



## 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

Updated Nov 08, 2021

16.86

## Low Risk

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

Source: Morningstar

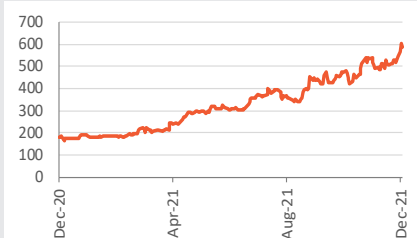
## Company details

Market cap:	Rs. 20,287 cr
52-week high/low:	Rs. 647 / 160
NSE volume: (No of shares)	2.9 lakh
BSE code:	532889
NSE code:	KPRMILL
Free float: (No of shares)	8.7 cr

## Shareholding (%)

Promoters	74.7
FII	3.6
DII	13.4
Others	8.3

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	15.9	32.7	92.1	222.6
Relative to Sensex	20.9	36.1	83.2	201.0

Sharekhan Research, Bloomberg

## KPR Mill Ltd

## Capacity expansion and export demand to drive growth

## Consumer Discretionary

Sharekhan code: KPRMILL

Reco/View: Buy



CMP: Rs. 590

Price Target: Rs. 755



Upgrade



Maintain



Downgrade

## Summary

- We maintain Buy on KPR Mill Limited (KPR) with a revised PT of Rs. 755. Integrated business model, sustained export demand, and strong return profile makes it a best play in the textile space.
- New garment production capacity of 42 million garments is commissioned at Tamil Nadu; garment business revenue is expected to post a CAGR of 22% over FY2021-FY2024 with total capacity of 157 million garments.
- Capital allocation in high RoCE business (garment – 30%; ethanol – 22-23%) will help in improving RoCE to 31.9% in FY2024 from 25.2% in FY2021.
- Export demand remains strong in the US and Europe, while free trade agreement with European Union, retailers/large international players scouting for sustainable supply option in Asia, and US likely to put sanctions on countries such as Bangladesh are potential growth drivers for the company in the medium term.

KPR Mill Limited's (KPR's) integrated business model and expansion in the garment business will help it post sustainable strong revenue growth in the medium term. The company's revenue and PAT posted CAGR of ~6% and ~16%, respectively, over FY2017-FY2021. Higher export demand from US/Europe markets and increased garmenting capacity would help revenues and PAT to grow at CAGR of 16% and 32% (OPM to expand by 367 bps) over FY2021-24. Cumulative free cash flow (FCF) between FY2017-FY2021 stood at over Rs. 800 crore. Cash flows are expected to improve further in the coming years with improved profitability and stable working capital management. Capital allocation in the high RoCE business (garment – 30%; ethanol – 22-23%) will help in improving RoCE to 31.9% in FY2024 from 25.2% in FY2021.

- Expansion of garmenting capacity:** KPR commissioned its new 42 million garment production capacity at Chengapally, Tamil Nadu, in November 2021. With this, the total garment manufacturing capacity will increase to 157 million garments per annum. Capacity expansion will drive the company's growth and help to meet growing market opportunities. With scale-up in garment capacity and increased utilisation, we expect revenue of the garment business to post a 22% CAGR over FY2021-FY2024.
- OPM to stand at 22-23% in H2FY2022:** KPR holds cotton inventory that will last till October. In addition, the cost of inventory held by the company is at a lower price of Rs. 41,000 versus current price of Rs. 61,000. The company will build up cotton inventory in the new season and, with prices currently trading higher, it will impact margins in H2FY2022. Hence, consolidated OPM in H2FY2022 is expected to settle down at 22-23%.
- Return profile to become strong:** KPR has one of strongest balance sheets among textile players with debt-free status and strong cash-generation ability. Its cumulative FCF stood at Rs. 800 crore+ over FY2017-FY2021. Post the expansion of the garment facility and sugar (ethanol) capacity, there are no major capex plans in the immediate terms. Return ratios of the company are expected to improve strongly, with RoE and RoCE at 26.3% and 31.9% in FY2024 from 24.5% and 25.2% in FY2021, respectively, once new garmenting capacity (expected RoCE of 30%) and ethanol capacity (expected RoCE of 25%) use maximum utilisation level along with sustained expansion in OPM.

## Our Call

**View – Maintain Buy with a revised PT of Rs. 755:** KPR's stock price has delivered a strong return of 4.6x since our initiation of the idea in October 2020. Structural changes in the Indian textile industry with improving demand in the export market due to China +1 factor aided KPR to deliver strong financial performance in the past one year. Export demand remains strong in the US and Europe, while free trade agreement (FTA) with European Union, retailers/large international players scouting for sustainable supply option in Asia, and US likely to put sanctions on countries such as Bangladesh are potential growth drivers for the company in the medium term. This along with expanded capacities in the garmenting/sugar division provides strong earnings visibility. Thus, we maintain KPR as one of our top picks in the textile space and maintain our Buy recommendation on the stock with a revised price target (PT) of Rs. 755 (rolling it over FY2024 earnings). The stock is currently trading at 22.8x/17.7x its FY2023/FY2024E EPS.

## Key Risks

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

## Valuations (Consolidated)

Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	3,530	4,517	5,252	6,418
OPM (%)	23.5	26.2	26.7	27.2
Adjusted PAT	515	767	918	1,181
% Y-o-Y growth	36.8	48.7	19.7	28.7
Adjusted EPS (Rs.)	15.0	22.3	26.7	34.3
P/E (x)	39.4	26.5	22.1	17.2
P/B (x)	8.6	6.6	5.2	4.0
EV/EBIDTA (x)	24.9	17.5	14.4	11.2
RoNW (%)	24.4	28.3	26.2	26.3
RoCE (%)	25.2	30.7	30.1	31.9

Source: Company; Sharekhan estimates

## Commissioning of garment production capacity

The company commissioned its new 42 million garment production capacity at Chengapally, Tamil Nadu, in November 2021. With this, the total garment manufacturing capacity will increase to 157 million garments per annum from 115 million garments per annum currently. As per management, capacity utilisation at the new plant will be ramped up gradually in the next nine to twelve months. Of the total incremental capacity, the company plans to utilise 60-70% for existing clients, while the balance will be utilised for new clients. The new garment capacity of 42 million pieces would require around 5,000 workers, of which ~1,000 have already been hired. Management has guided that it takes around 45 days to train the workers and get them ready to join the production facility. Moreover, the company is further exploring opportunities to expand its garment capacity post stabilisation of the current garment expansion project. Capacity expansion will drive growth for the company and help meet growing market opportunities.

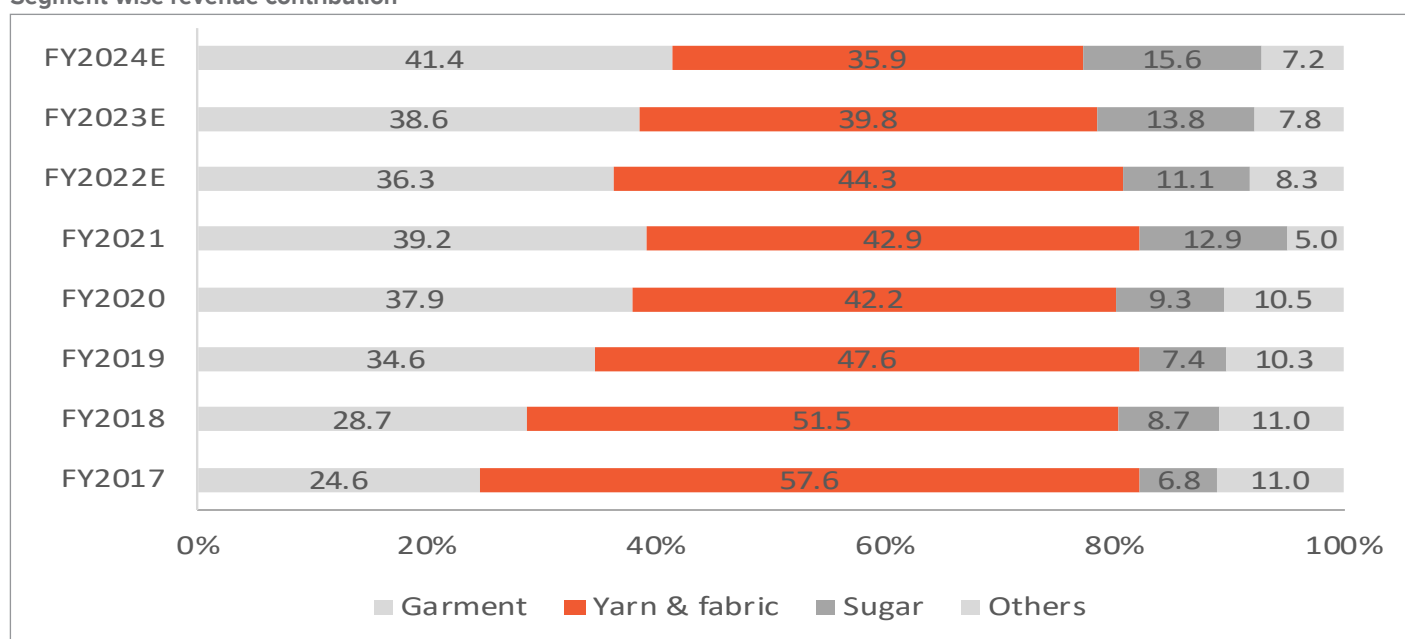
## Favourable demand scenario to aid growth

Management has indicated that the company is witnessing strong customer interest as many large global retailers have begun to reduce their dependence on China and are, consequently, considering India as an alternative sourcing destination. Domestic demand is also expected to improve on account of recovery in the economy with increased mobility and higher vaccination pace. This along with a possible FTA with UK will act as an additional trigger for higher demand for the company's products. We expect the garmenting division's revenue to post a CAGR of 24% over FY2021-FY2024 (while volumes would post an ~18% CAGR) due to strong export demand and capacity expansion of the garmenting division.

## ROCE to improve due to better mix

With capacity expansion in the garment and the sugar divisions, the company expects incremental revenue from both the divisions. With this, the share of garmenting and sugar divisions is expected to increase from 39% and 13% in FY2021 to 41% and 16% in FY2024E, respectively. The company's strategy of focusing on the high asset turnover garmenting segment for future growth provides scope for improvement in return ratios over the medium to longer term. We expect return ratios of the company to improve with RoE and RoCE at 26.3% and 31.9% in FY2024 from 24.5% and 25.2% in FY2021, respectively, once new garmenting capacity (expected RoCE of 30%) and ethanol capacity (expected RoCE of 25%) are used at maximum utilisation level along with sustained expansion in OPM.

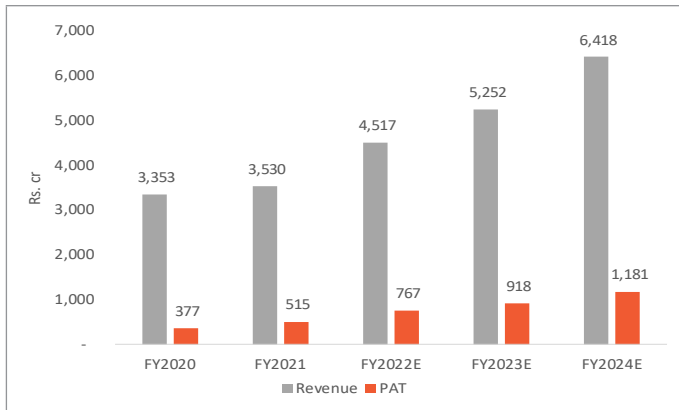
## Segment-wise revenue contribution



Source: Company; Sharekhan research

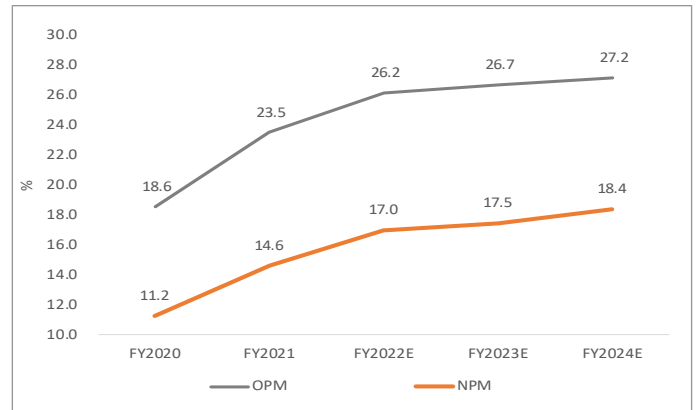
## Financials in charts

### Revenue and profit to grow in the coming years



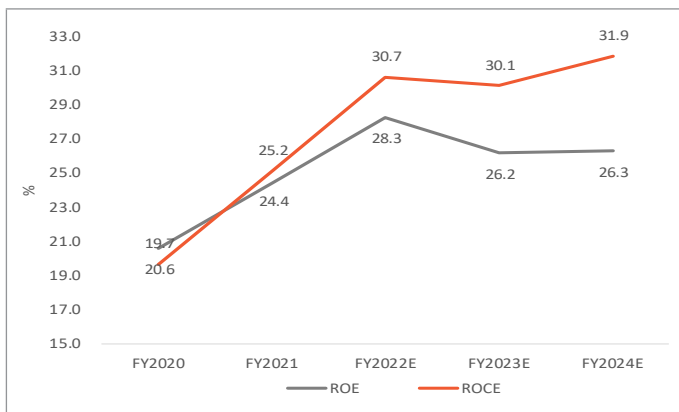
Source: Company, Sharekhan Research

### Margins to improve significantly



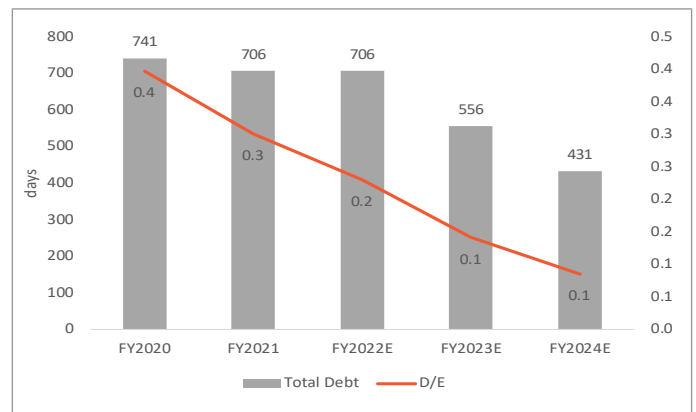
Source: Company, Sharekhan Research

### Higher return ratios in the future



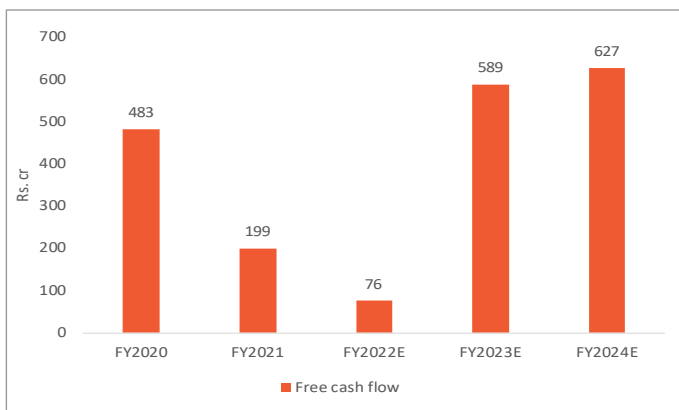
Source: Company, Sharekhan Research

### Company to reduce debt



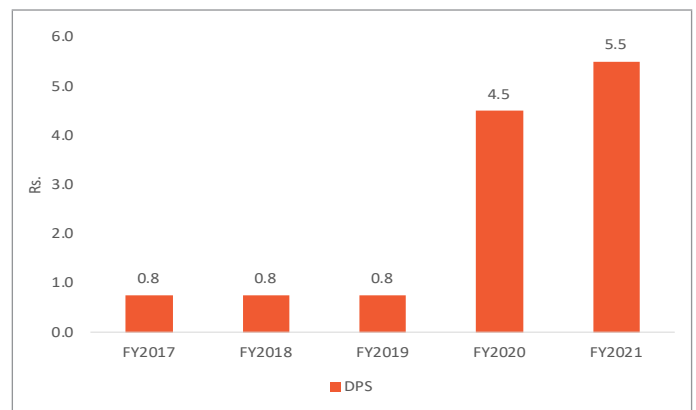
Source: Company, Sharekhan Research

### Trend in free cash flows



Source: Company, Sharekhan Research

### Consistent dividend payout history



Source: Company, Sharekhan Research

## Outlook and Valuation

### ■ Sector outlook – Long-term growth prospects improving

Most textile companies received strong orders from regions such as the US and Europe due to pent-up demand for garment apparels and home textile products as retailers are building up the stock with the gradual opening of economies in most of these regions. The Indian textile industry's long-term growth prospects are intact. Capacity augmentation with value-added products, key export markets focusing on increasing supply from India, and the government's supportive policies provide a scope for textile companies to post robust growth in the long run. With the government extending the RoSCTL Scheme till March 2024 and keeping rates unchanged, it will be beneficial for textile companies and would add to their profitability.

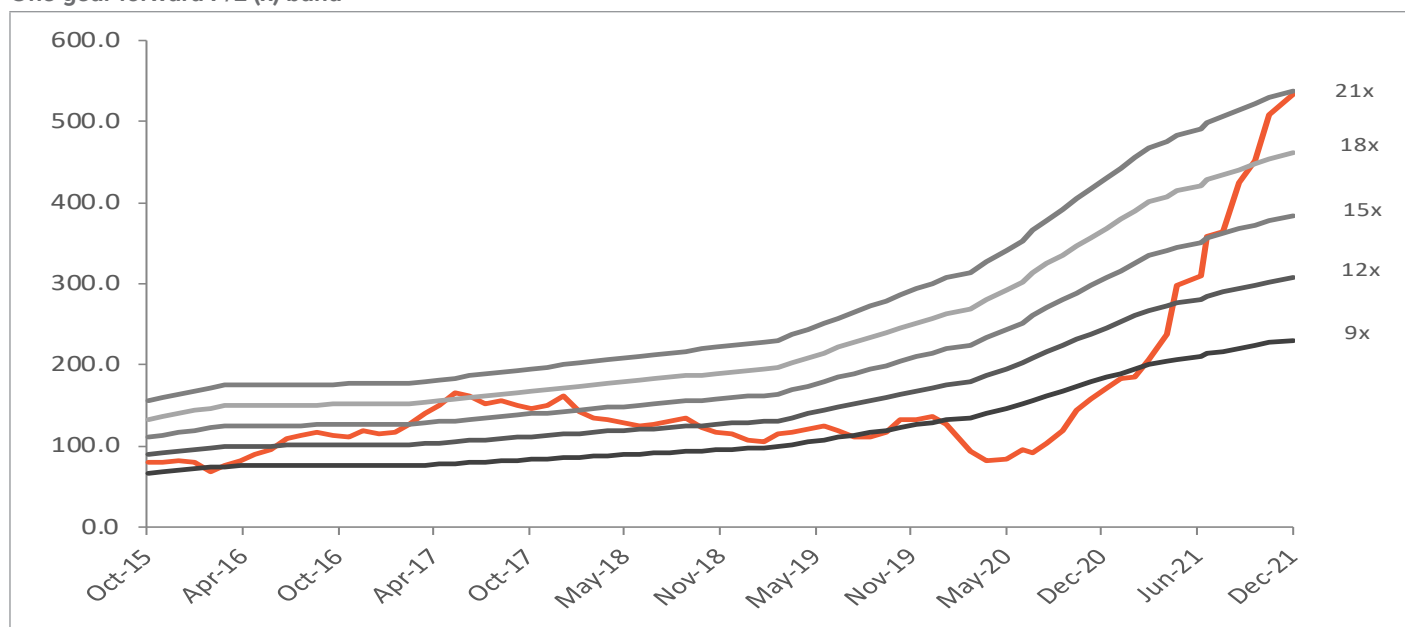
### ■ Company outlook – New garment capacity to drive growth in the long run

KPR continued its strong growth momentum in Q2FY2022 with revenue growing at 28.6% y-o-y and OPM expanding by 894 bps y-o-y. Revenue growth was backed by strong growth in the textile business (growth of 26.5% y-o-y), while higher operating leverage and improved efficiencies aided OPM expansion. The company will be scaling up its garmenting facility by 42 million pieces per annum. With scale-up in garment capacity and increased utilisation, we expect revenue of the garment business to post a 22% CAGR over FY2021-FY2024. This along with increased revenue contribution from the sugar business would lead to strong double-digit revenue growth in the coming years. Higher contribution from value-added yarn products and improving margins of the sugar division will help consolidated margins to stand at 27% in FY2024.

### ■ Valuation – Maintain Buy with a revised PT of Rs. 755

KPR's stock price has delivered a strong return of 4.6x since our initiation of the idea in October 2020. Structural changes in the Indian textile industry with improving demand in the export market due to China + 1 factor aided KPR to deliver strong financial performance in the past one year. Export demand remains strong in the US and Europe, while free trade agreement (FTA) with European Union, retailers/large international players scouting for sustainable supply option in Asia, and US likely to put sanctions on countries such as Bangladesh are potential growth drivers for the company in the medium term. This along with expanded capacities in the garmenting/sugar division provides strong earnings visibility. Thus, we maintain KPR as one of our top picks in the textile space and maintain our Buy recommendation on the stock with a revised PT of Rs. 755 (rolling it over FY2024 earnings). The stock is currently trading at 22.8x/17.7x its FY2023/FY2024E EPS.

#### One-year forward P/E (x) band



Source: Sharekhan Research

#### Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Arvind	-	19.2	10.9	9.7	6.7	5.3	3.1	5.8	8.0
KPR Mill	39.4	26.5	22.1	24.9	17.5	14.4	25.2	30.7	30.1

Source: Company, Sharekhan estimates

## About company

KPR is one of the largest vertically integrated textile manufacturing companies in India present 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 readymade knitted apparel per annum, including a 10-million knitted garment capacity in Ethiopia. KPR has recently forayed into the retail segment with FASO, a 100% organic innerwear, sportswear, and athleisure brand. The company also has sugar business with sugar production capacity of 5,000 TCD, ethanol capacity of 130 KLPD, and power-generation capacity of 40 MW. In FY2021, 65% of the total revenue came from the domestic market, whereas exports contributed 35% to revenue. The company exports 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 a sturdy balance sheet. The strength of its integrated model helps the company to achieve consistent operating margins that are much better than some 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 garment revenue through increased capacity utilisation from the newly commissioned Ethiopia facility are some of the medium to long-term growth drivers for KPR.

## Key Risks

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

## Additional Data

### Key management personnel

KPD Sigamani	Managing Director
KP Ramasamy	Chairman
P Nataraj	CEO & MD
PL Murugappan	CFO
P Kandaswamy	Company Secretary

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	L&T Mutual Fund Trustee Ltd	6.3
2	Franklin Resources	3.2
3	DSP Investment Management	2.3
4	Aditya Birla Sunlife Asset Mgmt	3.0
5	Nippon Life India Asset Mgmt	1.3
6	L&T Investment Management	1.1
7	IDFC Mutual Fund	0.7
8	Dimensional Fund Advisors	0.5
9	Canara Robeco Asset Mgmt	0.3
10	Tata Asset Management	0.1

Source: Bloomberg (Old data)

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## 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 deteriorating 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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Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: [compliance@sharekhan.com](mailto:compliance@sharekhan.com);

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