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Institutional Equities

Arvind

back in vogue

Arvind

13 April 2012

Reuters: ARVN.BO; Bloomberg: ARVND IN

Initiating Coverage

Back in Vogue

With a strong portfolio of 21 brands and aggressive 23.9% CAGR in retail expansion at 1.58mn sq ft, we expect Arvind's brands and retail business to show 25.6% CAGR over FY11-14E at Rs19.1bn and increase its share from 22% to 32.7% over the same period. Positive result of major capex of Rs4.3bn over FY11-12 would be visible in FY13-14. Its stock is currently trading at 6.5x/4.9x FY13/14E P/E and 5.2/4.2x EV/EBITDA, below the mean of 8.1x and 6.5x, respectively. Strong 12.4% revenue CAGR aided by 104bps higher operating margin, working capital efficiency and debt reduction by 26.5% should drive profitability CAGR by 45.6% over FY11-14E, generate free cash flow of Rs5.2bn over FY13-14E, improve adjusted RoCE by 303bps over FY11-14E and calls for expansion of PE multiple. We assign a Buy rating to Arvind with a SOTP-based TP of Rs117, valuing it at 9.1x/6.4x/1.2x PE, EV/EBITDA, P/B for FY13E.

Lower debt, interest rates to drive profitability: Bumper cotton production led to softening of prices, which would reduce Arvind's ex-cash working capital requirement to 26.8% of sales in FY14E from 28.3% in FY11. Free cash flow of Rs5.2bn over FY12-14E would reduce its debt by 26.5% to Rs16.2bn and its adjusted D/E ratio from 1.6x to 0.6x over FY11-14E. Lower debt, falling interest rates and improved credit rating would prune interest costs from 6.4% to 3.3% of sales over FY11-14E and drive net profit CAGR by 45.6% over the same period. Monetisation of real estate assets, as and when it happens, would sweeten its cash flow and debt reduction programme.

Fast paced growth of B&R business: From a denim producer for corporate clients, Arvind is turning into a brand power house catering to consumers directly. Aggressive retail expansion, growth through multiple drivers like distribution expansion, new brands launch and category expansion would drive the brands and retail (B&R) division's revenue CAGR by 25.6% to Rs19.1bn and increase its revenue share to 32.7% from 22% over FY11-14E. We expect its operating margin to rise by 140bps to 9.5%, which would increase segmental RoCE by ~109bps to 14.0% over FY11-14E.

Strong free cash flow and return ratios: With the decline in cotton prices and hence working capital needs, a 104bps improvement in operating margin over FY11-14E and lower capex, Arvind should generate positive free cash flow of Rs5.2bn over FY13-14E. Following weak demand, we expect the performance of its textile and retail divisions to remain muted in 1HFY13, thereby pruning consolidated margin by 20bps to 14.2% and RoCE by 96bps in FY13E. However, with the revival in demand and soft cotton prices, its revenue should grow 14.3%, operating margin should improve by 40bps and RoCE by 123bps in FY14E. Adjusted RoCE/RoE should improve from 11.7%/11.0% in FY11 to 14.8%/18.3%, respectively, in FY14E. Positive free cash flow from FY13 onwards and improving return ratios should drive up the valuation multiple.

Y/E Mar (Rsmn)	FY10	FY11	FY12E	FY13E	FY14E
Net sales	32,612	40,897	48,258	50,768	58,027
EBITDA	4,099	5,562	6,970	7,230	8,498
Net profit	433	1,420	2,512	3,267	4,389
EPS (Rs)	1.8	5.6	9.9	12.8	17.3
EPS growth (%)	*-*	*204.7*	*76.8*	*30.1*	*34.3*
EBITDA margin (%)	*12.6*	*13.6*	*14.4*	*14.2*	*14.6*
PE ratio (x)	45.3	14.9	8.4	6.5	4.9
Price/BV (x)	1.5	1.2	1.0	0.9	0.7
EV/EBITDA (x)	9.8	7.6	5.8	5.2	4.2
RoCE (%)	*9.2*	*11.1*	*13.5*	*12.5*	*13.7*
RoE (%)	*3.7*	*9.5*	*13.0*	*14.1*	*16.2*

Source: Company, Nirmal Bang Institutional Equities Research

BUY

Sector: Retail

CMP: Rs84

Target Price: Rs117

Upside: 39%

Jignesh Kamani, CFA
jignesh.kamani@nirmalbang.com
+91-22-3926 8239

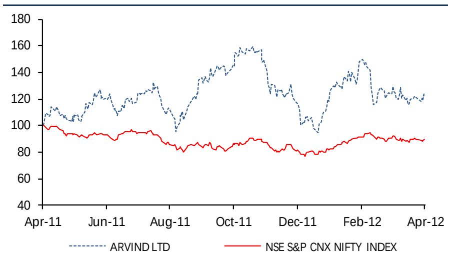
Saiprasad Prabhu
saiprasad.prabhu@nirmalbang.com
+91-22-3926 8172

Key Data

Current Shares O/S (mn)	254.6
Mkt Cap (Rsbn/US$mn)	21.4/416.7
52 Wk H / L (Rs)	111/62
Daily Vol. (3M NSE Avg.)	3,650,824

Share holding (%)	1QFY12	2QFY12	3QFY12
Promoter	43.5	43.4	43.4
FII	11.2	13.6	15.5
DII	16.9	18.7	18.4
Corporate	4.6	3.7	3.8
General Public	23.8	206	19.0

One Year Indexed Stock Performance



Price Performance (%)

	1 M	6 M	1 Yr
Arvind	(5.4)	(15.6)	22.5
Nifty Index	(2.4)	4.4	(10.4)

Source: Bloomberg

Valuation

Currently, Arvind trades at 5.2x/4.2x its FY13/14 EV/EBITDA, below its 10-year median of 6.5x. We expect the company to improve its EBITDA by 15.2% CAGR over FY11-14E as against 5.6% CAGR over FY06-11. Its stock is trading attractively on other valuation parameters too, P/E at 6.5x/4.9x its FY13/14E EPS of Rs12.8/17.3, respectively, below its two-year median of 8.1x. We expect the company to report RoE of 13.0%/14.1%/16.2% in FY12/13/14E against 3.7%/9.5% in FY10/11, respectively. **Adjusted D/E ratio, which was as high as 2.2x in FY09, should reduce to 1.1x in FY12E and to 0.6x in FY14E. Debt, in absolute terms, should reduce by 26.5% to Rs16.2bn over FY11-14E. High debt increased volatility in net profit and hurt the margins of the company, thereby capping its valuation in the past. Its stock is also trading at 42.1% and 42.5% discount to its comparable peer Raymond on P/E and P/B basis, respectively, based on FY13E financials, which is not warranted given the strong return ratios and positive free cash flow and we expect the valuation gap to narrow down to 10-15% once the strong performance is visible in FY13/14E.**

Strong revenue CAGR of 12.4% supported by operating margin improvement of 104bps, working capital efficiency and debt reduction by 26.5% should drive profitability CAGR by 45.6% over FY11-14E, generate free cash flow of Rs5,244mn over FY12-14E, improve adjusted RoCE by 303bps over FY11-14E and calls for expansion of the valuation multiple.

As Arvind has diversified its business model from a commodity denim fabric manufacturer to a consumer-centric business house with the focus on brands and retailing business, we have valued each of its divisions separately based on the EV/EBITDA multiple. Peer textile manufacturer Vardhman Industries is trading at 5.3x, but it is expected to report subdued RoE of 8.7% for FY13E. Aarvee Denim, second largest denim manufacturer (after Arvind), has been trading in the EV/EBITDA band of 4-7x. Arvind itself was trading in the EV/EBITDA band of 5-8x during FY03-07 and at that time the company was a manufacturer of commodity textiles i.e. denim. With a better margin and higher returns ratio of 16.7%, up 236bps over FY11-13E, we expect Arvind's textile division to command a premium to competitors like Vardhman Industries, Aarvee Denim etc and we have valued it at 5.5x EV/EBITDA. Stocks of retailers like Pantaloon and Shoppers Stop are trading in the range of 9-15.4x EV/EBITDA. The B&R business of Arvind is evolving and currently is smaller in size compared to established players. Its retail area of 1mn sq ft, compared to 2.9mn sq ft of Shoppers Stop (standalone), with sales of Rs19.2bn in FY12E, is 42% of Shopper Stop's FY12E consolidated revenue. On account of the evolving nature of its business, we have valued Arvind's B&R business near the lower end of Shoppers Stop's valuation band of 9-15.4x. We have valued its textile division (66.4%/80.6% of FY13E sales/EBITDA) at 5.5x, and high growth B&R business (29.0%/17.5% of FY13E sales/EBITDA) at 8x. Arvind has a large land bank of ~500 acres and it is planning to monetise these assets, either through developing land parcels or selling land parcel in bits and pieces. According to the management, the current value of its land assets after development would be around Rs10bn i.e. Rs39 per share. We have valued the land parcel at 33% of its net asset value of Rs39 in our target price. We assign a Buy rating to the stock with a SOTP-based target price of Rs117, valuing it at 9.1x/6.4x/1.2x PE, EV/EBITDA, P/B respectively, for FY13E.

Exhibit 1: Comparative valuation

	Mkt Cap	CMP	Net sales (Rsbn)			*EBITDA (%)*			*CAGR (%) FY11-13*			P/B (x)			P/E (x)			EV/EBITDA (x)			*RoE (%)*		
Comparison	**(Rsbn)**	**(Rs)**	**FY12E**	**FY13E**	**FY14E**	***FY12E***	***FY13E***	***FY14E***	***Sales***	***EBITDA***	***PAT***	**FY12E**	**FY13E**	**FY14E**	**FY12E**	**FY13E**	**FY14E**	**FY12E**	**FY13E**	**FY14E**	***FY12E***	***FY13E***	***FY14E***
Arvind*	21.4	84	48.3	50.8	58.0	*14.4*	*14.2*	*14.6*	*9.7*	*10.4*	*32.2*	1.0	0.9	0.7	8.5	6.5	4.9	5.8	5.2	4.2	*13.0*	*14.1*	*16.2*
Raymond	24.9	405	35.4	38.9	44.3	*15.1*	*15.4*	*15.0*	*11.9*	*11.4*	*16.7*	1.8	1.6	1.5	13.6	11.2	9.6	7.0	6.2	5.6	*14.2*	*14.8*	*16.0*
BRFL	34.3	255	26.9	32.4	NA	*25.9*	*26.3*	*NA*	*NA*	*NA*	*NA*	1.1	1.0	NA	15.9	10.8	NA	9.4	7.7	NA	*7.6*	*9.8*	*NA*
Kewal Kiran	7.7	625	3.0	3.7	4.7	*23.8*	*25.0*	*25.3*	*24.4*	*28.1*	*29.4*	3.3	2.8	2.2	14.9	11.8	9.5	9.6	7.5	5.8	*24.0*	*25.4*	*27.4*
Pantaloon Retail	36.1	167	126.9	148.7	168.3	*8.8*	*8.8*	*8.9*	*15.2*	*15.9*	*44.1*	1.1	1.1	1.0	26.0	18.3	14.5	10.6	9.0	7.9	*4.9*	*6.4*	*6.7*
Shoppers Stop	29.6	359	28.9	35.4	42.1	*4.2*	*5.2*	*5.4*	*20.6*	*37.3*	*69.2*	5.5	5.0	4.2	94.7	44.1	30.1	26.5	17.5	14.1	*6.5*	*11.7*	*17.4*

Note: Bloomberg estimates for other companies excpet Arvind

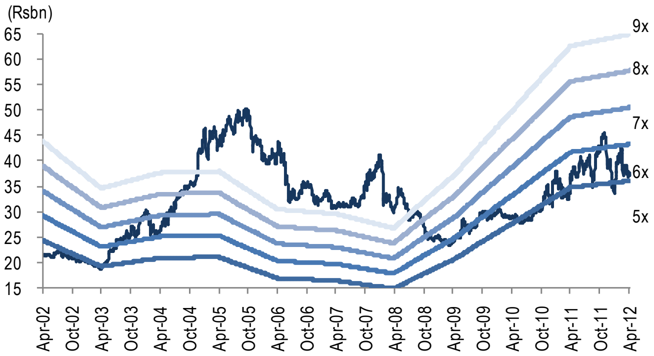
Source: Bloomberg, Nirmal Bang Institutional Equities Research

Exhibit 2: SOTP-based valuation

SOTP			
Segment	**EBITDA (Rsmn)**	**Target EV/EBITDA multiple (x)**	**Value (Rsmn)**
Textile	5,827	5.5	32,048
Brands & retail	1,266	8.0	10,127
Others	139	5.0	696
Enterprise value			42,872
Less Debt			16,468
Target market cap			26,403
Core business target price (Rs/share)			**104**
Land back: 33% of its NAV of Rs39 **(Rs/share)**			13
Target price (Rs/share)			**117**

Source: Nirmal Bang Institutional Equities Research

Exhibit 3: One-year forward EV/EBITDA



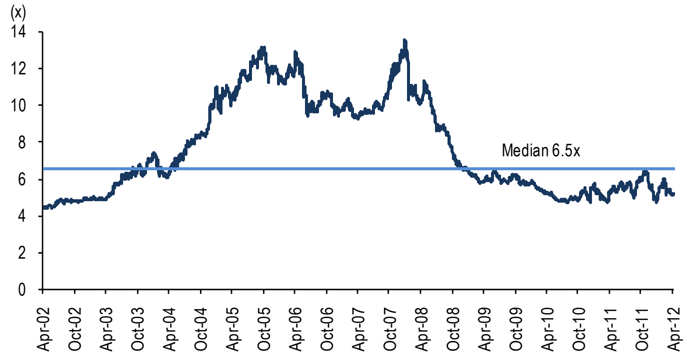
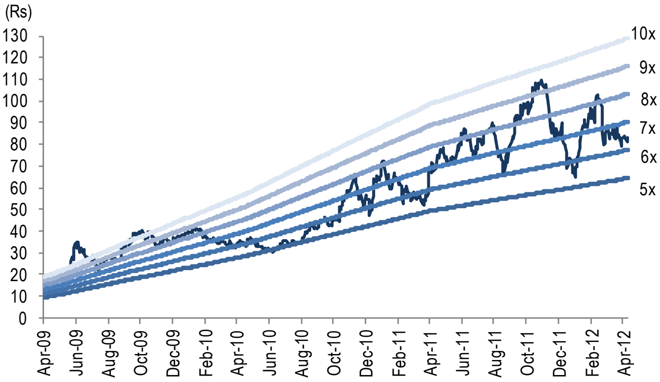


Exhibit 4: One-year forward P/E



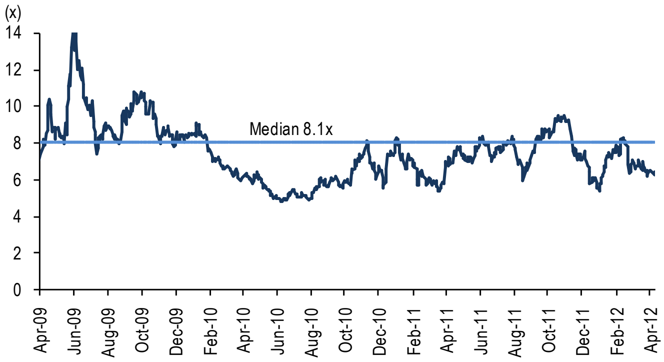
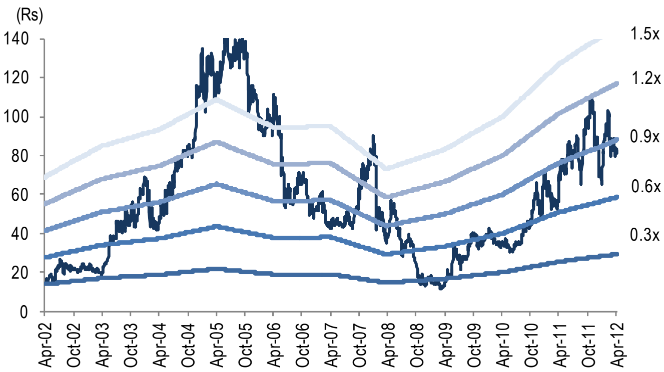
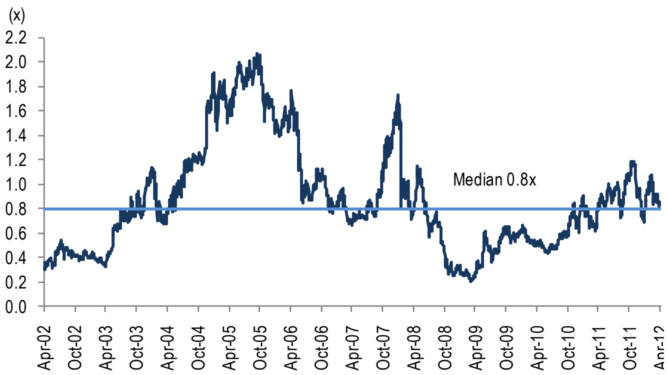


Exhibit 5: One-year forward P/B





Source: Bloomberg, Nirmal Bang Institutional Equities Research

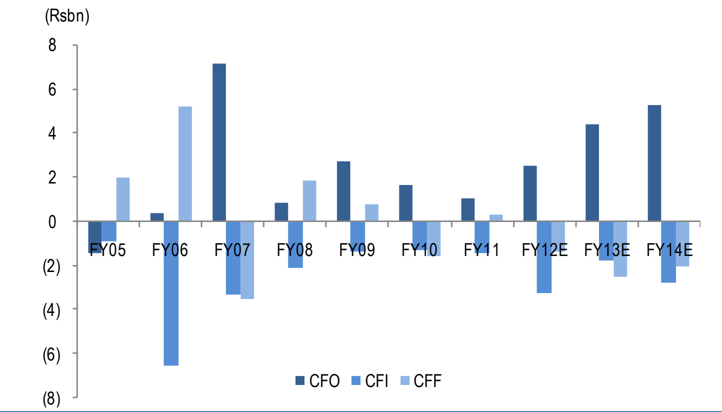
Investment Arguments

Healthy free cash flow generation

The company was cash flow positive over FY08-11 at the operating level, but lower in absolute terms, generating cumulative cash flow of Rs7.4bn, a mere 5.8% of sales of Rs127.7bn on account of poor profitability and higher interest costs. The company invested Rs6.1bn over FY08-11 to expand its facilities aggressively and set up retail outlets over this period and as a result, its free cash flow was negative for two out of four years, cumulatively generating free cash flow of mere Rs320mn over the same period. **The company incurred capex of Rs3.2bn in FY12 to expand its denim/knitting capacity and increase its retail reach. However, on the back of healthy operating cash flow of Rs2.6bn, the company would report negative free cash flow of mere Rs660mn in FY12. With the decline in cotton prices, working capital requirement would ease and, in addition, we expect the margins to improve, thereby resulting in the company generating operating cash flow of Rs9.8bn over FY13-14E.**

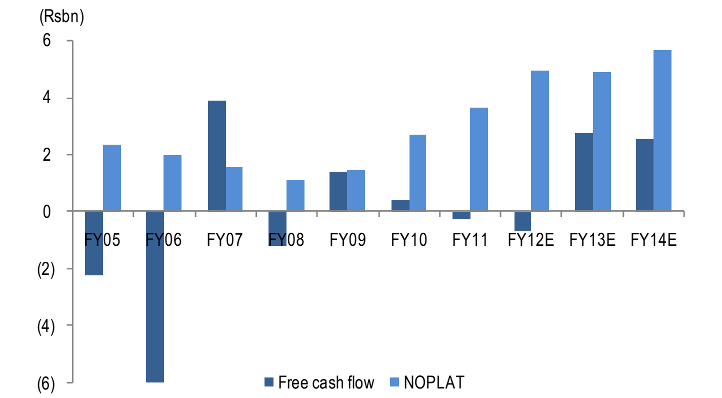
We expect the company to consolidate its expansion plans on the manufacturing front and focus more on the B&R division's expansion. On account of lower capex of Rs4.5bn over FY13-14E as against Rs3.2bn in F12E and strong operating cash flow, the company should report positive free cash flow of Rs5.2bn over the same period. Positive free cash flow from FY13 onwards would lead to a re-rating of its valuation multiple. In addition, the company has a land bank of ~500 acres, monetisation of it, as and when it happens, would increase cash flow substantially, which we have not factored in our financial estimates. On the back of lower capex, strong operating cash flow and monetisation of real estate assets, we expect Arvind to pay off its debts and de-leverage its balance sheet, improve its credit rating and also profitability.

Exhibit 6: Cash flow trend



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Improvement in free cash flow



Source: Company, Nirmal Bang Institutional Equities Research

Better product mix, higher utilisation to improve return ratios

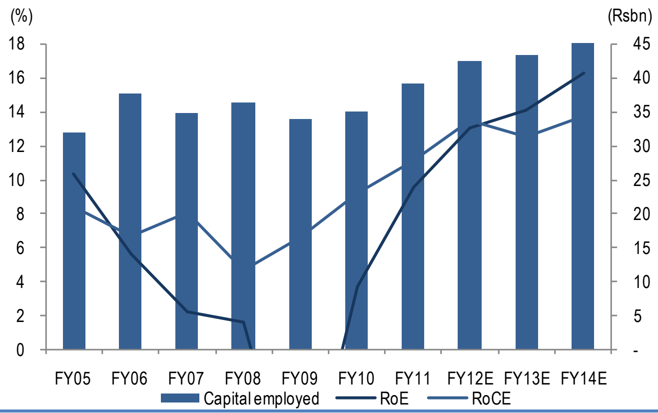
Textile manufacturing is a low asset turnover business with asset turnover of 1-1.5x on account of high capex requirement, while its B&R business has high asset turnover of 1.6-2x. The company incurred capex of Rs3.2bn in FY12 to expand its denim/knitting capacity and increase its retail reach, the benefit of which would be visible in FY13/14. In addition, with a higher share of B&R the overall asset turnover should improve from 1.0x in FY11 to 1.2x in FY14E. As the company expanded its retail presence aggressively in the past two years, majority of its outlets are relatively new and did not contribute to operating profit meaningfully in FY11/12, and thereby the EBITDA margin of its B&R business ranged between 5.8-8.7% over 1QFY11 to 3QFY12 compared to textile EBITDA margin of 15.7%-18% over the same period. Rise in cotton prices and imposition of 10% excise duty in the Union Budget for 2011-12 also affected the profitability of Arvind's B&R business.

Following weak demand from the US and lower domestic consumption, we expect the performance of its textile and retail divisions to remain muted in 1HFY13. Operating margin of its textile division would reduce by 70bps to 17.1% in FY13E, which would reduce consolidated margin by 20bps to 14.2% and RoCE by 96bps, However, with revival in demand and soft cotton prices, revenue from the textile division should increase by 8.7% in FY14E. After a decline of 70bps in FY13E, the operating margin of its textile division should improve by 60bps in FY14E. With stabilisation of cotton prices at the lower level, demand for branded garments should improve in 2HFY13 and, in addition, with the stabilisation of operations, majority of the outlets set up in the past two years should report improvement in profitability in FY14.

Following weak demand and oversupply situation in commercial real estate, lease rentals should be under control and the company should benefit out of it. As a result, EBITDA margin of its branded garments segment should improve by 140bps over FY11-14E, from 8.1% to 9.5%. RoCE of its branded garments segment should improve by ~109/123bps to 14.0% in FY14E from 12.9%/12.8% in FY11/12E, respectively, driving consolidated RoCE by 262/27bps to 13.7% in FY14E from 11.1%/13.5% in FY11/12E, respectively.

In addition, we expect interest costs to decline substantially on: 1) Reduction in debt, in absolute terms, because of lower working capital and lower capex requirement, 2) Improved credit rating, and 3) Lower interest rates. As a result, net profit margin should improve from 3.5%/5.2% in FY11/12E to 6.4%/7.6% in FY13/14E, respectively. On the back of lower leverage, its leverage multiplier would reduce from 2.5x in FY11 to 1.7x in FY14E, and even after that due to higher asset turnover and higher net profit margin RoNW should improve from 9.5%/13.0% in FY11/12E to 14.1%/16.2% in FY13/14E, respectively. The company re-valued its land bank, which increased its networth by Rs2,301mn in FY11. Adjusting networth by re-valuation reserve, RoNW should improve by 737bps to 18.3% in FY14E from 11% in FY11, compared to 670bps improvement factoring re-valuation reserve in networth. Similarly its adjusted RoCE should improve by 303bps compared to 262bps improvement factoring re-valuation reserve over FY11-14E.

Exhibit 8: Improving RoNW (%)



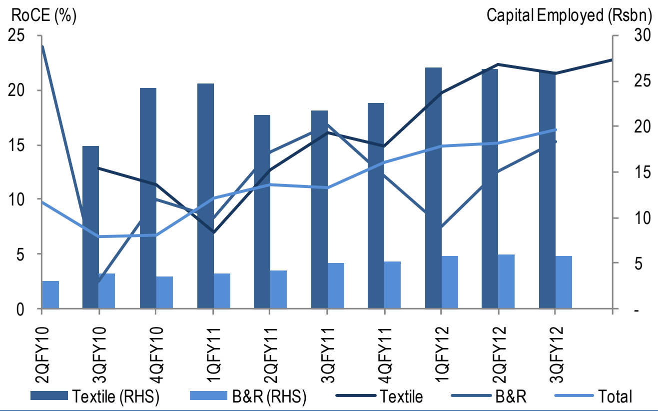
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: DuPont analysis

Y/E March	FY08	FY09	FY10	FY11	FY12E	FY13E	FY14E
EBIT (%)	*5.77*	*5.02*	*7.27*	*9.38*	*10.82*	*10.35*	*10.82*
Interest burden (x)	0.17	(0.75)	0.20	0.46	0.94	0.67	0.78
Tax burden (x)	0.85	1.23	0.92	0.81	0.51	0.93	0.90
Net sales/total assets (x)	0.75	0.78	0.94	1.10	1.17	1.17	1.28
Net profit/net sales (x)	0.82	(4.62)	1.33	3.47	5.20	6.44	7.56
Total assets/net worth (x)	2.65	2.88	2.95	2.50	2.14	1.87	1.67
RoNW (%)	*1.6*	*(10.3)*	*3.7*	*9.5*	*13.0*	*14.1*	*16.2*
Adjusted RoNW (%)	*1.7*	*(10.5)*	*3.8*	*11.0*	*15.5*	*16.3*	*18.3*

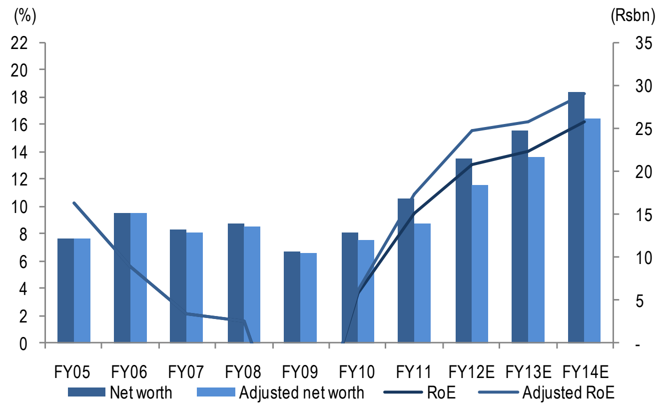
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 10: Segmental RoCE trend (%)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: Strong improvement on adjusted RoE



Source: Company, Nirmal Bang Institutional Equities Research

Bumper cotton production to soften prices

As per CRISIL Research, cotton production in India is estimated to increase by 6% to 5.3bn kg in CS11 (cotton season - October to September) and by 6% to 5.6bn kg in CS12 due to higher acreage. Acreage under cotton increased in most cotton producing states such as Maharashtra, Andhra Pradesh, Madhya Pradesh, Punjab, Karnataka and Tamil Nadu because of all-time high prices in CS10. Given the higher production and slowdown in demand, the closing stock inventory position is projected to improve and as a result the stock- to -use ratio, which touched its lowest level of 1.3x in CS11, would increase to 2.6x in CS12E and 3.7x in CS13E. Factoring this, cotton prices plunged 40.5% to Rs100 per kg in August 2011 from Rs168/kg in March 2011.

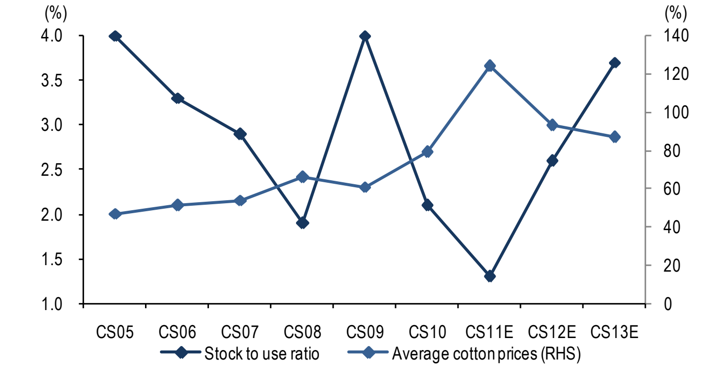
Cotton prices averaged Rs126/kg in CS11 and would soften by ~25% to Rs90-95/kg in CS12 and then ease marginally to Rs85-90/kg in CS13E.

Exhibit 12: India's cotton balance sheet

Cotton season	CS07	CS08	CS09	CS10	CS11E	CS12E
Opening stock - bn kg	1.0	0.9	0.6	1.2	0.7	0.5
Area - mn hectare	9.1	9.4	9.4	10.3	11.2	11.5
Yield - kg per hectare	521.0	554.0	524.0	486.0	475.0	490.0
Production	4.8	5.2	4.9	5.0	5.3	5.6
Growth (%)	*-*	*8.3*	*(5.8)*	*2.0*	*6.0*	*5.7*
Import	0.1	0.1	0.2	0.1	0.1	0.1
Total availability	5.8	6.2	5.7	6.3	6.1	6.2
Domestic consumption	3.9	4.1	3.9	4.3	4.5	4.5
Growth (%)	*-*	*5.1*	*(4.9)*	*10.3*	*4.7*	*-*
Exports	1.0	1.5	0.6	1.4	1.1	0.8
Growth (%)	*-*	*50.0*	*(60.0)*	*133.3*	*(21.4)*	*(27.3)*
Total consumption	4.9	5.6	4.5	5.7	5.6	5.3
Growth (%)	*-*	*14.3*	*(19.6)*	*26.7*	*(1.8)*	*(5.4)*
Closing stock	0.9	0.6	1.2	0.7	0.5	0.9
Stock to use ratio	2.9	1.9	4	2.1	1.3	2.6
Average price (Rs per kg)	53.7	65.8	60.5	78.7	124	93
Growth (%)	*-*	*22.5*	*(8.1)*	*30.1*	*57.6*	*(25.0)*

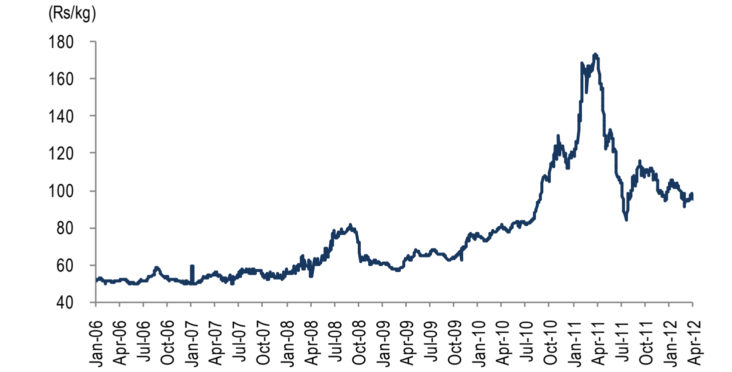
Source: Crisil research, Nirmal Bang Institutional Equities Research

Exhibit 13: Improving stock-to-use ratio



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 14: Declining cotton prices



Source: Bloomberg, Nirmal Bang Institutional Equities Research

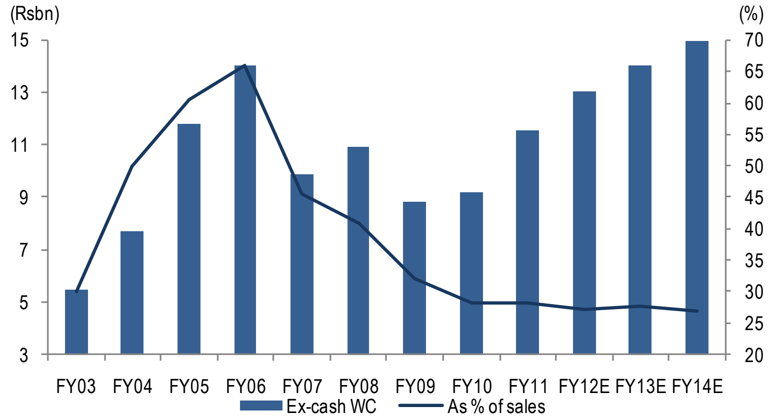
Lower cotton prices to reduce working capital

Cotton production takes place only in five months (October to February) of any cotton season (October to September), while it is consumed during the entire year. The company has to buy a substantial portion of its annual requirement during the cotton production period, resulting in high inventory period of 100-150 days for the company. Inventory formed a substantial part of working capital for the company, constituting 25-35% of its sales during FY08-11 as against ex-cash net working capital of 28-41% of sales during the same period. Raw materials and work-in-progress formed a significant portion of total inventory, at 20-40% each. Even the prices of finished goods, forming 25-35% of inventory, depend upon the prices of the raw material i.e. cotton.

World cotton production declined 8% to 22bn kg, the lowest in the past six cotton seasons (CS) in CS10, while cotton consumption increased 6% to 25bn kg. Improved global demand, combined with a decline in production, led to firm demand-supply situation in global markets, and its prices touched a high of US$2.3 per pound in March 2010 from US$0.67 per pound in October 2009. Domestic price (of Shankar 6 cotton grade) also increased by 113% to Rs168/kg in March 2011 from Rs79/kg in March 2010.

Following high cotton prices, inventory days for Arvind increased to 130 in FY11 from 101 in FY10, and inventory requirement in value terms increased by 58.9% in FY11 as against sales growth of 25.4% in the same year which increased its working capital requirement. We expect the situation to turn favourable in FY12/13. On account of lower cotton prices, inventory days for Arvind would reduce to 107 days in FY12 from 130 days in FY11 and in absolute terms inventory would grow by only 4.6% CAGR over FY11-14E against sales growth of 12.4% (textile volume growth of 5.2%) over the same period. Bumper cotton production would lead to softening of prices, thereby reducing its ex-cash working capital requirement to 26.8% of sales in FY14E from 28.3% in FY11. On the back of lower working capital requirement, we expect the debt level to reduce by Rs1,370mn to Rs20,741mn in FY12E and by Rs5,870mn to Rs16,241mn in FY14E from Rs22,111mn in FY11.

Exhibit 15: Working capital (WC) to remain under control



Source: Company, Nirmal Bang Institutional Equities Research

B&R business operates with efficient working capital cycle

We believe the higher share of B&R business would not exert pressure on Arvind's working capital cycle. Arvind Lifestyle Brand (ALBL) has higher inventory at 126 days and higher receivables at 101 days (compared to that of 116 days and 75 days for Arvind's standalone operations) in FY11. On account of this ALBL required gross current assets at 72.3% of sales in FY11 as against standalone Arvind's requirement of 60.2% of sales. Higher gross current assets got compensated by higher current liabilities at 45.1% of sales for ALBL compared to 23.7% of sales for standalone Arvind. Following higher current liabilities, ex-cash working capital for ALBL was lower at 25.8% of sales compared to 35.4% of sales for standalone Arvind in FY11. Arvind Retail (ARL) had negligible receivables, while higher inventory of 113 days was compensated by higher creditor days of 87 days in FY11. On the back of strong credit period, its ex-cash working capital stood at 9.2% of sales in FY11 against 35.4% for standalone Arvind. B&R business witnessed ex-cash working capital at 24.2% of sales compared to 32.4% of sales for standalone Arvind in FY11.

Arvind has already taken measures to improve the inventory turnover of its B&R business, the effect of which would be visible in FY13/14. Earlier, Arvind was monitoring the performance of each brand, but it has now changed the strategy and clubbed all its brands under various categories like youth, men formal, sportswear etc. Based on this strategy, the company can focus on growth of a particular category and improve the performance of a weak brand in this category by introducing fast moving designs of a brand into other brands of the same variety.

Earlier, each store/outlet was maintaining inventory details and was responsible for re-stocking of its inventory, which reduced inventory turnover. Currently, Arvind is carrying out centralised monitoring of inventory at all its stores and a central team would take decisions to transfer slow-moving inventory in a store to other stores and also re-stock inventory across stores. On account of lower working capital requirement for the B&R business as compared to standalone business and with multiple levers to improve the working capital cycle of the B&R division as the business evolves, we don't foresee higher share of the B&R business exerting pressure on consolidated working capital cycle of the company.

Exhibit 16: Working capital trend of various businesses

	FY10	FY11	FY10	FY11	FY10	FY11
(no of days)	ALBL		ARL		Arvind standalone	
Inventories	95	126	114	113	77	116
Debtors	83	101	1	5	66	75
Loan and advances *	36	40	25	33	63	39
Gross current assets (as % of sales)	***59.3***	***72.3***	***38.5***	***40.7***	***56.2***	***60.2***
Creditors	63	80	98	87	62	67
Other liabilities	51	87	20	29	13	27
Provision	1	2	1	1	1	1
Current liabilities (as % of sales)	***30.8***	***45.1***	***32.1***	***31.2***	***19.1***	***23.7***
Net current assets (as % of sales)	***28.5***	***25.8***	***5.8***	***9.2***	***37.1***	***36.5***
Ex-cash working capital (as % of sales)	*26.9*	*25.8*	*5.8*	*9.2*	*35.2*	*35.4*

Note: Loan and advances exclude advances to subsidiary

Source: Company, Nirmal Bang Institutional Equities Research

Lower debt, interest rates and improved credit rating to drive profitability

Arvind had a high D/E ratio of 1.3x in FY11, but the company re-valued its land during the year which increased its net worth by Rs2,301mn, adjusting for which the ratio stood at 1.6x with a weak interest coverage of 1.5x. We expect the adjusted D/E ratio to reduce from 1.6x in FY11 to 0.6x in FY14E on account of the following: 1) Lower working capital requirement, 2) Strong business profit/cash flow, 3) Money received from sales/developmental profit of real estate, and 4) Lower capex likely from FY13.

The company divested its 40% stake in VF Arvind Brands Pvt Ltd to VF Mauritius for Rs2,570mn (Rs2,270mn after tax) in November 2011 and used the proceeds to retire high-cost debt. Debt, in absolute terms, would also decline by 26.5% to Rs16,241mn in FY14E from Rs22,111mn in FY11. The company would also be a beneficiary of declining interest rates in FY13/14. With improvement in cash flow and reduction in D/E ratio, the company has already witnessed improvement in its credit rating in 3QFY12. We expect the credit rating of the company to improve further during 1HFY13 following more debt reduction and improving D/E ratio. On the back of lower debt, declining interest rates and improved credit rating, the interest coverage ratio should improve to 3.3x in FY14E from 1.5x in FY11.

Following poor demand and higher forex loss, the company was in the red in FY09, lifting the D/E ratio to a high level of 2.2x with gross debt of Rs23bn. The company had interest coverage ratio of mere1.5x in FY11/12. On account high debt, its net profitability was vulnerable to the adverse denim cycle, economic slowdown and high interest rates. As the company has made strong efforts to reduce its D/E ratio to the normal level since FY10, we expect a re-rating of its valuation once the fruits of its debt reduction efforts are visible over FY13-14. **Interest costs, which accounted for 6.4%/7.2% of sales in FY11/12E and 68.5/66.7% of EBIT should come down to 3.3% of sales and 30.2% of EBIT in FY14E and improve its net profit margin. Even though we expect a 20bps decline in operating margin in FY13E on the back of lower interest costs, net profit margin should improve by 123bps in FY13E.**

Exhibit 17: Declining D/E ratio

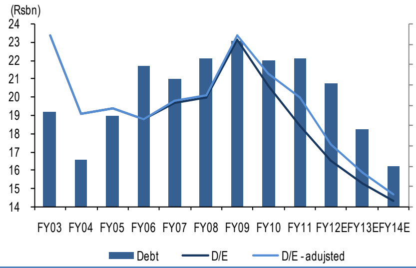


Exhibit 18: Better interest coverage

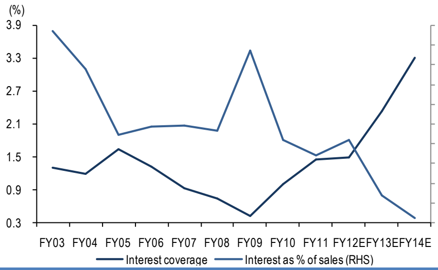
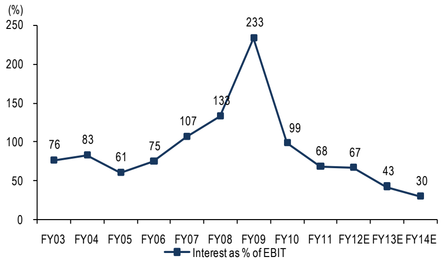


Exhibit 19: Declining interest costs



Source: Company, Nirmal Bang Institutional Equities Research

Branded business to grow at a healthy pace

ALBL (Arvind Lifestyle Brand) markets six licensed premium brands like Arrow, US Polo, Izod, Energie, Cherokee, Gant etc through its 329 stores spread over an area of 0.303mn sq ft. Arvind is one of the few companies which have a such strong portfolio of licensed brands in India. **In order to capitalise on its strong brand portfolio, the company aggressively expanded its retail reach by 59.7% to 0.303mn sq ft in 3QFY12, thereby driving revenue by 43% YoY to Rs1,660mn. The company witnessed strong like-to-like growth of 16.2% in ALBL.** The company increased its revenue by 37.4% CAGR over FY09-11 to Rs4,160mn in FY11 on the back of aggressive expansion, which increased its retail area by 30.1% CAGR to 0.215mn sq ft in FY11. There are multiple drivers which would drive branded business in future like expanding the distribution reach of its brands, launching new brands to occupy vacant segments and expansion of brand categories.

Expanding the distribution reach of brands

The company is extending its distribution reach by setting up new outlets, occupying a dominant position in menswear department of department stores, and through international expansion. The company increased its retail reach from 139 outlets in FY10 to 329 outlets in 3QYF12. It added 42 new outlets in 3QFY12 alone with an average area of 855 sq ft per outlet. ALBL has an aggressive plan to increase its retail space from 0.215mn sq ft in FY11 to 0.320mn in FY12E and to 0.5mn in FY14E by setting up exclusive brand outlets for Arrow, US Polo, Club America, Flying Machine and other brands. Various brands of ALBL occupy 30% of the space of menswear department of department stores like Lifestyle, Shoppers Stop, Central, Globus etc. On account of its strong occupancy, the company can command better control over competing brands as regards display, pushing up new brands and all other aspects.

Exhibit 20: Arvind occupies 30% space of menswear department of department stores

Categories in menswear department	No of brands stocked	No of Arvind brand	*% share*
Super premium brands in select stores	8	2	*25*
Formal	7	2	*28*
Sportswear	7	3	*43*
Denim	8	2	*25*
Total	**30**	**9**	***30***

Source: Company, Nirmal Bang Institutional Equities Research

International expansion

The company was able to extend its licensing out of India for brands like Arrow, Cherokee etc. It introduced the Arrow brand in Splash, the number one department store chain in the Middle East, adding 70 new doors for the brand. ALBL has also launched the Arrow brand in South Africa. Cherokee license was also extended to the Middle East. The company is planning to take its own brand, Flying Machine, overseas. With the geographic diversification, ALBL is better placed against cyclicality/slowdown in any particular region.

New brands to occupy vacant segments

To strengthen its position in the premium menswear segment, the company launched US Polo Associated brand in April 2010, which dominated the market right from the beginning, and Izod brand in March 2010. With the launch of these brands together with Arrow, the company substantially strengthened its premium menswear portfolio. Arrow accounted for over 50% revenue of its branded garment sales, and the company enhanced its target market by including sportswear and women's wear categories. Arrow and Flying Machine continued their upward journey, growing 51% and 39%, respectively, in FY11. Gant, the bridge to luxury brands, posted a growth rate of more than 100% during the year. The company successfully launched and positioned yet another brand, Engerie, in FY11.

It is planning to launch two new international brands in the youth (Mossimo under Mega Mart format) and women's space (Elle) in the premium category next year (FY13). On account of its largest manufacturing facility, best product quality and deeper understanding of the Indian market, Arvind is the most preferred partner in India for collaboration for any overseas brand/player. As ALBL occupies 30% space in menswear department of department stores, it gets favorable treatment in launching new brands compared to competitors

Exhibit 21: Brand portfolio

Categories	Men – Formal	Men – Sports	Youth	Women
Bridge to luxury		Gant	Energie	Gant
Premium brands	Arrow, US Polo	Arrow Sport, Izod, US Polo	Flying machine, **Brand X**	Arrow, **Brand Y**
Value retail	Mega Mart			

Source: Company, Nirmal Bang Institutional Equities Research

Expansion of brand categories

In order to extract more out of the same brand and drive same-store growth, the company is extending its brands. It launched leather goods under the Arrow brand in September 2010 and footwear in February 2011. It also launched footwear under the Flying Machine brand in September 2010. Similarly, it capitalised the strength of US Polo brand by launching footwear in September 2010, luggage in December 2010 and kids' garments in February 2011. On account of these brand extensions, we expect Arvind to increase average revenue per sq ft.

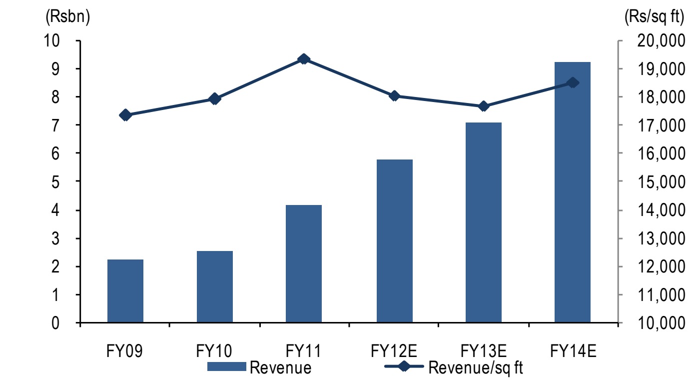
Exhibit 22: Brand extension and timeline

Brand	Category extension	Launch timeline
Arrow	Leather goods, footwear	September 2010, February 2011
Flying Machine	Footwear	September 2010
US Polo Assn.	Kids, footwear, luggage	February 2011, September 2010, December 2010
Izod	Active wear	To be finalised

Source: Company, Nirmal Bang Institutional Equities Research

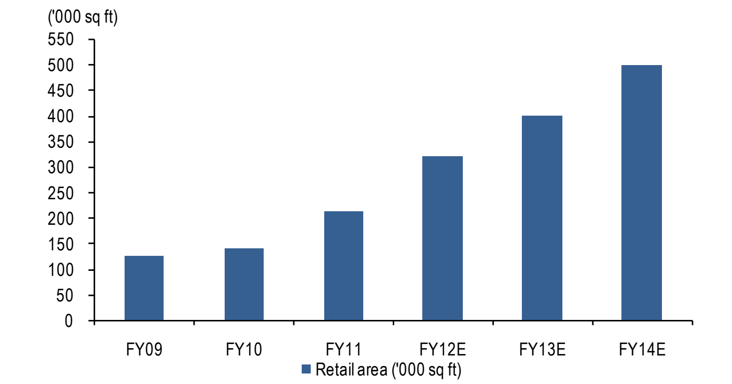
The company increased its ALBL revenue by 37.4% CAGR over FY09-11, to Rs4,160mn in FY11, on the back of aggressive expansion which increased its retail area by 30.1% to 0.215mn sq ft in FY11. **We expect ALBL to increase its retail reach by 32.6% CAGR over FY11-14E to 0.5mn sq ft. There are multiple drivers which would boost branded garment business in future like expanding the distribution reach of its brands, launching new brands to occupy vacant segments and expansion of brand categories. We expect net revenue to show 30.6% CAGR over FY11-14E to Rs9,271mn.**

Exhibit 23: Aggressive expansion to drive revenue



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 24: Rising retail reach



Source: Company, Nirmal Bang Institutional Equities Research

Capitalising on brand JVs

Apart from exclusive strength of the six brands discussed above, the company formed two joint ventures, VF Arvind Brands Pvt Ltd (VFABPL) in September 2006, and Arvind Tommy JV. VFABPL, with Arvind and VF Mauritius holding 40% and 60% stake, respectively, is engaged in the marketing of products under the brands Lee and Wrangler. VFABPL reported revenue of Rs2,840mn (Arvind's share Rs1,136mn) in FY11. In line with the terms of the JV formed in September 2006, Arvind exited from the venture in November 2011 by selling its 40% stake to VF Mauritius for a cash consideration of Rs2,570mn, valuing it at ~2x sales and ~17x EV/EBITDA on trailing basis. The company utilised the cash proceeds to repay high-cost debt. The Arvind Tommy JV, with 50% holding by each partner, is engaged in the marketing of products under the brand Tommy Hilfiger. The JV reported revenue of Rs800mn in FY11. We expect the Arvind Tommy JV to show 20% CAGR, but on account of the exit from VFABPL, revenue from its brand JVs would decline 23.4% to Rs691mn over FY11-14E.

Rapid roll-out of Mega Mart Hub and Spoke model

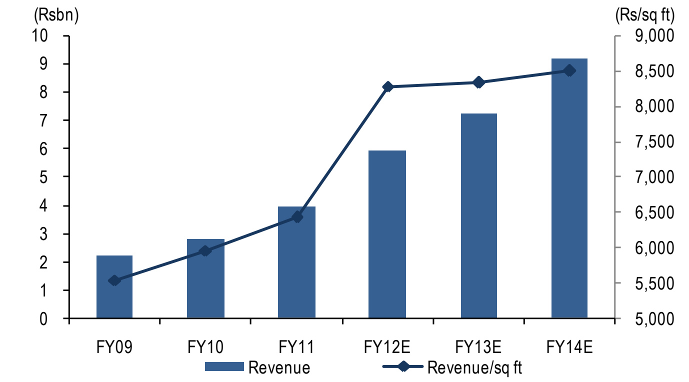
Currently, Arvind has a portfolio of 21 brands comprising 14 owned brands, 6 licensed brands and 1 joint venture brand, making it the pioneer in the branded retail business in India. Its strong portfolio of 14 own brands includes Newport University, Elitus, Mea Casa, DODGE, Bay Island, Donuts, Colt, R&T, Flying Machine, Excalibur, Ruggers, Karigari etc. Most of these brands cater to the value retailing segment. In order to push its brand, the company ventured into the concept of Mega Marts in FY09 where all of its owned brands are marketed. In order to attract customers and increase footfalls, the company provided discounts on its licensed brands like Arrow, Lee, US Polo etc. Over a period, the concept was widely accepted by clients and the company had 219 Mega Mart stores as of end 3QFY12, up from 117/143 stores in FY09/10. Its retail reach, in area terms, increased by 24.1% CAGR over FY09-11 to 0.617mn sq ft in FY14 from 0.401 mn sq ft in FY09. Revenue showed 33.7% CAGR over FY09-11 to Rs3,970mn in FY11 from Rs2,222mn in FY09. Out of total 200 Mega Mart stores in FY11, the company opened ~57 stores in FY11 alone. Profitability of new outlets is relatively low initially and it will take 1.5-2 years to stabilise these outlets, as a result these stores would also report better profitability by FY13.

Mega Mart stores get an advantage over competitors like the Loot, Brand Factory, etc on the back of in-house sourcing of various brands. Being the owner/licensee and manufacturer of many brands, Arvind has the flexibility to sell slow moving/older but popular stocks of its premium collection at a discount and attract customers, who end up getting value for money through the brands owned by the company.

In order to roll out Mega Marts nationwide, Arvind is following the Hub and Spoke model, whereby it would set up large format Mega Marts in Tier-I towns offering over 200 brands at a discount under one roof, thereby driving brand visibility and also managing the inventory to support other small format stores. The company plans to up small neighborhood stores in Tier-I towns and own stores in Tier-II and Tier-III towns, while setting up franchisee stores in Tier-IV towns.

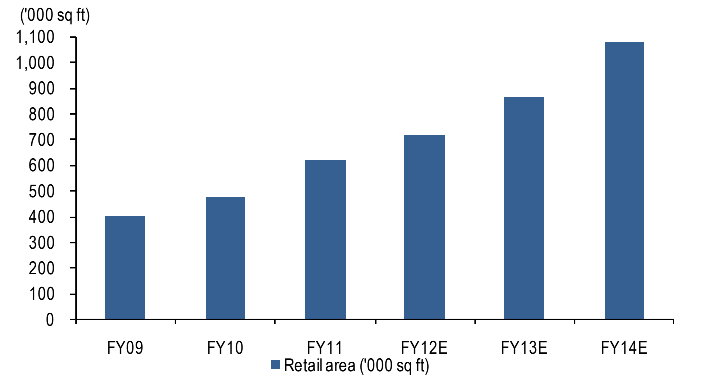
As per the management, the company is planning to add 0.3mn sq ft every year, leading to incremental revenue of Rs2.5bn apart from like-to-like growth. As the company's sales comprise value-for-money products under Mega Mart, its volumes are highly sensitive to price hikes. With the imposition of 10% excise duty in the Union Budget 2011-12 and increase in cotton prices, selling prices were increased in the 9MFY12 period and as a result, the company witnessed poor like-to-like growth of 4.7% in 3QFY12 against 21% in 1HFY11. With softening of cotton prices by 40.5%% over March 2011 to August 2011, the company has been able to procure cotton (during the cotton production season October 2011 to February 2012) at lower prices for FY13. Following lower cotton prices, garment prices have already started declining, thereby propelling volume growth from 4QFY12 onwards. **We expect the company to increase its retail reach by 20.5% CAGR to 1.08mn sq ft over FY11-14E. On the back of aggressive retail penetration, we expect ARL's net revenue to show 32.3% CAGR to Rs9,188mn in FY14E from Rs3,970mn in FY11.**

Exhibit 25: Aggressive expansion to drive revenue



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 26: Rising retail reach



Source: Company, Nirmal Bang Institutional Equities Research

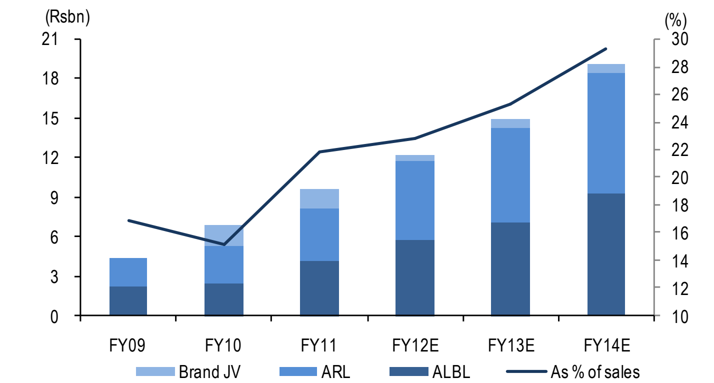
Focus shifts from BTB to BTC

From a denim producer for its corporate clients, Arvind is turning into a brand power house catering to consumers directly through various JVs, exclusive licenses, own brands and sales through a wide network of exclusive brand outlets, shop-in-shop outlets and aggressive expansion of its own Mega Mart stores. Currently, the company has a strong portfolio of 21 brands, both owned and licensed. This will span multiple channels and price points, with each brand appropriating sharp and differentiated consumer proposition. Arrow is the lead brand in the premium segment with its positioning as the best-in class style for premium consumers. Excalibur brand addresses young executives' need for dressing solutions.

Flying Machine brand is being positioned as the platform of 'Youth Expression' with a vision to grow it into an iconic youth brand. Newport is clearly positioned as a 'campus wear' brand for college students seeking 'affordable fashion'. Brands in mass premium channels are sold across exclusive outlets, department stores, cash-and-carry, multi-brand and factory outlets. Ruff and Tuff is the lead brand in the mass segment and is largely merchandised through the emerging channel of hypermarkets. The company's share in the mass segment will rise further by offering private label solutions to hypermarkets.

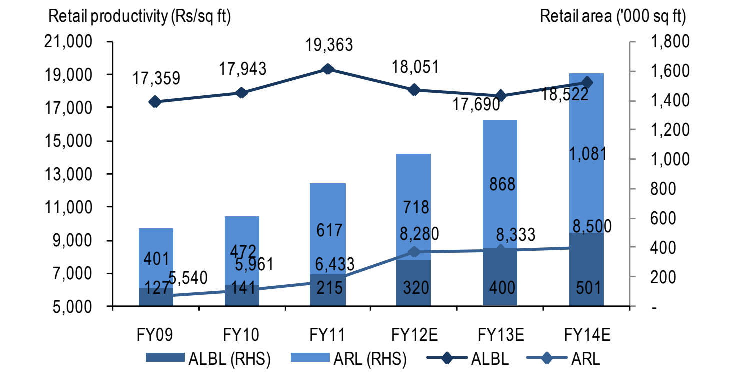
Its B&R business (along with JVs) contributed 27% to its consolidated revenue in 3QFY12 from 24% in 3QFY11 (excluding VF Arvind JV). The company sold its 40% stake in VFABPL to JV partner VF Mauritius Holding and as a result, contribution of the B&R division reduced from 29% in 2QFY12 to 27% in 3QFY12. We expect, the company to increase its retail area by 23.9% CAGR from 0.832mn sq ft in FY11 to 1.581mn sq ft in FY14E at a cost of Rs3.5bn. **Aggressive retail expansion, growth through multiple drivers like expanding the distribution reach of brands, launch of new brands to occupy vacant segments and expansion of brand categories would increase the share of the B&R division to 32.7% in FY14E from 27% in 3QFY12. We expect revenue from the B&R division (including brand JVs) to grow 25.6% to Rs19,150mn over FY11-14E.**

Exhibit 27: Good growth in brands & retail division's revenue



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 28: Retail productivity

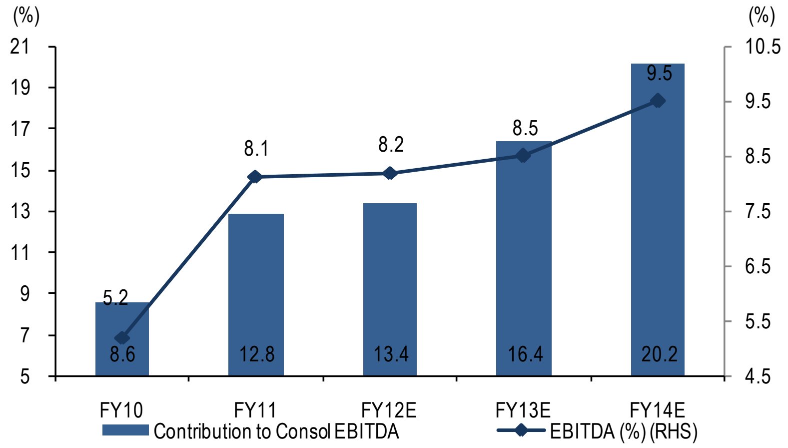


Source: Company, Nirmal Bang Institutional Equities Research

B&R division's margins to improve

Arvind has gradually improved its B&R division's margin (along with JVs' margins) to 8.1% in FY11 from 5.2% in FY10. The company opened ~86 Mega Mart stores in the FY11 alone. For any store, it takes 1.5-2.0 years to break even and hence profitability would rise over FY12/14 once the margins of these outlets improve. Even after adjusting the negative impact of new outlets, which would be operating at a lower margin initially, strong improvement in existing outlets would pull up the B&R division's consolidated margin. On account of economies of scale, we expect advertisement costs as a percentage of sales to reduce from ~6% in FY11 to ~4.5-5% in FY14E. With stabilisation of cotton prices at a lower level, retail prices of garments have started declining which would support volume growth. In addition, the company would get the benefit from bulk sourcing of goods and better utilisation of its existing distribution network. We expect its B&R division's margins to improve by 140bps from 8.1% in FY11 to 9.5% in FY14E. On account of lower garment prices and high-cost raw material inventory (cotton), margins would decline in 4QFY12, but with the high-cost inventory getting exhausted in 4QFY12 itself the company is likely to get the benefit of low-cost inventory for entire FY13, thus driving back profitability from 1QFY13 onwards. **Strong sales and higher margin would drive the B&R division's RoCE from 12.9%/12.8% in FY11/12 to 14.0% in FY14E and in addition the division's contribution to consolidated EBITDA should increase from 13.7% in FY11 to 20.2% in FY14E, which should lead to a re-rating of Arvind share price.**

Exhibit 29: Improving brand and retail division's margins



Source: Company, Nirmal Bang Institutional Equities Research

Land monetisation

Arvind, which has a large land bank of ~500 acres (current value ~Rs10bn i.e. Rs39/share), is planning to monetise these assets, either through developing land parcels or via joint ventures with established players or by selling land parcels in bits and pieces. The company, in June 2010, formed a JV with the Safal Group to develop 1mn sq ft and offer 1,200-1,500 residential units over next the two-three years. In May 2011, it formed another JV with Tata Housing to develop 135 acres (9mn sq ft) over a period of five-six years into an integrated township on the outskirts of Ahmedabad. **According to the management, the total project revenue would be ~Rs20bn over the next five-six years (out of which Rs7.5bn would be booked in Phase I). Tata Housing has valued the land parcel of 135 acre at Rs2.5bn and for transferring 50% of its stake to Tata Housing, Arvind would receive Rs1.25bn towards the cost of the land and the JV would develop 9mn sq ft and share future revenue and construction costs. At an average realisation of Rs2,500/sq ft the JV would receive revenue of Rs22.5bn over five-six years and after taking into account the construction cost of Rs1,200 per sq ft and discounting net cash flow over a life span of six years, we have valued the JV at Rs7bn. As Arvind has a 50% stake in the JV, the value of its stake would be Rs3.5bn or Rs14/share.**

The company expects revenue of ~Rs2bn from real estate JVs in FY13 only, which would help in reducing its debt. As per the management, the current value of its land assets after development would be around Rs10bn or Rs39 per share. On account of the subdued economic environment and likely delay in execution/project launch, we have valued it at 33% of net asset value of Rs39. Timely monetisation of land parcels, as and when it happens, can reduce our 66.7% discount to NAV and would increase our target price by that amount.

Exhibit 30: Details of land bank

Location	Area (Acres)	Plan	Expected cash flow (Rsmn)	Cash flow realised (Rsmn)
Moti-Bhoyan, Gandhinagar (near Ahmedabad)	135	Township (JV with Tata Housing)	5,690	530
Khokra, Ahmedabad (1/3rd portion)	17	Land sale	470	470
Khokra, Parishkar, Ahmedabad (1/3rd portion)	17	Residential and commercial space (JV with B Safal)	870	470
Khokra, Ahmedabad (1/3rd portion)	17	Residential and commercial space	1,250	-
Naroda, Ahmedabad	35	Residential and commercial space	5,570	-
Jethlaj, Gandhinagar (near Ahmedabad)	220	Currently under planning	1,640	-
Bangalore	0.214 mn sq ft	Commercial	490	-
Others	-	-	750	-
Total	**441**		**16,730**	**1,470**

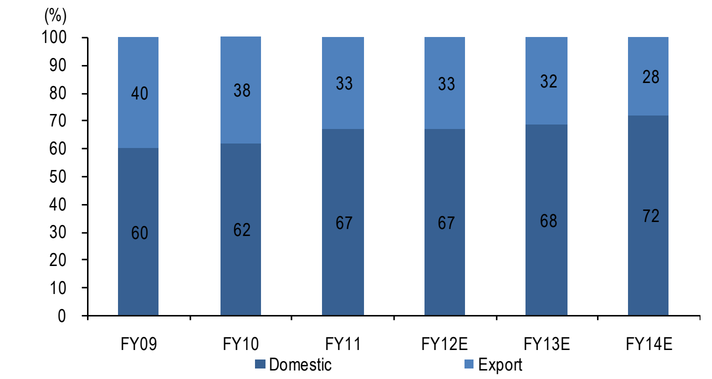
Source: Company

Rising share in domestic business

Arvind started its business of manufacturing denim fabric for marquee overseas clients. With the over-supply situation for denim fabric in FY06-07, its EBITDA margin declined from 21.6% in FY05 to 12.3% in FY08. Global meltdown, which led to slowdown in key markets of the US/EU led to margin falling to 10.9% in FY09, the lowest since FY02. In addition, higher overseas exposure made it vulnerable to forex fluctuations. On back of poor demand and higher forex loss the company made net loss of Rs994mn in FY09.

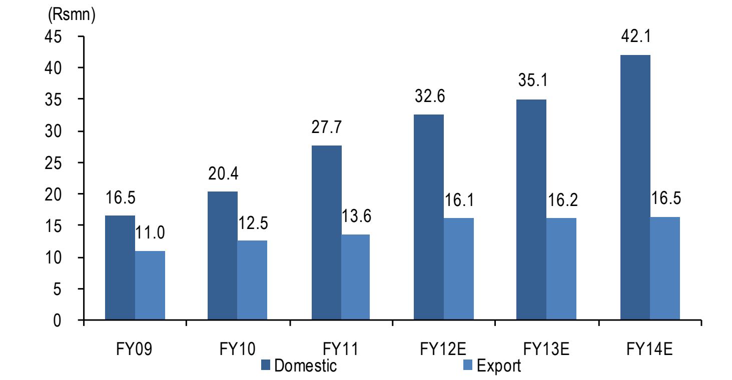
With its aggressive expansion plan for the B&R division and increased focus on Indian market, share of domestic revenue increased to 67% in 3QFY12 from 62% in FY10. On account of higher domestic sales, the company would be relatively less impacted from the US/EU slowdown compared to FY08-10. Denim export volume declined from 32mn metres in the 9MFY11 period to 29mn metres in the 9MFY12 period, which was more than compensated by strong domestic denim sales volume, which increased from 39mn metres to 42mn metres over the same period. Strong domestic volume was on account of increased market share of Arvind from clients like Levis, Lee, Wrangler, Pepe etc. **Following lower overseas volume, higher domestic sales of denim fabrics and existing share of the B&R division's business, the share of domestic business would increase from 67% in 3QFY12 to 72% in FY14E. Higher domestic sales would reduce volatility in profitability on account of forex movement, global issues etc, which would drive up valuation.**

Exhibit 31: Rising share of domestic revenue



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 32: Local growth to compensate low overseas revenue



Source: Company, Nirmal Bang Institutional Equities Research

Better utilisation and product mix to improve textile margin

Arvind operated its denim manufacturing capacity at ~87% in 3QFY12, which is expected to go up to 90% by 4QFY12 and to 94%/97% in FY13/14E, respectively. The company is operating its shirting and khaki capacity at ~100% currently. As Arvind is operating its shirting and khaki facility at full capacity and denim utilisation capacity is slated to touch the optimum level in FY13, the company is shifting its product mix towards more value added products, which would increase the margin of the textile division and provide some cushion against the expected fall in margin in 1HFY13.

Profitability of denim fabric players to be under pressure in 2HFY12/1HFY13E

CRISIL Research expects denim demand to show 7% CAGR over 2010-14E, led by domestic demand. Denim fabric capacity is expected to show 5% CAGR, from 600mn metres to 730mn metres over 2010-14E. As a result, capacity utilisation rate is likely to firm up to 80% by 2014E. However, following poor demand and capacity utilisation rate, the margin may be under pressure in 2HFY12. With cotton prices declining by 40.5% from a peak of Rs168/kg in March 2011, fabric and garment prices have started easing. However, on account of weak sales during Diwali festival, most of the retail outlets have high-cost inventory which needs to be cleared. Lower garment prices and higher raw material costs would exert pressure on margins in 2HFY12 for denim fabric players and other retailers. We expect Arvind to witness pressure on margins in 4QFY12.

However, once the high-priced inventory is cleared, the effect of lower cotton prices and the resultant lower garment prices would be visible in the spring season i.e. March 2012 onwards. Lower garment prices would drive volume and thereby capacity utilisation rates of denim fabric manufacturers and also of other textile manufacturers. Lower cotton prices and higher capacity utilisation would increase the margins of Arvind in 2HFY13/FY14E.

US demand expected to bounce back

The US imported 218mn dozen of denim garments in CY10 from countries like China, Bangladesh, Mexico, Vietnam, Cambodia, Pakisthan, India etc. Imports of denim garments have shown a CAGR of 6% over CY00-07 to 210.6mn dozen. Following global meltdown, there was a slowdown in denim consumption and as a result, import volume declined 3.5% in CY08 and 3.2% in CY09, but again bounced back in CY10 and registered a growth of 10.8%. With the economic crisis worsening in the US, the imports of denim garments declined 8.7% in YTD until October 2011. Following declining import volumes, most of the players including Arvind have reported lower export volumes.

Arvind's denim export volume declined 9.4% to 29mn metres in the 9MFY12 period. As witnessed in CY08/09, we expect US import volume to remain muted in 1HCY12 and then bounce back from 2HCY12. We expect volume growth to remain muted in 2HFY12/1HFY13 for Arvind and as a result, the company should report flat growth in 4QFY12 but volume and profitability should bounce back gradually from 2HFY13. As a result, we expect the operating margin of the textile division to decline 70bps to 17.1% in FY13E and after that improve 60bps to 17.7% in FY14E. This should lead to consolidated margin dropping 20bps in FY13E and improving by 40bps in FY14E. We believe the subdued export volume is already factored in the share price, but with revival in demand and profitability the valuation should rise gradually.

Exhibit 33: Growth in US denim imports

(%)	CY96	CY97	CY98	CY99	CY00	CY01	CY02	CY03	CY04	CY05	CY06	CY07	CY08	CY09	CY10	CY11 (YTD)
World	3.9	16.6	15.3	10.4	13.6	1.3	10.9	10.1	(1.5)	14.7	4.5	2.6	(3.5)	(3.2)	10.8	(8.7)
China	(15.7)	9.9	(2.8)	(15.4)	12.8	20.9	2.9	(10.3)	11.9	334.1	13.2	16.5	(1.8)	58.1	26.7	(16.1)
ASEAN	0.6	8.9	28.1	25.9	(5.0)	1.7	53.4	47.5	(18.6)	29.8	27.1	12.5	2.0	(15.4)	12.4	(7.3)
Bangladesh	3.1	29.7	(2.1)	18.6	4.0	2.9	18.5	(20.1)	20.9	102.5	62.7	21.1	23.8	7.7	8.3	4.7
Mexico	33.7	33.4	30.0	19.4	16.0	(9.5)	0.6	(11.3)	0.7	(13.7)	(15.7)	(9.8)	(10.5)	(12.0)	4.5	(9.4)
Vietnam	-	(22.9)	1.1	11.2	508.1	(16.5)	3,004	210.1	(44.1)	7.3	34.1	42.5	13.1	(3.3)	13.4	(12.2)
CBI	1.5	20.7	5.7	0.1	7.6	(1.6)	2.1	9.4	3.5	(12.8)	(16.2)	(12.5)	(17.3)	(20.2)	0.2	0.9
Indonesia	39.7	(0.9)	8.0	10.6	(24.0)	33.6	(0.2)	4.3	12.7	96.2	58.1	4.5	(2.5)	(3.7)	14.9	0.9
CAFTA-DR	1.5	22.1	5.2	0.9	9.2	(1.7)	3.1	8.6	3.8	(12.0)	(15.3)	(12.9)	(18.4)	(22.4)	1.3	(2.5)
Cambodia	-	-	259.1	63.5	2.5	(11.7)	44.4	23.5	2.5	35.2	13.8	31.3	2.4	(26.5)	20.9	(7.2)
Pakistan	9.1	14.9	(5.5)	37.1	21.7	(2.4)	28.3	7.9	10.3	67.4	26.6	19.3	5.5	(12.9)	2.3	(0.2)
India	(0.1)	1.8	(1.3)	4.8	17.0	2.7	37.8	(2.5)	36.2	158.1	0.5	3.1	2.4	(5.9)	(16.3)	(5.0)

Source: Otexa, Nirmal Bang Institutional Equities Research

Future growth drivers

Fabric retailing

Considering the huge opportunity in fabric retailing business, Arvind started focusing on it since FY09. In just two years, it opened 850 shop-in-shops and 40 exclusive Arvind stores. It has a distribution network of 250 distributors selling Arvind fabrics through 25,000 retail shops. The company is planning to increase exclusive stores on franchisee basis to 100 in FY13E.

Ready-to-stitch packs

Arvind also introduced innovative packaging in the form of ready-to-stitch (RTS) packs where the company provides cut fabric piece along with necessary accessories (like zip, buttons etc) with the brand Arvind embossed on them. It would substantially reduce inventory level at retail outlets and also offer multiple designs/collections. In addition, it increases realisation per metre of fabric as compared to selling pure vanilla fabric.

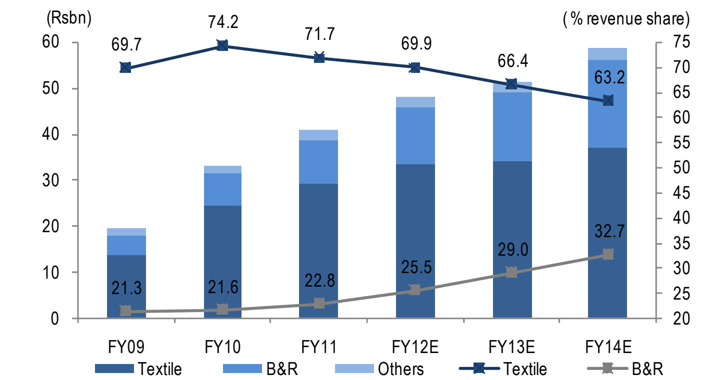
Financials

Arvind has increased its denim capacity by 12.5% from 96mn metres to 108mn metres over FY10-11. Similarly, it increased the capacity of woven fabrics by 9.1% to 72mn metres and as a result, its textiles volume grew 17.1% to 212mn metres in FY11. On the back of aggressive capex, strong demand and higher cotton prices, the company reported 19.9% growth in textile revenue, at Rs29,360mn in FY11. Following an aggressive expansion plan, its B&R division's revenue (including JVs) increased 31.1% to Rs9,350mn, driving consolidated sales by 25.4% to Rs40,897mn in FY11.

The company increased its gross block by Rs16,826mn over FY07-11 to Rs40,729mn, which drove its revenue CAGR by 14% over FY06-11 and by 22.1% CAGR over FY09-11. The company gradually reduced its dependence on denim and textiles. Contribution from its textiles business reduced from 75% in FY10 to 68% in 3QFY12, while contribution from the B&R division (including JVs) increased to 27% in 3QFY12 from 19% in FY10. Following weak demand from the US and India and lower realisation, revenue from the textile division would grow by a mere 1.9% in FY13E. The company is increasing its woven capacity by 38.9% to 100mn metres over FY11-14E. On the back of capacity addition and higher utilisation, the textile division's revenue should grow 8.7% to Rs37,040mn in FY14E from Rs34,076mn in FY13E. We expect Arvind to increase the retail reach of ALBL by 32.6% CAGR to 0.5mn sq ft and that of ARL by 20.5% to 1.081mn sq ft.

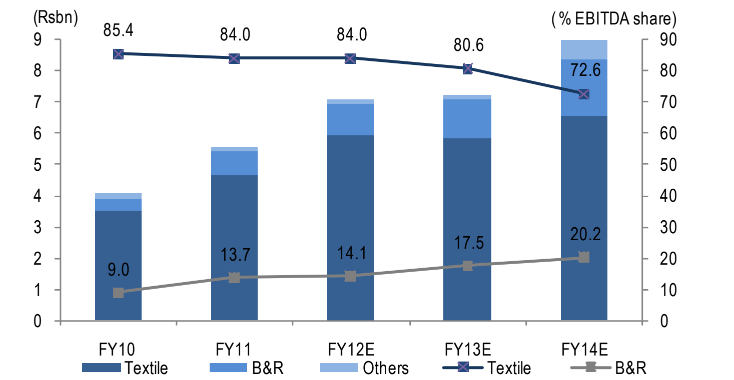
Aggressive retail expansion supported by multiple growth drivers like expanding the distribution reach of brands, launching new brands to occupy vacant segments and expansion of brand categories would enable its B&R (including JVs) division's revenue to show 25.6% CAGR, at Rs19,150mn over FY11-14E and increase its share to 32.7% in FY14E from 22% in FY11. We expect consolidated revenue to show 12.4% CAGR at Rs58,027mn over FY11-14E.

Exhibit 34: Rising revenue share of B&R division



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 35: B&R division's EBITDA to inch up gradually



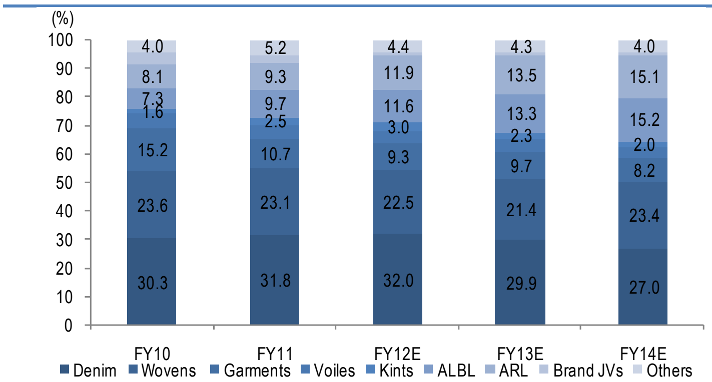
Source: Company, Nirmal Bang Institutional Equities Research

Following over-supply and stiff competition, which was aggravated by global meltdown, operating margin declined from 21.6% to 10.9% over FY05-09. Over this period, the company closed its unviable manufacturing facilities, increased domestic sales, added more customers, increased market share from existing customers and also ventured into B&R business. On the back of these measures, operating margin improved 274bps to 13.6% over FY09-11 and 167bps to 14.6% in the 9MFY12 period. The company reduced the prices of its finished products i.e. garments, but still carried high-cost inventory of the raw material i.e. cotton. As a result, the margins would be under pressure in 4QFY12. Further, with the slowdown in key consuming markets i.e. US/EU and lower domestic demand, the margins would be under pressure in the near term, to the extent of 50bps in 1HFY13E. However, following lower cotton prices, fabric/garment prices would start easing in the spring season (March 2012 onwards) once the high-cost inventory is cleared at retail stores. Lower garment prices should improve domestic demand.

Domestic demand for denim fabric is expected to show 7% CAGR over 2010-14E, as against capacity growth of 5% CAGR from 600mn metres to 730mn metres over the same period. Following subdued demand likely in the near term, the margins of the textile segment should decline by 70bps in FY13E. **However, with revival in demand and lower capacity addition, capacity utilisation of denim fabric manufacturers should improve. We expect the capacity utilisation level of Arvind to increase from 87% in 3QFY12 to 97% in FY14E. This would increase the margin of textile division by 60bps in FY14E.** However, we expect the textile division's margin to decline by 70bps in FY13E to 17.1%, but increase by 60bps to 17.7% in FY14E on the back of revival in demand and higher capacity utilisation.

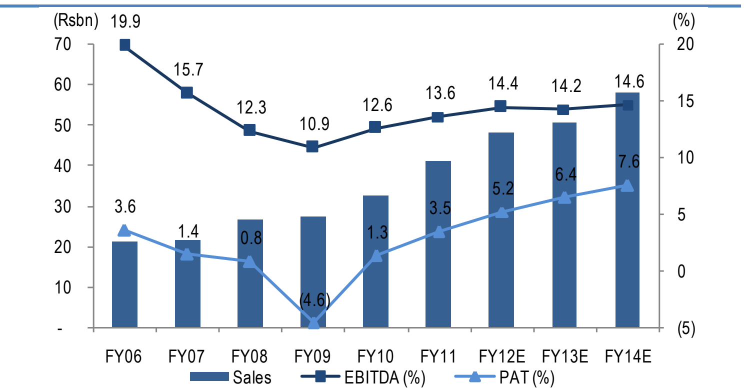
With lease rentals under limits, economies of scale, better bargaining power with suppliers and lower advertisement costs, we expect the B&R division's margins to improve by 30bps in FY13E and by 100bps in FY14E. We expect consolidated margin to decline by 20bps to 14.2% in FY13E, but improve by 40bps to 14.6% in FY14E. **We expect Arvind's debt to reduce 26.5% to Rs16,241mn in FY14E from Rs22,111mn in FY11 on the back of lower working capital, strong cash flow from operations and lower capex, which would reduce adjusted D/E ratio to 0.6x in FY14E from 1.6x in FY11. Lower debt level, better credit rating and declining interest rates would reduce interest costs by 46% to Rs1,896mn in FY14E from Rs3,485mn in FY12E. Interest costs as a percentage of sales should decline from 6.4%/7.2% in FY11/12E to 3.3% in FY14E and drive net profit margin. On the back of lower interest costs, adjusted net profit should show 45.6% CAGR against EBITDA CAGR of 15.2% over FY11-14E, at Rs4,389mn.**

Exhibit 36: Revenue break-up



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 37: Revenue , profitability trend



Source: Company, Nirmal Bang Institutional Equities Research

Quarterly trend

On the back of strong domestic denim sales, higher realisation and aggressive growth of the B&R division, Arvind reported 18.6% YoY growth in sales at Rs11,902mn in 3QFY12. The company increased its B&R division's margin by 30bps to 8.7% and that of textile division's by 110bps to 18%.Operating margin improved by 236bps to 15.1%. On the back of strong revenue growth and improvement in margins, operating profit increased 40.6% YoY to Rs1,797mn. The company incurred forex loss of Rs378mn, reported under the head of interest expenses in 3QFY12 and as a result PBDT declined by 12%. The company received Rs2,450mn from disposal of stake in VF Arvind brand JV, which was reported under extraordinary income in 3QFY12, and adjusting for that net profit increased 8.6% to Rs518mn in 3QFY12.

Exhibit 38: Quarterly financial performance

Y/E March (Rsmn)	3QFY11	2QFY12	3QFY12	*YoY (%)*	*QoQ (%)*	9MFY11	9MFY12	*YoY (%)*
Net sales	**10,036**	**12,557**	**11,902**	***18.6***	***(5.2)***	**28,910**	**36,461**	***26.1***
Raw material & finished goods purchase	4,649	6,105	5,378	*15.7*	*(11.9)*	13,511	17,175	*27.1*
% of sales	*46.3*	*48.6*	*45.2*			*46.7*	*47.1*	
Employee expenses	974	1,116	1,166	*19.7*	*4.5*	2,868	3,351	*16.8*
% of sales	*9.7*	*8.9*	*9.8*			*9.9*	*9.2*	
Other expenses	3,135	3,548	3,561	*13.6*	*0.4*	8,785	10,600	*20.7*
% of sales	*31.2*	*28.3*	*29.9*			*30.4*	*29.1*	
Total expenditure	**8,758**	**10,769**	**10,105**	***15.4***	***(6.2)***	**25,164**	**31,127**	***23.7***
Operating profit	**1,278**	**1,788**	**1,797**	***40.6***	***0.5***	**3,746**	**5,335**	***42.4***
OPM (%)	***12.7***	***14.2***	***15.1***			***13.0***	***14.6***	
Interest	540	955	1,147	*112.6*	*20.1*	1,765	2,941	*66.6*
PBDT	**739**	**832**	**650**	***(12.0)***	***(21.9)***	**1,981**	**2,394**	***20.9***
Depreciation	418	414	404	*(3.5)*	*(2.5)*	1,325	1,228	*(7.3)*
Other income	159	197	343	*116.2*	*74.3*	429	655	*52.5*
Extraordinary income	-	-	2,450			-	2,450	
PBT	**479**	**615**	**3,039**	***534.6***	***393.9***	**1,085**	**4,271**	***293.6***
Tax	2	1	606			1	607	
Effective tax rate (%)	*0.3*	*0.1*	*19.9*			*0.1*	*14.2*	
Adjusted PAT	**477**	**459**	**518**	***8.6***	***12.8***	**976**	**1,569**	***60.7***
NPM (%)	***4.7***	***3.7***	***4.4***			***3.4***	***4.3***	

Source: Company, Nirmal Bang Institutional Equities Research

In line with peers, Arvind decreased the prices of its finished products, but still carries high-cost inventory (of cotton raw material). As a result, operating margin would be under pressure in 4QFY12. Following weak demand from the US and lower domestic consumption, we expect the performance of its textile and retail division to remain muted in 1HFY13, and the margin of textile division to decline by 70bps to 17.1% in FY13, which would reduce consolidated margin by 20bps to 14.2% for the year. However, with revival in demand and soft cotton prices, revenue should grow 14.3% and margins should improve by 40bps in FY14E.

Key concerns

Sharp increase in cotton prices

Cotton prices had increased 113% in March 2011 to Rs168/kg from Rs79/kg in March 2010. Following bumper production, cotton prices corrected 40%, from a peak of Rs168/kg in March 2011 to Rs100/kg in August 2011. We expect cotton prices to remain subdued on account of higher production and lower demand. Following lower cotton realisation relative to alternate crops, if the farmers decide to produce alternate crops, it would reduce cotton production and thereby increase its prices. High cotton prices would increase denim fabric and garment prices, thereby hurting demand. In addition, high cotton prices would increase the working capital cycle of the company and also the D/E ratio and interest costs.

Sharp rupee appreciation

Arvind derives 33% of its sales from export markets and hence any sharp appreciation in the rupee against the US dollar can reduce its realisation as well as competitiveness against Chinese / Bangladeshi players.

Delay in real estate venture

Arvind has a land bank of ~500 acres valued ~Rs10bn and in order to get better value from its assets, the company formed JVs with Tata Housing and Safal Group to develop 135 acres and 15 acres, respectively. The JV with Tata Housing is to develop a township having an area of 9mn sq ft over the next five years. Cash flow from the project depends upon successful execution by meeting the deadline and demand for residential/commercial property in that region. Any slowdown in demand or delay in execution of the projects can impact cash flow, which can hurt the de-leveraging plan of Arvind. The company has not formed any JV for the balance land parcel and has also not identified any buyer for that and as a result, any delay in disposal of land can impact its capex plan or de-leveraging plan. We have not considered any cash flow from its real estate venture in our financial estimates and considered only 33% of its net asset value in our target price.

Competition from branded apparel segment

Players like Kewal Kiran, Wills, Raymond etc are also aggressively expanding their retail reach. Many new international brands are planning to enter the Indian market. With foreign direct investment expected in multi-brand retail, these brand entities may set up their outlets in India, thereby providing stiff competition to Arvind.

Threat from Bangladesh/Chinese players

Off late, Bangladesh has emerged as a low-cost supplier of textile products to the US and EU and has gained strong market share. Any further increase in the market shares of Bangladesh/Chinese suppliers can come at the cost of Indian players like Arvind, hurting their revenues and margins. As the export markets' share in Arvind's revenue is on a declining mode, higher competition from Bangladesh/Chinese players would have limited impact on the company. Arvind is also planning to set up a facility in Bangladesh, once gas allocation is made to the company and this would also reduce its production costs and increase the competitive advantage.

Further slowdown in EU/US or domestic demand

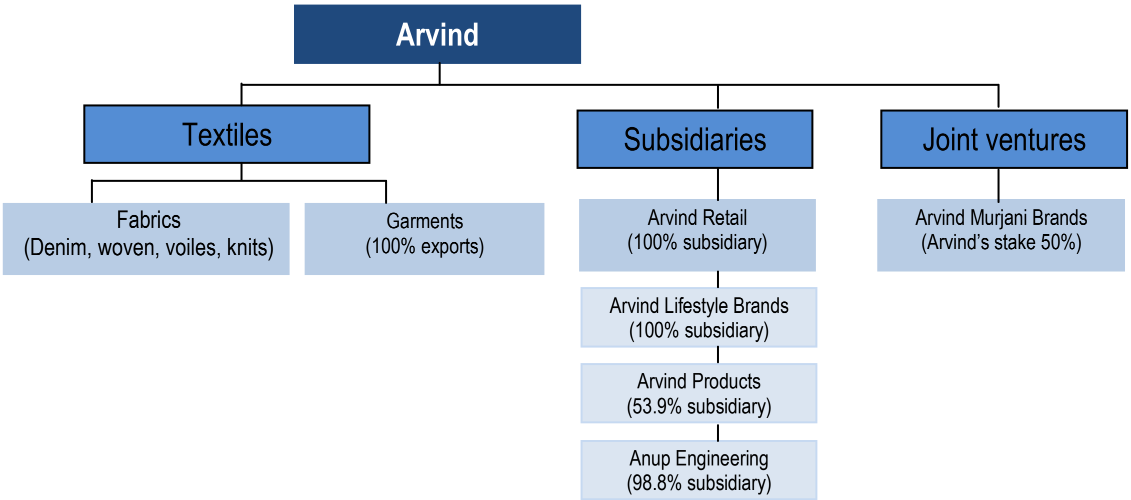
Demand for textile products from the EU/US has been subdued, which is already factored in sales volume of Arvind and thereby on its share price. Domestic demand has also witnessed a slowdown over the past six months, as witnessed from lower SSG (same-store sales growth) of competitors like Shoppers Stop, Pantaloon, Trent, Westside etc. We believe the market has already factored in near-term slowdown in demand. However, if the demand remains subdued for a longer period in the EU/US as well as in India, them it may hurt volume and plant utilisation level for Arvind, leading to lower profits. We believe that with the reduction in cotton prices, garment prices should decline, which would drive up demand from 2HFY13 in the domestic market.

Company overview

Arvind is one of the largest producers of denim in the world, with an annual capacity of 108mn metres. It is the largest manufacturer, marketer and exporter of textile fabrics and garments in India. The company also has a strong presence in the B&R business with one of the strongest portfolio of brands in the country and Mega Mart, the fastest growing value retail chain.

The company, established in 1931 as Arvind Mills, is the flagship of the Lalbhai Group. It was the first company to introduce the globally accepted fabric - denim - to India in 1986. It is also the largest producer, marketer and exporter of textile fabrics in India with a fabric manufacturing capacity of 84mn metres which includes shirting, voiles, khakhis and knits. Arvind is a preferred supplier to internationally renowned brands like Polo, Armani Exchange, Diesel, Gap, Banana Republic, Calvin Klein, Hugo Boss, Esprit, Zara, Levi's, Miss Sixty, Ann Taylor, Brooks Brothers, Express and Eddie Bauer. Arvind was one of the first companies to get internationally renowned brands to Indian markets, beginning with the Arrow brand in 1993 and since then its brand portfolio has only got stronger. Arvind has an unmatchable brand portfolio comprising in-house and licensed brands in the country with names like Flying Machine, Arrow, Tommy Hilfiger, US Polo, Izod, Gant, New Port, Excalibur etc. In 2008, the company launched its value retail chain Mega Mart. Currently, Mega Mart has emerged as one of the India's largest value retail operating with a retail space of over 0.7 mn sq ft.

Exhibit 39: Business segments



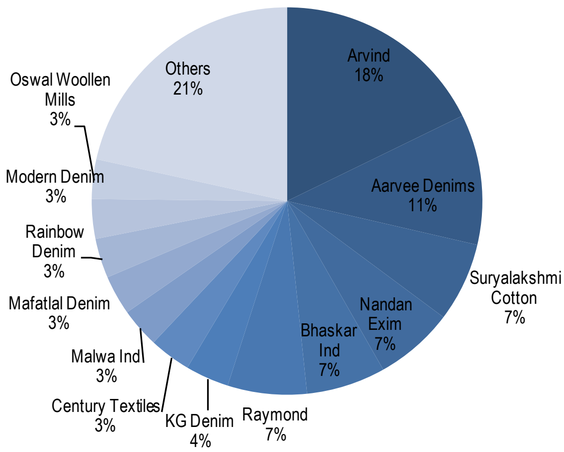
Source: Company

Exhibit 40: Player-wise capacity in FY11 (mn metres)

Capacity			
Arvind	108	Rainbow Denim	20
Aarvee Denims and Exports	66	Modern Denim	20
Suryalakshmi Cotton Mills	40	Oswal Woollen Mills	20
Nandan Exim	40	Blue Blends (India)	18
Bhaskar Industries	40	RSWM	14
Raymond	40	KG Fabriks	12
KG Denim	22	Ashima	45
Century Textiles and Industries	21	Ginni International	10
Malwa Industries	20	Sangam (India)	8
Mafatlal Denim	20	Others	24
Total		**608**	

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 41: Indian denim fabric industry's market share in FY11



Source: Company, Nirmal Bang Institutional Equities Research

Textiles

Denim

Arvind was the first company to introduce Denim in India in 1986 and currently is the largest denim producer in the world with a capacity of 108mn metres per year. The company is a preferred supplier of denim to most reputed denim brands in the world like Miss Sixty, Diesel, Replay, Armani Exchange, Ann Taylor, Hugo Boss, Calvin Klein, Polo Ralph, A & F, Jack & Jones, Levi's, Gap, Zara, Esprit, H & M and Quick Silver. In FY11, the company sold over 96mn metres of denim fabric, of which 47% was exported and 53% was sold in India. We expect the denim volume to show a CAGR of 5.5% over the next two years.

In the domestic market, Arvind has an overall market share of 18%. It supplies ~ 65% of its production to trade channels while the balance 35% is supplied to branded garment players.

Wovens (shirting/khaki)

With a capacity of 84mn metres, Arvind is the largest player of woven fabrics in India in FY12. The company has one of the best customer base, supplying to reputed brands like Banana Republic, Brooks Brothers, Ann Taylor, Hugo Boss, Calvin Klein, Polo Ralph, Eddie Bauer, Express, J Crew, Louis Phillip, Van Heusen, Arrow, Color Plus, Esprit, Paul Smith, and Park Avenue. **In FY11, the shirting segment of the company saw a stellar volume growth of 13%, selling 44mn metres while khaki witnessed an increase of 62% to 21mn metres. This growth was mainly driven by rapid expansion in retail distribution and introduction of innovative products. The company increased its capcity by 16.7% to 84mn metres in FY12 and is increasing further by 19% to 100mn metres in FY14. On back of higher capacity, we expect the volume to show a CAGR of 16.6% over FY2-14E.**

Voiles

With a manufacturing capacity of 38mn metres, Arvind is a market leader in this segment with a market share of around 40%. Arvind has an extensive countrywide distribution network of 250 dealers. In FY11, the company sold 34mn metres of voiles and is expected to consolidate its operations in FY12-14.

Subsidiaries

Arvind Lifestyle Brands (ALBL) and Arvind Retail (ARL)

In FY10, the company de-merged its B&R business into two wholly-owned subsidiaries, Arvind Lifestyle Brands (ALBL) and Arvind Retail (ARL). Currently, Arvind has a portfolio of 21 brands with 14 owned brands, 6 licensed brands and 1 joint venture brand, making it the pioneer in the branded retail business in India. **Arvind also owns India's fastest growing value retail chain Mega Mart under Arvind Retail. In FY11, the branded business witnessed a growth of 64.4% at Rs4,160mn. ARL posted revenue growth of 31.5% at Rs3,970mn. We expect this segment to show 31.4% CAGR over FY11-FY14E, accounting for around 31.5% of the company's turnover.**

Arvind Lifestyle Brands (ALBL)

Arvind had 329 stores, of which ~80% were company-operated and ~20% franchisee-operated at the end 3QFY12. The company currently has retail space of around 303,363 sq ft. **Going ahead, it plans to increase the retail space to 600,000 sq ft by 2014. We expect ALBL to increase its retail space by 32.6% CAGR to 500,000 sq ft over FY11-14E, which would increase its revenue by 30.6% CAGR to Rs9.3bn over the same period.**

Arvind Retail (ARL)

Mega Mart is one of the fastest-growing value retail chains in India with a three-year CAGR of 32.2% over FY08-11. It has a wide offering of over 200 brands under one roof, which are available at attractive discounts all round the year. Arvind currently has 219 stores and is targeting to add 60 stores per year. The company has stores in two formats i.e. small format stores and large format stores. Arvind uses a Hub and Spoke model for opening stores, where it opens a couple of large format stores in Tier-1 cities. Arvind operates self-operated small format stores in Tier-1 and Tier-2 cities and franchisee-operated stores in Tier-3 and Tier-4 towns. **Arvind plans to increase the retail space from 0.698mn sq ft in 3QFY12 to 1.8mn sq ft by 2015E. We expect the company to grow its retail reach at a relatively slower pace of 20.5% CAGR at 1.081mn sq ft by FY11-14E, which would drive its revenue by 32.3% CAGR to Rs9,188mn over the same period.**

(i) Small format stores: These are stores with a size of 3,000-6,000 sq ft. Currently, Arvind has ~213 small format stores, of which ~80% are company-operated and the rest 20% stores are franchisee-operated. EBITDA margin in small format stores is 8-9%.

(ii) Large format stores: These are stores with a size of 40,000- 50,000 sq ft and offer a range of around 200 brands. The ratio of sales of Arvind brands (owned and licensed) to outside brands in these stores is 20:80. Arvind currently has six large format stores. EBITDA margin hovers around 6-7% for these stores. The company plans to add two-three large format stores every year.

Anup Engineering (90.8% subsidiary)

Anup Engineering was a company under the Board for Industrial and Financial Reconstruction (BIFR) which was acquired by Arvind in 1997. Anup, which is into heavy fabrication, is one of the very few companies in the country which have integrated fabrication facilities under one roof. Its range of products includes process equipment, pressure vessels, heat exchangers, columns, centrifuges, chlorine tonners and vessels, expansion bellows etc. The company posted a turnover of Rs1,070mn in FY11.

Joint venture – Arvind Murjani Brands

Arvind Murjani Brands (AMBPL): This is a 50:50 JV between the Murjani Group and Arvind. The JV has an exclusive licence to sell the brand Tommy Hilfiger across India. In FY11, this JV posted a top line of Rs800mn, with Arvind's share at Rs400mn.

Financials (consolidated)

Exhibit 42: Income statement

Y/E March (Rsmn)	FY10	FY11	FY12E	FY13E	FY14E
Net sales	32,612	40,897	48,258	50,768	58,027
Growth (%)	18.8	25.4	18.0	5.2	14.3
Raw material costs	14,708	18,687	21,647	22,875	26,029
Power & fuel	2,506	3,059	3,619	3,808	4,352
Staff	3,381	3,898	4,585	4,823	5,513
Other Manufacturing Expenses	4,501	5,306	6,274	6,600	7,428
Selling and Administration Exp	2,498	2,715	3,185	3,351	3,830
Miscellaneous Expenses	919	1,669	1,979	2,081	2,379
Total expenditure	28,513	35,334	41,288	43,537	49,530
EBITDA	4,099	5,562	6,970	7,230	8,498
Growth (%)	37.5	35.7	25.3	3.7	17.5
EBITDA margin (%)	12.6	13.6	14.4	14.2	14.6
Other income	437	548	627	508	499
Extra-ordinary items		-	2,540		
Interest costs	2,340	2,627	3,485	2,241	1,896
Gross profit	2,197	3,483	6,652	5,497	7,100
Growth (%)	281.4	58.5	91.0	(17.4)	29.2
Depreciation	1,727	1,725	1,747	1,977	2,217
Profit before tax	470	1,759	4,905	3,519	4,883
Growth (%)	(145.7)	274.1	178.9	(28.2)	38.7
Tax	(61)	105	294	246	488
Effective tax rate (%)	(12.9)	6.0	6.0	7.0	10.0
Net profit	531	1,653	4,611	3,273	4,395
Growth (%)	(148.5)	211.6	178.9	(29.0)	34.3
Minority interest	31	5	5	6	6
Extraordinary items	67	228	2,094	-	-
Adjusted PAT	433	1,420	2,512	3,267	4,389
Growth (%)	(134.1)	228.3	76.8	30.1	34.3

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 44: Balance Sheet

Y/E March (Rsmn)	FY10	FY11	FY12E	FY13E	FY14E
Equity	2,320	2,544	2,544	2,544	2,544
Reserves	10,431	14,404	19,010	22,277	26,666
Net worth	12,826	16,948	21,554	24,821	29,210
Minority Int	141	161	166	172	178
Short-term loans	10,455	10,205	10,605	10,105	9,605
Long-term loans	11,570	11,906	10,136	8,136	6,636
Total loans	22,025	22,111	20,741	18,241	16,241
Deferred tax liability	134	216	461	637	881
Liabilities	**35,126**	**39,435**	**42,922**	**43,871**	**46,510**
Gross block	38,360	40,729	44,804	46,521	49,265
Depreciation	14,048	15,454	17,201	19,178	21,395
Net block	24,312	25,275	27,603	27,342	27,870
Capital work-in-progress	579	1,575	717	744	788
Long-term Investments	437	440	440	440	440
Inventories	8,012	12,730	12,272	13,061	14,584
Debtors	4,259	5,012	6,365	6,839	7,654
Cash	597	588	1,104	1,332	1,860
Other current assets	3,899	4,460	5,308	5,584	6,383
Total current assets	16,767	22,791	25,049	26,816	30,481
Creditors	5,265	6,723	7,799	8,224	9,356
Other current liabilities	1,704	3,923	3,089	3,249	3,714
Total current liabilities	6,969	10,646	10,887	11,473	13,069
Net current assets	9,798	12,145	14,162	15,344	17,411
Total assets	**35,126**	**39,435**	**42,922**	**43,871**	**46,510**

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 43:Cash flow

Y/E March (Rsmn)	FY10	FY11	FY12E	FY13E	FY14E
EBIT	2,372	3,838	5,223	5,253	6,281
Inc./(dec.) in working capital	(391)	(2,355)	(1,501)	(954)	(1,540)
Cash flow from operations	**1,982**	**1,483**	**3,722**	**4,300**	**4,741**
Other income	437	548	627	508	499
Depreciation	1,727	1,725	1,747	1,977	2,217
Deferred liabilities	(122)	82	245	176	244
Interest paid (-)	(2,340)	(2,627)	(3,485)	(2,241)	(1,896)
Tax paid (-)	61	(105)	(294)	(246)	(488)
Extraordinary items	(31)	(5)	(5)	(6)	(6)
Net cash from operations	**1,712**	**1,100**	**2,557**	**4,467**	**5,310**
Capital expenditure (-)	(1,296)	(1,383)	(3,217)	(1,744)	(2,788)
Net cash after capex	**416**	**(283)**	**(660)**	**2,723**	**2,522**
Inc./(dec.) in short-term borrowing	1,139	(250)	400	(500)	(500)
Inc./(dec.) in long-term borrowing	(2,210)	336	(1,770)	(2,000)	(1,500)
Inc./(dec.) in preference capital	(336)	(76)	-	-	-
Inc./(dec.) in borrowings	(1,407)	10	(1,370)	(2,500)	(2,000)
(Inc.)/Dec. in investments	(355)	(3)	-	-	-
Minority Int	31	20	5	6	6
Equity issue/(buyback)	195	336	-	-	-
Cash from financial activities	**(1,536)**	**362**	**(1,365)**	**(2,494)**	**(1,994)**
Extraordinary Items	-	-	2,540	-	-
Others	1,320	(88)	-	-	-
Opening cash	397	597	588	1,104	1,332
Closing cash	597	588	1,104	1,332	1,860
Change in cash	200	(8)	516	228	528

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 45: Key ratios

Y/E March	FY10	FY11	FY12E	FY13E	FY14E
Per share (Rs)					
EPS	1.8	5.6	9.9	12.8	17.3
Book value	55.3	66.6	84.7	97.6	114.8
Valuation (x)					
P/E	45.9	15.1	8.5	6.5	4.9
P/sales	0.6	0.5	0.4	0.4	0.4
P/BV	1.5	1.3	1.0	0.9	0.7
EV/EBITDA	9.9	7.6	5.8	5.2	4.2
EV/sales	1.2	1.0	0.8	0.7	0.6
Return ratios (%)					
RoIC	7.7	9.9	12.3	11.6	13.0
RoCE	9.2	11.1	13.5	12.5	13.7
RoE	3.7	9.5	13.0	14.1	16.2
Margins (%)					
EBITDA margin	12.6	13.6	14.4	14.2	14.6
PBIT margin	7.3	9.4	10.8	10.3	10.8
PBT margin	1.4	4.3	10.2	6.9	8.4
PAT margin	1.3	3.5	5.2	6.4	7.6
Turnover ratio					
Asset turnover ratio (x)	0.9	1.0	1.1	1.2	1.2
Avg. inventory period (days)	101	130	107	108	106
Avg. collection period (days)	47	44	47	48	47
Avg. payment period (days)	66	68	68	68	68
Solvency ratios (x)					
Debt-equity	1.7	1.3	1.0	0.7	0.6
Interest coverage	1.0	1.5	1.5	2.3	3.3
Growth (%)					
Sales	18.8	25.4	18.0	5.2	14.3
EBITDA	37.5	35.7	25.3	3.7	17.5
PAT	-	228.3	76.8	30.1	34.3

Source: Company, Nirmal Bang Institutional Equities Research

Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

HOLD 0-15%

SELL < 0%

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Team Details:

Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	+91 22 3926 8098 / 99
Hemindra Hazari	Head of Research	hemindra.hazari@nirmalbang.com	+91 22 3926 8017 / 18
Sales and Dealing:			
Neha Grover	AVP Sales	neha.grover@nirmalbang.com	+91 22 3926 8093
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 3926 8230, +91 22 6636 8833
Sudhindar Rao	Dealing Desk	sudhindar.rao@nirmalbang.com	+91 22 3926 8229, +91 22 6636 8832
Pradeep Kasat	Dealing Desk	pradeep.kasat@nirmalbang.com	+91 22 3926 8100/8101, +91 22 6636 8831
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 3926 8102/8103, +91 22 6636 8830

Nirmal Bang Equities Pvt. Ltd.

Correspondence Address
B-2, 301/302, Marathon Innova,
Nr. Peninsula Corporate Park
Lower Parel (W), Mumbai-400013.
Board No. : 91 22 3926 8000/1
Fax. : 022 3926 8010