Initiating Coverage

PDS Ltd.

November 29, 2022

RETAILRESEARCH

PDS Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Textiles	Rs. 348	Buy in Rs 345-362 band and add more on dips in Rs 307-313 band	Rs.383	Rs. 417	2-3 quarters

HDFC Scrip Code	PDSLTDEQNR
BSE Code	538730
NSE Code	PDSL
Bloomberg	PDSL:IN
CMP – Nov 28, 2022	348
Equity Capital (Rs Cr)	26
Face Value (Rs)	2
Equity Share O/S (Cr)	13
Market Cap (Rs Cr)	4539
Book Value (Rs)	67
Avg. 52 Wk Volumes	64447
52 Week High	419
52 Week Low	273

Share holding Pattern % (September, 2022)	
Promoters	66.52
Institutions	3.69
Non Institutions	29.79
Total	100.0

* Refer at the end for explanation on Risk Ratings

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Our Take:

PDS Limited (PDSL) is a design-led plug-and-play platform, providing customised manufacturing and sourcing solutions to the world's leading textile retailers and brands. The company has created an integrated platform focussed on design, sourcing and manufacturing. The platform is enabled by PDSL's expertise in robust risk management, social, environmental, and ethical compliance, and value-added services. The platform facilitates sustainable and responsible sourcing with its foundation laid in an entrepreneurial business model. The company is able to identify the right product for the right market and the right factory which is further supported by a strong compliant supply chain and a core understanding of different geographies and markets. The capabilities of PDS platform enable multi-country sourcing from countries like India, Bangladesh, China, Pakistan, Sri Lanka, Myanmar, Turkey, and Vietnam. Similarly, multi-product sourcing for all categories pertaining to apparel, fashion, home furnishing has also been well established. Supported by creative inputs from their market intelligence, PDS has steadily perfected the product development aspect of their business through innovative fabrics, extensive trend research, graphics and sampling. The PDSL platform enables speed to market and finally cost-effectiveness along with margin improvement through strategic sourcing / favourable credit terms for retailers and suppliers.

We believe that in the past years, the company has been able to build a strong foundation on which it can now capture several burgeoning opportunities with its innovative operating model and inherent strengths. Going ahead, the company is working around expanding its geographic presence, increasing margins, on-boarding new partnerships and collaborations, leveraging Sourcing as a Service, and deploying digital technologies to drive efficient operations.

Further, the investments made through its Venture Tech portfolio enables PDSL to sense the pulse of the market and proactively offer new solutions to stay ahead of the curve. The collaborations add on to its 'sustainable fashion' offering and helps it expand the presence in the fashion value chain.

Valuation & Recommendation:

PDSL has an ambition to cross the USD 2.5 bn (~doubling from current levels) top line mark over next five years, powered by geographic expansion, operational excellence, strategic investments, collaborative partnerships and a high-margin, asset light business model. It continues to implement various cost-optimisation measures (e.g. choosing the right partner manufacturer for the right order) and efficient logistics to maximize returns. With the help of its asset-light model, maturing of new business verticals over the next 2-3 years, and turnaround of manufacturing, it is set to generate higher returns.

We think the base case fair value of the stock is Rs 383 (13x FY24E EPS) and the bull case fair value is Rs 417 (14x FY24E EPS). Investors can buy the in stock Rs 345-362 band (12x FY24E EPS) and add more on dips in Rs 307-313 (10.5x FY24E EPS).

Financial Summary

Particulars (in Rs Cr)	Q2FY23	Q2FY22	YoY-%	Q1FY23	QoQ	FY20	FY21	FY22	FY23E	FY24E
Operating Income	2921.2	2340.4	25%	2194.9	33%	6,648	6,213	8,828	10,936	12,951
EBITDA	119.2	73.1	63%	84.3	41%	186	230	323	416	518
Reported PAT	93.9	37.0	154%	51.6	82%	46	84	248	280	377
Diluted EPS (Rs)	7.1	2.8	154%	3.9	82%	3.5	6.5	19.1	21.5	28.6
RoE-%						9.0	14.0	32.7	28.6	30.2
P/E (x)						98.7	53.8	18.3	16.2	12.2
EV/EBITDA						25.6	19.8	13.8	10.7	8.1

(Source: Company, HDFC sec)

Revenue from Operations increased by 33% to Rs 2,921cr from Rs 2,195cr in Q2FY22. Reported Gross Profit at Rs 495 Cr compared to Rs 360 Cr, increased by 37%. Gross Margins increased by 55bps to 17.0% vs 16.4%. EBITDA increased by 41% to Rs 119 Cr from Rs 84 Cr in Q2FY22. EBITDA Margin increased to 4.1% vs 3.8%. Finance costs have increased due to the increased cost of borrowing over the last year; impact has been partially mitigated by increase in early payment discounts captured in gross margins. Other income stood at Rs 39 Cr (up 260% YoY) and includes gain from real estate sale. This led to sharp jump of 70% YoY in APAT.

The manufacturing segment recorded growth of 13% with a topline of Rs 147 Cr. The segment turned profitable in Q4FY22 and continued its profitability journey. The sourcing segment clocked a topline of Rs 2835 Cr in Q2FY23, accounting for 95% of the company's topline with a growth of 35% compared to the previous year. The segment reported an EBIT of 3.3% with a ROCE of 44%.

Key Triggers

Evolution of PDSL

Pearl Global was established in 1987 and consisted of manufacturing, trading, marketing & distribution and exports of readymade garments. It segregated its global marketing, sourcing & distribution business from its garment manufacturing business and now the existing company is purely engaged in manufacturing and exports of readymade garments.

Promoted by Mr. Deepak Seth, and his two sons: Mr. Palak Seth and Mr. Pulkit Seth, the company entered the secondary market in 2007. Till 2014, PGIL operated (through its subsidiaries) with two distinct business segments:

Manufacturing and Merchant Trade Manufacturing – through facilities in Bangladesh, India and Indonesia. Merchant Trade – Indian office procures orders from customers and outsources them to own/third party factories in Bangladesh, and Indonesia.

Sourcing Marketing and Distribution (SDM) Vast marketing network spread across Hong Kong, United States and UK which procures orders from the customers and outsources them entirely to third-party manufacturers. It also has facilities handling apparels processing and distribution in the US and UK.

Post the Scheme of Arrangement of the Company with PDS Multinational Fashions Limited, the SDM business of the Group divested into PDS as on May 13, 2014.

PDS Multinational Fashions issued six fully paid up equity shares of Rs.10 to the shareholders of Pearl Global Industries for every five fully paid up equity shares of Rs 10 each held, amounting to Rs.25.99 crore on June 5, 2014.

PDS Multinational Fashions Ltd thus ceased to be a subsidiary of PGIL and accordingly it's Q1FY15.

Pearl Global Industries Ltd. (PGIL) – PGIL manufactures readymade garments, across categories (knits/woven/denims/non-denims/outerwear) and segments (men's wear, women's wear as well as children's wear). The company (along with its subsidiaries) has its manufacturing base in India (Gurugram, Chennai and Bengaluru), Bangladesh, Vietnam and Indonesia, with a total capacity to manufacture ~80 million pieces of garments per annum. PGIL is an approved vendor of renowned international brands and retailers, e.g., GAP, Banana Republic, PVH Corp., Kohl's, Macy's, Primark, Target, Next, etc. PGIL is listed on BSE and NSE; its market capitalisation as on 17th November, 2022 stood at Rs. 884 Cr.

Financial snapshot of PGIL

Particulars (in Rs Cr)	FY18	FY19	FY20	FY21	FY22
Revenue from Operations	1,496	1,758	1,685	1,491	2,714
EBITDA	24.8	88.1	66.9	60.6	140.6
EBITDA Margin (%)	1.7%	5.0%	4.0%	4.1%	5.2%
Profit After Tax	23.1	67.1	21.7	17.5	70.1
Earnings per Share (in Rs)	11.1	31	9.9	8	31.5

(Source: PGIL, HDFC sec)

PDS Ltd. - PDS Multinational Fashions Limited changed its name to PDS Limited. (PDSL) in February 2022.

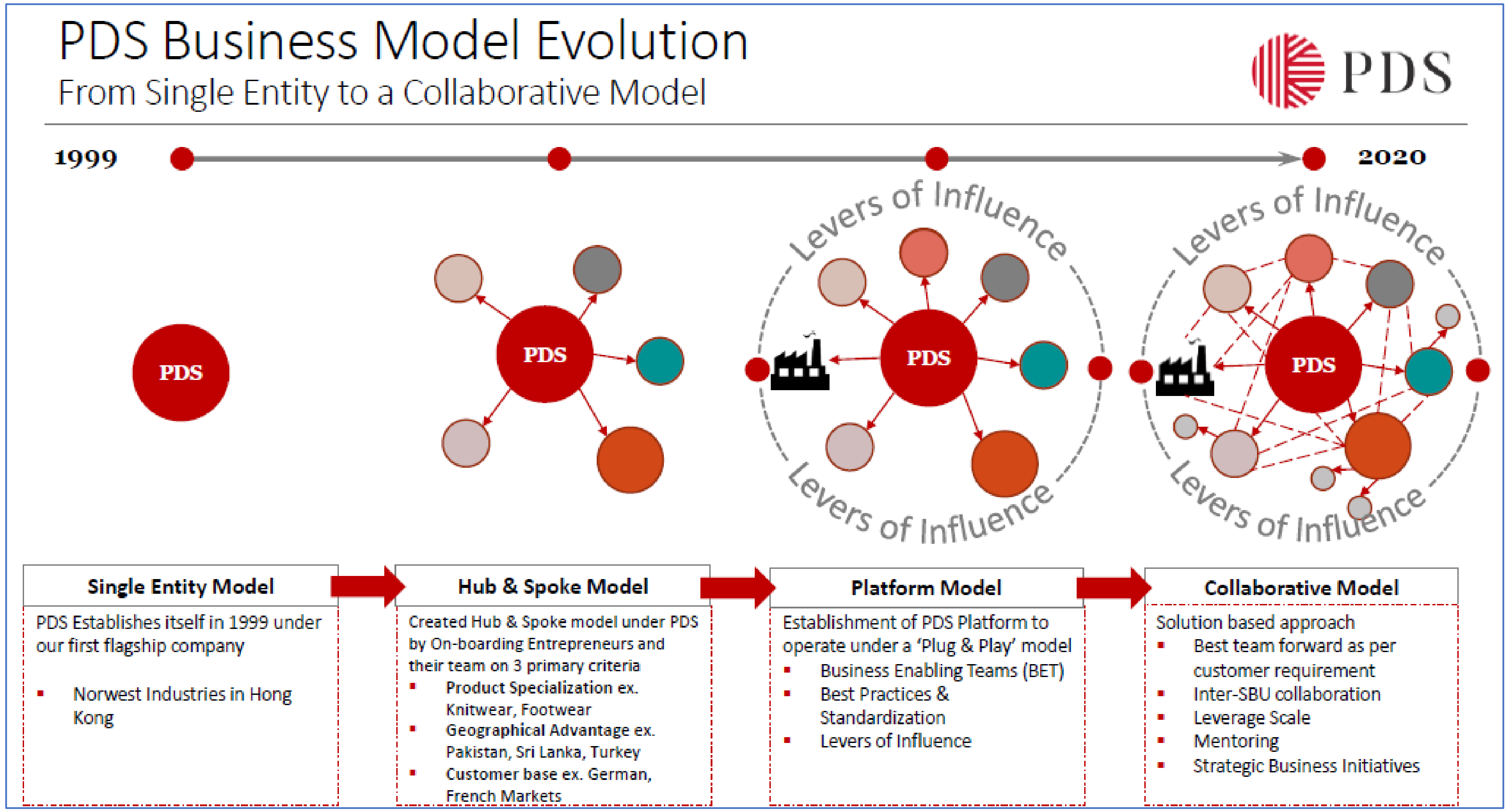
The idea of PDSL germinated with two flagship companies – Norwest Industries Limited in Hong Kong and Poeticgem Limited in the UK – launched by the promoter family in 1999. Starting out as a single entity, PDS gradually progressed into a hub and spoke model with a strategy to on-board entrepreneurs and their teams based on product specialisation, geographical advantage, or existing customer base. With its asset light business model, rather than acquiring companies, PDS partnered with them to ensure mutual growth.

It then transitioned into a platform model where new partners were on-boarded to the PDS Group in a plug and play format. This gave them the opportunity to work closely with the biggest brands in the fashion industry and learn industry-best practices. This, in turn, accelerated the company's expansion process and strengthened its operational capabilities. Today, PDS has evolved to operate on a unique collaborative model, with refined processes and a solution-based approach.

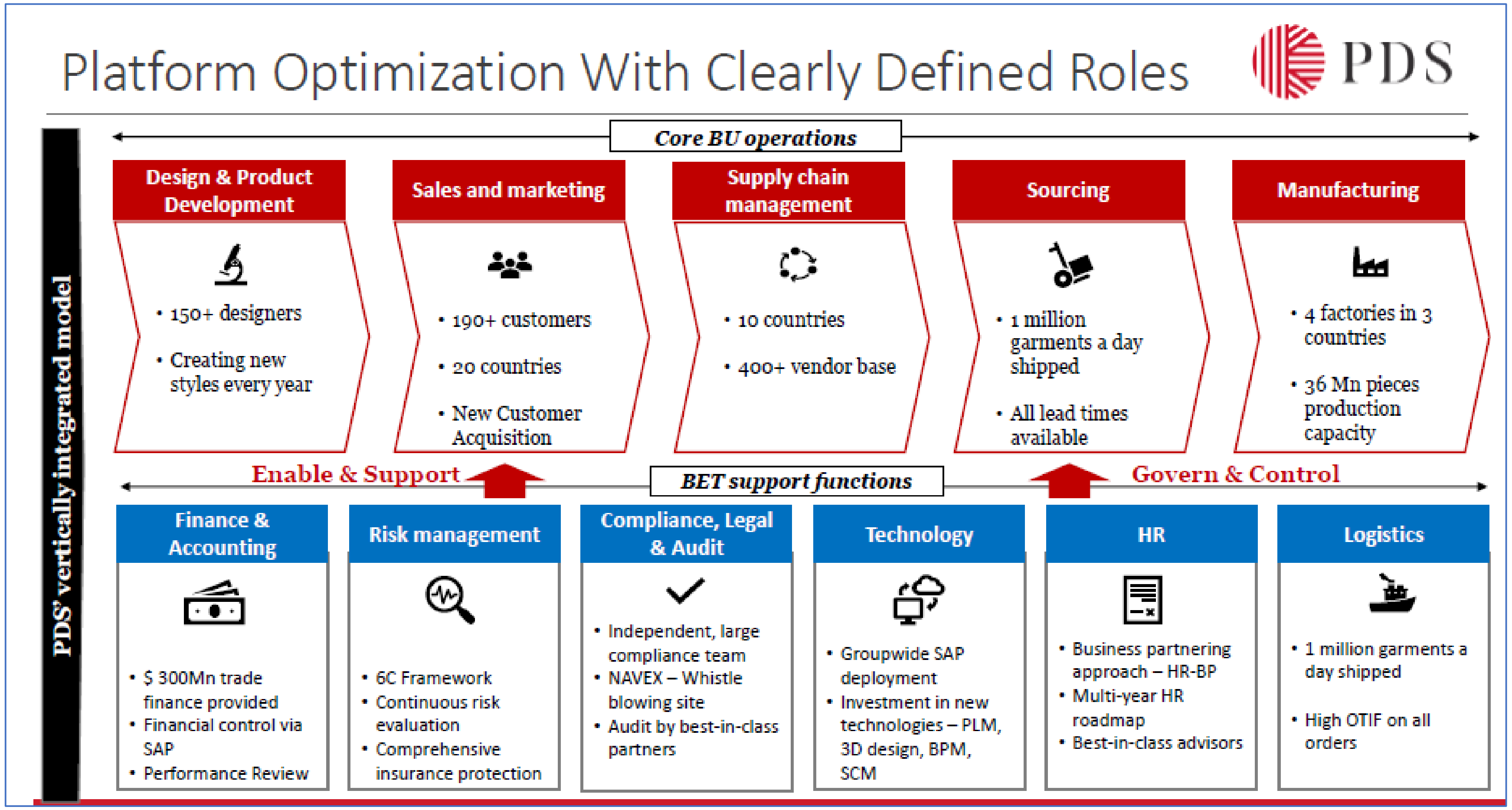
What is the relevance of Plug & Play model and what attracts entrepreneurs to PDSL?
While prima facie, it might look like a pure trading business, there's lot more as company not just acts as an intermediary between brands/retailers and manufacturers, it provides total supply chain solutions. The key reason to have Plug & Play model is given the nature (relationship based) of the outsourcing business, it cannot be centrally driven. Entrepreneurs operating a standalone outsourcing business model tend to plateau on their own after a certain point. On joining PDSL, their buying power increases as they get access to the combined network of all customers and vendors.

The business heads/entrepreneurs undertake the business development part and work with PDSL's network of vendors. Their core responsibility is building and maintaining relationships with customers and P/L management. PDSL takes on the backend functions of the companies (audit, finance, risk management, etc.). PDSL takes over the operations of the business heads and provide them access to an extensive vendor network. Entrepreneurs, in turn, bring in the contacts and domain expertise. There is usually a pre-agreed 3-year business plan wherein entrepreneurs are supported with initial setup costs and expected to turn profitable in three years. Being a part of such a big network helps business heads negotiate better with customers and vendors, and meet compliance needs effectively. There is a profit share mechanism that the business heads get a cut of; PDS supports them with this. It is a win-win situation for both PDS and business heads. Operating across business verticals through individual subsidiary, however, has created a complex group structure which may be a concerning factor for some investors. PDSL, though has robust system of internal and external controls. ~58% of its 88 subsidiaries are audited by Big 5. 83%/100% of sales and PBT is audited by Big 5 auditors.

PDS Ltd.



PDS Business Model Evolution
From Single Entity to a Collaborative Model
PDS
1999
2020
PDS
Levers of Influence
Single Entity Model
PDS Establishes itself in 1999 under our first flagship company
Norwest Industries in Hong Kong
Hub & Spoke Model
Created Hub & Spoke model under PDS by On-boarding Entrepreneurs and their team on 3 primary criteria
Product Specialization ex. Knitwear, Footwear
Geographical Advantage ex. Pakistan, Sri Lanka, Turkey
Customer base ex. German, French Markets
Platform Model
Establishment of PDS Platform to operate under a 'Plug & Play' model
Business Enabling Teams (BET)
Best Practices & Standardization
Levers of Influence
Collaborative Model
Solution based approach
Best team forward as per customer requirement
Inter-SBU collaboration
Leverage Scale
Mentoring
Strategic Business Initiatives



(Source: Company, HDFC sec)

Journey of PDSL

Year	Particulars
1999	Promoter family established first flagship companies Norwest Industries Hong Kong, Poeticgem in UK
2003-05	Received approval for sourcing operations in India
	Established sourcing operations in China, Bangladesh
2007-08	Entered into denims through establishment of Zamira Fashion in Hong Kong
	Launched direct marketing operations in Chile under the names – PG Group and PG Home
	Marked entry into non-apparel category of home wear and home furnishing

2009-10	Formed division in UK for design, supply and manufacture of licensed apparel products
	Launched Bangladesh direct marketing operations
2012-13	Established direct marketing business operations in India
	Established operations in Turkey, Germany, Sri Lanka and Spain
	Expanded direct marketing offices in Melbourne, Australia
	Commenced Corporate Services operations in Bangalore
	Received license for operations in Myanmar
	Set up leased manufacturing operations in Sri Lanka
2014	Listed on Indian Stock exchanges post demerger
	Launched NAVEX to strengthen PDS' code of conduct for global compliance
	Entered into JV with Techno Germany
	Launched operations in Cambodia
	Fabric sourcing division setup in Shanghai
	Launched sourcing operations in Belgium and Paksistan
	JJ Star operations started in South China
2016-17	Launched manufacturing facilities in Bangladesh under Progress Apparels (Bangladesh) Limited and Green Smart Shirts Limited
	Forayed into Technology business to develop and offer cloud-based software and mobile application in HRM-Qandle
2018	Commissioned the two manufacturing units in Bangladesh
	PDS Towers inaugurated in Gurgaon, India
	Acquired a manufacturing unit in Sri Lanka (erstwhile TRINCO factory)
	Strategic investment in Atterley.com Holdings, an online fashion retailer
2019-20	Acquired Kik Services Unit Limited in Bangladesh (Techno Sourcing Bangladesh Ltd)
	Acquired Lilly & Sid Ltd, UK engaged in branded kids apparel
2020-21	Appointed Group CEO for driving sustainable growth, profitability and value creation
	Business Heads on-boarded to drive business in new geographies and categories
2021-22	Established an independent office infrastructure to act as an exclusive vendor for Hanes Brands Inc. in Bangladesh
	Entered into a strategic collaboration with s.Oliver Group
	Launched Lilly + Sid from UK in the Indian market through an exclusive tie-up with Reliance Retail's fashion marketplace jio.com, supplemented by the brand website lillyandsid.co.in
	Launched 100% organic kids wear brand Turtledove London in India

(Source: Company, HDFC sec)

Outsourcing – The Key to Streamline Fashion Manufacturing

The ready to wear apparel industry is the quintessential example of a buyer-driven commodity chain marked by power asymmetries (irregularities) between the suppliers and global buyers of final apparel products. Global buyers determine what is to be produced, where, by whom, and at what price. In most cases, these lead firms outsource manufacturing to a global network of contract manufacturers in developing countries that offer the most competitive rates. Lead firms include retailers and brand owners and are typically headquartered in the leading markets — Europe, Japan, and the United States. These firms tend to perform the most valuable activities in the apparel value chain—design, branding, and marketing of products— and in most cases, they outsource the manufacturing process to a global network of suppliers.

These retailers/brand owners face several challenges in locating and contacting the factories that fit the brand's needs and demands. The entire process of hunting for the right source is arduous, time-consuming, and expensive. Any blunders in an exceptionally time-sensitive garment procurement process can give rise to production & shipping delays. This can result in additional costs and, ultimately, losses for both manufacturers and purchasers. It is a sad reality that in the hastily progressing world of fabrics and garments, keeping up with the competition is a challenging task.

Retailers/brand owners usually need to visit prospective factories across the globe and undergo numerous steps of the sourcing process before a trustworthy provider is found. The hunt for the perfect material provider is a day-to-day challenge faced by sourcing managers – not all factories match each other. It is also hard to compare capacities and demands across the globe. Therefore, an outsourcing platform for fashion manufacturers has become the need of the era. Intermediaries like PDSL offer sourcing platforms which are unique technological innovations that bring manufacturers and brands closer together.

Thus, outsourcing is the future. It holds the potential to reduce lead sourcing times, surge production flexibility, reduce unreliable suppliers, simplify communications, deliver sophisticated products, and build proficient inventories.

PDSL has mastered the outsourcing model over past 2 decades

PDSL offers total supply chain solutions to its customers which include value retailers as well as high-end fashion brand retailers around the world including Europe. Its multi-stream business model enables the company to offer multi-country, multi-gender and multi-product options to its global customers. PDSL meets the needs of international businesses by providing competitive new designs, pricing, quality, and reliable delivery.

By leveraging its global networks, market knowledge, and advanced technology and information systems, the company has the capacity and flexibility to respond rapidly to evolving consumer trends. These capabilities make PDSL a preferred vendor for garment retailers around the world.

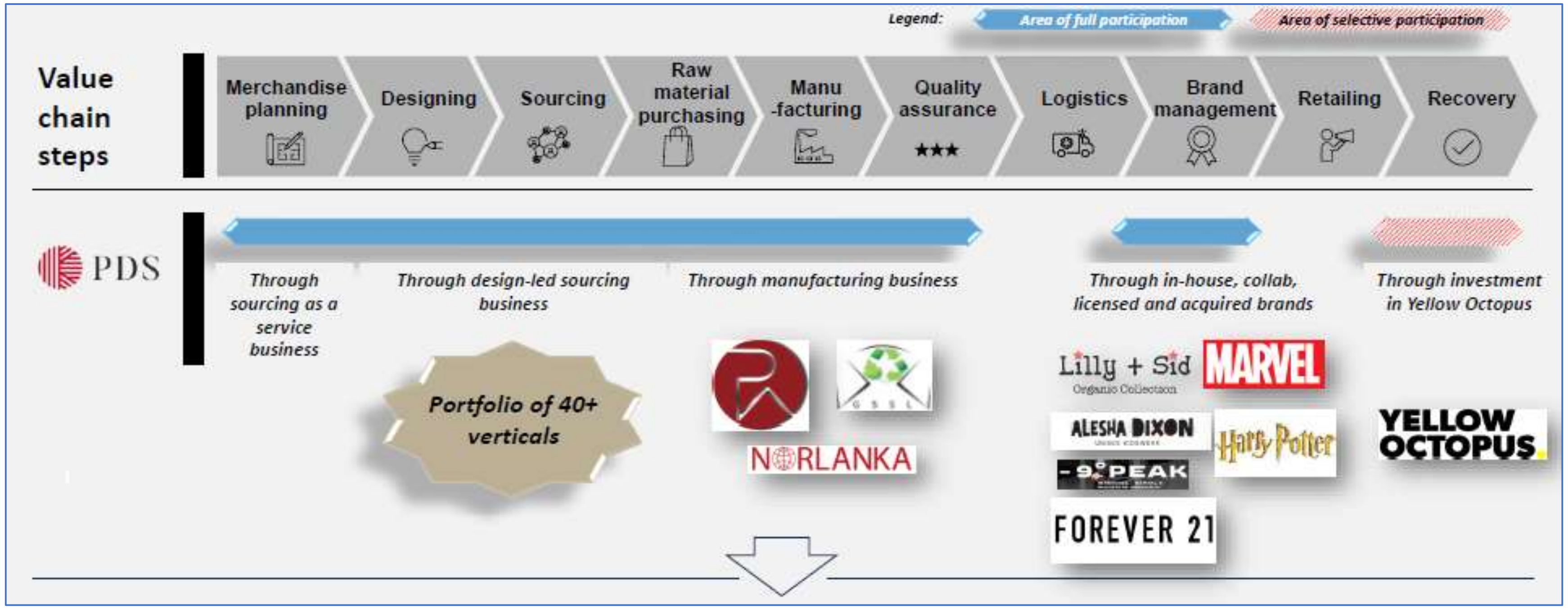
The company's services cover the entire supply chain through three distinct yet interconnected Business Networks: design & product development, trading, marketing and distribution and sourcing of garments.

PDSL's marketing and merchandizing teams interacts with customers at their locations, which help it to understand customers' specific requirements. It caters to customers' needs of competitive pricing, quality, on-time delivery and compliance with global labour practices. PDSL leverages the competitive advantages of each location to optimize value for its customers, while maximizing its own gross margins.

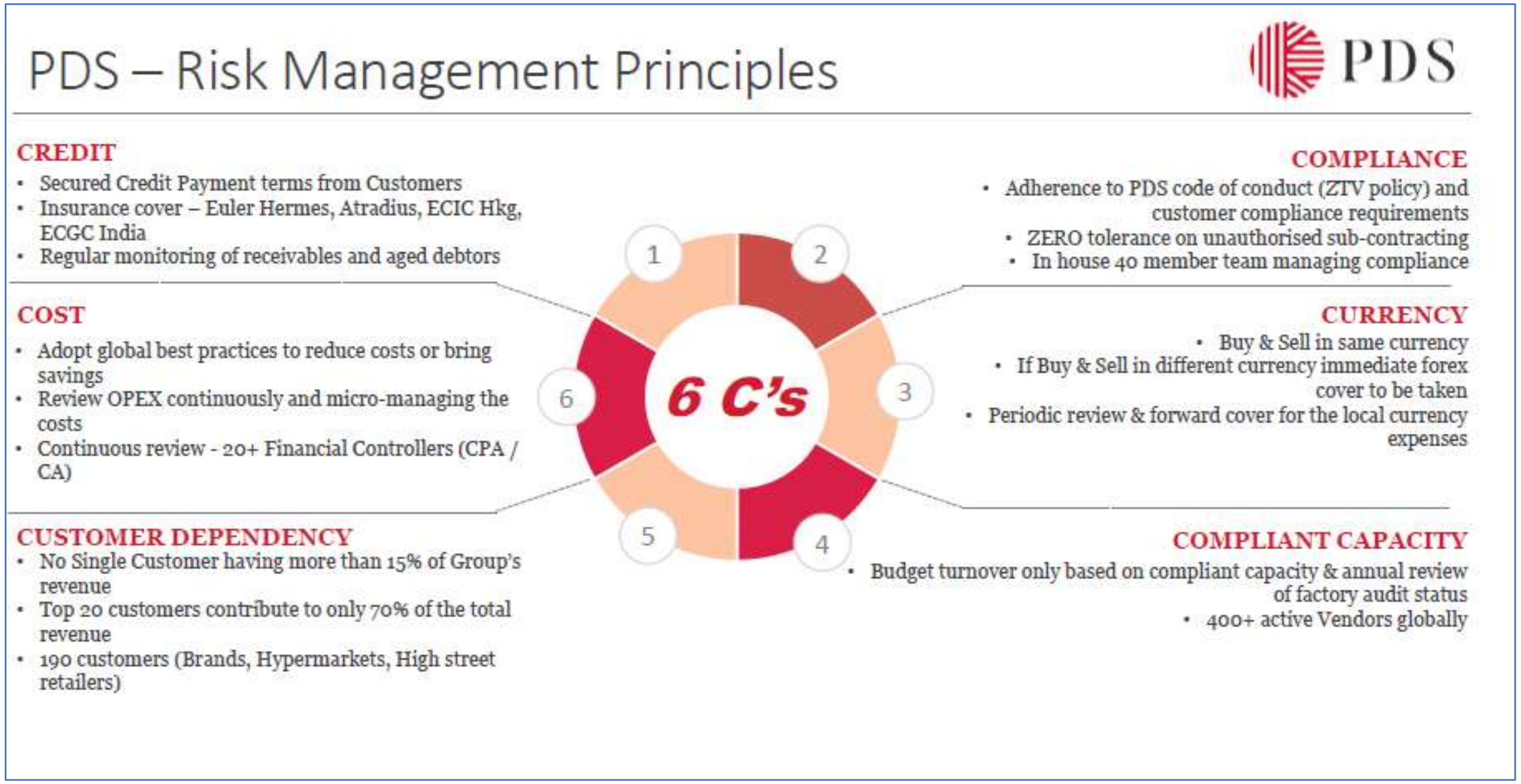
PDSL has developed strong relationships with over 600 third-party manufacturing units in Sri Lanka, Bangladesh, India, China and Turkey. It seeks to source garments efficiently and cost effectively for its customers by matching a product order from the customer with most competitive third-party manufacturing unit. The sourcing offices employ about ~3300 personnel, including people who manage businesses with these units. PDSL manages the quality of goods manufactured by them, timely shipment of inventory, local and international logistics and export documentation on behalf of its customers.

We believe that PDSL's integrated global business model positions it to take advantage of synergies in product design, development, marketing, distribution and sourcing of ready-to-wear apparel products. Most importantly it runs a super-efficient and low-risk model from an inventory, currency and credit risk perspective. PDSL is distinctly positioned with all the key ingredients required to fill the gap that may exist in a value chain.

PDS as a 'strategic vendor' is uniquely positioned in the fashion apparel value chain. PDSL is known for its one-stop shop, design capability and ESG transparency



PDSL has a robust risk management mechanism



(Source: Company, HDFC sec)

Geographical expansion of both retailer and manufacturer network

Almost all of PDSL's sales have been to customers located in UK, Europe and US. In order to de-risk its model and propel its growth, PDSL is expanding to newer markets. It is deepening its presence in the US, which is one of the top five apparel. According to the management, contribution from North American sales is likely to cross 20% (~16% in FY22) in near term. To service the US markets, PDSL is evaluating sourcing locations in Central and South America, aiming at achieving shorter design to market lead times.

Apart from the US, the company is also focusing on Australia and New Zealand, and entering Scandinavia as a prospective market.

On sourcing front, PDSL at present is predominantly concentrated in Bangladesh. It is evaluating and increasing its presence in Vietnam.

Further, it is strengthening its capabilities in Turkey and surrounding regions including Jordan and Egypt

Expanding Design-led Sourcing to Sourcing as a Service
In FY22, PDSL bolstered its service offering under the Sourcing as a Service customized solution.

Brands and retailers are increasingly focusing on their core business to drive earnings and are opting to outsource, to meet their sourcing needs. In order to capture this opportunity, PDS has started to offer Sourcing as a Service to large brands and retailers, who are exploring outsourcing options exclusive to pre-agreed territories.

In FY22, PDSL's Germany-based subsidiary Techno Design signed an exclusive agreement with a leading German brand, s.Oliver. As part of this arrangement, Techno Design will have exclusive sourcing rights from India and Sri Lanka for the s.Oliver group. Under this arrangement PDSL also acquired their Indian operations.

Further, PDSL entered into an arrangement with Hanes Brand (USA) which enables it to operate as their sole and exclusive vendor for Bangladesh. The agreement further allows the company to source merchandise from a factory network in Egypt, and India, on a non-exclusive basis. PDS has created an exclusive team along with an independent office infrastructure in Bangladesh, to provide services under this agreement. According to the management, this partnership has potential to translate into an annual potential of USD 400 million merchandise value scale-up opportunity over the next four to five years.

Recently, it entered into an arrangement with Wibra. Wibra is a Dutch discount store chain selling mostly textiles and clothing for children, men, and women, intimate wear, home furnishing textiles, and other household goods. It operates over 280 stores in the Netherlands and Belgium. According to agreement, Kleider Sourcing, PDS's subsidiary, is the now sole agent for apparel, home textile, and hard goods in Bangladesh for Wibra.

Post the initial success of partnership with Hanes Brands and s.Oliver, PDSL is initiating arrangements with other leading retailers and brands, providing them similar and customised solutions. The partnerships will be both exclusive and non-exclusive, and diverse in terms of geographies and brand associations**. These arrangements have the potential to churn USD 1 billion worth annual merchandise value in next 4-5 years.**

(Source: Company, HDFC sec)

Sky is the limit for growth

Having already established its presence in garments industry, PDSL plans to implement its learnings by expanding in other categories including home fashion, accessories and footwear. Each of these categories offer multi-billion dollar opportunity, not to mention the scale up potential of garments alone. PDSL is a unique player and among the very few across the globe that could capitalise on the outsourcing trend. Further, it runs a super-efficient and low-risk model from an inventory, currency and credit risk perspective.

In Q2FY23, PDSL acquired DBS Lifestyle, a design-led company catering to fashion and home categories. DBS owns over 20,000 original textile designs and patterns and adds nearly 2500 artworks. DBS caters to the needs of 200+ Fashion & 150+ Home clients globally across 15 countries on three continents.

Manufacturing division getting on profitable path

PDSL, in FY18, forayed into its own manufacturing division by establishing two factories in Bangladesh. Later, it set up a unit in Sri Lanka. These facilities have expertise in formal tailoring, blazers, school wear, shirts, softs and kids wear. In-house manufacturing adds incremental value at each step of the product development cycle and helps address specific requirements of the customer. High quality control, in-depth knowledge of the end-to-end process and better operational efficiency enables quicker responses to customer feedback and product layout changes.

In FY22, revenues from manufacturing division nearly doubled to Rs 547 Cr from Rs 285 Cr in FY21. PAT loss narrowed by 80% YoY. In Q4FY22, the business turned PAT positive. This was the result of better collaboration with its sourcing verticals, favourable product mix and operating leverage. The company is focussing on increasing efficiencies, driving bulk orders, and disciplined execution. The company's plants are running at 100% capacity utilisation levels, however, there's a lot of scope to improve efficiencies (~60% currently) by improving turnaround time and better cost management. If used optimally, it can generate EBITDA of 6-8%. No more lines or factories to be added here.

How one reconciles dichotomy between an asset light platform company, and also having manufacturing plants? The key reason for setting up own manufacturing facilities is the reluctance of some of the large retailers (Gap, Levi's, H&M, etc.) to work with sourcing companies who don't have their own factories. Additionally, having a well-established facilities in Bangladesh gives PDSL an edge given stringent compliance policies that Bangladesh based manufactures are subjected to and with Bangladesh being the lowest cost operators in the world.

PDS's manufacturing facilities

Particulars	Progress Apparel, Bangladesh	Green Smart Shirts, Bangladesh	Nor Lanka, Sri Lanka	Parc Designs, India
Total capacity	2,500 machines	2,000 machines	320 machines	1,000 machines
Compliance	Accord Compliance	All local guidelines	All local guidelines	All local guidelines
Focused manufacturing/ Speciality	Primarily focused on bottom wear	Formal and casual shirts/blouses for ladies, men and kids	Specialises in knit, kids wear	Specialises in Ladies Softs and girls-wear
Major customers	Next, C&A and Express	Next, Primark and Bestseller	ASDA George, Next, Primark	Bestseller and Matalan
Ownership pattern	Subsidiary	Subsidiary	Based on job-work arrangement	Held through minority stake

(Source: Company, HDFC sec)

Scaling up of in-house brands is margin accretive

Leveraging its design-to-market capabilities, PDSL has curated a portfolio of in-house brands. These also include brands that are conceptualised in collaboration with retailers and influencers.

The successful launch of in-house brands such as Adapt and Wiseprotec makes us confident about the development of more such in-house brands. In late FY20, it had acquired brands such as UK based Lilly & Sid and Turtledove London which is focussed on kids' wear, and has been showing good traction. Expanding of own brands and licensing portfolio will drive the margin expansion.

(Source: Company, HDFC sec)

PDSL has always focused on building a strong team on entrepreneurs; it has recently hired senior professionals across business verticals

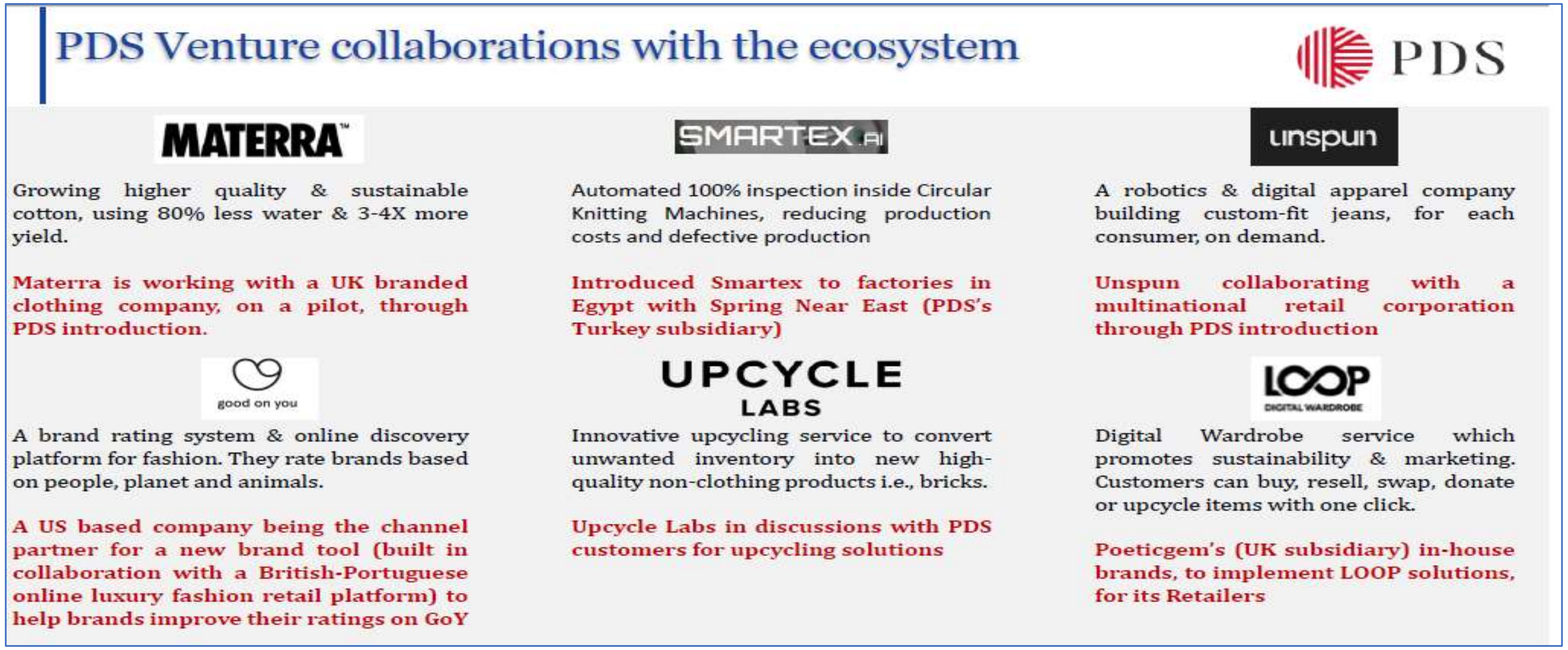
(Source: Company, HDFC sec)

PDS Venture Tech Investments

PDS invests in ventures that focus on creating a sustainable value chain for the fashion industry, reducing wastage or sustainable usage of raw materials, and using advanced analytical tools to improve revenues and profitability. It prefers funding ventures in the seed stage, which have less than US$1 million in revenue or pre-series/early stage ventures, where revenues range between US$1-5 million. The company pursues investment opportunities that strengthen its focus areas:

Technology: Fashion Tech, Consumer Tech & Other Tech
Consumer Brands: B2B, D2C
Sustainability: Materials, Circular Economy, Sustainable Communities

Some of the PDSL's impact investments



(Source: Company, HDFC sec)

While these investments may/may not generate substantial capital gains, they enhance the company's value proposition for customers and vendors. Further, this enables to nurture collaborations and synergies with the PDS ecosystem. PDSL has also partnered with leading funds for co-investing in select opportunities

As of 30th September, 2022, PDSL has invested around a cumulative sum of USD 19 mn (~ Rs 155 Cr) across start-ups. It plans to invest ~USD 5 mn p.a. in FY23 and FY24. Post that, the company won't invest fresh funds, and investments, if any, will be done from the gains generated from the current portfolio.

Financial Triggers

The PDS platform is focused on expanding it service offering and global footprint. Over past few quarter, the company has added new business verticals focused on catering to new customers, new categories and new geographies which augments the PDS platform. The investment in these areas lays down a strong foundation that will help the company not only to expand the ticket size of its existing relationships, but also bring new customers into the fold. These new verticals are driven by leading industry professionals with strong domain expertise and customer relationships who have joined the PDS platform. While PDS's investment towards these new verticals is currently being captured in operating costs, these new verticals will generate value as they mature and grow within the PDS ecosystem. PDS is also exploring avenues to strengthen its capabilities in geographies like Egypt, Jordan, Central and South America and Turkey to name a few.

Additionally, the value of China's apparel exports is 5X that of Bangladesh's. With a 'China+1' theme, we expect sourcing to move from China to other countries. This can immensely benefit PDS as it has access to manufacturers across multiple countries. This could result in steady market share gains for PDSL.

PDSL's sourcing division has grown at 32% CAGR over FY18-22. Going ahead, on the back of factors discussed above, we expect the company to grow at 21% CAGR over FY22-24E.

The manufacturing segment which started contributing in FY17 reported revenues of Rs 547 Cr (6% of the sales) in FY22. Going ahead, we expect it to grow at 13% CAGR over FY22-24E.

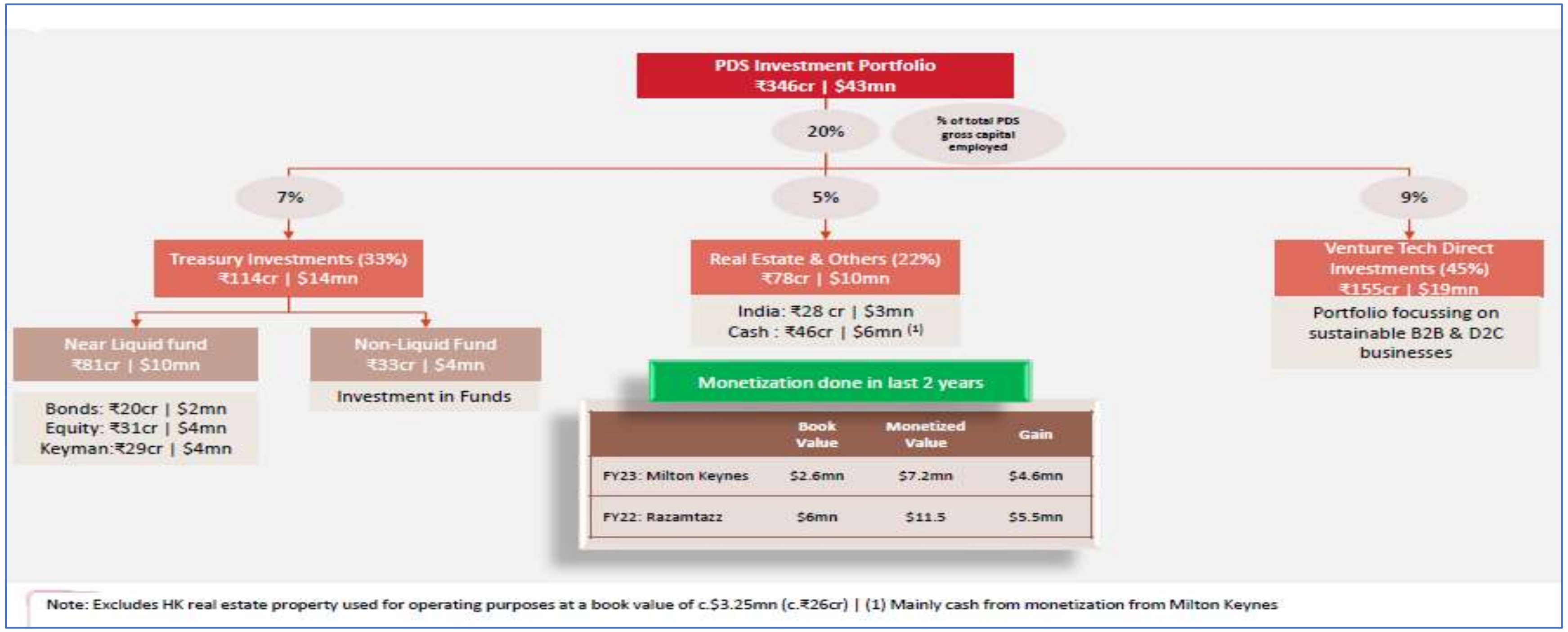
Thus, on consolidated basis we expect the company to clock a revenue CAGR of ~21% over FY22-24E. While management of PDS has set a conservative target of doubling the revenues over next 5 years, we believe the company is poised well to achieve the target ahead of time.

On the margin front, our conservative estimates suggest consolidated EBITDA margins to improve by 30 bps over FY22-24E on the back of turnaround in manufacturing segment and increasing contribution from Sourcing as a Service vertical.

PDS enjoys lower tax rate with its larger subsidiaries located in low tax zones. We build-in a tax rate of 8% (avg. of last 5 years) but expect the tax rate of 15% in line with prevailing global minimum tax rate from FY25.

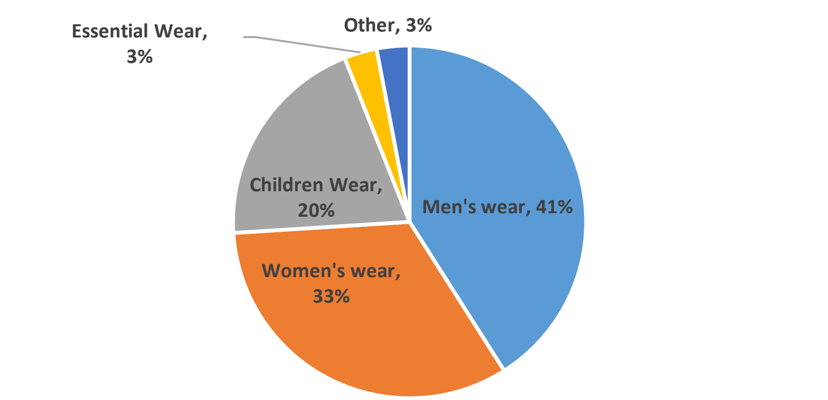
PDS has limited working capital given majority of its revenues come from its sourcing business where it holds limited inventory and nearly offsets its debtor and creditor days. Inventory could increase going forward as manufacturing business scales-up. Given the limited capex requirement (being asset-light and no further expansion on manufacturing front), majority of the CFO is expected to translate into FCF.

Sound capital allocation policy

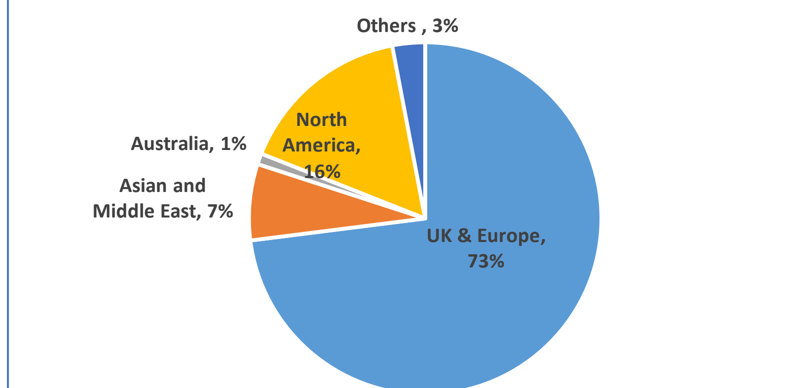


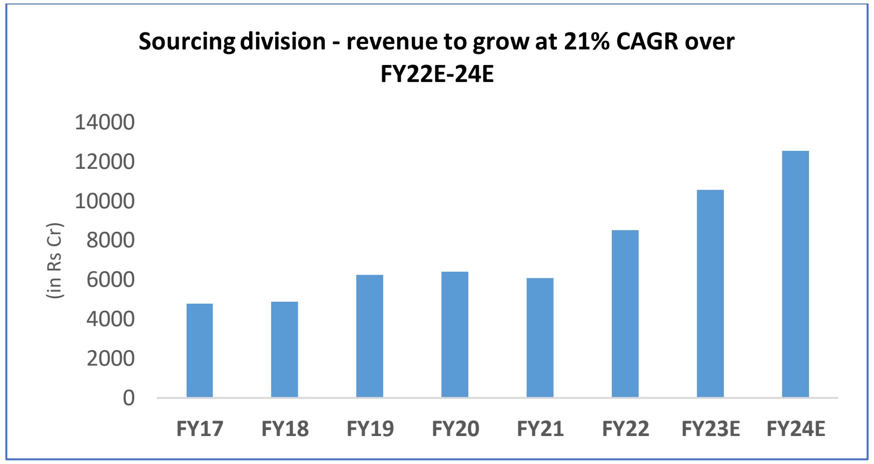
(Source: Company, HDFC sec)

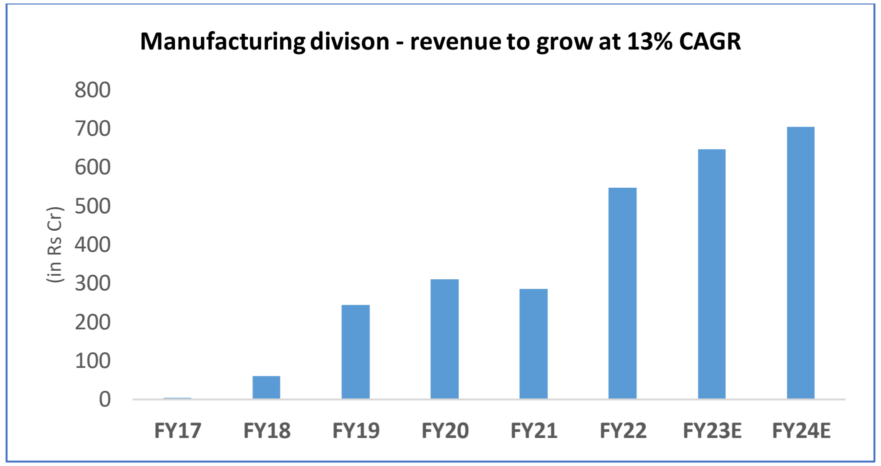
Category-wise revenue split - H1FY23

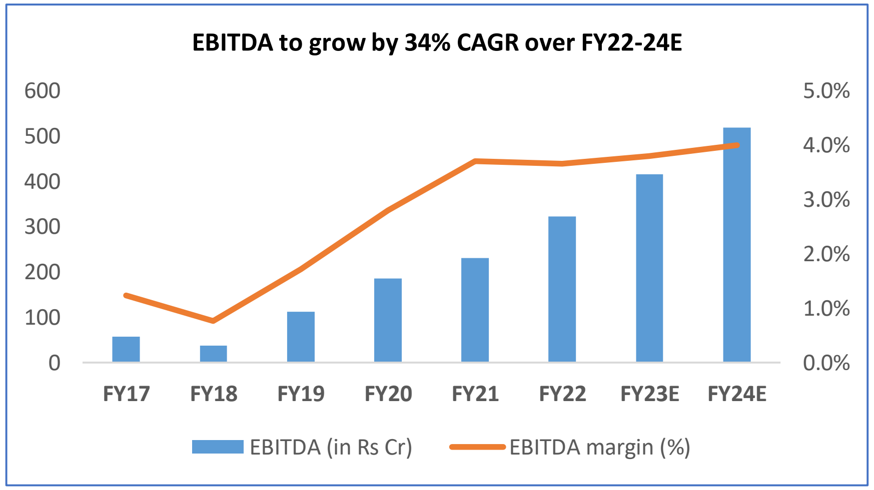


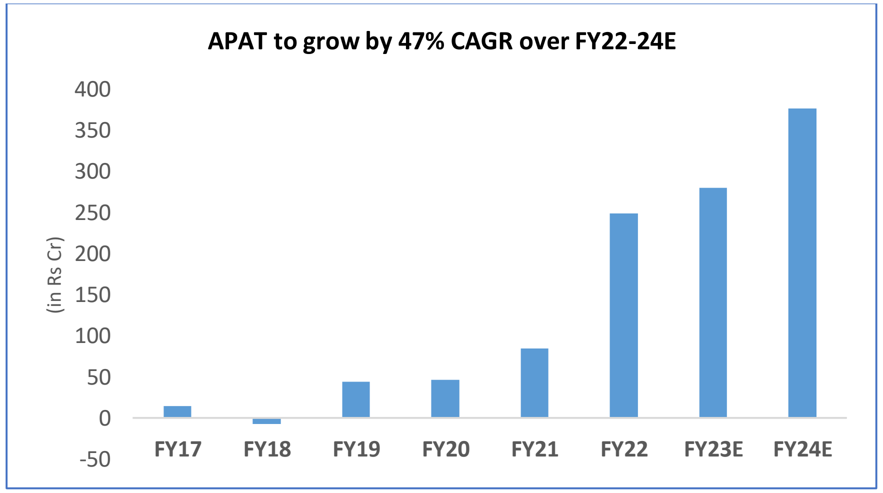
Geography-wise revenue split - H1FY23

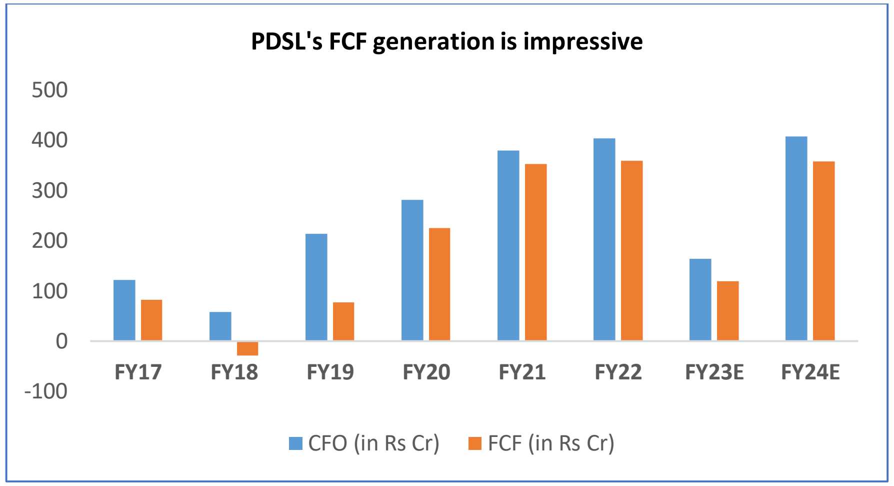


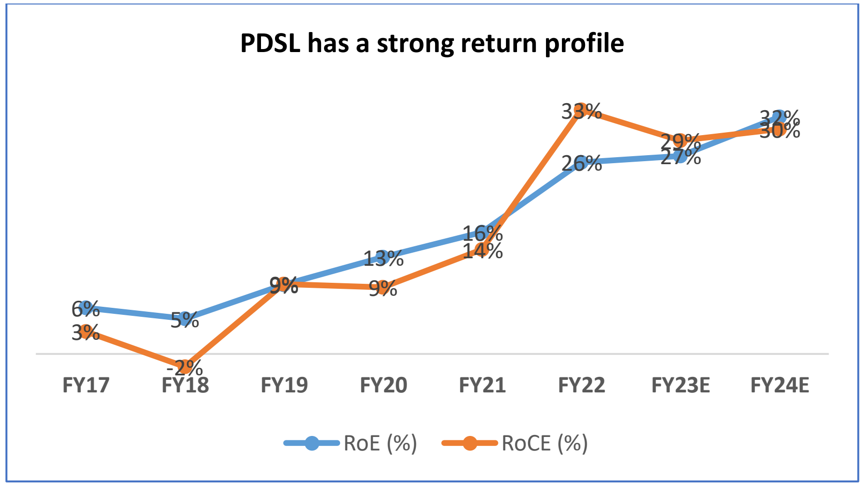

Sourcing division - revenue to grow at 21% CAGR over FY22E-24E
14000
12000
10000
8000
6000
4000
2000
0
(in Rs Cr)
FY17
FY18
FY19
FY20
FY21
FY22
FY23E
FY24E


Manufacturing divison - revenue to grow at 13% CAGR
800
700
600
500
400
300
200
100
0
(in Rs Cr)
FY17
FY18
FY19
FY20
FY21
FY22
FY23E
FY24E


EBITDA to grow by 34% CAGR over FY22-24E
600
500
400
300
200
100
0
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
FY17
FY18
FY19
FY20
FY21
FY22
FY23E
FY24E
EBITDA (in Rs Cr)
EBITDA margin (%)


APAT to grow by 47% CAGR over FY22-24E
400
350
300
250
200
150
100
50
0
-50
(in Rs Cr)
FY17
FY18
FY19
FY20
FY21
FY22
FY23E
FY24E





(Source: Company, HDFC sec)

Key risks

Significant portion of revenues comes from a limited number of buyers

TESCO, ASDA Wal-Mart, Matalan, Primark, Sainsbury, DUNNES, MAX, Zara, Next, River Island and Arcadia are among its largest customers and accounted for a significant portion of revenues. Since PDS does not have long-term sales contracts with customers and is not an exclusive supplier to its large customers, its revenues from major customers may vary from year to year and from quarter to quarter. As PDS sells most of its debtor dues through factoring, the risk of bad debts or delayed payments is mitigated.

Company relies on its Subsidiaries to generate earnings

Currently, the Company has limited supply and distribution operations and conducts a significant portion of its operations through its direct or indirect Subsidiaries. A substantial portion of the Company's assets are held by, and a substantial part of its earnings and cash flows are attributable to, its Subsidiaries. If earnings from the Subsidiaries were to decline.

High dependence on customers located in U.K and Europe

In last few years, almost all of the company's sales have been to customers located in UK, Europe and US. Europe and UK account for 73% of its sales in FY23. The apparel industry is highly dependent upon the overall level of consumer spending. If the current economic condition in the above countries does not improve substantially or if there is any substantial reduction in the levels of discretionary spending, the company's customers may significantly reduce or postpone their imports. However the fact that PDS focuses on mass retailers insulates them from a slowdown to an extent.

Business is dependent on third-party manufacturing units

Company sources source products from approximately 600 factories operated by third-parties located in Bangladesh (60% of total), China, Sri Lanka, Turkey and India, who may also supply apparel to the company's competitors. These manufacturing units are subject to operating risks which could affect PDSL's profitability. Further, PDSL and its customers may be subject to liability and negative publicity if third-party manufacturers violate labour laws or engage in unethical practices.

Any sharp volatility in raw materials or freight rates like that seen recently could impact the equation between the manufacturer and the retailer and PDS may have to pitch in to share a part of the higher costs.

Forex fluctuations is a theoretical risk for PDS; however as its deals its finances out of Hong Kong in USD, a large portion of this risk is mitigated.

PDS earns low operating margins in the range of 3.5-5%. However given the low capital requirements its return ratios are very healthy. Also in bad years, margins have not fallen sharply.

PDS has over the last few years added 18 new verticals that are yet to turn profitable (having been in existence for less than 30 months). If these new ventures take longer to break even or PDS keeps adding them at a fast pace, then it may affect the growth in profitability.

About the company:

PDS Limited (PDSL) is a global fashion infrastructure company offering product development, sourcing, manufacturing, and distribution for major brands and retailers worldwide. The company operates a vast global network covering over 50 offices, 22 countries, and over 3,300 associates, and 6,500 factory associates worldwide.

Financials

Income Statement

Particulars (in Rs Cr)	FY19	FY20	FY21	FY22	FY23E	FY24E
Net Revenues	**6486**	**6648**	**6213**	**8828**	**10936**	**12951**
Growth (%)	***31.7***	***2.5***	***-6.5***	***42.1***	***23.9***	***18.4***
Operating Expenses	6374	6462	5983	8506	10521	12433
EBITDA	**112**	**186**	**230**	**323**	**416**	**518**
Growth (%)	***195.3***	***66.6***	***23.6***	***40.3***	***28.8***	***24.7***
EBITDA Margin (%)	***1.7***	***2.8***	***3.7***	***3.7***	***3.8***	***4.0***
Depreciation	26	52	68	70	77	80
Other Income	16	27	37	86	55	52
EBIT	**101**	**160**	**200**	**339**	**394**	**489**
Interest expenses	32	49	26	28	35	24
PBT	**69**	**97**	**174**	**311**	**359**	**465**
Tax	0	9	22	17	30	38
PAT	**69**	**88**	**152**	**293**	**329**	**427**
Share of Asso./Minority Int.	-25	-42	-68	-45	-48	-54
Adj. PAT	**44**	**46**	**84**	**248**	**281**	**373**
Growth (%)	***-660.5***	***4.9***	***83.2***	***194.6***	***12.9***	***32.9***
EPS	3.4	3.5	6.5	19.1	21.5	28.6

Balance Sheet

Particulars (in Rs Cr) - As at March	FY19	FY20	FY21	FY22	FY23E	FY24E
SOURCE OF FUNDS						
Share Capital	26	26	26	26	26	26
Reserves	442	533	621	846	1062	1357
Shareholders' Funds	**468**	**559**	**647**	**872**	**1088**	**1383**
Minority Interest	31	52	69	64	112	166
Total Debt	700	747	490	623	378	233
Net Deferred Taxes	0	1	1	3	3	3
Total Sources of Funds	**1199**	**1359**	**1207**	**1562**	**1581**	**1784**
APPLICATION OF FUNDS						
Net Block & Goodwill	256	383	364	419	387	357
CWIP	14	21	5	3	3	3
Investments	178	185	254	364	464	584
Other Non-Curr. Assets	11	6	29	39	33	52
Total Non Current Assets	**460**	**594**	**651**	**825**	**887**	**996**
Inventories	136	183	197	305	390	461
Debtors	1029	832	910	1421	1648	1952
Cash & Equivalents	370	502	431	665	339	328
Other Current Assets	176	267	157	182	314	322
Total Current Assets	**1711**	**1785**	**1695**	**2573**	**2690**	**3062**
Creditors	748	579	892	1566	1498	1774
Other Current Liab & Provisions	225	442	247	270	498	500
Total Current Liabilities	**973**	**1021**	**1139**	**1836**	**1996**	**2274**
Net Current Assets	738	764	555	737	693	788
Total Application of Funds	**1198**	**1359**	**1207**	**1562**	**1581**	**1784**

PDS Ltd.

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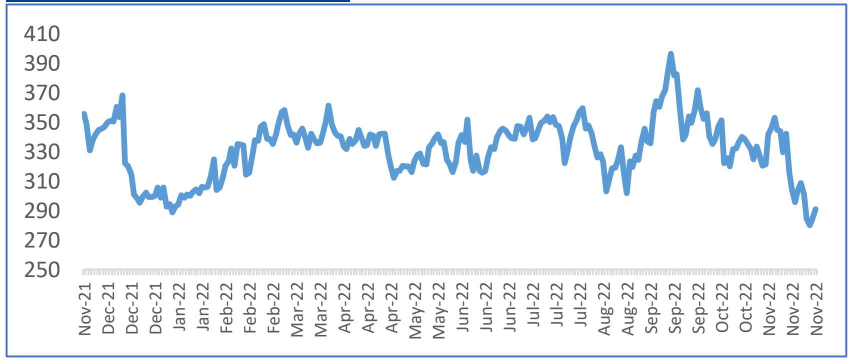
Cash Flow Statement

Particulars (in Rs Cr)	FY19	FY20	FY21	FY22	FY23E	FY24E
Reported PBT	69	91	170	310	359	465
Non-operating & EO items	2	20	11	-7	17	-2
Interest Expenses	30	46	24	27	35	24
Depreciation	26	52	68	70	77	80
Working Capital Change	101	81	120	27	-293	-122
Tax Paid	-15	-10	-13	-24	-30	-38
OPERATING CASH FLOW (a)	**213**	**281**	**379**	**403**	**164**	**407**
Capex	-137	-56	-27	-44	-45	-50
Free Cash Flow	77	225	353	358	119	357
Investments	19	-17	-74	-79	-100	-120
Non-operating income	-83	18	13	-97	0	0
INVESTING CASH FLOW (b)	**-200**	**-55**	**-88**	**-221**	**-145**	**-170**
Debt Issuance / (Repaid)	147	-34	-252	127	-245	-145
Interest Expenses	-32	-56	-26	-27	-35	-24
FCFE	129	136	13	282	-261	67
Dividend	0	-18	-47	-96	-65	-78
Others	0	-21	-21	-26	0	0
FINANCING CASH FLOW (c)	**115**	**-128**	**-347**	**-22**	**-345**	**-248**
NET CASH FLOW (a+b+c)	**129**	**97**	**-55**	**160**	**-326**	**-11**

One-year share price data



(Source: Company, HDFC sec)

Key Ratios

Particulars	FY19	FY20	FY21	FY22	FY23E	FY24E
Profitability Ratios (%)						
EBITDA Margin	1.7	2.8	3.7	3.7	3.8	4.0
EBIT Margin	1.6	2.4	3.2	3.8	3.6	3.8
APAT Margin	0.7	0.7	1.4	2.8	2.6	2.9
RoE	9.4	9.0	14.0	32.7	28.6	30.2
RoCE	9.3	13.0	16.3	25.7	26.6	31.8
Solvency Ratio (x)						
Net Debt/EBITDA	3.0	1.3	0.3	-0.1	0.1	-0.2
Net D/E	0.7	0.4	0.1	0.0	0.0	-0.1
Per Share Data (Rs)						
EPS	3.4	3.5	6.5	19.1	21.5	28.6
CEPS	5.4	7.5	11.7	24.4	27.4	34.8
BV	35.9	42.9	49.7	67.0	83.6	106.2
Dividend	0.0	0.0	3.2	4.8	5.0	6.0
Turnover Ratios (days)						
Debtor days	51	51	51	48	51	51
Inventory days	6	9	11	10	12	12
Creditors days	35	36	43	51	51	46
Valuation						
P/E	103.5	98.7	53.8	18.3	16.2	12.2
P/BV	9.7	8.1	7.0	5.2	4.2	3.3
EV/EBITDA	43.5	25.6	19.8	13.8	10.7	8.1
EV / Revenues	0.7	0.7	0.7	0.5	0.4	0.3
Dividend Yield (%)	0.0	0.0	0.9	1.4	1.4	1.7
Dividend Payout (%)	0.0	0.0	48.7	25.0	23.2	21.0

(Source: Company, HDFC sec)

HARSH RAJENDRA SHETH

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RETAILRESEARCH

HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

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