Apr'07– this will increase capacity by 15% yoy to 30mn pieces p.a. It has also increased the workforce by 15% YTD to 46,500 to service this capacity growth. In addition it has on the anvil additional garmenting units in Hyderabad and upcoming SEZ in Bangalore. The management has budgeted capex of Rs.1bn over the next 2 years, which will largely be funded by existing IPO funds (Rs.200mn) and internal accruals.

Gokaldas

Company description

Gokaldas Exports is India's largest apparel exporter in terms of revenue. Its annual capacity of 26m pieces gives it an advantage over other domestic companies, which are now starting to ramp-up capacity after quotas were dismantled on 1 Jan 2005. The company's wide product range (for men, women and children), design capabilities, focus on niche segments like outerwear (53% of FY06 revenues), and expertise in managing multiple orders make it a preferred vendor to many fashion brands and retailers around the world. Gokaldas offers integrated facilities; it manufactures the accessories it needs in-house, and offers value-added services like laundry, embroidery and printing. The company relies on exports, which account for 98% of sales. The Hinduja Group in Bangalore controls the company, with the major shareholders having a 75% stake.

Investment thesis

We reiterate our Buy/Medium Risk (1M) on Gokaldas Exports with target price of Rs.800 based on P/E of 15x Sept'07E, a significant premium to Citigroup's textile universe average of 10x P/E. We think it offers the best exposure to the garment outsourcing theme post quotas.

With Gokaldas' large capacity, good relationships with global brands and healthy order-book position; we believe the company is well positioned for growth. Its strategy to focus on outerwear (which offers margins of 10% compared with the garment industry average of 7-8%), enrich its wide product range and expand customer base should lead to a lower-risk business model. With new garment manufacturing capacity coming on-stream and new customers being added as the company enters new markets, we believe Gokaldas has strong growth potential.

The stock is trading at a P/E of 11.2x Sept'07E earnings, premium to domestic industry valuations 10x. We expect this premium to continue with global reforms favoring India post quotas (especially after US and EU re-imposed quotas on China as a safeguard measure). With expected healthy earnings CAGR of 22% over FY06-09, superior ROCEs vs. sector and stock likely to offer better liquidity given recent announcement of 1:2 split, we expect valuations to appreciate.

Valuation

Our target price of Rs800 is based on 15x P/E for Sept'07E earnings. We have lowered our target from the 16.5x we ascribe to leaders in the textile segments, to factor in lack of liquidity and low free float which affects re-rating. However, our target multiple still places the stock at a premium to our India textile universe valuations of 10x Sept'07E P/E. Our premium valuation is a function of Gokaldas' leadership in garment exports from India, largest garment capacities, rich product mix and preferred vendor status with a spectrum of global brands. In our opinion P/E captures the strong earnings growth potential and hence is our primary valuation tool.

The stock is trading at a P/E of 11.2x Sept'07E earnings, toward the lower end of the historical P/E band (10-15x). With global reforms favoring India, healthy earnings growth visibility and the company's superior capital efficiency, we see upside potential to current valuations.

Risk

We rate Gokaldas Medium Risk. This is different from the Speculative Risk rating assigned by our quantitative risk rating system (which measures the stock's volatility over a 260-day period) to stocks that have less than one year's trading history.

The key reasons for our assigning a Medium Risk rating include: 1) secular growth prospects for Indian garment manufacturers now that quotas have been removed; 2) we expect a strong medium-term growth trend given the global macro changes in the apparel industry; 3) the company is a leading garment exporter in India, it has good relationships with global brands, and large capacity; and 4) we rate many of the company's regional peers that are in our coverage universe Low Risk.

The main risks to our investment thesis and target price are:

- Client concentration – Gokaldas has a high dependence on its top-10 customers (which account for 80% of revenues currently). With GAP alone accounting for 43% of revenues, any slowdown in orders from the company would impact Gokaldas' growth prospects;
- Intensifying competition, which is resulting in increasing price pressure;
- Any appreciation of the Rupee vs. the USD could affect exports and thus earnings. A 5% appreciation of the Rupee could lead to a 7-8% fall in earnings, as exports accounted for 98% of FY05 revenues;
- Any labor unrest in the company's 46,500-strong workforce could adversely impact productivity. In addition, fixed wage rates that are not linked to productivity could adversely impact cost Gokaldas' cost competitiveness going forward; and
- More rapidly changing fashion trends could result in shorter delivery schedules and increases in freight costs.
- Closely held shareholding pattern, with promoters holding 75% stake could pose a risk

If any of these risk factors plays out, Gokaldas' share price is likely to have difficulty attaining our target price

Alok Industries (ALOK.BO)

Buy: Growth Visibility Improves

Buy/Medium Risk	1M
Price (16 Nov 06)	Rs68.45
Target price	Rs100.00
Expected share price return	46.1%
Expected dividend yield	2.2%
Expected total return	**48.3%**
Market Cap	Rs11,662M
	US$258M

Price Performance (RIC: ALOK.BO, BB: ALOK IN)

- Maintain Buy — We maintain Buy/Medium Risk on Alok with a target price of Rs100 based on 10x Sept'07E P/E on par with sector valuations. This is premised on expectation of rapid earnings CAGR of 38% over FY06-09E on back of higher operating leverage with most capex in apparel fabric and bed-linen now operational.
- Home textiles, key driver — We expect home textiles to be a key growth driver as additional capacities come on-stream and the healthy order book improves visibility. We estimate 30% of revenues from this segment in FY09E (vs. 21% today) with a CAGR of 37% from FY06-FY09E.
- Enriching product mix — 1) Tie-up with Teviz Textile Vizela SA, Portugal for manufacture of high-end yarn dyed flannel shirting fabric and 2) acquisition of a 60% stake in Mileta International, a Czech textile company in yarn dyeing shirting fabric are steps toward enriching Alok's product mix and improving profitability.
- Significant expansion operational — Most of phase II expansion is now operational and the balance will be commissioned by 2HFY07 (after initial delays). Phase III expansion of Rs.11bn will focus on backward integration - this will be funded through a mix of debt and internal accruals and be commissioned by March 2008.
- Other triggers — 1) Growing order book for exports, 2) higher operating leverage benefits as more expansion in garmenting, knits, made-ups go on-stream shortly and 3) attractive valuations of 7.3x Sept'07E P/E with rapid earnings growth offer upside re-rating potential.

Statistical Abstract

Year to 31-Mar	Net Profit (Rs)	FD EPS (Rs)	EPS Gr. (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	ROCE (%)
2005	797	5.8	-26%	11.8	1.5	9.1	6.7%
2006	1,016	5.1	-12%	13.4	1.7	10.0	5.1%
2007E	1,603	8.1	58%	8.5	1.4	8.0	6.9%
2008E	2,147	10.8	34%	6.3	1.2	6.6	7.3%
2009E	2,666	13.4	24%	5.1	1.0	5.5	8.4%

Source: Company Reports and CIR Estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	11.8	13.4	8.5	6.3	5.1
EV/EBITDA adjusted (x)	8.4	8.3	7.0	6.1	5.3
P/BV (x)	1.5	1.7	1.4	1.2	1.0
Dividend yield (%)	1.8	2.2	2.9	2.9	4.4
Per Share Data (Rs)					
EPS adjusted	5.80	5.10	8.05	10.78	13.39
EPS reported	5.80	5.10	8.05	10.78	13.39
BVPS	44.63	40.56	48.70	57.49	67.87
DPS	1.20	1.50	2.00	2.00	3.00
Profit & Loss (RsM)					
Net sales	12,293	14,207	19,083	24,553	28,804
Operating expenses	-10,485	-12,054	-15,993	-20,491	-23,843
EBIT	**1,808**	**2,154**	**3,091**	**4,062**	**4,961**
Net interest expense	-691	-668	-905	-1,050	-1,090
Non-operating/exceptionals	118	54	105	100	50
Pre-tax profit	**1,235**	**1,540**	**2,291**	**3,112**	**3,921**
Tax	-343	-448	-687	-965	-1,255
Extraord./Min.Int./Pref.div.	-96	-76	0	0	0
Reported net income	**797**	**1,016**	**1,603**	**2,147**	**2,666**
Adjusted earnings	797	1,016	1,603	2,147	2,666
Adjusted EBITDA	2,384	2,958	4,389	5,762	6,848
Growth Rates (%)					
Sales	15.7	15.6	34.3	28.7	17.3
EBIT adjusted	17.4	19.1	43.5	31.4	22.1
EBITDA adjusted	23.9	24.1	48.4	31.3	18.9
EPS adjusted	-26.2	-12.0	57.8	33.9	24.2
Cash Flow (RsM)					
Operating cash flow	**-63**	**2,090**	**1,996**	**2,381**	**2,921**
Depreciation/amortization	576	805	1,298	1,700	1,888
Net working capital	-1,531	193	-906	-1,466	-1,632
Investing cash flow	**-3,605**	**-11,062**	**-6,768**	**-5,251**	**-1,884**
Capital expenditure	-3,567	-10,743	-7,100	-5,250	-1,250
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	**7,063**	**9,043**	**151**	**4,987**	**-1,147**
Borrowings	5,005	8,256	720	5,385	-550
Dividends paid	-187	-299	-398	-398	-597
Change in cash	**3,395**	**71**	**-4,621**	**2,117**	**-110**
Balance Sheet (RsM)					
Total assets	**22,463**	**33,178**	**36,233**	**44,548**	**47,291**
Cash & cash equivalent	5,008	5,370	886	3,113	2,967
Accounts receivable	4,030	3,545	4,714	5,790	6,487
Net fixed assets	8,793	18,742	24,544	28,094	27,457
Total liabilities	**15,639**	**24,423**	**26,536**	**33,102**	**33,776**
Accounts payable	1,427	1,541	2,498	3,570	4,611
Total Debt	13,189	21,445	22,165	27,550	27,000
Shareholders' funds	**6,824**	**8,755**	**9,697**	**11,446**	**13,515**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	19.4	20.8	23.0	23.5	23.8
ROE adjusted	17.2	14.5	18.0	20.3	21.4
ROIC adjusted	10.7	8.2	8.2	8.8	9.7
Net debt to equity	119.9	183.6	219.4	213.5	177.8
Total debt to capital	65.9	71.0	69.6	70.6	66.6

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

Powered by: dataCentral

Key Points

Focus on enriching product mix

With superior technology machines for new expansion commissioned – Alok is now focusing on enriching its product mix. Company's 1) tie-up with Teviz Textile Vizela SA, Portugal for manufacture of high-end yarn dyed flannel shirting fabric and 2) acquisition of a 60% stake in Mileta International, a Czech textile company in yarn dyeing shirting fabric with annual revenue of €18m for €13.96 are steps toward this strategy. This will provide it with a) necessary technical and design support, b) high-end processing facilities in Czech with access to superior processing technology, and c) Mileta's existing brands portfolio - *Mileta, Erba, Cottonova, Lord Nelson, Wall Street, Osaka, Erbelle and licensee rights of Daks for handkerchiefs*.

We believe these initiatives are long-term positives - give Alok direct access to fashion brands like Marks & Spencer, Hugo Boss and Zara, current Mileta customers, a foothold in the fashion-conscious European market, and allow the company to leverage on low-cost facilities for becoming a sourcing base. We forecast apparel fabric realization growing at 3% CAGR over FY06-09E and expect this to contribute toward improved profitability.

Significant expansions operational, and more to go on-stream

Most of phase II expansion – primarily in apparel fabric and bed-linen are now operational. However, balance expansion of Phase II in knits, garment and made-up manufacturing are likely to get commissioned over the next six months in phases. While there have been some delays from its earlier schedule, improved visibility on timing (2HFY07E) of these capacities phasing in is positive. This should provide Alok with stronger growth opportunities and an increased presence at the higher end of the textile value chain – reducing dependence on apparel fabric (45% of FY06 revenues).

This apart, the company has further embarked on a Phase III expansion entailing Rs.11bn – primarily for backward integration to spinning and additional capacities in 1) weaving & processing in bed linen processing, 2) apparel weaving and 3) incremental capacities in garment and made-up manufacturing. As per management, this will be funded through a mix of debt (Rs.9bn) and internal accruals and would be operational by March '08. In our view, while it would result in savings in raw material costs and improve margins, this will continue to hinder improvement in ROCEs.

Capacity expansion Rollout Plan

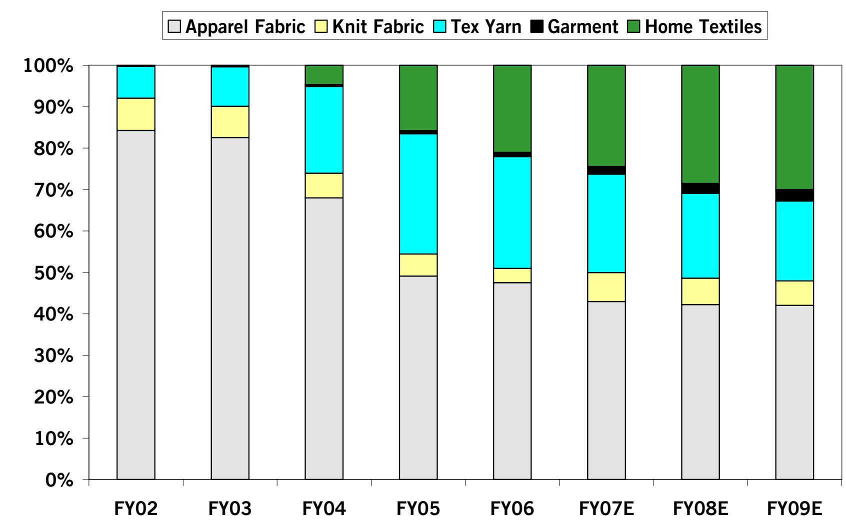
Segment	Existing	Phase II	Phase III	Total	Exp. Comm.
Texturizing Yarn (TPA)	86,000			86,000	
POY Plant		47,000		47,000	1QFY08
Weaving					
Fabric (mn mtrs)					
Apparel Fabric	57.5		25.0	82.5	Mar'08
Home Textiles	45.2		24.8	70	Mar'08
Knit (TPA)	6,400	10,400		16,800	2HFY07
Yarn (Ring Frame) TPA		51,000 spindles (5250 MT)	200,000 spindles (15000 MT)	250,000 spindles (20250 MT)	2HFY07, Mar'08
Processing					
Apparel Fabric (mn mtrs)	52.5	30		82.5	3QFY07
H.Textiles Fabric (mn mtrs.)	60		22.5	82.5	Mar'08
Knit Fabric (TPA)	3,000	13,800		16,800	3QFY07 in phases
Yarn Dyeing (TPA)	450	2,550		3,000	3QFY07 in phases
Bed Linen (mn sets)	2.5	3.5	4.0	10.0	2HFY07 in phases
Garments (mn pcs)	1	7	7	15	2HFY07 in phases
Terry Towels (TPA)	na	6,700		6,700	2H2007
Open Ended Yarn (TPA)	na	1,830		1,830	2H2007

Source: Company Reports and Citigroup Investment Research

Wide product range to de-risk revenue mix

Alok offers a wide product range across the textile value chain beginning from weaving, processing to finished garments. Its ability to offer a wide range of processed woven and knitted fabrics in 100% cotton, polyester, viscose and its blends with a range of finishes largely differentiates itself from peers. Its foray into home textiles has further expanded its product range. Given the growing thrust on vendor rationalization, we expect this wide product range to complement overall growth. Further efforts to enrich the product mix will contribute toward de-risking the company's revenue mix.

Alok's Changing Revenue Mix



Source: Citigroup Investment Research

Alok Industries

Company description

Alok has the largest textile processing capacity (60m meters) in India. Its manufacturing facilities, superior quality, wide product range in apparel fabrics (45% of FY06 revenues) and home textiles (22% of FY06 revenues) have made it a preferred vendor for global retailers such as Wal-Mart, JC Penny, GAP and garment exporters in India. It spans the textile value chain, with completely integrated facilities for yarn texturizing (27% of revenues), weaving, knitting, processing, made-ups and garments. Exports make up 27% of its revenues; but with the phasing out of quotas, the company's ramp-up in home textiles and its thrust on exports; we expect the share of exports to increase to 34% by FY09E. It is controlled and managed by the Jiwrajka family, with the major shareholders owning a 25% stake.

Investment thesis

We rate Alok a Buy/Medium Risk with a target price to Rs.100 based on 10x Sept'07.3E P/E on par with sector. Our thesis is premised on the solid growth opportunity in home textiles and Alok's major parts of expansion in weaving-processing capacities of bed linen and apparel fabric now operational. We see this providing the company with significant operating leveraging and earnings CAGR of 38% over FY06-09E.

Key growth drivers are 1) More expansions going on-stream over next two years 2) thrust on diversifying to a richer product mix and 3) growing order book for exports. Its presence across a significant part of the textile value chain and close ties with global retailers should help exploit the outsourcing opportunities in the sector and improve margins. However the company's aggressive capex plans will hinder improvement of ROCEs.

Valuation

Our 12-month target price of Rs100 is based on 10x Sept'07E P/E - on par with the sector. The stock is trading at 7.3x Sept'07E P/E toward the lower end of its historical P/E band of 8-10x of last two years and at a 22% discount to sector – we see this trend breaking out and expect valuations to catch up with the industry. Better earnings growth on back of recently commissioned capacities and management's assurance of no further equity dilutions are key reasons to this. Because P/E captures the earnings growth potential of a company, we consider it as our primary valuation method. In our view, already announced Rs.11bn expansions (Phase III) will remain a drag on ROCE.

Risk

We rate Alok Industries Medium Risk in view of most parts of phase II expansion now being operational and risks of further delay in commissioning of new capacities having reduced. However, risk of any equity dilutions and the prospect of the company reporting the lowest ROCE of 5% in the sector still remain. The main company specific risks include:

- Delay in commissioning of new capacity by a quarter would push back the growth we are projecting for FY07-08;
- significant increase in interest cost, would adversely impact earnings growth assumption – given its high leverage (debt/equity at 2.3x FY07E);

- Sharp increases in cotton prices by more than 10% from Rs.50/kg would impact profitability by 7-8%, on our estimates;
- appreciation of the rupee by more than 5% from the base level of Rs44 will reduce price realizations of exports, which contributed 27% of FY06 revenues but which are expected to increase sharply as new capacity goes on stream;
- Any over-priced acquisition of spinning facilities in its bid to backward integrate its home textiles business

Vardhaman Textiles Ltd (VART.BO)

Buy: Compelling Valuations

Buy/Low Risk	**1L**
Price (16 Nov 06)	Rs286.30
Target price	Rs350.00
from Rs405.00	
Expected share price return	22.2%
Expected dividend yield	1.7%
Expected total return	**24.0%**
Market Cap	Rs16,539M
	US$365M

Price Performance (RIC: VART.BO, BB: VTEX IN)

- Maintain Buy — The stock trades at compelling valuations of 8.1x Sept 07E P/E, a 20% discount to sector average of 10x. Given leadership in yarn, thrust on vertical integration and strong management team, we see valuations catching-up with industry ones. However, factoring its near-term muted growth, we lower our target price to Rs350 based on 10x Sept 07E P/E, which still offers ETR of 24%.

- Key growth drivers — 1) Large-scale vertical integration into fabrics as the company adds fabric manufacturing capacity; 2) Thrust on value addition and diversification to a richer product mix in yarn; and 3) sustained growth in sewing thread business with garmenting operations on the rise.

- Expansion progressing as scheduled — The company commissioned brown field expansion in fabric and spindles in 1H06. The green field integrated expansion at MP will start in phases by Mar'08. This involves capex of Rs20bn over next three years, funded by debt, FCCBs and internal accruals.

- Earnings growth to accelerate in FY07-09E — With existing plants operating at optimum capacity utilization and near-term margins under pressure, we see muted earnings growth of 9% for FY07E. However, we expect growth rates to accelerate, resulting in an earnings CAGR of 27% over FY07-09E as significant expansion projects are commissioned.

- Subsidiaries EPS accretive — The company's subsidiaries in yarns (VMT Spinning, 73% stake) and thread (Vardhaman Threads, 100% sub) are doing well and are likely to contribute 5-6% of incremental earnings, currently not factored into our estimates – this would make valuations even more compelling.

Statistical Abstract

Year to 31-Mar	Net Profit (Rs)	FD EPS (Rs)	EPS Gr. (%)	P/E (x)	P/BV (x)	EV/ EBITDA (x)	ROCE (%)
2005	1,208	20.9	100.7	13.7	2.1	7.2	12.2
2006	1,691	29.3	40.0	9.8	1.7	6.7	10.5
2007E	1,843	31.9	9.0	9.0	1.5	6.8	9.1
2008E	2,476	38.6	21.1	7.4	1.1	6.1	9.5
2009E	3,303	51.5	33.4	5.6	1.0	4.9	10.7

Source: Company Reports and CIR estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	13.7	9.8	9.0	7.4	5.6
EV/EBITDA adjusted (x)	7.4	6.8	6.9	5.9	4.7
P/BV (x)	1.4	1.7	1.5	1.1	1.0
Dividend yield (%)	1.6	1.4	1.7	1.7	2.1
Per Share Data (Rs)					
EPS adjusted	20.90	29.28	31.91	38.64	51.54
EPS reported	20.90	33.98	31.91	38.64	51.54
BVPS	207.81	166.47	193.38	249.63	295.17
DPS	4.50	4.00	5.00	5.00	6.00
Profit & Loss (RsM)					
Net sales	18,583	18,937	21,001	25,562	31,170
Operating expenses	-16,593	-16,475	-18,201	-21,740	-25,997
EBIT	**1,990**	**2,462**	**2,801**	**3,821**	**5,173**
Net interest expense	-584	-378	-590	-715	-650
Non-operating/exceptionals	191	150	215	195	195
Pre-tax profit	**1,597**	**2,234**	**2,426**	**3,301**	**4,718**
Tax	-389	-543	-582	-825	-1,416
Extraord./Min.Int./Pref.div.	0	272	0	0	0
Reported net income	**1,208**	**1,963**	**1,843**	**2,476**	**3,303**
Adjusted earnings	1,208	1,692	1,843	2,476	3,303
Adjusted EBITDA	2,960	3,476	3,896	5,311	6,823
Growth Rates (%)					
Sales	71.3	1.9	10.9	21.7	21.9
EBIT adjusted	77.6	23.8	13.7	36.4	35.4
EBITDA adjusted	75.4	17.4	12.1	36.3	28.5
EPS adjusted	100.7	40.1	9.0	21.1	33.4
Cash Flow (RsM)					
Operating cash flow	**205**	**2,378**	**1,873**	**1,265**	**3,526**
Depreciation/amortization	970	1,013	1,095	1,490	1,650
Net working capital	-1,972	-599	-1,065	-2,701	-1,427
Investing cash flow	**-4,700**	**-2,913**	**-8,190**	**-5,646**	**-1,205**
Capital expenditure	-4,700	-3,302	-6,430	-7,112	-1,369
Acquisitions/disposals	0	273	-1,964	1,388	320
Financing cash flow	**4,494**	**807**	**6,316**	**4,381**	**-2,320**
Borrowings	2,275	1,038	6,605	2,031	-1,936
Dividends paid	-260	-231	-289	-320	-384
Change in cash	**0**	**272**	**0**	**0**	**0**
Balance Sheet (RsM)					
Total assets	**17,923**	**23,517**	**30,128**	**36,282**	**36,647**
Cash & cash equivalent	227	2,715	1,368	608	243
Accounts receivable	2,084	2,220	2,310	3,067	3,429
Net fixed assets	8,087	10,376	15,710	21,333	21,052
Total liabilities	**9,920**	**13,901**	**18,957**	**20,286**	**17,733**
Accounts payable	412	491	513	405	487
Total Debt	7,496	11,022	16,280	17,550	15,250
Shareholders' funds	**8,003**	**9,617**	**11,171**	**15,996**	**18,914**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	15.9	18.4	18.5	20.8	21.9
ROE adjusted	18.6	19.2	17.7	18.2	18.9
ROIC adjusted	12.7	11.3	10.2	10.2	11.1
Net debt to equity	90.8	86.4	133.5	105.9	79.3
Total debt to capital	48.4	53.4	59.3	52.3	44.6

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

Powered by: dataCentral

Key Points

Expansion projects progressing as scheduled

With brown field expansion projects in fabric and yarn having been completed in phases by 1H06, Vardhaman is focusing on the greenfield integrated yarn and fabric plant in Madhya Pradesh scheduled for commissioning in phases by March 2008. This will cover yarn requirements for captive consumption and take advantage of increasing demand for high value added and good quality yarn. The entire expansion of around Rs20bn will likely be funded by a mixture of debt (80%, primarily TUF loans), US$60m FCCB raised in Feb 2006 (convertible at Rs423/share, our assumption to convert in FY08), and internal accruals. With new capacities expected to be phased in over the next few years, we expect healthy growth rates going forward.

Capex roll-out plan

Categories	Existing	Expansion	Total	Exp. Comm.
Yarn - Spindles	500,000	50,000	550,000	4QFY07
		50,000	600,000	1QFY08
		50,000	650,000	2QFY08
		50,000	700,000	3QFY08
		40,000	740,000	4QFY08
Fabric (mn mtrs)	45.0	25	70	1H2007
		25	95	Mar'08
Sewing Thread	8,500	1,000	9,500	Dec'06
		1,000	10,500	mid-2007

Source: Company Reports and Citigroup Investment Research estimates

Vardhaman Textiles Ltd

Company description

Vardhaman Textiles (erstwhile Mahavir Spinning Mills) is a leader in its sector, with 500,000 spindles offering the widest product range in cotton and blended yarn in India. It is the second-largest company with an 18% market share in sewing threads. The company has a vertically integrated business model, giving it a significant presence in fabrics (17% of FY06 revenues). It is also present in special and alloy steel hot rolled products and is a vendor to OEMs in the automotive and engineering space. Its superior quality and wide product range in higher-value- add products make it a preferred supplier to domestic and international manufacturers in textiles and apparels. Direct exports contribute 21% of revenues, excluding the sales to exporters. It is the flagship company of the SP Oswal Group, with the major shareholders owning a 62% stake.

Investment thesis

We maintain our Buy (1L) rating on Vardhaman Textiles with a reduced target price of Rs350, as we roll over to Sept 07E based on 10x P/E, still on par with sector valuations.

Vardhaman's large-scale expansion, focus on higher value addition and vertical integration into fabric will help de-risk its business model by reducing dependence on commodity yarn business. We expect large capacity expansions in fabric, growth in sewing thread and thrust on diversifying to richer product in yarn to drive growth. Improving outlook for its subsidiaries manufacturing different yarns and threads for the textile industry would complement overall growth by 5-6%. Expansion in yarn and fabric are part of a strategy to invest in capital-intensive projects taking advantage of TUF (Technology Upgradation Fund). We believe this will differentiate Vardhaman from other Indian companies and maintain focus on core segments in the textile value chain, like spinning and weaving.

The stock is currently trading at 8.1x Sept 07E P/E at 20% discount to sector average of 10x. With future expansion largely driven by fabric and new capacities going on-stream in phases and superior management quality, we see valuations catch-up with those of the industry.

Valuation

We are reducing our target price to Rs350 from Rs405 as we roll over to 10x Sept 07E P/E (12.7x FY07E earlier), on par with sector average. P/E is our primary valuation tool as we think it best captures earnings growth potential. While the company's efforts to move away from the commodity business of yarn and its vertical integration into fabric are positive, earnings growth will be back-ended as significant expansions are likely to get commissioned in phases only by FY08.

The stock is currently trading at compelling valuations of 8.1x Sept 07 P/E, a 20% discount to the industry, towards the mean of its two-year historical trading band (6-10x). With our forecasts of accelerating earnings growth over FY07-09E, the company's leadership in yarns and its strong management team, we see the stock's valuation catching-up with those of the industry in the near term.

Risk

We rate Vardhaman Textiles Low Risk based on our quantitative risk rating system, which measures the stock volatility over a 260-day period. The main company specific risks include:

- Any sharp increase in cotton prices of over 10-12% above Rs48/kg would impact our earnings estimates by 8-9% as cotton is a key raw material for Vardhaman's product range;
- Any fall of more than 2-3% in yarn price realizations, due to the commodity nature of business, would impact the profitability of the company's yarn business by 3-5%;
- Any delay in the commissioning of fabric capacities would further lower our forecasted revenue growth of 19% CAGR over FY06-08E; and
- Lower-than-the-expected 3% CAGR decline over FY05-08E in price realizations of steel alloy business would adversely impact the operating profitability of its steel alloy business (18% of total operating profits).

If any of these risk factors plays out, Vardhaman’s share price is likely to have difficulty attaining our target price.

Welspun India (WLSP.BO)

Hold: High Earnings Volatility

Hold/Medium Risk	2M
Price (16 Nov 06)	Rs91.85
Target price	Rs110.00
Expected share price return	19.8%
Expected dividend yield	0.0%
Expected total return	**19.8%**
Market Cap	Rs6,713M
	US$148M

Price Performance (RIC: WLSP.BO, BB: WLSI IN)

- **Maintain Hold/Medium Risk** — We rate Welspun Hold/Medium Risk (2M) with a target price of Rs110 based on 12x Sept'07E P/E. With production still ramping-up at newly commissioned plants, margin pressures and the adverse impact of forex fluctuations, we see high earnings volatility in the near-term; Medium Risk rating leaves moderate upside.

- **Margins under pressure** — EBITDA is under pressure despite strong revenue growth, due to: 1) higher RM costs and overheads on bed-linen with production still ramping up; 2) some price pressure on towels and 3) increased power costs. Initiatives to improve bed linen utilization and switch to gas for power are positive, but benefits should take a couple more quarters to reflect.

- **Bed linen, growth driver** — Favorable response from buyers and increasing order flows drive bed linen growth; however, utilization levels are still below breakeven. We see share of bed linen revenues increase to 39% by FY09E (vs. 9% in FY06); Terry towels witness steady volume growth with some price pressure.

- **Expansion progressing as scheduled** — Phase I expansion (Rs.5.7bn) is fully commissioned; the company is progressing on course with phase II (Rs.6.5bn), due by 4QFY07, which will step up capacity and backward integration – timely ramp-up of production at new plants will be the key to earnings growth.

- **Why not Sell?** — We see limited downside due to: a) earnings CAGR still strong at 34% for FY06-09E; b) vertical integrated model with scale and presence in branded home textile exports; c) bed-linen scale up to 60% utilization, encouraging; and d) stock trading at 9.8x Sept'07E earnings, at par with sector.

Statistical Snapshot

Year to 31-Mar	Net Profit (Rs)	FD EPS (Rs)	EPS Gr. (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	ROCE (%)
2005	337	5.6	-7%	16.4	1.7	12.7	6%
2006	440	5.7	3%	16.0	1.3	12.3	5%
2007E	618	8.1	40%	11.4	1.2	8.1	6%
2008E	815	10.6	32%	8.7	1.1	6.6	7%
2009E	1,068	13.9	31%	6.6	0.9	5.7	8%

Source: Company Reports and CIR Estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	16.4	16.0	11.4	8.7	6.6
EV/EBITDA adjusted (x)	10.6	10.9	7.2	5.9	5.2
P/BV (x)	1.7	1.3	1.2	1.1	0.9
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Per Share Data (Rs)					
EPS adjusted	5.58	5.74	8.05	10.61	13.90
EPS reported	5.58	4.97	8.05	10.61	13.90
BVPS	55.37	68.32	76.37	86.99	100.89
DPS	0.00	0.00	0.00	0.00	0.00
Profit & Loss (RsM)					
Net sales	4,763	6,537	8,839	10,889	12,520
Operating expenses	-4,072	-5,833	-7,556	-9,279	-10,524
EBIT	**692**	**705**	**1,283**	**1,610**	**1,996**
Net interest expense	-170	-246	-485	-525	-515
Non-operating/exceptionals	85	234	145	130	105
Pre-tax profit	**606**	**692**	**943**	**1,215**	**1,586**
Tax	-221	-217	-302	-389	-508
Extraord./Min.Int./Pref.div.	-48	-93	-23	-11	-11
Reported net income	**337**	**381**	**618**	**815**	**1,068**
Adjusted earnings	337	440	618	815	1,068
Adjusted EBITDA	969	1,191	1,978	2,500	2,921
Growth Rates (%)					
Sales	29.9	37.2	35.2	23.2	15.0
EBIT adjusted	28.0	1.9	82.1	25.5	24.0
EBITDA adjusted	40.9	22.9	66.1	26.4	16.9
EPS adjusted	-7.2	2.7	40.4	31.8	31.0
Cash Flow (RsM)					
Operating cash flow	**1,269**	**-565**	**2,640**	**1,576**	**465**
Depreciation/amortization	277	486	695	890	925
Net working capital	606	-1,466	1,304	-140	-1,538
Investing cash flow	**334**	**-942**	**-302**	**0**	**0**
Capital expenditure	0	0	0	0	0
Acquisitions/disposals	134	-805	826	0	0
Financing cash flow	**-1,645**	**-727**	**-1,284**	**-474**	**-368**
Borrowings	-3,490	-2,362	-1,284	-474	-368
Dividends paid	0	0	0	0	0
Change in cash	**-42**	**-2,234**	**1,054**	**1,102**	**97**
Balance Sheet (RsM)					
Total assets	**11,580**	**15,509**	**18,048**	**19,528**	**20,426**
Cash & cash equivalent	799	810	137	168	192
Accounts receivable	348	417	575	708	876
Net fixed assets	8,286	10,256	13,105	14,184	14,046
Total liabilities	**7,880**	**10,001**	**12,009**	**12,764**	**12,595**
Accounts payable	1,318	747	2,058	2,349	1,824
Total Debt	6,022	8,395	9,006	9,511	9,903
Shareholders' funds	**3,700**	**5,508**	**6,039**	**6,764**	**7,831**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	20.3	18.2	22.4	23.0	23.3
ROE adjusted	12.2	10.3	11.1	13.0	14.8
ROIC adjusted	7.2	4.4	7.2	8.1	9.1
Net debt to equity	141.2	137.7	146.9	138.1	124.0
Total debt to capital	61.9	60.4	59.9	58.4	55.8

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

Powered by: dataCentral

Welspun India

Company description

Welspun India is among Asia's largest terry towels manufacturer and the fourth largest in the world. A wide product range, fully integrated scaleable capacities and ability to offer value-added products make it a preferred supplier to global retailers in the EU and US. It already has a presence in retailing, having the license to market under Nautica, Umbra in the US and Tommy Hilfiger in India, and owns the Chirsty brand in UK, SPACES brand in India. The company's foray into bed-linen is a step to position itself as a single-point vendor in home textiles. Exports constitute 95% of revenues. Given company's vertically integrated business model in home textiles, most expansion now operational, we expect Welspun to deliver high growth. It is a flagship company of the Welspun Group (34% holding).

Investment thesis

We rate Welspun Hold/Medium Risk (2M) with a target price of Rs110. With most expansions phased in, initiatives to move up the value chain with a focus on branded home textiles and backward integration, we believe Welspun offers a strong business model for growth. The company's strategy to expand to bed linen and decorative bed sets would enrich product mix and improve profitability, in our view. However, with production at new expansions still ramping-up, initial high overheads in bed-linen, some price pressure on towels and adverse impact of forex fluctuations - we see high earnings volatility in the near-term. That said, with post revision earnings CAGR still strong at 34% for FY06-09E and stock trading at reasonable valuations of 9.8x Sept'07E P/E, at par with sector, downside appears limited – hence we rate the stock a Hold (2M).

Valuation

Our target price of Rs110 is based on 12x P/E for Sept 07E earnings. We believe Welspun will trade at a premium to Citigroup's textile universe (which include key players like Raymond, Arvind Mills, Gokaldas Exports, Alok Industries, Vardhman Textiles) valuations of 9.8x Sept 07E P/E. The premium is a function of Welspun's rapid earnings growth, leadership in terry towels and being a proxy for playing the outsourcing theme in home textiles, given its thrust on exports.P/E is our primary valuation tool as we see it as best capturing the company's strong earnings growth potential. With earnings CAGR of 34% over FY06-09E, global scale capacities in terry towels and a more dynamic business model, we see upside potential to stock valuations and trading closer to the median of its 3-year historical trading brand of 7.5-13x. We expect the stock to continue trading at a premium as growth plays out.

Risk

We rate Welspun Medium Risk, as opposed to the High Risk rating assigned by our quantitative risk-rating system. The key reasons we opt for a Medium Risk rating include: (1) Secular growth prospects in home textiles post quotas and shrinking capacities in the US; (2) Rapid growth on account of new capacity expansion; (3) Welspun's leadership position in India and its relationships with global brands; and (4) Peer stocks are rated Low or Medium Risk. The downside risks to our target price include: (1) Appreciation of the rupee; (2) Sharp increases in cotton prices; and (3) Delays in commissioning new projects. The upside risks to our target price include: 1) Faster than expected break even of the bed-linen business; and 2) Long-term sourcing tie-ups with global branded home textile retailers.

JCT (JCTL.BO)

Buy: Capex Delayed but Expect Strong EPS Growth

Buy/High Risk	**1H**
Price (16 Nov 06)	Rs7.49
Target price	Rs10.00
from Rs21.00	
Expected share price return	33.5%
Expected dividend yield	0.0%
Expected total return	**33.5%**
Market Cap	Rs2,574M
	US$57M

Price Performance (RIC: JCTL.BO, BB: JCT IN)

- **Retain Buy** — Delays in expansion and modernization of facilities are slowing the pace of a turnaround, deferring earnings growth to FY08-09E. We have therefore cut our target price, to Rs10, and estimates, but still forecast a robust EPS CAGR of 77% over FY06-09.

- **Capex delayed, but progress appears promising** — Initial hiccups in raising funds from FCCBs delayed capex of Rs3bn by 12 months. The company plans to modernize integrated textile facilities, enter polyester fabric exports and expand into nylon yarn. With the funds now in place, management hopes to complete these plans over the next 15 months — a positive, in our view.

- **Textile outlook remains strong** — Focus on a rich product mix in fabrics (51% of FY06 revenues), significant savings in power costs (15% of sales) and improved efficiencies should further improve profitability and expand overall margins. We forecast EBITDA margin to increase from 4.5% in FY06 to 16.0% by FY09.

- **Nylon yarn business under pressure** — Because of volatility in crude prices and stiff competition from polyester yarn, which is limiting pricing increase, profitability of nylon yarn (40% of FY06 revenues) is under pressure. JCT's efforts to backward integrate and cut power costs should provide some relief.

- **Potential price triggers** — (1) Accelerated turnaround; (2) timely execution of capex plans; and (3) benefits from a recent approval for carbon credit sales for a newly commissioned 5.5MW captive power plant — not yet in our estimates.

Statistical Abstract

Year to 31-Mar	Net Profit (Rs M)	FD EPS (Rs)	EPS Gr. (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	ROCE (%)
2005	21	0.1	NM	NM	2.0	8.8	5.8
2006	95	0.3	NM	27.0	1.9	9.6	6.4
2007E	121	0.4	27.3	21.2	1.7	10.1	6.3
2008E	438	1.0	185.2	7.4	1.0	6.1	10.5
2009E	672	1.5	53.6	4.8	0.8	4.6	13.2

Source: Company Reports and Citigroup Investment Research estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	122.3	27.0	21.2	7.4	4.8
EV/EBITDA adjusted (x)	12.3	20.4	10.8	5.9	4.4
P/BV (x)	1.9	1.8	1.7	1.0	0.8
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Per Share Data (Rs)					
EPS adjusted	0.06	0.28	0.35	1.01	1.55
EPS reported	0.06	0.28	0.35	1.01	1.55
BVPS	4.02	4.16	4.51	7.66	9.21
DPS	0.00	0.00	0.00	0.00	0.00
Profit & Loss (RsM)					
Net sales	6,042	5,262	5,451	6,947	7,617
Operating expenses	-5,962	-5,264	-5,196	-6,333	-6,786
EBIT	**80**	**-2**	**255**	**614**	**831**
Net interest expense	-243	-195	-225	-245	-275
Non-operating/exceptionals	187	308	105	120	195
Pre-tax profit	**24**	**111**	**135**	**489**	**751**
Tax	-3	-15	-14	-51	-79
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	**21**	**95**	**121**	**438**	**672**
Adjusted earnings	21	95	121	438	672
Adjusted EBITDA	397	237	500	964	1,216
Growth Rates (%)					
Sales	11.5	-12.9	3.6	27.4	9.6
EBIT adjusted	193.9	-102.6	12,328.3	140.4	35.4
EBITDA adjusted	78.6	-40.3	111.1	92.6	26.2
EPS adjusted	109.6	353.4	27.3	185.2	53.6
Cash Flow (RsM)					
Operating cash flow	**325**	**1,491**	**315**	**808**	**720**
Depreciation/amortization	317	239	245	350	385
Net working capital	-14	1,156	-52	20	-338
Investing cash flow	**-181**	**-1,791**	**-1,879**	**-1,094**	**-873**
Capital expenditure	-175	-1,467	-1,394	-1,619	-604
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	**0**	**0**	**0**	**1,340**	**0**
Borrowings	0	0	0	0	0
Dividends paid	0	0	0	0	0
Change in cash	**143**	**-300**	**-1,564**	**1,054**	**-154**
Balance Sheet (RsM)					
Total assets	**5,339**	**5,616**	**7,261**	**8,194**	**9,049**
Cash & cash equivalent	108	98	124	90	128
Accounts receivable	494	383	463	590	647
Net fixed assets	1,664	2,892	4,041	5,310	5,529
Total liabilities	**3,584**	**3,824**	**5,421**	**4,650**	**4,906**
Accounts payable	1,001	1,088	1,139	1,376	1,472
Total Debt	2,227	2,518	4,108	3,020	3,212
Shareholders' funds	**1,755**	**1,791**	**1,840**	**3,544**	**4,143**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	6.6	4.5	9.2	13.9	16.0
ROE adjusted	1.5	6.8	8.2	17.9	18.4
ROIC adjusted	2.1	-0.5	5.6	10.2	11.7
Net debt to equity	120.8	135.1	216.6	82.7	74.4
Total debt to capital	55.9	58.4	69.1	46.0	43.7

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

Powered by: dataCentral

Key Points

Capex delayed, but progress appears promising

Investment of Rs3bn planned in the next 15 months

Initial hiccups in raising funds from FCCBs (Rs1.34bn) have delayed the execution of JCT's capex of Rs3bn by 12 months. The funds are for modernization of the Phagwara textile plant, new capacity for nylon/polyester fabric, increased capacity in nylon filament yarn, and additional captive power plants. Given the US$30m recently raised through FCCBs (at 2.5% coupon and a conversion price of Rs14.8 per share) and debt under TUF (Rs1.6bn), management plans to progress with the planned expansion over the next 15 months. In our view, these new capacities will enable JCT to take advantage of the growth in textiles post-quotas.

Entry into nylon/polyester fabric — a growth area

JCT is creating a niche for itself

JCT plans to set up dedicated facilities in nylon/polyester fabric to supply global brands in outerwear and sportswear. With growing demand for outerwear and sportswear and no major players manufacturing high-quality nylon/polyester fabric in Sri Lanka, Bangladesh, Pakistan and India, we see JCT creating a niche for itself. It plans to leverage off its solid relationships with sportswear brands such as Nike. JCT plans to set up capacity of 28.8m meters, which is scheduled for commissioning by 4Q FY07 and should increase revenues by Rs1.1bn by FY09E.

Likely benefits from carbon credit sales

From early next year, JCT is likely to benefit from the recent approval for carbon credit sales for a newly commissioned 5.5MW captive power plant. According to management, this should yield incremental income of Rs20 per annum for the next six years. A similar carbon credit is expected for the company's 6MW captive power plant at Hoshiarpur, expected in 2H FY07. We have not factored any income from this in our estimates.

Nylon filament yarn earnings under pressure

The company's efforts to backward integrate into nylon chips and set up a 6MW captive power plant by 2H FY07 should provide some relief

With volatility in crude prices adversely impacting caprolactum prices (a key raw material for nylon yarn) and stiff competition from imports/polyester yarn, margins and profitability of nylon filament yarn (40% of FY06 revenues) are under pressure. Factoring in the increasing pressure on price realization and focus on volume growth, we expect nylon filament yarn revenues to grow by an 11% CAGR over FY06-09. The company's efforts to backward integrate into nylon chips and set up a 6MW captive power plant by 2H FY07 should provide some relief.

Estimates, target price reduced

We are reducing our revenue and net profit estimates for JCT to account for (1) delays in modernization of the company's textile facilities, (2) the adverse impact of high caprolactum prices on nylon yarn profitability, (3) a one-year delay in the expansion plan for the nylon fabric business; and (4) 18% equity dilution in FY08E due to the US$30m FCCBs (issue of 90.4m shares on conversion vs. our estimate of 76.3m shares) issued in April 2006.

We have cut our estimates due to significantly lower margins in FY06, driven by a sharper-than-expected decline in nylon filament margins, higher overheads because of disruption in production at a plant, stable fabric realizations (vs. our expectation of 9% growth) and an extra-ordinary loss of Rs10m due to the scheme of amalgamation of its subsidiaries. We had earlier factored in a revenue CAGR of 23% over FY06-08 on 9% growth in fabric prices over FY07-08, nylon filament yarn revenue growth of 27% for FY06 (vs. actual of 15%) and a 19% CAGR for FY07-08E. We are now assuming a textile revenue CAGR of 12% on 6% growth in fabric prices over FY06-08E and lower nylon filament yarn revenue growth of 11% for FY06-08.

Based on our new assumptions and management plans to complete capex over the next 15 months, we expect revenue and earnings CAGRs of 15% and 91% respectively over FY06-08. With the company's thrust on higher value-add fabric and increased visibility on expansion, we expect earnings to grow 54% in FY09.

Because of the recent fall in the stock price to levels much below the conversion price (Rs14.8/share) for the outstanding US$30m FCCBs, we believe the FCCBs are unlikely to be converted in the near term. We have reduced our equity capital forecast and increased our debt estimates accordingly.

Earnings Revision (Rupees in Millions, Percent)

Year to	FY07E			FY08E		
31-Mar	New	Old	% Chg	New	Old	% Chg
Revenue	5,451	7,706	-29	6,947	9,155	-24
Net Profit	121	663	-82	438	934	-53
EPS	0.4	1.6	-78	1.0	2.2	-54

Source: Citigroup Investment Research estimates

JCT

Company description

JCT enjoys a strong presence in the cotton and blended fabrics segments. It is a leader in textile-grade nylon filament yarn in India. Its integrated facilities — from yarn to finished fabric — give the company the flexibility to offer superior quality and a wide product range to customers. It is a vendor to global brands such as Nike, Esprit, Columbia Sports, Zara, Wal-Mart, and an established supplier to the defense forces in India. It is a preferred vendor of cotton trouser fabrics to exporters. It is the flagship company of the Thapar Group in textiles, with the major shareholders owning a 52% stake. JCT has three plants in Northern India.

Investment thesis

We maintain our Buy/High Risk (1H) rating. We believe the key growth drivers for JCT are in place. It is modernizing its weaving and processing facilities and is focusing on value-added fabric for garment exports. The company's strategy to focus on niche businesses, such as nylon/polyester fabric for sportswear, and leverage on its solid relationship with Nike, should in our view reduce risks. Further, JCT should benefit from carbon credit sales (not factored into our estimates). The stock has sharply underperformed over the past six months, likely discounting the delay in the company’s expansion plans. It currently trades at a 13% discount to the sector.

Valuation

Our target price of Rs10 is based on 10x FY08E P/E, a 10% premium to our sector valuation of 9x in recognition of the company's diversification to value-added products and an earnings CAGR of 77% over FY06-09E. Because JCT has now restructured and has turned around with healthy profitability, we believe P/E is a good tool to value the company.

Risk

We rate JCT as High Risk based on our quantitative risk-rating system, which tracks 260-day volatility. The main downside risks to our target price include:

- Further delay in modernization and commissioning of new capacities would lower our assumption of 6% CAGR growth in price realizations and impact profitability.
- Sharp increases in cotton prices of over 10-12% from Rs45/kg and caprolactum over Rs115/kg would impact our margin expansion and overall earnings growth assumptions.
- One-time retirement costs to reduce the work force.

Labor strikes at any plant could adversely impact our growth assumptions.

S Kumars Nationwide (SKMK.BO)

Sell: Rich Valuations

Sell/High Risk	3H
Price (16 Nov 06)	Rs78.60
Target price	Rs67.00
from Rs61.00	
Expected share price return	-14.8%
Expected dividend yield	0.0%
Expected total return	**-14.8%**
Market Cap	Rs12,467M
	US$275M

Price Performance (RIC: SKMK.BO, BB: SKUM IN)

- **Retain Sell/High Risk** — We maintain our Sell/High Risk (3H) rating on S Kumars with an increased target price of Rs.67 based on 11x FY08E P/E. Although the growth outlook for the company appears robust, at valuations of 13x FY08E P/E, a 44% premium to the sector appears excessive, and we believe most of the growth is priced in.

- **Margins likely to stagnate** — While a richer product mix coupled with lower raw material consumption expand margins to 19.6% in FY07E, 320bps gain over FY06 is lower than 830bps growth in FY06. We believe margins will stagnate ahead due to higher overheads on aggressive rollouts of stores and expansions.

- **Retail execution, the key** — We like the company's strategy of transforming from a commodity textile player to a branded retailer in garments and home textiles; however, execution is key. With competition intensifying in retail, a timely rollout of 129 stores by Mar'07 and 420 more stores by 2010 vs. 29 stores today is crucial.

- **Growth outlook strong, but priced in** — We expect earnings CAGR of 42% in FY06-09, largely frontloaded, but current high valuations price in this growth. Further, the company's plans to raise additional $90mn for its aggressive expansion/acquisition plans, would result in c24% equity dilution and make near-term valuation richer.

- **Remains most expensive** — S Kumars is the most expensive stock in our textile universe on P/E, EV/EBITDA and P/BV for FY08. We believe this is unwarranted because commoditized textiles still dominate revenues (67% of FY06 sales), it has a high dependence on outsourcing (a lower P/E business) and branded retailing has still to make any meaningful contribution to profitability.

Statistical Abstract

Year to 31-Mar	Net Profit (Rs)	FD EPS (Rs)	EPS Gr. (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	ROCE (%)
2005 (6m)	91	0.59	(144.5)	133.2	(34.2)	77.6	0.82
2006	421	2.59	338.6	30.4	4.7	16.8	5.92
2007E	908	4.19	61.8	18.8	2.5	12.2	9.42
2008E	1,321	6.09	45.4	12.9	2.1	10.6	10.81
2009E	1,596	7.36	20.8	10.7	1.7	9.2	11.67

Source: Company Reports and CIR Estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	na	30.4	18.8	12.9	10.7
EV/EBITDA adjusted (x)	na	na	11.3	9.0	7.7
P/BV (x)	na	19.9	3.5	2.8	2.2
Dividend yield (%)	na	0.0	0.0	0.0	0.0
Per Share Data (Rs)					
EPS adjusted	na	2.59	4.19	6.09	7.36
EPS reported	na	2.59	4.19	6.09	7.36
BVPS	na	3.95	22.15	28.24	35.59
DPS	na	0.00	0.00	0.00	0.00
Profit & Loss (RsM)					
Net sales	na	8,895	11,142	13,269	15,204
Operating expenses	na	-7,955	-9,523	-11,295	-12,935
EBIT	**na**	**940**	**1,619**	**1,974**	**2,269**
Net interest expense	na	-451	-580	-505	-486
Non-operating/exceptionals	na	61	35	45	40
Pre-tax profit	**na**	**550**	**1,074**	**1,514**	**1,823**
Tax	na	-102	-140	-167	-200
Extraord./Min.Int./Pref.div.	na	-26	-26	-26	-26
Reported net income	**na**	**421**	**908**	**1,321**	**1,596**
Adjusted earnings	na	421	908	1,321	1,596
Adjusted EBITDA	na	1,462	2,179	2,584	2,941
Growth Rates (%)					
Sales	na	na	25.3	19.1	14.6
EBIT adjusted	na	na	72.4	21.9	14.9
EBITDA adjusted	na	na	49.0	18.6	13.8
EPS adjusted	na	na	61.8	45.4	20.8
Cash Flow (RsM)					
Operating cash flow	**na**	**-440**	**26**	**1,666**	**1,205**
Depreciation/amortization	na	523	560	610	673
Net working capital	na	-1,411	-1,469	-292	-1,090
Investing cash flow	**na**	**318**	**-1,245**	**-924**	**-1,061**
Capital expenditure	na	-232	-1,245	-924	-1,061
Acquisitions/disposals	na	0	0	0	0
Financing cash flow	**na**	**93**	**5,091**	**740**	**114**
Borrowings	na	-28	1,923	728	116
Dividends paid	na	0	0	0	0
Change in cash	**na**	**-30**	**3,872**	**1,482**	**258**
Balance Sheet (RsM)					
Total assets	**na**	**15,109**	**17,676**	**18,735**	**20,496**
Cash & cash equivalent	na	177	179	107	123
Accounts receivable	na	4,908	5,905	6,369	7,298
Net fixed assets	na	3,828	4,513	4,826	5,215
Total liabilities	**na**	**12,954**	**11,359**	**11,097**	**11,262**
Accounts payable	na	1,000	1,434	1,923	2,207
Total Debt	na	11,721	9,800	9,000	8,900
Shareholders' funds	**na**	**2,156**	**6,317**	**7,638**	**9,234**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	na	16.4	19.6	19.5	19.3
ROE adjusted	na	na	33.3	24.2	23.0
ROIC adjusted	na	na	10.0	11.2	12.0
Net debt to equity	na	535.5	152.3	116.4	95.1
Total debt to capital	na	84.5	60.8	54.1	49.1

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

Powered by: dataCentral

Key Points

Retail scale-up, remains a challenge

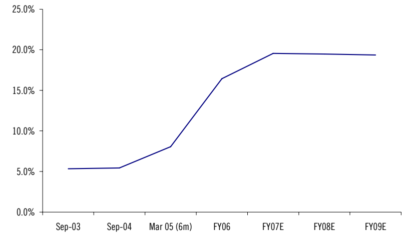
S Kumars plans to scale up its presence in retailing of branded apparels and home-textile products. Management has aggressive plans to expand its brand portfolio and widen the existing network of exclusive brand outlets. The company established a 100% subsidiary, Brandhouse Retails, to focus on managing exclusive brand outlets for the company's own brands and tie-up with international brands for marketing its products in India. It recently entered into agreement with international luxury brands 'Escada' (women's wear and accessories), 'Dunhill' (men's wear and accessories) and Stephen Brothers (for high-end shirts) marketing their products in India.

Aggressive plans to add 107 stores by Mar'07 and to have 552 stores by 2010-11 – timely execution the key

Having already established its presence in the premium segment through Reid & Taylor, the company is targeting the mid-premium segment. It launched 'Carmichael House' in home textile products and recently launched a new brand 'Belmont' targeting the mid-price garments and fabric customers. Company now has 29 exclusive brand outlets (vs.16 stores as on Mar'06) and plans to add 100 new exclusive brand outlets by Mar'07 and targets to have 552 stores and 20 brands by 2010-11. With competition intensifying in the branded retailing space from domestic and international brands, timely execution of this strategy will be key. With peers in branded retailing scaling up, new international brands queuing up to enter India and real-estate prices spiraling, risk of delays in rolling out new stores is high, in our view. While we see this retail build-out as a positive and forecast the share of retailing revenues will increase from 2% of FY06 sales to 12% by FY09E, we believe the gestation period for this business to contribute meaningfully to profitability is long. Higher overheads following aggressive expansion of new stores and increased brand promotion expenses are likely to restrict margin growth

EBITDA margin likely to stagnate

S Kumars's EBITDA Margin



Source: Citigroup Investment Research

Richer product mix in consumer textiles and worsted fabric coupled with lower raw material consumption will expand margins to 19.6% in FY07, 320bps gain over FY06; however, this will be lower than 830bps growth in FY06 - we believe room for margin growth is limited ahead. We expect margins to stagnate at 19%, due to 1) higher overheads on an aggressive rollout of retail stores for branded apparels/home textiles, 2) increased brand promotion expenses, and 3) upside to EBITDA margin capped by the commodity nature of the consumer textile business in uniform wear/work wear, with c80% being outsourced.

More equity capital being raised

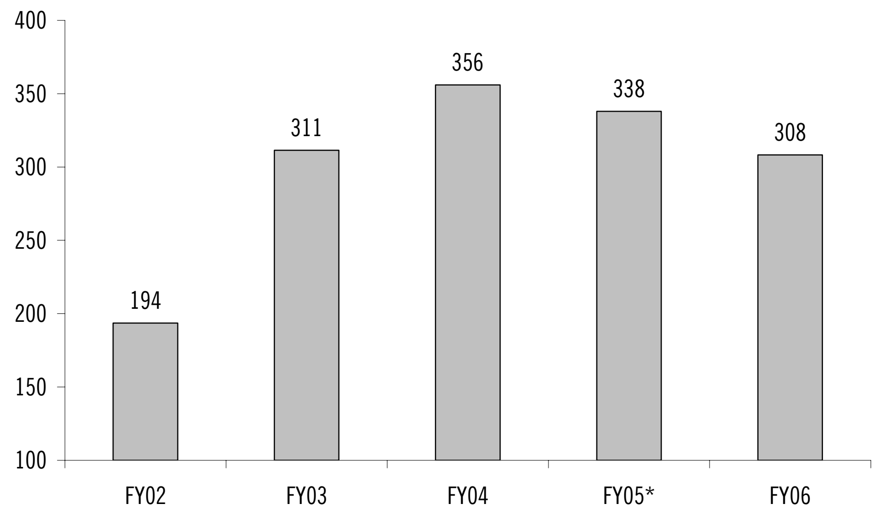
The company is raising further equity capital of $90m for funding its aggressive expansions/acquisitions plans in existing businesses. The management has recently approved to issue equity shares/fully convertible debentures/capital to institutional investors ($65mn) and promoters ($25mn) at Rs.80 per share. This would result in approximately 24% equity dilution over and above its fully diluted equity of 216.90mn (factoring in earlier dilutions for $50mn FCCB and promoter loans) - we believe this will lower near-term EPS growth.

High working capital intensity

S Kumars traditionally has had a long working capital of 300-plus days due to its commodity consumer textile business. This has reduced from a peak of 356 days in FY04 to 308 days in FY06, but still significantly higher than the textile industry average of 125-150 days. With capex plans on the anvil and a working capital cycle of 300-plus days despite the high dependence on outsourcing

(61% of FY06 sales), we could see increased pressures on cash flows going forward.

S Kumars' Working Capital Cycle (No. of Days)



Source: Citigroup Investment Research; PN: FY05*- Adj. for 6m financial year

S Kumars Nationwide

Company description

S Kumars Nationwide is a leader in uniform fabrics with a 30% market share of the organized sector and is the largest institutional supplier of uniforms. The S Kumars brand is popular in the domestic blended fabric market for suitings, daily wear and work wear. It is the second largest in India in worsted fabric (c.15% market share) given its tie-up with Reid & Taylor, Scotland to manufacture and market worsted fabric under the Reid & Taylor brand in India. S Kumars also has a presence in home-textiles and branded garments, which it is looking to scale up. Its integrated plants, along with a strategy to outsource, have established its presence in the domestic market. Exports make only a small contribution of 2% to revenues. It is the flagship company of the S Kumar Group (a 52% stake) with three plants.

Investment thesis

We rate S Kumars a Sell/High Risk (3H), with an increased target price of Rs67 based on 11x FY08E P/E, at a 25% premium to sector valuations of 9x. Although the growth outlook for the company appears robust, at valuations of 13x FY08E P/E- 44% premium to sector, appear excessive. We believe most of the growth is priced in. The company's efforts to transform itself from being a commodity textile player to a retailer in branded textiles are positive, in our view. However, with competition intensifying in the branded retailing space from domestic and international brands, we believe (1) timely execution of new store rollouts will be key, and (2) the gestation period for the retailing business to contribute meaningfully to profitability will be long. That said, given management's aggressive plans to add 100 new exclusive brand outlets (vs.29 today) by March 2007 and to have 552 stores and 20 brands by 2010-11, we expect higher overheads on new-store rollouts and increased brand promotion expenses will restrict margin growth.

The stock is trading at 13x FY08E P/E, a large premium to our India textile universe valuation. This is the most expensive stock in our universe on P/E, EV/Sales, EV/EBITDA and P/BV. We believe this is unjustified for the following reasons: 1) commoditized consumer textile still dominates revenues; 2) high dependence on outsourcing (61% of FY06 sales), which is a lower P/E business; 3) branded retailing has still to contribute meaningfully to profitability; and 4) risk of long working capital cycles. Further, plans to raise additional equity capital of $90mn would result in c24% equity dilution and make near-term valuations even richer.

Valuation

Our increased target price of Rs67 is based on 11x FY08E P/E, our primary valuation method. Our target multiple still places the stock at a 25% premium to our India textile universe's FY08E valuation of 9x (that was earlier 8x FY08E PE), factoring in S Kumars growth potential and focus on the retail business. The stock is trading at a 15% premium to industry leader Raymond. Because S Kumars is highly dependent on outsourcing (61% of sales) — a low P/E business — and the company's branded retailing business has still to make any meaningful contribution to profitability, we believe the current valuations are stretched. Plans to raise additional equity capital of $90mn would dilute equity by approximately 24%, making near-term valuations more expensive.

Risk

We rate S Kumars as High Risk based on our quantitative risk-rating system, which tracks 260-day historical share price volatility. Other factors that support our High Risk rating are:

- The company's commodity consumer textiles business still dominates with 67% of revenues and 46% of operating profit for FY06.
- Low capital efficiency and high working capital cycle of 300-plus days.
- Given the intensifying competition in Indian retailing market, risk of delay in rolling out management's aggressive retailing plans appears high.
- Outstanding arrears in preference dividend of Rs237m as on FY06 becoming payable over 2009-2014 would dilute cash flows going forward.
- Increase of corporate guarantee given to other group projects to the tune of Rs5.5bn. If this be exercised it would impact cash flows of S Kumars' core business.

The upside risks to our target price include:

- Any long-term outsourcing arrangement with Reid & Taylor, Scotland for supply of worsted fabrics and garments from its upcoming capacity would be positive and provide a stronger growth outlook than our estimates.
- Any equity stake sale in Brandhouse Retail (100% retailing venture) in the near term would improve valuations for the retailing business. Any large outsourcing arrangement for home textiles exports.

Abhishek (ABHP.BO)

Sell: Upside Priced In

Sell/Medium Risk	3M
Price (16 Nov 06)	Rs23.55
Target price	Rs23.00
from Rs22.50	
Expected share price return	-2.3%
Expected dividend yield	4.2%
Expected total return	**1.9%**
Market Cap	Rs4,573M
	US$101M

Price Performance (RIC: ABHP.BO, BB: ABIN IN)

- Retain Sell/Medium Risk — We rate Abhishek as Sell/Medium Risk (3M) with a new target price of Rs23 based on 8.5x Sept'07E P/E. With muted earnings growth and no major earnings surprises forecasted, we believe all the potential upside is priced in.

- Pricing pressures dampen terry towel growth— While outsourcing opportunities for terry towels remains strong, increasing price pressures dampen growth rates. We see healthy volume growth of 15% CAGR, but 4% CAGR decline in prices would lower Abhishek's towel revenue growth to 10% CAGR over FY06-09E.

- Large capex still on anvil — While much of the textile expansion in terry towels and yarns is now complete, Abhishek still has significant capex of Rs10bn over FY06-09E on the anvil: 1) two 20MW captive power plants, 2) paper (Rs6.8bn) and 3) incremental expansion in terry towels and yarn (Rs2.1bn).

- We forecast earnings CAGR of 1% over FY06-09E — Revenues will grow at 15% CAGR and EBITDA at 20% CAGR, but we forecast earnings CAGR of 1% over FY06-09 due to higher depreciation and interest costs post expansion with 9% equity dilution on equity warrants outstanding (conversion at Rs33 per share).

- Upsides priced in — With the stock trading at 8.6x FY07E P/E, toward the mean of the two-year historical P/E band (7.5 -11x), we believe potential upside is priced in. Muted earnings growth and large-scale paper expansion will hinder price performance and re-rating, in our view.

Statistical Abstract

Year to 31-Mar	Net Profit (Rs)	FD EPS (Rs)	EPS Gr. (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	ROCE (%)
15m ended Mar 05	426	2.19	18.8	10.7	1.5	6.4	8.8
2006	568	2.93	33.4	8.0	1.3	7.3	7.9
2007E	513	2.64	(9.7)	8.9	1.2	6.8	6.9
2008E	555	2.86	8.3	8.2	1.1	6.8	7.3
2009E	644	3.01	5.2	7.8	1.0	5.9	6.6

Source: Company Reports and CIR Estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	na	8.0	8.9	8.2	7.8
EV/EBITDA adjusted (x)	na	na	6.2	6.1	5.9
P/BV (x)	na	1.3	1.2	1.1	1.0
Dividend yield (%)	na	4.2	4.2	4.2	4.2
Per Share Data (Rs)					
EPS adjusted	na	2.93	2.64	2.86	3.01
EPS reported	na	2.93	2.64	2.86	3.01
BVPS	na	18.46	20.10	21.96	24.69
DPS	na	1.00	1.00	1.00	1.00
Profit & Loss (RsM)					
Net sales	na	7,436	8,954	10,097	11,212
Operating expenses	na	-6,553	-7,911	-8,752	-9,714
EBIT	**na**	**883**	**1,043**	**1,345**	**1,497**
Net interest expense	na	-254	-420	-680	-650
Non-operating/exceptionals	na	91	70	85	60
Pre-tax profit	**na**	**720**	**693**	**750**	**907**
Tax	na	-152	-180	-195	-263
Extraord./Min.Int./Pref.div.	na	0	0	0	0
Reported net income	**na**	**568**	**513**	**555**	**644**
Adjusted earnings	na	568	513	555	644
Adjusted EBITDA	na	1,497	1,838	2,295	2,597
Growth Rates (%)					
Sales	na	na	20.4	12.8	11.0
EBIT adjusted	na	na	18.1	29.0	11.3
EBITDA adjusted	na	na	22.8	24.9	13.2
EPS adjusted	na	na	-9.7	8.3	5.2
Cash Flow (RsM)					
Operating cash flow	**na**	**940**	**1,127**	**1,190**	**1,530**
Depreciation/amortization	na	614	795	950	1,100
Net working capital	na	-242	-181	-316	-215
Investing cash flow	**na**	**-2,844**	**-2,529**	**-4,173**	**-1,642**
Capital expenditure	na	-2,620	-2,966	-4,255	-1,725
Acquisitions/disposals	na	-247	348	0	0
Financing cash flow	**na**	**-2,161**	**-1,790**	**-3,371**	**-542**
Borrowings	na	-2,032	-1,596	-3,177	-328
Dividends paid	na	-194	-194	-194	-214
Change in cash	**na**	**-4,065**	**-3,193**	**-6,355**	**-655**
Balance Sheet (RsM)					
Total assets	**na**	**11,822**	**13,678**	**17,373**	**18,290**
Cash & cash equivalent	na	486	142	195	129
Accounts receivable	na	360	448	505	561
Net fixed assets	na	7,676	9,847	13,152	13,777
Total liabilities	**na**	**8,237**	**9,774**	**13,108**	**13,002**
Accounts payable	na	457	569	702	862
Total Debt	na	6,895	8,150	11,250	11,000
Shareholders' funds	**na**	**3,585**	**3,904**	**4,265**	**5,288**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	na	20.1	20.5	22.7	23.2
ROE adjusted	na	na	13.7	13.6	13.5
ROIC adjusted	na	na	7.7	8.1	7.5
Net debt to equity	na	178.8	205.1	259.2	205.6
Total debt to capital	na	65.8	67.6	72.5	67.5

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

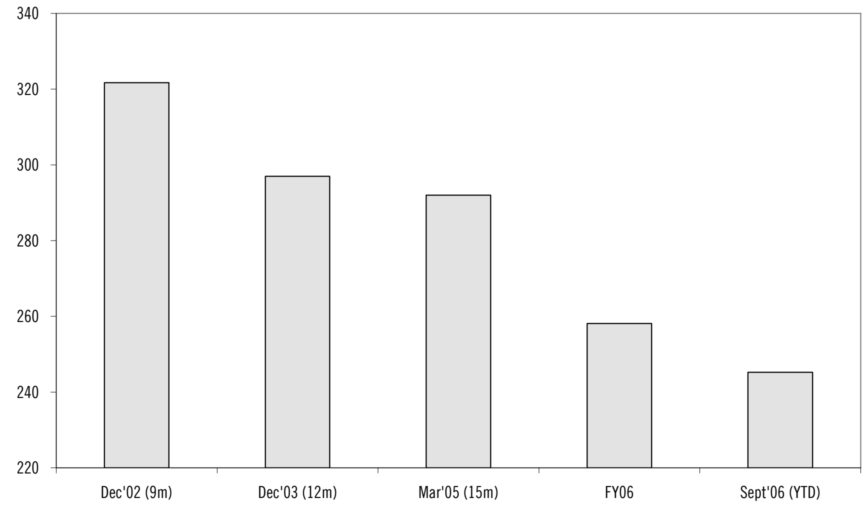
Powered by: dataCentral

Key Points

Pricing pressures to dampen terry towel growth

India's terry towel exports to the US continue to rise on the back of increasing outsourcing opportunities with quotas re-imposed on China. Export volumes grew a rapid 52% YTD in Aug'06; however, increased pricing pressures have dampened revenue growth to 40% YTD in Aug'06. We see a similar trend for Abhishek: we estimate healthy volume growth of 15% CAGR; however, we expect a 4% CAGR decline in prices to lower the company's towel revenue CAGR to 10% over FY06-09. Although Indian companies are focusing on providing innovative products in terry towels to achieve higher realization, competitive pressures remain an overhang on price realizations.

Abhishek's Terry Towel price realizations (Rs.Kg)



Source: Citigroup Investment Research

Large capex still on anvil, primarily for Paper

With most of the textile expansions in terry towels and yarns now operational, it is aggressively working toward ramping capacities and paper. It has on its anvil a capital expenditure of Rs10bn over next 2-3 years, which includes Rs.1.4bn for two 20MW captive power plants (to commission in 3QFY07 and Sept'07, respectively), Rs.6.8bn for paper and further investment of Rs.2.1bn for incremental expansion in terry towels and yarns.

Muted earnings CAGR of 1% expected

With terry towel exports on the rise, expansions in yarn complete and growth in paper post new expansion, we forecast revenue CAGR of 15% over FY06-09E; EBITDA growth will likely be higher at 20% given the benefits accruing from economies of scale and savings in power costs. However, higher interest and depreciation costs on new expansions and 9% equity dilution due to equity warrants issued and outstanding (conversion at Rs.33 per share) and likely to convert in FY09E; we see muted earnings CAGR of 1% over FY06-08E.

Abhishek

Company description

Abhishek is among the largest integrated terry towel manufacturers (54% of FY06 revenues) in India with a capacity of 29,000 MT. It also has a presence in value-added cotton yarn (28% of FY06 revenues). Abhishek is a significant player in agro-based paper (18% of FY06 revenues), focusing on the cream wove segment. Its wide product range and integrated facilities in terry towels make it a preferred vendor to global retailing giants such as Wal-Mart. Exports constituted 56% of FY06 revenues, largely driven by terry towels. With the new capacities in terry towels now phased in, we expect the share of exports to increase. Abhishek is a flagship company of the Trident Group, with the major shareholders having a 64% stake. The company has two plants, both close to the raw-material sourcing region of Punjab.

Investment thesis

We rate Abhishek as Sell/Medium Risk (3M) with a target price of Rs23 based on 8.5x Sept'07E P/E. With muted earnings growth and no major earnings surprises forecasted, we believe all the potential upside is priced in. Given Abhishek's scale advantages and relationships with global retailers, it looks well positioned to take advantage of outsourcing opportunity in terry towels. However, slower-than-expected growth in towels and declining profitability of its paper and chemical business are emerging growth concerns. Further, the company's aggressive expansion into the paper business (33% of FY06 operating profits), which is a commodity business, and a muted earnings CAGR of 1% over FY06-09E, are likely to hinder price performance and re-rating.

Valuation

Our increased target price of Rs23 (up from Rs.22.5 earlier) is based on 8.5x Sept'07E earnings (as against Mar'07E earlier) — a 30% discount (lower than 45% assumed earlier) to our target multiple of 12x for Welspun, which has a wider presence in home textiles. The discount is lowered, on recent reduction in target multiple for Welspun, to factor in the earnings volatility and some price pressure on terry towels. However, we still consider Welspun to command a reasonable premium given its product mix focus on higher- value products in home textiles and the absence of paper. We use P/E as our primary valuation tool, as we believe it captures the company's growth potential.

Risk

We rate Abhishek Industries as Medium Risk based on our quantitative risk-rating systems, which tracks 260-day historical share price volatility.

The main upside risks to our target price include:

- De-merger plans to split the business into separate textile and paper companies would result in value un-locking and re-rating;
- Increase in paper prices of 10% above a price of Rs32,500/MT would complement earnings growth and downplay the impact on valuations.
- Any depreciation of the rupee vs. the USD could affect exports and thus earnings. A 5% depreciation of the rupee could lead to a 3-4% rise in earnings, as exports accounted for 56% of FY06 revenues.

Welspun (WLSP.BO - Rs91.85; 2M)

Valuation

Our target price of Rs110 is based on 12x P/E for Sept 07E earnings – we have lowered our earlier target multiple of 15.5x, to factor in the earnings volatility and liquidity concerns that hinder stock performance. However, we still believe Welspun will trade at a premium to Citigroup's textile universe (which include key players like Raymond, Arvind Mills, Gokaldas Exports, Alok Industries, Vardhman Textiles) valuations of 10x Sept 07E P/E. The premium is a function of Welspun's rapid earnings growth, leadership in terry towels and being a proxy for playing the outsourcing theme in home textiles, given its thrust on exports. P/E is our primary valuation tool as we see it as best capturing the company's strong earnings growth potential. With earnings CAGR of 34% over FY06-09E, global scale capacities in terry towels and a more dynamic business model, we see upside potential to stock valuations of 11.5x FY07E, at discount to the sector and trading closer to the median of its 3-year historical trading brand of 7.5-13x.

Risk

We rate Welspun Medium Risk, as opposed to the High Risk rating assigned by our quantitative risk-rating system. The key reasons we opt for a Medium Risk rating include: (1) Secular growth prospects in home textiles post quotas and shrinking capacities in the US; (2) Rapid growth on account of new capacity expansion; (3) Welspun’s leadership position in India and its relationships with global brands; and (4) Peer stocks are rated Low or Medium Risk. The downside risks to our target price include: (1) Appreciation of the rupee; (2) Sharp increases in cotton prices; and (3) Delays in commissioning new projects. The upside risks to our target price include: 1) Faster than expected break even of the bed-linen business; and 2) Long-term sourcing tie-ups with global branded home textile retailers.

Analyst Certification Appendix A-1

We, Ashish Jagnani and Paul Chanin, research analysts and the authors of this report, hereby certify that all of the views expressed in this research report accurately reflect our personal views about any and all of the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

IMPORTANT DISCLOSURES

Citigroup Global Markets Inc. or its affiliates beneficially owns 1% or more of any class of common equity securities of Abhishek Industries Ltd, Alok Industries Ltd, Arvind Mills Ltd, Gokaldas Exports Ltd, S Kumars Nationwide Ltd and Vardhaman Textiles Ltd. This position reflects information available as of the prior business day.

Citigroup Global Markets Inc. or an affiliate received compensation for products and services other than investment banking services from Alok Industries Ltd, Gokaldas Exports Ltd, NIEN HSING TEXTILE, Raymond Ltd, TEXWINCA HLDGS, Victory City International Holdings Ltd, WEIQIAO TEXTILE CO and Welspun India Ltd in the past 12 months.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following company(ies) as clients, and the services provided were non-investment-banking, securities-related: Alok Industries Ltd, Raymond Ltd, TEXWINCA HLDGS, Victory City International Holdings Ltd, WEIQIAO TEXTILE CO and Welspun India Ltd.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following company(ies) as clients, and the services provided were non-investment-banking, non-securities-related: Alok Industries Ltd, Gokaldas Exports Ltd, NIEN HSING TEXTILE, Raymond Ltd, TEXWINCA HLDGS and WEIQIAO TEXTILE CO.

Analysts' compensation is determined based upon activities and services intended to benefit the investor clients of Citigroup Global Markets Inc. and its affiliates ("the Firm"). Like all Firm employees, analysts receive compensation that is impacted by overall firm profitability, which includes revenues from, among other business units, the Private Client Division, Institutional Sales and Trading, and Investment Banking.

For important disclosures (including copies of historical disclosures) regarding the companies that are the subject of this Citigroup Investment Research product ("the Product"), please contact Citigroup Investment Research, 388 Greenwich Street, 29th Floor, New York, NY, 10013, Attention: Legal/Compliance. In addition, the same important disclosures, with the exception of the Valuation and Risk assessments and historical disclosures, are contained on the Firm's disclosure website at www.citigroupgeo.com. Private Client Division clients should refer to www.smithbarney.com/research. Valuation and Risk assessments can be found in the text of the most recent research note/report regarding the subject company. Historical disclosures (for up to the past three years) will be provided upon request.

Citigroup Investment Research Ratings Distribution

Data current as of 30 September 2006	Buy	Hold	Sell
Citigroup Investment Research Global Fundamental Coverage (2914)	46%	40%	14%
% of companies in each rating category that are investment banking clients	44%	43%	32%
Hong Kong -- Asia Pacific (78)	51%	14%	35%
% of companies in each rating category that are investment banking clients	48%	82%	33%
India -- Asia Pacific (105)	59%	16%	25%
% of companies in each rating category that are investment banking clients	52%	65%	38%
Citigroup Investment Research Quantitative World Radar Screen Model Coverage (5954)	29%	44%	26%
% of companies in each rating category that are investment banking clients	32%	25%	24%
Citigroup Investment Research Quantitative Decision Tree Model Coverage (338)	47%	0%	53%
% of companies in each rating category that are investment banking clients	46%	0%	47%
Citigroup Investment Research Quantitative European Value & Momentum Screen (605)	30%	40%	30%
% of companies in each rating category that are investment banking clients	40%	36%	39%
Citigroup Investment Research Asia Quantitative Radar Screen Model Coverage (1603)	20%	60%	20%
% of companies in each rating category that are investment banking clients	26%	21%	17%
Citigroup Investment Research Quant Emerging Markets Radar Screen Model Coverage (1252)	20%	60%	20%
% of companies in each rating category that are investment banking clients	27%	25%	28%
Citigroup Investment Research Australia Quantitative Top 100 Model Coverage (99)	29%	40%	30%
% of companies in each rating category that are investment banking clients	52%	40%	27%
Citigroup Investment Research Australia Quantitative Bottom 200 Model Coverage (180)	30%	40%	30%
% of companies in each rating category that are investment banking clients	6%	8%	7%
Citigroup Investment Research Australia Quantitative Scoring Stocks Model Coverage (10)	50%	0%	50%
% of companies in each rating category that are investment banking clients	20%	0%	20%

Guide to Fundamental Research Investment Ratings:

Citigroup Investment Research's stock recommendations include a risk rating and an investment rating.

Risk ratings, which take into account both price volatility and fundamental criteria, are: Low (L), Medium (M), High (H), and Speculative (S).

Investment ratings are a function of Citigroup Investment Research's expectation of total return (forecast price appreciation and dividend yield within the next 12 months) and risk rating.

For securities in emerging markets (Asia Pacific, Emerging Europe/Middle East/Africa, and Latin America), investment ratings are: Buy (1) (expected total return of 15% or more for Low-Risk stocks, 20% or more for Medium-Risk stocks, 30% or more for High-Risk stocks, and 40% or more for Speculative stocks); Hold (2) (5%-15% for Low-Risk stocks, 10%-20% for Medium-Risk stocks, 15%-30% for High-Risk stocks, and 20%-40% for Speculative stocks); and Sell (3) (5% or less for Low-Risk stocks, 10% or less for Medium-Risk stocks, 15% or less for High-Risk stocks, and 20% or less for Speculative stocks).

Investment ratings are determined by the ranges described above at the time of initiation of coverage, a change in investment and/or risk rating, or a change in target price (subject to limited management discretion). At other times, the expected total returns may fall outside of these ranges because of market price movements and/or other short-term volatility or trading patterns. Such interim deviations from specified ranges will be permitted but will become subject to review by Research Management.

Your decision to buy or sell a security should be based upon your personal investment objectives and should be made only after evaluating the stock's expected performance and risk.

Guide to Quantitative Research Investment Ratings:
Citigroup Investment Research Quantitative Research World Radar Screen recommendations are based on a globally consistent framework to measure relative value and momentum for a large number of stocks across global developed and emerging markets. Relative value and momentum rankings are equally weighted to produce a global attractiveness score for each stock. The scores are then ranked and put into deciles. A stock with a decile rating of 1 denotes an attractiveness score in the top 10% of the universe (most attractive). A stock with a decile rating of 10 denotes an attractiveness score in the bottom 10% of the universe (least attractive).
Citigroup Investment Research Quantitative Decision Tree model recommendations are based on a predetermined set of factors to rate the relative attractiveness of stocks. These factors are detailed in the text of the report. Each month, the Decision Tree model forecasts whether stocks are attractive or unattractive relative to other stocks in the same sector (based on the Russell 1000 sector classifications).
Citigroup Investment Research Quantitative European Value & Momentum Screen recommendations are based on a European consistent framework to measure relative value and momentum for a large number of stocks across the European Market. Relative value and momentum rankings are equally weighted to produce a European attractiveness score for each stock. The scores are then ranked and put into deciles. A stock with a decile rating of 1 denotes an attractiveness score in the top 10% of the universe (most attractive). A stock with a decile rating of 10 denotes an attractiveness score in the bottom 10% of the universe (least attractive).
Citigroup Investment Research Asia Quantitative Radar Screen and Emerging Markets Radar Screen model recommendations are based on a regionally consistent framework to measure relative value and momentum for a large number of stocks across regional developed and emerging markets. Relative value and momentum rankings are equally weighted to produce a global attractiveness score for each stock. The scores are then ranked and put into quintiles. A stock with a quintile rating of 1 denotes an attractiveness score in the top 20% of the universe (most attractive). A stock with a quintile rating of 5 denotes an attractiveness score in the bottom 20% of the universe (least attractive).
Citigroup Investment Research Quantitative Australian Stock Selection Screen rankings are based on a consistent framework to measure relative value and earnings momentum for a large number of stocks across the Australian market. Relative value and earnings momentum rankings are weighted to produce a rank within a relevant universe for each stock. The rankings are then put into deciles. A stock with a decile rating of 1 denotes an attractiveness score in the top 10% of the universe (most attractive). A stock with a decile rating of 10 denotes an attractiveness score in the bottom 10% of the universe (least attractive).
Citigroup Investment Research Quantitative Research Australian Scoring Stocks model recommendations are based on a predetermined set of factors to rate the relative attractiveness of stocks. These factors are detailed in the text of the report. Each month, the Australian Scoring Stocks model calculates whether stocks are attractive or unattractive relative to other stocks in the same universe(the S&P/ASX 100) and records the 5 most attractive buys and 5 most attractive sells on the basis of the criteria described in the report.

For purposes of NASD/NYSE ratings-distribution-disclosure rules, a Citigroup Investment Research Quantitative World Radar Screen and European Value & Momentum Screen recommendation of (1), (2) or (3) most closely corresponds to a buy recommendation; a recommendation from this product group of (4), (5), (6) or (7) most closely corresponds to a hold recommendation; and a recommendation of (8), (9) or (10) most closely corresponds to a sell recommendation.
For purposes of NASD/NYSE ratings distribution disclosure rules, a Citigroup Investment Research Asia Quantitative Radar Screen or Quantitative Emerging Markets Radar Screen recommendation of (1) most closely corresponds to a buy recommendation; a Citigroup Investment Research Asia Quantitative Radar Screen or Quantitative Emerging Markets Radar Screen recommendation of (2), (3), (4) most closely corresponds to a hold recommendation; and a recommendation of (5) most closely corresponds to a sell recommendation.
For purposes of NASD/NYSE ratings-distribution-disclosure rules, a Citigroup Investment Research Quantitative Research Decision Tree model recommendation of "attractive" most closely corresponds to a buy recommendation. All other stocks in the sector are considered to be "unattractive" which most closely corresponds to a sell recommendation.
Recommendations are based on the relative attractiveness of a stock, they can not be directly equated to buy, hold and sell categories. Accordingly, your decision to buy or sell a security should be based on your personal investment objectives and only after evaluating the stock's expected relative performance.
For purposes of NASD/NYSE ratings-distribution-disclosure rules, a Citigroup Investment Research Quantitative Australian Stock Selection Screen model ranking in the top third of the universe most closely corresponds, subject to market conditions, to a buy recommendation. A ranking in the bottom third of the universe, subject to market conditions, most closely corresponds to a sell recommendation. All other stocks in the universe correspond to a hold recommendation. However, because Citigroup Investment Research Quantitative Australian Stock Selection Screen model rankings are based on the relative attractiveness of a stock as compared to other stocks in the same universe, they can not be directly equated to buy, hold and sell categories. Accordingly, your decision to buy or sell a security should be based on your personal investment objectives and only after evaluating the stock's expected absolute performance.
For purposes of NASD/NYSE ratings-distribution-disclosure rules, membership of the Citigroup Investment Research Quantitative Australian Scoring Stocks Model buy portfolio most closely corresponds to a buy recommendation; membership of the Citigroup Investment Research Quantitative Australian Scoring Stocks Model sell portfolio most closely corresponds to a sell recommendation. However, because Citigroup Investment Research Quantitative Australian Scoring Stocks Model recommendations are based on the relative attractiveness of a stock, they can not be directly equated to buy, hold and sell categories. Accordingly, your decision to buy or sell a security should be based on your personal investment objectives and only after evaluating the stock's expected absolute performance.

OTHER DISCLOSURES

Citigroup Global Markets Inc. or its affiliates beneficially owns 2% or more of any class of common equity securities of Gokaldas Exports Ltd.

Citigroup Global Markets Inc. or its affiliates beneficially owns 5% or more of any class of common equity securities of Abhishek Industries Ltd, Alok Industries Ltd, Arvind Mills Ltd, S Kumars Nationwide Ltd and Vardhaman Textiles Ltd.

Citigroup Global Markets Inc. or its affiliates holds a long position in any class of common equity securities of Alok Industries Ltd, Arvind Mills Ltd, Gokaldas Exports Ltd, NIEN HSING TEXTILE, Raymond Ltd, S Kumars Nationwide Ltd and WEIQIAO TEXTILE CO.

For securities recommended in the Product in which the Firm is not a market maker, the Firm is a liquidity provider in the issuers' financial instruments and may act as principal in connection with such transactions. The Firm is a regular issuer of traded financial instruments linked to securities that may have been recommended in the Product. The Firm regularly trades in the securities of the subject company(ies) discussed in the Product. The Firm may engage in securities transactions in a manner inconsistent with the Product and, with respect to securities covered by the Product, will buy or sell from customers on a principal basis.

Securities recommended, offered, or sold by the Firm: (i) are not insured by the Federal Deposit Insurance Corporation; (ii) are not deposits or other obligations of any insured depository institution (including Citibank); and (iii) are subject to investment risks, including the possible loss of the principal amount invested. Although information has been obtained from and is based upon sources that the Firm believes to be reliable, we do not guarantee its accuracy and it may be incomplete and condensed. Note, however, that the Firm has taken all reasonable steps to determine the accuracy and completeness of the disclosures made in the Important Disclosures section of the Product. The Firm's research department has received assistance from the subject company(ies) referred to in this Product including, but not limited to, discussions with management of the subject company(ies). Firm policy prohibits research analysts from sending draft research to subject companies. However, it should be presumed that the author of the Product has had discussions with the subject company to ensure factual accuracy prior to publication. All opinions, projections and estimates constitute the judgment of the author as of the date of the Product and these, plus any other information contained in the Product, are subject to change without notice. Prices and availability of financial instruments also are subject to change without notice. Notwithstanding other departments within the Firm advising the companies discussed in this Product, information obtained in such role is not used in the preparation of the Product. Although Citigroup Investment Research does not set a predetermined frequency for publication, if the Product is a fundamental research report, it is the intention of Citigroup Investment Research to provide research coverage of the/those issuer(s) mentioned therein, including in response to news affecting this issuer, subject to applicable quiet periods and capacity constraints. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security. Any decision to purchase securities mentioned in the Product must take into account existing public information on such security or any registered prospectus.

Investing in non-U.S. securities, including ADRs, may entail certain risks. The securities of non-U.S. issuers may not be registered with, nor be subject to the reporting requirements of the U.S. Securities and Exchange Commission. There may be limited information available on foreign securities. Foreign companies are generally not subject to uniform audit and reporting standards, practices and requirements comparable to those in the U.S. Securities of some foreign companies may be less liquid and their prices more volatile than securities of comparable U.S. companies. In addition, exchange rate movements may have an adverse effect on the value of an investment in a foreign stock and its corresponding dividend payment for U.S. investors. Net dividends to ADR investors are estimated, using withholding tax rates conventions, deemed accurate, but investors are urged to consult their tax advisor for exact dividend computations. Investors who have received the Product from the Firm may be prohibited in certain states or other jurisdictions from purchasing securities mentioned in the Product from the Firm. Please ask your Financial Consultant for additional details. Citigroup Global Markets Inc. takes responsibility for the Product in the United States. Any orders by US investors resulting from the information contained in the Product may be placed only through Citigroup Global Markets Inc.

The Citigroup legal entity that takes responsibility for the production of the Product is the legal entity which the first named author is employed by. The Product is made available in Australia to wholesale clients through Citigroup Global Markets Australia Pty Ltd. (ABN 64 003 114 832 and AFSL No. 240992) and to retail clients through Citigroup Wealth Advisors Pty Ltd. (ABN 19 009 145 555 and AFSL No. 240813), Participants of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. If the Product is being made available in certain provinces of Canada by Citigroup Global Markets (Canada) Inc. ("CGM Canada"), CGM Canada has approved the Product. Citigroup Place, 123 Front Street West, Suite 1100, Toronto, Ontario M5J 2M3. The Product may not be distributed to private clients in Germany. The Product is distributed in Germany by Citigroup Global Markets Deutschland AG & Co. KGaA, which is regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin). Frankfurt am Main, Reuterweg 16, 60323 Frankfurt am Main. If the Product is made available in Hong Kong by, or on behalf of, Citigroup Global Markets Asia Ltd., it is attributable to Citigroup Global Markets Asia Ltd., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong. Citigroup Global Markets Asia Ltd. is regulated by Hong Kong Securities and Futures Commission. If the Product is made available in Hong Kong by The Citigroup Private Bank to its clients, it is attributable to Citibank N.A., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong. The Citigroup Private Bank and Citibank N.A. is regulated by the Hong Kong Monetary Authority. The Product is made available in India by Citigroup Global Markets India Private Limited, which is regulated by Securities and Exchange Board of India. Bakhtawar, Nariman Point, Mumbai 400-021. If the Product was prepared by Citigroup Investment Research and distributed in Japan by Nikko Citigroup Ltd., it is being so distributed under license. Nikko Citigroup Limited is regulated by Financial Services Agency, Securities and Exchange Surveillance Commission, Japan Securities Dealers Association, Tokyo Stock Exchange and Osaka Securities Exchange. Akasaka Park Building, 2-20, Akasaka 5-chome, Minato-ku, Tokyo 107-6122. The Product is made available in Korea by Citigroup Global Markets Korea Securities Ltd., which is regulated by Financial Supervisory Commission and the Financial Supervisory Service. Hungkuk Life Insurance Building, 226 Shinmunno 1-GA, Jongno-Gu, Seoul, 110-061. The Product is made available in Malaysia by Citigroup Global Markets Malaysia Sdn Bhd, which is regulated by Malaysia Securities Commission. Menara Citibank, 165 Jalan Ampang, Kuala Lumpur, 50450. The Product is made available in Mexico by Acciones y Valores Banamex, S.A. De C. V., Casa de Bolsa, which is regulated by Comision Nacional Bancaria y de Valores. Reforma 398, Col. Juarez, 06600 Mexico, D.F. In New Zealand the Product is made available through Citigroup Global Markets New Zealand Ltd., a Participant of the New Zealand Exchange Limited and regulated by the New Zealand Securities Commission. Level 19, Mobile on the Park, 157 lambton Quay, Wellington. The Product is made available in Poland by Dom Maklerski Banku Handlowego SA an indirect subsidiary of Citigroup Inc., which is regulated by Komisja Papierów Wartosciowych i Gield. Bank Handlowy w Warszawie S.A. ul. Senatorska 16, 00-923 Warszawa. The Product is made available in the Russian Federation through ZAO Citibank, which is licensed to carry out banking activities in the Russian Federation in accordance with the general banking license issued by the Central Bank of the Russian Federation and brokerage activities in accordance with the license issued by the Federal Service for Financial Markets. Neither the Product nor any information contained in the Product shall be considered as advertising the securities mentioned in this report within the territory of the Russian Federation or outside the Russian Federation. The Product does not constitute an appraisal within the meaning of the Federal Law of the Russian Federation of 29 July 1998 No. 135-FZ (as amended) On Appraisal Activities in the Russian Federation. 8-10 Gasheka Street, 125047 Moscow. The Product is made available in Singapore through Citigroup Global Markets Singapore Pte. Ltd., a Capital Markets Services Licence holder, and regulated by Monetary Authority of Singapore. 1 Temasek Avenue, #39-02 Millenia Tower, Singapore 039192. Citigroup Global Markets (Pty) Ltd. is incorporated in the Republic of South Africa (company registration number 2000/025866/07) and its registered office is at 145 West Street, Sandton, 2196, Saxonwold. Citigroup Global Markets (Pty) Ltd. is regulated by JSE Securities Exchange South Africa, South African Reserve Bank and the Financial Services Board. The investments and services contained herein are not available to private customers in South Africa. The Product is made available in Taiwan through Citigroup Global Markets Inc. (Taipei Branch), which is regulated by Securities & Futures Bureau. No portion of the report may be reproduced or quoted in Taiwan by the press or any other person. No. 8 Manhattan Building, Hsin Yi Road, Section 5, Taipei 100, Taiwan. The Product is made available in Thailand through Citicorp Securities (Thailand) Ltd., which is regulated by the Securities and Exchange Commission of Thailand. 18/F, 22/F and 29/F, 82 North Sathorn Road, Silom, Bangrak, Bangkok 10500, Thailand. The Product is made available in United Kingdom by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. This material may relate to investments or services of a person outside of the UK or to other matters which are not regulated by the FSA and further details as to where this may be the case are available upon request in respect of this material. Citigroup Centre, Canada Square, Canary Wharf, London, E14 5LB. The Product is made available in United States by Citigroup Global Markets Inc, which is regulated by NASD, NYSE and the US Securities and Exchange Commission. 388 Greenwich Street, New York, NY 10013. Unless specified to the contrary, within EU Member States, the Product is made available by Citigroup Global Markets Limited, which is regulated by Financial Services Authority. Many European regulators require that a firm must establish, implement and make available a policy for managing conflicts of interest arising as a result of publication or distribution of investment research. The policy applicable to Citigroup Investment Research's Products can be found at www.citigroupgeo.com. Compensation of equity research analysts is determined by equity research management and Citigroup's senior management and is not linked to specific transactions or recommendations. The Product may have been distributed simultaneously, in multiple formats, to the Firm's worldwide institutional and retail customers. The Product is not to be construed as providing investment services in any jurisdiction where the provision of such services would be illegal. Subject to the nature and contents of the Product, the investments described therein are subject to fluctuations in price and/or value and investors may get back less than originally invested. Certain high-volatility investments can be subject to sudden and large falls in value that could equal or exceed the amount invested. Certain investments contained in the Product may have tax implications for private customers whereby levels and basis of taxation may be subject to change. If in doubt, investors should seek advice from a tax adviser. Advice in the Product has been prepared without taking account of the objectives, financial situation or needs of any particular investor. Accordingly, investors should, before acting on the advice, consider the appropriateness of the advice, having regard to their objectives, financial situation and needs.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST