Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Welspun India Ltd

Growth levers in place

Consumer Discretionary	Sharekhan code: WELSPUNIND
Reco/View: Buy ↔	CMP: **Rs. 143**
Price Target: **Rs. 170** ↔	

↑ 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 14.83

Updated Oct 08, 2021

Low Risk

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

Source: Morningstar

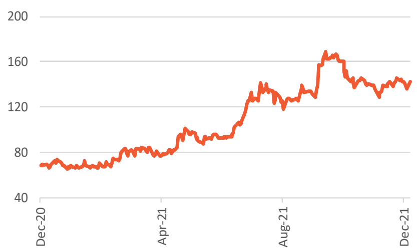
Company details

Market cap:	Rs. 14,085 cr
52-week high/low:	Rs. 171 / 65
NSE volume: (No of shares)	35.0 lakh
BSE code:	514162
NSE code:	WELSPUNIND
Free float: (No of shares)	29.3 cr

Shareholding (%)

Promoters	70.4
FII	8.1
DII	5.8
Others	15.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.4	-8.4	53.1	104.1
Relative to Sensex	9.7	-3.9	44.4	80.7

Sharekhan Research, Bloomberg

Summary

- Welspun India Limited (WIL) expects to maintain double-digit revenue growth in the home textile segment with buoyant demand environment and share gains in US home textile exports. Business is expected to post a CAGR of 15% over FY2021-FY2024.
- Raw-material inflation and higher logistics cost to pull down margins in the near term. Doubling of margin-accretive emerging businesses such as flooring (Rs. 750 crore-800 crore by FY2024) and advanced material (Rs. 650 crore-700 crore by FY2024) would help margins to improve to 20% and above in the coming years.
- The company is targeting to become net cash positive by FY2025-FY2026 by repaying debt of Rs. 500 crore-600 crore per annum because of improving cash flows. RoE and RoCE to improve to 22.9% and 23.2%, respectively, by FY2024 from 16.6% and 1.4% in FY2021.
- We maintain Buy on Welspun India Limited (WIL) with a PT of Rs. 170. The stock is trading at attractive valuation of 14.8x/11.5x its FY2023/FY2024E EPS.

Welpsun India Limited's (WIL) market share in US home textile exports has consistently improved with terry towel export share increasing to 24-25% from 19% in CY2020 and share of bedsheets improving to 16% from 12% in CY2020. Strong acceptance of WIL-owned brands on the online platform is helping the brands to grow at 40%+ in the recent times. The company's B2B business is growing at 7-8%, better than industry growth of 4-5%. Management has indicated strong order book and China + 1 will help to maintain good growth in the home textile space in the coming years. Emerging businesses such as flooring and advanced material are expected to grow more than 2x to Rs. 700 crore-800 crore each by FY2024. This will enable the company's OPM to improve above 20% over the next two years. The company is targeting to become net cash positive by FY2025 with strong cash flows helping debt to reduce in the coming years.

- **Demand for home textile products remains resilient despite pandemic scare:** Despite Omicron scare, demand for home textile products has remained resilient in US and European markets. WIL has a strong order book for H2FY2022, which will help to maintain its strong double-digit revenue growth. Further, management is confident of maintaining strong growth in the medium term, as its market share in key markets is consistently improving and China +1 factor is aiding to gain good orders from key markets. This along with increased capacities would help revenue of WIL's home textile business to post a CAGR of 15% over FY2021-FY2024.
- **Emerging businesses are scaling up well:** WIL's emerging businesses such as flooring and advanced material have strong potential to grow because of product quality and cost advantages. The flooring business is expected to post revenue of Rs. 800 crore by FY2024 from Rs. 318 crore in FY2021 with increased distribution in the domestic market and improving demand due to lower replacement cost of tiles compared to conventional tiles. On the other hand, advanced material business is expected to achieve turnover of Rs. 650 crore-700 crore by FY2024 with strong acceptance for its products, largely used in the medical/industrial segments. Both the businesses are margin accretive, which would help overall profitability to improve in the coming years. WIL's overall OPM to improve to 20%+ over FY2023-FY2024 from current 16-18%.
- **Aim of becoming net cash positive by FY2025-FY2026:** WIL's debt stands at Rs. 2,300 crore. Management targets to achieve EBIDTA of around Rs. 1,600 crore in FY2022 and expects it to consistently improve in the coming years in the backdrop of strong business fundamentals. The company will utilise Rs. 600 crore of EBIDTA for capital expenditure, Rs. 200 crore for buyback, and retain Rs. 180 crore-200 crore of cash on books. Further, the company plans to utilise Rs. 500 crore-600 crore per annum for reduction in debt. Thus, management targets to become net cash positive by FY2025-FY2026.

Our Call

View – Recommend Buy with an unchanged PT of Rs. 170

Market share gains in the home textile market in the US, higher demand from retail clients of Europe/UK coupled with strong growth in B2C business will drive the core home textile business in the near to medium term. Emerging business (including flooring) will add substantially to revenue over the next two to three years. We expect WIL's revenue and PAT to post a CAGR of 16.5% and 31.2%, respectively, over FY2021-FY2024. The stock is currently trading at 11.4x its FY2024E earnings. We maintain our Buy rating on the stock with an unchanged PT of Rs. 170.

Key concern: Any slowdown in any of the key markets, including the US and Europe or sustained increase in key input prices/logistics cost, would act as key risks to our earnings estimates in the near term.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	7,340	8,879	10,454	11,651
OPM (%)	18.4	18.2	19.7	20.8
Adjusted PAT	551	677	973	1,254
Adjusted EPS (Rs.)	5.5	6.7	9.7	12.5
P/E (x)	26.0	21.2	14.7	11.4
P/B (x)	3.9	3.4	2.9	2.4
EV/EBIDTA (x)	12.4	10.5	8.0	6.3
RoNW (%)	16.6	17.3	21.4	22.9
RoCE (%)	14.4	15.2	19.8	23.2

Source: Company; Sharekhan estimates

Demand scenario continues to remain strong

The company continues to witness higher demand growth along with strong order book across geographies with increased consumer spending for hygiene products. According to OTEXA data for US, order levels have surpassed pre-pandemic levels, indicating continued global recovery. Despite Omicron scare, management expects the demand environment to remain strong as China + 1 factor is aiding Indian players to gain good orders. In Europe and the US, online demand continues to remain strong; and WIL supplied its products in these regions through its subsidiaries in UK/US (maintaining inventory of around 30-35% of order), thereby preventing any loss of order/delay in orders due to supply constraints of unavailability of containers for shipment. The company has witnessed market share gains in markets such as the US (70% of overall revenue) with the terry towel market share having improved to 24-25% from 19% in December 2020, while the bedsheet market's share has improved to 16% from 12% in December 2020. Own brands are growing at a much faster rate of 35-40% (through online channels) compared to B2B sales in the US (growing at 5-7%). Contribution of the branded business is expected to go to 15% of revenue by FY2024 compared to 8% in FY2021. In the US, the company targets double-digit growth during FY2022.

OPM to remain under pressure in the near term; Expected to improve by 19-20% in FY2023

The company expects margins to remain under pressure in the near term due to logistics/raw-material headwind. Commodity price inflation and supply-side constraints continue with cotton prices touching 10-year high level in October 2021, coal prices moving from $55 per barrel to more than $170 per barrel, sea freight increasing 3x y-o-y, increasing warehousing costs, and higher supply chain lead time of 60-90 days. This led to EBITDA loss of around ~2% in Q2FY022. Cotton comprises 50% of the total cost. The company had sufficient inventory of cotton till November 2021 at prices similar to last year price of Rs. 45,000 per candy, which reduced the pressure on gross margins. If higher cost of freight, raw-material inflation, and logistical issues sustain, it will put stress on margins in the near term. To mitigate the impact of logistics/raw-material headwind, the company has undertaken one round of price hike at the start of year and took the second round of price increase in October 2021 (full impact of price hikes would come in from Q4). The company expects cotton prices to correct in the second half of the year, which will help margins to come back on track. This along with scale up in the flooring and advance material business (margin-accretive businesses) would help the company to post OPM of 19-20% in FY2023, which would consistently improve in the subsequent years.

Flooring business to grow by 3x to reach Rs. 1,000 crore by FY2025

WIL started the flooring business in February 2020 with an aim to cater to replacement demand in the Indian market, which has a market size of ~Rs. 6,000 crore (expected to grow to Rs. 8,000 crore-9,000 crore in 4-5 years). However, due to COVID-19, the company started exports for this business. Currently, domestic market share of the flooring business is 25%, but management has guided for a mix of 50:50 for domestic and international business in the next three-five years. Flooring products are currently sold through 100 dealers in India. The company is endeavouring to add more dealers in the coming years. With easing COVID-19 restrictions, the carpet business has seen strong traction with orders coming from UK, Middle East, US, Canada, and New Zealand, including repeat orders. The company is targeting the flooring business to contribute revenue of Rs. 1,000 crore by FY2025. The company is planning to do capital allocation of Rs. 1,200 crore for the flooring business; and with optimum capacity utilisation (85-90%), revenue of the flooring business is expected to go up to Rs. 2,300 crore-2,400 crore in 2-3 years (2x asset turnover) with working capital days expected to remain constant at 75-80 days. The company plans to achieve this growth from expanding its distribution reach and because of lower replacement cost. Replacement cost of WIL's flooring products is lesser as compared to vitrified tiles. Moreover, WIL offers five-year warranty for flooring products and replacement time is just one day compared to other tile forms. Both these factors will aid in the growth of the flooring business.

Comparison of replacement cost (Cost per sq feet)

Particulars	Welspun tiles	Vitrified tiles
Tile cost	Rs. 150-160	Rs. 150-160
Labour cost	Rs. 5	Rs. 80-100
Total cost	Rs. 155-165	Rs. 230-260

Source: Company; Sharekhan research

Advanced textile business gaining momentum

In advanced textile, WIL caters to segments such as industrials and medical usage. The company received strong demand for these products during COVID-19 and expects demand to continue to remain strong. Management expects the advanced textile business to grow at over 30% and expects to achieve a turnover of Rs. 400 crore in FY2022 and Rs. 650 crore-700 crore by FY2024 (asset turnover of 2x at optimum capacity utilisation) with working capital days stable at 75-80 days.

Aim of becoming net cash positive by FY2025-FY2026

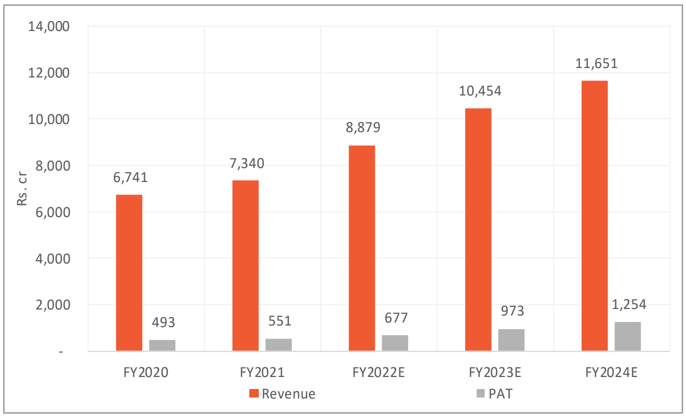
The company's current debt stands at Rs. 2,300 crore, which is expected to reduce to Rs. 2,200 crore by the end of FY2022. Management targets to achieve EBIDTA of around Rs. 1,600 crore in FY2022. The company will utilise Rs. 600 crore of EBIDTA for capital expenditure, Rs. 200 crore for buyback, and retain Rs. 180 crore-200 crore of cash on books. Further, the company plans to utilise Rs. 600 crore to pay-off debt. With double-digit growth in revenue and sustained improvement in profitability, WIL aims to become net cash positive by FY2025. With sustained reduction in debt, interest cost of the company is expected to reduce consistently over the next two to three years.

Other key highlights

- The company entered the Dow Jones Sustainability World Index in December 2021 due to strong environmental performance as well as significant improvement in its social and governance impact parameters. In its maiden ranking on the DJSI, WIL's ESG Score stands at 48, which is over 62% higher than the average industry score. Additionally, with a score of 45, the entity's environmental dimension scores are 75% higher than the industry's average, while the social dimension score, at 50, is 54% higher than the industry's average. Sharp focus on product innovation, customer centricity, inclusive growth, and resource efficiency have led to WIL's entrance into the prestigious sustainability indices. This reaffirms the company's strategic efforts to integrate ESG drivers and a circular approach in all aspects of its operations.
- Management has indicated that the company is currently evaluating whether it will apply for the PLI scheme for advanced textiles. This comes on the backdrop of stringent rules and regulations that need to be complied with while applying for the scheme.
- The current geographical distribution of the company includes 70% contribution from US, 15-16% from US and Europe, 5% from India, and 10% from rest of the world. Management stated that rest of the world is registering a higher growth rate as compared to the other regions.
- Emerging businesses (including flooring and advance materials) are expected to be key revenue growth drivers in the long run and would help the company's revenue and PAT to post CAGR of 17% and 30%, respectively, over FY2021-FY2024.

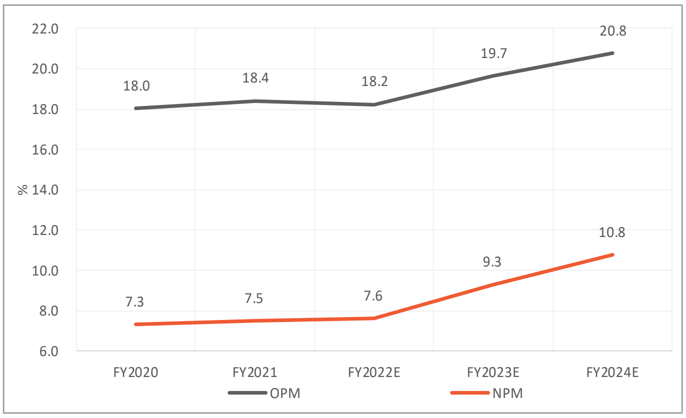
Financials in charts

Revenue and profit to grow in the coming years



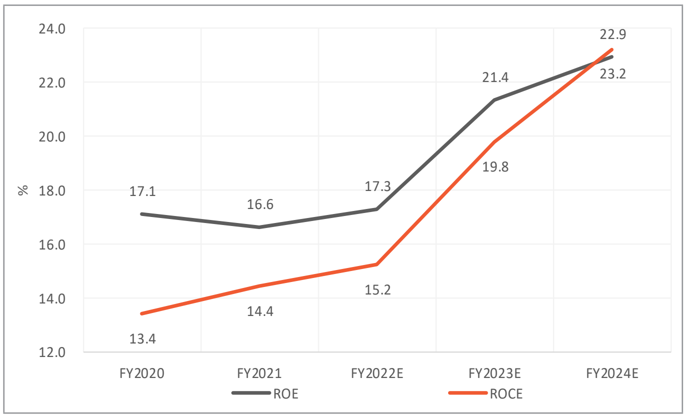
Source: Company, Sharekhan Research

Margins to improve significantly



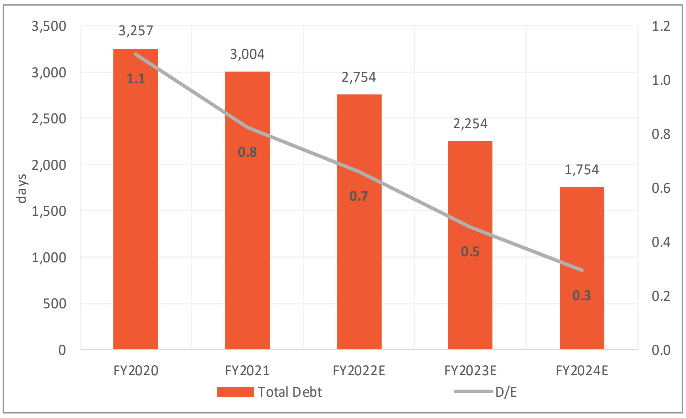
Source: Company, Sharekhan Research

Higher return ratios in the future



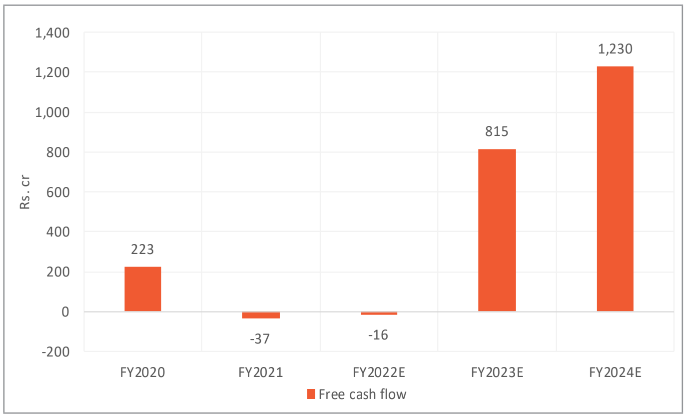
Source: Company, Sharekhan Research

Company to reduce debt



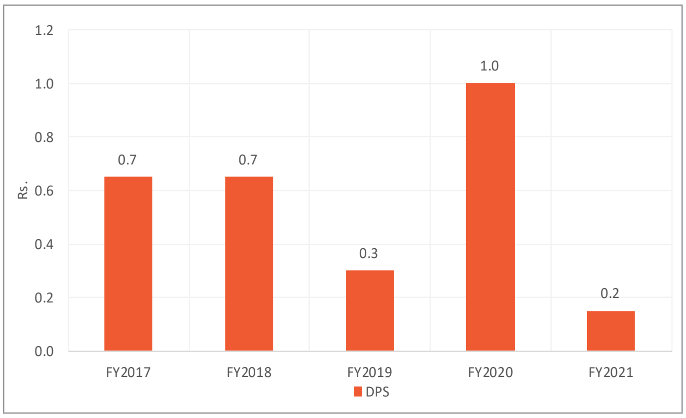
Source: Company, Sharekhan Research

Trend in free cash flows



Source: Company, Sharekhan Research

Consistent dividend payout history



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector Outlook – India's share in US home textile improving

The Indian home textile sector is reaping the benefits of market share gains in export markets such as the US and Europe with top competitors such China losing market share in the past two years. India's share in bedlinen export to the US has improved to 58% from ~50% in CY2019; while in terry towel exports, it has improved to 44% from 39% in CY2019. This along with sustained strong demand due to higher focus on home hygiene in the pandemic environment provided home textile companies strong growth levers. Top players such as WIL and HSL have expanded the capacities for bed linen/terry towel sensing to fulfil strong demand coming in from key markets because of higher spends on hygiene products and customers looking at India as an alternate supply base.

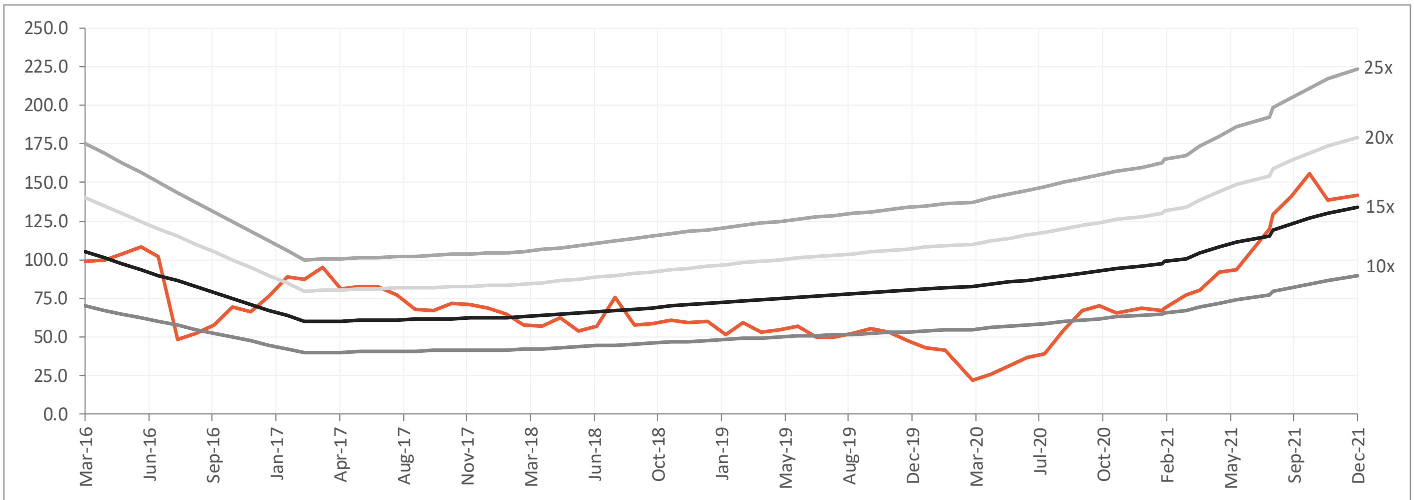
■ Company Outlook – Capacity expansion and scale up in the emerging business to drive growth

Recovery in the domestic and exports market led to strong performance in Q2FY2022. The company expects to maintain double-digit revenue growth momentum over FY2021-FY2023, driven by sustained good demand for home textile products in the US market and scale up in the advance textile, flooring, and branded business. On the other hand, increased cotton and yarn prices coupled with higher freight cost will put stress on margins in the near term. However, a better mix and scale up in revenue of the margin-accretive businesses such as flooring and advanced material would help OPM to improve to 20% in FY2023 and would consistently improve in the subsequent years. We expect WIL's revenue and PAT to post a CAGR of 16.5% and 31.2%, respectively, over FY2021-FY2024.

■ Valuation – Recommend Buy with an unchanged PT of Rs. 170

Market share gains in the home textile market in the US, higher demand from retail clients of Europe/UK coupled with strong growth in B2C business will drive the core home textile business in the near to medium term. Emerging business (including flooring) will add substantially to revenue over the next two to three years. We expect WIL's revenue and PAT to post a CAGR of 16.5% and 31.2%, respectively, over FY2021-FY2024. The stock is currently trading at 11.4x its FY2024E earnings. We maintain our Buy rating on the stock with an unchanged PT of Rs. 170.

One-year forward P/E (x) band



Source: Company, Sharekhan research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21E	FY22E	FY23E
KPR Mill	40.6	27.3	22.8	25.7	18.0	14.8	25.2	30.7	30.1
Himatsingka Seide	-	11.0	5.4	15.0	7.1	4.6	3.3	11.1	17.8
Welspun India	26.0	21.2	14.7	12.4	10.5	8.0	14.4	15.2	19.8

Source: Company, Sharekhan estimates

About company

WIL, a Welspun Group company, started its activities in 1985 as Welspun Winilon Silk Mills Private Limited, a synthetic yarn business, which went on to become Welspun Polyesters (India) Limited and, finally, Welspun India Limited emerged in 1995. The company offers a variety of products such as towels in different sizes and qualities, bedsheets using state-of-the-art technology, and the best quality of Egyptian cotton. WIL is Asia's largest and is among the top four terry towel producers in the world (number one player in the US). The company's business is spread across continents and has a distribution network in 50+ countries, such as US, UK, Canada, Australia, Italy, Sweden, and France. About 95% of the total products are exported.

Investment theme

WIL is one of the leading players in the global textile market with capacities of 80,000 metric tonne (MT) and 90 million metres of terry towels and bedlinen capacity largely catering exports markets. The company will benefit from recovery in the US, where it has a market share of 19% and 13% in the terry towel and bed sheets segments, respectively. New ventures such as flooring business and advance textile revenue would add on to revenue in the near to medium term. This along with benign cotton prices and improved revenue mix would aid in improving profitability consistently in the near to medium term. Improving cash flows would aid the company to reduce debt on books over FY2021-FY2023.

Key Risks

- **Decline in revenue of key exporting markets:** Any decline in the revenue of key exporting markets such as US and Europe due to change in the trade policy, slowdown in the macro environment, or increased competition from other international players would be key risks to our earnings estimates.
- **Unfavourable currency movement:** About 95% of WIL's revenue comes from export markets such as the US and Europe. Hence, any adverse currency movement would act as a key risk to revenue growth.
- **Increased cotton prices:** Any significant increase in global cotton prices (including Egypt) would act as a key risk to profitability.

Additional Data

Key management personnel

Rajesh Mandawewala	Executive Director and MD
Dipali Goenka	CEO-MD
Sanjeev Sancheti	Chief Financial Officer
Shashikant Thorat	Company Secretary and Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	DSP Investment Managers Pvt. Ltd.	3.5
2	Life Insurance Corp. of India	1.9
3	L&T Mutual Fund Trustee Ltd./India	1.2
4	The Vanguard Group Inc.	1.1
5	Dimensional Fund Advisors LP	0.9
6	Aditya Birla Sun Life Asset Manage	0.7
7	Norges Bank	0.5
8	BlackRock Inc.	0.5
9	GAM Holding AG	0.2
10	Birla Sun Life Insurance Co. Ltd.	0.2

Source: Bloomberg (Old data)

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

Know more about our products and services

For Private Circulation only

Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;