Stock Note

Indo Count Industries Ltd.

August 22, 2023

RETAILRESEARCH

Indo Count Industries Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Textiles	Rs. 242.4	Buy in Rs. 238-245 band and add more on dips in Rs. 206-211 band	Rs. 266	Rs. 292	2-3 quarters

HDFC Scrip Code	INDCOUEQNR
BSE Code	521016
NSE Code	ICIL
Bloomberg	ICNT IN
CMP (Aug 21, 2023)	242.4
Equity Capital (RsCr)	39.6
Face Value (Rs)	2
Equity Share O/S (Cr)	19.8
Market Cap (RsCr)	4785
Book Value (Rs)	91
Avg. 52 Wk Volumes (in '000s)	505
52 Week High	249
52 Week Low	101

Share holding Pattern % (June, 2023)	
Promoters	58.74
Institutions	9.16
Non Institutions	32.10
Total	100.0

* Refer at the end for explanation on Risk Ratings

Fundamental Research Analyst
Harsh Sheth
Harsh.Sheth@hdfcsec.com

Our Take:

With a presence of more than three decades, Indo Count Industries Ltd. (ICIL) is a largest manufacturer and exporter of bed sheets, bed linen, and quilts from India. It is recognized among the top three global bed sheet suppliers in the US. The product basket of the company includes sheet sets, fashion bedding, utility bedding and institutional bedding. Indo Count is 4 star export house and has state of art manufacturing facilities at Kolhapur, Maharashtra. With the successful acquisition of Home Textile Business of GHCL at Bhilad, the company has now manufacturing presence in twin states geographies viz. Gujarat and Maharashtra. Starting with a capacity of 36 million meters, ICIL has enhanced its capacity to 153 million meters. The company has three divisions namely Spinning, Home Textiles and Retail.

In a bid to de-risk their supply chain/concentration from China, global manufacturers have started shifting manufacturing operations from China (initiative known as 'China +1') to alternate sourcing destinations. India stands out as a suitable '+ 1' destination due to India's competency across factor cost and a well-established textile ecosystem (across cotton segment). Further, effective implementation of UK FTA could provide a clear runway for double digit revenue CAGR in case of Indian textile exporters over the coming decade. Indian textile goods attract on an average 9% import duty in the U.K. The FTA will ensure duty free exports.

Inventories at big box retailers and fashion brands are ebbing, and companies believe this could accentuate export demand and contribute to better revenues by H2FY24. Home textile manufacturers including ICIL are already seeing demand normalizing for essentials. In addition to cotton prices, crude prices and freight costs too have begun to soften, benefits of which will be visible on margins in the coming quarters. Considering multiple tailwinds, ICIL expects 15- 20% CAGR volume growth and 200-300 bps margin improvement over the next 3-4 years.

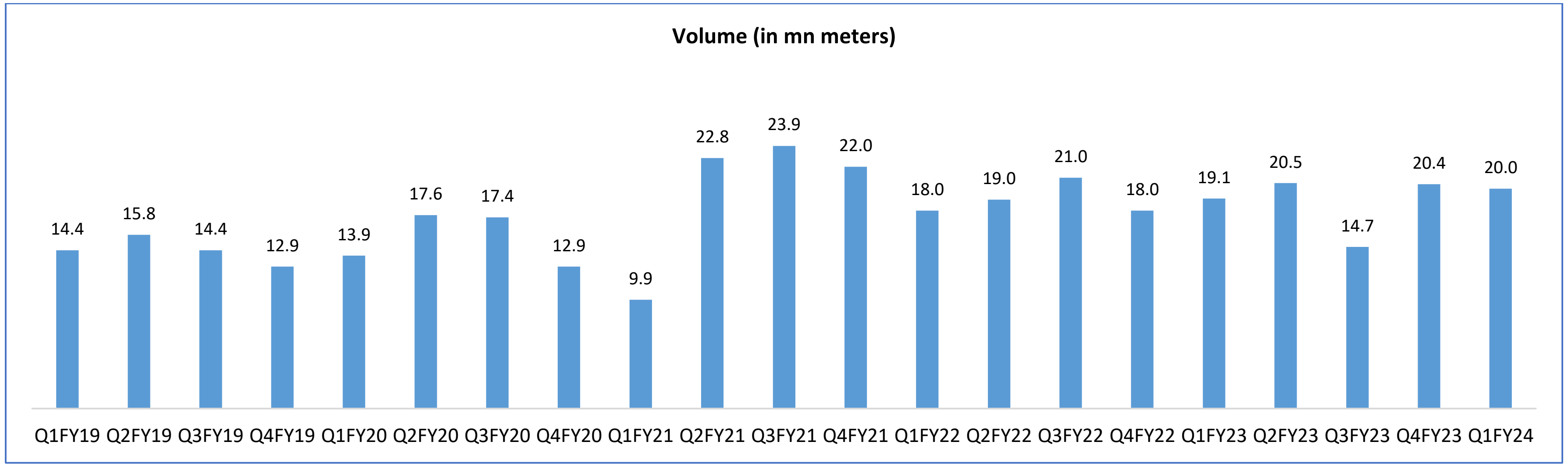
Valuation & Recommendation:

In FY23, Home Textile industry faced multiple headwinds, such as the demand slowdown in international markets due to high inflation, supply chain disruptions due to logistics, which affected inventory levels and a record high commodity cost. Having endured these headwinds, the sector is seeing signs of revival with lower cotton prices and freight costs, and reduction in inventory at retailer with gradual pick up demand. The management has guided for 14-20% volume growth in FY24. Going ahead, we expect ICIL to report 14%/19%/22% in revenue/EBITDA/PAT over FY23-25E driven by i) pickup in demand in US markets, and ICIL's strong relationship with marquee clients such as Walmart, Target, Bed, Bath & Beyond etc, ii) India capturing China's share (China plus one), iii) increasing contribution from high-margin Fashion, Utility and Institutional bedding segment.

We think the base case fair value of the stock is Rs 266 (12.5x FY25E EPS) and the bull case fair value is Rs 292 (14x FY25E EPS). Investors can buy the in stock Rs 238-245 band (11.5x FY25E EPS) and add more on dips in Rs 215-221 band (10.5x FY25E EPS).

Financial Summary

Particulars (in Rs Cr)	Q1FY24	Q1FY23	YoY-%	Q4FY23	QoQ-%	FY21	FY22	FY23	FY24E	FY25E
Operating Income	741	703	5%	807	-8%	2,519	2,842	3,012	3,389	3,902
EBITDA	125	122	2%	144	-13%	377	434	454	549	644
APAT	74	77	-5%	95	-22%	251	359	277	337	409
Diluted EPS (Rs)	3.7	3.9	-5%	4.8	-22%	12.7	18.2	14.0	17.0	20.7
RoE-%						22.1	24.9	16.4	17.4	18.2
P/E (x)						19	13	17	14	12
EV/EBITDA						14	13	12	10	8



(Source: Company, HDFC sec)

Q1FY24 Highlights:

ICIL has been experiencing improvement in demand due to normalized inventory levels at the retailers end hence, there is an uptick in the order booking. Sales Volume for Q1FY24 stood at 20.03 mn. mtrs. V/s 19.10 mn. mtrs. in Q1FY23. The management is optimistic that the growth phase should return in subsequent quarters and it anticipates double-digit sequential growth in volumes.

Gross margin expanded by 413 bps sequentially to 59.6% due to correction in cotton prices and freight rates and better supply-chain efficiencies. However, on YoY basis it contracted by 246 bps. EBITDA stood at Rs 125 cr, with an EBITDA margin contraction of 49 bps YoY to 16.9% on lower gross margin and higher operating overheads.

Key Triggers:

Broad basket of In-house brands

Historically, ICIL's focus revolved around bed sheets and the segment contributed >90% of its overall business during the same period. In 2017, the company moved up the value chain by foraying into new bedding segments, which includes Fashion bedding (Decorative bedding), Institutional linens (catering to high-end hotels, resorts and cruises), and Utility bedding (basic white bedding). With this initiative, ICIL expanded its addressable market by 3x.

Company has created 17 brands - each brand possesses distinct attributes, is offered exclusively in particular geographies, caters to specific user segments and is available at multiple price points. In recent past, the company has completed two licensed brand tie-ups (Jasper Conran and Gaiam) and is planning to add more such brands to its portfolio in future.

ICIL's brand portfolio

(Source: Company, HDFC sec)

ICIL's offerings

(Source: Company, HDFC sec)

Increasing share of value added products to drive margin expansion -
Management is focused on increasing the contribution of the value-added segment in its topline with emphasis on promoting the fashion, utility, and the institutional bedding products. Management intends to scale the share of value-added products to 30% of revenue (~19% in FY23) in the future. For the same, the company has invested in building a manufacturing plant for its fashion utility products.

Long standing relationship with retailers in USA: USA accounts for over 70% of ICIL's revenues. ICIL has long established relationships with US retailers. Some of the retailers ICIL caters to are Walmart, Target, Bed Bath & Beyond and JC Penney. Order size in the US market has been rising, which should boost volumes, going forward.

Signing of FTA with the UK could be a major positive trigger: The company's UK distribution is omnichannel, and the company expects 6-7% volumes from the UK to M&S, ASDA, Primark, Wilkins, etc. UK buyers are looking to move out of China while the supply chain from Pakistan to the UK too is unstable. Management expects the UK FTA to conclude by the end of FY24, could benefit the company and the industry in future.

Increasing traction in domestic branded business

"Boutique Living" and "Layers" are ICIL's two key brands in domestic market. "Boutique Living" is an aspirational brand, which over the years is proving to be a game-changer for premium customers of home accessories, Layers is a value-driven brand, which has a consolidated acceptance in the Indian marketplace.

The company is banking on these two brands to get a larger pie of the promising and expanding Indian textile market. On this line, the Company is channelising itself towards B2C, B2B and D2C segments through high-quality product offerings across a variety of price points, building visibility through digital campaigns and also leveraging omnichannel and e-commerce distribution.

ICIL's domestic business generated 2.5% of its total revenue as at FY23 (~2% in FY22); however, the company expects the B2C segment to contribute 5% of its overall revenue over the next 2-3 years. Going forward, we expect these brands to develop more traction and contribute increased share to total revenue.

GHCL acquisition

ICIL acquired the home textile business of GHCL on a going concern basis. The acquisition includes the existing home textile manufacturing facility of GHCL at Bhilad, Vapi and specified assets (inventory and intellectual property) of its overseas subsidiary. The total cost of acquisition is ~ Rs 576 cr (Rs 539 cr for Indian home textile business and Rs 37 cr for GHCL's US subsidiary). GHCL primarily has products in the bedding segment and has a processing capacity of 45 million meters, cutting and sew capacity of 30 million meters and a weaving capacity of ~ 12 million metres.

The product profile of GHCL is complementary to ICIL's product profile with 65% of revenues coming from USA. GHCL also has a presence in the Europe and Australian market. ICIL would benefit from addition of new customers through GHCL acquisition. Access to Australian market is especially significant as India has recently signed an FTA with Australia.

ICIL management indicated they would target cross selling ICIL's products to the new customers acquired from GHCL. GHCL also has certain unique products which ICIL can sell to its existing customers thereby widening the product portfolio of ICIL.

Industry Scenario

Global market: The global home textile market in 2022 was valued at US$125.58 billion. The market is expected to reach US$174.14 billion by 2028. Factors such as rising income levels, expanding real estate industry, increase in consumer spending on home renovation and decoration, rapid urbanisation, growth in E-commerce, upsurge in fabric demand for lightweight products and many other factors would eventually result in the increasing demand for home textiles as textiles are an easy and often sustainable way to create change.

In-home textiles in Asia Pacific dominated the market in 2022, owing to the availability of cheap labor, raw material, products, etc. Asia Pacific is divided into four regions: China, India, Japan and the Rest of Asia Pacific. The U.S. is expected to be the largest and fastest-growing region in North America. However, in Europe, Germany holds the majority of the share of the market. Germany's home textile market is expected to grow as Germany is also the largest importer of home textiles in Europe.

Home Textiles Market

Top 10 exporting countries		Top 10 importing countries	
Country	Market Share	Country	Market Share
China	43.9%	United States	24.6%
India	8.6%	Germany	8.4%
Turkey	5.9%	United Kingdom	4.8%
Pakistan	5.4%	Japan	4.5%
Germany	4.5%	France	4.1%
Netherlands	3.6%	Netherlands	3.3%
United States	3.5%	Canada	2.9%
Belgium	2.7%	Italy	2.3%
Poland	2.1%	Spain	2.2%
France	1.5%	Australia	2.1%

(Source: Company, HDFC sec)

Indian scenario: Home textile is the most significant export contributor in the textile industry after readymade garments. India contributes almost 7% of the world's home textile trade. It is also one of the top suppliers in the world's biggest home textile- consuming market, the U.S. Further, continuous efforts in quality improvement, innovations through R&D programs, and other value- added features have allowed India's home textile products to gain more popularity in the global market. Naturally, such superior quality products make Indian companies a leader in the U.S. and the U.K., contributing almost two-thirds to their exports.

Domestic demand: Indian consumers are moving towards ready-to-use products like readymade sofas, cushion covers, curtains, bed sheets, etc., instead of customising them. A large portion of the domestic consumption in home textiles is of the bed & bath category alone. Still, most of this demand is met by unorganised or MSME sectors. Changing the definition of furnishing would also include furniture and home décor accessories, and these numbers would get bigger.

Performance in FY23: After an ecstatic performance in FY21 and FY22, the overall textile exports from India contracted in 2022. An estimated 16-18% de-growth is seen in home textile export in FY23, impacted by the recessionary trend in Europe and cut down on nonessential expenses in the U.S. amid high inflation. The depreciating rupee against the dollar and China+1 policy across the globe restricted the turnover fall for Indian home textile players, but margins were poorly impacted due to lower operating leverage attributed by lower capacity utilisation.

The trend in FY24: Demand momentum is expected to recover from the second half of FY24 as freight and cotton costs show moderation and inventory exhausts with retailers. Further, falling commodity and crude prices will bolster margins and enhance India's competitiveness in export markets while successfully gaining market share in the garments and home textile categories in key export markets.

Future trend: Growth in home textiles in India seems quite positive in coming years, driven by healthy export demand with benefits from reciprocal FTAs (free trade agreements). Increased hygiene consciousness, rising consumer spending on home renovation, expansion in the real estate market, and fashion sensitivity towards domestic furniture will also contribute to the industry’s steady rise. The India Home Textile Market size is estimated at US$ 8.74 billion in 2023 and is expected to reach US$ 13.98 billion by 2028, growing at a CAGR of 9.84% during the forecast period (2023-2028).

Factors that give India an advantage in Global Home Textiles market

(Source: Company, HDFC sec)

Financial Summary

Going ahead, we expect ICIL to report ~14% CAGR growth in revenues over FY23-25E driven by robust volume growth.

With stability in cotton prices, reasonable volume growth in sheet sets and increased contribution from high margin Fashion/Utility/Institutional and B2C segments, we expect EBITDA margins to sustain in the range of 16-18%. On the back of healthy revenue growth and margin expansion, PAT is expected to grow at ~22% CAGR over FY23-25E.

No major capex in near term: In addition to acquisition of home textile business of GHCL, the company has undertaken i) modernization of Gokul Shirgaon with Compact spinning technology, ii) brownfield expansion of 90 mn metres to 108 mn metres, iii) addition in cut/sew facilities and additional Top of the Bed (TOB) capacity, and iv) Additional spinning capacity at Pranavaditya Spinning Mills with a total spindlage capacity of ~68,000 spindles. ICIL is planning to utilise the expanded capacity over next three years, which should support the volume growth over the period.

Going ahead, the management has indicated that it has completed all majority capex and in FY24 it would incur a capex of ~ Rs 65 cr (Rs 23 cr for the spinning plant and ~Rs 40 cr for normal maintenance capex). Thus, with majority of the capex behind us, we expect balance sheet deleveraging to accelerate even further.

With improvement in profitability and limited capex requirements in near term, we expect ICIL to generate cumulative free cashflow of ~Rs 540 cr that should aid in further reduction in debt levels post ~Rs 443 cr YoY reduction in gross debt in FY23.

Improving profitability and sweating of assets at optimum level over next 2-3 years would aid in improvement of return profile.

Key Concerns

US economy slowdown: A slowdown in the US economy would be a risk to our estimates, as more than 70% of the revenue is contributed by the US market.

Volatility in RM (yarn/cotton) prices: As more than 70% of the spinning and weaving activities are outsourced, an increase in yarn prices would impact margins.

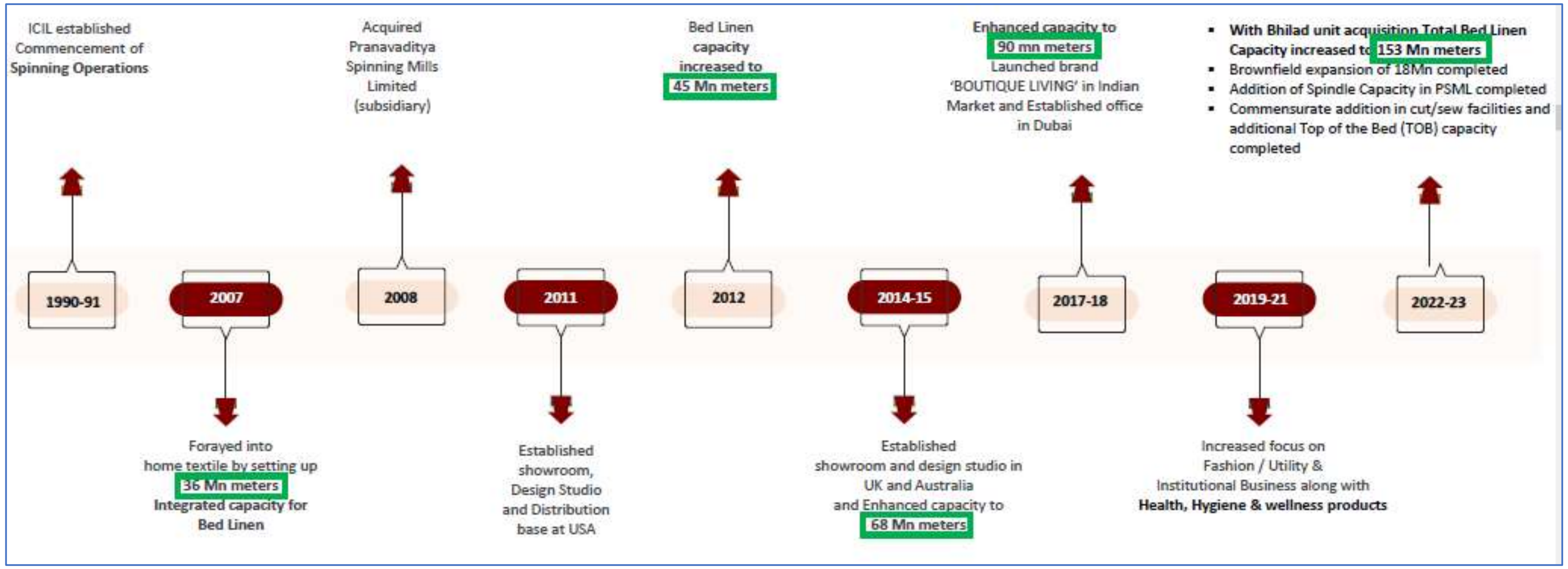
Product dependency: Indo Count's 90/95% of the revenue/EBITDA comes from bedsheets.

Forex Risk: Being a net exporter, the company is exposed to foreign currency fluctuation risks. The company has a forex policy of hedging at least 60-65% of its order book.

About the company

Indo Count Industries Limited (ICIL) was incorporated in 1988 as a cotton yarn manufacturer and commenced production at its export-oriented spinning unit in 1991 with an installed capacity of ~30,000 spindles. In 2006, ICIL commenced forward integration of its operations by setting up a state-of-the art home textiles manufacturing unit in Kolhapur, Maharashtra with an installed capacity of ~36 million metres per annum. Over the years, ICIL has emerged and established itself as one of India's leading suppliers and exporters of bed linen. It is among the leading bed sheet suppliers to the US. In April 2022, ICIL completed the acquisition of GHCL's home textile unit with an installed capacity of 45 million metres per annum along with commensurate cut and sew capacity. ICILs bedding capacity increased to 153mn, with 45mn capacity added at GHCL's plant in Vapi, Gujarat, and the rest 108mn meters at existing Kolhapur unit of Indo Count. In line with the acquisition, the company added 68,000 spindles to its spindle capacity taking the total spindle capacity to 1,40,000. The company plans to utilise the entire spindle capacity for captive consumption.

Key milestones of ICIL



(Source: Company, HDFC sec)

Peer Comparison

Company	M Cap (in Rs. Cr.)	Revenue (in Rs. Cr.)			EBITDA Margin (%)			PAT			RoE (%)			P/E (X)		
		FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E
Indo Count	4785	3012	3389	3902	15%	16%	17%	277	338	414	16%	18%	18%	17	14	12
Welspun India	11161	8094	9069	10262	9%	15%	17%	199	620	852	5%	14%	17%	57	17	13
Trident	18182	6332	7620	8667	15%	17%	19%	442	675	920	11%	15%	17%	41	28	19

(Source: Bloomberg, HDFC sec)

Financials

Income Statement

Particulars (in Rs Cr)	FY20	FY21	FY22	FY23	FY24E	FY25E
Net Revenues	**2080**	**2519**	**2842**	**3012**	**3389**	**3902**
Growth (%)	***7.5***	***21.1***	***12.8***	***6.0***	***12.5***	***15.1***
Operating Expenses	1897	2143	2408	2557	2840	3258
EBITDA	**183**	**377**	**434**	**454**	**549**	**644**
Growth (%)	***17.6***	***105.6***	***15.2***	***4.6***	***20.8***	***17.3***
EBITDA Margin (%)	***8.8***	***15.0***	***15.3***	***15.1***	***16.2***	***16.5***
Depreciation	43	43	41	65	75	78
Other Income	55	38	140	31	41	45
EBIT	**194**	**371**	**533**	**421**	**515**	**611**
Interest expenses	39	28	47	62	59	57
PBT	**57**	**340**	**486**	**359**	**456**	**553**
Tax	-16	91	127	82	119	144
PAT	**73**	**249**	**359**	**277**	**337**	**409**
Share of Asso./Minority Int.	1	2	0	0	0	0
Adj. PAT	**74**	**251**	**359**	**277**	**337**	**409**
Growth (%)	***22.5***	***239.7***	***43.1***	***-22.8***	***21.7***	***21.5***
EPS	3.7	12.7	18.2	14.0	17.0	20.7

Balance Sheet

Particulars (in Rs Cr) - As at March	FY20	FY21	FY22	FY23	FY24E	FY25E
SOURCE OF FUNDS						
Share Capital	39	39	39	40	40	40
Reserves	947	1245	1551	1753	2040	2385
Shareholders' Funds	**986**	**1285**	**1591**	**1793**	**2080**	**2424**
Minority Interest	0	0	0	0	0	0
Total Debt	329	576	1319	876	716	546
Net Deferred Taxes	57	80	66	69	69	69
Total Sources of Funds	**1372**	**1940**	**2977**	**2738**	**2866**	**3040**
APPLICATION OF FUNDS						
Net Block & Goodwill	575	561	634	1114	1109	1101
CWIP	6	8	21	180	180	180
Investments	0	167	2	143	143	143
Other Non-Curr. Assets	10	12	365	53	64	74
Total Non Current Assets	**591**	**748**	**1022**	**1490**	**1497**	**1499**
Inventories	524	718	1068	895	1021	1122
Debtors	242	516	494	409	483	534
Cash & Equivalents	150	40	400	108	43	88
Other Current Assets	188	274	278	158	195	224
Total Current Assets	**1105**	**1548**	**2241**	**1570**	**1742**	**1970**
Creditors	129	235	165	225	260	299
Other Current Liab & Provisions	187	115	120	96	113	129
Total Current Liabilities	**316**	**350**	**286**	**321**	**373**	**428**
Net Current Assets	788	1198	1955	1249	1369	1541
Total Application of Funds	**1379**	**1946**	**2977**	**2738**	**2866**	**3040**

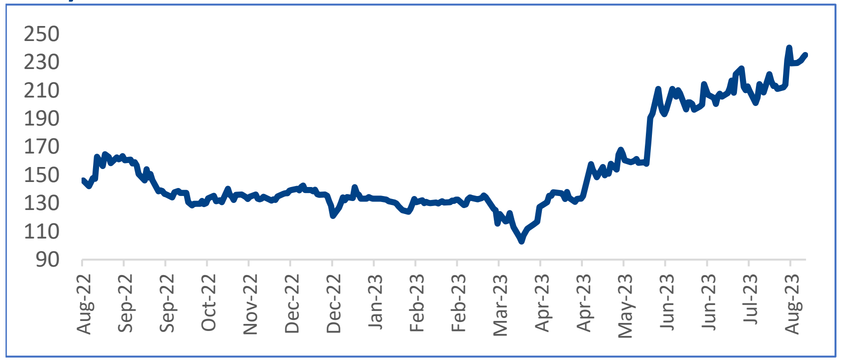
Cash Flow Statement

Particulars (in Rs Cr)	FY20	FY21	FY22	FY23	FY24E	FY25E
Reported PBT	155	343	486	359	456	553
Non-operating & EO items	-162	80	31	-10	-9	-9
Interest Expenses	37	18	30	50	59	57
Depreciation	43	43	41	65	75	78
Working Capital Change	92	-429	-484	391	-188	-128
Tax Paid	-26	-75	-141	-88	-119	-144
OPERATING CASH FLOW (a)	**140**	**-20**	**-37**	**767**	**273**	**408**
Capex	-33	-36	-452	-354	-70	-70
Free Cash Flow	107	-56	-489	413	203	338
Investments	46	-166	169	-142	0	0
Non-operating income	3	13	25	10	0	0
INVESTING CASH FLOW (b)	**16**	**-189**	**-258**	**-486**	**-70**	**-70**
Debt Issuance / (Repaid)	14	228	729	-461	-160	-170
Interest Expenses	-39	-28	-46	-63	-59	-57
FCFE	131	-9	389	-242	-16	111
Share Capital Issuance	0	0	0	0	0	0
Dividend	-14	-12	-30	-39	-50	-65
Others	-1	-2	-7	-12	0	0
FINANCING CASH FLOW (c)	**-40**	**185**	**646**	**-574**	**-268**	**-293**
NET CASH FLOW (a+b+c)	**116**	**-23**	**352**	**-293**	**-65**	**46**

Key Ratios

Particulars	FY20	FY21	FY22	FY23	FY24E	FY25E
Profitability Ratios (%)						
EBITDA Margin	8.8	15.0	15.3	15.1	16.2	16.5
EBIT Margin	9.3	14.7	18.8	14.0	15.2	15.7
APAT Margin	3.5	9.9	12.6	9.2	9.9	10.5
RoE	7.5	22.1	24.9	16.4	17.4	18.2
RoCE	14.9	23.4	22.4	15.1	18.8	21.2
Solvency Ratio (x)						
Net Debt/EBITDA	1.0	1.4	2.1	1.7	1.2	0.7
Net D/E	0.2	0.4	0.6	0.4	0.3	0.2
PER SHARE DATA (Rs)						
EPS	3.7	12.7	18.2	14.0	17.0	20.7
CEPS	5.9	14.9	20.2	17.2	20.8	24.6
BV	50.0	65.1	80.6	90.5	105.0	122.4
Dividend	0.6	1.5	2.0	2.0	2.5	3.3
Turnover Ratios (days)						
Debtor days	44	55	65	55	48	48
Inventory days	93	90	115	119	103	100
Creditors days	24	26	26	24	26	26
Valuation (X)						
P/E	65	19	13	17	14	12
P/BV	5	4	3	3	2	2
EV/EBITDA	27	14	13	12	10	8
EV / Revenues	2	2	2	2	2	1
Dividend Yield (%)	0.2	0.6	0.8	0.8	1.0	1.4
Dividend Payout	16.1	11.8	11.0	14.3	14.7	16.0

One-year Share Price Chart



HARSH RAJENDRA SHETH

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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.

HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066

Compliance Officer: Murli V Karkera Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

For grievance redressal contact Customer Care Team Email: customercare@hdfcsec.com Phone: (022) 3901 9400