

# Welspun India

## Whole new weave

### Leveraging innovation, branding to transform into a B2C player

Welspun India (WLSI IN) is increasingly transforming from a B2B into a B2C player (sales up from ~9% in FY13 to ~11% in FY15). The company is also taking its key UK-based terry towel brand, *Christy*, to the US, China & the Middle East. It is using the shop-in-shop (SIS) model and e-Commerce to boost B2C sales of key domestic brands. India branded sales grew more than 50% CAGR over FY13-15 and plans to increase domestic sales from 5% in FY15 to ~20% in the next 5-6 years. This move away from a pure commodity play into maker of innovative products and its focus on strategic partnerships has led to significant margin expansion. Margin has improved from an average of 15% over FY10-14, 20% in FY14 and 24% in FY15.

### Capacity expansion along with export opportunities driving sales

In recent years, India's exports to the US and the EU have grown sharply at the expense of China in the home textiles segment, given cost advantage and favorable government policies. The company has continued to keep pace with demand by expanding capacity in bed linen (~36% of sales) by 20% to 72mn meters in FY16 with an expected increase by 18% YoY in FY17, and in terry towel (~51% of sales) by 20% YoY to 60,000 tonnes in FY16 with an expected rise by 10% YoY in FY17. Bed linen is likely to register a sales CAGR of 20% over FY15-17E to ~INR 25bn, driven by volume growth. Terry towels is expected to show a sales CAGR of 11% over FY15-17E to INR 30bn.

### Lower manufacturing cost puts India in a sweet spot

Lower labor cost (China: USD 3.00 per operator per hour vs India's USD 1.12 in 2014), captive power coupled with steady supply at competitive rates and availability of raw materials (cotton) at lower cost than China have helped India's textiles manufacturers keep their costs lower than peers. As per Werner International, terry towel manufacturing cost in India is ~10% lower than in China.

## Valuation

We initiate coverage of Welspun India with a **Buy** rating and a TP of INR 1,127 based on an average of 14x FY17E P/E and 8x FY17E EV/EBITDA. The stock is currently trading at 9.7x FY17E P/E and 6x FY17E EV/EBITDA, which is at a sharp discount to global peers from China trading in the range of 25-36x FY17E P/E and 21-23x FY17E EV/EBITDA. We believe Welspun is slated for a rerating on 1) sustainability of 20%+ earnings growth, 2) high ROE, 3) a new dividend policy with a 25% payout, 4) free cashflow generation of INR 8.3bn over FY16-17E, and 5) likely reduction in net debt-equity ratio from 1.9x FY15 to 1.2x FY17E despite having capex of INR 13bn over FY15-17E.

### Key Financials

YE March	Revenue (INR mn)	YoY (%)	EBITDA (INR mn)	EBITDA margin (%)	Adj PAT (INR mn)	YoY (%)	Fully DEPS (INR)	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY15	53,025	18.0	12,742	24.0	5,398	486.3	53.7	42.5	23.5	14.5	8.2
FY16E	60,205	13.5	14,645	24.3	6,100	13.0	60.7	37.0	22.6	12.9	7.4
FY17E	71,287	18.4	17,530	24.6	8,064	32.2	80.3	37.5	24.3	9.7	6.0
FY18E	83,127	16.6	20,607	24.8	10,505	30.3	104.6	37.4	28.2	7.5	4.8

Note: pricing as on 22 July 2015; Source: Company, Elara Securities Estimate

## Rating: Buy

Target Price: INR 1,127

Upside: 44%

CMP: INR 780 (as on 22 July 2015)

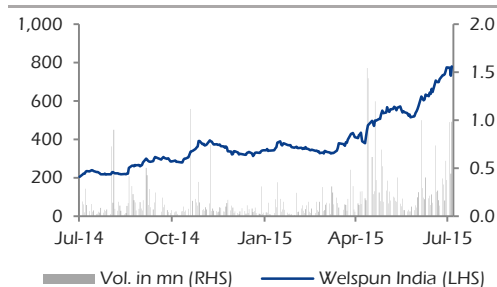
### Key data

Bloomberg/Reuters Code	WLSI IN/WLSP.BO
Current/Dil Shares O/S (mn)	100/100
Mkt Cap (INR bn/USD mn)	78/1,233
Daily Volume (3M NSE Avg)	245,437
Face Value (INR)	10

1 US\$= INR 63.6

Note: \*as on 22 July 2015; Source: Bloomberg

### Price & Volume



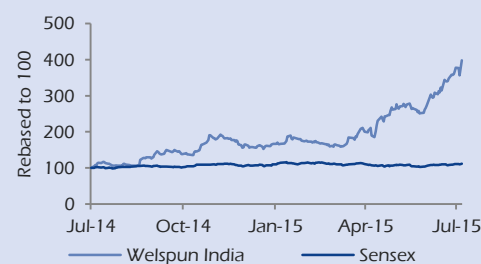
Source: Bloomberg

Shareholding (%)	Q1FY15	Q2FY15	Q3FY15	Q4FY15
Promoter	73.4	73.3	73.3	73.5
Institutional Investors	6.1	7.8	7.8	8.5
Other Investors	8.8	7.8	8.5	7.5
General Public	11.7	11.1	10.4	10.6

Source: BSE

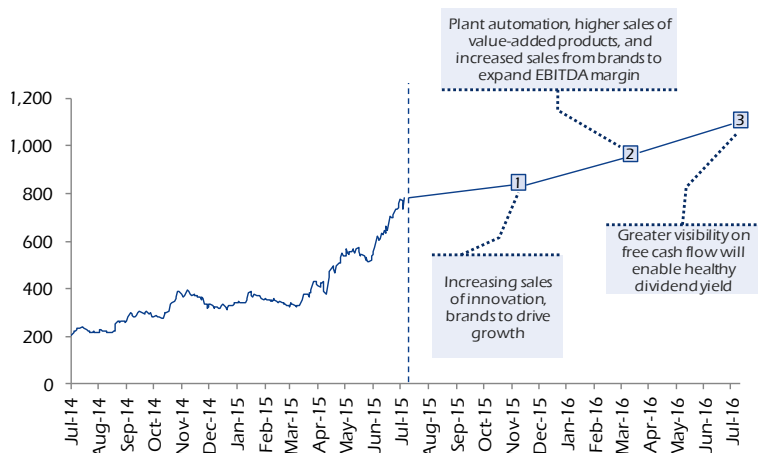
Price performance (%)	3M	6M	12M
Sensex	2.2	(1.7)	9.5
Welspun India	83.7	129.1	252.4
Trident	29.2	28.7	35.7
Himatsingka Seide	65.0	55.7	71.4
Indo Count Ind	75.1	101.3	600.1

Source: Bloomberg



Source: Bloomberg

**Valuation trigger**



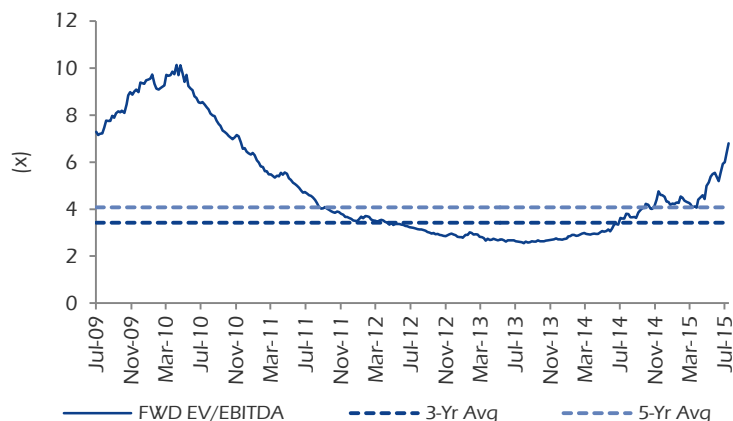
Source: Bloomberg, Elara Securities Estimate

**Valuation**

	FY17E
<b>PE-based</b>	
EPS (INR)	80.3
Target PE (x)	14.0
<b>Target price (INR)</b>	<b>1,124</b>
Weightage (%)	50.0
<b>EV/EBITDA-based</b>	
EBITDA (INR mn)	17,530
Target EV/EBITDA (x)	8.0
Target EV (INR mn)	140,240
Target market cap (INR mn)	113,606
<b>Target price (INR)</b>	<b>1,130.9</b>
Weightage (%)	50.0
<b>Weighted target price (INR)</b>	<b>1,127</b>
Upside (%)	44

Source: Elara Securities Estimate

**Valuation driver**



Source: Capitaline, Company, Elara Securities Estimate

**Investment summary**

- Strategic shift on innovation, brands & ancillarization and focus on e-Commerce to drive growth
- Lower manufacturing cost puts India and Welspun India in a sweet spot
- Better export demand coupled with capacity expansion to drive terry towel and bed linen sales

**Valuation trigger**

1. Increasing sales of innovation, brands to drive growth
2. Plant automation, higher sales of value-added products, and increased sales from brands to expand EBITDA margin
3. Greater visibility on free cash flow will enable healthy dividend yield

**Key risks**

- Adverse fluctuation in INR will lower export opportunity, and consequently, impact earnings
- An economic slowdown in the US and the EU, which make up ~80% of total sales, may impact earnings
- Higher cotton price due to rising cost of cultivation in India could lower cost advantage over China

**Our assumptions**

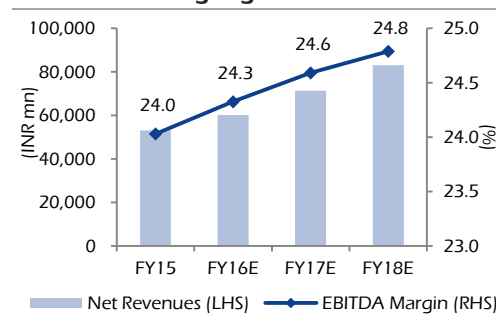
- In the terry towel segment, we expect volume growth of 10.8% & 8.8% and 2.5% realization contraction and 4.8% realization growth in FY16E and FY17E, respectively
- In the bed linen segment, we assume ~20% volume growth and 2.5% realization contraction in FY16E and 15.6% volume growth and 6.8% realization growth in FY17E

**Consolidated Financials (YE March)**

Income Statement (INR mn)	FY15	FY16E	FY17E	FY18E
Net Revenue	53,025	60,205	71,287	83,127
<b>EBITDA</b>	<b>12,742</b>	<b>14,645</b>	<b>17,530</b>	<b>20,607</b>
Add:- Non operating Income	949	997	997	997
OPBIDTA	13,691	15,642	18,527	21,604
Less :- Depreciation & Amortization	3,329	4,252	4,826	4,992
<b>EBIT</b>	<b>10,362</b>	<b>11,390</b>	<b>13,701</b>	<b>16,611</b>
Less:- Interest Expenses	2,829	2,481	2,110	1,530
<b>PBT</b>	<b>7,533</b>	<b>8,910</b>	<b>11,590</b>	<b>15,082</b>
Less :- Taxes	2,090	2,762	3,477	4,524
Add/(Less): - Extra-ordinaries	-	-	-	-
Add: Share of Loss in Associate	-	-	-	-
Less: Minority Interest	45	47	50	52
<b>Reported PAT</b>	<b>5,398</b>	<b>6,100</b>	<b>8,064</b>	<b>10,505</b>
<b>Adjusted PAT</b>	<b>5,398</b>	<b>6,100</b>	<b>8,064</b>	<b>10,505</b>
Balance Sheet (INR mn)	FY15	FY16E	FY17E	FY18E
Share Capital	1,005	1,005	1,005	1,005
Reserves	13,314	17,630	23,335	30,768
Borrowings	30,851	34,730	32,852	26,759
Minority Interest	378	425	475	527
Deferred Tax (Net)	641	641	641	641
<b>Total Liabilities</b>	<b>46,188</b>	<b>54,431</b>	<b>58,308</b>	<b>59,699</b>
Gross Block	43,148	53,148	58,148	60,148
Less:- Accumulated Depreciation	18,663	22,915	27,741	32,734
Net Block	24,485	30,233	30,407	27,415
Add:- Capital work in progress	1,564	2,000	400	400
Goodwill on Acquisition	1,785	1,785	1,785	1,785
Investments	1,420	1,420	2,420	2,920
Cash & bank balances	3,252	3,590	3,813	4,416
Net Working Capital	13,682	15,402	19,483	22,764
Other Assets	-	-	-	-
<b>Total Assets</b>	<b>46,188</b>	<b>54,431</b>	<b>58,308</b>	<b>59,699</b>
Cash Flow Statement (INR mn)	FY15	FY16E	FY17E	FY18E
Cash profit adjusted for non cash items	11,642	12,880	15,050	17,079
Add/Less : Working Capital Changes	(2,399)	(1,720)	(4,081)	(3,281)
Operating Cash Flow	9,243	11,160	10,969	13,798
Less:- Capex	(5,767)	(10,436)	(3,400)	(2,000)
Free Cash Flow	3,476	724	7,569	11,798
Financing Cash Flow	(3,102)	(386)	(6,347)	(10,695)
Investing Cash Flow	(304)	-	(1,000)	(500)
<b>Net change in Cash</b>	<b>71</b>	<b>338</b>	<b>222</b>	<b>603</b>
Ratio Analysis	FY15	FY16E	FY17E	FY18E
<b>Income Statement Ratios (%)</b>				
Revenue Growth	19.3	14.0	19.4	17.3
EBITDA Growth	38.3	14.9	19.7	17.6
PAT Growth	28.7	13.0	32.2	30.3
EBITDA Margin	24.0	24.3	24.6	24.8
Net Margin	10.2	10.1	11.3	12.6
<b>Return &amp; Liquidity Ratios (%)</b>				
Net Debt/Equity (x)	1.9	1.7	1.2	0.7
ROE (%)	42.5	37.0	37.5	37.4
ROCE (%)	23.5	22.6	24.3	28.2
<b>Per Share data &amp; Valuation Ratios</b>				
Diluted EPS (INR)	53.7	60.7	80.3	104.6
EPS Growth (%)	28.7	13.0	32.2	30.3
DPS (INR)	10.5	15.2	20.1	26.1
P/E (x)	14.5	12.9	9.7	7.5
EV/EBITDA (x)	8.2	7.4	6.0	4.8
EV/Sales (x)	2.0	1.8	1.5	1.2
Price/Book (x)	5.5	4.2	3.2	2.5
Dividend Yield (%)	1.3	1.9	2.6	3.4

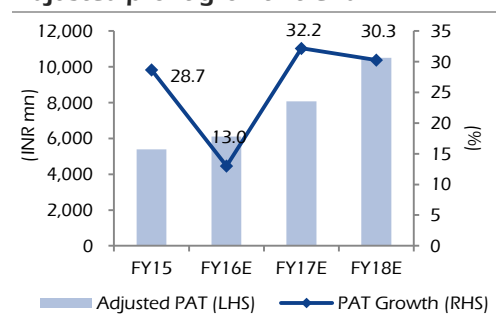
Note: pricing as on 22 July 2015; Source: Company, Elara Securities Estimate

**Revenue & margin growth trend**



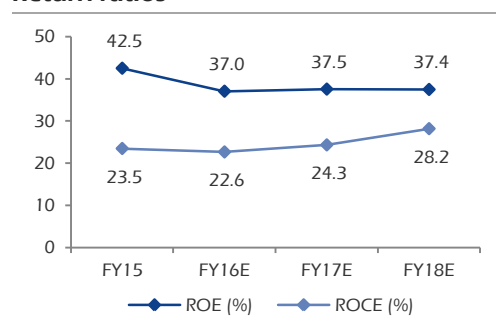
Source: Company, Elara Securities Research

**Adjusted profit growth trend**



Source: Company, Elara Securities Research

**Return ratios**



Source: Company, Elara Securities Research

Robust growth in the terry towel and bed linen segments to drive growth

Plant automation, higher sales of value-added products and increase in branded sales to expand EBITDA margin

## Betting on a new model

- ❑ Transforming into a B2C player via innovation, branding
- ❑ Adding new geographies to lower dependency on the US
- ❑ Revving up sales by targeting underpenetrated markets, channels and products

### Making innovations, branding matter

Welspun India’s business model has been changing, with increased focus on innovation, branding and ancillarization to keep it asset-light. In the past five years, it has moved away from transaction-oriented to strategic partnership, volume-based to value-based growth, cost-plus pricing to value-based pricing, pure manufacturer to original manufacturer and commodity manufacturer to own brand & innovative products. It also has increased backward integration in fabric from 35% to ~75% in FY15. However, the company is embracing ancillarization to implement an asset-light business model. Ancillarization in spinning is expected to be operational in FY17 while in weaving it is likely to be operational by FY18. Ancillarization will help the company control quality and stabilize return ratios.

### Tapping new growth opportunities

Welspun India has been increasing its presence across home textiles manufacturing (towel to bed linen to rugs) value chain. This along with cost advantage it enjoys over China & Pakistan in the home textiles segment is opening up huge opportunities globally.

Welspun is driving sales by targeting underpenetrated markets, channels and products. To meet this demand, the company has expanded capacity in bed linen by 20% YoY from 60mn meters in FY15 to 72mn meters in FY16 and an expected increase by 18% YoY in FY17 to 85mn meters. This would lead to a sales CAGR of 20% in bed linen to INR 25bn over FY15-17E. Welspun’s terry towels business is expected to register a sales CAGR of 11% over FY15-17E to INR 30bn, driven by capacity expansion by 20% YoY from 50,000 tonnes in FY15 to 60,000 tonnes in FY16 and an expected increase by 10% YoY in FY17 to 66,000 tonnes. We expect EBITDA margin expansion of

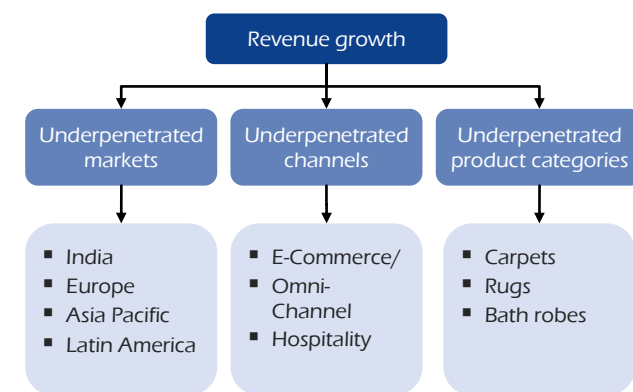
60bp to 24.6% over FY15-17E on plant automation, higher sales of value-added products and increasing branded sales. Hence, we expect an earnings CAGR of 22.2% over FY15-17E.

**Exhibit 2: Changing approach to business**

5 years ago	Current business model
<ul style="list-style-type: none"> <li>▪ Pure manufacturer</li> <li>▪ Cost-plus pricing</li> <li>▪ Volume-based growth</li> <li>▪ 35% integration</li> <li>▪ Transaction-oriented</li> <li>▪ Commodity manufacturer</li> <li>▪ Pure B2B player</li> </ul>	<ul style="list-style-type: none"> <li>▪ Original design manufacturer</li> <li>▪ Value-based pricing</li> <li>▪ Value-based growth</li> <li>▪ 75% integration</li> <li>▪ Strategic partnership</li> <li>▪ Own brand &amp; innovative products</li> <li>▪ Transforming into B2C</li> </ul>

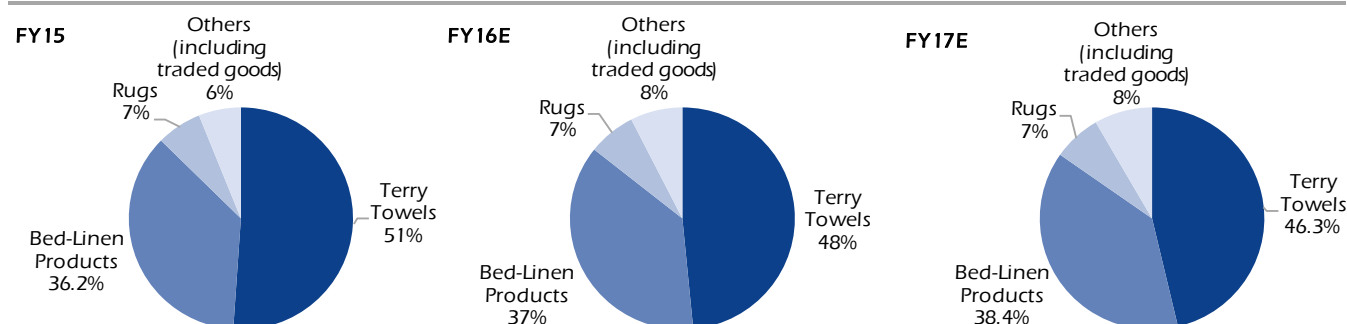
Source: Company, Elara Securities Research

**Exhibit 3: Key growth drivers**



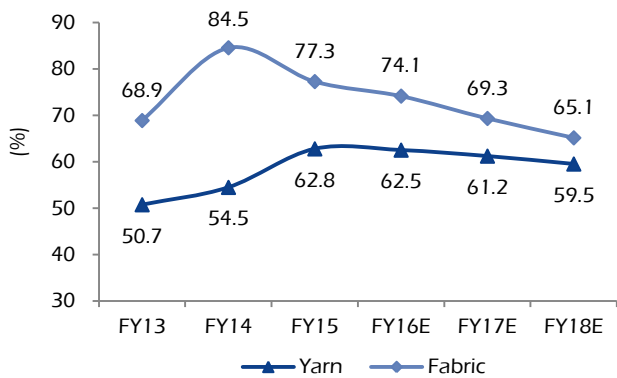
Source: Company, Elara Securities Research

**Exhibit 1: Revenue mix**



Source: Company, Elara Securities Estimate

**Exhibit 4: Backward integration trend**

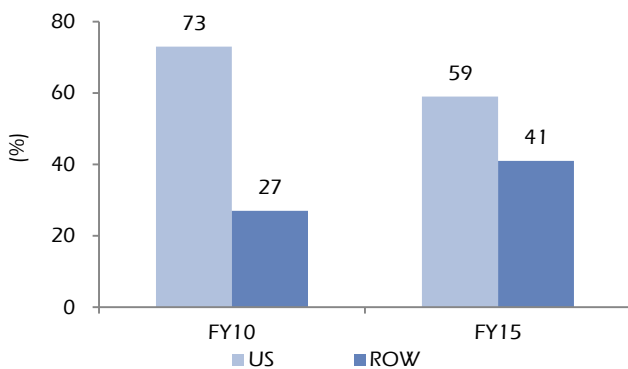


Source: Company, Elara Securities Estimate

**Looking beyond the US market**

Welspun India is gradually lowering its dependency on the US by diversifying into newer geographies. US sales contribution declined from 73% in FY10 to 59% in FY15 while the ROW's share increased from 27% in FY10 to 41% in FY15. It is focused on Europe where it is growing consistently. The company has huge scope for further market share expansion there. New geographies, such as Japan, South Korea & Australia as well as the domestic market, also have huge growth potential.

**Exhibit 5: Reducing dependency on the US**

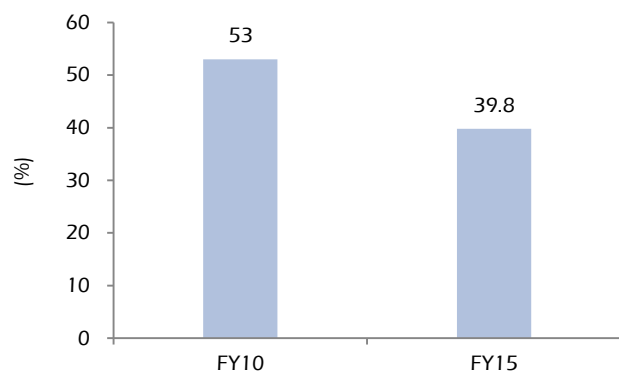


Source: Company, Elara Securities Research

**Channeling e-Commerce at the expense of big retail**

The company is working on increasing its B2C sales. It is trying to reduce its concentrated risk by acquiring new clients across geographies. Revenue from its top 5 customers fell from 53.0% in FY10 to 39.8% in FY15. We believe increased focus on other channels, such as e-Commerce, hospitality and branded sales, will lower dependency on large retailers and boost growth.

**Exhibit 6: Sales – top five customers**



Source: Company, Elara Securities Research

**Launching products in underpenetrated segments**

Welspun introduces new products every 3-4 years. During FY13-14, the company forayed into carpets, which started revenue contribution over FY14-15. Recently, it added products like bath robes to boost growth.

**Success through innovation**

The company's another strategic focus is to innovate in three key areas: products, process and supply chain. It usually takes nine months to launch an innovative product. Innovative products accounted for 31.0% of overall revenue in FY15, surging from 19.6% in FY11. The company has applied for six patents to date (hygro cotton yarn patented in the UK and five others pending approval). Other key innovations are *Eco Dry* towels and *Flexifit*.

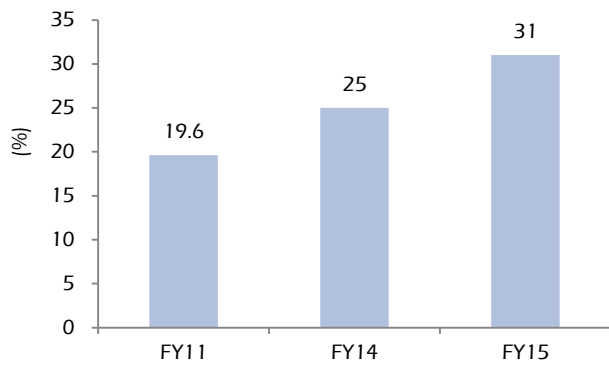
**Exhibit 7: Innovative product range**

 <p><b>Bed Technologies</b></p> <ul style="list-style-type: none"> <li>Flexifit (exclusive Licensee)</li> <li>Eversmooth</li> <li>Cotton Touch</li> <li>Smart Bedskirt</li> <li>Perfect Sheet</li> <li>Hygro Comfort</li> <li>Bleach Safe</li> </ul>	 <p><b>Bath Technologies</b></p> <ul style="list-style-type: none"> <li>Hygro Cotton</li> <li>Quick Dry</li> <li>Bleach Safe</li> <li>Eucalyptus</li> <li>Silk</li> <li>Bamboo</li> <li>Aerospun</li> <li>Spot Stop</li> </ul>	 <p><b>Sleep Solutions</b></p> <ul style="list-style-type: none"> <li>Earth Pillow</li> <li>Sneeze eezzz</li> <li>Hygrofil</li> <li>My Favorite Pillow</li> </ul>	 <p><b>Rugs</b></p> <ul style="list-style-type: none"> <li>Bleach Safe</li> <li>Eucalyptus</li> <li>Drylon</li> <li>Hygro</li> <li>Quick Dry</li> <li>Aerofil</li> <li>Hygro Cotton</li> </ul>
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Note: Hygro Cotton yarn features a unique hollow core that increases absorbency and loft. The more you wash, the softer it gets. Source: Company and Elara Securities Research

# Welspun India

**Exhibit 8: Innovation revenue contribution increasing**



Source: Company, Elara Securities Research

### Increasing share of branded sales

Welspun India is currently focused on creating a global as well as domestic brand in the terry towel and bed linen segments. It already has a terry towel global brand, *Christy*. Global branded sales currently make up ~11% of consolidated sales. The company acquired an 85% stake in CHT Holdings in 2006, the holding company of UK's leading towel brand, *Christy*. It acquired the rest in 2009.

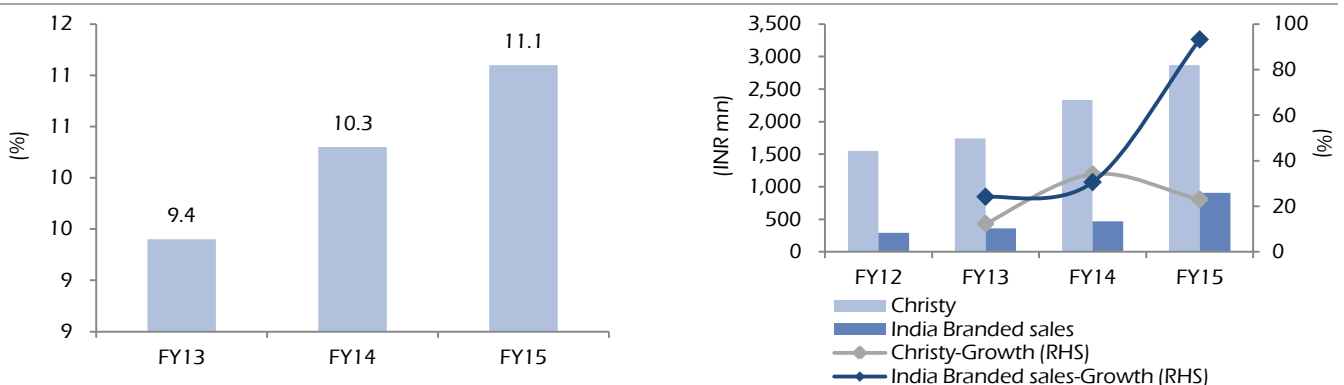
Welspun also has home textiles brands in the domestic market. The key brands include *Welhome* and *SPACES*. The company has adopted low capex and low-risk shop-in-shop (SIS) model in the domestic market with a fixed percentage of sales share. Branded sales growth is expected to be robust, particularly in India. The global expansion of *Christy* into geographies, such as the US, China & the Middle East, and increasing penetration of key domestic brands via SIS and e-Commerce would drive branded sales in the country. India branded sales grew more than 50% CAGR over FY13-15 and plans to increase domestic sales from 5% in FY15 to ~20% in the next 5-6 years.

**Exhibit 10: Brands and licenses of Welspun India**

	<ul style="list-style-type: none"> <li>Premium brand with presence in India and the Middle East</li> <li>Footprints of more than 200 shop-in-shop outlets and distribution</li> </ul>
	<ul style="list-style-type: none"> <li>Mass brand presence via retailers; also growing via the distributor network</li> </ul>
	<ul style="list-style-type: none"> <li>Largest terry towel brand in the UK with growing presence in China and the Middle East</li> <li>Present in over 40 retailers within the UK</li> <li>Present in the US and seeing aggressive growth in e-Commerce</li> </ul>
	<ul style="list-style-type: none"> <li>Mass brand in the UK with a focus on bedding</li> <li>Growing aggressively in affordable fashion</li> </ul>
	<ul style="list-style-type: none"> <li>Suppliers of the Wimbledon towels</li> <li>A souvenir that even the star tennis players covet</li> </ul>
	<ul style="list-style-type: none"> <li>License holder of the Rugby World Cup 2015 towels</li> </ul>
	<ul style="list-style-type: none"> <li>Licensed the <i>Amy Butler</i> range of home products for the US business with a special focus on e-Commerce</li> </ul>
	<ul style="list-style-type: none"> <li>Launched own brand of luxury linen in the US via e-Commerce partners</li> </ul>
	<ul style="list-style-type: none"> <li>Licensed the <i>Annie Phillip</i> brand for floor coverings in the US, the UK and India</li> </ul>

Source: Company, Elara Securities Research

**Exhibit 9: Branded sales revenue contribution up from 9.4% in FY13 to 11.0% in FY15**



Source: Company, Elara Securities Research

## Cost warrior

- ❑ Cost advantage, favorable policies put domestic textiles makers in a sweet spot
- ❑ Labor in India is ~2.7x cheaper than in China in 2014
- ❑ Manufacturing cost of terry towel in India is ~10% lower than in China

## Cheaper, safer, more stable

India is well poised to make long-term gains from the global home textiles market. On the other hand, China's home textiles market is expected to remain under pressure, given 1) rising domestic consumption, likely affecting exports, 2) jump in labor cost, 3) stringent environmental laws, raising power cost, and 4) and a sharp currency appreciation, which has made its exports less competitive than India's. Importers of home textiles are also concerned about the geopolitical risk associated with Pakistan. These factors have given a fillip to India as a more stable alternative to China and Pakistan.

India home textiles industry is also likely to get a boost, given that 1) the rupee has depreciated by ~31% over 2009-15 while the yuan has appreciated by 9%, thereby increasing consumption in China, and 2) favorable policies by India's government.

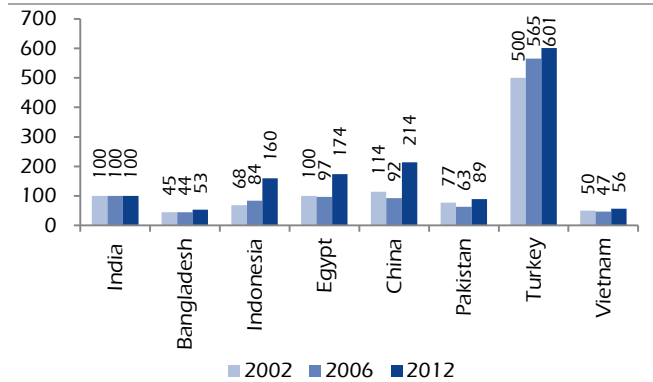
### Domestic textile makers benefit from cheap labor

India's enjoys a labor cost advantage over China, which is its key competitor in home textiles. This benefit serves as a huge leverage for domestic home textiles companies. As per Werner International, management consultant to the world's textiles, apparels & fashion industry, labor costs in China's textiles industry surged 4x from USD 0.69 per operator per hour in 2000 to USD 3.00 in 2014 vs an increase in India by ~2x from USD 0.58 in 2000 to USD 1.12 in 2014. Hence, labor cost per operator per hour in India is ~2.7x lower than in China in 2014.

### Benefits from lower manufacturing cost

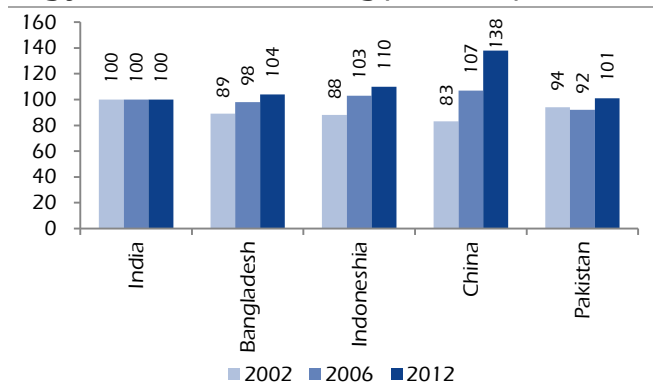
Lower labor cost, captive power coupled with steady supply of power at competitive rates and availability of raw materials (cotton) at a much lower cost over China have helped India's manufacturers to lower cost. As per Werner International, terry towel manufacturing cost in India is ~10% cheaper than in China.

Exhibit 11: Labor Wage Cost Index (India=100)



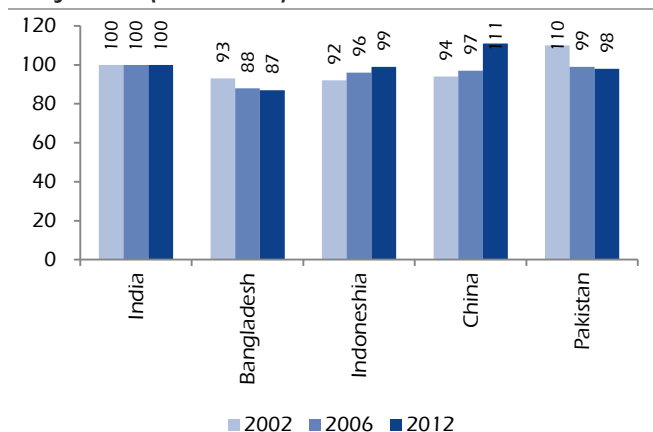
Source: Texprocil & Elara Securities Research

Exhibit 12: Manufacturing Cost Index: 30 combed ring yarn on cones for knitting (India=100)



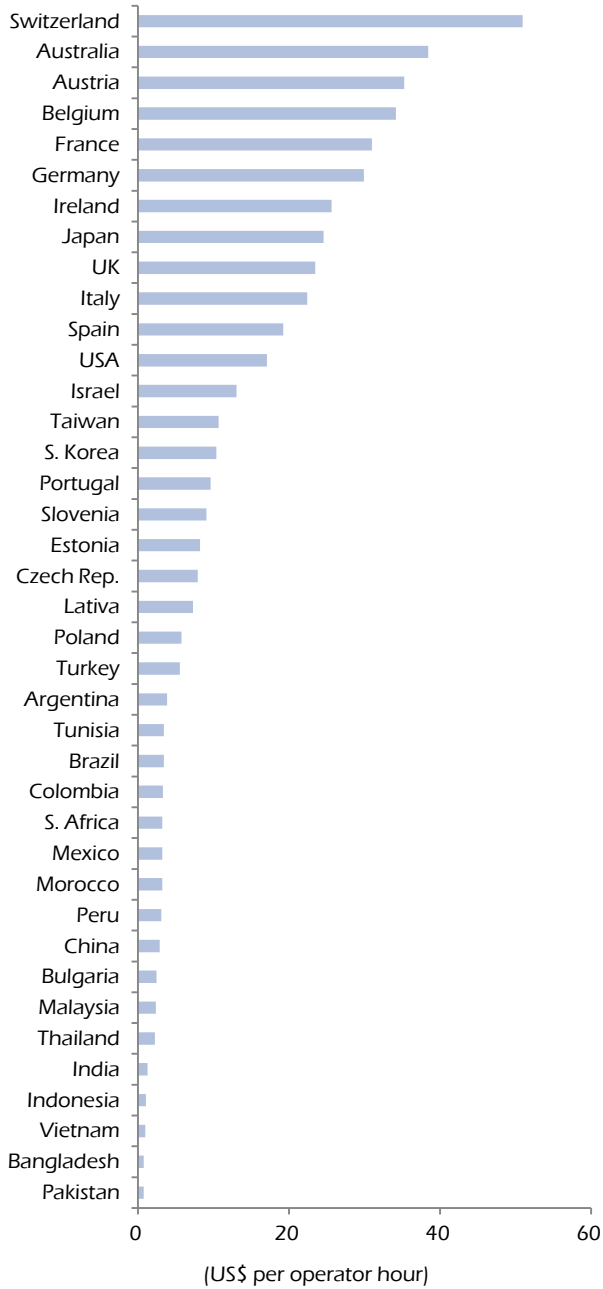
Source: Texprocil & Elara Securities Research

Exhibit 13: Manufacturing Cost Index - made ups terry towel (India=100)



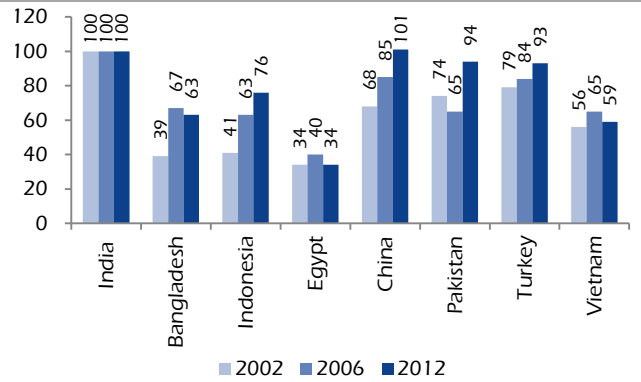
Source: Texprocil & Elara Securities Research

Exhibit 14: Textiles industry labor cost – 2014



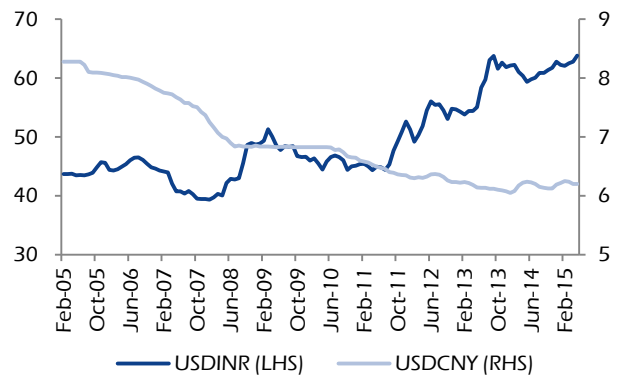
Source: wernerinternational.com, Elara Securities Research

Exhibit 15: Power Cost Index (India=100)



Source: Texpencil & Elara Securities Research

Exhibit 16: The rupee, yuan movement over the USD



Source: Bloomberg



## The way to grow

- ❑ Better export demand coupled with capacity expansion to drive terry towel and bed linen sales
- ❑ Terry towels business to deliver a sales CAGR of 11% over FY15-17E
- ❑ Bed linen business to register a sales CAGR of 20% over FY15-17E

### India top dog in US terry towels race

The US imported USD 1.6bn in terry towels in 2014, according to Otexa, Office of US Textiles and Apparels, a division of the US Commerce Department. Of this, India's market share was ~37% (USD 571mn) in 2014.

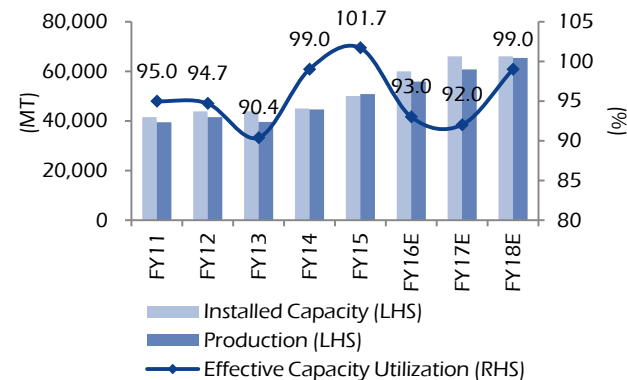
India's share in US exports of terry towels is likely to increase further, with the stabilization in the US economy and a cost advantage over China. India's market share in the towel segment in the US rose from 30.5% in 2010 to 36.5% in 2014 whereas China's declined from 26.7% in 2010 to 25.8% in 2014.

### Terry towel sales CAGR of 11% over FY15-17E

Welspun's share in the towel segment in the US rose from 14.7% in 2013 to 16.4% in 2014, according to Otexa. Its terry towel business contributed 51% of overall sales in FY15. This business is expected to register a sales CAGR of 11% over FY15-17E to INR 30bn, primarily driven by volume growth. Lower cost and a weak rupee against the US dollar are its key drivers. Capacity expansion by 20% YoY from 50,000 tonnes in FY15 to 60,000 tonnes in FY16 and an expected increase by 10% YoY in FY17 to 66,000 tonnes would drive a sales volume CAGR of 9.8% over FY15-17E to 60,720 tonnes in FY17E.

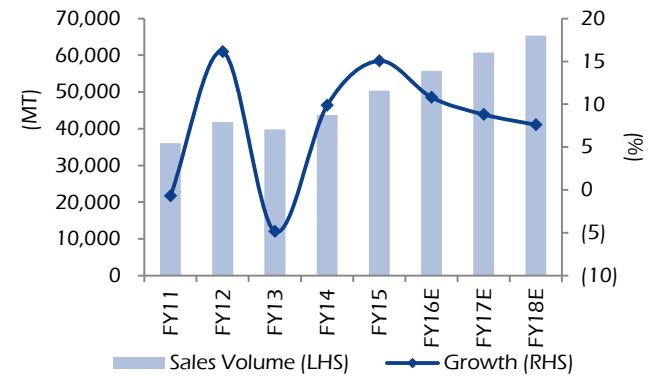
We expect a sales realization CAGR of just 1% over FY15-17E to INR 494/tonne. However, realization is expected to grow at a CAGR of 2% over FY15-17E to USD 8.2/tonnes. Higher contribution from value-added products and brands are likely to drive realization.

**Exhibit 17: Installed capacity and utilization trend**



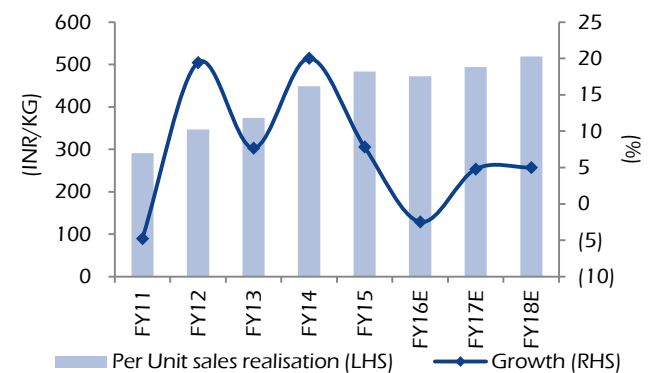
Source: Company, Elara Securities Estimate

**Exhibit 18: Sales volume CAGR of 11% over FY15-17E**



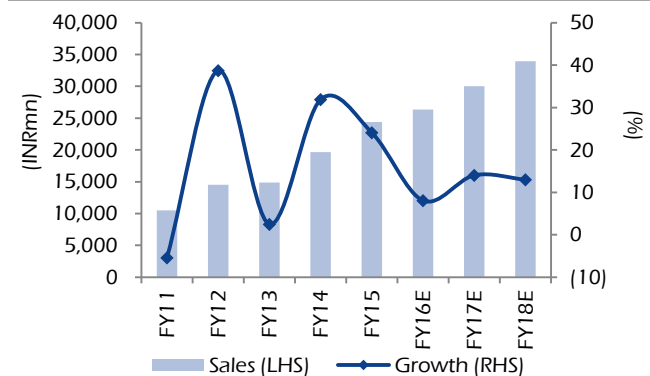
Source: Company, Elara Securities Estimate

**Exhibit 19: Realization likely to stabilize**



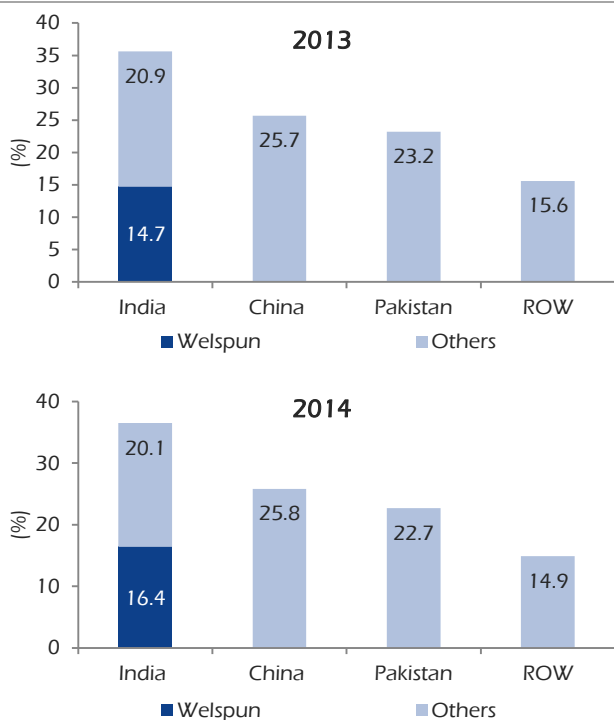
Source Company, Elara Securities Estimate

**Exhibit 20: Revenue CAGR of 12% over FY15-17E**



Source: Company, Elara Securities Estimate

**Exhibit 21: Market share of Welspun in the US terry towels import share**



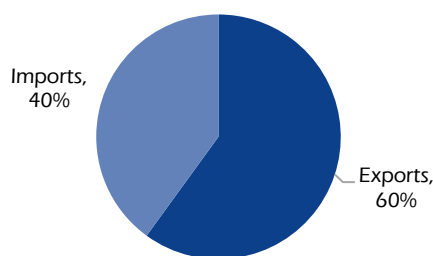
Source: Company, Elara Securities Research

**Exhibit 22: Terry towel capacity of key firms**

Capacity (tpa)	FY14	FY15	FY16E
Trident	42,000	90,000	90,000
<b>Welspun India</b>	<b>45,000</b>	<b>50,000</b>	<b>60,000</b>
Alok	13,400	13,400	13,400

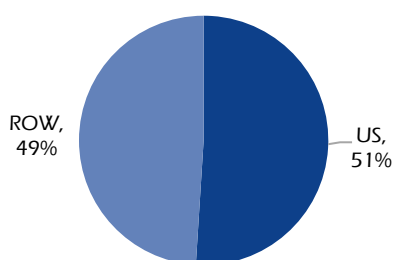
Source: Annual reports, investor presentations

**Exhibit 23: India's terry towel market at USD 1.9bn (2013)**



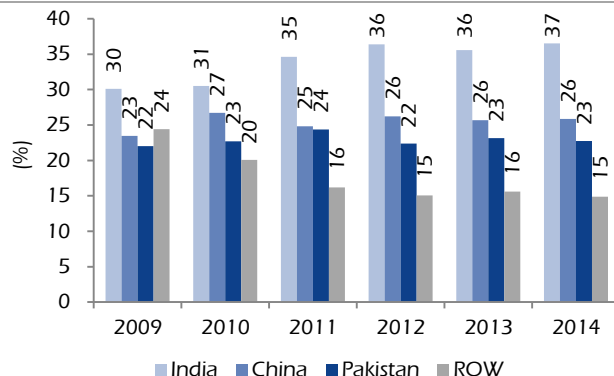
Source: Emergingtextiles.com, Technopak Analysis

**Exhibit 24: Towel exports destinations (2013)**



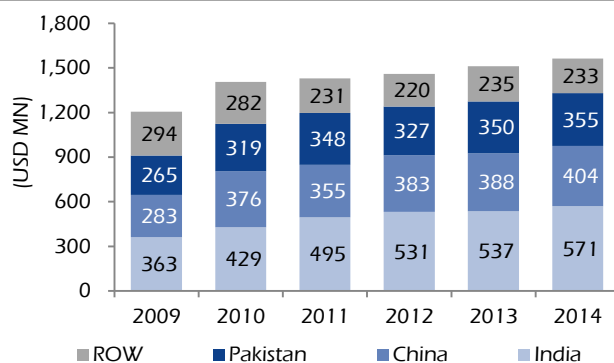
Source: Emergingtextiles.com, Technopak Analysis

**Exhibit 25: India gaining market share in the US terry towel market**



Source: Otxea and Elara Securities Research

**Exhibit 26: India terry towel exports to the US grow at 9.5% CAGR over 2009-14**



Source: Otxea, Elara Securities Research

## Robust growth in bed linen to sustain

### India's market share continues to grow in the US

The US imported USD 1.9bn in bed linen in 2014, according to Otxea, Office of US Textiles and Apparels, a division of the US Commerce Department. Of this, India's market share was ~47% (USD 870mn) in 2014. In volume terms, India stood at 34.3% (~139mn tonnes).

India's market share in the bed linen segment in the US rose from 33% in 2010 to 47% in 2014 while China's declined from ~30% in 2010 to 23.3% in 2014. Lower manufacturing cost and a weak rupee against the US dollar were behind the market share gains in the US. Beside India, China and Pakistan also export in this segment to the US. The two nations together contributed ~53% by volume (214mn tonnes) and 40% by share (USD 739mn) in 2014.

*Welspun's share in the bed linen segment in the US increased from 7.3% in 2013 to ~10.0% in 2014.*

**EU share likely to rise**

In the EU bed linen market, India faces increased competition from Turkey, Bangladesh and China. The Free Trade Agreement between Pakistan and the EU for a ~10% free duty has helped Pakistan to better leverage its products over peers (Turkey, Bangladesh, India and China), leading to a higher market share of 33.7%. India is currently in the process of negotiating a similar deal with the EU to reduce duty by 5-10%.

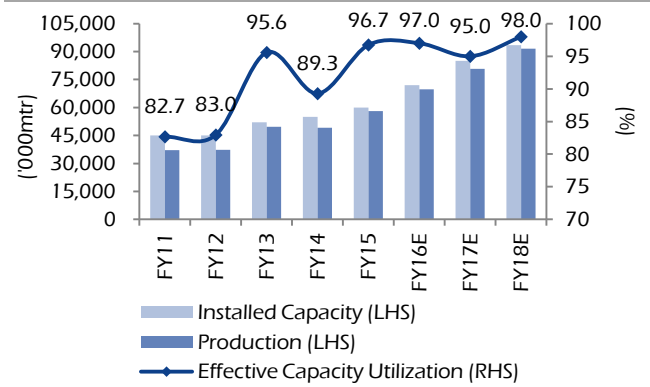
In the US as well as the EU, Welspun continues to innovate and launch high value-added products to sustain robust volume growth. The company has applied for six patents to date (including hygro cotton yarn patented in the UK and five other patents pending approval).

**Bed linen sales CAGR of 20% over FY15-17E**

Welspun's bed linen business contributes 36% to overall sales in FY15. We expect this business to register a sales CAGR of 20% to INR 25bn over FY15-17E, primarily driven by volume growth. Better demand coupled with cost advantage over peers and a weakening rupee against the US dollar is likely to fuel growth. Capacity expansion by 20% YoY from 60mn meters in FY15 to 72mn meters in FY16 and expected to increase to 85mn meters in FY17 along with higher exports are expected to drive a sales volume CAGR of 17.7% over FY15-17E to 80,750 tonnes in FY17E.

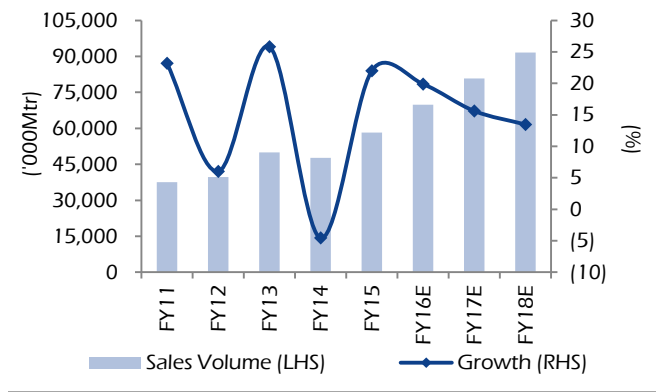
We expect sales realization CAGR of just 2% to INR 309/meter over FY15-17E. However, we assume a realization CAGR in USD terms of ~3% to USD 5.1/meter over FY15-17E. Higher contribution of value-added products through innovation and brands is likely to drive realization. Revenue contribution of the bed linen segment is expected to increase from ~36.2% in FY15 to ~38.4% in FY17E.

**Exhibit 27: Installed capacity and utilization trend**



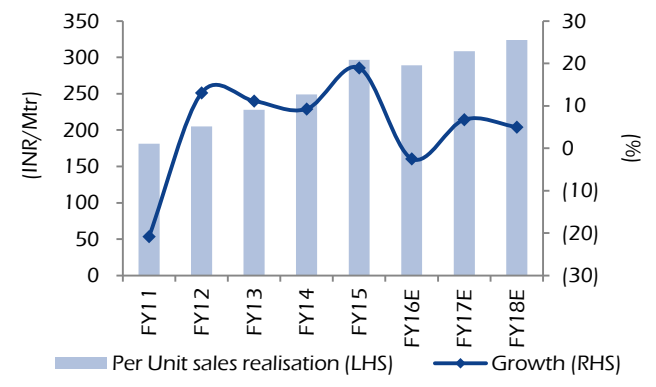
Source: Company, Elara Securities Estimate

**Exhibit 28: Sales volume CAGR of 18% over FY15-17E**



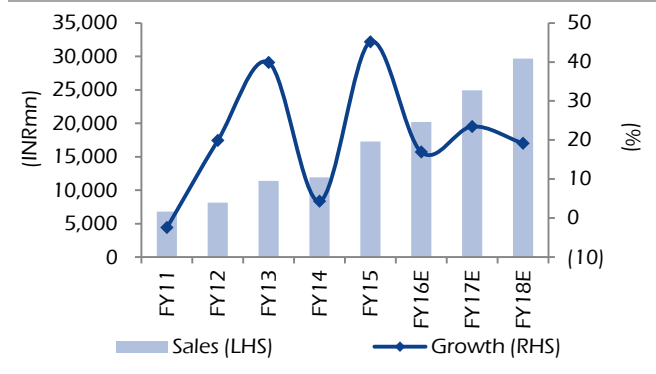
Source: Company, Elara Securities Estimate

**Exhibit 29: Realization likely to stabilize**



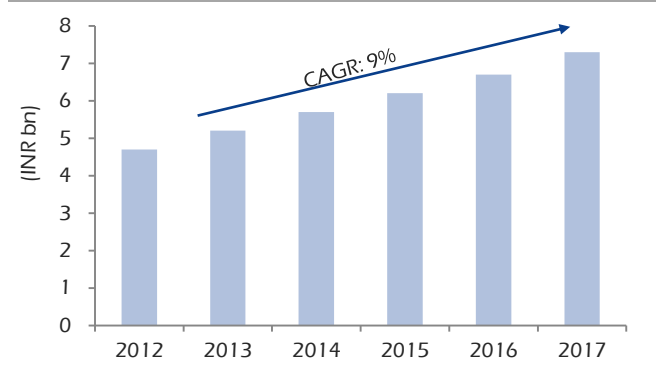
Source Company, Elara Securities Estimate

**Exhibit 30: Revenue CAGR of 20% over FY15-17E**



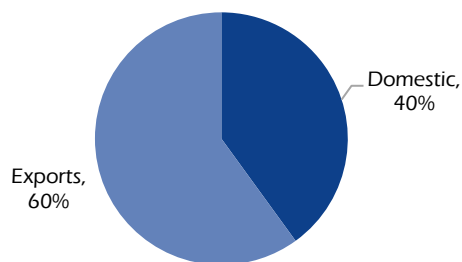
Source: Elara Securities Estimate

**Exhibit 31: India's bed linen market at sales CAGR of 9% over FY13-17E**



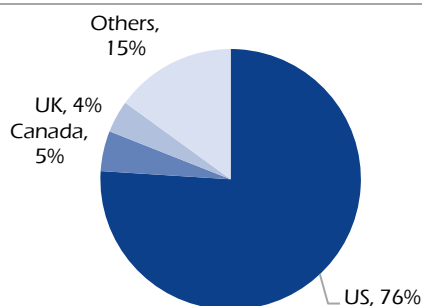
Source: Emergingtextiles.com, Technopak Analysis

**Exhibit 32: India's bed linen market at USD 5.2bn (2013)**



Source: Emergingtextiles.com, Technopak Analysis

**Exhibit 33: Bed linen export destinations (2013)**



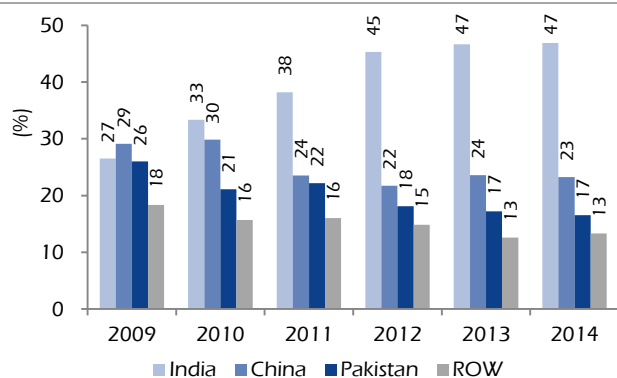
Source: Emergingtextiles.com, Technopak Analysis

**Exhibit 34: Bed sheet capacity of key companies**

Capacity (mn meters pa)	FY14	FY15	FY16E
Trident	-	-	43
<b>Welspun India</b>	<b>55</b>	<b>60</b>	<b>72</b>
Indo Count	45	68	68
Himatsingka	23	23	23
Alok	150	150	150

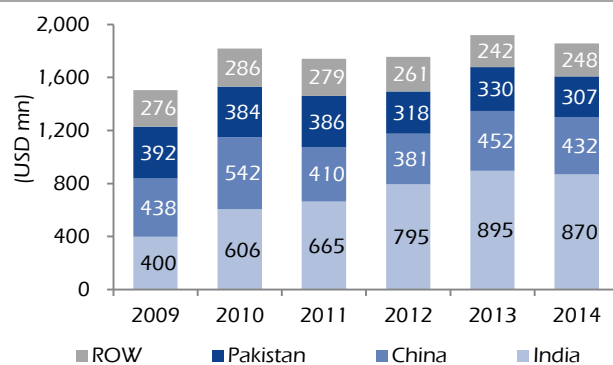
Source: Annual reports, investor presentations

**Exhibit 35: Market share in US sheets (cotton) imports**



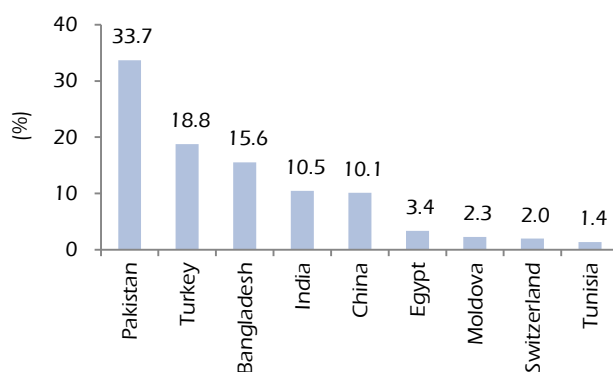
Source: Otxea and Elara Securities Research

**Exhibit 36: Market size in US sheets (cotton) imports**



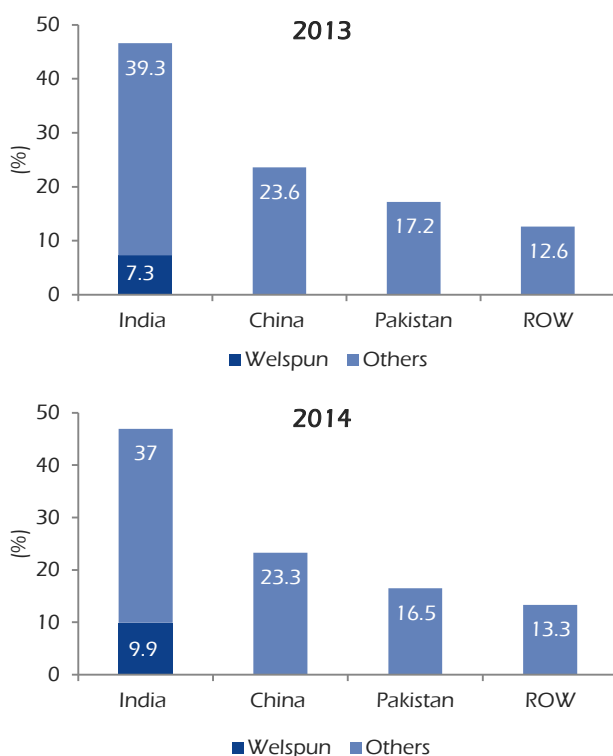
Source: Otxea, Elara Securities Research

**Exhibit 37: Market Share in EU bed linen (cotton) imports (2013)**



Source: Emergingtextiles.com

**Exhibit 38: US cotton sheets imports (country-wise)**



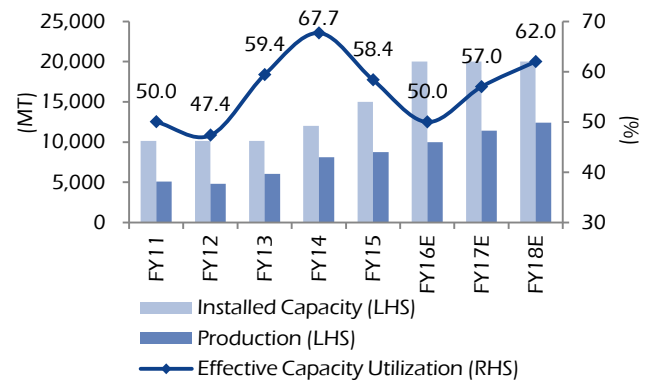
Source: Otxea, Elara Securities Research

**Rugs CAGR of 20% over FY15-17E**

Welspun's rugs segment contributes 6.5% of overall sales in FY15. We expect this business to register a sales CAGR of 20% to INR 4.5bn over FY15-17E, primarily driven by volume growth. Capacity expansion from 15,000 tonnes in FY15 to 20,000 tonnes in FY16 coupled with exports demand would drive a sales volume CAGR of 14% over FY15-17E to 11,440 tonnes in FY17E.

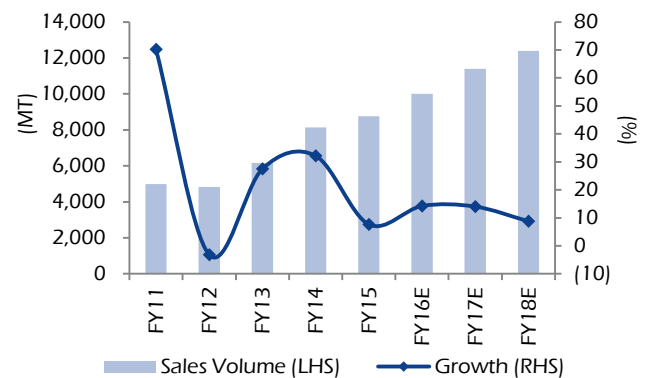
We expect a sales realization CAGR of just 5% to INR 394/tonne over FY15-17E. However, we expect a realization CAGR in USD terms of 6% to USD 6.5/tonne over FY15-17E.

**Exhibit 39: Installed capacity and utilization trend**



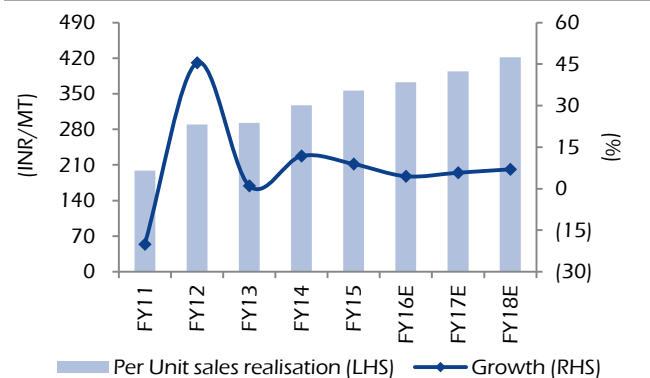
Source: Company, Elara Securities Estimate

**Exhibit 40: Sales volume CAGR of 14.3% over FY15-17E**



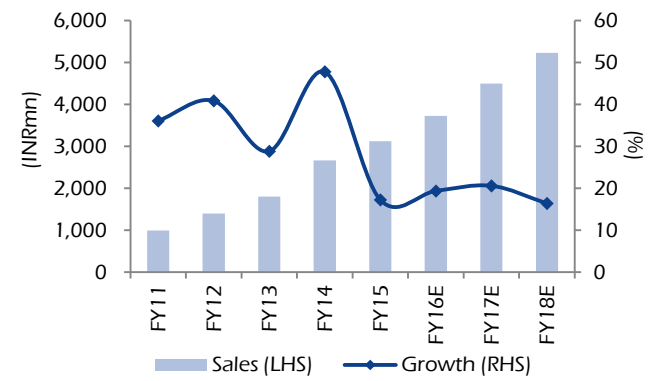
Source: Company, Elara Securities Estimate

**Exhibit 41: Realization CAGR of 5% over FY15-17E**



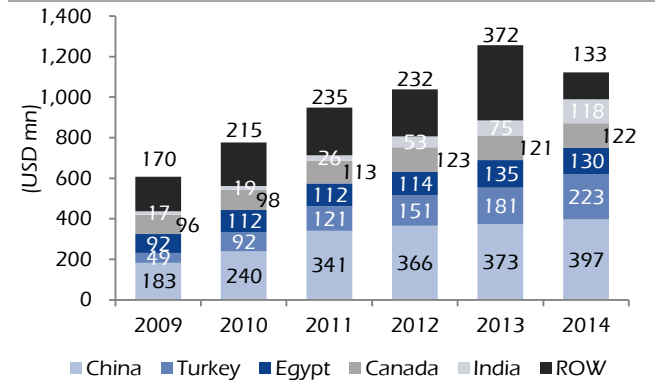
Source Company, Elara Securities Estimate

**Exhibit 42: Revenue CAGR of 20% over FY15-17E**



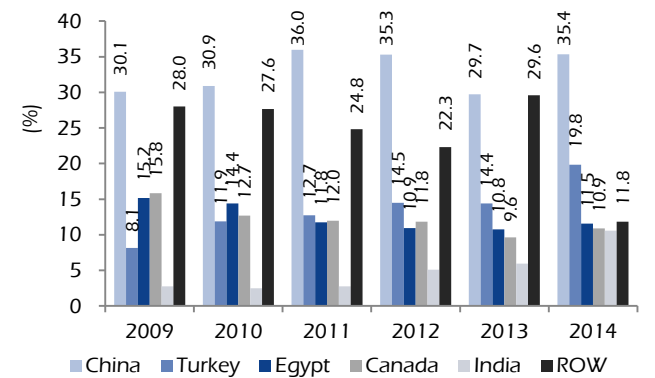
Source: Company, Elara Securities Estimate

**Exhibit 43: US MMF floor coverings imports (country-wise)**



Source: Otexa and Elara Securities Research

**Exhibit 44: US MMF floor coverings' import share**



Source: Otexa and Elara Securities Research

## Exhibit 45: Key revenue growth assumptions

	FY15	FY16E	FY17E	FY18E
<b>USD-INR</b>	<b>61.2</b>	<b>60.9</b>	<b>60.2</b>	<b>60.2</b>
<b>Terry towel</b>				
Sales (INR mn)	24,366	26,330	30,022	33,922
YoY growth (%)	24.1	8.1	14.0	13.0
Sales Volume (tonnes)	50,356	55,800	60,720	65,340
YoY growth (%)	15.1	10.8	8.8	7.6
Sales realization (INR/KG)	484	472	494	519
YoY growth (%)	7.8	(2.5)	4.8	5.0
<b>Bed linen</b>				
Sales (INR mn)	17,269	20,189	24,921	29,693
YoY growth (%)	45.1	16.9	23.4	19.1
Sales Volume ( '000 meters)	58,255	69,840	80,750	91,630
YoY growth (%)	22.0	19.9	15.6	13.5
Sales realization (INR/meter)	296	289	309	324
YoY growth (%)	19.0	(2.5)	6.8	5.0
<b>Rugs</b>				
Sales (INR mn)	3,122	3,726	4,493	5,229
YoY growth (%)	17.2	19.3	20.6	16.4
Sales Volume (tonnes)	8,755	10,000	11,400	12,400
YoY growth (%)	7.6	14.2	14.0	8.8
Sales realization (INR/KG)	357	373	394	422
YoY growth (%)	8.9	4.5	5.8	7.0

Source: Company, Elara Securities Estimate

## Ripe for rerating

- ❑ Earnings CAGR of 22% over FY15-17E, driven by robust growth in terry towels and bed linen
- ❑ Margin expansion likely on plant automation and higher sales of value-added products
- ❑ Initiate with a Buy rating and a TP of INR 1,127

## Net profit CAGR of 22%

We expect a revenue CAGR of ~16% over FY15-17E, owing to healthy sales volume growth across terry towels, bed linen and rugs. Increased automation would keep employee cost stable. Operating leverage due to automation, higher sales of value-added products, owing to regular launches of innovative products, and increased branded sales are likely to expand EBITDA margin by 60bp to 24.6% over FY15-17E from 24% in FY15. As a result, we expect a net profit CAGR of 22.2% over FY15-17E.

### Improving debt profile

Net debt-equity is likely to decrease from 1.9x in FY15 to 1.2x in FY17E, due to higher free cash flow.

### Capex of INR 13bn over FY16-17

Management has guided capex of INR 13bn over FY16-17 to modernize the Gujarat mill at Vapi, expand capacity in towels & sheets and increase automation. The company plans to raise long-term debt of ~INR 9bn under the technology upgradation fund (TUF) scheme over FY16-17. The Central and State governments will offer an interest subsidy of ~4.5% and ~5.5% on debt under TUF, respectively.

#### Exhibit 46: Capex over FY14-15

Segment-wise	(INR mn)
Spindles (spinning)	6,500
Weaving	1,800
Rugs / carpets	830
Upgradation of open-end yarn capacity	600
Debottlenecking of the existing plant	1,600
Miscellaneous	1,670
<b>Total</b>	<b>13,000</b>

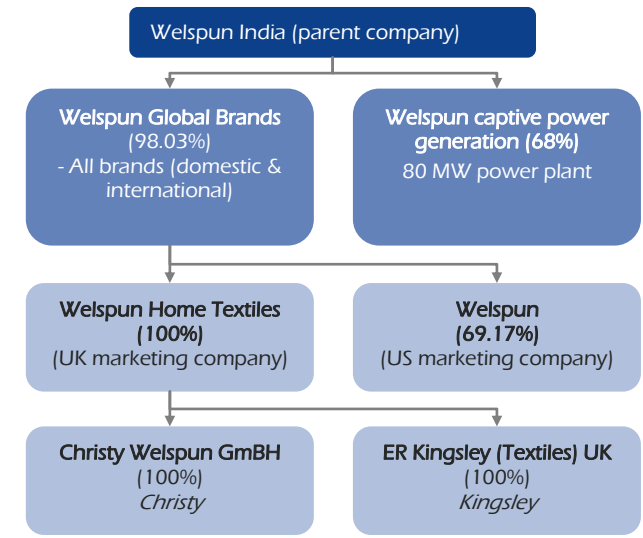
Source: Company, Elara Securities Research

#### Exhibit 47: Capex over FY16-17

	(INR mn)
Vapi mill modernization	6,700
Capacity addition in Towels	3,500
Capacity addition in sheet capacity	1,300
Increasing automation, debottlenecking	1,500
<b>Total</b>	<b>13,000</b>

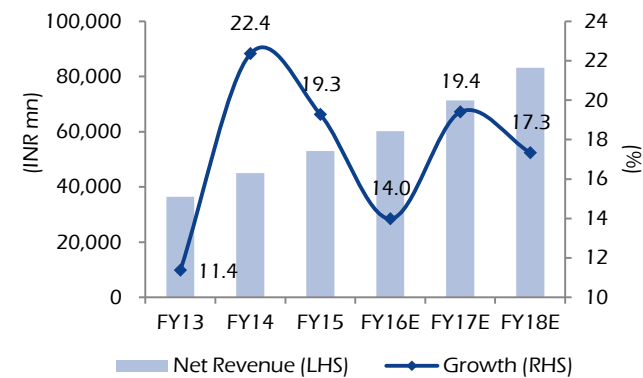
Source: Company, Elara Securities Research

#### Exhibit 48: Welspun corporate structure



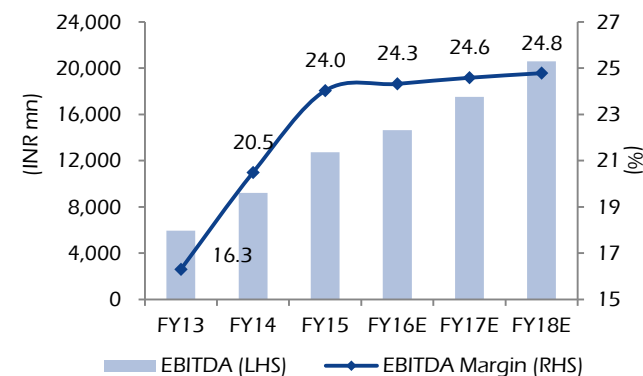
Source: Company, Elara Securities Research

#### Exhibit 49: Revenue CAGR of 16% over FY15-17E



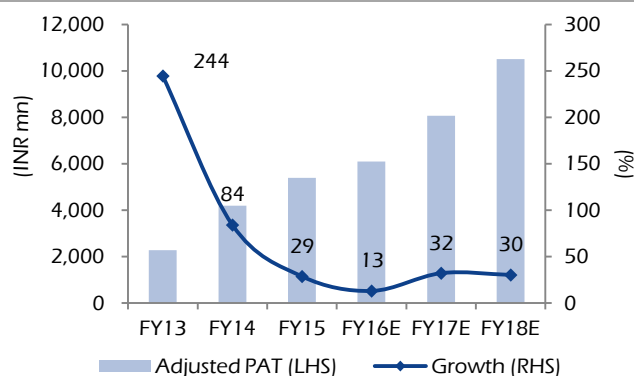
Source: Company, Elara Securities Estimate

#### Exhibit 50: EBITDA CAGR of 17.3% over FY15-17E



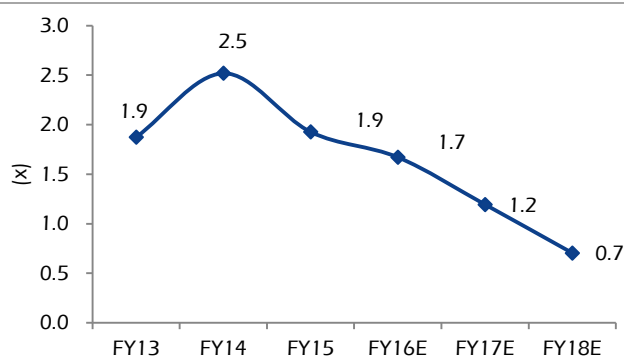
Source: Company, Elara Securities Estimate

**Exhibit 51: Net profit CAGR of 22.2% over FY15-17E**



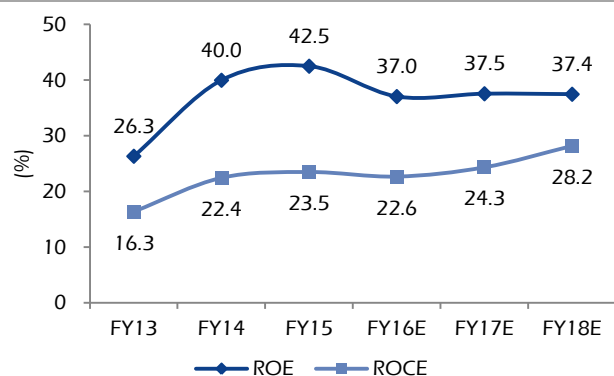
Source: Company, Elara Securities Estimate

**Exhibit 52: Net debt-equity ratio of 1.9x in FY15 likely to fall to 1.2x in FY17E**



Source: Company, Elara Securities Estimate

**Exhibit 53: Return ratios**



Source: Company, Elara Securities Estimate

## Rerating candidate

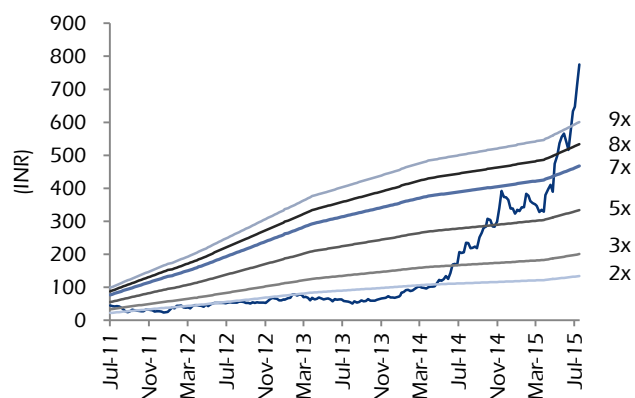
We believe Welspun is slated for a rerating, owing to 1) sustainability of 20%+ earnings growth, 2) high ROE, 3) a new dividend policy with 25% payout, 4) free cashflow generation of INR 8.3bn over FY16-17E, and 5) a likely fall in net debt-equity ratio from 1.9x FY15 to 1.2x FY17E despite having capex of INR 13bn over FY16-17E.

## Initiate Buy with a TP of INR 1,127

At the current market price, the stock trades at 14.5x FY15 EPS of INR 53.7, 12.9x FY16E EPS of INR 60.7 and 9.7x FY17E EPS of INR 80.3 and 8.2x FY15 EBITDA of INR 12.7bn, 7.4x FY16E EBITDA of INR 14.6bn and 6x FY17E EBITDA of INR 17.5bn. Welspun is also trading at a sharp discount to home textiles players from China, which are trading in the range of 25-36x FY17E P/E and 21-23x FY17E EV/EBITDA.

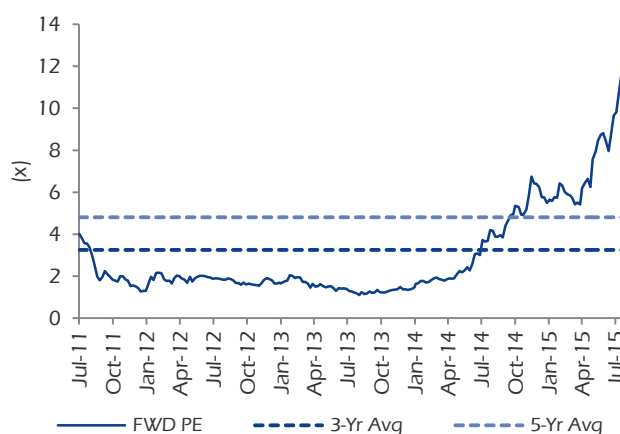
We initiate coverage of Welspun India with a **Buy** rating and a target price of INR 1,127. We arrive at the target price based on an average of 14x FY17E EPS of INR 80.3 and 8x FY17E EBITDA of INR 17.5bn, implying potential upside of 44% from the current levels.

**Exhibit 54: P/E band**



Source: Company, Capitaline, Elara Securities Estimate

**Exhibit 55: Re-rating on better earnings visibility**



Source: Company, Capitaline, Elara Securities Estimate



**Exhibit 56: Welspun currently trades at 6x FY17E EV/EBITDA vs global peers' at 21-23x FY17E EV/EBITDA**

	Country	Market cap	EBITDA margin (%)			EV/EBITDA (x)			P/E (x)			ROE (%)		
		(USD mn)	FY15	FY16E	FY17E	FY15	FY16E	FY17E	FY15	FY16E	FY17E	FY15	FY16E	FY17E
Welspun India*		1,282	24.0	24.3	24.6	8.2	7.4	6.0	14.5	12.9	9.7	42.5	37.0	37.5
Trident *	India	251	18.3	19.1	19.1	6.0	5.5	4.3	13.4	7.8	5.0	9.9	13.3	18.1
Indo Count Industries		474	15.6	17.1	17.3	6.7	5.1	4.2	20.1	15.6	12.5	44.0	39.5	34.8
Hunan Mendale Home Textile	China	1,168	11.5	15.1	15.8	39.4	27.1	23.2	54.0	42.1	35.7	9.9	12.3	13.2
Luolai Home Textile		2,406	17.1	17.8	18.9	30.4	25.5	20.8	38.5	29.0	24.7	16.6	17.1	17.5

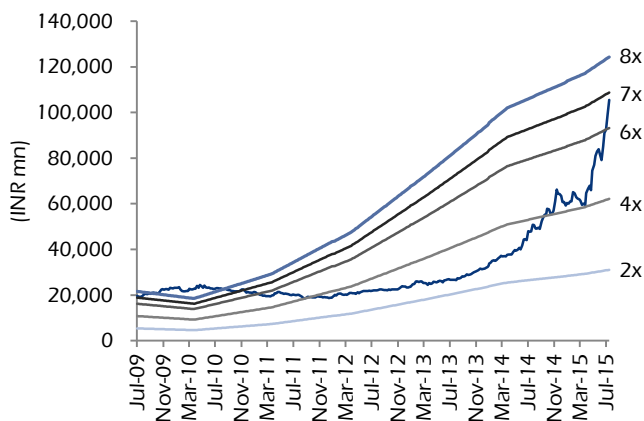
Note: pricing as on 22 July 2015; Source: Bloomberg, Company, \*Elara Securities Estimate

**Exhibit 57: DuPont analysis**

	FY10	FY11	FY12	FY13	FY14	FY15	FY16E	FY17E	FY18E
Net profit/ PBT (x)	0.74	0.03	0.80	0.76	0.70	0.72	0.68	0.70	0.70
PBT/ EBITDA (x)	0.77	0.19	0.23	0.51	0.65	0.59	0.61	0.66	0.73
EBITDA/ sales (x)	0.15	0.11	0.11	0.16	0.20	0.24	0.24	0.25	0.25
Sales/ assets (x)	0.81	0.85	1.18	1.19	1.21	1.20	1.20	1.26	1.41
Assets/ net worth (x)	4.95	4.16	3.87	3.52	3.55	3.48	3.05	2.62	2.10
ROE (%)	33.3	0.2	9.4	26.3	40.0	42.5	37.0	37.5	37.4

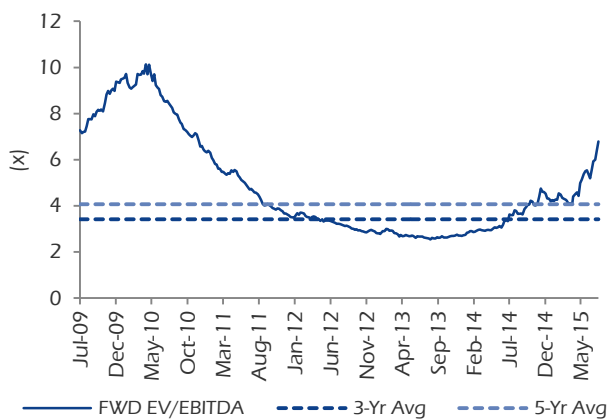
Source: Capitaline, Company, Elara Securities Estimate

**Exhibit 58: EV/EBITDA band**



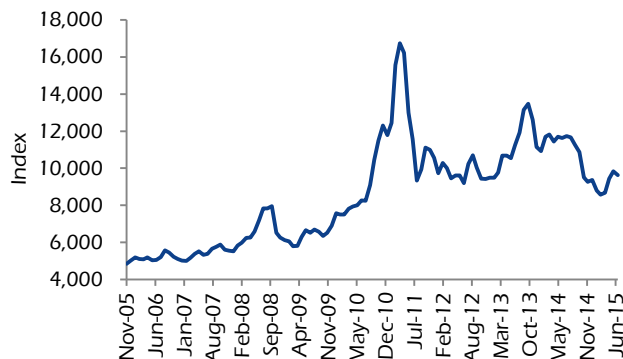
Source: Capitaline, Company, Elara Securities Estimate

**Exhibit 59: Re-rating on better earnings visibility**



Source: Capitaline, Company, Elara Securities Estimate

**Exhibit 60: Cotton price trend**



Note: Shankar 6 is a type of cotton Source: Bloomberg

**Exhibit 61: Valuation**

	FY17E
<b>PE-based</b>	
EPS (INR)	80.3
Target PE (x)	14.0
<b>Target price (INR)</b>	<b>1,124</b>
Weightage (%)	50.0
<b>EV/EBITDA-based</b>	
EBITDA (INR mn)	17,530
Target EV/EBITDA (x)	8.0
Target EV (INR mn)	140,240
Target market cap (INR mn)	113,606
<b>Target price (INR)</b>	<b>1,130.9</b>
Weightage (%)	50.0
<b>Weighted target price (INR)</b>	<b>1,127</b>
Upside (%)	44

Source: Elara Securities Estimate

## Annexure

### Exports to propel India's home textiles

According to Consulting Firm Technopak, the global home textiles market is likely to grow at a sales CAGR of 5.0% over FY13-17; however, India's home textiles market may grow at a higher pace of 10.5% CAGR during the same period, owing to increased exports growth of ~12%. The global market size of home textiles is likely to reach to USD 96bn in FY17 from USD 78bn in 2013. The global towel market size was at ~USD 16bn in 2013, around 20% of the global home textiles market while the non-towel global market was at USD 62bn. The bed linen market size in the US was at USD 14bn in 2013, 54% of overall US home textiles market. The US and Europe together consume ~79% of the global home textiles market.

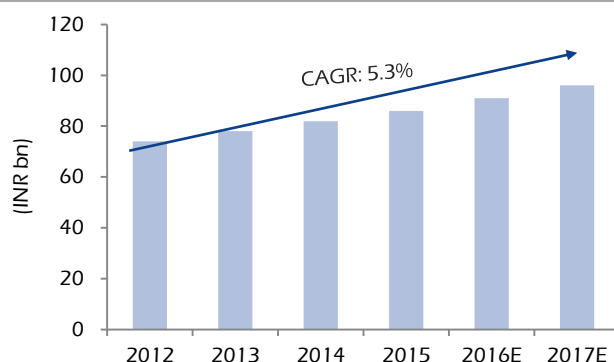
#### Organized players have an edge

In India, less than 10% of the home textiles market is driven by organized players. This creates huge opportunity for organized firms to grab at a bigger market share. Organized players also have an edge over the unorganized on the back of innovation and capability to handle large orders. Of the various segments within home textiles, bed & bath linen contributes two-thirds of the total market size. Kitchen linen, curtains, upholstery and rugs & carpets make up the rest. The major consumption hubs of the world are the developed economies, with the US and the EU leading the pack. Production hubs lie in developing countries of East & Southeast Asia and countries like Turkey and Egypt. India's major competitors in the cotton towel business are China, Pakistan and Turkey. The country enjoys a majority share of the US market in terms of cotton towel exports and the third-largest share of the EU market.

#### Further market share gains likely

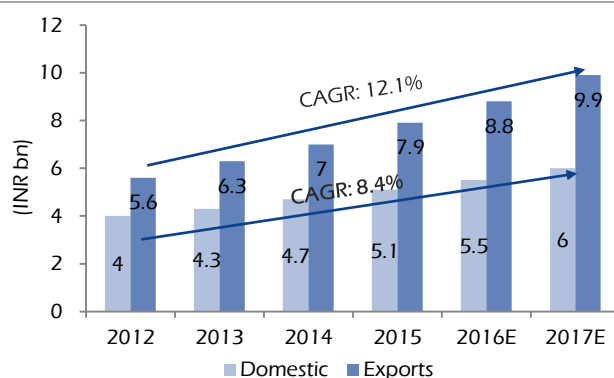
India's market share in the towel segment in the US rose from 30.5% in 2010 to 36.5% in 2014 whereas China's declined from 26.7% in 2010 to 25.8% in 2014. India's market share in towel in Europe was 17% in 2013. India's market share in the bed linen segment in the US rose from 33% in 2010 to 47% in 2014 whereas China's declined from ~30.0% in 2010 to 23.3% in 2014. We believe lower cost of production coupled with impending opportunity will help India to increase its market share in the global home textiles market.

Exhibit 62: Global home textiles market



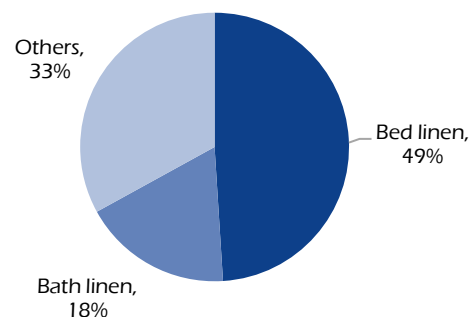
Source: Global and Indian Textile & Apparel Trade, Technopak Analysis

Exhibit 63: India's home textiles market



Source: India's Home Product Market, Technopak Analysis, www.ibef.org

Exhibit 64: India home textiles: category-wise (2013)



Source: India's Home Product Market, Technopak Analysis, www.ibef.org

Exhibit 65: Category-wise breakdown for India

(INR bn)	FY11E	FY16P	FY21P	CAGR 2011-21 (%)
Bed linen	90	132	194	8
Towels	33	48	71	8
Curtains	19	30	48	10
Blankets	15	20	29	7
Upholstery	12	19	31	10
Kitchen linen	11	16	24	8
Rugs & carpets	5	8	13	10
<b>Total</b>	<b>184</b>	<b>274</b>	<b>408</b>	<b>8</b>

Source: India's Home Product Market, Technopak Analysis, www.ibef.org

## Company Description

Welspun India (WIL) is one of the largest home textiles players in the world with a strong network in more than 50 countries. It is the largest integrated towel manufacturer in Asia with manufacturing bases at Anjar and Vapi in Gujarat. The company offers a wide range of home textile products, providing a “one-stop shop solution” for home textiles” across the globe. It enjoys strong relationships with key retailers in the US and Europe and supplies to 14 out of 30 key global retailers. Wal-Mart, Target, JC Penney, Ikea, Carrefour and Macy’s are a few of its marquee clients. Its product range covers bed & bath textiles, such as bed sheets, pillow cases, comforters, quilts, and mattress pads to bath rugs, towels, bath robes and area & accent rugs. Exports contribute ~95% of WIL’s production, of which the US market makes up ~60% and the rest by various countries, such as Canada, the UK & Japan and Europe.

## Board of Directors & Management

### Balkrishan Goenka, Chairman

Balkrishan Goenka is among India's most dynamic businessmen and chairman of the Welspun Group – a USD 3bn multinational conglomerate. He is ranked among India's most powerful CEOs by *The Economic Times*. BKG is a member in the Young Presidents Organization. He likes wearing different hats as modestly describes himself as, "a simple merchant on a global scale".

### RR Mandawewala, Managing Director

RR Mandawewala is a qualified chartered accountant (ICAI). He is in-charge of operations of the textiles business and has enabled Welspun to develop a global reach to more than 50 countries. RR has more than 25 years of experience in industries varying from textiles to SAW pipes. He is a prolific speaker and is associated with leading business councils, such as CII, FICCI, IMC, BCC, Texprocil and FIEO.

### Dipali Goenka, Executive Director

Dipali Goenka is the managing director of Welspun Global Brands and executive director of Welspun India. As the driving force behind its textiles business, she has successfully led the development of two of the most recognized brands in India, SPACES Home & Beyond and Welhome. A graduate in psychology, Dipali also has completed the owners/president management program from Harvard University. She has led retail initiatives in India and set up an award-winning design studio at Welspun, with a global perspective. Dipali also spearheads Welspun Group's CSR activities, which include Welspun Vidyamandir High School and Welspun Anganwadi at Anjar, Gujarat, as well as other initiatives related to education, empowerment & health, and the environment.

### Altaf Jiwani, CFO

Altaf Jiwani leads a team of 125 members spread across five locations, including the US and the UK. He is a part of the company's core team, which is working towards catapulting Welspun into the next trajectory of sustainable growth. With 25 years' experience in corporate finance across industries, Altaf has worked in various sectors, such as textiles, electronics and auto ancillaries. He worked with the RPG Group for more than 19 years where he was recognized as an “outstanding achiever” for his contribution to the Group's growth. Altaf has worked closely with transformational teams and leading global consulting firms, such as McKinsey. An expert in foreign exchange risk management, he has mobilized long-term working capital finance in domestic as well as overseas markets through debt and equity.

### J Barry Leonard, US President & CEO

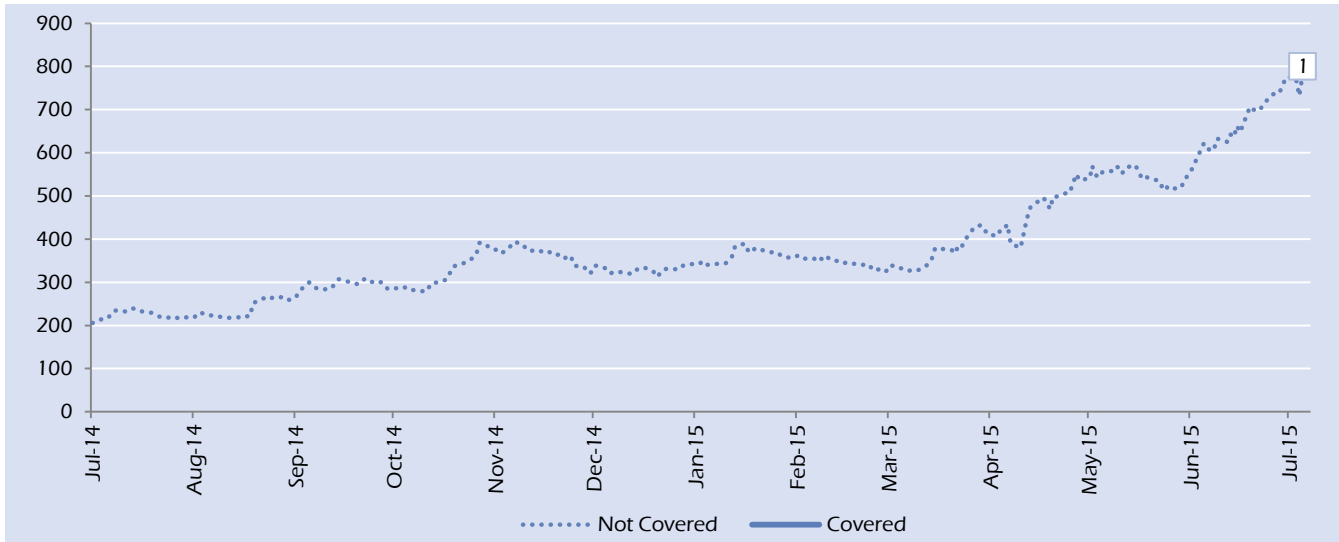
J Barry Leonard is currently president and CEO of Welspun USA, based in New York. Barry has a bachelor's degree in textiles technology from North Carolina State University in 1975 and a master's degree from the Institute of Textile Technology in 1977. He also has completed a post graduation fellowship at the Institute of Textile Technology in 1979 and the Post Harvard Business School Advanced Management program in 1990. Barry has been a leader in the home fashions industry for more than three decades. He was focused on the operational integration of Croscill Living's three companies to maximize profitability and growth. He was CEO and president of Croscill Home LLC, Glenoit LLC, and Ex-Cell Home Fashions, Inc.

Photos from our visit to Welspun's Anjar plant in Gujarat recently



Source: Company, Elara Securities Research

### Coverage History



Date	Rating	Target Price	Closing Price
22-Jul-2015	Buy	INR 1,127	INR 780

### Guide to Research Rating

<b>BUY</b>	Absolute Return >+20%
<b>ACCUMULATE</b>	Absolute Return +5% to +20%
<b>REDUCE</b>	Absolute Return -5% to +5%
<b>SELL</b>	Absolute Return < -5%

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