KPR Mill Limited

Adding muscle to grow

Consumer Discretionary	Sharekhan code: KPRMILL	Company Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral - Negative

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 834**	
Price Target: **Rs. 980**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

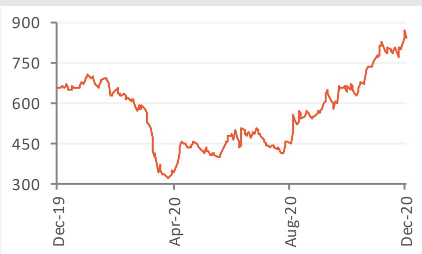
Company details

Market cap:	Rs. 5,739 cr
52-week high/low:	Rs. 898 / 317
NSE volume: (No of shares)	0.6 lakh
BSE code:	532889
NSE code:	KPRMILL
Free float: (No of shares)	1.7 cr

Shareholding (%)

Promoters	74.7
FII	1.9
DII	16.2
Others	7.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.8	48.7	74.4	28.8
Relative to Sensex	-0.4	28.0	38.6	15.0

Sharekhan Research, Bloomberg

Summary

- KPR Mill's (KPR's) new garment capacity of 42 mn pieces (total capacity will be 157 mn pieces) will start operating from mid-FY22. New capacity to add ~Rs. 150 crore and ~Rs. 500 crore in FY2022/23.
- Recent spike in COVID-19 cases acts as a risk to exports (especially to European market) in the short term. However, increasing demand for Indian textile products in the key export markets and augurs well from a medium term perspective.
- Increase in contribution from high-margin garment business and value-added products would help margins improve y-o-y (management targets OPM of 23%). RoE and RoCE will move above 20% in FY23.
- With OPM of ~20%, lean balance sheet and improving return ratio KPR is one of the better plays in textile space. We recommend a Buy on the stock with a PT of Rs. 980.

KPR Mill (KPR) is augmenting its garmenting capacity by 42 million pieces at a capital expenditure of Rs. 250 crore. The new capacity will be operational by mid-FY2022 and will increase garmenting capacity to 157 million pieces. The capex will be funded through low-cost debt and equity (in the ratio of 75:25). In the first year of operations, the new capacity is likely to be operational at a 25% utilisation level and gradually increase to 80% in FY2023. The facility will add Rs. 145-150 crore of revenue in FY2022 and Rs. 470-500 crore in FY2023 (management targets revenues of Rs. 600 crore). Overall demand for textile products improved from August and remained good till October (readymade garment exports were higher by 9-13% in September-October). KPR's revenues grew by ~22% in Q2FY2021 led by strong volume growth in the fabric and yarn segment. Garmenting sales volume improved to 26 million pieces from just 15 million pieces in Q1FY2021. The recent spike in COVID-19 cases acts as a risk to exports (especially to Europe) in the short term. However, increasing demand for Indian textile products in the key export markets and augurs well from a medium-term perspective. Owing to higher contribution from garmenting business and value-added yarn products along with vertical integration, overall OPM is expected to 21.5% by FY2023. This will also aid return ratios to cross 20% mark with RoE and RoCE standing at 21.6% and 25.6% by FY2023E.

Our Call

View: Recommend Buy with PT of Rs 980: We have increased our earnings estimates for FY2022/23 by 4% and 12% to factor in the impact of capacity augmentation. The stock has given a handsome of return of ~27% in last two months. The increase in garmenting capacity, improving growth prospects in exports markets backed strong government reforms and focus on adding value-added products provides a further upside to the stock with better earnings visibility. The stock is currently trading at 9.8x its FY2023E earnings. With an OPM of ~20%, lean balance sheet and improving return ratio KPR is one of the better plays in textile space. We recommend Buy on the stock with the price target of Rs 980.

Key risk

Any decline in the export revenues due to lower demand from international clients or significant increase in the raw material prices would act as a key risk to our earnings estimates.

Valuation (Consolidated) Rs cr

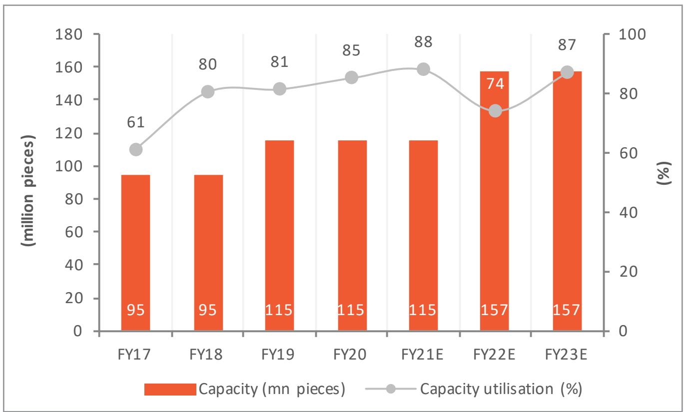
Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	3,384	3,353	3,114	3,845	4,434
OPM (%)	18.1	18.6	19.3	20.1	21.4
Adjusted PAT	335	377	329	458	585
% Y-o-Y growth	15.3	12.5	-12.7	39.3	27.9
Adjusted EPS (Rs.)	48.7	54.7	47.8	66.5	85.1
P/E (x)	18.1	15.3	17.5	12.6	9.8
P/B (x)	3.4	3.1	2.7	2.3	2.0
EV/EBIDTA (x)	11.1	10.2	10.3	7.9	6.1
RoNW (%)	19.9	20.6	16.4	19.8	21.6
RoCE (%)	21.1	19.7	17.7	22.4	25.6

Source: Company; Sharekhan estimates
**We now convert KPR Mill Limited into a Stock Update; It was earlier a 'Viewpoint' under our coverage*

Garment business to be key growth lever in long run

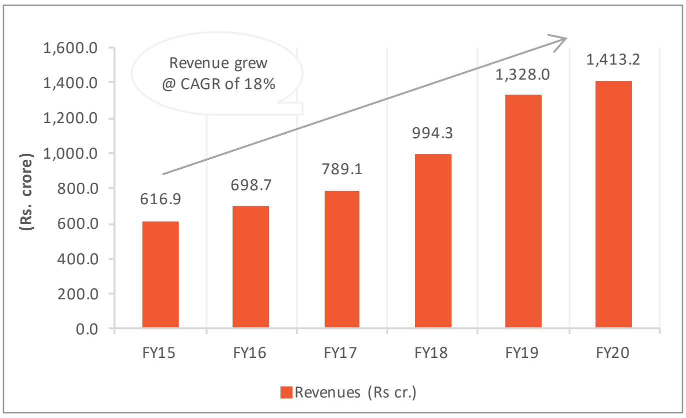
KPR is transforming itself from volatile yarn business to steady growth profitable garmenting business (contribution of garmenting revenues has gone up to 42% in FY2020 from 24% in FY2015 with capacity expansion of 56 million pieces over the same period). KPR Mill (KPR) is augmenting its garmenting capacity by 42 million pieces, which will be operational by mid of FY2022 (total garment capacity will expand to 157 million pieces from current 115 million pieces). The capex for the capacity augmentation will be funded through low cost debt and equity (in the ratio of 75:25). In first year of operation the new capacity is likely to operational at 25% capacity utilisation and will gradually increase to 80% in FY2023. It will add Rs. 145-150 crore in FY2022 and around Rs. 470-500 crore in FY2023 (management is target revenues of Rs. 600crore). Thus revenue contribution of the garmenting business will rise to 48% in FY2023.

Trend in garment capacity and utilisation



Source: Company, Sharekhan Research

Garment revenues grew at CAGR of 18% over FY15-20



Source: Company, Sharekhan Research

Garment exports clock good recovery in September-October; near-term demand needs to be monitored

Demand for textile products improved from August and stayed good till October largely led by improving demand from markets such as the US and Europe. Readymade garment exports rose 10-14% in September-October. KPR's revenues grew by ~22% in Q2FY2021 on strong volume growth in fabric and yarn segment. Garmenting sales volume improved to 26 million pieces from just 15 million in Q1FY2021. The recent spike in COVID-19 cases might slightly impact sales. Hence, we expect revenues in H2FY2021 to grow by high single digits to low double digit as we will keenly monitor garmenting sales volumes in the coming months.

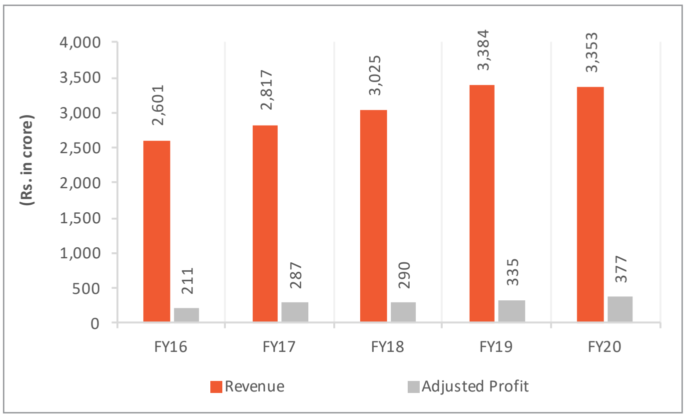
India's readymade garment exports

Month	FY20	FY21	mom %
April	9786.0	962.9	-90.2
May	10661.5	3908.8	-63.3
June	8560.9	6083.7	-28.9
July	9390.1	7973.1	-15.1
August	8966.6	8093.6	-9.7
September	7702.6	8745.3	13.5
October	7866.5	8648.4	9.9

Source: DGCI, SharekhanResearch

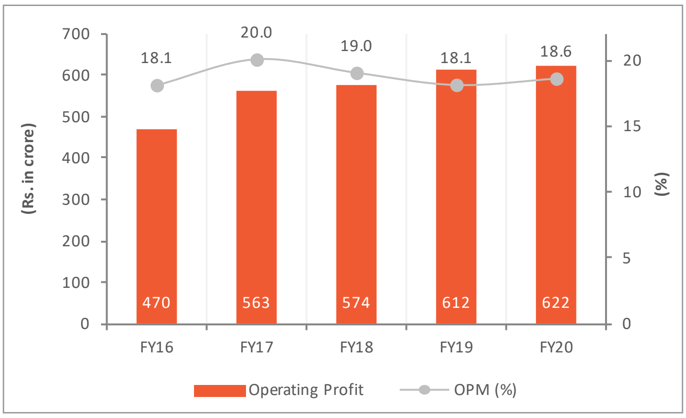
Financials in charts

Trend in Revenues and PAT



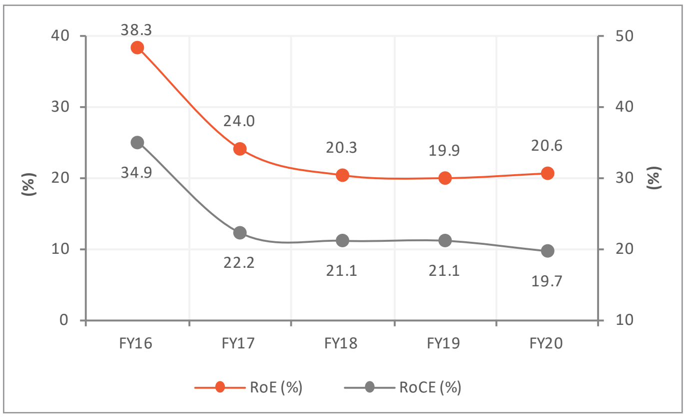
Source: Company, Sharekhan Research

OPM to improve in 21% in FY2023



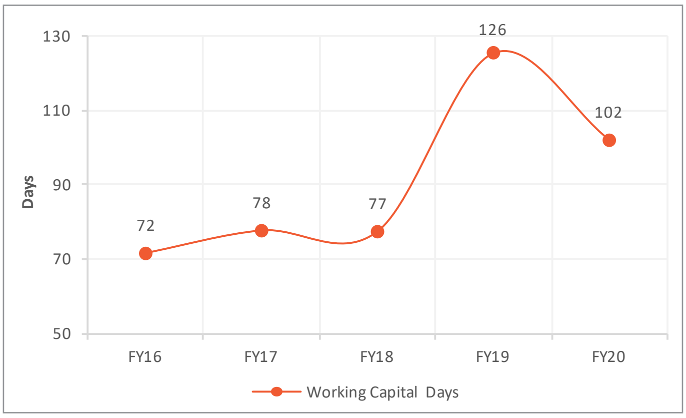
Source: Company, Sharekhan Research

Trend in return ratios



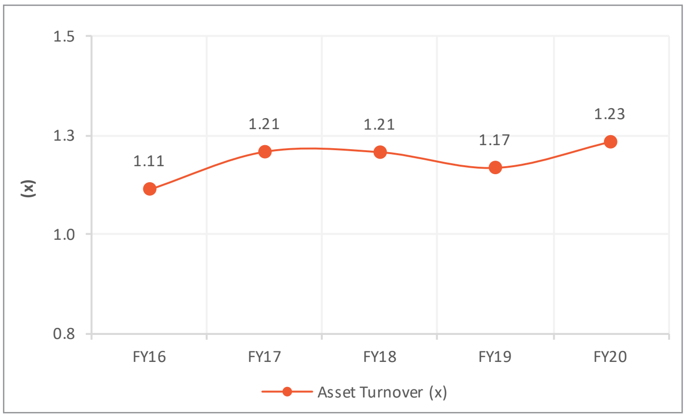
Source: Company, Sharekhan Research

Working capital days



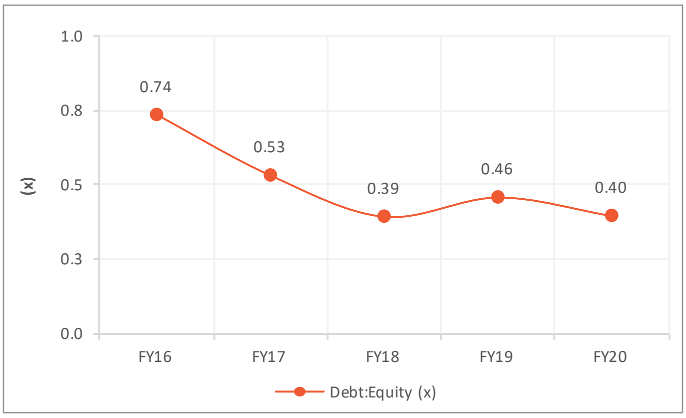
Source: Company, Sharekhan Research

Asset turnover ratio



Source: Company, Sharekhan Research

Debt: Equity ratio



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Long-term growth prospects getting better

H1FY2021 performance was affected by lesser exports and lower domestic sales during the lockdown period. Demand for textile products improved from August and remained good till October largely led by better demand from markets such as the US and Europe. Readymade garment exports were higher by 10-14% in September-October. Most textile companies registered good orders from the US and UK due to pent-up demand for apparel and home textile as retailers were building up the stock prior to festive season. However, the recent spike in the COVID-19 cases (especially Europe) act as a risk to the near term demand environment. However, the long-term growth prospects of Indian textile industry is intact. The augmentation of capacity for value-added products, key export markets focusing on shifting to India for long-term supply and supportive government policies offer textile companies scope to post good growth in the long run.

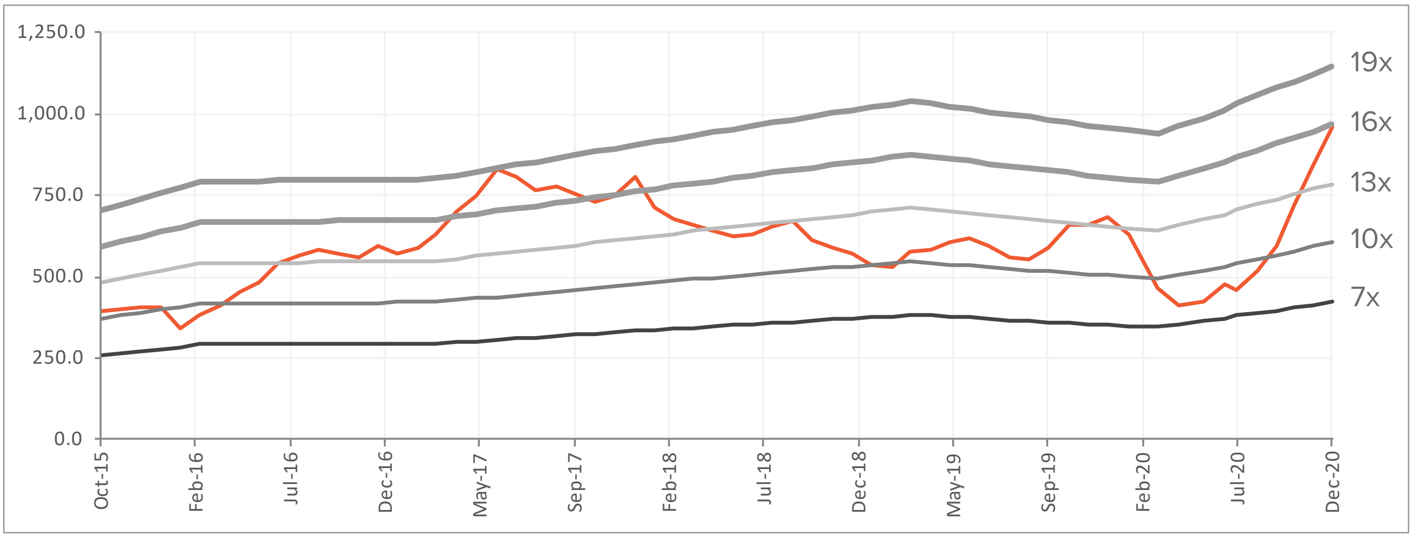
■ Company Outlook – FY2022/23 to see strong demand

Consolidated revenues decreased by 13.2%yoy (largely affected by 16% decline in textile business revenues) in H1FY2021. OPM stood at ~21% for the period. With improving retail demand in export markets, we expect revenue growth momentum to sustain with garmenting facility expected to operate in optimal utilisation. Thus, we expect the company to end FY2021 with low single-digit revenue decline and OPM of 20%. The company will be scaling up the garmenting facility by 42 million pieces per annum. With scale up in the garment capacity and increase in the utilisation, we expect garment business revenues to grow at CAGR of 16% over FY2020-23. This along with higher contribution from value-added yarn products will help margins to go above 21% in FY2023. A sturdy balance sheet would help return ratios RoE and RoCE are expected to improve to 23% each from 19% currently.

■ Valuation – Recommend Buy with PT of Rs 980

We have increased our earnings estimates for FY2022/23 by 4% and 12% to factor in the impact of capacity augmentation. The stock has given a handsome of return of ~27% in last two months. The increase in garmenting capacity, improving growth prospects in exports markets backed strong government reforms and focus on adding value-added products provides a further upside to the stock with better earnings visibility. The stock is currently trading at 9.8x its FY2023E earnings. With an OPM of ~20%, lean balance sheet and improving return ratio KPR is one of the better plays in textile space. We recommend Buy on the stock with the price target of Rs 980.

One-year forward P/E band(x)



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Arvind	79.2	8.3	5.9	6.3	4.4	3.9	3.1	5.8	7.0
KPR Mill	17.5	12.5	9.8	10.3	7.9	6.1	17.7	22.4	25.6

Source: Company, Sharekhan estimates

About company

KPR is one of the largest vertically integrated textile manufacturing companies in India with presence across the value chain from 'fibre-to-fashion'. KPR has 12 technology-oriented manufacturing units with a capacity to produce 1,00,000 MT of yarn per annum; 40,000 MT of fabrics per annum and 115 million ready-made knitted apparel per annum including a 10-million knitted garment capacity in Ethiopia. KPR has recently got into the retail segment FASO, a 100% organic innerwear, sportswear and athleisure brand. The company also has sugar business with production capacity of 5,000 TCD and recently operational ethanol facility of 130 KLPD. Around 65% of the total revenue comes from the domestic market whereas 35% is exported to over 60 countries including Europe, Australia and the US.

Investment theme

KPR is one of India's largest vertically integrated textile players, which has steady financial record with sturdy balance sheet. The strength of its integrated model helps the company to achieve consistent operating margins that are much better than some of the exporting peers. A shift in base from China to India, addition of more international clients, transforming itself from volatile yarn business to profitable garment business, scale-up in the retail business and scale-up in the garmenting revenues through increase in capacity utilisation from newly-commissioned Ethiopia facility are some of the medium to long-term growth drivers for KPR.

Key Risks

- Any decline in the export revenues due to lower demand from international clients or significant increase in the raw material prices would act as a key risk to our earnings estimates.
- Any volatility in key raw material prices such as cotton prices can affect the profitability of the company.

Additional Data

Key management personnel

KPD Sigamani	Managing Director
K.P. Ramasamy	Chairman
P.Nataraj	CEO & Managing Director
P. L. Murugappan	Chief Financial Officer
P Kandaswamy	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	L&T Mutual Fund Trustee Ltd	6.4
2	Franklin Resources Inc	3.3
3	DSP Investment Managers Pvt Ltd	2.3
4	Aditya Birla Sun Life Asset Management Co	1.7
5	Aditya Birla Sun Life Trustee Co Pvt Ltd	1.6
6	L&T Investment Management Ltd	1.1
7	Reliance Capital Trustee Co Ltd	0.9
8	IDFC Mutual Fund	0.8
9	ICICI Prudential Asset Management	0.5
10	Dimensional Fund Advisors LP	0.5

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

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