



Easing of RM prices to enable gradual margin recovery

About the stock: Vardhman Textiles (VTL) (earlier known as Mahavir Spinning) is part of the Vardhman Group, a large textile conglomerate with a presence across the textile value chain.

- Vardhman is among the few textile companies that have been able to maintain a debt equity ratio below one despite continuous capacity addition
- Healthy cash flows have enabled VTL to maintain reasonable debt levels

Q4FY23 Results: Vardhman Textiles (VTL) reported a QoQ increase in revenues though revenues remained lower YoY. Easing of raw material cost led to QoQ improvement in gross margins and EBITDA margins.

- On a QoQ basis, sales increased 5% to ₹ 2486 crore (YoY decline of 8%)
- Gross margin improved 147 bps QoQ to 38.5% (YoY decline of 987 bps). EBITDA margin improved 300 bps QoQ to 10.5% (YoY decline of 790 bps). PAT was up 55% QoQ to ₹ 158 crore (YoY decline of 51%)

What should investors do? VTL is operating near full capacity in yarn (60-65% of revenues) and would announce capex on visibility of better margins. Though revenue growth in FY24 could remain moderate, margins could improve from the second half of FY24 with the arrival of new cotton and better competitive positioning in the export market. The long term story for large textile exporters from India remains on track. We believe the worst is over and there would be a gradual improvement in margins in ensuing quarters and over the longer term. Hence, VTL would be able to deliver better revenue growth with normalised margins driven by demand enablers like China+1 strategy of global retailers and government initiatives related to signing FTAs with trade partner countries.

- We maintain our **BUY** rating on the stock

Target Price and Valuation: We value VTL at ₹ 375 i.e. 8x FY25E earnings.

Key triggers for future price performance:

- The key factor for enhanced competitiveness and improvement in profitability will be price parity of Indian cotton prices with global cotton
- Stress witnessed by competing countries like Pakistan owing to varied internal factors can be beneficial for Indian cotton spinners, which can lead to increased order flow from global clients
- China+1 strategy of global retailers and government initiatives like FTAs would provide sustainable long term growth opportunity
- We expect revenue CAGR of 6.3% (FY23-25E) and margins to improve towards the lower band of the normal long term range of 18-22% in FY25

Alternate Stock Idea: Apart from VTL, in our textile coverage, we also like Nitin Spinners (BUY with a target price of ₹ 290).

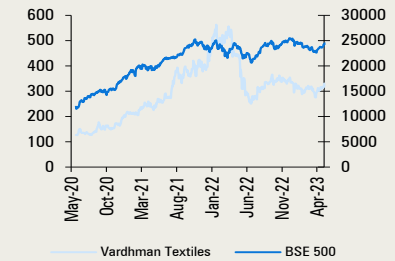
Stock data

Particular	Amount
Market Capitalisation (₹ Crore)	9,396
Debt (FY23) (₹ Crore)	1,677
Cash (FY23) (₹ Crore)	374.2
EV (₹ Crore)	10,699.0
52 week H/L	377 / 246
Equity Capital (₹ Crore)	57.8
Face Value (₹)	2

Shareholding pattern

	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Promoter	62.9	62.9	63.8	63.9	63.9
FII	8.3	7.5	7.0	7.1	6.9
DII	16.9	16.6	16.7	16.9	17.0
Others	12.0	13.0	12.5	12.2	12.3

Price Chart



Recent event & key risks

- VTL's current yarn utilisation trending at 100%
- **Key Risk:** (i) Lower than expected capacity expansion (ii) Lower-than-expected margin

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Key Financial Summary

Financials	FY20	FY21	FY22	5 year CAGR (FY16-21)	FY23P	FY24E	FY25E	2 year CAGR (FY23-25E)
Net Sales	6,735.0	6,139.9	9,622.3	7.2%	10,137.5	10,619.1	11,444.5	6.3%
EBITDA	937.3	813.8	2,273.9	15.3%	1,324.0	1,618.3	2,055.2	24.6%
Adjusted PAT	577.5	414.4	1,546.9	31.0%	795.2	962.7	1,299.9	27.9%
P/E (x)	15.9	22.2	6.0		11.6	9.6	7.1	
EV/EBITDA (x)	11.6	13.3	4.9		8.0	6.9	5.7	
RoCE (%)	7.7	5.5	21.2		9.3	10.8	12.7	
RoE (%)	9.5	6.4	20.1		9.3	10.2	12.3	

Key takeaways of Q4FY23 conference call

- Q4FY23 witnessed an improvement in utilisation levels of Indian cotton spinners to 80%+ from 70% level in Q3FY23. Over the last few quarters, Indian spinners have been at a disadvantage with Indian cotton cost being significantly higher than global cotton prices, which has made it difficult for Indian yarn players to compete in international markets. The management indicated that cotton yarn demand has improved as China has resumed buying cotton yarn from India. Further, stress witnessed by competing countries like Pakistan is expected to aid in improvement of cotton yarn buying from India. Pakistan usually exports coarse count cotton yarn and Indian players have been able to replace Pakistan as a sourcing destination. However, margins in the coarser count cotton yarn were lower than finer counts but it enables the Indian cotton yarn industry to maintain utilisation at healthy levels
- VTL's cotton yarn utilisation is trending at ~100% while fabric utilisation was lower and trending at ~80% compared to usual utilisation level of 90%+
- On the expansion front, of the 1 lakh spindles, 35000 spindles (vortex) had become operational in October 2022 and remaining 65000 spindles are also operational now. On further expansion, the management indicated that it would monitor the situation and decide over the next few quarters as current margins in the cotton yarn segment were not very lucrative. The company alluded to the possibility that it could add capacity of ~2 lakh spindles later in H2FY23 or in FY24 depending on the improvement in demand and margin scenario
- On the demand front, the management indicated that demand is expected to gradually pick up as the inventory held by global retailers reduces. Some global retailers have started placing orders in small lots signifying a reduction of inventories with them. The management expects improved order flow from clients who were sitting on earlier inventory and have been able to gradually liquidate the same
- Over the longer term, the management remain positive on the prospects of the industry owing to the China+1 strategy of global retailers, which should be beneficial for Indian textile players
- From a cotton sourcing perspective, the company highlighted that key considerations are quality of cotton and pricing. Normally, the company prefers purchasing good quality cotton in early season cotton arrivals. However, currently the company's cotton inventory is lower than normal level of six to seven months at two month's level. The company is planning to utilise its cash balance to gradually accumulate cotton as and when the industry scenario improves
- From a profitability perspective, the fabric business is currently able to generate better margins than the cotton yarn business. The management expects margins in H1FY23 to be lower than normal range of 18-22%. Improvement in EBITDA margin is possible from October 2023 onwards when cotton prices can soften on account of arrival of new season cotton
- On the capex front, we have factored in a capex of ₹ 500 crore for FY24E

Financial Summary

Exhibit 1: Profit and loss statement		₹ crore			
(Year-end March)	FY22	FY23P	FY24E	FY25E	
Total operating income	9,622.3	10,137.5	10,619.1	11,444.5	
Growth (%)	56.7	5.4	4.8	7.8	
Raw Material Expenses	4,560.7	5,929.9	5,942.5	6,127.6	
Employee Expenses	729.1	767.2	785.8	824.0	
Mfg, Admin & selling Exps	2,058.7	2,116.4	2,272.5	2,437.7	
Total Operating Expenditure	7,348.4	8,813.5	9,000.8	9,389.3	
EBITDA	2,273.9	1,324.0	1,618.3	2,055.2	
Growth (%)	179.4	-41.8	22.2	27.0	
Depreciation	367.5	394.4	431.9	452.5	
Interest	99.7	102.2	133.1	148.5	
Other Income	224.5	192.0	180.5	228.9	
Exceptional income	0.0	0.0	0.0	0.0	
PBT	2,031.2	1,019.4	1,233.8	1,683.1	
Total Tax	519.7	255.2	310.9	424.1	
PAT	1,511.5	764.2	922.9	1,259.0	
Minority Interest / Others	4.3	9.6	2.8	3.8	
PAT (after minority interest)	1,546.9	795.2	962.7	1,299.9	
Growth (%)	273.3	-48.6	21.1	35.0	
EPS (₹)	54.4	28.0	33.9	45.7	

Source: Company, ICICI Direct Research

Exhibit 2: Cash flow statement		₹ crore			
(Year-end March)	FY22	FY23P	FY24E	FY25E	
PAT	1,546.9	795.2	962.7	1,299.9	
Add: Depreciation	367.5	394.4	431.9	452.5	
(Inc)/dec in Current Assets	-633.1	844.6	-1,373.9	-1,057.2	
Inc/(dec) in CL and Provisions	-10.3	-167.5	184.0	-54.1	
Others	0.0				
CF from operating activities	1,271.1	1,866.7	204.8	641.2	
(Inc)/dec in Investments	-616.5	-857.8	127.4	-72.6	
(Inc)/dec in Fixed Assets	-319.1	-838.7	-500.0	-820.6	
(Inc)/dec in CWIP	-163.3	190.2	-429.0	-100.0	
Others	-77.5	166.4	7.5	7.2	
CF from investing activities	-1,176.3	-1,340.0	-794.0	-986.1	
Issue/(Buy back) of Equity	0.3	0.0	0.0	0.0	
Inc/(dec) in loan funds	134.8	-305.6	677.5	446.0	
Others	-319.6	31.3	-68.4	-191.8	
CF from financing activities	-184.5	-274.3	609.1	254.3	
Net Cash flow	-89.8	252.5	19.9	-90.6	
Opening Cash	211.5	121.7	374.2	394.1	
Closing Cash	121.7	374.2	394.1	303.5	

Source: Company, ICICI Direct Research

Exhibit 3: Balance Sheet		₹ crore			
(Year-end March)	FY22	FY23P	FY24E	FY25E	
Liabilities					
Equity Capital	56.8	56.8	56.8	56.8	
Reserve and Surplus	7,646.9	8,506.6	9,394.3	10,499.2	
Total Shareholders funds	7,703.8	8,563.4	9,451.1	10,556.0	
Total Debt	1,983.0	1,677.5	2,355.0	2,801.0	
Deferred Tax Liability	249.1	268.3	268.3	268.3	
Other LT Liabilities	22.0	18.6	21.4	24.7	
Minority Interest / Others	137.5	88.5	92.3	92.3	
Total Liabilities	10,095.4	10,616.3	12,188.1	13,742.3	
Assets					
Gross Block	8,651.8	9,490.5	9,990.5	10,790.5	
Less: Accu Depreciation	5,161.1	5,555.5	5,987.5	6,419.4	
Net Block	3,490.7	3,935.0	4,003.0	4,371.1	
Capital WIP	241.2	51.0	480.0	580.0	
Total Fixed Assets	3,731.9	3,986.0	4,483.0	4,951.1	
Investments	1,691.1	2,548.8	2,421.4	2,494.0	
Inventory	2,882.3	2,392.7	3,491.2	4,546.4	
Debtors	1,321.2	1,191.0	1,454.7	1,442.3	
Loans and Advances	6.4	6.2	4.2	4.6	
Other Current Assets	907.6	683.0	696.6	710.6	
Cash	121.7	374.2	394.1	303.5	
Total Current Assets	5,239.2	4,647.1	6,040.8	7,007.4	
Creditors	864.4	695.4	884.2	824.3	
Provisions	19.3	20.9	16.0	21.9	
Total Current Liabilities	883.7	716.2	900.2	846.1	
Net Current Assets	4,355.5	3,930.9	5,140.6	6,161.2	
Others Assets	317.0	150.6	143.1	135.9	
Application of Funds	10,095.4	10,616.3	12,188.1	13,742.3	

Source: Company, ICICI Direct Research

Exhibit 4: Key ratios					
(Year-end March)	FY22	FY23P	FY24E	FY25E	
Per share data (₹)					
EPS	54.4	28.0	33.9	45.7	
Cash EPS	67.4	41.9	49.1	61.7	
BV	271.1	301.3	332.6	371.4	
DPS	8.2	4.2	5.1	6.9	
Cash Per Share	4.3	13.2	13.9	10.7	
Operating Ratios					
EBITDA Margin (%)	23.6	13.1	15.2	18.0	
PBT Margin (%)	21.1	10.1	11.6	14.7	
PAT Margin (%)	15.7	7.5	8.7	11.0	
Inventory days	109.3	86.1	120.0	125.0	
Debtor days	50.1	50.0	50.0	50.0	
Creditor days	31.7	35.0	37.0	37.0	
Return Ratios (%)					
RoE	20.1	9.3	10.2	12.3	
RoCE	21.2	9.3	10.8	12.7	
RoIC	25.0	12.8	13.9	16.1	
Valuation Ratios (x)					
P/E	5.9	11.5	9.5	7.0	
EV / EBITDA	4.8	7.9	6.8	5.7	
EV / Net Sales	1.1	1.0	1.0	1.0	
Market Cap / Sales	0.9	0.9	0.9	0.8	
Price to Book Value	1.2	1.1	1.0	0.9	
Solvency Ratios					
Debt/EBITDA	0.9	1.3	1.5	1.4	
Debt / Equity	0.3	0.2	0.2	0.3	
Current Ratio	6.1	6.7	6.8	8.5	
Quick Ratio	2.7	3.2	2.9	3.0	

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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