Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Arvind Ltd

Strong Q4; Medium-term outlook intact

Consumer Discretionary	Sharekhan code: ARVIND
Reco/View: Buy ↔	CMP: Rs. 108
	Price Target: Rs. 145 ↓

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX

	+	=	-
Right Sector (RS)		✓	
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↓	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 19.1

Updated Feb 08, 2022

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

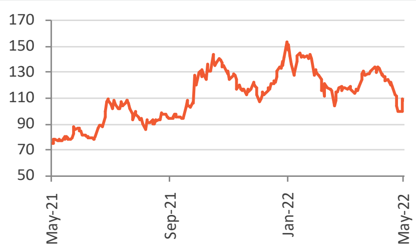
Company details

Market cap:	Rs. 2,812 cr
52-week high/low:	Rs. 159 / 72
NSE volume: (No of shares)	16.8 lakh
BSE code:	500101
NSE code:	ARVIND
Free float: (No of shares)	15.3 cr

Shareholding (%)

Promoters	41.3
FII	12.6
DII	12.1
Others	34.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-19.8	-16.3	-17.9	44.6
Relative to Sensex	-14.6	-10.0	-8.2	36.6

Sharekhan Research, Bloomberg

Summary

- Arvind Limited (Arvind) registered yet another quarter of strong performance in Q4FY2022, with revenue growing by 33% to Rs. 2,203.5 crore and PAT increasing by 47% to Rs. 94 crore.
- Management has guided for 8-10% revenue growth in FY2023 with H1 performance expected to be subdued due to global uncertainties and higher inflation. Garment and AMD businesses to grow by 18-20%. Margins to remain under pressure due to higher cotton prices.
- Management is upbeat about medium-term outlook with large opportunities in the export market. Management is focusing on expanding capacities through de-bottlenecking mechanism. Debt reduced by Rs. 258 crore in FY2022 and is expected to further reduce going ahead.
- The stock trades at 8.8x/6.4x its FY2023E/FY2024E EPS. We maintain Buy with a revised PT of Rs. 145.

Arvind Limited (Arvind) ended FY2022 on a strong note by posting yet another quarter of strong performance with strong volume and price-led growth boosted by high domestic and export demand. Strong revenue growth of 33.2% y-o-y to Rs. 2,203.5 crore can be attributed to robust performance by both textile and advanced materials divisions (AMD), which grew by 37% and 34% y-o-y, respectively. Price increases and efficient raw-material management aided the company to post 111 bps y-o-y improvement in gross margin. The denim, woven, and garmenting divisions registered strong revenue growth of 36%, 48%, and 30%, respectively, during the quarter. Higher project cost of Rs. 75 crore-80 crore for asset monetisation, increased global logistics cost, and domestic freight cost led to a 191-bps y-o-y decline in EBITDA margin to 10.7% in Q4. The company has reduced debt by Rs. 268 crore as compared to March 2021 and net debt stands at Rs. 1,682 crore in FY2022.

Key positives

- Denim, woven, and garment sales volume grew by 10%, 14%, and 10%, respectively, y-o-y in Q4.
- AMD business registered strong growth of 34% y-o-y to Rs. 267 crore.
- Debt reduced by Rs. 268 crore on a y-o-y basis; interest cost fell by 21% y-o-y in FY2022 due to reduction in debt.

Key negatives

- EBITDA margin of the textile business fell by 300 bps y-o-y to 10.7%, affected by higher global logistics cost, increased cotton prices, and spike in domestic freight cost.

Management Commentary

- Export demand is likely to remain uncertain in the near term due to rising global inflation and geopolitical disturbance in Europe. On the other hand, domestic demand is expected to remain firm due to the ongoing marriage season and expected strong forthcoming festive season.
- Management targets revenue growth of 8-10% in FY2023, which will be driven by double-digit growth in the garment and AMD businesses. Management is upbeat about medium-term growth outlook as China + 1 factors, government signing FTAs with various regions, and global retailers looking for alternate supply base provide strong growth visibility in the coming years.
- The company has raw-material inventory of 2-2.5 months. The company expects cotton prices to stabilise from November 2022 once the new crop is out in the market. Thus, in the near term, margins are expected to remain under pressure. However, the same is expected to gradually improve once cotton prices correct from their high.
- The company would be doing capital expenditure of Rs. 200 crore for augmenting its garmenting and AMD capacities through de-bottlenecking exercise. This will be largely done through internal cash flows. Higher generation of cash flows and asset monetisation might lead to further debt reduction by Rs. 300 crore in FY2023.

Revision in estimates – We have revised downwards our EBITDA estimates for FY2023 and FY2024 to factor in lower EBITDA margins, which will be impacted by input cost inflation. However, we maintain our earnings estimates for FY2023 and FY2024 as the effective tax rate will be lower to 25-26% from 35% earlier.

Our Call

View: Maintain Buy with a revised PT of Rs. 145: Strong performance in H2FY2022 aided Arvind to post strong performance in FY2022 with double-digit growth in revenue and PAT. The company is optimistic about its medium-term growth prospects with emerging opportunities in the export market and improving demand in the domestic market. Better mix would help profitability to improve consistently in the medium term. The stock trades at 8.8x/6.4x its FY2023E/24E EPS (and 5.3x/4.0x its FY2023/24E EV/EBITDA). We maintain our Buy recommendation on the stock with a revised price target of Rs. 145.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenue	5,073	8,034	8,832	9,939
EBITDA margin (%)	9.1	9.8	8.8	9.5
Adjusted PAT	8	254	318	439
% YoY growth	-93.7	-	25.3	37.9
Adjusted EPS (Rs.)	0.3	9.9	12.3	17.0
P/E (x)	-	10.9	8.8	6.4
P/B (x)	1.0	0.9	0.9	0.8
EV/EBITDA (x)	9.5	5.5	5.3	4.0
RoNW (%)	0.3	9.0	10.3	12.8
RoCE (%)	3.1	7.8	7.9	9.5

Source: Company; Sharekhan estimates

Good Q4; Strong revenue growth of 33.2% y-o-y; PAT grew at 47.4% y-o-y

Arvind's revenue grew by 33.2% y-o-y to Rs. 2,203.5 crore in Q4FY2022, driven by robust performance by both textile and AMD businesses, which grew 37% and 34.4% y-o-y to Rs. 1,824 crore and Rs. 267 crore, respectively. Overall, consolidated gross margins improved by 111 bps y-o-y and 728 bps q-o-q to 52.6% on account of higher realisation and strong volume growth. EBITDA margin declined by 191 bps y-o-y, while it marginally improved by 26 bps q-o-q to 10.7% owing to price hikes and better operating leverage. EBITDA grew by 13% y-o-y to Rs. 235 crore. This along with lower interest cost led to a 47.4% y-o-y increase in PAT to Rs. 94 crore, higher than our expectation of Rs. 70.3 crore. Reported PAT stood at Rs. 87.6 crore. For full year FY2022, revenue grew by 58.4% y-o-y to Rs. 8,033.7 crore on a low base of 30% revenue decline in FY2021. Revenue growth is driven by 65% y-o-y growth in the textile business and 51% y-o-y growth in AMD. Gross margin declined by 159 bps y-o-y due to high input cost inflation during the year. EBITDA margin increased marginally by 70 bps to 9.8% and EBITDA grew by 70.4% y-o-y to Rs. 788.3 crore. This along with lower interest expense and depreciation cost led to significant rise in adjusted PAT to Rs. 254.2 crore from Rs. 8 crore in FY2021. The company reduced net debt by ~Rs. 42 crore and Rs. 268 crore compared to December 2021 and March 2021, respectively. Long-term debt reduced from Rs. 1,371 crore to Rs. 957 crore.

Robust growth in textile revenue; Better price realisation across segments

The textile business reported revenue of Rs. 1,824 crore in Q4FY2022 as against Rs. 1,331 crore in Q4FY2021, rising 47% y-o-y. The denim segment's revenue grew by 36.4% y-o-y to Rs. 562 crore, wovens segment reported revenue growth of 47.5% y-o-y to Rs. 655 crore, while the garments segment's revenue increased by 29.7% y-o-y to Rs. 467 crore. Price realisation improved across segments with denim average realisation improving by 27% y-o-y to Rs. 247/metre, up from Rs. 195/metre in Q4FY2021, while woven fabrics' average realisation rose by 33% y-o-y to Rs. 200/metre, up from Rs. 151/metre in Q4FY2021. EBITDA margin stood at 10.7% versus 13.7% in Q4FY2021 owing to input cost inflation, which mitigated the impact of higher volume and increased realisation. For full year FY2022, textile revenue grew by 66% y-o-y to Rs. 6,611 crore, while EBITDA margin improved by 70 bps y-o-y to 10.7%. Management has targeted the fabrics segment to grow by 5-10%, while the garments segment is expected to grow by over 20% in the next 2-3 years.

Segment-wise performance Rs cr

Category	Q4FY2022	Q4FY2021	y-o-y %
Denim	562	412	36.4
Woven	655	444	47.5
Garments	467	360	29.7
Others	221	218	1.4
Inter segment	(98)	(109)	
Total	**1,807**	**1,325**	**36.4**

Source: Company, Sharekhan Research

Volumes were higher across segments due to continued strength in domestic market and sharp improvement in export demand. Denim volumes increased by 10% y-o-y to 22 million metres. In the woven fabrics segment, volume growth came in at 14% to 32 million metres. Garments volumes stood at 11 million pieces, up from 10 million pieces in Q4FY2021.

Recovery across all segments (million metres)

Category	Market	Q1FY22	Q2FY22	Q3FY22	Q4FY22	FY2022	FY2021
Denim	Domestic	4	7	8	8	27	26
	Exports	16	18	18	14	66	36
	Total	**20**	**25**	**25**	**22**	**93**	**62**
Woven	Domestic	10	13	12	13	48	67
	Exports	13	18	23	19	73	15
	Total	**23**	**31**	**35**	**32**	**121**	**82**
Garments	**million pcs**	**7**	**9**	**10**	**11**	**37**	**32**

Source: Company, Sharekhan Research

Robust performance by AMD business

The AMD business grew by 34.4% y-o-y to Rs. 267 crore. EBITDA margin declined to 12.5% from 13.8% in Q4FY2021. For full year FY2022, AMD business reported revenue of Rs. 1,024 crore, registering 50% y-o-y growth, while EBITDA margin contracted to 12.5% from 14.4% in FY2021. Human protection business hit Rs. 500 crore mark with 75% coming from the top five customers. Arvind launched new products such as high visibility, anti-microbial, and quilted. In the Industrials business, lines continued to grow as capacities expanded and utilisation improved. The company plans to unlock potential of higher value categories such as viscose NW and mono x mono filtration products. The composites business saw marquee wins including supplies to Wilson (raquets) and Indian Coach Factory (parts of Vande Bharat trains). The company eyes strong new product momentum going ahead. Arvind plans to focus on building key accounts, wherein they can start to deliver good repeat/continuing business and targets growth of over 20% in the AMD segment in the next 2-3 years.

Key conference call highlights

- **Demand to be impacted in the near term, long-term outlook strong:** As per management, demand will be subdued in the near term due to multiple factors, including global uncertainties, high inflation, and logistical challenges. However, in the medium-long term, management expects demand to be strong due to higher demand because of China +1 factor and overall increase in domestic demand. Management has guided for volume growth of 8-10% in FY2023/FY2024.
- **Margins under pressure in the near term:** Management expects margins to be under pressure in the near term as cotton prices are expected to remain elevated until new crop of cotton is available from October, which might help to cool down prices. The company currently holds cotton inventory of 2-2.5 months.
- **Capex of Rs. 200 crore for FY2023:** In FY2022, the company incurred capex of Rs. 185 crore and management has stated that it will undertake capex of ~Rs. 200 crore in the next 12-18 months for growth as well as for certain cost-saving initiatives. A major part of the capex will be utilised for the garments and AMD segments to cater to rising demand in these segments. Around Rs. 25 crore-30 crore will be utilised to set up a hybrid power plant. A part of the capex will be from the PLI scheme, whereas remaining will be done by the company.
- **Garment capacity to be higher:** The company recently enhanced its garment capacity from 32 million pieces to 36 million pieces. The company is planning to further increase capacity to 45 million pieces by FY2023 through expansion in existing capacities. Management also indicated that the company will consider outsourcing for garments, which is a capital-efficient option. Arvind is planning to move capacity from Ethiopia to India. This will lead to 5-7% capacity reduction in the near term, but the company plans to restore the capacity.
- **Debt reduction to continue:** The company reduced net debt by ~Rs. 42 crore and Rs. 268 crore compared to December 2021 and March 2021, respectively. Net debt stands at Rs. 1,682 crore as of March 31, 2022. The company has guided on further reducing debt by ~Rs. 300 crore in the next 12-18 months. During FY2022, part of debt reduction was from land sale. Further, the company has identified land worth book value of Rs. 450 crore-500 crore as non-productive land and will be monetising the same over the next 3-4 years (market value of the land is Rs. 650 crore-700 crore). Proceeds from selling the land will aid in the company's plan to reduce debt.
- **Tax to be at 25%:** The company is expected to adopt the new tax regime. Thus, the company's tax rate is expected to be at 25% going ahead.

Results (Consolidated) Rs cr

Particulars	Q4FY22	Q4FY21	Y-o-Y (%)	Q3FY22	Q-o-Q (%)
Total revenue	**2,203.5**	**1,654.9**	**33.2**	**2,275.7**	**-3.2**
Raw material cost	1,043.6	802.1	30.1	1,243.4	-16.1
Employee cost	200.0	190.4	5.1	208.9	-4.3
Other expenses	724.9	454.4	59.5	586.5	23.6
Total operating cost	1,968.6	1,446.9	36.1	2,038.8	-3.4
EBITDA	**235.0**	**208.0**	**13.0**	**236.8**	**-0.8**
Other income	9.8	21.4	-54.2	13.2	-25.9
Interest & other financial cost	40.4	50.9	-20.6	40.5	-0.3
Depreciation	72.3	68.6	5.4	67.2	7.5
Profit before tax	**132.1**	**109.9**	**20.2**	**142.3**	**-7.2**
Tax	38.1	46.1	-17.5	48.1	-20.9
Adjusted PAT	94.0	63.8	47.4	94.2	-0.2
Minority Interest (MI)	1.1	0.1	-	0.2	-
Extraordinary item	7.5	10.5	-29.1	0.0	-
Reported PAT	**87.6**	**53.3**	**64.2**	**94.3**	**-7.1**
Adj. EPS (Rs.)	3.6	2.5	46.3	3.6	-0.2
			bps		**bps**
GPM (%)	52.6	51.5	111	45.4	728
EBITDA Margin (%)	10.7	12.6	-191	10.4	26
NPM (%)	4.0	3.2	75	4.1	-17
Tax rate (%)	28.8	42.0	-	33.8	-500

Source: Company, Sharekhan Research

Segmental performance Rs cr

Particulars	Q4FY22			Q4FY21		
	Revenue	EBITDA	EBITDA Margin (%)	Revenue	EBITDA	EBITDA Margin (%)
Textile	1,824.1	160.1	8.8	1,331.2	152.5	11.5
Advanced Materials	267.1	20.3	7.6	198.7	9.9	5.0
Others	139.1	-2.5		140.0	-3.7	
Total	**2,230.3**	**177.9**	**8.0**	**1,669.8**	**158.7**	**9.5**

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Near-term outlook uncertain; Long-term growth prospects intact

Export demand is expected to stay uncertain as inflation, rising interest rates, and geopolitical disturbances reduce demand visibility. On the other hand, domestic demand is expected to remain firm due to the ongoing marriage season and expected strong forthcoming festive season. However, long-term growth prospects of the Indian textile industry are intact. Augmentation of capacity with value-added products, key export markets focusing on increasing supply from India, and the government's support policies provide scope for textile companies to post robust growth in the long run. Textile companies are expected to benefit and report higher profitability with the government extending the RoSCTL scheme till March 2024 and keeping rates unchanged. Margins are likely to be under pressure as raw material and other input costs do not show any signs of near-term relief. Cotton prices are expected to soften moderately by November upon new crop arrival and margins are expected to improve from Q3FY2023.

■ Company outlook - Garments and AMD business to drive growth

Management targets revenue growth of 8-10% in FY2023, which will be driven by double-digit growth in the garment and AMD businesses. Management is upbeat about medium-term growth outlook as China + 1 factor, government signing FTAs with various regions, and global retailers looking for alternate supply base provide strong growth visibility in the coming years. Further, the company has added new customers in its list and is marketing new products to existing customers, which will drive export sales going ahead. Domestic demand is expected to stay strong post the festive season. Margins are expected to remain under pressure in the near term. However, the same is expected to gradually improve once cotton prices correct from their high. The company is on track for its debt reduction plan and expects to reduce debt by Rs. 300 crore in FY2023.

■ Valuation - Maintain Buy with a revised PT of Rs. 145

Strong performance in H2FY2022 aided Arvind to post strong performance in FY2022 with double-digit growth in revenue and PAT. The company is optimistic about its medium-term growth prospects with emerging opportunities in the export market and improving demand in the domestic market. Better mix would help profitability to improve consistently in the medium term. The stock trades at 8.8x/6.4x its FY2023E/24E EPS (and 5.3x/4.0x its FY2023/24E EV/EBITDA). We maintain our Buy recommendation on the stock with a revised price target of Rs. 145.

Peer Comparison

Companies	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
KPR Mill	23.7	19.7	16.1	17.0	12.9	10.5	31.0	29.5	30.3
Arvind	10.9	8.8	6.4	5.5	5.3	4.0	7.8	7.9	9.5

Source: Company, Sharekhan estimates

About company

Arvind is an innovation-driven and customer-centric global textile play present in garmenting segments such as denim, woven, knits, and technology-driven and high-margin businesses such as AMD. In FY2019, the company created value for shareholders by demerging its branded fashion and retail business and engineering business into two separate listed entities – Arvind Fashion and Anup Engineering. The demerger helped the company to scale up its core textile business in domestic as well international markets. The company is focusing on improving its return ratios by enhancing its profitability through vertical integration, introducing differentiated next-generation products, and scaling up the advance material business.

Investment theme

Arvind delivered strong performance in FY2022 aided by strong volume and realisation growth. Improving capacity utilisation of new garment facilities will drive growth of the textiles business in the medium term. High export demand for textile products and improving efficiencies would help margins of the textiles business to improve in the near term. Increased scale of the AMD business would improve profitability in the long run. We will keenly monitor the performance in the coming quarters. An uptick in the performance of the garmenting segment would act as a key trigger for the stock.

Key Risks

- Volatile currency and higher cotton prices remain one of the key risks for margin expansion and would continue to affect earnings growth in the near term.
- Any unexpected slowdown in the garmenting business would affect revenue growth in the near to medium term.

Additional Data

Key management personnel

Sanjay S. Lalbhai	Chairman and Managing Director
Swayam Saurabh	Chief Financial Officer
Ramnik V. Bhimani	Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	HDFC AMC	4.63
2	Quant Money Managers Ltd.	3.11
3	HSBC AMC	1.81
4	Oekoworld Lux SA	1.64
5	Mahindra Manulife Inv Mgmt Pvt. Ltd.	1.48
6	Zen Securities	1.38
7	AML Employees Welfare Trust	1.35
8	Dimensional Fund Advisors LP	1.19
9	Klima Okoworld	1.16
10	Aditya Birla Sun Life AMC Ltd.	0.55

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

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