Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Arvind Limited

Better growth prospects ahead

Consumer Discretionary | Sharekhan code: ARVIND | Company Update

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

+ Positive = Neutral - Negative

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 51**	
Price Target: **Rs. 68**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

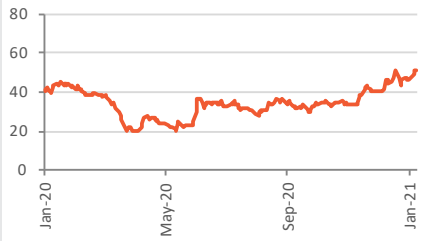
Company details

Market cap:	Rs. 1,321 cr
52-week high/low:	Rs. 53 / 19
NSE volume: (No of shares)	24.5 lakh
BSE code:	500101
NSE code:	ARVIND
Free float: (No of shares)	14.3 cr

Shareholding (%)

Promoters	44.7
FII	12.6
DII	6.4
Others	36.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	8.6	45.3	42.7	21.4
Relative to Sensex	0.4	23.9	8.4	3.7

Sharekhan Research, Bloomberg

Summary

- Arvind Limited (Arvind) will be one of the key beneficiaries of government revamped focus on improving the textile industry's growth prospects and higher demand for textile products in international markets.
- In Q2FY2021, business recovered to 66% of pre-COVID levels; and in Q3FY2021, business is expected to improve to 80% of pre-COVID levels due to higher demand from the exports market and improving demand in the domestic market.
- The sharp increase in cotton prices would be mitigated by higher contribution from the advance material business (having OPM of 13% better than core OPM of ~10%) and cost-saving initiatives undertaken in H1FY2021.
- Improved visibility of sustainable revenue growth and better margins in the coming years would be key re-rating trigger for the stock. We maintain our Buy recommendation with a revised PT of Rs. 68.

Government of India has revamped its focus on improving the growth prospects of the Indian textile sector by introducing various schemes and improve India's share in the textile export market. To capture large export opportunities in the man-made-fibre (MMF) segment (globally dominant fibre), the government is planning to introduce PLI scheme for the textile sector with a corpus of Rs. 10,683 over five years. The objective of the scheme is to promote the building of new facilities and attract investments in the MMF sector and advance material sector under Greenfield and Brownfield investments. The scheme will attract foreign investment, helping local manufacturers achieve scale, and making Indian exports competitive. It aims to enhance exports and make India an integral part of the global supply chain. Further, the government has decided to extend the benefits of the Remission of Duties and Taxes on Exported Products (RoDTEP) to all export goods starting January 1, 2021. The RoDTEP scheme would refund to exporters the embedded central, state, and local duties or taxes that were so far not being rebated or refunded. We believe companies such as Arvind will be one of the key beneficiaries of such schemes/ incentives as ~40% of its revenue come from the export of textile products. Further, the company is focusing on scaling up its advance material (technical textile) business, which currently contributes ~10% to the total revenue (business grew at a CAGR of 21% over FY2018-FY2020 with OPM of 13%). Initiatives planned by the government would help in scaling up the business fast in the coming years. Higher exports from the core textile business and scale-up of the technical textile business would help revenue to grow in strong double digits in the coming year. Further, better revenue mix and higher exports would help OPM to gradually improve on a y-o-y basis. The company repaid its debt by Rs. 100 crore in Q2FY2021; and with better cash flows, it further expects to reduce its debt by Rs. 100 crore in the coming quarters.

Our Call

View: Retain Buy with a revised PT of Rs. 68: Arvind will be one of the key beneficiaries of government revamped focus on improving the textile industry's growth prospects and higher demand for textile products in international markets. We expect strong recovery in FY2022, driven by strong recovery in the B2C retail industry in the domestic market, sustained growth in the AMD space, and improving demand in export markets. The stock is trading at discounted valuations of 6.7x its FY2023E earnings and 4.1x its FY2023E EV/EBITDA. Improved visibility of sustainable revenue growth and better margins in the coming years would be key re-rating triggers for the stock. We maintain our Buy recommendation on the stock with a revised PT of Rs. 68 (valuing the stock at 9x its FY2023E EPS).

Key Risks

Any slowdown in the export markets and rise in key input prices would act as a key risk to our earnings estimates.

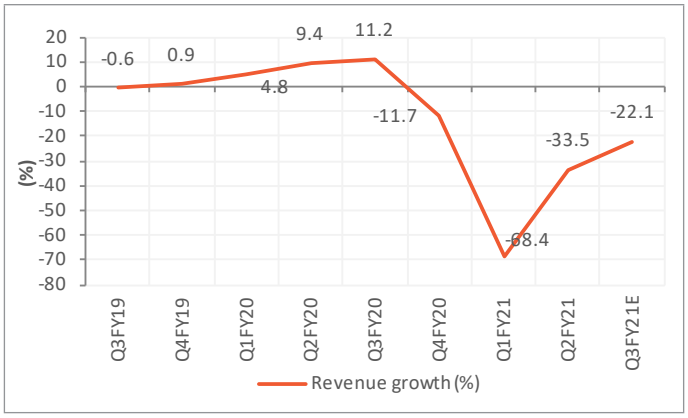
Valuations (Consolidated) — Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	7,142	7,369	5,067	7,056	7,725
OPM (%)	10.0	9.4	9.0	9.6	10.0
Adjusted PAT	269	128	15	140	196
% YoY growth	-6.1	-52.3	-	-	40.2
Adjusted EPS (Rs.)	10.4	4.9	0.6	5.4	7.6
P/E (x)	4.9	10.5	89.7	9.4	6.7
P/B (x)	0.5	0.5	0.5	0.5	0.4
EV/EBIDTA (x)	4.7	4.8	6.6	4.6	4.1
RoNW (%)	10.1	4.6	0.5	5.1	6.8
RoCE (%)	7.2	5.9	3.1	5.8	7.0

Source: Company; Sharekhan estimates

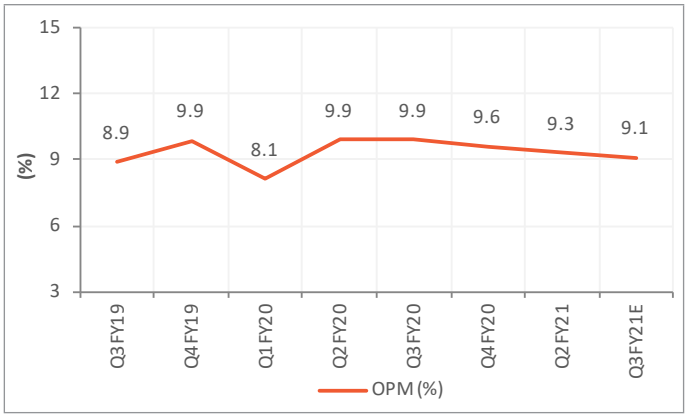
Financials in charts

Trend in revenue growth



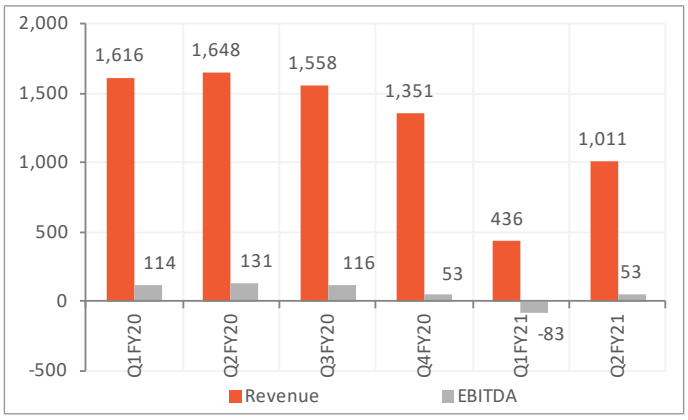
Source: Company, Sharekhan Research

Trend in OPM (%)



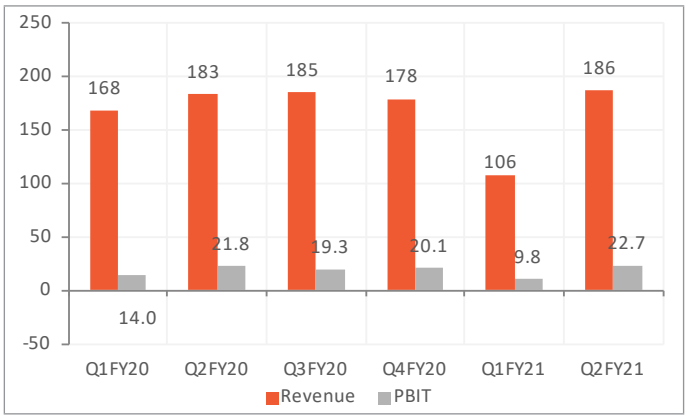
Source: Company, Sharekhan Research

Trend in textile business revenues and EBITA



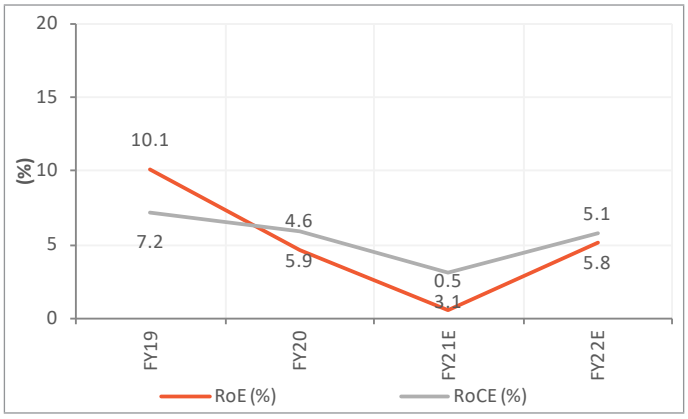
Source: Company, Sharekhan Research

Trend in advance materials revenues and EBIDTA



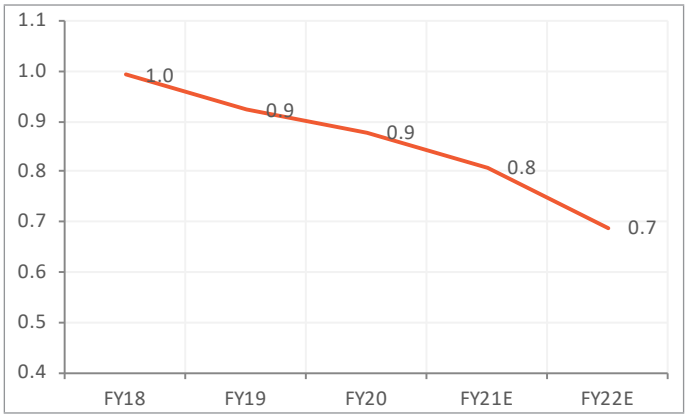
Source: Company, Sharekhan Research

Return ratios to gradually improve



Source: Company, Sharekhan Research

Debt/Equity ratio improving



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector outlook: Long-term growth prospects improving

The Indian textile sector's 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 on account of 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 countries such as US and UK due to pent-up demand for apparel and home textile as retailers were building up the stock prior to the festive season. However, the recent spike in COVID-19 cases (especially Europe) acts as a risk to the near-term demand environment. However, long-term growth prospects of the Indian textile industry are intact. The augmentation of capacity with value-added products, key export markets focusing on shifting to India for long-term supply, and government's support policies provide scope for textile companies to post good growth in the long run.

■ Company outlook - FY2021 to remain subdued, strong recovery expected in FY2022

H1FY2021 was hit by production halts and supply chain issues that persisted in Q1. Recovery was faster in the export market but remained a little slower in the domestic market. Thus, FY2021 will remain subdued. Faster recovery in the export market, healthy growth in garment sales volumes, and sustained growth in AMD will help the company post faster recovery in FY2022. Improving capacity utilisation of new garment facilities will drive growth of the textiles business in the medium term. Scaling-up of garment operations and improving efficiencies would help margins of the textiles business to improve in the near term. The AMD division would maintain its growth trajectory due to better demand. The company expects OPM of 13% and 14% for the textile and AMD businesses, respectively. Optimum utilisation of capacities and savings in structural fixed costs will help margins improve in the near to medium term.

■ **Valuation - Retain Buy with a revised PT of Rs. 68:** Arvind will be one of the key beneficiaries of government's revamped focus on improving the textile industry's growth prospects and higher demand for textile products in international markets. We expect strong recovery in FY2022, driven by strong recovery in the B2C retail industry in the domestic market, sustained growth in the AMD space, and improving demand in export markets. The stock is trading at discounted valuations of 6.7x its FY2023E earnings and 4.1x its FY2023E EV/EBITDA. Improved visibility of sustainable revenue growth and better margins in the coming years would be a key re-rating trigger for the stock. We maintain our Buy recommendation with a revised PT of Rs. 68 (valuing the stock at 9x its FY2023E EPS).

Peer valuation

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
KPR Mill	20.0	14.4	11.3	11.7	9.0	7.0	17.7	22.4	25.6
Arvind	89.7	9.4	6.7	6.6	4.6	4.1	3.1	5.8	7.0

Source: Company; Sharekhan estimates

About company

Arvind is an innovation-driven and customer-centric global textile play present in garment segments such as denim, woven, and 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 will help 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's FY2020 performance was affected by slowdown in the demand environment, while FY2021 performance was affected by COVID-19 led disruption. Improving capacity utilisation of the new garment facilities will drive growth of the textiles business in the medium term. Scaling up of garmenting operations 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. Any 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.
- Sustained slowdown in the garmenting business would continue to affect revenue growth in the near to medium term.

Additional Data

Key management personnel

Sanjay S. Lalbhai	Chairman and Managing Director
Jayesh K. Shah	Whole Time Director and Chief Financial Officer
Ramnik V. Bhimani	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	HDFC Asset Management Co. Ltd.	4.7
2	Franklin Resources Inc.	2.3
3	Dimensional Fund Advisors LP	1.9
4	Vanguard Group Inc.	1.8
5	Kotak Mahindra Asset Management Co	1.8
6	TT International Investment Management	1.8
7	Life Insurance Corporation of India	1.6
8	HSBC Asset Management India Pvt Ltd	1.5
9	Fundrock Management Co SA	1.1
10	Merril Lynch Markets Singapore Pte Ltd	1.1

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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