

Initiating Coverage KPR Mill Ltd.

22-March-2021



Industry	LTP	Base Case Fair Value	Bull Case Fair Value	Recommendation	Time Horizon
Textile	Rs.1063.45	Rs.1090	Rs.1186	Buy on dips to Rs.994 and add more at Rs.880	2 quarters

HDFC Scrip Code	KPRMILEQNR
BSE Code	532889
NSE Code	KPRMILL
Bloomberg	KPR:IN
CMP March 22, 2021	1063.45
Equity Capital (Rscr)	34
Face Value (Rs)	5
Equity Share O/S (cr)	6.88
Market Cap (Rscrs)	7318
Book Value (Rs)	271
Avg. 52 Wk Volumes	152941
52 Week High	1151.00
52 Week Low	316.90

Share holding Pattern % (Dec, 2020)	
Promoters	74.72
Institutions	17.62
Non Institutions	7.66
Total	100.0

Fundamental Research Analyst

Jimit Zaveri

jimit.zaveri@hdfcsec.com

Our Take:

KPR is a leading business conglomerate in India, which is engaged in textiles, sugar, ethanol, and power generation. Textiles is its core business, wherein it is vertically integrated, with a presence across the entire value chain from the manufacturing of cotton yarn to processed fabric and ready garments. KPR is one of the largest exporters (in volume terms) of knitted garments from India with a capacity of 115mn pcs/annum. Going forward, it plans to augment its capacity by another 42mn pcs/annum. In order to leverage its knitting manufacturing expertise and expand its B2C business, it has recently launched a new innerwear and athleisure brand FASO.

The company has a focus on the export market, which has led to export revenue growing from 33% of sales in FY15 to 42% in FY20. The company's major export destinations are the United Kingdom, China, Australia and the US. Additionally, it has invested in a captive power plant which has helped it reduce power costs.

The newly announced capex plan will increase borrowing on the balance sheet but would cover garmenting under TUFs and attract 50% interest subsidy for ethanol capacity. Also, the new capacities will come up under a new subsidiary, which will be eligible for the lower tax rate of ~15%.

Valuations & Recommendation:

We expect the company to benefit from its (1) strong balance sheet, (2) longstanding relationship with marquee Indian and global clients, (3) fully integrated presence from manufacturing yarn to garments, and (4) investment in captive power plants. Also, the company's new venture in B2C branded innerwear segment, the recent commissioning of its ethanol facility, and the expansion of garmenting capacity by 42mn pcs/annum lend it strong growth visibility. While the COVID-led lockdown had adversely impacted H1FY21, the company has witnessed a strong recovery Q3 onwards. Going forward, we expect a 10% CAGR in top-line and 13% EPS CAGR over FY20-23E.

KPR is one the key long term stories to play the Indian garment export theme. Its competitive advantages, integrated operations, focus on value added products, and strong balance sheet remain the key triggers.

We believe the base case fair value of the stock is Rs 1090 (14.2x FY23E EPS), while the bull case fair value is Rs 1186 (15.5x FY23E EPS). Investors willing to take some risk can look to buy the stock on dips to Rs 994 (13.0x of FY23E EPS) and add more at Rs 880 (11.5x of FY23E EPS).



Financial Summary

Particulars (Rs cr)	Q3FY21	Q3FY20	YoY-%	Q2FY21	QoQ-%	FY19	FY20	FY21E	FY22E	FY23E
Total Operating Income	930	770	21%	942	-1%	3,384.0	3,352.6	3,335.9	3,877.9	4,420.9
EBITDA	251	137	83%	189	33%	611.8	622.0	709.1	770.2	876.8
APAT	156	94	66%	113	39%	334.9	376.7	408.4	449.1	526.4
Diluted EPS (Rs)	22.71	13.72	66%	16.36	39%	48.7	54.7	59.3	65.3	76.5
RoE-%						19.9	20.6	19.9	18.3	18.1
P/E (x)						21.7	19.3	17.8	16.2	13.8
EV/EBITDA						11.7	11.5	10.1	9.3	8.2

(Source: Company, HDFC sec)

Q3FY21 Result Update

- Revenue stood at Rs.930 cr, +21%/-1% y-o-y/q-o-q. Gross margin expanded significantly, by 707 bps YoY to ~50%, on account of favorable spreads and the advantage of being vertically integrated. The net profit of the company stood at Rs.156 cr, +66%/39% y-o-y/q-o-q. In Q3 FY21, garments production grew by 21.92% YoY to 27.87 mn garments as against 22.86 mn in the previous year.

Segment-wise

- Revenue from the textile segment grew by 18.5% y-o-y to Rs.805 cr and EBIT for the segment grew by 119.8% y-o-y to Rs.193 cr.
- Revenue from the sugar segment grew by 66.9% y-o-y to Rs.109 cr while its EBIT grew by 51.7% y-o-y to Rs.20 cr.
- Revenue from 'Other' segment de-grew by 37.2% y-o-y to Rs.16 cr while EBIT de-grew by 43.2% y-o-y to Rs.1 cr.

Long-term Triggers

Established track record of operations and experienced promoters

The promoters of the company have been in the textile business for nearly three decades and have a presence in almost all segments of the cotton textile value chain. KPR produces cotton yarn, knitted fabrics, and knitted apparels and has facilities in the Tiruppur-Coimbatore region. With a capacity of about 3.5 lakh spindles, the company is one of the leading players for supplying yarn to the Tirupur market, which is a major centre for the export of cotton textiles. KPR also produces knitted garments, which are directly exported to buyers, mainly in Europe and America. The company has spinning mills at Sathyamangalam & Karumathampatti, Neelambur & Arasur at Coimbatore, apart from a processing unit at Perundurai, and Erode & garment units at Arasur, Coimbatore and Thekkalur (Tiruppur). The company is one of



the largest yarn and Knitted garment manufacturers in India. It has over 1,200+ customers for yarn & fabric and around 60 top international brands.

Integrated operations with a strong presence in the textile industry

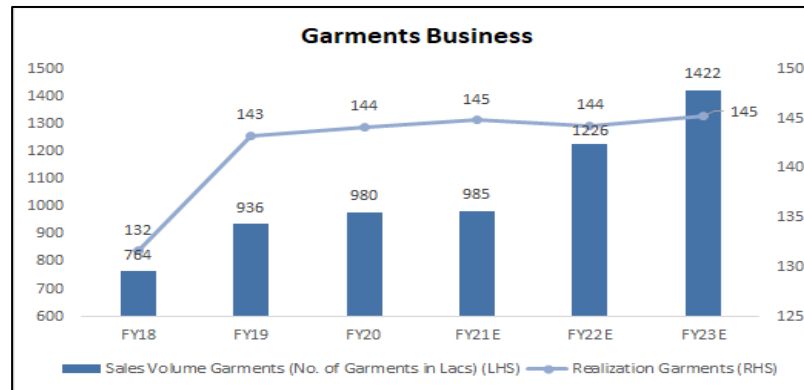
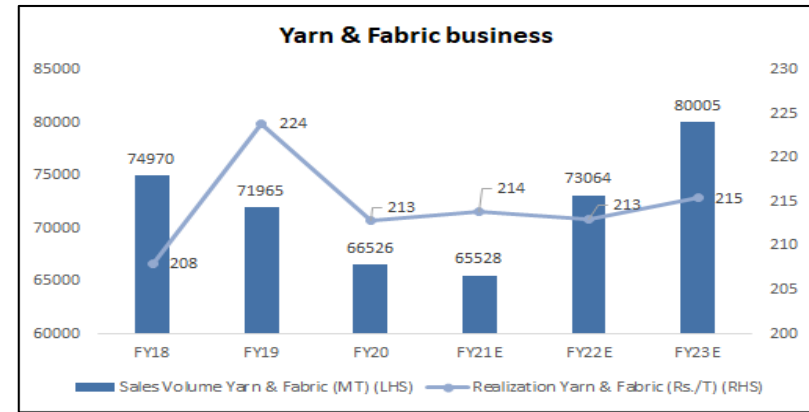
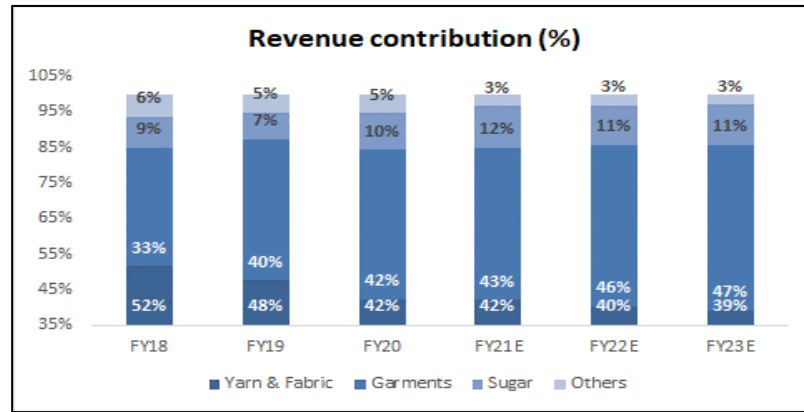
KPR is vertically integrated across the textile chain value (from manufacturing of cotton yarn to processed fabric to garments), which lends it strong operational flexibility. It can produce 1,00,000 MT of yarn per annum; 40,000 MT fabrics per annum; 115 million ready-made knitted apparel per annum (including 36 mn pieces of the leased facility from its subsidiary, K.P.R Sugar Mill Limited). Its processing facility can process 22,000 MT per annum and it owns 66 windmills with a total power generation capacity of 61.92 MW. To diversify further, the company has ventured into branded innerwear and led expansion in garments through subsidiaries. In FY19, the company set up a garment unit in Ethiopia with a production capacity of 10 mn garments per annum. It uses the best quality cotton 'Shankar 6' as the raw material to maintain quality.



(Source – Company, HDFC sec Research)



In FY20, KPR ventured into the branded retail segment through the launch of premium quality men’s innerwear and athleisure products. It launched these under the brand name FASO (Fashion Adapted Sustainable and Organic) in the states of Tamil Nadu, Kerala, Andhra and Telangana. FASO categories include briefs, trunks, boxer shorts, vests, gym vests and muscle tees. FASO uses combed organic cotton and micro nylon elastic.



(Source – Company, HDFC sec Research)

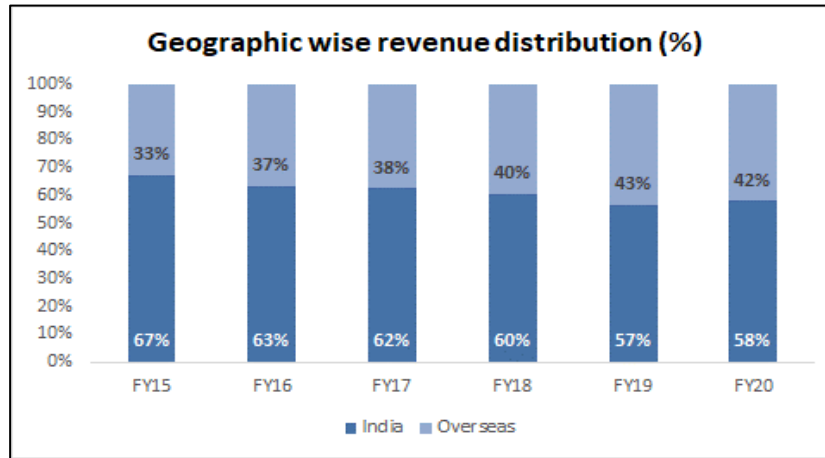


Increase in share of value-added products

KPR's entire yarn capacity upgraded to value-added yarn (Compact, Melange, Color Melange, PC, Slub, Grindle & Vortex yarn). 33% of yarn and ~47% of fabric is used as captive consumption to manufacture value-added products.

KPR registered a flat operating income during FY20, supported mainly by garments. Over the past few years, KPR's product mix has witnessed a gradual change with an increase in the share of value-added products (mainly garments) in the sales mix.

Geographic diversification and reputed customer base



(Source – Company, HDFC sec Research)

KPR has a diversified revenue stream. Of the total exports, yarn constituted 8.4% (PY: 19%), garment 89% (PY: 78%) and fabric 2% (PY: 2%) in FY20. The company's major export destinations are the United Kingdom, China, Australia and the US. The top-5 export destinations for the company contributed 62% of total exports and 26% of total income in FY20 as against 77% and 34% respectively in FY19. During FY20, the top-10 export clients contributed 72% of total exports and accounted for 30.6% of total income while the top-10 domestic customers contributed 9.3% of domestic sales and 5.4% of total income. No single customer is contributing over 10% of KPR's total income.



Investment in captive power plant

KPR is one of the largest captive power generators in the textile Industry. The company has invested in eco-friendly windmills at Tirunelveli, Tenkasi, Theni and Coimbatore districts in Tamil Nadu with the total wind power capacity of 61.92 MW. This capacity is currently meeting 60% of the company's textile power requirement.

Further, it has invested in a 40 MW Co-Gen Power Project. With Co-gen Power, KPR has attained self-sufficiency in meeting a substantial part of its power requirement throughout the year. This investment helps it reduce its power costs and improve the margin.

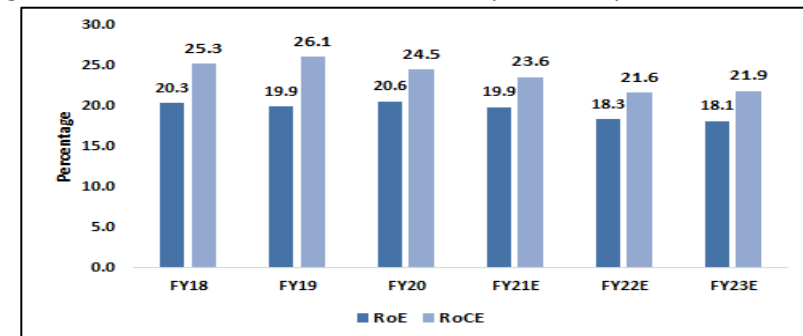
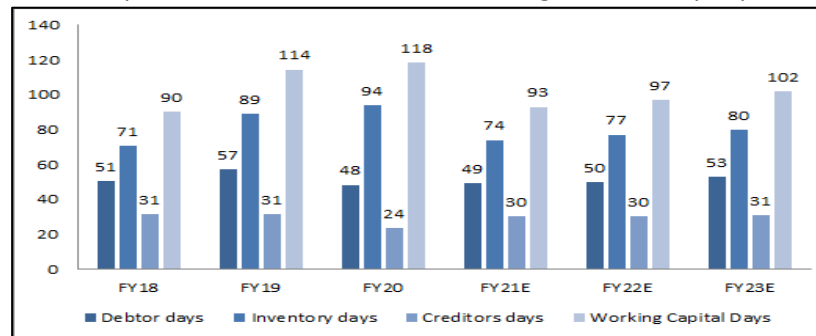
Ethanol plant to add value to the sugar segment

KPR has successfully established an ethanol plant with a capacity of 90 KLPD at a sugar factory in Karnataka. Ethanol production has commenced in FY20. Its full-fledged commercial operation has already started in the current fiscal.

The company is planning a capex of Rs.500 crore by setting up a sugar (10,000 TCD) and ethanol plant (230 KLPD). The project is expected to become operational by November 2021. The existing sugar ethanol capacity has a revenue potential of ~Rs.550 cr and the new capacity that is being set up is expected to generate revenue of ~Rs.600 cr.

Stable financial performance

KPR has low debt with debt/equity of 0.4x and interest coverage of 10.4x in FY20. The company has stable return ratios and working capital, which help maintain the balance sheet strength. The company had bought back shares in FY19, which should improve the per-share value.





China plus one strategy

Global companies have stepped up efforts to implement the 'China Plus One' strategy of diversifying their supply chains in the wake of the COVID-induced disruptions and US-China trade tensions. This provides a chance for India to emerge as a global manufacturing hub. KPR being one of largest garment exporters from India is likely to benefit out of this.

What could go wrong?

The adverse price movement of cotton

Cotton is one of the most important commercial crops cultivated in India. In the raw material consumption basket of the Indian textile industry, the proportion of cotton is around 60%. . Any significant volatility in cotton prices can impact the operating margins of the company. KPR usually books the cotton price at the time of signing the contracts with the clients, thereby mitigating its exposure to raw material price volatility.

Decent yarn sales come directly or indirectly from the Tiruppur market

The company sells its major produce to Tiruppur's knitwear and garment manufacturers. Over the years, KPR has reduced its exposure to the Tiruppur market; however, it continues to cater to this market indirectly through a large exposure to several smaller players in the industry who in turn export.

Change in government policy with respect to ethanol blending:

Any change in government policy towards interest subsidy on term loan for ethanol capacity and ethanol blending in petrol can impact the performance of its sugar and ethanol business.

Increasing exposure to sugar business (which is a cyclical commodity business) could impact the valuations that KPR attracts.

Ethiopian operations can face labour and logistic challenges. KPR could face challenges in training the work force in the initial stages. The company's plant is situated ~ 800 km from the nearest port Djibouti, which could pose logistics challenges.

About the company

KPR is promoted by three brothers, Mr K.P. Ramasamy, Mr K.P.D. Sigamani and Mr P. Nataraj. KPR is an integrated player producing cotton yarn (3.5 lakh spindles), cotton knitted fabrics (capacity of 27,000 MT p.a) and garments (capacity of 105 million pieces p.a.) from its facilities



located in the Tiruppur-Coimbatore region. With a capacity of 354,240 spindles, KPR is one of the leading players and supplier of yarn. It had also set up a garment unit with a capacity of 10 mn pieces per annum in Ethiopia through its subsidiary in FY19. The company has entered the Retail business by launching a new innerwear and athleisure brand 'FASO - Italian at Heart'.

The company has installed windmills, which have a total generation capacity of 61.92MW of green power, for captive consumption at Tamil Nadu, in order to become 75% self-reliant with regards to power requirements.

The journey so far

1984	Maiden business at Coimbatore, India
1989	Knitted garment export at Tirupur.
1995	First spinning unit at Sathyamangalam with 6,000 spindles. Increased to 30,240 spindles by 1999
2001	Spinning mill at Karumathampatti with 30,240 spindles; Knitting facility and windmill for captive use
2003	Spinning unit at Neelambur with 50,784 spindles; Knitting facility and windmill
2005	At Arasur 1,00,800 spindles; Knitting facility, Garment Unit of 26 million garments and windmills
2008	Fabric Processing Unit at SIPCOT, Perundurai 9,000 MT per annum with trendsetter Effluent Treatment Plant
2010	Exclusive value-added Compact Spinning unit of 1,03,680 spindles at Karumathampatti and windmills
2011	Modernization & expansion of 21,216 spindles at Sathyamangalam
2012	Another Value-added product Melange yarn. 16,608 spindles at Karumathampatti.
2013	Co-gen cum Sugar Plant at Karnataka - 30 MW & 5000 TCD capacity
2014	Expanded Garment capacity at Arasur by 10 mn garments,
2015	New greenfield Garment capacity at Thekkalur with 12 mn garments
2016	Established New greenfield garment facility of 36 mn garments at Thekkalur Plant III
2017	Established new Eco-friendly Processing capacity with Advanced Technology - 9,000 MT. Established Sophisticated high-resolution printing division - 7,500 MT
2018	Established 10 Million Garment manufacturing unit at Mekelle, Ethiopia
2019	Increased Processing capacity by 4000 MT. Brownfield garment expansion by 10 mn garments in existing facilities. Set up 130 KLPD Ethanol Plant along with 10 MW Co-gen power. Retail segment: 'FASO' 100% Organic Cotton Men's innerwear Sportswear and Athleisure.
2020	Knitting facility of 13000 MT at karumathampatti. Vortex Viscose Yarn capacity of 4000 MT at Neelambur

Income Statement

(Rs Cr)	FY19	FY20	FY21E	FY22E	FY23E
Net Revenue	3384	3353	3336	3878	4421
Growth (%)	11.9	-0.9	-0.5	16.3	14.0
Operating Expenses	2772	2731	2627	3108	3544
EBITDA	612	622	709	770	877
Growth (%)	6.5	1.7	14.0	8.6	13.8
EBITDA Margin (%)	18.1	18.6	21.3	19.9	19.8
Other Income	36.9	36.5	40.0	42.0	50.0
Depreciation	131.1	137.1	146.7	153.7	164.3
EBIT	518	521	602	658	762
Interest	48.9	49.7	50.1	58.3	59.0
Shares of Profit in Joint Ventures (net of Tax)	0.0	0.0	0.0	0.0	0.0
PBT	469	472	552	600	703
Tax	133.7	95.0	143.9	151.1	177.1
RPAT	335	377	408	449	526
Growth (%)	15.3	12.5	8.4	10.0	17.2
EPS	48.7	54.7	59.3	65.3	76.5

Balance Sheet

As at March	FY19	FY20	FY21E	FY22E	FY23E
SOURCE OF FUNDS					
Share Capital	36.3	34.4	34.4	34.4	34.4
Reserves	1754	1831	2209	2624	3112
Shareholders' Funds	1790	1866	2243	2658	3147
Long Term Debt	130	207	238	297	223
Long Term Provisions & Others	60	54	73	92	117
Total Source of Funds	1980	2127	2554	3047	3487
APPLICATION OF FUNDS					
Net Block	1149	1328	1431	1757	1689
Non-Current Investments	2	2	3	3	3
Deferred Tax Assets (net)	10	15	15	14	14
Long Term Loans & Advances	57	42	50	55	61
Other Assets	0	0	0	0	0
Total Non Current Assets	1218	1387	1499	1829	1767
Current Investments	0	7	14	15	17
Inventories	1006	716	676	818	969
Cash & Equivalents	76	155	642	768	988
Other Current Assets	48	67	74	82	89
Total Current Assets	1765	1510	1980	2347	2845
Short-Term Borrowings	691	534	587	728	655
Trade Payables	222	132	216	255	301
Other Current Liab & Provisions	83	101	118	142	165
Short-Term Provisions	7	3	4	4	4
Total Current Liabilities	1003	770	925	1130	1125
Net Current Assets	762	740	1055	1217	1720
Total Application of Funds	1980	2127	2554	3047	3487

(Source: Company, HDFC sec Research)

Cash Flow Statement

(Rs Cr)	FY19	FY20	FY21E	FY22E	FY23E
Reported PBT	469	472	552	600	703
Non-operating & EO items	-37	-36	-40	-42	-50
Interest Expenses	49	50	50	58	59
Depreciation	131	137	147	154	164
Working Capital Change	-187	102	172	-37	-283
Tax Paid	-134	-95	-144	-151	-177
OPERATING CASH FLOW (a)	291	629	738	583	417
Capex	74	-179	-103	-326	68
Free Cash Flow	365	450	634	256	485
Investments	-43	10	-9	-4	-6
Non-operating income	37	36	40	42	50
INVESTING CASH FLOW (b)	67	-132	-72	-289	113
Debt Issuance / (Repaid)	-20	71	49	78	-48
Interest Expenses	-49	-50	-50	-58	-59
FCFE	295	471	634	276	377
Share Capital Issuance	-1	-2	0	0	0
Dividend	-10	-36	-31	-34	-38
FINANCING CASH FLOW (c)	-80	-17	-32	-14	-145
NET CASH FLOW (a+b+c)	278	480	634	280	384

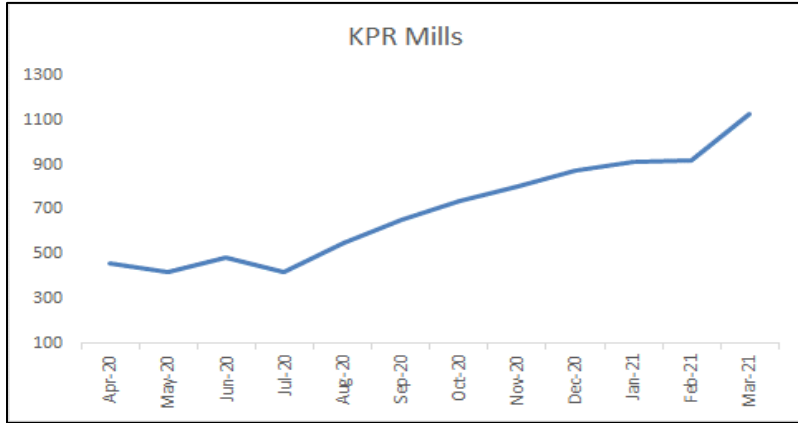
Key Ratios (%)

	FY19	FY20	FY21E	FY22E	FY23E
Profitability (%)					
EBITDA Margin	18.1	18.6	21.3	19.9	19.8
EBIT Margin	15.3	15.5	18.1	17.0	17.2
APAT Margin	9.9	11.2	12.2	11.6	11.9
RoE	19.9	20.6	19.9	18.3	18.1
RoCE	26.1	24.5	23.6	21.6	21.9
Solvency Ratio					
D/E	0.5	0.4	0.4	0.4	0.3
Interest Coverage	10.6	10.5	12.0	11.3	12.9
PER SHARE DATA					
EPS	48.7	54.7	59.3	65.3	76.5
CEPS	64.2	74.7	80.7	87.6	100.4
BV	247	271	309	366	434
Dividend	0.8	4.5	4.5	5.0	5.5
Turnover Ratios (days)					
Debtor days	57	48	49	50	53
Inventory days	89	94	74	77	80
Creditors days	31	24	30	30	31
Working Capital Days	114	118	93	97	102
VALUATION					
P/E	21.7	19.3	17.8	16.2	13.8
P/BV	4.3	3.9	3.4	2.9	2.4
EV/EBITDA	11.7	11.5	10.1	9.3	8.2
Dividend Yield	0.1	0.4	0.4	0.5	0.5
Dividend Payout	1.5	8.2	7.6	7.7	7.2

(Source: Company, HDFC sec Research)



One Year Price Chart



(Source: Company, HDFC sec Research)

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Compliance Officer: Binkle R. Oza Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

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