Result update – Q1FY17

Sangam India Ltd. – Maintain our "BUY" rating 24th Aug, 2016

CMP: Rs. 275|Target Rs. 424|Time horizon: 1 year |Basis of valuation: FY18E Financials| Upside: 53 %| Market Cap: Rs. 1,073 cr.| FV: Rs. 10

(Rs cr)	Q1FY17	Q1FY16	%yoy	Q4FY16	%qoq
Total Income from Operations	**407.9**	**366.6**	11.3	**387.4**	5.3
Material costs	(219.9)	(194.8)	12.9	(205.9)	6.8
Purchase of stock in trade	(22.0)	(1.5)	1,408.9	(3.5)	-
Changes in inventory	12.0	1.6	635.6	(8.1)	(248.6)
Power and Fuel	(38.8)	(40.4)		(35.8)	8.5
Employee benefit expenses	(39.4)	(33.1)	19.1	(36.2)	9.0
Other expenditure	(43.6)	(36.8)	18.3	(43.7)	(0.1)
Operating profit	**56.2**	**61.7**	(8.9)	**54.4**	3.3
OPM (%)	***13.8%***	***16.8%***	***(310) bps***	***14.0%***	**(190) bps**
Depreciation	(19.4)	(20.4)	(4.6)	(18.0)	8.0
Interest	(16.5)	(17.5)	(5.5)	(15.0)	10.5
Other income	2.8	2.1	31.3	12.4	(77.6)
PBT	**23.0**	**25.9**	(11.4)	**33.8**	(32.1)
Tax	(7.7)	(8.9)	(13.2)	(7.8)	(1.4)
Effective tax rate (%)	***33.5%***	***34.2%***		***23.1%***	45.1
Adjusted PAT	**15.3**	**17.1**	(10.5)	**26.0**	(41.3)
Adj. PAT margin (%)	***3.7***	***4.7***	***(90.9)***	***6.7***	(44.2)
Equity capital	**39.4**	**39.4**	-	**39.4**	-
FV	**10.0**	**10.0**	-	**10.0**	-
No. of equity shares	**3.9**	**3.9**	-	**3.9**	-
EPS for the quarter	**3.87**	**4.33**	(10.5)	**6.59**	(41.3)

Source: Company, Ajcon Research

Q1FY17 result analysis

The Company's topline witnessed an increase of 11.3 percent on yoy basis to touch Rs. 407.9 crores in Q1FY17. On Qoq basis, moderate growth of 5.3 percent was seen.

Q1FY17 EBITDA witnessed a decline of 8.9 percent to touch Rs. 56.2 crores on yoy basis owing to increase in Material costs. The increase was mainly on account of rising cotton and PSF prices. According to CRISIL, cotton prices are expected increase by 3% in FY17 from a decline of 8% in FY16 due to a) slight increase in the MSP of cotton to Rs. 41 per kg from Rs. 40.5 per kg in CS2015-16 (Cotton Season) and 2) narrowing of demand –supply gap due to decrease in acreage and fall in cotton yield in CS2015-16. PSF prices are expected to rise 4% in FY17 from a decline of 15% in FY16 and VSF prices are expected to rise 3% due to increase in raw material prices of rayon grade wood pulp.

Employee expenses also witnessed a significant ramp up. In Q1FY17, Employee expenses rose by 19.1% to Rs. 39.4 crores owing to focus on retail.

OPM declined by 310 bps in Q1FY17 to 13.8% in QIFY17 as against 16.8% in Q1FY16. Q4FY16 OPM stood at 14%. The above stated reasons contributed to the fall in OPM.

PAT decreased by 10.5% to touch Rs. 15.3 crores in Q1FY17. On QoQ basis too, PAT witnessed a significant decline of 41 percent.

The Company is executing an expansion project having outlay of Rs. 198 crores being part funded by Term Loans of Rs. 157.50 crores and balance from internal accruals. The project envisages installation of 26736 spindles on P/V Dyed Yarns. 74 imported Airjet Shuttleless Weaving Machines, One Denim Line and 2 MW Solar Power Plant. The Project activities are in progress as per schedule.

Key developments

Sangam India plans to open 10-15 stores in tier I and tier II metro towns by March 2017 and has floated a 100 per subsidiary for the purpose.

It plans to offer more than 100 exclusive ranges of products in these stores. Till date, the company has appointed 700 MBOs (Multi Brand Outlets) all over India and intends to take this network to 1,000 by the end of this fiscal.

The company plans to set up 10-15 EBOs (Exclusive Brand Outlets) by the end of this financial year, its Chairman R P Soni said. It has already started its online retail initiative with c9fashion.com and has tied up with several online retailers in the country. He said a 100 percent subsidiary - Sangam Lifestyle Ventures - has been floated for its retail business. The new subsidiary will focus on developing new exclusive chain of stores under C 9 Fashion brand name while the company will continue to expand its multi-brand outlets. "We have received an encouraging response to our recent foray into seamless garmenting. What enthuses us is that this response is despite the fact that we are yet to fully roll out our brand and marketing campaigns. We are hopeful of a much higher revenue contribution and better operating margin from this segment going forward," he said. Sangam (India) reported a 49.39 percent rise in net profit at Rs 77.04 crore for the last fiscal. Increased integration focus on exports helped the company maintain realisations, despite falling prices.

Profit and Loss Account

(Rs cr)	FY16	FY15	%yoy
Income from Operations	**1,511.5**	**1,476.9**	2.3
Material costs	(830.3)	(830.6)	(0.0)
Purchase of stock in trade	(12.5)	(24.7)	(49.4)
Changes in inventory	22.2	7.4	201.6
Power and Fuel	(157.9)	(155.5)	1.5
Employee benefit expenses	(139.9)	(118.6)	17.9
Other expenditure	(159.7)	(137.4)	16.2
Operating profit	**233.3**	**217.4**	7.3
OPM (%)	***15.4***	***14.7***	70 bps
Depreciation	(76.2)	(80.4)	(5.2)
Interest	(64.0)	(67.2)	(4.8)
Other income	17.6	2.7	542.0
PBT	**110.8**	**72.5**	52.8
Tax	(33.4)	(20.6)	62.2
Effective tax rate (%)	***30.1***	***28.4***	
PAT	**77.4**	**51.9**	49.1
Adj. PAT margin (%)	***5.1***	***3.5***	*160 bps*
Equity capital	39.4	39.4	0.1
FV (Rs.)	10.0	10.0	-
No. of equity shares (cr)	3.9	3.9	0.1
EPS (Rs.)	**19.63**	**13.18**	49.0

Source: Company, Ajcon Research

Balance Sheet (Rs. crs.)

	Particulars	Audited	Audited
		FY16	**FY15**
A	**EQUITY AND LIABILITIES**		
1.	**Shareholder's Funds**		
a)	Share Capital	39.42	39.42
b)	Reserves & Surplus	399.83	332.28
	Networth	**439.25**	**371.70**
2.	**Non – current Liabilities**		
a)	Long – term borrowings	281.34	257.78
b)	Deferred tax liabilities	42.05	40.35
c)	Other long-term liabilities	-	-
d)	Long – term provisions	-	-
		323.39	**298.13**
3.	**Current liabilities**		
a)	Short-term borrowings	301.5	276.93
b)	Trade payables	76.47	75.05
c)	Other current liabilities	137.48	142.83
d)	Short term provisions	14.17	11.97
		529.62	**506.78**
	Total – Equity & Liabilities	**1292.26**	**1176.61**
B	**ASSETS**		
1.	**Non-current assets**		
a)	Fixed assets	598.94	565.69
b)	Non-current investments	5.85	5.85
c)	Long-term loans and advances	19.71	14.51
		624.50	**586.05**
2.	**Current assets**		
a)	Inventories	294.49	265.09
b)	Trade receivables	271.10	251.71
c)	Cash & Cash Equivalents	3.61	3.91
d)	Short-term loans and advances	76.43	57.72
e)	Other current assets	22.13	12.13
		667.76	**590.56**
	Total - Assets	**1292.26**	**1176.61**

Source: Company

Investment rationale

Strong background

Established in 1984, Sangam India Ltd. is the flagship company of Sangam Group a Rs. 4,000 crores + business conglomerate having diverse business interests across textiles, steel, infrastructure, power and energy sectors. Mr. RP Soni, Chairman & First Generation entrepreneur, leads the Group. Sangam ranks among the leading players in Indian textiles sector with presence in PV (polyester viscose), dyed yarn and fabrics. One of market leaders in PV dyed yarn with 25% share. Today, SIL is a leading manufacturer of PV yarn in India. The company is also present in the Indian synthetic blended fabric and denim segments with brands such as Sangam Suitings and Sangam Denim. Sangam also has garnered respectable market – share in denim segment within three years of commencement of production. Sangam was promoted as a fabric manufacturing unit, under the name of Arun Synthetics Pvt. Ltd, by Mr. R.P. Soni and Mr. S.N. Modani. The company took a strategic decision to backward integrate and forayed into spinning in 1995 by installing 17,280 spindles for manufacturing PV dyed yarn. Sangam's manufacturing facilities are located in Bhilwara, Rajasthan. As of FY15, the company has a spinning capacity of 211,296 spindles and 3,128 rotors; weaving capacity of 437 looms; and processing capacity of 53 mn meters P.A.

Largest producer of PV dyed yarn

SIL is the largest producer of PV dyed yarn in Asia at Single location. SIL is a forerunner in manufacturing ready to stitch Fabric with the annual capacity to produce 24 million meters of fabric and 32 million meters of denim.

Marquee clients

The company's client base includes Raymond, RSWM, Banswara Syntex, Donear, Siyaram and Grasim. It has a network of 100 dealers and 1,000 retailers across India.

Domestic Clientele: Raymonds, Siyaram Silk Mills, Grasim Bhiwani Textile, BSL Ltd., Donear Industries, S. Kumar Nationwide, Shri. Dinesh Mills, RSWM.

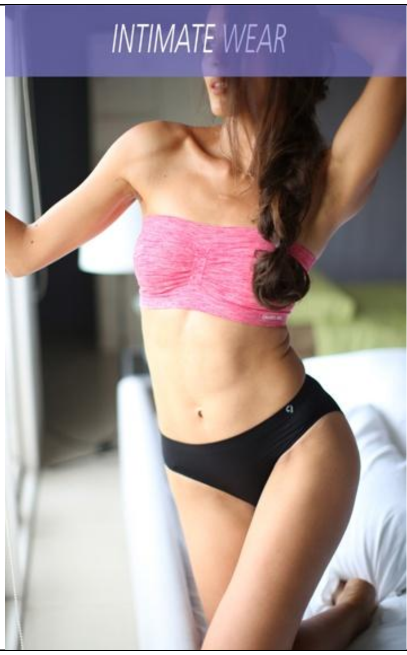
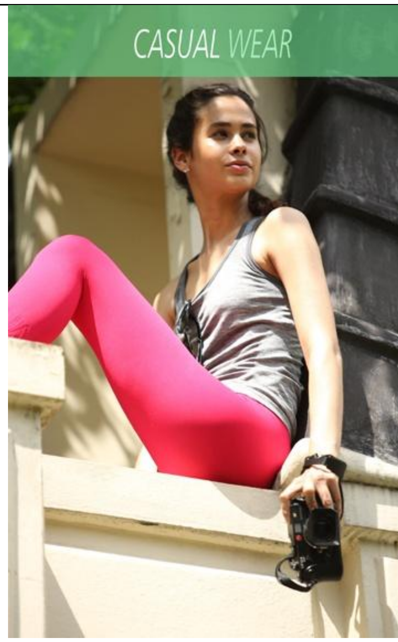
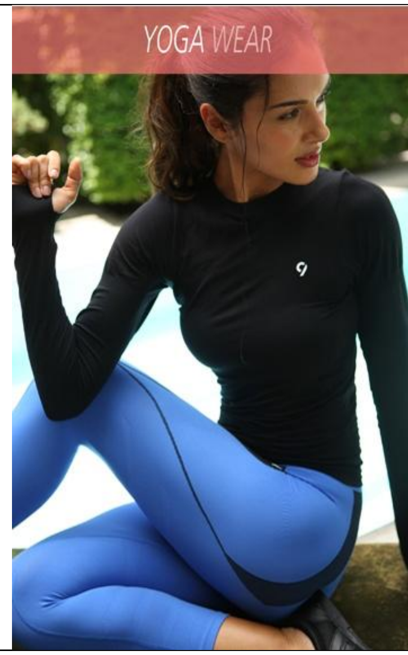
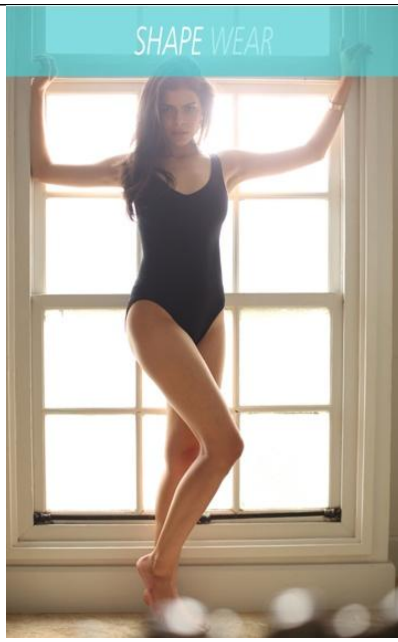
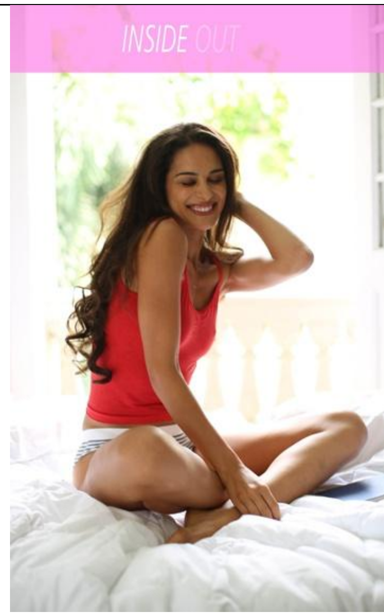
Overseas Cientele: Bossa Ticaret Ve Sanayi Islatmeleri (Turkey – PV Dyed Yarn), Oguz Textil (Turkey – PV Dyed Yarn), Baekart (USA – PV Dyed Yarn), TBM Textil bezero De Menezes (Brazil – PV Grey Yarn), Vanden Berghe Roger NV (Belgium – Carpet Yarn), EDPA (USA – Cotton Yarn, Knitted fabric), Melmar Knit Wear Company (Egypt – Cotton Yarn)

Foray in Seamless Wear garment segment to improve margins

Recently, SIL has forayed into seamless garments for women under Channel Nine brand. For this segment, the Company has latest world class seamless technology imported from Italy. Having established its presence across the value chain, its foray into branded seamless garments not only will enable it to extend its value proposition directly to consumer segments through its own brand; but more importantly pave way for improving margins going forward. Given the explosion of demand in the women-wear segment, Channel Nine would offer diverse range at affordable price across customer segments. Channel Nine range comprises an exquisite range of seamless garments for women including Intimate wear (seamless bra and panties), Active wear (seamless sports bra and leggings), Yoga wear (Yoga T shirt, Yoga Legging, Yoga Track Pant) Shape wear (low compression and high compression), Casual wear (leggings and tanktop), Outwear, products for fitness, shaping and technical products. Apparels with performance features like odour resistance and moisture management find loyalty with customers. The rising per capita income and change in lifestyle has increased demand for quality products. However, with the increasing exposure to international fashion trends, the Indian consumer today wants more than just need – based clothing. In addition to old parameters like basic functionality, comfort and price, better look, perfect fit and trendiness have also become key purchase parameters. Innovations in casual wear products are primarily related to product design, color selection options and fiber mix.

SIL is also leveraging its existing channels of distribution as well as initiating newer channels (online) to capture the market share in Rs.15,000 crore domestic apparel industry. SIL has introduced seamless garment manufacturing facility with 36 seamless knitting machines with current capacity to produce 3.6 mn pieces per annum which will eventually scale up to 10.8mn units by FY18. The steady increase in the operating margin percentage is mainly due to the higher margins in the seamless garments

business. Key clients in Seamless Garments include Nike, Urban Yoga, JC Penny and many other reputed players.

Competition Mapping (Product & Price)

Brand	Sports Wear	Inner Wear	Casual Wear	Shape Wear	Night Wear	Swim Wear	Men's range	Seamless range	Pricing
Channel Nine	√	√	√	√	-	-	-	√	Rs. 299 onwards
Enamor	√	√	-	√	√	-	-	-	Rs. 199 onwards
Amante	-	√	-	√	√	-	-	-	Rs. 395 onwards
Zivame	√	√	√	√	√	√	-	√	Rs. 400 onwards
Adidas	√	-	-	-	-	-	√	√	Rs. 800 onwards
Nike	√	-	-	-	-	-	√	√	Rs. 800 onwards

Source: Company, Ajcon Research

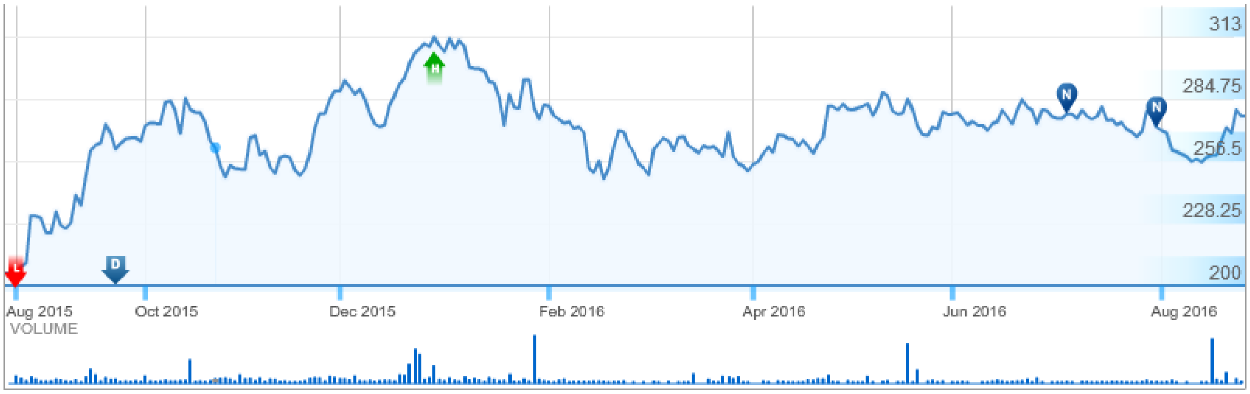
Successful backward integration

The company has successfully modified their capacities, thereby resulting in better integration and efficiency in the value chain. Today, its denim fabrics and seamless garments rely minimally on the externally sourced raw materials. The Company's in-house consumption of PV yarn has grown from 5% in 2010-11 to 18% in 2014-15. At the same time, they consume about 50% of the cotton yarn captively, despite nearly doubled capacities in the same period. SIL is initiating further investments in yarn and fabric capacities to ensure complete integration of the textile value chain in the coming years. Investments in capacities lead to scale. However, they have continued to focus on reducing controllable costs to improve their profitability, despite regular expansion.

Impressive financial performance and strong cashflows

Sangam has witnessed a topline compounded annual growth rate (CAGR) of 10% in its revenues and 29% in its net profits over the period FY10-16. In the same period, it has invested over Rs300 crore in capex (forward and backward integration) but reduced its debt/equity ratio to 1.33 x in FY2016 from over 3.6x in FY2010 due to focus on cash inflows. The return ratios have also improved consistently with return on equity (RoE) and return on capital employed (RoCE) at over 15% in FY2016 from less than 10% in FY2010. The significant improvement and consistency in its financial performance is driven by its efforts to continuously move in backward-forward integration.

Stock Price Movement



Source: www.moneycontrol.com

Recommendation & Valuation

Sangam being probably the only Company which has all the segments of textiles industry including seamless women which has value addition. With due consideration to factors like a) Company managed by very well qualified, experienced and dedicated professional management, b) a fully corporate governance compliant Company with full transparency, c) diversified product mix with market leadership in most of its products, d) foray into seamless female garments segment with its own brand of "Channel Nine" which will add tremendous value to the Company, e) impressive financial performance with strong cash flows, f) prudent debt management – debt/equity to improve to 0.99x by FY18E from current 1.33x in FY16 inspite of expansions for capacity additions, g) ROE set to improve, h) stock attractively trading at cheap valuations of 7x at estimated FY18 EPS, hence we recommend a "BUY". We value the stock at Rs. 424 (by assigning a multiple of 12x (which is appropriate considering the strengths of the Company and its market leadership) at revised FY18E EPS of Rs. 35.4.

Based on Q1FY17 results and raw material scenario, we keep the topline estimates as the same. However, we revise the EBITDA margins to 15.8% in FY18 and consequent effect on projected EPS is as under.

Financial Summary (Rs. in crores)

Particulars	2014-15	2015-16	2016-17	2017-18
	Aud.	Aud.	Proj.	Proj.
Net Revenue from Operation	1468.6	1511	1941.7	2281.74
Other Income	11.02	17.59	15.23	17.14
Total Income	1479.6	1528.9	1956.9	2298.8
Increase %	2.37	3.3	27.9	17.47
EBITDA	220.13	233.3	305.2	363
EBITDA Margin%	14.99%	15.4	15.6%	15.8%
Interest	67.22	64	70.98	56.35
Depreciation	80.40	76.2	100.68	109.16
Prov. For Book debts.	0.35	-	-	-
PBT	72.16	110.8	133.54	197.49
Income tax	20.59	33.4	40.25	59.5
Net Profit	51.57	77.4	93.29	137.99
N.P. Margin	3.49%	5.1%	4.76	6.0
Book Value (Rs.)	94.29	111.4	137	172
P/BV (x)	2.74	2.49	2.02	1.61
EPS (Rs.)	13.08	19.54	23.9	35.4
P/E (x)	21	14	9	7
ROE (%)	13.87%	17.5	17.5	20.5
Inventory days	66	71	67	64
Debtors days	58	65	64	60
Creditors days	32	18	30	29
Debt/Equity (x)	1.65	1.33	1.44	0.99

Source: Company, Ajcon Research

Recommendation parameters for fundamental reports:

Buy – Absolute return of 20% and above
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Book profits: On achieving the price target given in the research report for a particular Company or on a occurrence of a specific event leading to change in fundamentals of the Company recommended

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