Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

KPR Mill Ltd

Mixed Q3; Improved outlook

Stock Update

Result Update

Consumer Discretionary	Sharekhan code: KPRMILL

Reco/View: Buy	↔	CMP: Rs. 536	Price Target: Rs. 640	↔

↑ 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 16.86

Updated Dec 08, 2022

Low Risk

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

Source: Morningstar

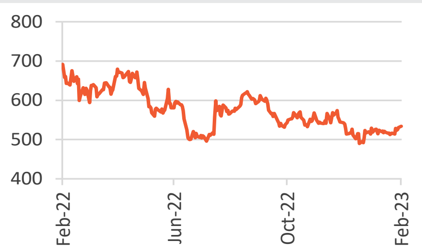
Company details

Market cap:	Rs. 18,321 cr
52-week high/low:	Rs. 727 / 480
NSE volume: (No of shares)	3.1 lakh
BSE code:	532889
NSE code:	KPRMILL
Free float: (No of shares)	8.6 cr

Shareholding (%)

Promoters	74.8
FII	3.5
DII	13.9
Others	7.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	2.0	-0.9	-6.4	-18.6
Relative to Sensex	2.7	0.3	-8.8	-22.8

Sharekhan Research, Bloomberg

Summary

- KPR Mill (KPR) posted mixed performance in Q3FY2023, with revenue growing by 13.6% y-o-y, while negative operating leverage impacted both gross margin and EBITDA margin, which declined sharply by 434 bps and 544 bps y-o-y, to 39.4% and 18.8%, respectively, leading to a 17.6% y-o-y decline in PAT to Rs. 175 crore.
- Management has guided for overall revenue growth of 10% per annum for the next 2-3 years, aided by capacity expansion across businesses coupled with recovery in export demand. Further, positive operating leverage will drive margins improvement.
- Integrated business model along with a strong capacity expansion plan in the sugar and textile business would aid faster recovery for KPR, once the demand scenario improves. Higher free cash flow generation of Rs. 1,300 crore over FY2024/FY2025E will aid future capacity expansion programme. Ethanol blending could also be an additional growth lever.
- At 19x/15x its FY2024E/FY2025E EPS and 12x/10x its FY2024E/FY2025E EV/EBITDA, the stock offers favourable risk reward. We maintain our Buy recommendation on the stock with an unchanged PT of Rs. 640.

Q3FY2023 was mixed bag show for KPR Mill with revenue growth at 13.6% y-o-y to Rs. 1,431 crore, while gross margin and EBITDA margin declined by 434 bps and 544 bps y-o-y to 39.4% and 18.8%, respectively, and PAT declined by 17.6% y-o-y to Rs. 175 crore. Profitability was impacted by higher input cost, unfavourable mix, higher employee expenses, and increased other expenses. Revenue of the textile business grew by 10.3% y-o-y to Rs. 1,152 crore, aided by strong performance by the garment segment, while the fabric and yarn segment posted a muted quarter. Garment volumes were higher by 6.4% y-o-y, while fabric and yarn volume witnessed a decline of 4.2% y-o-y. PBIT margin of the textile business contracted by 872 bps y-o-y to 13.3%. Sugar business revenue grew by 28% y-o-y to Rs. 252.7 crore and PBIT margin sharply improved from 16.7% in Q3FY2022 to 33.7% in Q3FY2023. For 9MFY2023, revenue grew by 25% y-o-y to Rs. 4,072 crore, while EBITDA margin fell by 359 bps to 22.5% and PAT declined by 2.7% y-o-y to Rs. 605 crore. The company declared an interim dividend of Rs. 2 per share for FY2023.

Key positives

- Garment revenue is up 33% y-o-y, led by 6.4% volume growth and 25.2% realisation growth.
- Sugar business reported strong 28% y-o-y revenue growth; margins up from 16.7% in Q3FY2022 to 33.7% in Q3FY2023.

Key negatives

- Yarn and fabric revenue fell by 10.6% y-o-y due to a 4.2% decline in volume and a 6.6% dip in realisation.
- Gross/EBITDA margin declined by 434 bps/544 bps y-o-y and by 772 bps/725 bps q-o-q to 39.4%/18.8%, respectively.
- Textile business margin sharply declined by 872 bps y-o-y.
- Net debt at 9MFY2023-end increased to Rs. 730 core from Rs. 708 crore at FY2022-end.

Management Commentary

- KPR has announced capacity expansion and modernisation across its multiple facilities and businesses, including ethanol capacity expansion from existing 130 KLPD to 250 KLPD at a cost of Rs. 250 crore by FY2024, setting up a spinning mill for viscose yarn production at an outlay of Rs. 100 crore by FY2024, capacity expansion of its solar power plant by 12 MW at a cost of Rs. 50 crore by FY2023-end, and debottlenecking its existing processing and printing facilities at a cost of Rs. 50 crore. All these projects would incrementally add ~Rs. 100 crore to revenue in FY2024 and aid in improving the company's profitability.
- Order book for the garment business stands above Rs. 1,000 crore at Q3FY2023-end and the demand outlook is stable. Margin of the garment business came in at 21% in Q3FY2023 and the target margin for the garment business is at 22-24%.
- Sugar sales volume for the quarter was reported at 42,000 tonne, out of which 20,000 tonne was exported. Recovery rate (gross) in Q3FY2023 came in at 10.5-10.75%, while blended realisation for domestic and exported sugar stood at Rs. 33.5 per kg in Q3FY2023. The company targets 22-25% margin for the sugar business in the medium-long term.
- Management has guided 10% revenue growth per annum for the next 2-3 years. In terms of margins, management expects to maintain 9MFY2023 margin (~23%) for FY2023 and further improvement in margin is expected as the price of cotton stabilises.

Revision in estimates – We have lowered our earnings estimates for FY2023 due to lower-than-earlier-expected margins, while we broadly maintain our estimates for FY2024 and FY2025, as we retain the outlook over the medium-long term.

Our Call

View: Green shoots visible, Buy with an unchanged PT of Rs. 640: Notwithstanding, muted near-term performance owing to uncertainties in the export market, long-term growth prospects looks solid, led by India's emerging strength in textile exports. Further, an integrated business model along with strong capacity expansion plan in the sugar and textile business would aid faster recovery for KPR, once the demand scenario improves. Higher free cash flow generation of Rs. 1,300 crore over FY2024/FY2025E will aid future capacity expansion program. Ethanol blending could also be an additional growth lever. At 19x/15x its FY2024E/FY2025E EPS and 12x/10x its FY2024E/FY2025E EV/EBITDA, the stock offers favourable risk reward. We maintain our Buy recommendation on the stock with an unchanged price target (PT) of Rs. 640.

Key Risks

Any sustained slowdown in the the global export market due to inflationary pressure or any significant increase in input prices would act as a key risk to our earnings estimates.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E	FY25E
Revenue	3,530	4,822	5,533	6,403	7,475
EBITDA Margin (%)	23.5	25.3	22.7	23.8	24.5
Adjusted PAT	515	842	779	975	1,217
% Y-o-Y growth	36.8	63.4	-7.5	25.1	24.8
Adjusted EPS (Rs.)	15.0	24.5	22.6	28.3	35.4
P/E (x)	35.9	22.0	23.8	19.0	15.2
P/B (x)	7.9	5.8	4.7	3.8	3.1
EV/EBITDA (x)	22.8	15.8	15.0	12.0	9.7
RoNW (%)	24.4	30.4	21.9	22.3	22.5
RoCE (%)	25.2	31.0	23.5	25.7	27.6

Source: Company; Sharekhan estimates

Mixed Q3 – Revenue growth at 14% y-o-y; EBITDA margin down 434 bps y-o-y

Revenue grew by 13.6% y-o-y and 17.3% q-o-q to Rs. 1,431 crore in Q3FY2023, led by 10% y-o-y growth in the textile business revenue, while revenue of the sugar business grew by 28% y-o-y. Garments production stood flat at 32 mn garments, while garment sales increased by 6% y-o-y to 9.4 mn garments. Yarn and fabric sales volume declined by 4.2% y-o-y to 16,980 MT. Gross margin and EBITDA margin declined by 434 bps and 544 bps y-o-y and by 772 bps and 725 bps q-o-q to 39.4% and 18.8%, respectively, due to higher raw- material cost, unfavourable mix, increased employee expenses, and higher other expenses. PBIT margin of the textile business contracted by 872 bps y-o-y to 13.3%. PBIT margin of the sugar business sharply improved from 16.7% in Q3FY2022 to 33.7% in Q3FY2023. EBIDTA declined by 12% y-o-y to Rs. 269 crore. The decline in EBITDA coupled with lower other income and higher interest expense led to a 17.6% y-o-y dip in adjusted PAT to Rs. 175 crore. Net debt at 9MFY2023-end stood at Rs. 730 core (up from Rs. 708 crore at FY2022-end). The company declared an interim dividend of Rs. 2 per share for FY2023.

Mixed quarter for the textile business

Textile business revenue grew by 10.3% y-o-y to Rs. 1,152 crore, aided by strong performance by the garment segment, while the fabric and yarn segment posted a muted quarter. The garment business reported revenue of Rs. 597 crore in Q3FY2023, registering 33.3% y-o-y growth, aided by 6.4% y-o-y growth in sales volume to 29.4 million garments and 25.2% y-o-y growth in the realisation to Rs. 203 per piece. Fabric and yarn business revenue declined by 10.6% y-o-y to Rs. 499 crore in Q3FY2023 impacted by a 4.2% y-o-y decline in sales volume to 16,980 MT and a 6.6% dip in realisation to Rs. 294 per tonne. PBIT margin of the textile business contracted by 872 bps y-o-y to 13.3%.

Garment and fabric and yarn volumes and realisation

Particulars	Q3FY22	Q3FY22	y-o-y	Q2FY23	q-o-q
Garment					
Production (mn pieces)	31.9	32.2	-1.0	31.9	0.0
Sales (mn pieces)	29.4	27.6	6.4	25.3	16.1
Realisation (Rs./piece)	203.2	162.3	25.2	207.1	-1.9
Fabric and yarn					
Sales **(MT)**	16,980	17,731	-4.2	14,628	16.1
Realisation (Rs./tonne)	293.9	314.7	-6.6	366.4	-19.8

Source: Company, Sharekhan Research

Strong performance by the sugar business

Sugar business revenue grew by 28% y-o-y to Rs. 252.7 crore in Q3FY2023. PBIT margin sharply improved from 16.7% in Q3FY2022 to 33.7% in Q3FY2023.

Key conference call highlights

- **Multiple modernisation and expansion plans underway:** The company has announced capacity expansion and modernisation across its multiple facilities and businesses. KPR plans to expand its ethanol capacity from existing 130 KLPD to 250 KLPD at a cost of Rs. 250 crore by FY2024. The investments will be partly from internal accrual and partly through term loan availed at a lower interest rate. This expansion will lead to incremental revenue of Rs. 50 crore for the sugar business. The company is also looking to set up a spinning mill for viscose yarn production at an outlay of Rs. 100 crore to be funded through internal accruals by FY2024. KPR has also announced capacity expansion of its solar power plant by 12 MW at a cost of Rs. 50 crore to be funded by internal accruals by FY2023-end. For its processing and printing division, the company would be debottlenecking its existing facilities at a cost of Rs. 50 crore (to be funded from internal accruals), which would lead to a 20% increase in production. Management has guided that all these projects would incrementally add ~Rs. 100 crore to revenue in FY2024 and aid in improving the company's profitability.
- **Lower margins in the yarn and fabric business:** During the quarter, the company sold 15,000 tonne of yarn, generating a revenue of Rs. 450 crore, while fabric revenue was registered at Rs. 50 crore, with sales volume of 1,700 tonne. The business reported lower margins of 14% during the quarter.
- **Garments business maintained good traction:** Management has indicated that the order book for the garment business stands above Rs. 1,000 crore at Q3FY2023-end. KPR targets 35-36 million garment production per quarter. Garment business margin came in at 21% in Q3FY2023 and the target margin for the garment business is at 22-24%.

- **Strong Q3 for the sugar business:** Out of the total Rs. 252 crore revenue generated from the sugar business, Rs. 115 crore came from the sugar segment, Rs. 102 crore came from the ethanol segment, while the remaining Rs. 35 crore came from the power segment. Sugar sales volume for the quarter was reported at 42,000 tonne, out of which 20,000 tonne was exported. Recovery rate (gross) in Q3FY2023 came in at 10.5-10.75%, while blended realisation for domestic and exported sugar stood at Rs. 33.5 per kg in Q3FY2023. As per management, the company has received annual quota to export 27,000 tonne, out of which 7,000 sugar will be exported in Q4. The company targets 22-25% margin for the sugar business in the medium-long term.
- **Lower raw-material inventory due to volatile prices:** Management indicated that the company is maintaining lower level of cotton inventory (current inventory level is two months) as there is vast fluctuation in cotton prices. However, if cotton prices go down to Rs. 60,000 per candy, then the company might keep higher inventory, which would aid in recovering the margins.
- **Outlook maintained for the medium-long term:** Management has guided 10% revenue growth per annum for the next 2-3 years. In terms of margins, management expects to maintain 9MFY2023 margin (~23%) for FY2023 and further margin improvement is expected as the price of cotton stabilises.

Results (Consolidated) Rs cr

Particulars	Q3FY23	Q3FY22	y-o-y (%)	Q2FY23	q-o-q (%)
Total Revenue	**1,431.4**	**1,260.5**	**13.6**	**1,220.0**	**17.3**
Raw material cost	866.8	708.6	22.3	644.5	34.5
Employee cost	140.8	112.0	25.7	131.4	7.1
Other expenses	155.3	134.7	15.2	126.7	22.5
Total operating cost	1,162.8	955.3	21.7	902.6	28.8
EBITDA	**268.7**	**305.2**	**-12.0**	**317.4**	**-15.3**
Other income	13.3	25.4	-47.8	20.6	-35.5
Interest and Other Financial Cost	19.7	5.6	-	21.0	-6.0
Depreciation	29.4	41.8	-29.7	49.6	-40.9
Profit Before Tax	**232.8**	**283.2**	**-17.8**	**267.3**	**-12.9**
Tax	58.2	71.5	-18.5	64.0	-9.0
Adjusted PAT	**174.6**	**211.8**	**-17.6**	**203.3**	**-14.1**
Adjusted EPS (Rs.)	5.1	6.2	-17.0	5.9	-14.1
			bps		**bps**
GPM (%)	39.4	43.8	-434	47.2	-772
EBITDA Margin (%)	18.8	24.2	-544	26.0	-725
NPM (%)	12.2	16.8	-461	16.7	-447
Tax rate (%)	25.0	25.2	-21	23.9	108

Source: Company, Sharekhan Research

Segment-wise performance Rs cr

Particulars	Q3FY23	Q3FY22	y-o-y %	Q2FY23	q-o-q %
Revenue					
Textile	1,152.4	1,045.0	10.3	1,109.5	3.9
% Contribution to total revenue	*80.5*	*82.9*		*90.9*	
Garment (a)	597.0	448.0	33.3	524.0	13.9
Fabric and yarn (b)	499.0	558.0	-10.6	536.0	-6.9
Sugar	252.7	197.3	28.1	82.6	-
% Contribution to total revenue	*17.7*	*15.6*		*6.8*	
Others	26.4	18.2	44.9	27.9	-5.3
Total revenues	**1,431.4**	**1,260.5**	**13.6**	**1,220.0**	**17.3**
PBIT margin (%)			**bps**		**bps**
Textile	13.3	22.0	-872	25.3	-
Sugar	33.7	16.7	-	-17.2	-

Source: Company, Sharekhan Research

Outlook and Valuation

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

Export demand would stay uncertain as inflation, rising interest rates, and geopolitical disturbances reduce demand visibility in global markets. The value segment in the domestic market witnessed a drop in demand. However, the same is expected to see some pick up in the quarters ahead. The 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 would benefit and report higher profitability, as the government has extended the RoSCTL scheme until March 2024 and s keeping rates unchanged. Margins are likely to remain volatile in the near term but are likely to improve in FY2024. Cotton prices are expected to soften moderately by November upon new crop arrival and margins are expected to improve in the quarters ahead.

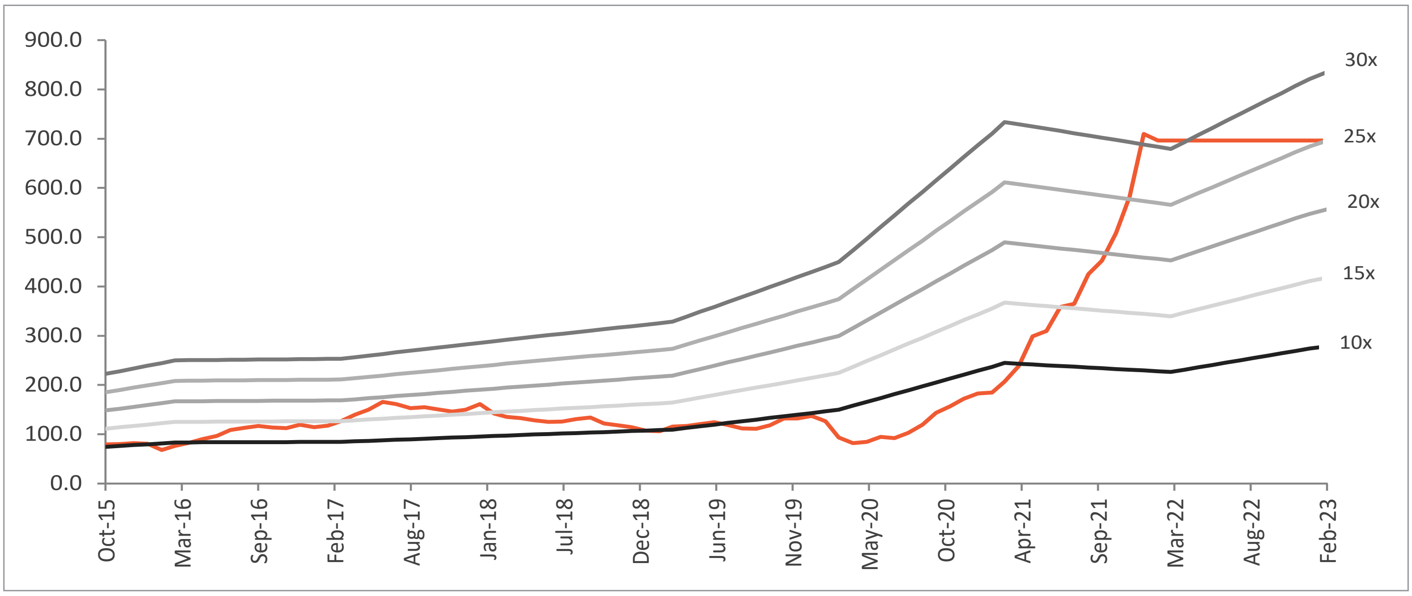
■ Company outlook - Near-term outlook weak; Long-term growth prospects intact

KPR posted mixed performance in Q3FY2023, with revenue growing by 13.6% y-o-y, while gross margin and EBITDA margin declined sharply by 434 bps and 544 bps y-o-y to 39.4% and 18.8%, respectively, leading to a 17.6% y-o-y decline in PAT to Rs. 175 crore. Slowdown in the export market would continue to impact the business in the near term. We expect the company to reap benefits of expanded garment capacity with recovery in export demand (likely in FY2024). The decline in cotton/yarn prices will provide some relief on margins. We expect the company's revenue and PAT to report CAGR of 15.7% and 13.1%, respectively, over FY2022-2025E.

■ Valuation - Green shoots visible, Buy with an unchanged PT of Rs. 640

Notwithstanding, muted near-term performance owing to uncertainties in the export market, long-term growth prospects looks solid, led by India's emerging strength in textile exports. Further, an integrated business model along with strong capacity expansion plan in the sugar and textile business would aid faster recovery for KPR, once the demand scenario improves. Higher free cash flow generation of Rs. 1,300 crore over FY2024/FY2025E will aid future capacity expansion program. Ethanol blending could also be an additional growth lever. At 19x/15x its FY2024E/FY2025E EPS and 12x/10x its FY2024E/FY2025E EV/EBITDA, the stock offers favourable risk reward. We maintain our Buy recommendation on the stock with an unchanged PT of Rs. 640.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Companies	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Arvind	9.9	7.2	5.1	5.1	4.8	3.5	7.7	8.2	10.0
KPR Mill	21.9	23.7	18.9	15.7	15.0	12.0	31.0	23.5	25.7

Source: Company; Sharekhan Research

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 1,04,000 MT of yarn per annum; 40,000 MT of fabric per annum; and 157 million ready-made knitted apparel per annum; and a 25,000 MT fabric processing capacity. KPR has recently forayed into the retail segment with FASO, a 100% organic innerwear, sportswear, and athleisure brand. The company also has a sugar business, with sugar production capacity of 20,000 TCD, ethanol capacity of 360 KLPD, and power-generation capacity of 90 MW. In FY2022, 62% of the total revenue came from the domestic market, whereas exports contributed 38% to revenue. The company exports to over 60 countries, including Europe, Australia, and the U.S.

Investment theme

KPR is one of India's largest vertically integrated textile players, which has a steady financial record with a sturdy balance sheet. The strength of its integrated model helps the company to achieve consistent EBITDA margin, which is much better than some exporting peers. A shift in base from China to India, addition of more international clients, transforming itself from a volatile yarn business to a profitable garment business, scale-up in the retail business, and scale-up in garmenting 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 can affect the company's profitability.

Additional Data

Key management personnel

KP Ramasamy	Chairman
KPD Sigamani	Managing Director
P. Nataraj	CEO and MD
P.L. Murugappan	CFO
P. Kandaswamy	Company Secretary and Compliance Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	SBI Funds Management Ltd.	3.85
2	L & T Mutual Fund Trustee Ltd.	2.08
3	DSP Investment Managers	1.68
4	DSP Value Fund	1.57
5	Nippon Life India Asset Management Company	1.27
6	Vanguard Group Inc.	0.78
7	Axis AMC	0.64
8	Franklin Resources Inc.	0.6
9	Aditya Birla Sun Life AMC	0.44
10	IDFC Mutual Fund	0.42

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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