Indo Count (INDCOU)

ICICI direct Research

CMP: ₹ 140 | Target: ₹ 150 (8%) | Target Period: 12 months | HOLD

August 3, 2022

Low cost cotton inventory saves the day…

About the stock: Indo Count is one of India's largest home textile manufacturer and exporters with an extensive product range spanning across bed sheets, quilts and bed linen. It has a presence in top nine out of 10 top big box retailers in the US.

- Indo Count is an integrated bedding solution provider, boasting capacity of 90 million meters per annum of dyeing/processing and cutting /sewing
- It exports to nearly 54 countries with US being the prime market (~75% of revenues and commanding ~20%+ market share in bed sheets)

Q1FY23: Indo Count (ICL) reported a resilient performance in Q1FY23 with gross margins (low cost inventory) saving the day. It has completed acquisition of the home textile business of GHCL, which is reflected in the current quarter's revenue.

- Overall volumes for the quarter were at 19.1 million metre (up 6% YoY). Excluding GHCL volumes, we expect volumes to have declined 22% YoY
- We believe the company has utilised most of its low cost cotton inventory, which has resulted in Indio Count reporting abnormally higher gross margins of 62% (vs. average 51-54%)
- The significant delta in gross margins (up 730 bps YoY) more than negated the negative impact of higher operating cost due to integration with GHCL and negative operating leverage (employee & other expenses as percentage to sales rose 346 bps YoY, 511 bps, respectively). Hence, EBITDA margin decline was restricted to 120 bps at 17.3% (up 270 bps QoQ)

What should investors do? The stock price has witnessed a steep correction in the last six months (~40%). India's market share loss in US bed sheets (from 61% to 53%), all-time high cotton prices, softening of US demand (lower housing sales) are some of the main factors weighing on the stock performance. Inventory days have spiked significantly while higher capex has also led debt to bloat to ₹ 1300 crore (D/E: 0.8x). While Q2FY23 is expected to remain challenging, the company expects a gradual recovery from Q3 onwards (but volumes lower than previous year).

- We maintain **HOLD** rating on the stock

Target Price and Valuation: We value ICL at ₹ 150 i.e. 7x FY24E EPS

Key triggers for future price performance:

- FTAs with UK/Europe to improve Indian textiles global competiveness
- With the latest acquisition of GHCL, it would be able to add a whole new avenue of customer base that is untapped, thereby leading to gain in global market share. ICL plans to cross sell its value added categories (fashion, institutional and utility categories) to the existing clientele of GHCL
- Focus on increasing share of B2C and D2C segment through its branded portfolio (owned and licenced). This would aid margins, going forward

Alternate Stock Idea: Apart from ICL, in our textile coverage we like KPR Mill.

- KPR Mills is among select vertically integrated textile players in India that has displayed consistent operating margins with strong return ratios

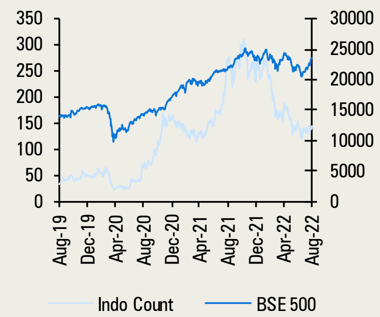
Particulars

Particulars	Amount
Market Capitalisation (₹ crore)	2,765.0
Total Debt (FY22) (₹ crore)	1,301.5
Cash (FY21) (₹ crore)	396.8
EV (₹ crore)	3,669.7
52 Week H / L	315 /123
Equity Capital (₹ crore)	39.5
Face Value (₹)	2.0

Shareholding pattern

	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22
Promoter	58.9	58.9	58.9	58.9	58.9
FII	10.0	9.8	9.7	9.4	9.3
DII	0.1	0.1	0.1	0.1	0.1
Others	31.0	31.2	31.3	31.6	31.7

Price Chart



Key risks

- **Key Risk:**(i) Inability to pass on higher RM costs (ii) Better than expected recovery in consumer demand

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Result Update

ICICI Securities – Retail Equity Research

Key Financial Summary

Financials	FY19	FY20	FY21	FY22	5 Year CAGR (FY17-22)	FY23E	FY24E	2 Year CAGR (FY22-24E)
Net Sales	1,934.2	2,080.1	2,519.2	2,942.0	6.4%	3,149.4	3,918.0	15.4%
EBITDA	155.7	183.2	376.7	534.0	10.5%	450.4	658.2	11.0%
Adjusted PAT	59.7	73.1	249.1	358.5	9.1%	251.4	413.5	7.4%
P/E (x)	46.3	37.8	11.1	7.7		11.0	6.7	
EV/EBITDA (x)	19.4	16.2	8.0	6.9		8.6	5.6	
RoCE (%)	10.0	14.6	20.2	18.5		13.0	18.8	
RoE (%)	6.1	7.4	19.4	22.6		14.0	19.2	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter & conference call highlights

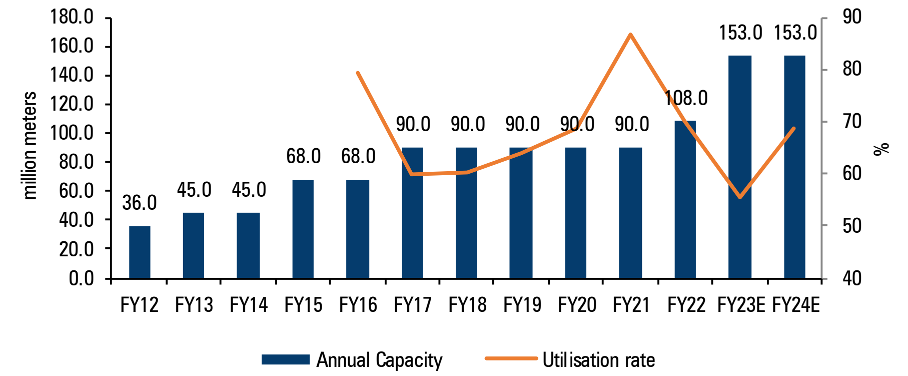
- The industry has been witnessing headwinds related to shortages and unavailability of shipping containers, increase in raw material & freight costs and longer transit duration (from five to six weeks to eight to nine weeks) Furthermore, demand has slowed down in key geographies like the US, UK and Europe, which has led to inventory pile up at the retailer's level. Overall share of India's bed sheet exports to the US has declined from 61% to 53% in YTDFY23
- Overall demand scenario has been sluggish globally, with consumer spend shifting towards necessity while spend on discretionary categories is lower owing to high inflation. The management believes that though there are near term demand headwinds, from a long term perspective it believes India is well positioned to gain market share owing to Government of India actively pursuing Free Trade Agreements with Australia, UAE, UK and Europe. The duty free access to these markets would enhance the competitive positioning of Indian home textile exporters and enable them to garner higher market share in these regions
- Despite significant cost inflationary pressure, the company was able to maintain its EBITDA margin guidance of 15-18% in Q1FY23. The reasons for the same included, constant efforts towards enhancing share of value added products and better hedging of RM prices (company invested OCF and undertook WC debt to invest in cotton). We expect margins to remain subdued in Q2FY23 mainly owing to gross margins normalising (51-52%) and negative operating leverage. With volumes recovering gradually from holiday season and domestic cotton prices expected to soften from November onwards (~₹ 190/kg), we expect the margin trajectory to recover from Q3 onwards
- The company has charted out capex worth ₹ 270 crore towards backward integration (addition of 68000 spindles by March 2023). The yarn would be mainly value added and would be utilised towards supporting recently acquired GHCL capacity (~192 new looms). The management expects share of backward integration to improve from current 10% to 25% over the next two to three years. The capex will be funded through a mix of debt (₹ 275 crore) and internal accruals (₹ 95 crore). On its organic expansion, the management indicated that expansion of capacity from 90 million metre to 108 million metre would be operational by Q3FY23 (capex: ~ ₹ 115 crore)
- Spike in working capital days (from 145 days to 175 days in FY22) and higher capex (GHCL acquisition: ₹ 340 crore and organic capex: ₹ 118 crore) had resulted in debt increasing significantly by 134% YoY to ₹ 1300 crore (D/E: 0.8x) in FY22. We expect debt to remain at bloated levels in FY23 owing to negative FCF. With no major capex requirements in FY24E, we expect the company to generate positive FCF and retire certain long term debt
- **With the latest acquisition of GHCL's home textile business (~45 million meters), Indo Count would become the largest home textile bedding company, globally, with annual capacity of 153 million metres. In the near term its expects the GHCL plant to operate at ~50% utilisation levels. Excluding GHCL, we expect ICL to clock 65 million metre volume, down 15% YoY (~70% CU). Overall volumes (including GHCL) are expected to increase 12% YoY to 85 million metre. We expect utilisation levels to increase gradually in FY24E**

Q1FY23 Earnings conference call highlights:

- The management indicated that despite challenging conditions including inflationary environment in US, sluggish customer offtake and a rise in overall input prices, the company has been able to report a resilient performance owing to its focus on value added products and investment in supply chain
- On the cost side, the management expects raw material (cotton) prices to decline in ensuing quarters. Also, the easing of supply chain (high cost and delay in transporting of goods) related issues would aid in improving the margin profile
- The operations of the plant acquired from GHCL have been integrated with the company and post organic expansion of 18 million metre, ICIL would have an installed capacity of 153 million metre. The GHCL facility is currently operating at around 50% utilisation level and the management expects to scale it up gradually. Also, the margin profile of the GHCL facility is lower than ICIL margin and the management expects to gradually improve GHCL's margin profile
- The management highlighted that it was focusing on increasing the share of value added products over the medium to longer term. The value added products have a superior margin profile compared to normal products with the valued added products gross margin being higher by 8-10%
- The company's 70000 spindle capacity expansion is on track. It expects the first phase to 25000 spindles to be completed by December, 2022 and be operational by March 2023. The company is planning to incur a capex of ₹ 270 crore in FY23 of which ₹ 175 crore would be funded through internal accruals and remaining ₹ 95 crore through debt

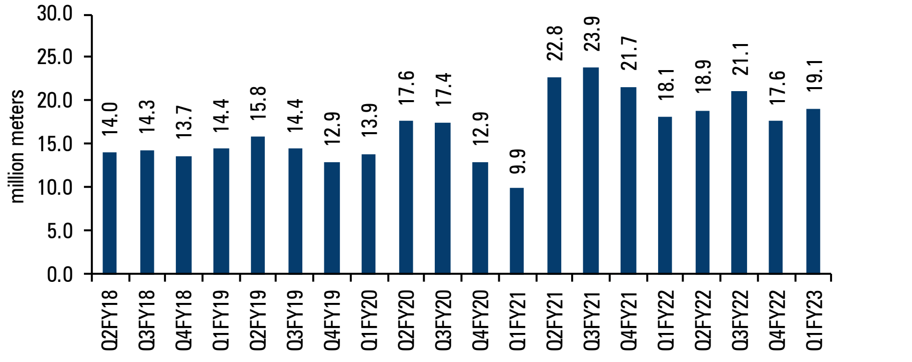
Financial story in charts

Exhibit 1: Capacity & utilisation rate (including GHCL capacity)



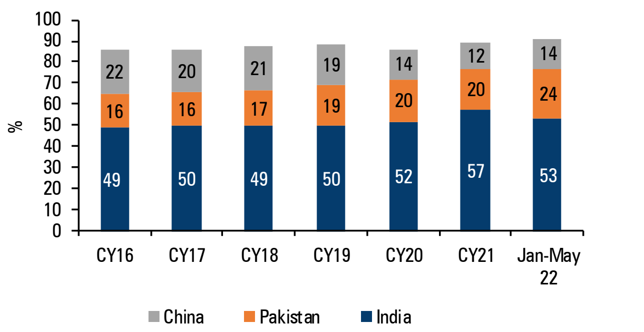
Source: Company, ICICI Direct Research

Exhibit 2: Volume trajectory quarterly trend (Q1FY23 includes GHCL volumes)



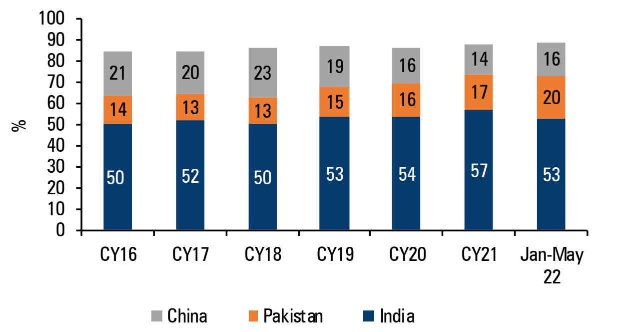
Source: Company, ICICI Direct Research

Exhibit 3: India's share in cotton bed sheet exports to US



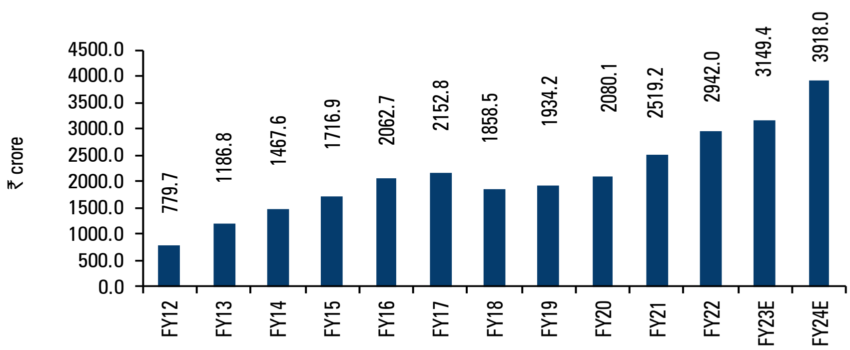
Source: Company, ICICI Direct Research

Exhibit 4: India's share in cotton pillow case exports to US



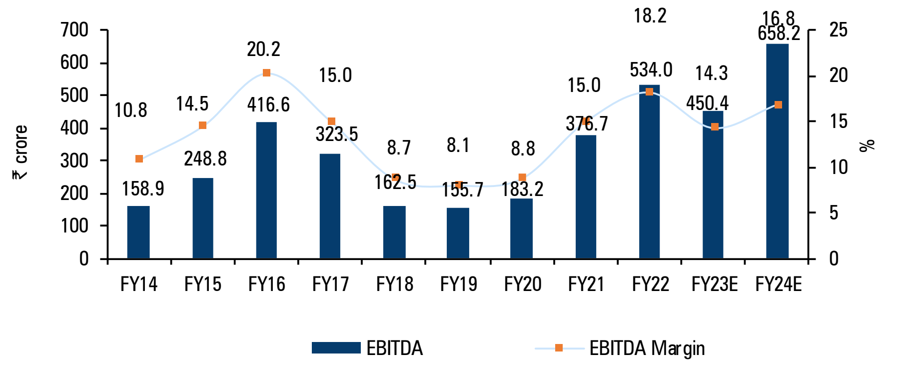
Source: Company, ICICI Direct Research

Exhibit 5: Revenue expected to grow at CAGR of 15% (including acquisition) in FY22-24E



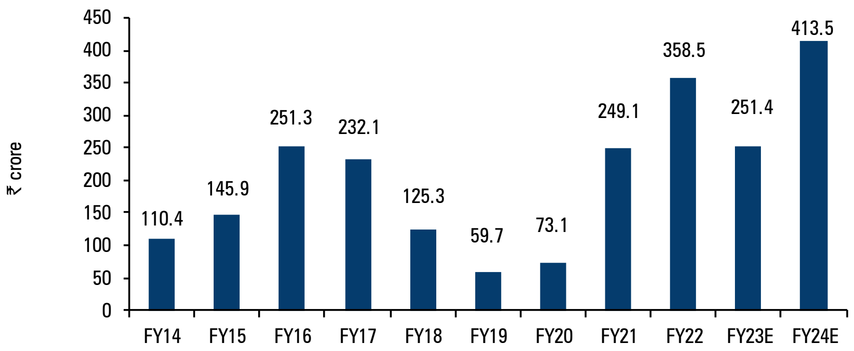
Source: Company, ICICI Direct Research

Exhibit 6: EBITDA and EBITDA margin trend



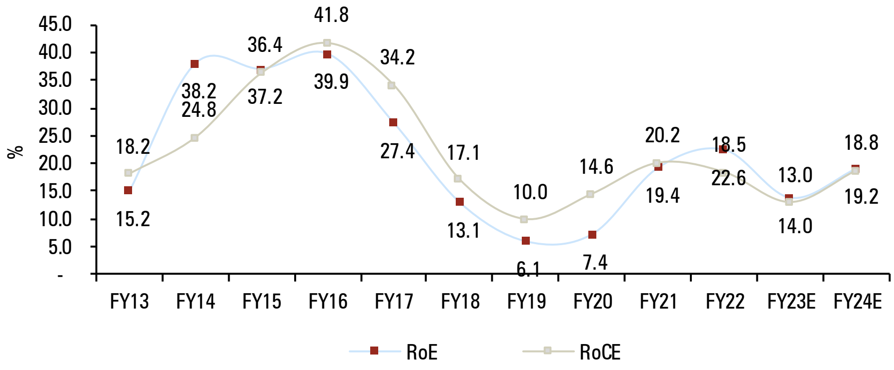
Source: Company, ICICI Direct Research

Exhibit 7: PAT expected to grow at CAGR of 8% in FY22-24E



Source: Company, ICICI Direct Research

Exhibit 8: Return ratio trend



Source: Company, ICICI Direct Research

Financial Summary

Exhibit 9: Profit and loss statement ₹ crore

(Year-end March)	FY21A	FY22E	FY23E	FY24E
Net Sales	2,519.2	2,942.0	3,149.4	3,918.0
Growth (%)	21.1	16.8	7.0	24.4
Total Raw Material Cost	1,269.8	1,353.0	1,464.5	1,802.3
Gross Margins (%)	49.6	54.0	53.5	54.0
Employee Expenses	159.0	191.2	292.9	313.4
Other Expenses	713.6	863.8	941.7	1,144.0
Total Operating Expenditure	2,142.5	2,408.0	2,699.0	3,259.8
EBITDA	376.7	534.0	450.4	658.2
EBITDA Margin	15.0	18.2	14.3	16.8
Interest	28.1	47.4	78.0	62.0
Depreciation	43.2	40.9	65.9	79.1
Other Income	37.8	40.2	20.0	20.0
Exceptional Expense	(3.7)	-	-	-
PBT	339.6	485.9	326.5	537.1
Total Tax	90.5	127.4	75.1	123.5
Profit After Tax	249.1	358.5	251.4	413.5

Source: Company, ICICI Direct Research

Exhibit 10: Cash flow statement ₹ crore

(Year-end March)	FY21A	FY22E	FY23E	FY24E
Profit/(Loss) after taxation	249.1	358.5	251.4	413.5
Add: Depreciation	43.2	40.9	65.9	79.1
Net Increase in Current Assets	-466.6	-442.1	-124.9	-255.4
Net Increase in Current Liabilities	77.6	-74.6	48.6	85.7
CF from operating activities	**-96.7**	**-117.3**	**240.9**	**323.0**
(Inc)/dec in Investments	-166.8	165.4	-1.0	0.3
(Inc)/dec in Fixed Assets	-31.6	-464.9	-419.3	-62.0
Others	-1.8	0.0	0.0	0.0
CF from investing activities	**-200.2**	**-299.4**	**-420.3**	**-61.7**
Inc / (Dec) in Equity Capital	0.0	0.0	0.0	0.0
Inc / (Dec) in Loan	207.7	745.0	-1.3	-266.0
Others	65.4	-59.7	-36.5	-60.7
CF from financing activities	**273.1**	**685.4**	**-37.8**	**-326.7**
Net Cash flow	-23.8	268.7	-217.1	-65.5
Opening Cash	150.5	126.5	395.2	178.1
Closing Cash	**126.6**	**395.2**	**178.1**	**112.7**

Source: Company, ICICI Direct Research

Exhibit 11: Balance Sheet ₹ crore

(Year-end March)	FY21A	FY22E	FY23E	FY24E
Equity Capital	39.5	39.5	39.5	39.5
Reserve and Surplus	1,245.1	1,547.0	1,760.6	2,112.1
Total Shareholders funds	1,284.6	1,586.5	1,800.1	2,151.6
Total Debt	556.4	1,301.5	1,300.2	1,034.2
Non Current Liabilities	94.3	91.3	92.5	93.8
Source of Funds	**1,935.3**	**2,979.2**	**3,192.8**	**3,279.6**
Gross block	1,040.9	1,139.5	1,647.5	1,977.5
Less: Accum depreciation	500.6	541.5	607.4	686.5
Net Fixed Assets	540.3	598.0	1,040.1	1,291.0
Capital WIP	7.7	23.9	270.0	2.0
Intangible assets	2.7	2.9	2.9	2.9
Investments	166.9	1.5	2.5	2.2
Inventory	718.0	1,068.0	1,095.8	1,180.8
Cash	126.5	395.3	178.1	112.7
Debtors	515.7	494.2	560.8	697.7
Loans & Advances & Other CA	191.2	304.9	335.3	368.9
Total Current Assets	1,551.5	2,262.3	2,170.1	2,360.0
Creditors	234.6	148.0	189.8	268.4
Provisions & Other CL	125.6	137.6	144.4	151.6
Total Current Liabilities	360.2	285.7	334.3	419.9
Net Current Assets	1,191.3	1,976.7	1,835.9	1,940.1
LT L& A, Other Assets	26.5	376.3	41.5	41.5
Other Assets	0.0	0.0	0.0	0.0
Application of Funds	**1,935.3**	**2,979.2**	**3,192.8**	**3,279.6**

Source: Company, ICICI Direct Research

Exhibit 12: Key ratios

(Year-end March)	FY21A	FY22E	FY23E	FY24E
Per share data (₹)				
EPS	12.6	18.2	12.7	20.9
Cash EPS	14.8	20.2	16.1	24.9
BV	65.0	80.3	91.1	108.9
DPS	0.6	1.5	1.9	3.1
Cash Per Share	6.4	20.0	9.0	5.7
Operating Ratios (%)				
EBITDA margins	15.0	18.2	14.3	16.8
PBT margins	13.5	16.5	10.4	13.7
Net Profit margins	9.9	12.2	8.0	10.6
Inventory days	104.0	132.5	127.0	110.0
Debtor days	74.7	61.3	65.0	65.0
Creditor days	34.0	18.4	22.0	25.0
Return Ratios (%)				
RoE	19.4	22.6	14.0	19.2
RoCE	20.2	18.5	13.0	18.8
RoIC	24.1	21.6	15.3	19.5
Valuation Ratios (x)				
P/E	11.1	7.7	11.0	6.7
EV / EBITDA	8.0	6.9	8.6	5.6
EV / Sales	1.2	1.2	1.2	0.9
Market Cap / Revenues	1.1	0.9	0.9	0.7
Price to Book Value	2.2	1.7	1.5	1.3
Solvency Ratios				
Debt / Equity	0.4	0.8	0.7	0.5
Debt/EBITDA	1.5	2.4	2.9	1.6
Current Ratio	4.0	6.5	6.0	5.4
Quick Ratio	2.0	2.8	2.7	2.5

Source: Company, ICICI Direct Research

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