

January 23, 2018

Kewal Kiran Clothing (KEWKIR)

₹ 1800

Revival in revenues remains critical...

- Kewal Kiran Clothing's (KKCL) Q3FY18 performance was below our expectations on all parameters with revenue, EBITDA margin and net profit lower than our expectations
- Q3FY18 revenues remained flattish at ₹ 94.4 crore against our estimate of ₹ 108.9 crore. Volume growth remained flattish with 1% YoY growth to 9.49 lakh pieces while realisation per piece declined 0.7% to ₹ 995 per piece
- Lower raw material cost enabled KKCL to report 690 bps YoY improvement in gross margins to 59.3%. However, negative operating leverage (employee, administration & selling expenses up 40 bps, 140 bps and 190 bps YoY, respectively) curtailed EBITDA margin expansion to 520 bps YoY to 16.7% (I-direct estimate: 18.2%)
- Higher fixed expenses further stymied profitability with interest and depreciation being higher by 65% and 21% YoY, respectively, to ₹ 1.5 crore each. Hence, PAT growth was restricted to 25% YoY to ₹ 10.4 crore (I-direct estimate: ₹ 15.2 crore)
- In terms of operating metrics, net working capital cycle (calculated on net sales) increased from 76 days in Q3FY17 to 88 days in Q3FY18. Subsequently, short-term borrowings rose 39% YoY to ₹ 59.7 crore as on December 31, 2017. The resultant pressure on working capital can be mainly attributed to higher credit period given to distributors, from an average of 70 to 90 days

Marginal growth for Killer brand...

Among the portfolio of brands, KKCL's largest brand Killer (55% of sales) grew marginally by 2% YoY to ₹ 49.5 crore while Integrity, Lawman brands declined 13%, 11% to ₹ 17.2 crore, ₹ 17.5 crore, respectively. Easies brand reported revenue growth of 30% YoY to ₹ 3.9 crore albeit on a smaller base. Category wise, jeans (64% of sales) reported healthy revenue growth of 11% YoY to ₹ 59.4 but decline in shirts and trousers category by 23% and 52%, dragged overall revenue downwards.

Maintaining intrinsic value of brands by refraining from heavy discounting

With various branded players resorting to aggressive promotional offers, KKCL has refrained from giving away heavy discounts. The management believes it would result in a dilution of its brand image and have a negative impact on its profitability. This resulted in sluggish revenue growth for KKCL this quarter. National chain stores (NCS) and e-commerce channel of sales reported 16%, 64% decline in revenues, respectively, for the current quarter. Revenues from MBO channels (42% of total sales) declined 4% YoY to ₹ 40.0 crore while retail channel sales registered revenue growth of 7% YoY to ₹ 21 crore.

Revenue growth remains critical; maintain BUY

KKCL has a lean balance sheet with debt/equity ratio comfortably placed at 0.1x and generating healthy return ratios (20%+ RoCE). Incorporating the muted 9MFY18 performance, we revise our estimates downwards for FY18-20E. We expect KKCL to clock sales, PAT CAGR of 7%, 12%, respectively, in FY17-20E. Revival of revenue growth remains critical, going forward. Given the strong brand legacy and a healthy balance sheet, we continue to maintain our **BUY** recommendation with a revised target price of ₹ 2050 (21.0x FY20 EPS of ₹ 97.4).

Rating matrix		
Rating	:	Buy
Target	:	₹ 2050
Target Period	:	12-18 months
Potential Upside	:	14%

What's changed?	
Target	Changed from ₹ 2260 to ₹ 2050
EPS FY18E	Changed from ₹ 75.8 to ₹ 69.0
EPS FY19E	Changed from ₹ 96.3 to ₹ 81.3
EPS FY20E	Changed from ₹ 113.1 to ₹ 97.4
Rating	Unchanged

Quarterly performance					
	Q3FY18	Q3FY17	YoY (%)	Q2FY18	QoQ (%)
Revenue	94.4	94.2	0.2	167.5	-43.7
EBITDA	15.7	10.8	45.7	48.8	-67.8
EBITDA (%)	16.7	11.5	521 bps	29.2	-1248 bps
PAT	10.4	8.3	25.2	35.2	-70.5

Key financials				
(₹ Crore)	FY17	FY18E	FY19E	FY20E
Net Sales	492	481	535	600
EBITDA	100	103	118	143
Net Profit	85	85	100	120
EPS (₹)	69.2	69.0	81.3	97.4

Valuation summary				
	FY17	FY18E	FY19E	FY20E
P/E	26.0	26.1	22.1	18.5
Target P/E	29.6	29.7	25.2	21.0
EV to EBITDA	22.0	21.5	18.6	15.5
Price to book	6.2	5.5	4.8	4.3
RONW (%)	23.8	21.1	21.9	23.1
ROCE (%)	23.8	21.4	22.1	23.9

Stock data	
Particular	Amount
Market Capitalisation (₹ Crore)	2,218.5
Debt (FY17) (₹ Crore)	40.5
Cash (FY17) (₹ Crore)	64.2
EV (₹ Crore)	2,194.8
52 week H/L	2200 / 1575
Equity Capital (₹ Crore)	12.3
Face Value (₹)	10

Price performance				
	1M	3M	6M	12M
Kewal Kiran Clothing	-7.0	-7.6	-2.6	0.1
Page Industries	-13.2	16.4	30.4	52.5
Arvind	1.6	13.9	18.0	21.0

Research Analysts	
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Variance analysis

	Q3FY18	Q3FY18E	Q3FY17	YoY (%)	Q2FY18	QoQ (%)	Comments
Revenue	94.4	108.9	94.2	0.2	167.5	-43.7	Flattish volume and realisations growth YoY
Other Income	3.5	4.7	3.7	-3.0	5.4	-34.8	
Raw Material Expense	38.4	47.5	44.8	-14.4	71.4	-46.2	
Employee Expense	15.3	18.5	14.9	2.8	18.4	-16.5	
Selling Expenses	8.2	5.4	6.4	28.2	6.4	27.4	
Manufacturing & Other Expense	16.8	17.6	17.3	-2.9	22.5	-25.6	
EBITDA	15.7	19.8	10.8	45.7	48.8	-67.8	
EBITDA Margin (%)	16.7	18.2	11.5	521 bps	29.2	-1248 bps	Lower raw material cost enabled KKCL to report 690 bps YoY improvement in gross margins. However, negative operating leverage curtailed the EBITDA margin expansion to 520 bps
Depreciation	1.5	1.5	1.2	21.0	1.4	4.2	
Interest	1.5	1.3	0.9	64.8	1.3	13.6	
PBT	16.3	21.7	12.3	32.4	51.5	-68.4	
Tax Outgo	5.9	6.5	4.0	47.1	16.3	-63.9	
PAT	10.4	15.2	8.3	25.2	35.2	-70.5	PAT growth was restricted to 25% owing to increase in depreciation and interest expense
Key Metrics							
Apparel Volume (Lakh pcs)	9.5	10.2	9.4	1.0	16.7	-43.1	
Average Realisation (₹)	994.5	1,062.8	1,001.9	-0.7	1,004.9	-1.0	
Gross Margin (%)	59.3	56.4	52.4	695 bps	57.4	196 bps	

Source: Company, ICICIdirect.com Research

Change in estimates

(₹ Crore)	FY18E			FY19E			FY20E		
	Old	New	% Change	Old	New	% Change	Old	New	% Change
Revenue	525.7	481.3	-8.4	608.0	535.1	-12.0	693.2	600.2	-13.4
EBITDA	110.1	102.8	-6.6	137.8	118.5	-14.0	161.6	142.6	-11.7
EBITDA Margin (%)	20.9	21.4	42 bps	22.7	22.1	-53 bps	23.3	23.8	45 bps
PAT	93.4	85.1	-8.9	118.7	100.2	-15.6	139.4	120.1	-13.8
EPS (₹)	75.8	69.0	-8.9	96.3	81.3	-15.6	113.1	97.4	-13.8

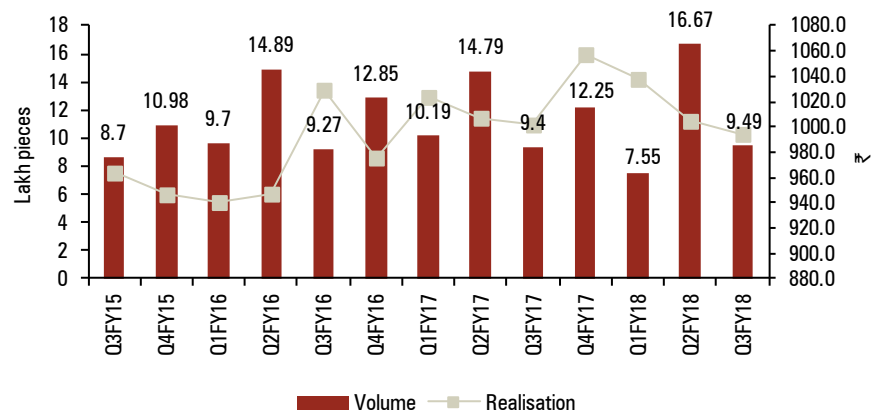
Source: Company, ICICIdirect.com Research

Company Analysis

Revenue de-growth expected in FY18; revival expected from FY19

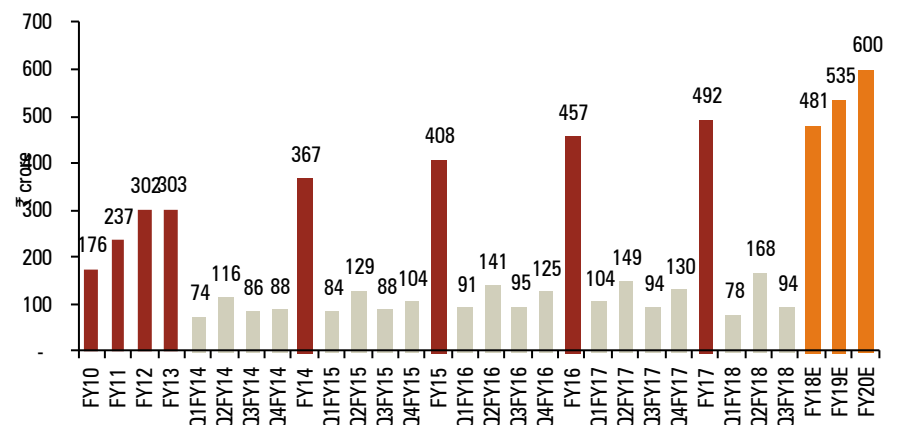
For 9MFY18, revenues declined 2.1% YoY to ₹ 340.3 crore. The decline was mainly owing to 2% decline in volumes to 33.7 lakh pieces, with average realisations remaining flattish at ₹ 1010/piece. The sluggish revenue growth can be attributed to a) de-stocking of inventory at the dealer's level prior to GST implementation and b) KKCL refraining from giving heavy discounts, which, in turn, impacted the volume offtake. Incorporating the muted performance for 9MFY18, we revise our revenue estimates downwards for FY18-20E. We expect KKCL to report a decline in revenue for FY18. We expect revenues for FY19E, FY20E to grow 11%, 12% to ₹ 535 crore, ₹ 600 crore, respectively.

Exhibit 1: Volume and realisation trend



Source: Company, ICICIdirect.com Research

Exhibit 2: Topline trajectory

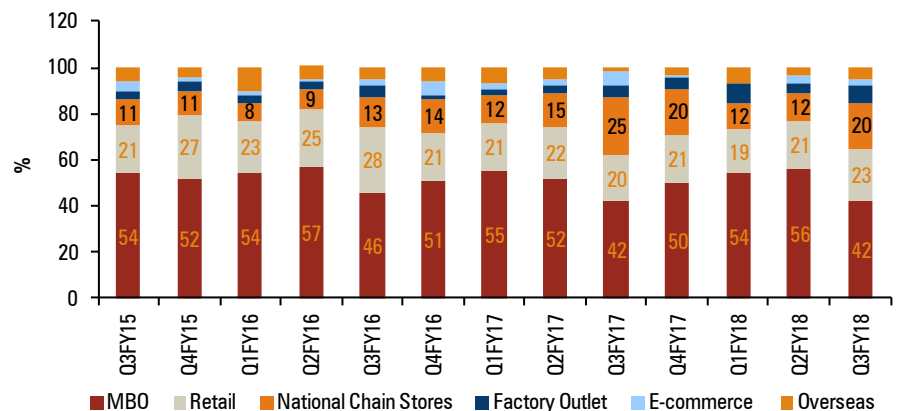


Source: Company, ICICIdirect.com Research

NCS & e-commerce channel sales report decline in revenues

With various branded players resorting to aggressive promotional offers, KKCL has refrained from giving away heavy discounts. The management believes it would result in a dilution of its brand image and have a negative impact on its profitability. This resulted in sluggish revenue growth for KKCL this quarter. National chain stores (NCS) and e-commerce channel of sales reported 16% and 64% decline in revenues for the current quarter. Revenues from MBO channels (42% of total sales) declined 4% YoY to ₹ 40.0 crore while retail channel sales registered revenue growth of 7% YoY to ₹ 21 crore.

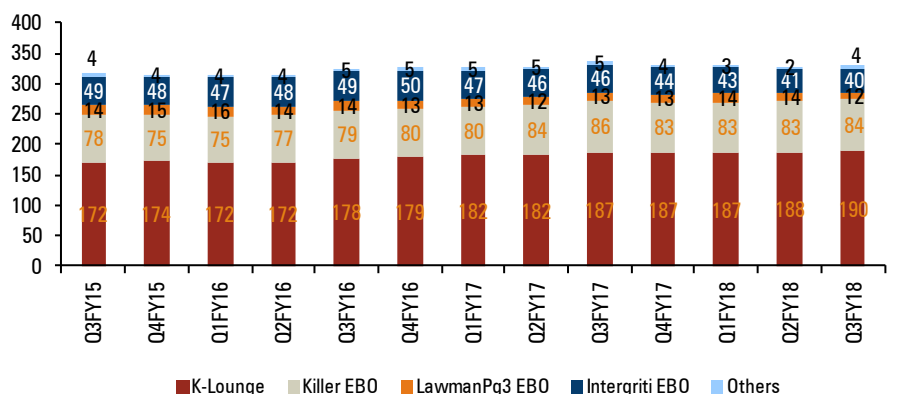
Exhibit 3: Channel-wise contribution to sales



Source: Company, ICICIdirect.com Research

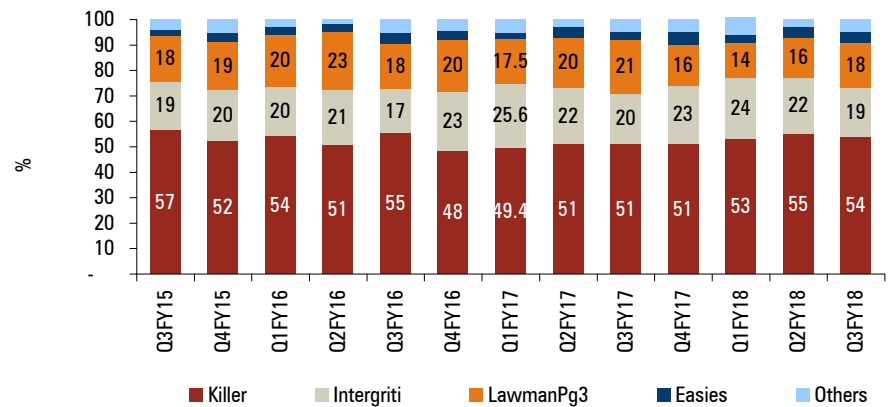
KKCL has an extensive network of 330 stores of which ~96% are franchisee owned and franchisee operated stores. Geographically, in Q3Y18, the eastern region continued to remain the dominant region with largest revenue share of 41% and registering topline growth of 39% YoY to ₹ 36.4 crore. West, North and Southern regions reported decline of 32%, 17% and 19%, respectively. Exports for the quarter declined 26% YoY to ₹ 5.8 crore.

Exhibit 4: KKCL's strong distribution network



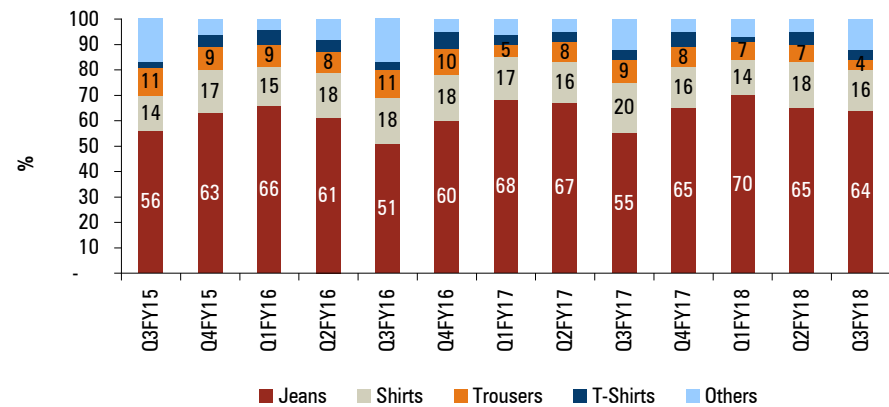
Source: Company, ICICIdirect.com Research

Exhibit 5: Brand-wise contribution to sales



Source: Company, ICICIdirect.com Research

Exhibit 6: Product wise contribution to sales



Source: Company, ICICIdirect.com Research

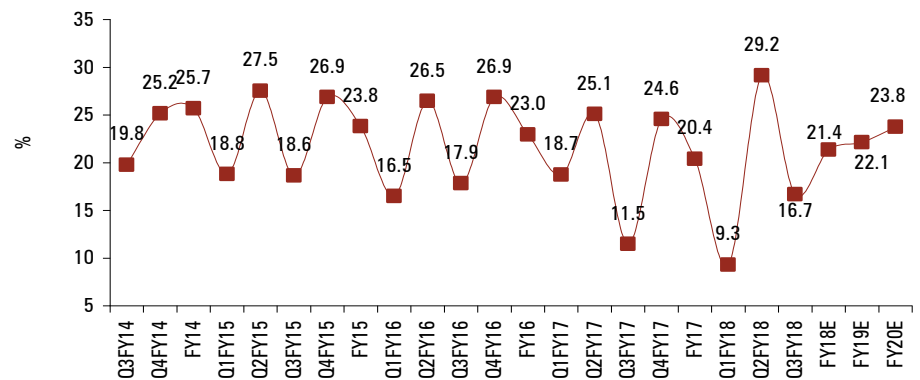
EBITDA expected to grow at CAGR of 12.7% over FY17-20E

Despite a decline in revenue for 9MFY18, EBITDA for the period increased 6.1% YoY to ₹ 71.9 crore, with margin expansion to the tune of 160 bps. With the company refraining from giving heavy discounts, we expect the margin profile to remain stable, going forward. We expect absolute EBITDA to grow at a CAGR of 12.7% in FY17-20E.

Killer, its flagship brand, continues to account for the largest share of revenues

Jeans remained the largest selling product

Exhibit 7: EBITDA margin trend

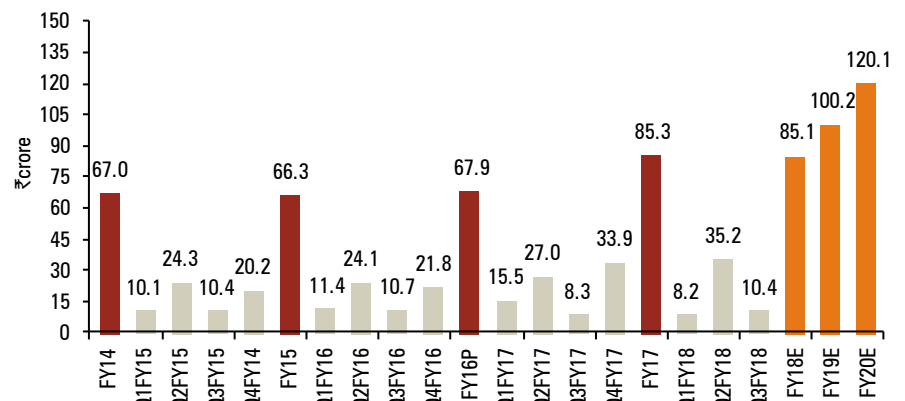


Source: Company, ICICIdirect.com Research

PAT expected to grow at CAGR of 12% over FY17-20E

On account of a decline in revenues for 9MFY18, we expect KKCL to register flattish PAT growth in FY18. PAT is expected to recover to ₹ 120.1 crore in FY20E from ₹ 85.3 crore in FY17E, driven by revival in revenue growth and improvement in EBITDA margin.

Exhibit 8: Net profit trend



Source: Company, ICICIdirect.com Research

Valuation

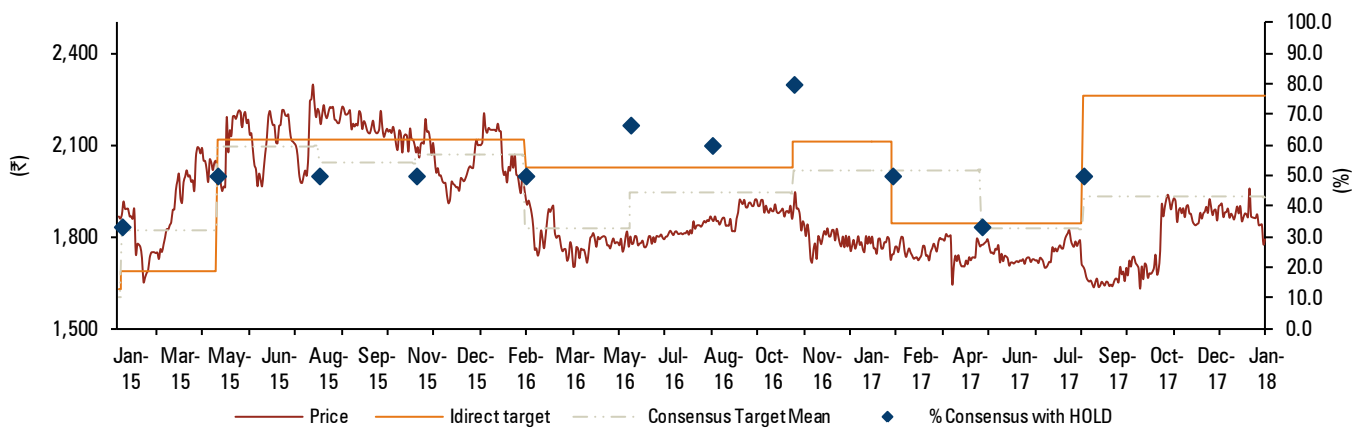
KKCL has over the years constantly delivered a strong performance depicting the fundamental strength of the company. The company is virtually debt free with comfortable debt/equity ratio at 0.1x as on FY17. KKCL has a capital efficient business model, generating 20%+ RoCE and strong EBITDA margins in the range of 20-23. Incorporating the muted 9MFY18 performance, we revise our estimates downwards for FY18-20E. We expect KKCL to clock sales, PAT CAGR of 7%, 12%, respectively, in FY17-20E. Revival of revenue growth remains critical, going forward. Given the strong brand legacy and a healthy balance sheet, we continue maintain **BUY** recommendation with a revised target price of ₹ 2050 (21.0x FY20 EPS of ₹ 97.4).

Exhibit 9: Valuations

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY17	492.4	7.7	69.2	25.5	26.0	22.0	23.8	23.8
FY18E	481.3	(2.2)	69.0	(0.2)	26.1	21.5	21.1	21.4
FY19E	535.1	11.2	81.3	17.8	22.1	18.6	21.9	22.1
FY20E	600.2	12.2	97.4	19.9	18.5	15.5	23.1	23.9

Source: Company, ICICIdirect.com Research

Recommendation history vs. consensus estimate



Source: Bloomberg, Company, ICICIdirect.com Research

Key events

Date	Event
Feb-11	After four consecutive quarters of healthy growth, revenue growth slipped to 18.4% (₹ 54.7 crore)
Jun-11	Revenues grew at 52.7% YoY to ₹ 68.9 crore; apparel volumes increased 17% YoY to 8.2 lakh pieces
Sep-11	Revenue growth continues; KKCL reported 38.5% YoY growth led by 19.3% volume growth in the apparel segment (12.6 lakh pieces)
Dec-11	After strong growth in H1FY12, revenue growth flattish at 1.9% YoY (₹ 64.2 crore). Consequently, PAT de-grew 22.4% YoY to ₹ 8.8 crore
Jul-12	The company witnesses 13% revenue dip in H1FY13 to ₹ 147.4 crore
Nov-12	After two quarters of de-growth, revenues increase 19.6% YoY to ₹ 76.8 crore
Jun-13	After flattish FY13, Q1FY14 witnessed KKCL returning to the 30% growth trajectory with revenues increasing 30.6% YoY to ₹ 73.7 crore
Sep-13	Revenues increase 28.6% YoY to ₹ 189.5 crore in H1FY14
Dec-13	Despite weak Q3FY14 results, investors were optimistic about the longer term picture. Hence, the stock rallied
Jun-14	The stock continues the upward move on the back of strong investor optimism. Despite relatively lower revenue growth, investors continue to believe in the growth potential of the company
Mar-15	Posts increase in EBITDA margins after five consecutive quarters of de-growth
Mar-16	Revenues for FY16 rise 12% YoY to ₹ 453 crore mainly driven by a volume growth of 11%
Mar-17	Demonetisation weighs heavily on the performance of KKCL as it registers flattish volume growth in FY17

Source: Company, ICICIdirect.com Research

Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Jain (Shantaben P)	30-Sep-17	49.9%	6.15	0.00
2	Nalanda Capital Pte Ltd	30-Sep-17	9.7%	1.20	0.00
3	Jain (Dinesh P)	30-Sep-17	5.9%	0.73	0.00
4	Jain (Vikas P)	30-Sep-17	5.9%	0.72	0.00
5	Jain (Hemant P)	30-Sep-17	5.6%	0.69	0.00
6	Jain (Kewalchand P)	30-Sep-17	5.6%	0.69	0.00
7	SBI Funds Management Pvt. Ltd.	30-Sep-17	3.2%	0.39	0.00
8	Kotak Mahindra Asset Management Company Ltd.	30-Sep-17	2.3%	0.28	-0.06
9	Matthews International Capital Management, L.L.C.	30-Sep-17	2.2%	0.28	-0.10
10	Aditya Birla Sun Life AMC Limited	30-Sep-17	1.0%	0.13	-0.13

Source: Reuters, ICICIdirect.com Research

Shareholding Pattern

(in %)	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17
Promoter	74.2	74.2	74.2	74.2	74.2
FII	13.2	13.0	12.9	12.7	12.3
DII	8.3	8.7	8.1	8.8	9.3
Others	4.3	4.1	4.9	4.3	4.3

Recent Activity

BUYS			SELLS		
Investor name	Value (Mn)	Shares (Mn)	Investor name	Value (Mn)	Shares (Mn)
Ambit Capital Pvt. Ltd.	3.26	0.13	Aditya Birla Sun Life AMC Limited	-3.47	-0.13
			Matthews International Capital Management, L.L.C.	-2.64	-0.10
			Kotak Mahindra Asset Management Company Ltd.	-1.48	-0.06

Source: Reuters, ICICIdirect.com Research

Financial summary

Profit and loss statement					₹ Crore			
(Year-end March)	FY17	FY18E	FY19E	FY20E				
Total operating Income	492.4	481.3	535.1	600.2				
Growth (%)	7.8	-1.4	11.2	12.2				
Raw Material Expenses	202.1	209.1	234.7	252.3				
Employee Expenses	59.6	62.6	68.0	75.0				
Manufacturing Expenses	47.7	38.5	37.5	45.0				
Selling Expenses	31.4	27.4	34.8	36.0				
Other expenses	52.0	40.9	41.7	49.2				
Total Operating Expenditure	392.8	378.5	416.7	457.5				
EBITDA	99.6	102.8	118.5	142.6				
Growth (%)	-4.2	3.2	15.2	20.4				
Depreciation	4.8	5.4	5.8	6.2				
Interest	5.3	5.9	5.8	5.8				
Other Income	28.6	26.5	32.1	36.0				
PBT	118.2	118.0	139.0	166.6				
Others	0.0	0.0	0.0	0.0				
Total Tax	32.9	33.0	38.8	46.5				
PAT	85.3	85.1	100.2	120.1				
Growth (%)	25.5	-0.2	17.8	19.9				
EPS (₹)	69.2	69.0	81.3	97.4				

Source: Company, ICICIdirect.com Research

Balance sheet					₹ Crore			
(Year-end March)	FY17	FY18E	FY19E	FY20E				
Liabilities								
Equity Capital	12.3	12.3	12.3	12.3				
Reserve and Surplus	345.7	390.4	445.9	508.3				
Total Shareholders funds	358.0	402.7	458.2	520.6				
Total Debt	40.5	52.9	51.4	51.0				
Deferred Tax Liability	0.5	0.4	0.3	0.2				
Other long term liabilities	14.4	14.7	15.0	15.3				
Total Liabilities	413.4	470.7	524.8	587.0				
Assets								
Gross Block	113.9	128.2	138.7	150.5				
Less: Acc Depreciation	47.2	52.6	58.4	64.6				
Net Block	66.7	75.6	80.3	85.9				
Capital WIP	7.3	8.0	6.2	5.8				
Total Fixed Assets	73.9	83.6	86.5	91.7				
Investments	190.2	224.7	257.9	296.0				
Inventory	50.7	55.4	60.1	67.4				
Debtors	106.2	112.1	124.6	141.4				
Loans and Advances	9.2	9.6	10.7	12.0				
Other Current Assets	0.8	1.5	1.6	1.7				
Cash	64.2	57.8	62.6	59.9				
Total Current Assets	231.0	236.4	259.7	282.4				
Creditors	39.5	40.1	45.0	48.4				
Other current liabilities	21.1	12.5	12.3	12.1				
Provisions	21.4	22.1	22.7	23.4				
Total Current Liabilities	82.0	74.7	80.0	83.9				
Net Current Assets	149.0	161.7	179.6	198.5				
Others Non-current Assets	0.3	0.8	0.8	0.8				
Application of Funds	413.4	470.7	524.8	587.0				

Source: Company, ICICIdirect.com Research

Cash flow statement					₹ Crore			
(Year-end March)	FY17	FY18E	FY19E	FY20E				
Profit After Tax	85.3	85.1	100.2	120.1				
Add: Depreciation	4.8	5.4	5.8	6.2				
(Inc)/dec in Current Assets	20.7	-11.8	-18.4	-25.5				
Inc/(dec) in CL and Provisions	-23.6	-7.4	5.4	3.9				
Others	0.0	0.0	0.0	0.0				
CF from operating activities	87.1	71.3	92.9	104.7				
(Inc)/dec in Investments	-32.3	-34.5	-33.2	-38.2				
(Inc)/dec in Fixed Assets	-11.5	-14.3	-10.6	-11.8				
(Inc)/dec in CWIP	-4.6	-0.7	1.8	0.4				
Others	0.3	-0.5	0.0	0.0				
CF from investing activities	-48.1	-50.0	-42.0	-49.6				
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0				
Inc/(dec) in loan funds	11.6	12.4	-1.6	-0.4				
Others	-11.1	-40.2	-44.5	-57.5				
CF from financing activities	0.5	-27.7	-46.1	-57.9				
Net Cash flow	39.5	-6.4	4.9	-2.8				
Opening Cash	24.7	64.2	57.8	62.6				
Closing Cash	64.2	57.8	62.6	59.9				

Source: Company, ICICIdirect.com Research

Key ratios								
(Year-end March)	FY17	FY18E	FY19E	FY20E				
Per share data (₹)								
EPS	69.2	69.0	81.3	97.4				
Cash EPS	73.1	73.4	86.0	102.4				
BV	290.5	326.8	371.8	422.4				
DPS	17.5	28.0	31.0	40.0				
Cash Per Share	52.1	46.9	50.8	48.6				
Operating Ratios								
EBITDA Margin (%)	20.4	21.4	22.1	23.8				
PBT Margin (%)	24.2	24.5	26.0	27.8				
PAT Margin (%)	17.5	17.7	18.7	20.0				
Inventory days	37.1	42.0	41.0	41.0				
Debtor days	79.3	85.0	85.0	86.0				
Creditor days	71.3	70.0	70.0	70.0				
Return Ratios (%)								
RoE	23.8	21.1	21.9	23.1				
RoCE	23.8	21.4	22.1	23.9				
RoIC	31.2	25.3	26.2	27.4				
Valuation Ratios (x)								
P/E	26.0	26.1	22.1	18.5				
EV / EBITDA	22.0	21.5	18.6	15.5				
EV / Net Sales	4.5	4.6	4.1	3.7				
Market Cap / Sales	4.5	4.6	4.1	3.7				
Price to Book Value	6.2	5.5	4.8	4.3				
Solvency Ratios								
Debt/EBITDA	0.8	1.0	0.9	0.7				
Debt / Equity	0.1	0.1	0.1	0.1				
Current Ratio	3.8	4.5	4.5	4.7				
Quick Ratio	3.0	3.4	3.5	3.6				

Source: Company, ICICIdirect.com Research

ICICIdirect.com coverage universe (Apparel)

Sector / Company	CMP		Rating	M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)			FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E
Kewal Kiran Clothing	1800	2050	Buy	2218	69.2	69.0	81.3	22.0	21.5	18.6	4.5	4.6	4.1	23.8	21.4	22.1	23.8	21.1	21.9
Page Industries	22724	22920	Hold	25380	238.7	299.9	395.1	95.2	75.8	57.5	59.8	47.3	36.5	51.6	55.8	61.0	40.0	41.8	44.9
Rupa & Company	460	505	Buy	3642	9.1	10.6	13.6	50.7	43.3	33.7	25.1	22.3	17.8	23.6	25.0	28.9	16.4	17.5	20.0
Vardhman Textiles	1473	1440	Buy	8486	118.1	139.9	160.2	12.5	10.5	9.2	8.1	6.8	5.9	12.6	14.1	15.1	13.5	14.1	14.5
Arvind Ltd	445	480	Buy	11534	12.3	12.4	14.0	36.3	35.9	31.9	14.5	13.8	12.7	11.0	9.9	10.4	11.9	9.0	9.6

Source: Company, ICICIdirect.com Research

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Buy: > 10%/15% for large caps/midcaps, respectively;

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Sell: -10% or more;



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