

Sector: Consumer Discretionary  
Company Update

	Change
Reco: <b>Hold</b>	↔
CMP: <b>Rs. 54</b>	
Price Target: <b>Rs. 66</b>	↓

↑ Upgrade ↔ No change ↓ Downgrade

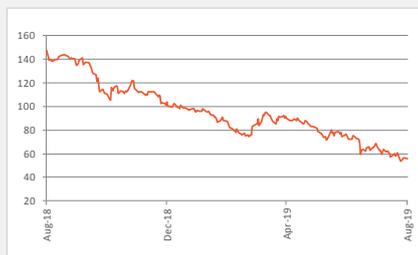
## Company details

Market cap:	Rs. 1,397 cr
52-week high/low:	Rs. 154/53
NSE volume: (No of shares)	35.0 lakh
BSE code:	500101
NSE code:	ARVIND
Sharekhan code:	ARVIND
Free float: (No of shares)	14.7 cr

## Shareholding (%)

Promoters	43.1
FII	21.6
DII	14.1
Others	21.3

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	-12.6	-29.5	-32.1	-60.7
Relative to Sensex	-6.2	-25.7	-32.8	-60.3

Sharekhan Research, Bloomberg

Arvind Limited's (Arvind) Q1FY2020 performance was affected by lower margins in the textile business due to subscale operations of its newer garmenting facilities. Revenue grew by ~5% y-o-y as the denim segment's volumes continued to remain under pressure (garmenting segment's revenue grew by 20% because of increased garment production). Revenue of advanced material business grew by 31% and margins improved on a y-o-y basis. Management expects revenue to grow by 6-7% and OPM is likely to sustain at 10% y-o-y for FY2020 (we have factored in OPM of 9.5%). We believe increased scale of advanced material business and better utilisation in new garmenting facilities will drive margins ahead. We maintain our Hold recommendation on the stock.

## Key positives

- Advanced material business (~8% of overall sales) delivered strong performance with revenue and EBITDA margins of the business improving by 511 BPS to 13%.
- Garmenting segment's (25.6% of textile business) revenue grew by 22% on account of operations of new facilities.

## Key negatives

- Denim segment (~30% of textile business) continues to post subdued performance with revenue growing by just 2%, EBITDA margin fell by 214 BPS to 9.7%.
- Denim export volumes declined by 3 million metres, whereas total volumes for the woven segment was down by ~2 million metres.
- The water business had a subdued quarter.
- Depreciation and finance costs increased by 20% and 26%, respectively, leading to adjusted PAT declining by ~68% y-o-y to Rs. 29.4 crore.

## Our Call

We have reduced our earnings estimates for FY2020 and FY2021 to factor in subdued performance in Q1FY2020. New garmenting plants are operating at a sub-optimal level and will take some time to scale up. Once the plants start operating at optimum utilisation, profitability of the textile business will improve. The stock has corrected by ~32% in the past three months. We maintain our Hold recommendation on the stock with a revised price target (PT) of Rs. 66.

## Key Risks

Volatile currency and higher cotton prices remain one of the key risks for margin expansion and would continue to affect earnings growth in the near term.

## Valuation

Particulars	FY18	FY19	FY20E	FY21E
Revenues	6,794	7,142	7,608	8,272
OPM (%)	9.9	10.0	9.5	9.3
Adjusted PAT	286	265	230	252
Adjusted EPS (Rs.)	11.2	10.3	8.9	9.7
P/E (x)	4.8	5.3	6.1	5.5
P/B (x)	0.5	0.5	0.5	0.4
EV/EBIDTA (x)	5.2	4.9	5.1	5.0
RoNW (%)	11.3	10.0	8.1	8.4
RoCE (%)	10.5	7.1	6.4	6.5

Source: Company, Sharekhan Estimates

**Revenue rose by ~5%; Profitability affected by sub-optimal operations of new facility:** For Q1FY2020, Arvind's revenue grew by 4.8% y-o-y to Rs. 1,897 crore as compared to Rs. 1,810 crore in Q1FY2019, contributed by 20% higher garment volumes and 31% growth in advanced materials. Gross margin declined by 417 BPS y-o-y due to 14% inflation in raw-material costs (cotton prices increased from Rs. 113 per kg to Rs. 126 per kg). This, along with increased employee expenses, led the operating profit to decline by 23% y-o-y to Rs. 154.4 crore, which was lower than our expectation. OPM declined by 298 BPS y-o-y to 8.1% due to reduction in textile margins as the newly commissioned garmenting facilities operated at sub-optimal scale while ramping up. Adjusted PAT for Q1FY2020 declined by 68% y-o-y to Rs. 29.4 crore due to higher finance costs and depreciation. There was a post-tax exceptional item of Rs. 5 crore (Rs. 6.2 crore pre-tax) related to retrenchment compensation. Thus, reported PAT came in at Rs. 24.4 crore. Adoption of Ind AS 116 did not have a material impact on the company's profitability.

**Weak performance by the denim business; Advance materials business shines:** The textile business saw 3.6% growth in revenue to Rs. 1,616 crore. Within the textiles business, the denim segment's revenue grew by mere 2% y-o-y to Rs. 481 crore due to softer demand and a decline in exports owing to lower export volumes (down by 3 million metres). Revenue from the woven segment grew by 6% y-o-y to Rs. 635 crore, while revenue from the garments segment grew by 22% y-o-y to Rs. 415 crore. EBITDA margin of the textile business fell by 214 BPS y-o-y from 11.9% in Q1FY2019 to 9.7% in Q1FY2020 due to lower sales volume, higher pre-operative costs in new manufacturing plants and the write-off in Arvind Stores as the company decided to convert all the retail stores to franchisee operations. Performance of the advanced material business was robust, with revenue rising by 31% y-o-y to Rs. 167 crore. EBITDA of the business came in at Rs. 18 crore in Q1FY2020 as against Rs. 10 crore in Q1FY2019 and EBITDA margin expanded by 297 BPS y-o-y to 11% because of operating leverage as the mature part of the portfolio has started scaling along with improved realisation from higher value-added products.

### Other conference call highlights

- ◆ Arvind would end FY2020 with garment manufacturing capacity of ~60 million pieces on account of scale up of existing plants and commissioning of new plants. It is expected to clock volumes of ~40-42 million pieces as against 34 million pieces in FY2019.
- ◆ The advanced materials segment is expected to grow by 30% to Rs. 800 crore in FY2020 and the margins are expected to improve.
- ◆ The garment segment is expected to clock revenue of ~Rs. 2,500 crore and margins of ~11-13% once the capacities have been fully scaled up.
- ◆ The revenue of the others category mainly consisting of Envisol is expected to stand at ~Rs. 300-400 crore for FY2020.
- ◆ The denim exports market saw an increase in the sale of super-premium and value products, thus squeezing the middle segment where Arvind operated. This affected the denim volumes for the last few quarters. However, going ahead, the company has tweaked the cost structure and made changes in the manufacturing setup and thus, the management expects the denim volumes to improve.
- ◆ The net debt at the end of Q1FY2020 stood at Rs. 3,024 crore, which increased sequentially on account of capex and opportunistic buying of cotton. Going ahead, the company has reduced its capex guidance to Rs. 250 crore (Rs. 175 crore done in Q1) in H1 and another Rs. 30-40 crore in H2. Also, the company is expected to reduce the debt by ~Rs. 300 crore by the end of FY2020.

**Results (Consolidated)**

Particulars	Rs cr				
	Q1FY20	Q1FY19	Y-o-Y (%)	Q4FY19	Q-o-Q (%)
Total revenue	1896.5	1809.6	4.8	1859.4	2.0
Raw material cost	954.7	835.5	14.3	832.4	14.7
Employee cost	246.6	233.2	5.8	214.5	15.0
Other expenses	540.8	539.8	0.2	628.9	-14.0
Operating profit	154.4	201.2	-23.2	183.6	-15.9
Other income	20.8	15.3	35.8	19.6	5.7
Interest & other financial cost	62.4	49.6	25.7	61.4	1.6
Depreciation	66.3	55.2	20.2	62.8	5.7
Profit before tax	46.4	111.6	-58.4	79.1	-41.3
Tax	17.6	29.7	-40.9	9.2	91.8
Adjusted PAT	28.9	81.9	-64.8	69.9	-58.7
Extraordinary item	5.0	6.9	-27.9	3.6	39.9
Minority Interest (MI)	0.5	0.3	92.0	0.3	41.2
Reported PAT	24.4	75.3	-67.6	66.7	-63.4
Adjusted PAT after MI	29.4	82.2	-64.3	70.3	-58.2
Adj. EPS (Rs)	1.1	3.2	-64.8	2.7	-58.7
			<b>BPS</b>		<b>BPS</b>
GPM (%)	49.7	53.8	-417	55.2	-558
OPM (%)	8.1	11.1	-298	9.9	-173

Source: Company; Sharekhan Research

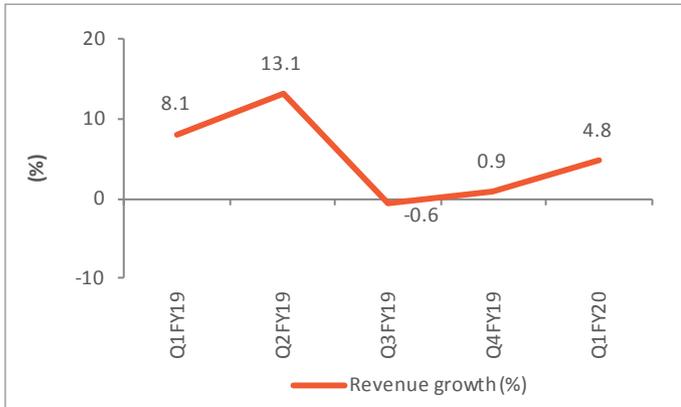
**Segmental Performance**

Particulars	Q1FY2020			Q1FY2019		
	Revenue	EBITDA	EBITDA Margin	Revenue	EBITDA	EBITDA Margin
Textile	1616	157	9.7	1560	185	11.9
Advanced Materials	167	18	11.0	128	10	7.8
Others	123	-7	-6.1	131	5	3.9

Source: Company; Sharekhan Research

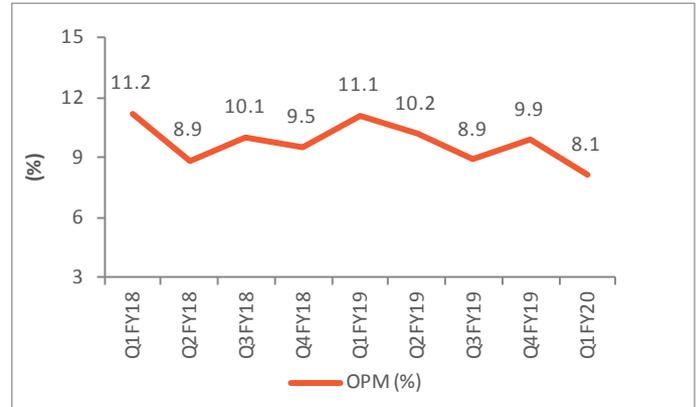
**Financials in charts**

**Revenue growth stood at 4.8% in Q1**



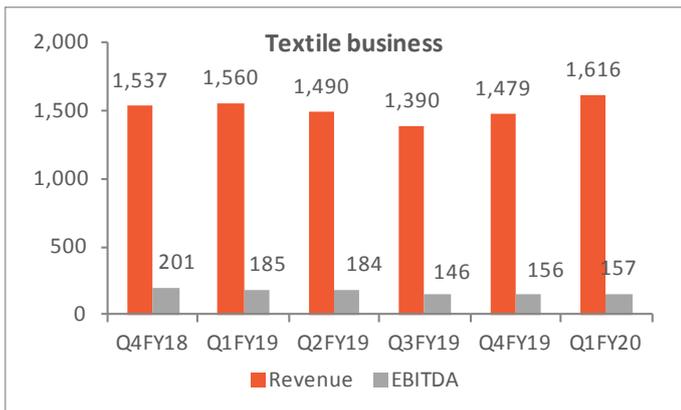
Source: Company, Sharekhan Research

**OPM came in at 8.1%**



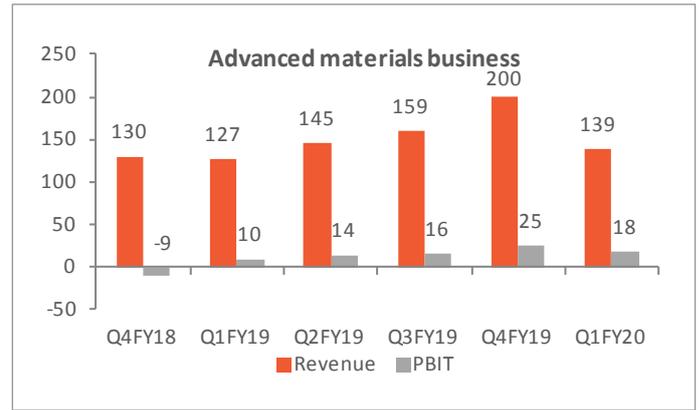
Source: Company, Sharekhan Research

**Textile business clocked revenue of Rs. 1,616 crore**



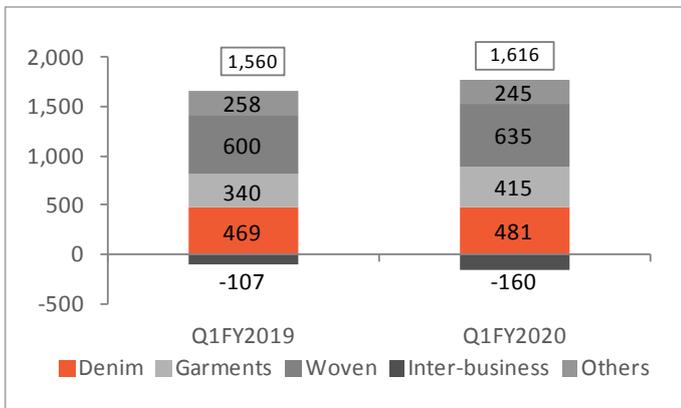
Source: Company, Sharekhan Research

**Advanced materials grew by 31% y-o-y**



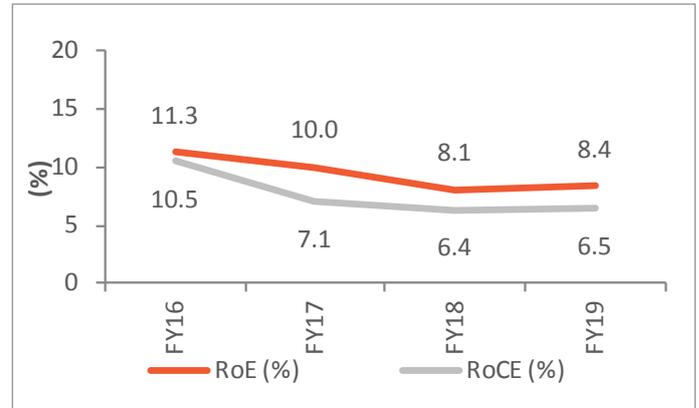
Source: Company, Sharekhan Research

**Garments performed well, others category declined**



Source: Company, Sharekhan Research

**Return ratios to remain in double digits**



Source: Company, Sharekhan Research

## Outlook

Arvind's performance in Q1FY2020 was subdued. Margins were affected by higher input costs and subscale operations of newer garment facilities. Going ahead, management expects revenue to grow by 6-7% in FY2020, supported by the advanced materials business. Denim volumes are expected to remain under pressure. Margins are expected to be lower in H1FY2020 on a y-o-y basis. However, with the new garment facility achieving optimal utilisation by the second half of the year, margins are expected to improve in H2FY2020. Management is confident of sustaining 10% OPM (we have factored in 9.5%). Increased scale of advanced materials business and improving utilisation of the new garment facilities will help drive margin expansion going ahead.

## Valuation

We have reduced our earnings estimates for FY2020 and FY2021 to factor in subdued performance in Q1FY2020. New garmenting plants are operating at sub-optimal levels and will take some time to scale up. Once the plant starts operating at optimum utilisation, profitability of the textile business will improve. The stock has corrected by ~32% in the past three months. We maintain our Hold recommendation on the stock with a revised PT of Rs. 66.

## Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
Raymond	23.2	18.0	14.6	9.9	8.4	7.2	10.5	13.9	14.7
Kewal Kiran Clothing	15.3	13.9	12.4	9.2	8.0	7.1	16.9	16.8	17.4
Arvind	5.3	6.1	5.5	4.9	5.1	5.0	7.1	6.4	6.5

Source: Company, Sharekhan estimates

## About company

Arvind is an innovation-driven and customer-centric global textile play with presence in garmenting segments such as denim, woven and knits and technology-driven and high-margin business such as advanced materials. In FY2019, the company created value for shareholders by demerging its branded fashion and retail business and engineering business into two separate listed entities – Arvind Fashion and Anup Engineering. The demerger will help the company to scale up its core textile business in domestic as well international markets. The company is focusing on improving its return ratios by improving its profitability through vertical integration, introducing differentiated next-generation products and scaling up the advance material business.

## Investment theme

Arvind's FY2019 performance was affected by slowdown in the garmenting segment (especially in exports markets), volatile currency and high working capital requirement resulting in lower revenue growth and increases in debt affecting the bottom-line with higher interest. Global demand for denim continues to remain muted and overall situation remains bleak at the start of the current fiscal. Increased scale of the advance material business would improve profitability in the long run. We will keenly monitor the performance in the coming quarters. Any uptick in the performance of the garmenting segment would act as a key trigger for the stock.

## Key Risks

- ♦ Volatile currency and higher cotton prices remain one of the key risks for margin expansion and would continue to affect earnings growth in the near term.
- ♦ Sustained slowdown in the garmenting business would continue to affect revenue growth in the near to medium term.

## Additional Data

### Key management personnel

Sanjay S Lalbhai	Chairman and Managing Director
Jayesh K Shah	Whole Time Director and Chief Financial Officer
R V Bhimani	Company Secretary

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Aura Securities Pvt Ltd	36.9
2	TT International Investment Management	5.0
3	HDFC Asset Management Co Ltd	4.7
4	Dimensional Fund Advisors LP	2.7
5	Franklin Resources Inc	2.6
6	Reliance Capital Trustee Co Ltd	2.6
7	AML EMPLOYEES WELFARE TRUST	2.5
8	Kotak Mahindra Asset Management Co	2.4
9	Vanguard Group Inc	1.8
10	Atul Ltd	1.6

Source: Bloomberg

Sharekhan Limited, its analyst or dependant(s) of the analyst might be holding or having a position in the companies mentioned in the article.

# Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

---

**Disclaimer:** This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst further certifies that neither he or its associates or his relatives has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: [compliance@sharekhan.com](mailto:compliance@sharekhan.com);

For any queries or grievances kindly email [igc@sharekhan.com](mailto:igc@sharekhan.com) or contact: [myaccount@sharekhan.com](mailto:myaccount@sharekhan.com)

---

**Registered Office:** Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;

Disclaimer: Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on [www.sharekhan.com](http://www.sharekhan.com); Investment in securities market are subject to market risks, read all the related documents carefully before investing.