INDIA

BUY

Sarla Performance Fibers

Textile

Initiating Coverage 19 September 2016

Spinning success with niche business model

We initiate coverage on Sarla Performance Fibers (SPFL) with a Buy and TP of Rs83. It's unique and niche business model of manufacturing client-specific yarn in a commoditised product gives it an edge and has a significant entry barrier among global players. It plans to expand in the US market with cash breakeven in FY18E through cross-selling to existing customers. Strong sustainable margin expansion coupled with ~20% RoE augurs well for the company along with low Net D/E. Sarla Flex further offers an upside of Rs27/sh (43%) to our TP at 50% capacity utilisation in FY18E while currently we have not assigned any value. SPFL's adjusted cash flow yield stands at attractive levels of 9.4%, PE of 8x on 18E basis.

- **Strong capabilities in niche specialised yarn:** SPFL manufactures polyester and nylon textured, twisted and dyed yarns; covered yarns; high-tenacity yarns and sewing thread used in niche applications. Client-specific value addition on 1) moulds, 2) denier difference, 3) types of twists and 4) colours in small quantities and specific packaging helps build long-term relationships with clients which act as significant entry barriers. Over the last decade, it has established a strong global footprint, supplying to over 45 countries across six continents, with manufacturing and distribution in close proximity to demand centres globally. Low dependence on any client further helps de-risk business.
- **Strengthening foothold through expansion in US:** Strategic entry in the US market would augur well over long term given the legal restrictions under CAFTA/NAFTA laws with duty waiver of up to 32% for end user, greater visibility and closer proximity to end customers, thereby increasing demand coupled with higher realisation. We expect the company to achieve cash breakeven in FY18E led by prudent cost management despite factoring modest 20-25% capacity utilisation. Any major client win with whom the company has existing long-term relationship would help it move to a different orbit. While we remain conservative by modeling mere 1% contribution of Sarla Flex on consolidted EBIDTA in FY18E, at 50% capacity utilisation it can have a disproportionate contribution of 21% in FY18E leading to significant upside in medium term.
- **Strong financial with industry-leading balance sheet:** The company has over the time invested in expansion (Sarla Flex, USA), de-bonding of Vapi unit and new product launches (Nylon 66) which would help it expand revenues, margins and PAT at a CAGR of 11.4%/27.6%/19.7%, respectively, over FY16-18E. We believe the quantum jump in margins would sustain going forward, with product mix change and turnaround in the US business. Additionally, SPFL will i) reduce net debt over next two years with strong cash flows; ii) generate healthy OCF, while low capex requirement for core business would generate strong FCF; iii) RoE of ~20% over next two years along with healthy dividend payout. SPFL scores high on our detailed corporate governance checks, as well.
- **Valuation and risks:** We believe SPFL should command premium to its domestic textile peers given its unique and niche business model, cash breakeven in the US subsidiary, industry-leading margins coupled with healthy cash flows and return ratios. Although we consider different valuation methods to value the company (PE – Rs77/sh, EV/EBIDTA – Rs75/sh), we finally value it on adjusted OCF (AOCF = OCF – Interest) to enterprise value (EV) yield to arrive at a TP of Rs83 and initiate with a Buy. SPFL's OCF/EV yield is at attractive levels of 9.4% on 18E basis, meriting re-rating. We believe at 50% capacity utilisation in Sarla Flex for FY18E we expect an incremental 43% upside of Rs27/sh at 10x PE. Key risks are sustained losses in US business and raw material volatility. *Currently, the stock has no institutional sell-side coverage.*

Target Price	Rs83
CMP*	Rs62
Upside	*34%*

Price Performance (%)*

	1M	6M	1Yr
SRPL IN	*6.2*	*3.3*	*14.1*
Nifty	*0.6*	*7.6*	*12.1*

Key Data	
Bloomberg Code	SRPL IN
Curr Shares O/S (mn)	83.5
Diluted Shares O/S(mn)	83.5
Mkt Cap (Rsbn/USDmn)	5.2/76.8
52 Wk H / L (Rs)	91.5/47
5 Year H / L (Rs)	91.5/7.4
Daily Vol. (3M NSE Avg.)	73086

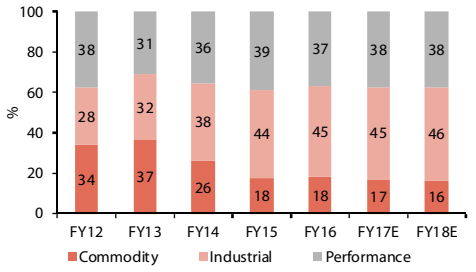
**as on 16 September 2016; Source: Bloomberg, Centrum Research*

Shareholding pattern *(%)* *

	June-16	Mar-16	Dec-15	Sep-15
Promoter	*55.2*	*55.2*	*55.2*	*55.2*
FIIs	*0.0*	*0.0*	*0.0*	*1.2*
DIIs	*14.4*	*14.4*	*14.3*	*15.9*
Others	*30.4*	*30.4*	*30.5*	*27.8*

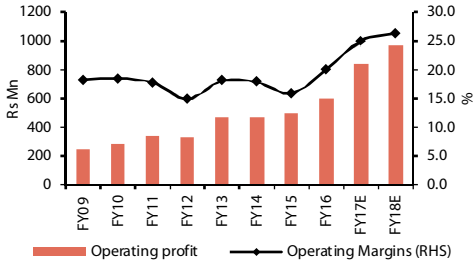
*Source: BSE, *as on 16 September 2016*

Revenue mix across product profile - SPFL



Source: Company, Centrum Research Estimates

Operating margin expansion



Source: Company, Centrum Research Estimates

Sarla US Financials

Rs mn	FY14	FY15	FY16	FY17E	FY18E
Sales	91	416	549	467	505
Operating Profit	(28)	(71)	(39)	(7)	7
PAT	(32)	(135)	8	(48)	(39)

Source: Company, Centrum Research Estimates

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Consolidated Financials

Y/E Mar(Rs mn)	Rev	*YoY (%)*	EBITDA	*EBITDA (%)*	PAT	*YoY (%)*	EPS (Rs)	*RoE (%)*	*RoCE (%)*	P/E (x)	EV/EBITDA (x)
FY14	2,618	*1.2*	467	*17.9*	278	*(0.9)*	4.0	*17.8*	*9.5*	4.5	5.7
FY15	3,121	*19.2*	496	*15.9*	279	*0.6*	3.4	*14.0*	*7.1*	11.1	8.4
FY16	2,977	*(4.6)*	597	*20.0*	450	*61.2*	5.4	*18.3*	*9.8*	11.7	10.1
FY17E	3,341	*12.3*	835	*25.0*	557	*23.7*	6.7	*19.7*	*10.8*	9.3	7.2
FY18E	3,696	*10.6*	972	*26.3*	646	*15.8*	7.7	*19.6*	*11.3*	8.0	5.9

Source: Company, Centrum Research Estimates

Centrum Equity Research is available on Bloomberg, Thomson Reuters and FactSet

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Strong capabilities in niche business model

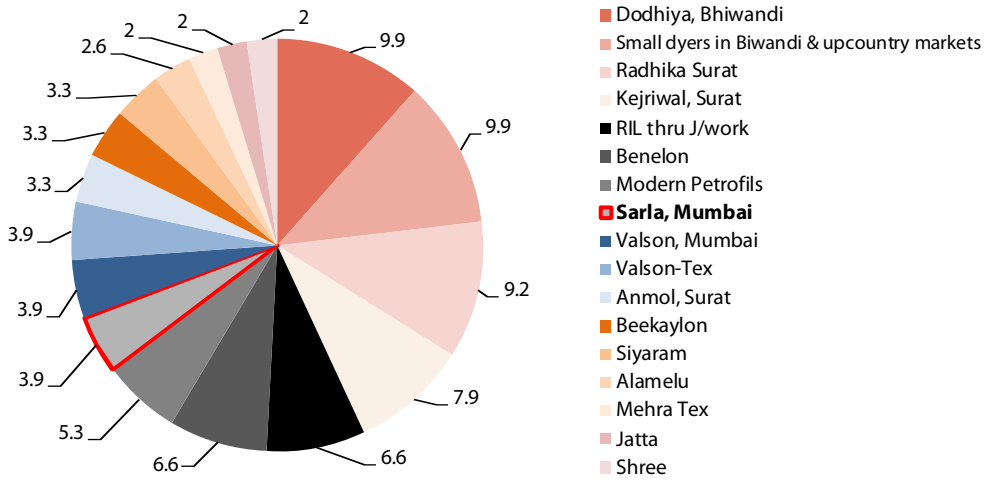
Sarla Performance Fibers Ltd (SPFL), one of the well-established and niche players in India, exports regular as well as high-tenacity polyester and nylon yarns. It began operations 22 years back as a commodity manufacturer of man-made fibre. However, in the last 10 years, it has successfully transformed its business strategy and implemented a niche business model. It has an installed capacity of 11,900 TPA for manufacturing yarns in Silvassa (Units 1 & 2) and a 3,200 TPA dyeing unit at Vapi. Unit 1 is engaged in texturising and twisting of nylon & polyester and covered & rubber covered yarn and Unit 2 is engaged mainly in the processing of high-tenacity yarn in addition to those carried out by Unit 1. The third unit at Vapi is engaged in dyeing of polyester & nylon yarn processed at Silvassa. The company is focused on difficult end-user applications and higher value-added yarns to leading global apparel brands and companies. While it still manufactures some commodity yarns, the major focus is on performance fibres. The company currently has ~4% market share in the conventional dyed yarn in India.

Exhibit 1: Manufacturing Facility – India

SILVASSA		VAPI
	12km distance	
Facility highlights • Two adjoining facilities • Installed capacity of 11,900 TPA • Can produce over 250 varieties of polyester & nylon yarn **Products on offer** • Textured polyester yarn • Bulkon • Textured nylon stretch yarns • Covered yarns • High-tenacity yarns		**Facility highlights** • In-house dyeing facility • Installed capacity of 3,200 TPA • State-of-the-art technology • Computerised shade matching and new colour development **Highlights** • Increased product offering to dyed yarn • Expansion, upgradation & modernisation undertaken in 2010

Source: Company, Centrum Research

Exhibit 2: Market share of conventional dyed yarns (%)

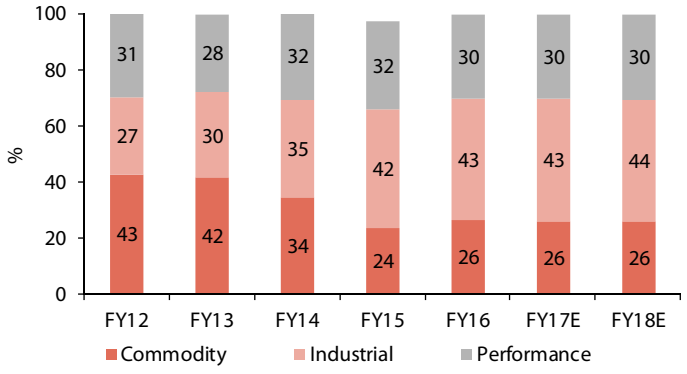


Source: AYM Syntex Presentation

Over the last few years, the company has conciously moved away from commodity yarn to industrial and performance yarn. Gross margins in commodity yarn are 20-25%, while that for industrial and performance yarn are 55-70%. Also, the mix between nylon and polyester is different, with nylon yarn having higher realisation than polyester yarn. Industrial yarns have applications in fishing nets, parachutes, shoes, seat belts, threads, car airbags etc. Performance yarn are used in socks, hosiery, elastics, inner wear, swimming costume, medical bandages etc. Commodity yarn are used in clothing.

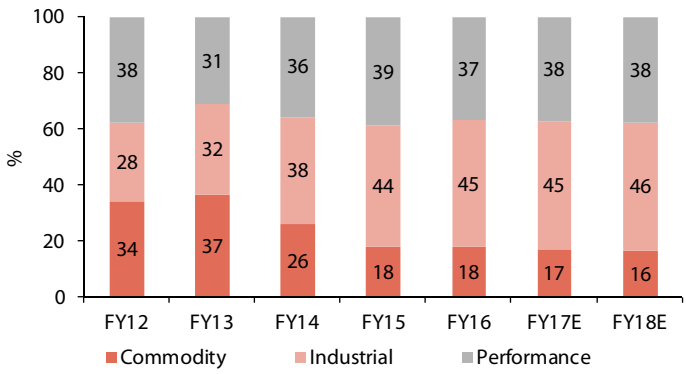
Volume mix for commodity has declined from 43% in FY12 to 26% in FY16, while that of industrial has increased from 27% to 43%. Share of performance has remained stable at ~30% over the same period. However, lower realisation for commodity yarn has mere 18% revenue share in FY16, while that of industrial has 45% revenue share.

Exhibit 3: Product mix by volumes



Source: Company, Centrum Research Estimates

Exhibit 4: Product mix by revenue



Source: Company, Centrum Research Estimates

One among a few players globally catering to specialised yarns

SPFL manufactures yarn on client-specific requirements only and has the ability to manufacture small quantities used in niche applications. Hence, the company is always focused on margins by moving up the value chain.

As the process and client requirement increases with specific value addition, the realisation/kg increases. We believe the realisation/kg is the highest in covered yarn where the company leads the market in India, followed by high-tenacity and twisted nylon yarn. Compared to polyester yarn, nylon yarn would always have higher realisation and margin. Addition of the dying process further increases the realisation and margins. **We believe the client-specific value addition is on 1) moulds, 2) denier difference, 3) different twists and 4) colours.** Hence, a specifically produced yarn cannot be sold to another customer. The company focusses more on tailor-made products, quality and delivery which helps build long-term relationships with customers. This ensures deeper relationship with the customer and increased wallet share over a period.

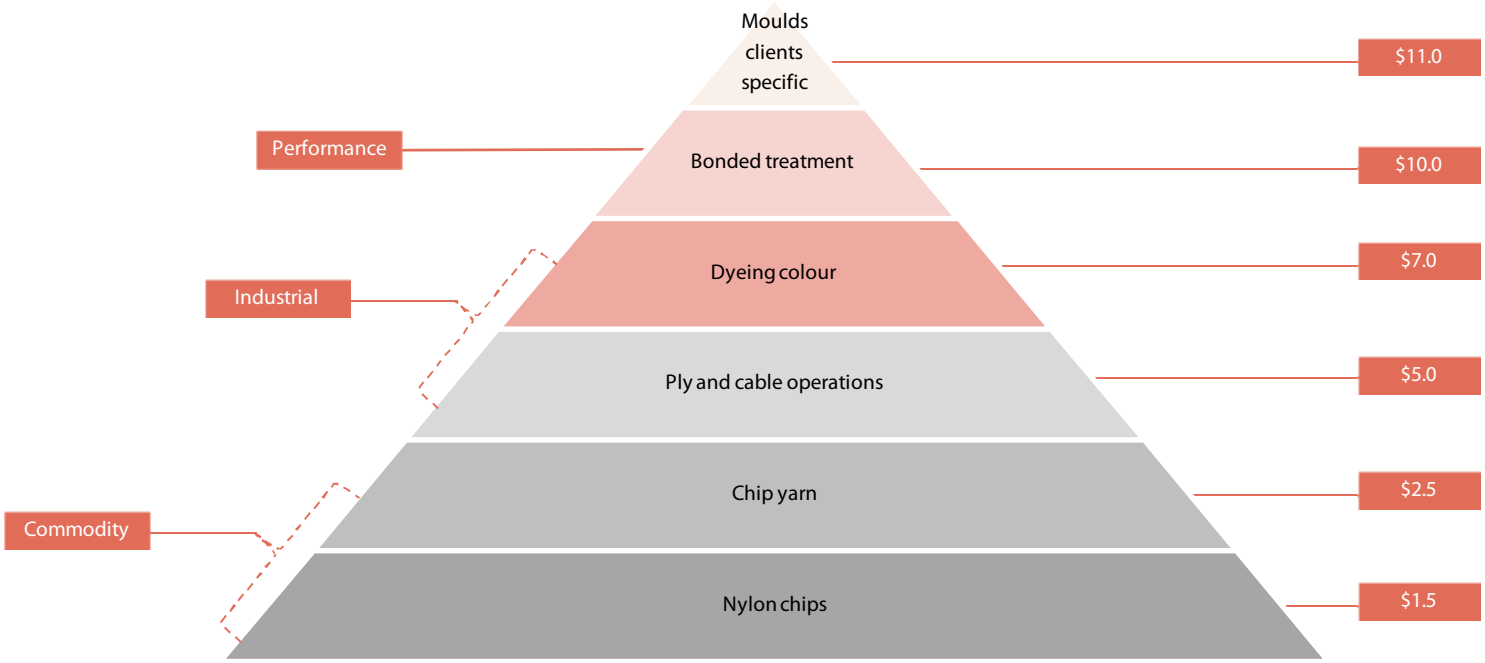
Since inception, SPFL understands that the key to developing a strong and deep relationship with its customers is to cater to their end-to-end needs and supply as many ingredients of the final product as possible. For instance, for an end-user industry such as socks, the customer would otherwise have to target different suppliers for manufacturing socks – covered yarn required for the heel, toe and the top, and textured polyester/nylon yarn for the remaining part of the socks.

Understanding this need, Sarla with its wide product range now supplies all the raw material needed to manufacture socks, making the company a preferred supplier and saving the time and energy for its customers to source from multiple suppliers. The company also caters holistically to elastics & narrow fabrics used in the manufacture of apparel. Today, Sarla constantly develops its product portfolio to cater to its specially defined niche end applications.

Exhibit 5: High-end application products made in India

Source:Company, Centrum Research

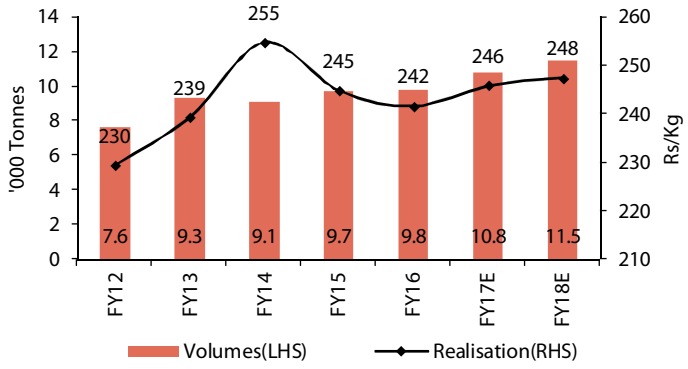
Exhibit 6: Steadily moving up the value chain



Source:Centrum Research

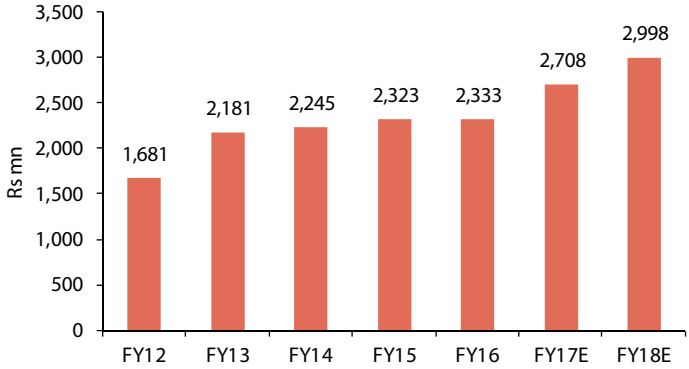
We have modelled mere 8% volume CAGR for the next two years, with capcaity utilisation at ~96% by FY18E. We believe the management focus is always on enhancing value rather than increasing volumes. Hence, volume growth would always be in single digit. We expect the realisaions growth at ~0-2% with product mix change. Hence, standalone revenue growth would be 12% over next two years.

Exhibit 7: Blended Volumes and Realisations



Source: Company, Centrum Research Estimates

Exhibit 8: Standalone Yarn sales



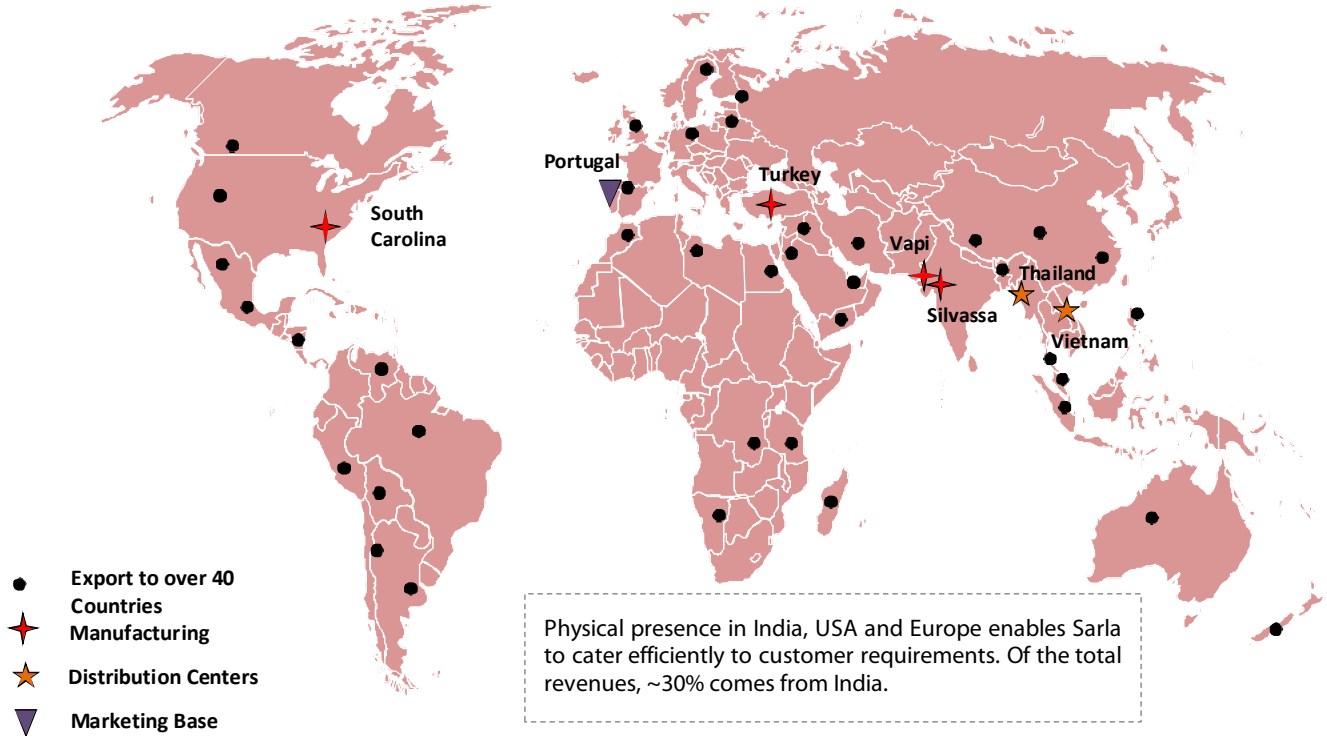
Source: Company, Centrum Research Estimates

Manufacturing & distribution hub in close proximity to demand centres globally

Customer relationships are the cornerstone of SPFL's marketing strategy, and to this end, the company has taken several initiatives. Specific teams are responsible for building relationships and responding to the needs of especially large clients, with focus on ensuring quality and expanding offerings. This has helped Sarla establish a strong footprint across the globe, supplying to over 45 countries across six continents.

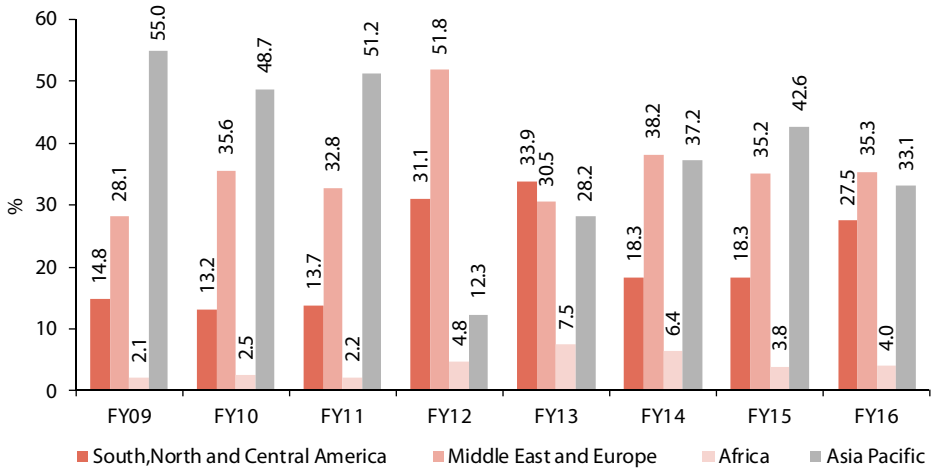
It has geographical presence in India, US and Europe. In 2009, the company set up a JV in Turkey with Gelal Corap San. Ve Tic. A.S under name 'SARLA TEKSTIL FILAMENT SANAYI ve TICARET A.S'. This will enable the company to service the customers in Europe and Turkey. The company also has a subsidiary in Portugal which markets its products to Europe and caters to customers regionally. Located at the western tip of Europe, Sarla Europe LDA is able to service customers in South America as well. Local employees help bridge language barriers, thus ensuring better reach to customers. Very few players operating in the European space for specialised yarns give Sarla an added advantage through its strong presence in the continent. The company also has distribution centres in Thailand and Vietnam.

Exhibit 9: Global Presence



Source: Company, Centrum Research

Exhibit 10: Turnover Break up (Geographical) (% of standalone export sales)



Source: Company, Centrum Research

High Entry Barrier

- Moulds form an integral part of the final product, with the company having more than 150 client-specific moulds.
- These are designed as per clients' specifications to fit the varied machinery used by them in their plants in different geographies.
- Clients' stickiness is due to quality and goodwill.
- Global brands demand consistent quality products across markets.
- Major overseas clients with long standing relationship built over the years.
- Multiple geographical presence.

Exhibit 11: Client-specific molds

Source: Company, Centrum Research

Case Study: Renfro Corporation

Sarla India has been the major supplier to Renfro India since 1995. Revenue contributed by Renfro grew steadily for many years. However, this has little or no correlation with credentials for supplying to its US parent – Renfro Corporation. Sarla Flex, Inc plans to sell its products from the US facility to the parent company – Renfro Corporation. Despite its track record of multiple decades in serving Renfro India, Sarla has to follow the regular process for empanelment as its preferred supplier. We believe getting empanelment/approvals from global vendors like Renfro Corporation is a big entry barrier.

Strong relationships with world's largest brands

To make a breakthrough into new businesses with key global players is one of the most challenging tasks in the textile sector. The company, through various initiatives, has successfully penetrated the global market and tied up with well-known brands like Jockey, Gildan, Renfro, Hanes, Delta Galil and Coats. This has given the company an opportunity to leap forward in the value chain by supplying

directly to end users, thus enhancing margins. Further, Sarla realises the need to maintain these relationships and in this regard has an enduring focus on providing best-in-class service, while also building its brand image and loyalty. Moreover, thrust is on minimising turnaround time for customers' enquiries, concerns or grievances.

The company believes that to establish customer confidence, the customer should be completely cognizant of the superior quality of products it manufactures. It consistently adheres to various methods of quality control, including rub fastness and wash fastness to ensure that the colour of the product does not rub into another fabric. Each finished cone of yarn is physically checked before being disseminated to the customer. A sample order is first sent to the customer for approval and only after it is verified/certified for 100% accuracy is the full order undertaken to ensure that the customer is satisfied with the quality, thus minimising wastage/dissatisfaction towards Sarla. With these sound practices, Sarla has been able to gain business from top international companies and supplies to their global locations.

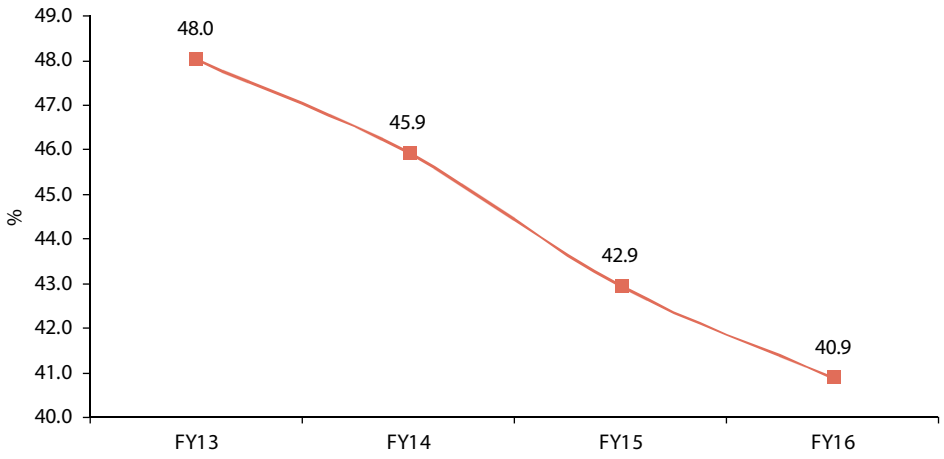
Sarla greatly emphasises on making its operations and business practices visible to the customer. It is one of the very few companies which encourage customers to frequently visit its plants so that they are comfortable about the quality of products manufactured and make a better informed decision.

Exhibit 12: Revenue contribution by TOP 5 customers (Standalone revenues)

Figures in INR million	Mar-13	%	Mar-14	%	Mar-15	%	Relationship
HANESbrands	179	*8*	221	*9*	234	*9*	5 to 10 Years
Vardhman	180	*8*	189	*8*	198	*7*	> 10 Years
RENFRO INDIA	105	*5*	153	*6*	182	*7*	> 10 Years
ARVIND	127	*5*	117	*5*	107	*5*	< 5 Years
Hung Fung Industries Company Limited	70	*3*	108	*4*	105	*4*	5 to 10 Years

Source: Company, Centrum Research

Exhibit 13: Revenue contribution by the TOP 10 customers (Standalone revenues)



Source: Company, Centrum Research

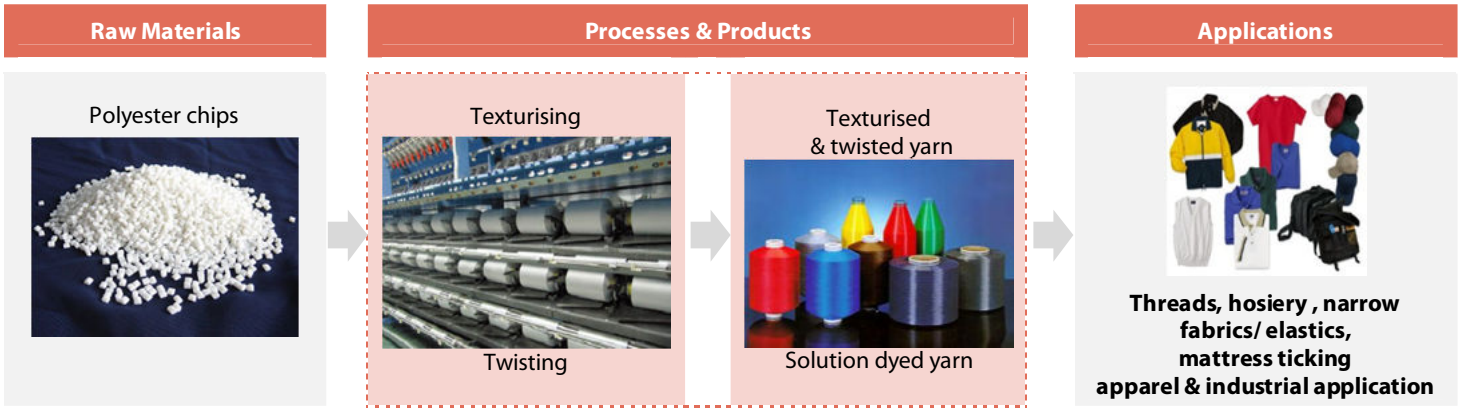
Exhibit 14: Global customers

Source: Company, Centrum Research

Strengthening foothold through expansion in US

In 2013, SPFL entered US markets through its 100% subsidiary Sarla Flex, Inc, which has an installed capacity of 9,900 TPA for POY and textured/twisted polyester yarn for end-use products such as apparel and Industrial, hosiery, threads, narrow fabrics/elastics and mattress ticking application. It was the first POY plant in the US since 1998 by any company. Because of free trade agreements and other trade regulations by the U.S. government, the U.S. textile industry, which is otherwise a distinctive geographic market on its own, is often considered in conjunction with other geographic markets or regions in North, South and Central America, such as the regions covered by either or both of NAFTA and CAFTA.

Exhibit 15: US manufacturing focused on general application products



Source: Company Presentation

Opportunity in the US market

- **Legal restrictions:** As per NAFTA and CAFTA laws, American apparel companies can source goods from US-based manufacturers if they want duty-free access for their garment in the US market.
- **Duty waiver:** Exporting to North and Central American countries is viable only for companies manufacturing locally in the regions as duties to the extent of 32% are waved off for them.
- **Greater visibility:** Proximity and visibility to customer would contribute significantly towards expanding and deepening customer relationships.
- **Demand boost:** Sarla expects to gain tremendous impetus after operations stabilise and with strong demand and marketing initiatives in place.
- **Higher realisation:** US prices are 55-70% higher than Asia/Far East which enhances profitability margins.

In addition, there are benefits like shorter lead time of ~6 weeks compared to 13-17 weeks in Asia from order to distributor, faster response to fashion trends and replenishment needs. Shorter lead time creates lower inventory and better cashflows.

Exhibit 16: Benefits of setting up plant in USA

Cost Component	Unit	India	US	Remarks
Raw materials	% of sales	>50%	<40%	Raw material cost as a % of sales is lower in the US than in India
Labour	$/hr	1.5	15	Labour costs are higher in the US than in India, but higher automation would reduce the same by 30%
Electricity	Rs/kWh	5	2.5	Electricity costs in the US are 50% of that in India
Borrowing cost	%	10-12% pa	3-5% pa	Borrowing cost in the US is one-third of that in India

Source: Company, Centrum Research

The savings in raw material cost, electricity and borrowing cost along with higher realisations in the US would result in higher profitability and return ratios. This will be the key driver of the overall profitability going forward.

Capacity utilisation at 20-25% range in near term

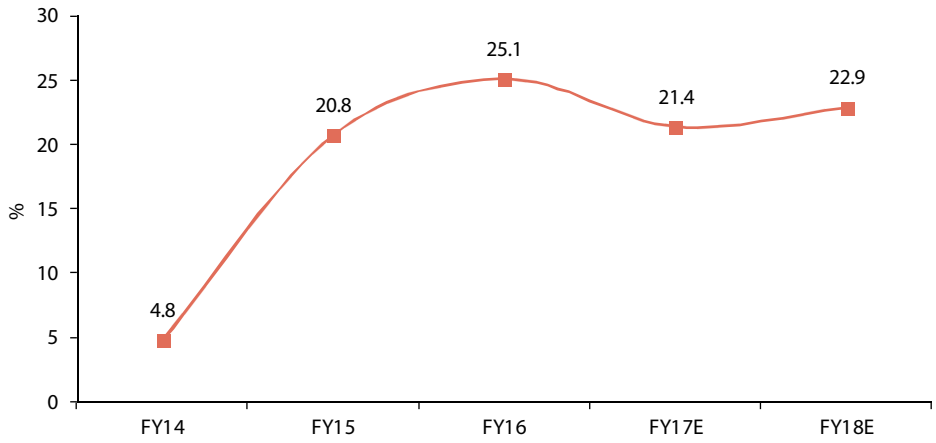
Within two years of starting operations the company has been able to scale up its operations to 25% capacity utilisation on the back of strong orders from clients such as Coats, Gildan, Pankti International, Standard Textile, American & Efrid etc. We expect the capacity utilisation to remain in 20-25% range by FY18. SPFL India is one of the well-established and niche players from India in the exports of regular as well as high-tenacity polyester and nylon yarns to the US. Management plans to use this as an entry strategy to target these customers with whom the company has had business relations for over a decade.

In order to scale up operation and further increase utilisation levels the management is targeting various end applications for its product range of yarns.

- **Hosiery/socks knitting** – Gildan & Renfro, two of the biggest sock knitters, have plants in Honduras and USA, respectively. Besides, Hanes brand has a large socks knitting facility in El-Salvador and USA. Management already has strong business relations with these companies for the past several years.
- **Circular knitting/weaving** – Large global brands like Fruit of the Loom, Russell, Hanes brands and Gildan have being moving more of their sourcing to Central America and reducing dependence on China. It is makes more commercial sense for these brands to increase their sourcing from these countries and take advantage of the duty-free access. A supply chain basically includes the yarn manufacturer, weaver or knitter and the garment sewing operation. Large South American Companies like Petenatti have also set up weaving and knitting operations in Central America and are actively looking to source CAFTA origin yarns to avail the duty-free status.
- **Narrow fabrics/elastics** – Asheboro Elastics, TESA, G.C. Moore and Narrowflex are some of the big elastics producers in Central America. Management has active business dealings with these companies.
- **Sewing threads** – American & Efrid (A&E) and Coats are the global leaders in this segment. They have large manufacturing facilities set up in Mexico, Honduras, Dominican Republic, Costa Rica for the dyeing, finishing and winding of sewing threads. Textured sewing threads are being increasingly used and preferred over spun polyester threads due to its inherent properties of stretch and elongation, especially in the sewing of knitted garments. Sarla, India has been dealing with these two global leaders for the past decade and Sarla Flex could be a strategic supplier to them from the US plant.

Any big order from any of the above clients can increase the capacity utilisation substantially while currently we are conservative in building utilisation at 20-25% range over next 2 years.

Exhibit 17: Steady increase in capacity utilisation



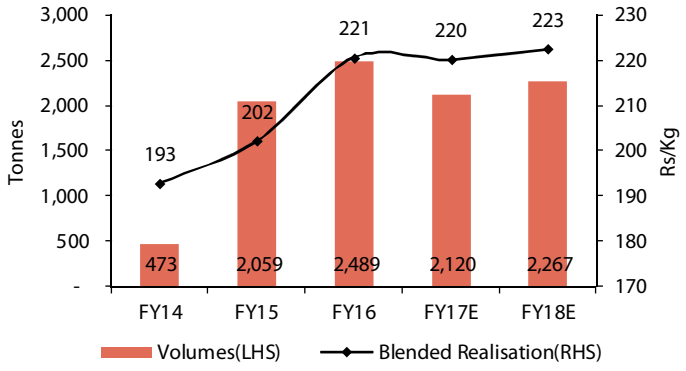
Source: Centrum Research Estimates

Expect cash breakeven in FY18E despite volumes remaining low

We have modeled a 4.5% CAGR decline in volumes over FY16-18E given highly competitive environment in the US market. The management also does not want to sell yarn to non-compliant CAFTA and NAFTA users or compete with imports from India or China into the US as these are non-compliant yarns. The strategy is to target customers who want compliant yarns, and for which they are able to pay a premium. Hence, the volume ramp-up would happen gradually.

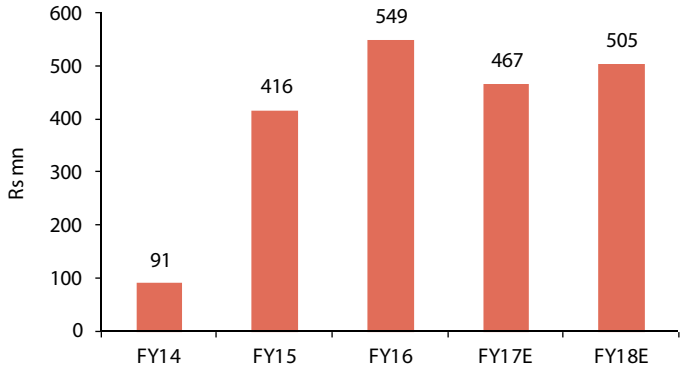
We believe a major order from an existing client would expedite the volume growth substantially. Despite a decline in reveneus over next 2 years, we believe company would be able to achieve cash breakeven in FY18E. We have modelled operating margin expansion from negative 7% in FY16 to positive 1.3% in FY18E on the back of operating leverage from employee expenses and fixed cost. We believe by FY18E, Sarla Flex would account for 14% of total revenues, 1% in operating profit on consolidated basis.

Exhibit 18: Blended volumes and realisations



Source: Company, Centrum Research Estimates

Exhibit 19: Revenue trend



Source: Company, Centrum Research Estimates

Sarla Flex operates at ~65% gross margins, with chips imported by JBF Industries, India and Recron, Malaysia. We believe other cost is highly fixed till ~50-60% capacity utilisation; hence, the company can achieve healthy margin expansion and profitability over next three years on the back of volume growth. We remain conservative and wait for traction in the business and hence have modelled operating profit of mere Rs7mn with a PAT loss of Rs39mn in FY18E.

Our sensitivity analysis suggest that Sarla Flex at 50% utilisation can operate at 24% operating margins and have peak margins upwards of 35% on healthy operating leverage at 70%+ utilisation. We believe the margins would be higher than standalone company margins in medium term and offer significant upside.

Exhibit 20: Sarla Flex Financials

Sarla US Financials (Rs Mn)	FY14	FY15	FY16	FY17E	FY18E
Sales	**91**	**417**	**549**	**467**	**505**
Growth %		*356.4*	*31.9*	*(15.0)*	*8.1*
COGS	32	148	205	166	177
Gross Profit	**60**	**268**	**344**	**301**	**328**
Gross margins %	*65.3*	*64.4*	*62.7*	*64.5*	*65.0*
Operating Profit	**(28)**	**(71)**	**(39)**	**(7.3)**	**6.7**
Operating Margin %	*(31.1)*	*(17.0)*	*(7.1)*	*(1.6)*	*1.3*
PAT	**(32)**	**(135)**	**8**	**(48)**	**(39)**
PAT Margins %	*(35.1)*	*(32.4)*	*1.5*	*(10.2)*	*(7.7)*

Source: Company, Centrum Reseaarch Estimates

Exhibit 21: Sensitivity at different capacity utilisation levels on financials of Sarla Flex (FY18E)

Capacity Utilisation (%)	*22.9(Base Case)*	*30.0*	*40.0*	*50.0*
Revenues (Rs Mn)	505	660	882	1,102
EBIDTA (Rs Mn)	7	72	170	262
EBIDTA Margins %	*1.3*	*10.9*	*19.2*	*23.8*
PAT (Rs Mn)	(39)	7	105	197

Source: Centrum Reseaarch Estimates

Phase-II of capacity expansion soon

This US facility is spread over 42 acres, with a constructed area of around 3.5 lakh sq. ft. Total cost incurred to acquire the land was approximately Rs40mn as the land was procured from the county which was a non-profit organisation. Hence, the company has enough space to double the capacity in the same facility. After capacity utilisation reaches ~60-70% with steady order flow from top clients, management would double its capacity to 18,000TPA. We believe the new capacity will come up in 2019/2020; however, it could be faster depending on the order flow.

Phase-I was funded through debt and internal accrual. The company took a debt of $12.87mn (cost of debt 1.38%) under the New Market Tax Credit (NMTC) scheme. As per the scheme, 70% of the amount would go back into an Investment Fund, while 30% will be written off after seven years. The 30% is similar to a capital subsidy received for setting up a project in an under-developed/backward area. For Phase-II expansion, with capex of ~$10mn, the company has already raised ~Rs450mn through QIP in FY15. The company would become net cash positive by the time the project would be on stream; hence, the company will not need to further raise funds.

Exhibit 22: US facility – Expansion plan

Further expansion of South Carolina facility

Expansion → **POY** → **Current capacity- 9,900 TPA** → **Capacity by 2019/2020 – 18,000 TPA**

New product addition – Flat yarn

Cost of project

USD mn	Phase I	Phase II	Total
Land	0.8	0	0.8
Building	1	1	2
Plant & machinery	9.4	9.25	18.65
Total plant & machinery	**11.2**	**10.25**	**21.45**
Pre-operative expenses	1.1	1	2.1
Working capital	1.5	2	3.5
Total current assets	**2.6**	**3**	**5.6**
Total cost of project	**13.8**	**13.25**	**27.05**
*The total cost projected is USD31mn			
* Cost of phase 1 already incurred			

- **Total cost of project – ~USD27mn**
- **Cost of Phase I already incurred**

Facility will directly cater to clients in North and Central American markets

Source: Company, Centrum Research

Exhibit 23: Competitors based on business segments

Company	Listing status	Products and services
Unifi	Listed	US-based Unifi is a multinational manufacturer and seller of polyester and nylon-textured yarns including high-volume commodity yarns, premium value-added yarns and other specialty yarns designed to suit customer preferences. The company has manufacturing units in the US, El Salvador, Colombia and Brazil and a sales office in China.
O'Mara, Inc	Private	The company manufactures polyester, nylon and other specialty yarns and has production units in the US.
NanYa Plastics Corp. of America	Private	A US-based manufacturer of polyvinyl chloride films, polyester fibre and ethylene glycol. It is a 100% subsidiary of Taiwan-based, Nan Ya Plastics Corporation.
Akra Polyester, S.A. de C.V.	Private	Based in Mexico (NAFTA region), the company manufactures and sells synthetic fibres and polyester yarns.
C S Central America S.A. de C.V.	Private	Based in El Salvador (CAFTA region), the company manufactures and sells polyester and nylon yarns.

Source: Company, Industry, Centrum Research

USA Market Profile

Apparel production is growing in the regions covered by the North American Free Trade Agreement (NAFTA) and the Central American Free Trade Agreement (CAFTA), which regions comprise the principal markets for the Company's Polyester Segments. The share of apparel production for these regions as a percentage of U.S. retail has stabilised at approximately 18% (Exhibit 29), while retail consumption has grown – especially for apparel made with synthetic yarns. The CAFTA region, which continues to be a competitive alternative to Asian supply chains for textile products, has maintained its share of synthetic apparel supply to U.S. retailers. The share of synthetic apparel versus cotton apparel has increased and provided growth for the consumption of synthetic yarns within the CAFTA region. The Company expects incremental growth into the foreseeable future, as retailers and brands maintain regional sourcing as part of their overall sourcing plans, retail sales grow, and consumer preferences continue to move from cotton to synthetic apparel.

The duty rate on imports into the U.S. of finished apparel categories that utilize polyester yarns generally range from 16% to 32%. For many years now, imports of fabric and finished goods into the U.S. have increased significantly from countries that do not participate in free trade agreements or trade preference programs, despite duties charged on those imports. The primary drivers for that growth were lower overseas operating costs, foreign government subsidization of textile industries, increased overseas sourcing by U.S. retailers, the entry of China into the World Trade Organization, and the staged elimination of all textile and apparel quotas. Although global apparel imports represent a significant percentage of the U.S. market, Regional FTAs (Exhibit 24), which follow general "yarn forward" rules of origin, provide duty free advantages for apparel made from regional fibers, yarns and fabrics, allowing the Company opportunities to participate in this growing market.

Exhibit 24: NAFTA/CAFTA

NAFTA	CAFTA
North American Free Trade Agreement (NAFTA) is a comprehensive trade agreement that sets the rules of trade and investment between the USA, Canada and Mexico. Since the agreement came into force on 1 January 1994, NAFTA has systematically eliminated most tariff and non-tariff barriers to free trade and investment between the three NAFTA countries.	Central America Free Trade Agreement (CAFTA) is an expansion of NAFTA to five Central American nations (Guatemala, El Salvador, Honduras, Costa Rica and Nicaragua) and the Dominican Republic.
How US textile and apparel companies benefits: Under the NAFTA, the US textile and apparel exporters benefit from duty-free entry on all qualifying products into Canada and Mexico, the two largest export markets for US textile and apparel products. NAFTA promotes opportunities for US fibre, textile and clothing manufacturers to expand sales and increase production to make full use of economies of scale and leverage complementary resources in the three countries to enhance export potential.	**How US textile and apparel companies benefits:** Prior to the CAFTA, tariff rates in the CAFTA-DR region on textile exports were as high as 18%. Under the CAFTA-DR, US exports of textiles are now duty-free, providing the fabric, yarn and thread manufacturers with the benefits of permanent and expanded duty-free trade.
Trade barrier elimination: NAFTA phased out all duties on textile and apparel goods within North America, meeting specific NAFTA rules of origin (for most products, the rule of origin is 'yarn forward', which means that goods must be produced from yarn made in a NAFTA country to benefit from preferential treatment) over a 10-year period. Prior to NAFTA, 65% of US apparel imports from Mexico entered duty-free and quota-free regions and the remaining 35% faced an average tariff rate of 17.9%. Mexico's average tariff on US textile and apparel products was 16%, with duties as high as 20% on some products.	**CAFTA-DR has state-of-the-art rules of origin**: Yarn-forward rule – A 'yarn-forward' rule ensures that virtually all of the textile and apparel items covered by the FTA utilise US or regional inputs. New Benefits for Thread and Elastics: For the first time in a free trade agreement, the CAFTA-DR requires thread and narrow elastic fabrics to originate from the region. As in past agreements, there is a provision to ensure the visible linings originate from the region.
Export highlights: US firms exported a total of $23.7 billion in textiles and apparel in 2015, including $6.5 billion to Mexico and $5.25 billion to Canada. Together, NAFTA partners account for 50% of total US exports of textiles and apparel.	**Exports highlights:** Central America is the second largest (after NAFTA) US textile export market in the world. The US exported $3.32 billion worth of textiles and apparel to the CAFTA-DR region in 2015. Together, CAFTA partners account for 14% of total US exports of textiles and apparel.

Source: Company, Centrum Research

Exhibit 25: US exports to world

US exports ($ mn)	2014	2015	YoY Change (%)	January-July 2015	January-July 2016	YoY Change (%)
World						
Yarn	5,249	4,911	*(6.4)*	2,933	2,648	*(9.7)*
Fabric	9,253	9,041	*(2.3)*	5,379	5,001	*(7.0)*
Made-up	3,792	3,677	*(3.0)*	2,154	2,045	*(5.1)*
Apparel	6,125	6,108	*(0.3)*	3,541	3,240	*(8.5)*
Total	**24,419**	**23,737**	***(2.8)***	**14,007**	**12,934**	***(7.7)***

Source: U.S. Department of Commerce, Office of Textiles and Apparel.

Exhibit 26: US imports of synthetic apparel ($ mn)

US imports ($ mn)	2013	2014	2015	YoY Change (%)	YTD May 2015	YTD May 2016	YoY Change (%)
NAFTA	1,456	1,528	1,544	*1.1*	649	631	*(2.7)*
CAFTA	3,088	3,321	3,516	*5.8*	1,303	1,408	*8.1*

Source: U.S. Department of Commerce, Office of Textiles and Apparel.

Exhibit 27: U.S. Exports to NAFTA region

US exports ($ mn)	2014	2015	YoY Change (%)	January-July 2015	January-July 2016	YoY Change (%)
NAFTA						
Yarn	**1,097**	**1,086**	*(1.0)*	**661**	**580**	*(12.3)*
Fabric	5,214	5,280	*1.3*	3,128	2966	*(5.2)*
Made-up	2,337	2,219	*(5.0)*	1,291	1283	*(0.6)*
Apparel	3,156	3,172	*0.5*	1,862	1580	*(15.1)*
Total	**11,804**	**11,757**	***(0.4)***	**6,942**	**6,409**	***(7.7)***

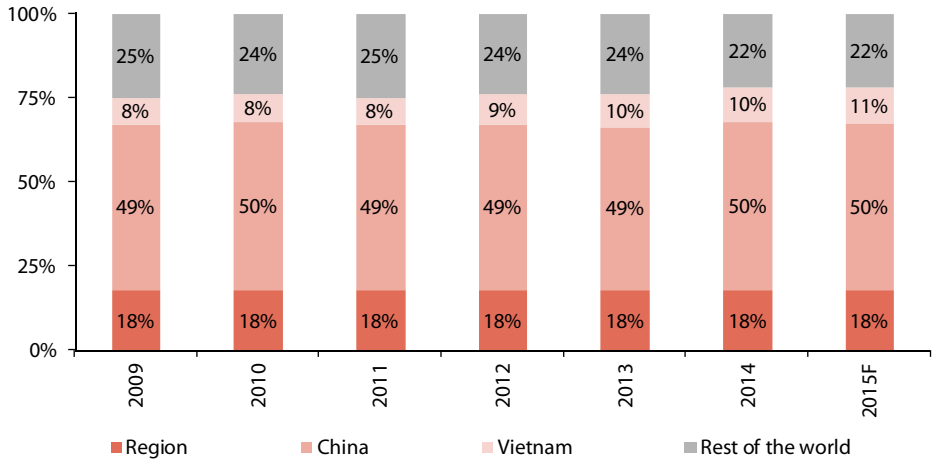
Source: U.S. Department of Commerce, Office of Textiles and Apparel.

Exhibit 28: U.S. Exports to CAFTA region

US exports ($ mn)	2014	2015	YoY Change (%)	January-July 2015	January-July 2016	YoY Change (%)
CAFTA-DR						
Yarn	**1,723**	**1,643**	*(4.6)*	**997**	**900**	*(9.7)*
Fabric	964	964	*0.0*	561	524	*(6.6)*
Made-up	109	123	*12.8*	73	58	*(20.5)*
Apparel	501	591	*18.0*	330	335	*1.5*
Total	**3,297**	**3,321**	*0.7*	**1,961**	**1,817**	***(7.3)***

Source: U.S. Department of Commerce, Office of Textiles and Apparel.

Exhibit 29: US synthetic apparel consumption share



Source: Otexa, Census Bureau, DOC, Federal Reserve

Case Study of Unifi, Inc

Company background

Established in 1969 and headquartered in Greensboro, NC, Unifi, Inc. is a multinational that manufactures and sells polyester yarn, nylon-textured and covered yarns and related raw materials. The company processes and sells high-volume commodity yarns, premium value-added (PVA) yarns and other customised specialty yarns. Unifi operates 10 manufacturing plants located in the US, El Salvador, Colombia and Brazil. The company has also entered into JV/affiliations in Israel and the US.

Business segments

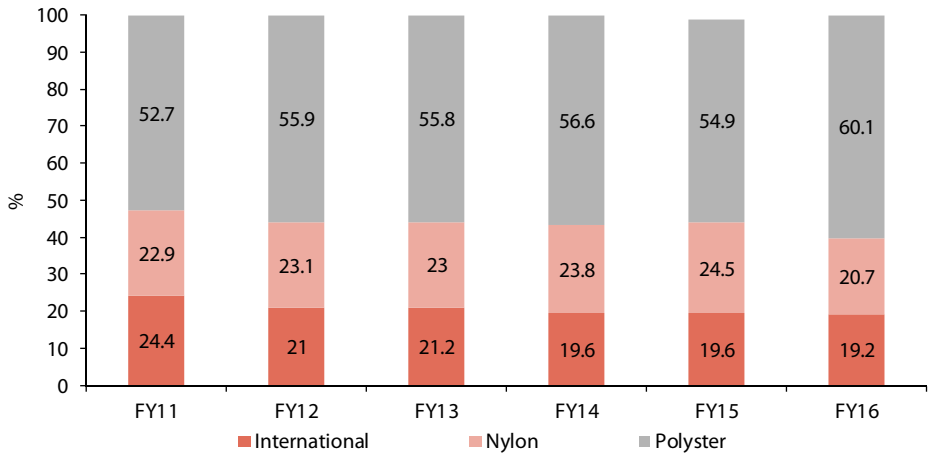
Unifi conducts business through three main segments: polyester, nylon and international. Apart from these, the company's 34% ownership in Parkdale America, LLC contributes substantially to its bottom line.

Exhibit 30: Unifi's business segment

Segments	Products	Revenue contribution as on FY16	Manufacturing sales location	Key suppliers
Polyester	Polyester chips, POY, textured, dyed, twisted, beamed and draw wound yarns	60.1%	US and EL Salvador	NanYa Plastics Corp. of America
Nylon	Textured, solution-dyed and covered spandex yarns	20.7%	US and Colombia	HHNF Fibers ltd, U.N.F. Industries ltd, UNF America, LLC, Invista S.a.r.l and Universal Premiere Fibers
International	Textured polyester and various types of resale yarns and staple fibre	19.2%	Brazil (manufacture and resale) & China (only sales office)	Reliance Industries Ltd

Source: Company, Centrum Research

Exhibit 31: Segment-wise revenue break up

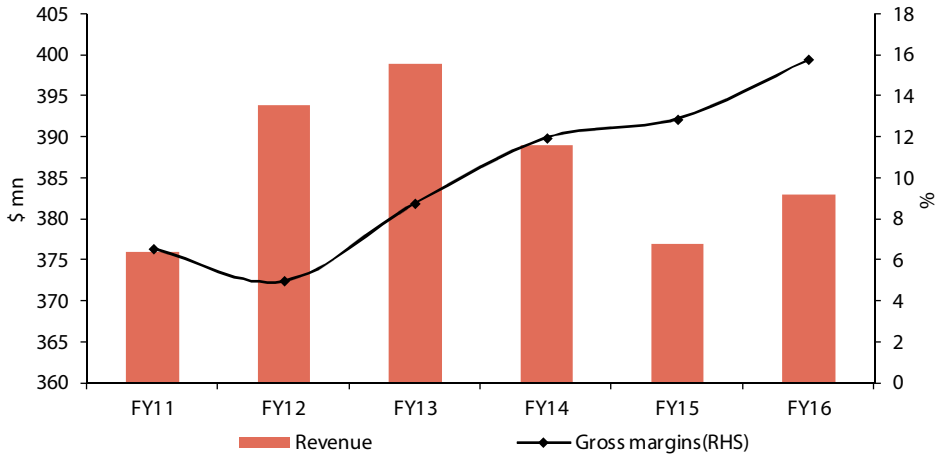


Source: Company, Centrum Research

Polyester

The Polyester segment manufactures chip, POY, textured, dyed, twisted, beamed and draw wound yarns, both virgin and recycled, with sales primarily to other yarn manufacturers and knitters and weavers that produce yarn and/or fabric for the apparel, hosiery, automotive upholstery, home furnishings, industrial and other end-use markets. The Polyester segment comprises sales and manufacturing operations in the US and El Salvador.

Exhibit 32: Polyester Revenue & Gross margins trend



Source: Company, Centrum Research

Exhibit 33: Financials for Unifi

USD mn	FY11	FY12	FY13	FY14	FY15	FY16
Net sales	**713**	**705**	**714**	**688**	**687**	**644**
Gross profit	75	54	73	83	91	94
Gross profit margins (%)	*10.5*	*7.7*	*10.2*	*12.1*	*13.2*	14.5
Selling, general & administrative expenses	45	44	47	46	50	41
Operating income	**29**	**9**	**23**	**32**	**39**	**45**
Operating margins (%)	*4.0*	*1.2*	*3.1*	*4.6*	*5.6*	6.9
Net income	**25**	**12**	**17**	**29**	**42**	**34**

Source: Company, Centrum Research; Note: Y/E June

Only company to manufacturer Nylon 66 in India

We believe the management has extended its philosophy of entry into niche market, high entry barriers, high margin product, low capex, and product synergies with existing clients in Nylon 66. Post successful commercial manufacturing of Nylon 66 yarn at Silvassa in Q3FY16 (pilot started in 2013), management plans to expand the capacity to 1,500TPA from current 450TPA in FY18, with an incremental capex of Rs100mn (initial capex of Rs100mn) having revenue potential of Rs600mn. Nylon 66 is a high-tenacity and lower shrinkage yarn product, extremely specialised and high-margin generating product used in parachutes, shoes, seat belts and car airbags, specialised sewing applications in automotive, shoes, leather, industrial filters and hoses.

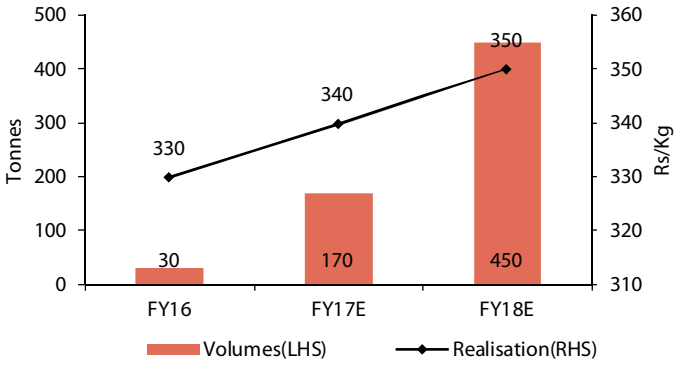
The company plans to achieve breakthrough with existing key customers (Vardhaman and Coats) and replace current imports in India. Currently, the two main customers in India import about 1,500 tons of Nylon 66. Thus, management will focus on these two customers that are purchasing other products from Sarla, in addition to sales to its existing clients in Spain.

We have modelled revenues of Rs158mn in FY18, with 28% capacity utilisation on expanded capacity. We believe the new capacity could come in H2FY18. Currently, the company has mere ~7% capacity utilisation, with revenues of Rs10mn which would increase to Rs58mn in FY17E. Operating margins in this product are ~35%.

Exhibit 34: Uses of Nylon 66

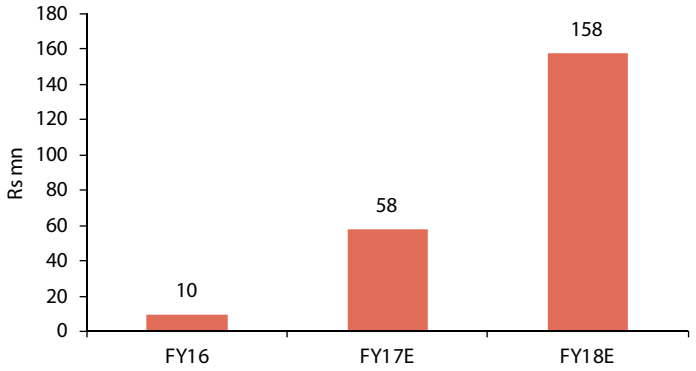
Source: Company, Centrum Research

Exhibit 35: Volumes & realisations trends



Source: Company, Centrum Research Estimates

Exhibit 36: Total revenues



Source: Company, Centrum Research Estimates

Financials

Healthy sales growth on the back of the domestic sales

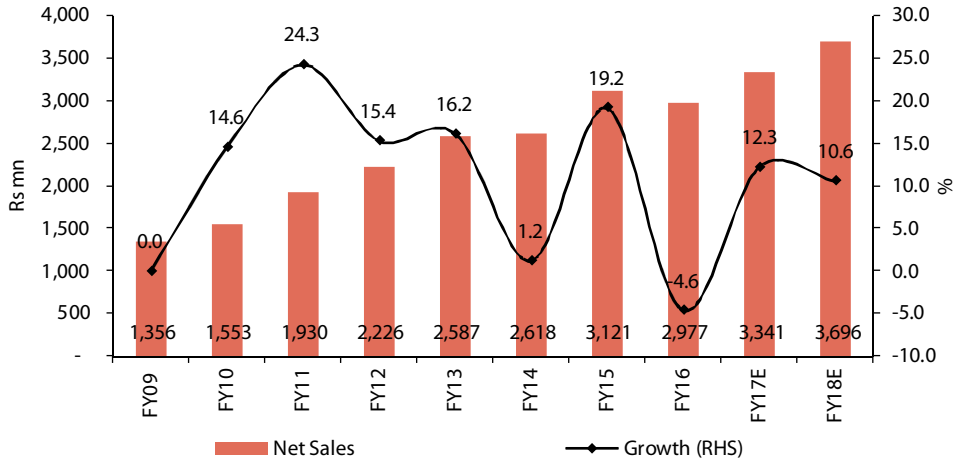
We expect the company to post revenue CAGR of 11.4% to Rs3,696mn over FY16-18E as against mere 4.8% over FY13-16. We believe the incremental revenue growth would be on the back of healthy growth in the standalone company despite Sarla Flex expected to post a decline of 4% over FY16-18E and would account for 14% of total revenues against 18% in FY16.

Standalone revenues for the company would grow at a CAGR of 12% over FY16-18E to Rs3,053mn. In FY16, the company posted 8.8% fall in revenues as trading revenues declined by Rs187mn, which is less than 2% margin business. Nylon 66 sales would see an exponential growth from mere Rs10mn in FY16 to Rs158mn in FY18E.

The company has de-bonded its Vapi unit from 100% EOU to domestic unit. With this move, the company would be able to garner ~8% duty drawback on exports (~Rs550-600mn) from the Vapi unit. However, the company would also pay higher excise duty (~14%) on domestic sales from the Silvassa unit, while the Vapi unit would not need to pay any excise duty for its sales as the input is duty paid. Hence, led by de-bonding of the Vapi unit, the company would save ~Rs20-25mn in incremental revenues. We believe bulk of the volume growth in the standalone company is on back of domestic sales.

The company is fully hedged despite garnering ~70-75% export billing in USD, 20% in Euro and less than 5% in Pound. The company had large import of RM and debt in foreign currency, while it also used PCFC loans for execution of the orders.

Exhibit 37: Revenue CAGR of 11.4% over FY16-18E



Source: Company, Centrum Research Estimates

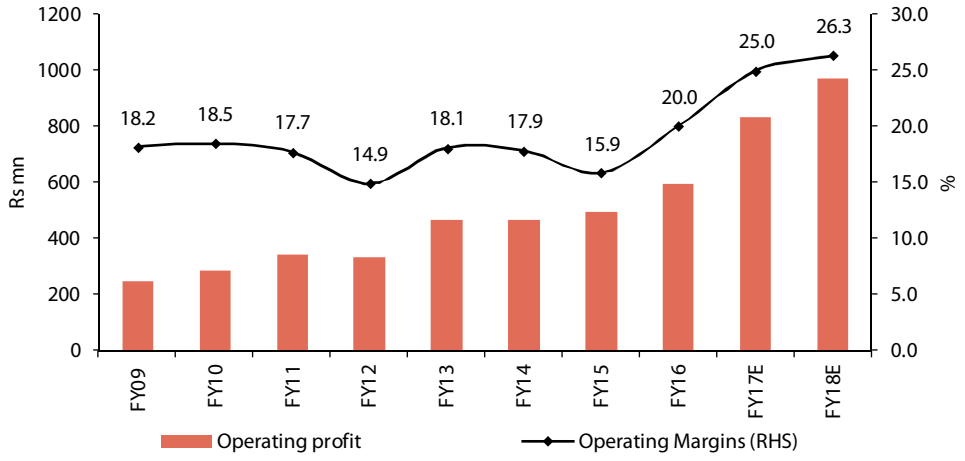
Steady margin expansion leading to 27% CAGR in operating profits

We believe operating profit for the company would grow at a CAGR of 27% over FY16-18E to Rs972mn against a CAGR of 13% over FY13-16. We believe the CAGR in the standalone company would be 28% on the back of 1) incremental revenues from wind turbine which have more than 95% margins, 2) Duty drawback and 3) core business having margin expansion on product mix change.

We have modelled gross margin expansion to 55.3% in FY18E from 51.8% in FY16 in the standalone company. Along with this, the company would have low overhead cost and power cost savings as it has started to buy power from energy exchange and has a benefit of Rs0.5p/unit in the Silvassa plant. Nylon 66 has 30-35% operating margin which is driving revenue growth with lower share from trading activity.

US subsidiary, Sarla Flex, which was loss making in the last three years, is expected to post a strong turnaround in the business over next three years from an operating loss of Rs39mn in FY16 to operating profit of Rs7mn in FY18E on the back of high fixed-cost model. We believe the company would not need to increase manpower till it achieves capacity utilisation of ~50%, while other expenses would remain under check. Hence, margins for the US business would be ~2% from current loss.

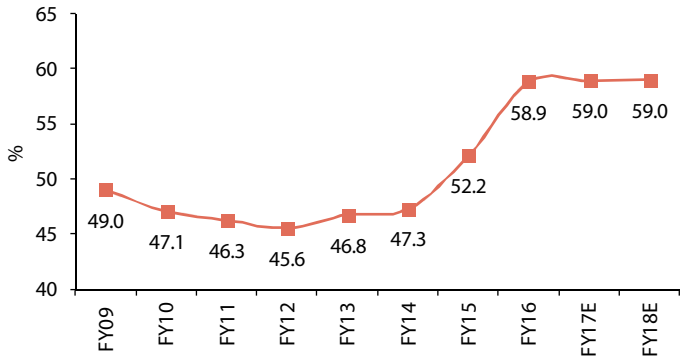
Exhibit 38: Operating profit and margins trends



Source: Company, Centrum Research Estimates

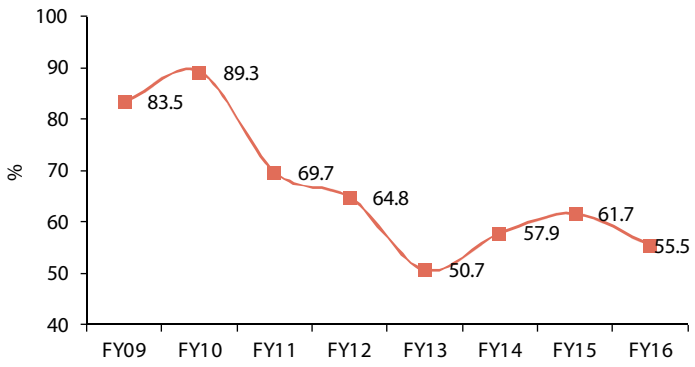
We have modelled gross margin expansion for the company on product mix change and entry into high-margin products, leading to gross margins of ~60% by FY18E on consolidated basis. Currently, POY accounts for ~48% of the total raw material which is bought from players such as Indo Rama Synthetic, Reliance Industries and Filatex. Nylon is purchased from Recron, Malaysia which is ~37% of raw material cost while Nylon chips are bought from Taiwan and account for 11% of the total RM cost. The company imports ~60% of the total RM. Typically, any change in RM prices higher than ±5% is passed on to the clients; hence, the company is not dependent on RM price volatility.

Exhibit 39: Gross Margins trend



Source: Company, Centrum Research Estimates

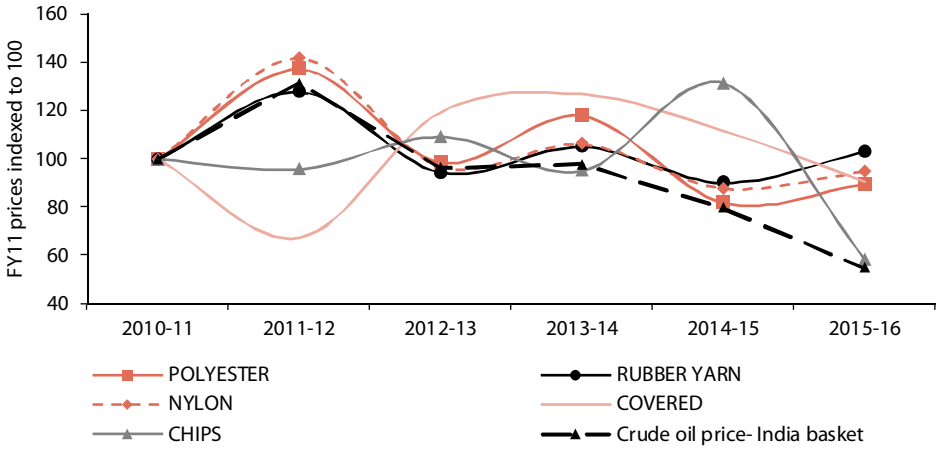
Exhibit 40: Imported % of RM consumption



Source: Company, Centrum Research

There is little correlation of RM prices to crude as seen in the chart.

Exhibit 41: Average prices for RM and its relation to crude prices



Source: Company, Centrum Research Estimates

Investment in wind turbine to save taxes

Over the years, the company has invested in the wind turbine to save taxes. Over the last six years, the company has ~10MW of wind turbine, while it is proposing to invest further in a 6MW plant, taking the total installed capacity to 16MW with a total capex of Rs1.06bn. Capex per MW is ~Rs60mn. Over the years, the company has financed the wind turbine business through 2:1 or 3:1 D/E. Given 80% depreciation in the wind turbine business, it makes economic sense to invest in this business. However, with the change in income tax, this benefit would be only till FY17, and going forward, the depreciation would be 40%. Coupled with this, the company does not need to pay income tax for 10 years out of 15 years, making the investment even sweeter.

The company has long-term contracts for these plants which are currently having ~22-25% PLF. They outsource maintenance to a third party and garner around ~95% operating profit. Revenue is typically ~8mn/MW/year.

We believe the payback from the proposed wind turbine would be five years, factoring in the new income tax laws from the second year. Also, the RoE on this business would be in double digits against the 6-8% yield if the company invests this amount in liquid debt funds. These wind turbine assets are highly tradable and would give immediate liquidity to the company if they would need cash for any eventuality.

Exhibit 42: Wind turbine business

Place	Year of commissioning	Capacity(in MW)
Baradiya, Gujarat	FY10	1.25
Satara, Maharashtra	FY11	2
Sangli, Maharashtra	FY13	4
Ratlam, MP	FY16	3
Proposed	FY17E	6
Total installed capacity		**16.25**
Total cumulative capex (Rs bn)		**1.06**

Source: Company, Centrum Research Estimates

Exhibit 43: Five-year payback in the new proposed 6MW wind turbine

Tax saving	Year 1	Year 2	Year 3	Year 4	Year 5
Depreciation -80% for Year 1, 40% later	288	29	17	10	6
tax saving @34%	98	10	6	4	2
Revenues – Power	48	48	48	48	48
Total	**146**	**58**	**54**	**52**	**50**

Source: Company, Centrum Research Estimates

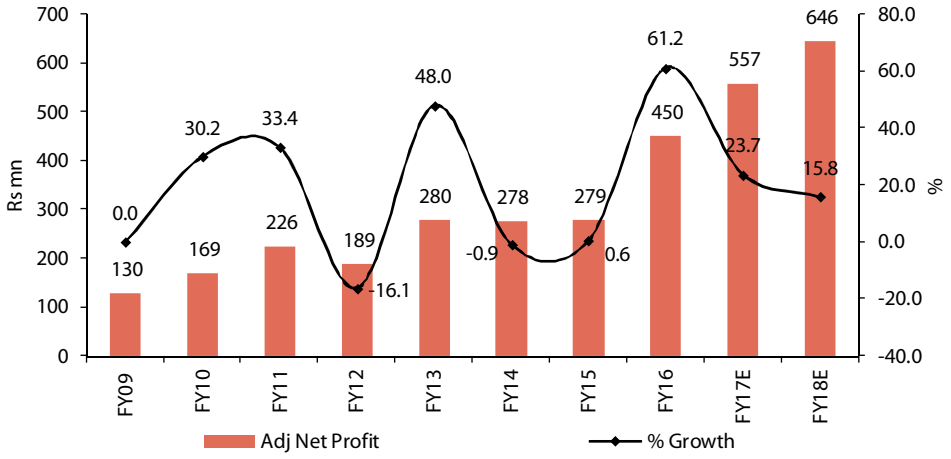
PAT to grow at a CAGR of 20% over FY16-18E

We have modelled PAT CAGR of 20% over FY16-18E on a consolidated basis to Rs646mn against a CAGR of 27% over FY14-16. We believe strong growth in operating profit and margin expansion would translate into profitability.

Currently, the company does not pay any tax in its subsidiaries as they are exempted. All the tax is paid in the standalone company. We have modelled ~25-26% tax rate for the standalone company over next two years. While the tax rate would be lower in FY17 as the company would be under MAT since they have invested in wind turbine, deferred tax liability would increase the tax rate. On consolidated basis, this translates into tax rate of ~20%. In FY16, the consolidated tax rate was 11% since the company had deferred tax benefit of Rs65mn in its US subsidiary.

We have modelled other income of Rs120-130mn over next two years against Rs130mn in FY16 since the company would generate high cash flows over the next two years. We believe the commission income that the company garnered in SOHL and custom duty drawback in the US subsidiary will decline going forward.

Exhibit 44: Adjusted net profit and growth trend

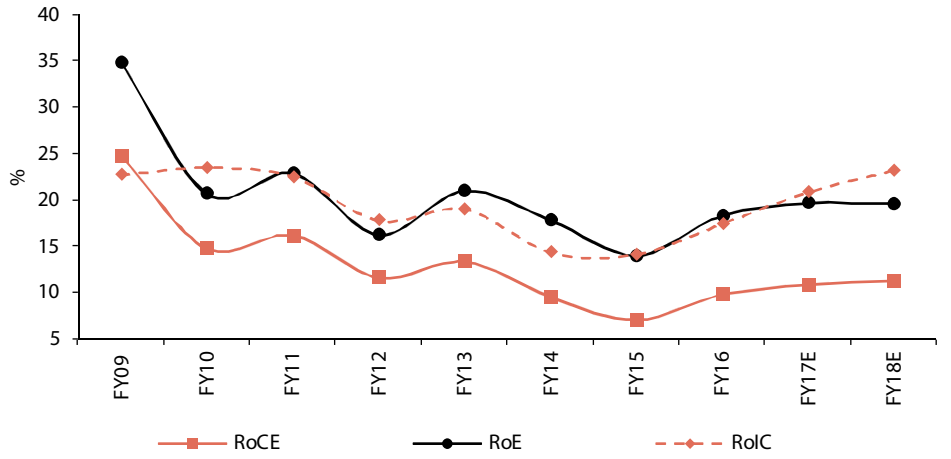


Source: Company, Centrum Research Estimates

ROE to rise going forward

We believe the return ratios for the company would slowly inch upwards, with RoE jumping upwards of ~20% over next two years with healthy profitability, while RoCE would increase to low teens despite high investments in the wind turbine business. We believe the low incremental capex and high cash on books, RoIC would touch 23% by FY18E.

Exhibit 45: Return ratio trend



Source: Company, Centrum Research Estimates

Exhibit 46: DuPont Analysis

	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E
PAT/Sales (x)	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2
Sales/Assets (x)	1.2	1.3	1.2	1.1	0.8	0.7	0.6	0.6	0.6
Assets/Equity (x)	1.5	1.5	1.6	1.8	2.2	2.3	2.1	2.0	1.9
RoE (%)	***20.7***	***22.8***	***16.3***	***21.0***	***17.8***	***14.0***	***18.3***	***19.7***	***19.6***

Source: Company, Centrum Research Estimates

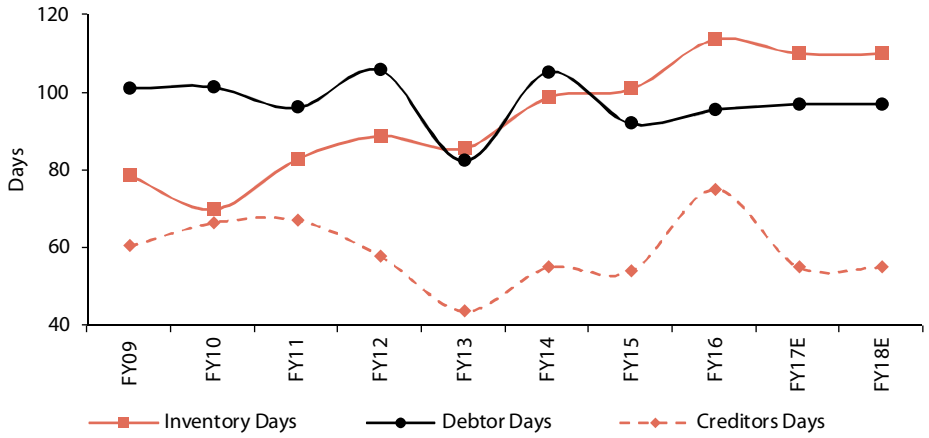
Working capital to remain under check

We believe the company's working capital days would remain under check, with inventory days at ~110 days. Typically, the company manufactures products upon receipt of orders, which are highly client specific. In the domestic business, the three large clients (like Hanes) place order on a quarterly basis wherein the company needs to maintain minimum inventory in transit, at warehouse and some in manufacturing. Vardhaman places orders on a monthly basis and Coats places orders on quarterly basis. In the US operations, the company needs to maintain RM inventory which increases the overall inventory.

Debtor days would be 95-100 days, while on standalone basis, it is ~75 days. As per our conference call with the marketing personnel in Portugal, SPFL takes order only if the client gives orders through Letter of Credit for which the company sometimes does bill discounting. This lowers the probability of bad debt.

Creditor days are expected to be ~55 days. In FY16, creditor days increased to 75 days as the company had to pay for the 3MW wind turbine; the payment to be done in FY17 instead of Q4FY16. Hence, it would stabilise at 55 days on consolidated basis, while on standalone basis, it would remain low at 30 days as the company is willing to take discount on cash payments given high liquidity on books.

Exhibit 47: Working capital days

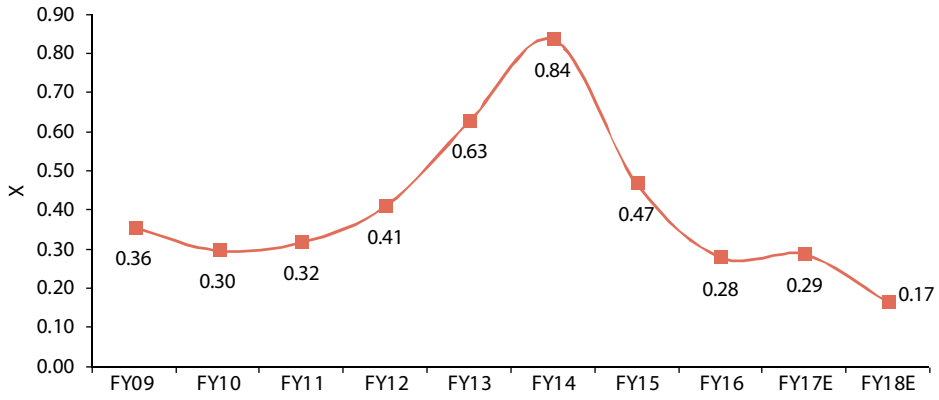


Source: Company, Centrum Research Estimates

Debt likely to remain low

We believe net D/E for Sarla would reduce going forward on strong cash flows and healthy profitability. The company requires incremental debt only for the wind turbine capex, but not for its regular business. The company has sufficient cash on books for Phase-II expansion in the US subsidiary. Of the consolidated debt, 40% is short term in nature; of the long-term debt, Rs600mn is under NMTC against which the company has outstanding investments of the same value. Hence, excluding the same, the actual long-term debt is marginal in the company. Bulk of the debt is earmarked for power business, while for the incremental power business, we believe the company will fund it in D/E ratio of 2:1 wherein it would borrow against fixed deposit as it comes under priority sector lending; hence, the company would still make ~1% spread.

Exhibit 48: Net debt to equity to reduce further

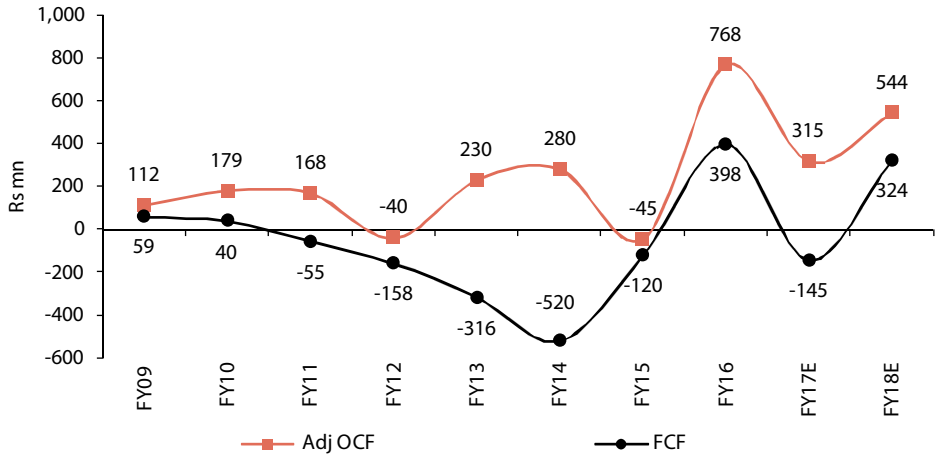


Source: Company, Centrum Research Estimates

Low capex and steady WC leads to healthy cash flows

We have modelled a capex of Rs680mn over the next two years; of this, Rs360mn is for 6MW wind turbine and Rs100mn capacity expansion for Nylon 66, while the remaining would be maintenance capex and machinery upgradation. Working capital would remain stable while the company would have low tax in cash flows on the back of investments in wind turbine. Hence, the cumulative adjusted OCF over next two year would be Rs858mn, while FCF generation would be Rs178mn. We believe, historically, the company has always been adjusted OCF positive with the management focus on low debtors and inventory. With capex intensity behind we expect the FCF generation to be strong going forward. Over the last eight years, the company has had capex of Rs2.3bn, of which Rs0.7bn is on wind turbine, ~Rs0.6bn on the US subsidiary, some in overseas subsidiaries and remaining in the domestic business.

Exhibit 49: OCF & FCF generation

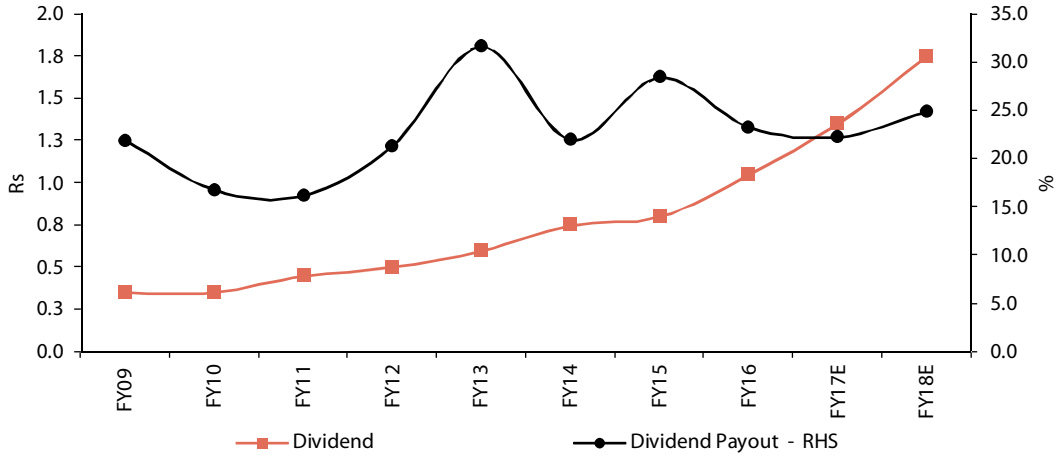


Source: Company, Centrum Research Estimates

Dividend payout to remain healthy

Over the last decade, management has always steadily increased the absolute dividend, which has increased from low of Rs0.35/share to Rs1.05/share in FY16. We expect the same to increase going forward given high cash flow generation and low capex requirement. We believe the dividend payout would be ~25% of the standalone profits as the US subsidiary was loss making. However, the dividend payout could increase further after the profitability of the subsidiary increases substantially.

Exhibit 50: Steady increase in dividend



Source: Company, Centrum Research Estimates

Exhibit 51: Common Size – Standalone business

Key Expense Breakup (Standalone)	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16
Revenue	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Raw Material	53.7	44.4	55.8	55.6	49.6	51.7	45.0	45.6
Traded Goods	1.2	7.7	2.2	4.2	5.0	5.3	11.1	4.8
(Increase)/Decrease in inventories	(2.4)	0.8	(3.1)	(4.2)	(1.3)	1.0	(2.0)	(2.2)
Total RM Cost	52.5	52.9	54.8	55.6	53.3	58.0	54.1	48.2
Gross Margin	47.5	47.1	45.2	44.4	46.7	42.0	45.9	51.8
Employee Cost	1.8	1.9	2.2	2.3	2.1	2.5	2.9	3.4
Power and Fuel	7.0	7.0	5.9	6.4	5.4	5.4	5.4	6.0
Other Operating expenses	11.2	11.0	10.3	11.4	12.5	8.2	9.6	9.5
EBIDTA Margin	16.4	17.2	15	13.1	16.3	15.3	16.9	20.6

Source: Company, Centrum Research Estimates

Exhibit 52: Common size – Consolidated business

Key Expense Breakup (Consolidated)	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16
Revenue	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Raw Material	51.9	42.0	50.6	52.5	47.0	49.3	43.8	41.3
Traded Goods	2.2	10.8	7.8	7.6	7.4	5.6	9.1	3.2
(Increase)/Decrease in inventories	(3.1)	0.1	(4.6)	(5.7)	(1.2)	(2.2)	(5.1)	(3.4)
Total RM Cost	51.0	52.9	53.7	54.4	53.2	52.7	47.8	41.1
Gross Margin	49.0	47.1	46.3	45.6	46.8	47.3	52.2	58.9
Employee Cost	1.7	1.7	2.1	2.2	2.0	4.6	8.7	7.2
Power and Fuel	6.3	5.9	4.8	5.3	4.9	5.4	6.5	7.2
Other Operating expenses	12.8	12.4	11.8	13.5	12.2	8.8	9.9	10.7
EBIDTA Margin	18.2	18.5	17.7	14.9	18.1	17.9	15.9	20.1

Source: Company, Centrum Research Estimates

Exhibit 53: Sensitivity Analysis

Sensitivity to key variables (FY17E)	*% increase*	*% impact on EBITDA*	*% impact on EPS*
RM cost	*1.0*	*(1.6)*	*(3.0)*

Source: Company, Centrum Research Estimates

Valuation

We look at different valuation methods to value the company.

PE method: The company does not have high other income as percentage of PBT; it is a full tax-paying company on standalone basis and has no one-off to boost profitability. Hence, we look at PE method to value the company. Average PE is 9x (FY18E) for the textile sector where the companies have low debt, exposure to global and domestic market, double-digit margins and high return ratios (Exhibit 58). Global peers like Unifi trade at 12x for FY18E. While we believe SPFL could trade at marginal premium to domestic peers and marginal discount to Unifi given the low scale of operation, we remain conservative and value the company at Rs77/sh, 10x FY18E EPS of Rs7.7.

EV/EBIDTA method: Given that the textile sector has been plagued by high debt, we also consider EV/EBIDTA method to value the company. Average EV/EBIDTA multiple for domestic textile stocks is 5.5x. Global player like Unifi is trading at ~8x FY18E EV/EBIDTA. We believe given low debt and interest cost, SPFL should trade at higher multiple to domestic peers and marginally lower to Unifi. However being conservative, we value the company at 7x FY18E EV/EBIDTA and arrive at a value of Rs75/sh.

Cash flow method: We believe the real operating earnings is captured in adjusted OCF as it is the earnings on which the management has complete flexibility in terms of the proportion of capital allocation and towards reinvestment for growth/dividend payout/payback of debt/retaining earnings for future use. The valuation tool AOCF/EV yield (%) values the company on an enterprise value basis, which, in turn, is derived from its real operating earnings. This, we believe, captures the company's value based on its real earnings versus reported earnings. We further average the AOCF on a five-year basis to arrive at the normalised cash flow of the company which helps reduce the peaks and troughs and reveals real earnings that the company is likely to generate on an average basis. Further, we analyse the trend of four-year average AOCF/EV yield (%) on a long-term basis which helps us understand the range in which the yield (%) has moved. On the basis of this range, we determine the multiple for future equity value of the company. We note that average AOCF/EV yield stands at 4.9% for SPFL and hence the implied EV/AOCF multiple of 20.4x. We use average AOCF over FY14-18E and 20.4x EV/AOCF multiple to arrive at our target EV and our TP of Rs83/sh.

Exhibit 54: Target price calculation

4 Year average Adj. OCF Yield (AOCF/EV) - % (FY13-16)	4.9
Implied EV/AOCF Multiple (x)	20.4
Average Adj. OCF (Rs mn) - FY14-18E	372
Target EV (Rs mn)	7,536
Less: Net debt (FY18E)	(585)
Target market cap (Rs mn)	6,951
No. of shares (mn)	83.5
Target Price/share (Rs)	**83**

Source: Company, Centrum Research Estimates

We believe premium multiple should be assigned to SPFL compared to domestic players over long run for following reasons:

Unique and niche business model: SPFL manufactures specialised yarn on client-specific requirements only and has the ability to manufacture small quantities used in niche applications. Client-specific value addition on 1) moulds, 2) denier difference, 3) variation in twists and 4) colours further enables the company to move up the value chain and command higher margins. We believe very few players have the ability to replicate the same.

Cash breakeven in US subsidiary - Sarla Flex: We expect the US subsidiary to turn around in FY18E on tight control on costs. We believe any major client win could turn the company's fortune and take it to the next higher level of growth and profitability. Management's prudent expansion plan is also a positive.

Operating margin – one of the best in textile industry: We believe over the next two years the operating margins for the company would be one of the best in the Indian textile industry, led by healthy gross margins, turnaround in the US subsidiary, new products such as Nylon 66 and prudent investment in the wind turbine.

Healthy cash flows and return ratios: We expect the OCF and FCF to remain healthy over next two years with low capex in the core business. Hence, strong margin expansion and profitability would lead to ~20% RoE for the company over next two years. Turning FCF positive in FY18E is an added positive in a sector where most companies are highly leveraged.

Sarla Flex offers Rs27/sh upside to our Target Price at 50% capacity utilisation

We believe with increasing capacity utilisation for Sarla Flex, the upside to the consolidated financials would be significant. While Sarla Flex contributes only 1% at EBIDTA on consolidated level at 23% capacity utilisation, at 50% utilisation it would contribute 21%. We believe the margin expansion would be significant on prudent cost management as shown in exhibit 23. Hence we believe Sarla Flex could offer Rs2.7 upside to our FY18E EPS at 50% utilisation resulting to Rs27/share upside (43%) in Target Price at 10x PE.

Exhibit 55: Sensitivity on consolidated financials at different utilisation rate for Sarla Flex

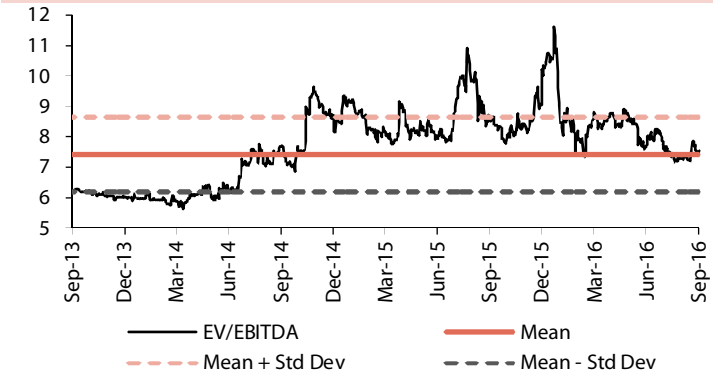
US Utilisation rate (%) - FY18E	22.9	30.0	40.0	50.0
Consolidated Revenues (Rs mn)	3,696	3,851	4,073	4,293
EBIDTA (Rs mn)	972	1,035	1,129	1,218
PAT (Rs mn)	646	690	785	875

Source: Company, Centrum Research

Peer comparison – No direct peers exist

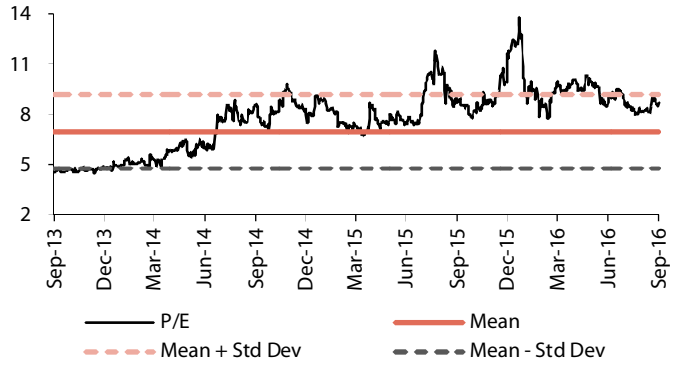
Since SPFL has no direct peers across the product line, we have tried to do a comparative analysis of textile companies having both domestic and export revenues. AYM Syntex is present in a similar business having different product profile; however, it has no coverage. We believe only Unifi, Inc is a direct comparable company to SPFL.

Exhibit 56: 1 year forward EV/EBITDA chart



Source: Bloomberg, Company, Centrum Research Estimates

Exhibit 57: 1 year forward P/E chart



Source: Bloomberg, Company, Centrum Research Estimates

Exhibit 58: Comparative Valuations

Company	Mkt Cap (Rsmn)	CAGR FY16-FY18E (%)			EBITDA Margin (%)			PE (x)			EV/EBITDA (x)			RoE (%)			Div Yield (%)		
		Rev.	EBITDA	PAT	FY16	FY17E	FY18E	FY16	FY17E	FY18E	FY16	FY17E	FY18E	FY16	FY17E	FY18E	FY16	FY17E	FY18E
Sarla*	**5,236**	***11.4***	***27.6***	***19.7***	***20.0***	***25.0***	***26.3***	**11.7**	**9.3**	**8.0**	**10.1**	**7.2**	**5.9**	***18.3***	***19.7***	***19.6***	***1.7***	***2.2***	***2.8***
Orbit Export	3,755	*14.6*	*15.1*	*15.3*	*30.4*	*30.1*	*30.7*	15.3	13.5	12.0	8.6	8.0	7.1	*23.8*	*20.8*	*21.3*	*0.0*	*0.0*	*0.0*
Vardhman Textiles	62,795	*3.6*	*5.6*	*15.7*	*21.1*	*21.5*	*21.9*	10.7	8.7	8.0	4.9	5.9	5.3	*16.0*	*17.5*	*16.6*	*0.0*	*1.4*	*1.6*
Nandan Denim	6,167	*11.8*	*20.8*	*23.1*	*16.5*	*17.9*	*19.3*	9.2	8.2	6.4	4.9	4.4	3.6	*20.9*	*19.6*	*20.4*	*1.4*	*0.0*	*0.0*
Welspun India	57,521	*11.7*	*9.5*	*12.0*	*26.2*	*25.1*	*25.2*	8.2	7.7	6.5	8.0	5.0	4.4	*41.1*	*32.3*	*29.9*	*1.3*	*2.5*	*3.3*
KPR Mill	41,826	*11.5*	*18.1*	*26.2*	*18.8*	*20.3*	*21.1*	19.9	15.4	12.5	8.3	8.6	7.5	*20.8*	*22.3*	*23.2*	*1.2*	*0.0*	*0.0*
Himatsingka Seide	25,687	*14.6*	*32.0*	*19.2*	*16.1*	*18.6*	*21.4*	15.4	13.7	10.8	9.3	8.5	6.6	*18.6*	*17.2*	*18.7*	*0.0*	*1.1*	*1.3*
Indo Count Industries	30,844	*15.7*	*19.2*	*18.7*	*20.0*	*20.9*	*21.2*	11.7	9.9	8.3	9.6	6.6	5.6	*49.1*	*39.6*	*33.7*	*0.2*	*1.3*	*1.7*
Sangam India	9,777	*17.4*	*22.1*	*31.6*	*15.5*	*16.4*	*16.8*	12.7	9.7	7.3	6.7	5.3	4.5	*19.0*	*19.9*	*21.4*	*0.0*	*1.2*	*1.5*
Global Peer																			
Unifi Inc#	479	*1.8*	*2.6*	*2.2*	*10.3*	*9.6*	*10.5*	13.4	14.9	12.3	8.7	9.4	8.3	*11.1*	*NA*	*NA*	*0.0*	*0.0*	*0.0*

*Source: Bloomberg consensus, Companies; *Centrum Research Estimates; #Mcap in USD mn, June End*

Exhibit 59: Quarterly Financials(Consolidated)

Y/E Mar (Rs mn)	Q2FY15	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16	Q1FY17
Total Income	807	767	794	800	816	738	701	750
COGS	410	312	311	371	330	281	303	312
Employees expenses	64	69	72	53	56	49	57	53
Other expenses	198	211	260	203	227	235	275	200
Total Expenditure	672	591	643	627	613	565	635	565
EBITDA	**134**	**176**	**151**	**172**	**203**	**174**	**66**	**185**
Depreciation	41	40	24	38	39	39	38	45
EBIT	94	136	127	134	164	134	28	140
Interest	11	30	12	15	14	16	20	18
Other Income	52	(27)	40	15	31	34	32	36
Exceptional Items	0	0	0	0	0	0	0	0
PBT	134	79	154	134	182	152	40	159
Total tax	34	22	42	34	50	1	(28)	58
Reported PAT	101	57	112	100	132	150	69	100
Adj PAT	**101**	**57**	**112**	**100**	**132**	**150**	**69**	**100**
Growth %								
Revenue	*19.9*	*21.8*	*10.6*	*(5.0)*	*1.2*	*(3.7)*	*(11.7)*	*(6.2)*
EBITDA	*28.0*	*26.4*	*60.4*	*39.9*	*51.2*	*(1.3)*	*(56.4)*	*7.3*
PAT	*6.6*	*(30.7)*	*79.6*	*58.3*	*31.3*	*161.9*	*(39.0)*	*(0.1)*
Margins%								
Gross Margin	*49.1*	*59.4*	*60.8*	*53.6*	*59.6*	*62.0*	*56.8*	*58.4*
EBITDA	*16.7*	*22.9*	*19.0*	*21.6*	*24.9*	*23.5*	*9.4*	*24.7*
EBIT	*11.6*	*17.7*	*16.0*	*16.8*	*20.1*	*18.2*	*3.9*	*18.7*
Adj PAT	*12.5*	*7.5*	*14.2*	*12.6*	*16.2*	*20.4*	*9.8*	*13.4*

Source: Company, Centrum Research

Exhibit 60: Shareholding pattern (%)

	Q1FY17	Q4FY16	Q3FY16	Q2FY16
Promoter	*55.2*	*55.2*	*55.2*	*55.2*
FIIs	*0.0*	*0.0*	*0.0*	*1.2*
DIIs	*14.4*	*14.4*	*14.3*	*15.9*
Others	*30.4*	*30.4*	*30.5*	*27.8*

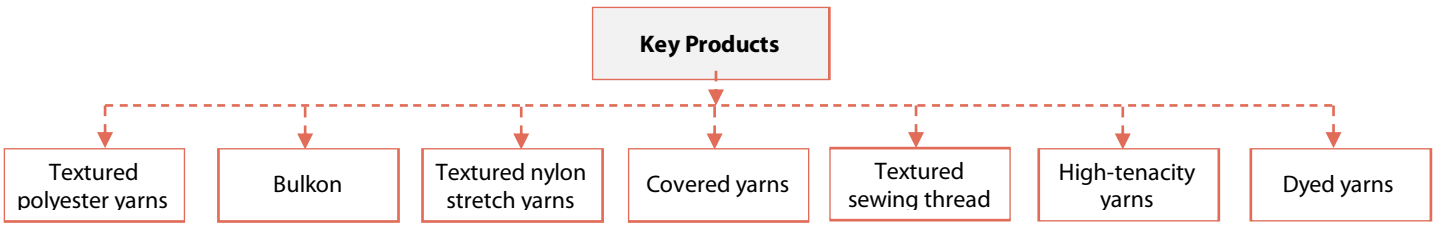
Source: BSE

Company Background

Sarla Performance Fibers Limited (formerly Sarla Polyester Limited) manufactures and exports polyester and nylon textured, twisted and dyed yarns; covered yarns; high-tenacity yarns and sewing thread. Beginning as a manufacturer of commodity yarns, the company has successfully established itself as a manufacturer of specialised and higher value-added yarns. Over the years, SPFL has expanded its activities with the expansion and upgradation of existing facilities in India, as well as through creation of new facilities overseas, with the primary objective of establishing close relationships with customers to provide quick and efficient services to them. The company exports to over 45 countries across six continents; it has subsidiary operations in the USA and Portugal, JV manufacturing operations in Honduras and Turkey, and distribution centres in Thailand and Vietnam.

Key Products

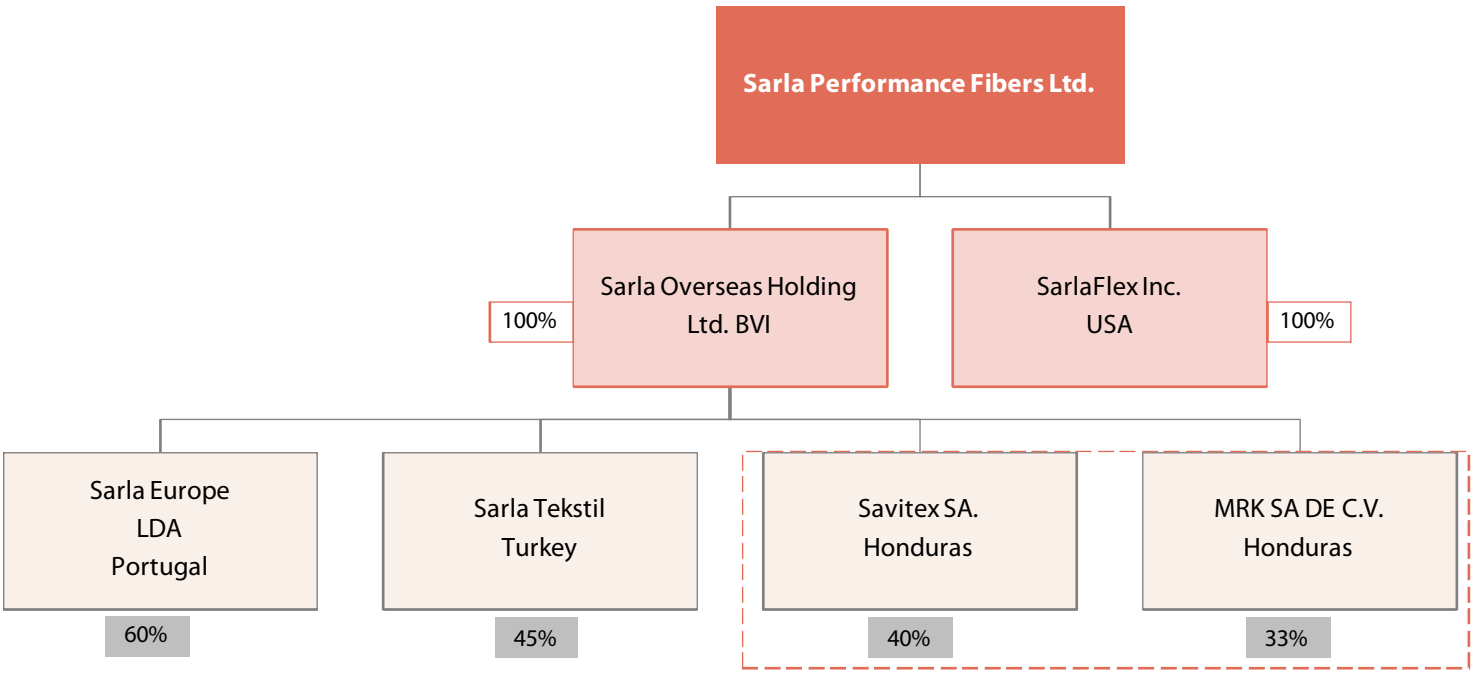
Exhibit 61: Key Products



Source: Company, Centrum Research

Group Structure

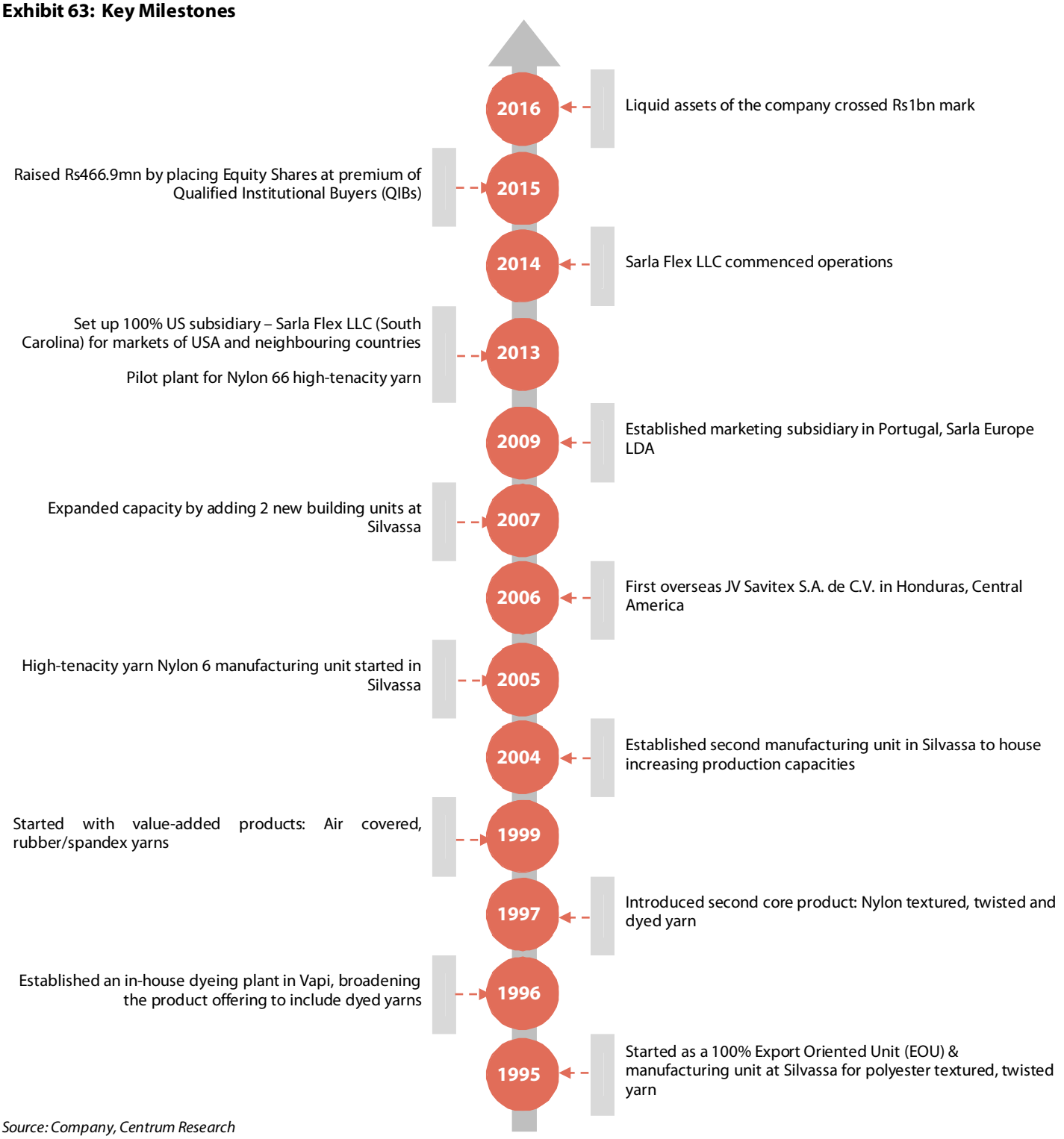
Exhibit 62: Group Structure



Source: Company, Centrum Research; Note: Management is in the process of winding up the JVs in Honduras

Milestones

Exhibit 63: Key Milestones



Source: Company, Centrum Research

Board of Directors

Exhibit 64: Board of Directors

Name	Position	Profile
Mr. Madhusudan S. Jhunjhunwala	Executive Chairman & Whole time Director-Promoter	Mr. Madhusudan S. Jhunjhunwala is the promoter of Sarla Performance Fibres. He is an Executive Chairman in the company since September 1994 and its director since inception. With a B.Com degree, he has a vast experience in Finance and Office administration.
Mr. Krishnakumar M. Jhunjhunwala	Managing Director - Promoter	Mr. Krishnakumar Jhunjhunwala holds a Bachelor Degree in Commerce from University of Mumbai and has more than 25 years of experience in the textile industry. He is associated with the company since June 1994.
Mr. Arun Vaid	Director Non-Executive Independent	Mr. Arun Vaid holds a Bachelor Degree in Commerce and has rich experience in trading of machinery. He is with the company since November 2000.
Mr. Jigar A. Shah	Director Non-Executive Independent	Mr. Jigar A. Shah holds a Bachelor Degree in Commerce and has a huge experience in financial analysis and fund management. He is in the company since July, 2006.
Mr. Parantap Dave	Director Non-Executive Independent	Mr. Parantap Dave is a Chartered Accountant by qualification and has a long experience in corporate advising. He has been associated with the company since September 2014.
Ms. Neha Jhunjhunwala	Director Non-Executive	Ms. Neha Jhunjhunwala holds a Bachelor Degree in Management Studies from University of Mumbai and a Master Degree in marketing and strategy from University of Warwick, London. She has been in the company as Vice President (Operations) from 1 June 2011; she is now also a Non-Executive Director w.e.f 31 March 2015, and has experience in managing operations and human resource management.

Source: Company, Centrum Research

Corporate governance – highlighting the finer points

Independent directors' representation on the board

The board of Sarla Performance has an equal number of promoters and Independent directors. Ms. Neha Jhunjhunwala was appointed Non-Executive Director w.e.f 31 March 2015; earlier, she was Vice President (Operations) from June 2011. In comparison, its peer AYM Syntex and Ambika Cotton Mills has a larger percentage representation of independent directors, indicating the value they add from their broader business perspectives.

Exhibit 65: Representation of Independent and Promoter directors on companies' boards

Company		FY10	FY11	FY12	FY13	FY14	FY15	FY16
Sarla Performance Fibres	**Total board members**	5	5	5	5	5	6	6
	Promoters group members	2	2	2	2	2	3	3
	Non-Executive directors - Independent directors	3	3	3	3	3	3	3
	% representation of promoter directors	***40***	***40***	***40***	***40***	***40***	***50***	***50***
	% representation of independent directors	***60***	***60***	***60***	***60***	***60***	***50***	***50***
AYM Syntex	**Total board members**	6	6	6	6	6	6	7
	Promoters group members	2	2	2	2	2	2	2
	Non-Executive directors - Independent directors	4	4	4	4	4	4	4
	% representation of promoter directors	***33***	***33***	***33***	***33***	***33***	***33***	***29***
	% representation of independent directors	***67***	***67***	***67***	***67***	***67***	***67***	***57***
Ambika Cotton Mills	**Total board members**	7	6	7	7	7	6	6
	Promoters group members	2	2	3	3	3	3	3
	Non Executive directors -Independent directors	5	4	4	4	4	3	3
	% representation of promoter directors	***29***	***33***	***43***	***43***	***43***	***50***	***50***
	% representation of independent directors	***71***	***67***	***57***	***57***	***57***	***50***	***50***

Source: Company, Centrum Research

Salaries of the promoters of Sarla Performance Fibres and its peers

Exhibit 66: Salaries of the promoters of Sarla Performance Fibres and its peers

Company		FY10	FY11	FY12	FY13	FY14	FY15	FY16
Sarla Performance Fibres	**Salaries and commissions (Rs mn)**							
	Mr. Madhusudan S. Jhunjhunwala-Executive Chairman & Whole time director-Promoter	2	3	3	4	6	8	10.8
	Mr.Krishnakumar M. Jhunjhunwala -Managing Director - Promoter	3	4	4	5	7	10	12
	Ms. Neha Jhunjhunwala- Director non Executive	0	0	1	1	1	1	1
	Total Promoters group salary	**5**	**7**	**8**	**10**	**14**	**18**	**24**
	% of net sales	*0.3*	*0.3*	*0.4*	*0.4*	*0.5*	*0.6*	*0.8*
	% of PBT	*2.3*	*2.4*	*3.4*	*2.9*	*3.6*	*4.5*	*4.6*
	% of PAT	*3.0*	*2.9*	*4.3*	*3.6*	*4.9*	*6.5*	*5.2*
AYM Syntex	Abhishek Mandawewala-(w.e.f 31.07.2015)-Executive Director-Promotor	0	0	0	0	0	0	8
	Total Promoters group salary	**0**	**0**	**0**	**0**	**0**	**0**	**8**
	% of net sales	*0*	*0*	*0*	*0*	*0*	*0*	*0.1*
	% of PBT	*0*	*0*	*0*	*0*	*0*	*0*	*1.3*
	% of PAT	*0*	*0*	*0*	*0*	*0*	*0*	*1.7*
Ambika Cotton mills	Sri P.V. Chandran- Chairman and managing director (Promoter & Executive)	7	8	8	8	14	15	2.4
	Mrs Bhavya Chandran-Director (Promoter group- Non Executive)	0	0	0	0	0	0	0
	Mrs.Vidya Jyothish Pillai -Director (Promotor group- Non executive)	0	0	0	0	0	0	0
	Total Promoters group salary	**7**	**8**	**8**	**8**	**14**	**15**	**3**
	% of net sales	*0.4*	*0.2*	*0.2*	*0.2*	*0.3*	*0.3*	*0.1*
	% of PBT	*3.1*	*1.3*	*2.4*	*1.9*	*2.4*	*2.4*	*0.4*
	% of PAT	*4.0*	*1.8*	*3.2*	*2.5*	*3.0*	*3.0*	*0.6*

Source: Company, Centrum Research

Independent directors profile and compensation

Exhibit 67: Independent directors profile and compensation

Name of companies	Independent directors name	No. of directorship in other cos	Name of companies in which director	FY16 Compensation (Rs mn)	*As % to FY16 PBT*
Sarla Performance Fibers ltd	Mr. Arun Vaid	1	Sarla Performance Fibers Ltd	0.1	*0.0*
	Mr. Jigar Shah	1	Sarla Performance Fibers Ltd	0.1	*0.0*
	Mr. Parantap Dave	3	Sarla Performance Fibers Ltd & Tree House Education & Accessories Ltd	0.1	*0.0*
AYM Syntex Ltd	Mr. Atul Desai	10	AYM syntex Ltd,JSW Holdings Ltd,Welspun Corp, RMG Alloy Steel LtdTCFC Finance Ltd and Welspun Investments & Commercials Ltd	0.5	*0.1*
	Mr.M.K. Tondon	2	AYM Syntex Ltd	0.2	*0.0*
	Mr. K. H. Viswanathan (w.e.f . 31.07.2015)	5	AYM Syntex Ltd, Ajanta Pharma & Welspun Corp Ltd	0.3	*0.0*
	Ms. Mala Todarwal	8	AYM Syntex Ltd & Welspun Investments & Commercials Ltd	0.3	*0.0*
Ambika Cotton Mills Ltd	Mr.K.N Sreedharan	2	Ambika Cotton Mills Ltd	0.1	*0.0*
	Dr.K.Venkatachalam	2	Ambika Cotton Mills Ltd	0.1	*0.0*
	Mr.R.Soundararaja Perumal	1	Ambika Cotton Mills Ltd	0.1	*0.0*

Source: Company, Centrum Research

Related party transactions –Clean history

Over the past years, SPFL has maintained a clean related party transaction history as compared to its peer AYM Syntex. In our study of related party transactions, we have not encountered any material related party transactions on either the revenue or expense side. This is a strong corporate governance trait of SPFL.

Exhibit 68: Major related party transactions

Company (Rs mn)	Particulars	FY10	FY11	FY12	FY13	FY14	FY15	FY16
Sarla Performance Fibres	Rent paid -**Associates**	1	1	1	1	1	1	1
	Advance Received	0	0	3	0	0	0	0
	Security Deposit -**Associates**	0	0	23	23	23	25	25
AYM Syntex	Sales of goods	28	58	242	334	501	686	794
	Purchase of goods & services	47	128	66	309	147	79	90
	Loans taken	108	0	0	26	0	250	0
	Repayment of loans taken	108	0	0	13	13	0	250
	Sale of investments	28	0	0	0	37	0	0
Ambika Cotton mills	**No significant related party transactions**	0	0	0	0	0	0	0

Source: Company, Centrum Research

Contingent Liability – No significant risks to net worth

Total contingent liability as of FY16 stood at Rs1.29bn which is 50% of net worth; however, 44% of the same is in the form of letter of credit issued by banks on behalf of Sarla Flex, Inc. With the turnaround of Sarla Flex already engineered, we do not foresee any risk on this front.

Exhibit 69: Contingent liability trends for Sarla Performance Fibres and its peers

Company (Rs mn)	Particulars	FY10	FY11	FY12	FY13	FY14	FY15	FY16
Sarla Performance Fibres	Letter of credit	202	335	249	112	187	187	285
	Stand-by letter of credit issued by banks on behalf of Sarla Flex, Inc	0	0	0	163	501	563	567
	Bank Guarantees	35	36	37	36	43	52	59
	Excise and custom duty related	185	189	220	233	277	277	120
	Bill discounted not matured	107	102	201	94	205	156	0
	CST Liability related	156	252	571	430	214	211	260
	Liability of income tax related to past years				1	1	6	7
	Total	**684**	**914**	**1278**	**1069**	**1430**	**1453**	**1298**
	% share of net worth	***76.7***	***84.4***	***102.7***	***75.0***	***84.5***	***63.2***	***49.6***
AYM Syntex	Guarantees given by banks	25	32	33	43	45	70	70
	Disputed Indirect taxes	130	98	120	140	132	134	134
	Disputed direct taxes	0	0	0	109	0	5	5
	Unexpired letter of credit	309	485	694	1083	80	160	128
	Excise and custom duty related	1	14	11	14	14	12	11
	The accumulated dividend payable on redeemable optionally convertible preferences shares	130	139	88	156	34	0	0
	Claims against the company not acknowledged as debt	15	14	14	14	14	14	14
	Bills receivables discounted	98	113	124	185	179	170	117
	Total	**708**	**894**	**1,084**	**1,743**	**499**	**565**	**479**
	% share of net worth	***109.6***	***113.3***	***100.8***	***162.1***	***44.2***	***38.6***	***24.7***
Ambika Cotton mills	Export Bills discounted	739	57	350	388	136	265	274
	Total	**739**	**57**	**350**	**388**	**136**	**265**	**274**
	% share of net worth	***54.2***	***3.2***	***17.9***	***17.6***	***5.2***	***8.8***	***8.2***

Source: Company, Centrum Research

Auditor details

SPFL's current auditor has been associated with the company for more than 10 years now. The auditor is also auditing other companies across sectors.

Exhibit 70: Auditor details

Name of company	Auditor name	Type	Other companies audited by the Auditor	Auditor for the company since	Auditor fees- FY16 (Rs mn)	*As % to PBT*
Sarla Performance Fibers Ltd	Sundarlal Desai & Kanodia	Statutory	Binayaka Tex Processors Ltd, Dolat Investments Ltd, Mangalam Organics Ltd and Remi Edelstahl Tubulars Ltd	At least 2005	0.9	*0.2*
AYM Syntex	MGB & Co LLP	Statutory	Arshiya Ltd, Dish TV, Essel Propack Ltd, Mangal Credit & Fincorp Ltd, TCFC Finance Ltd, Welspun Corp Ltd, Zee Entertainment Enterprises Ltd, Zee Learn Ltd and Zee Media Corporation Ltd	At least 2005	2.3	*0.4*
Ambika Cotton Mills	L. Venkatasubbu & Co., Chartered Accountants	Statutory	Non-significant	At least 2005	0.3	*0.1*

Source: Company, Centrum Research

Financials – Consolidated (Historical)

Exhibit 71: Income Statement

Y/E Mar(Rs mn)	FY09	FY10	FY11	FY12	FY13
Net Sales	**1,356**	**1,553**	**1,930**	**2,226**	**2,587**
Growth (%)		14.6	24.3	15.4	16.2
Employee Cost	23.5	27.1	39.7	48.6	52.6
%of Sales	*1.7*	*1.7*	*2.1*	*2.2*	*2.0*
Cost of goods sold	691	822	1,037	1,211	1,376
%of Sales	51.0	52.9	53.7	54.4	53.2
Other expenses	395	417	512	635	690
% of sales	*29.1*	*26.9*	*26.5*	*28.5*	*26.7*
EBIDTA	**246**	**287**	**342**	**332**	**468**
EBIDTA Margins (%)	*18.2*	*18.5*	*17.7*	*14.9*	*18.1*
Depreciation	52	56	66	80	82
Interest expenses	30	24	19	30	44
PBT for operations	**164**	**208**	**257**	**222**	**342**
Other income	2	9	18	13	8
PBT	**166**	**216**	**275**	**235**	**351**
Provision for tax	39	48	49	46	70
Effective tax rate (%)	*23.5*	*22.0*	*17.8*	*19.5*	*20.1*
Net Profit	**127**	**169**	**226**	**189**	**280**
Share of Profit/Loss from associates	2.7	0.5	0.0	0.0	0.0
Adj Net Profit	**130**	**169**	**226**	**189**	**280**

Source: Company, Centrum Research

Exhibit 72: Key Ratios

Y/E Mar	FY09	FY10	FY11	FY12	FY13
Growth ratios (%)					
Revenues	*NA*	*14.6*	*24.3*	*15.4*	*16.2*
EBIDTA	*NA*	*16.5*	*19.2*	*(3.0)*	*41.0*
Adj Net Profit	*NA*	*30.2*	*33.4*	*(16.1)*	*48.0*
Margin ratios (%)					
EBIDTA Margins	*18.2*	*18.5*	*17.7*	*14.9*	*18.1*
PBIT Margins	*14.3*	*14.9*	*14.3*	*11.3*	*14.9*
PBT Margins	*12.3*	*13.9*	*14.2*	*10.6*	*13.6*
PAT Margins	*9.6*	*10.9*	*11.7*	*8.5*	*10.8*
Return Ratios (%)					
ROCE	*24.8*	*14.8*	*16.2*	*11.6*	*13.4*
RoNW	*34.9*	*20.7*	*22.8*	*16.3*	*21.0*
RoIC	*22.7*	*23.5*	*22.5*	*17.8*	*19.0*
Turnover Ratios (Days)					
Inventory period	79	70	83	89	86
Collection period	101	101	96	106	82
Payment period	60	66	67	58	44
Net Working Capital	148	141	140	171	165
Solvency Ratio					
Debt-equity	0.5	0.4	0.4	0.5	0.8
Net Debt-equity	0.4	0.3	0.3	0.4	0.6
Current ratio	3.6	3.2	3.2	3.9	4.3
Interest coverage ratio	6.4	9.7	14.5	8.5	8.9
Dividend					
Dividend (Rs)	0.4	0.4	0.5	0.5	0.6
Dividend yield (%)	*0.6*	*0.6*	*0.8*	*0.9*	*1.1*
Dividend Payout (%)	*21.9*	*16.8*	*16.2*	*21.3*	*31.6*
Per Share (Rs)					
Basic (end pt) EPS - Rep	1.9	2.4	3.2	2.7	4.0
FDEPS (Adjusted)	1.6	2.0	2.7	2.3	3.4
FDEPS (Reported)	1.6	2.0	2.7	2.3	3.4
CEPS	2.6	3.2	4.2	3.9	5.2
Book Value	10.7	12.8	15.6	17.9	20.5
Valuations (x)					
PER	1.6	3.5	3.4	3.7	3.6
P/BV	0.3	0.7	0.7	0.6	0.7
EV/EBIDTA	1.9	3.0	3.2	3.6	4.1
AOCF/EV Yield (%)	*23.5*	*20.8*	*15.2*	*(3.3)*	*12.1*
EV/Sales	0.4	0.6	0.6	0.5	0.7
M-cap/Sales	0.5	0.4	0.4	0.3	0.3

Source: Company, Centrum Research

Exhibit 73: Balance Sheet

Y/E Mar(Rs mn)	FY09	FY10	FY11	FY12	FY13
Share Capital	70	70	70	70	70
Share Warrants	18	0.0	0.0	0.0	0.0
Reserves & Surplus	675	822	1,013	1,175	1,355
Total Shareholders Funds	**763**	**892**	**1,083**	**1,244**	**1,425**
Loan Funds	390	369	480	651	1143
Deferred Tax Liabilities	58	65	92	112	140
Total Capital Employed	**1,211**	**1,326**	**1,655**	**2,008**	**2,708**
Fixed Asset					
Gross Block	768	909	1,131	1,252	1,532
Less:- Accumulated Depreciation	232	285	353	428	510
Net Block	537	624	779	823	1,022
Capital WIP	0	0	0	0	266
Total fixed assets	**537**	**624**	**779**	**823**	**1,287**
Investments	13	9	-	15	28
Inventory	292	297	438	542	607
Debtors	376	432	508	645	584
Loans & advances	135	181	165	230	322
Other Current Assets	-	-	24	23	59
Cash & bank balances	112	96	135	125	218
Total current assets	**915**	**1,006**	**1,270**	**1,566**	**1,789**
Current liabilities and provisions	253	312	394	396	402
Net current assets	661	694	876	1,170	1,388
Mis Expenses	0	0	0	0	3.9
Total	**1,211**	**1,326**	**1,655**	**2,008**	**2,708**

Source: Company, Centrum Research

Exhibit 74: Cash Flow

Y/E Mar(Rs mn)	FY09	FY10	FY11	FY12	FY13
CF from operations					
Profit before tax	166	216	275	235	350
Depreciation & amortisation	52	56	66	80	82
Others	29	23	16	26	42
CF before WC changes	248	294	357	342	475
Working capital changes	(71)	(50)	(147)	(327)	(151)
Cash inflow from operations	**177**	**245**	**210**	**15**	**324**
Income tax paid	(35)	(41)	(23)	(25)	(51)
Cash from Operations	**142**	**203**	**187**	**(11)**	**273**
Adj. OCF (OCF-Interest)	**112**	**179**	**168**	**(40)**	**230**
Adj. FCF (AOCF-Capex)	**59**	**40**	**(55)**	**(158)**	**(316)**
Cash From Investing					
Capex	(42)	(130)	(220)	(108)	(546)
Investments	(24)	(7)	0	(15)	(14)
Others	15	(2)	19	13	15
Cash from investing	**(51)**	**(139)**	**(201)**	**(110)**	**(545)**
Cash from Financing					
Borrowings/ repayments	(36)	(20)	107	186	462
Interest paid	(36)	(29)	(25)	(39)	(57)
Dividend and Dividend Tax	(28)	(28)	(28)	(36)	(40)
Others	8.0	(3)	0.3	0.0	0.0
Share warrants	18.2	0.0	0.0	0.0	0.0
Cash from financing	**(74)**	**(81)**	**54**	**111**	**365**
Net change in cash	**18**	**(16)**	**40**	**(10)**	**93**

Source: Company, Centrum Research

Financials - Consolidated

Exhibit 75: Income Statement

Y/E Mar(Rs mn)	FY14	FY15	FY16	FY17E	FY18E
Net Sales	**2,618**	**3,121**	**2,977**	**3,341**	**3,696**
Growth (%)	*1.2*	*19.2*	*(4.6)*	*12.3*	*10.6*
Employee Cost	121.7	271	215	225	236
%of Sales	*4.6*	*8.7*	*7.2*	*6.7*	*6.4*
Cost of goods sold	1,379	1,492	1,224	1,371	1,514
%of Sales	52.7	47.8	41.1	41.0	41.0
Other expenses	650	861	940	910	973
% of sales	24.8	27.6	31.6	27.2	26.3
EBIDTA	**467**	**496**	**597**	**835**	**972**
EBIDTA Margins (%)	*17.9*	*15.9*	*20.0*	*25.0*	*26.3*
Depreciation	110	145	155	175	186
Interest expenses	69	64	65	80	86
PBT for operations	**289**	**287**	**377**	**580**	**701**
Other income	89	117	131	120	130
PBT	**378**	**404**	**508**	**700**	**831**
Provision for tax	100	123	57	143	185
Effective tax rate (%)	*26.5*	*30.5*	*11.1*	*20.4*	*22.3*
Net Profit	**278**	**281**	**451**	**557**	**646**
Minority interest	0	(1)	(1)	0	0
Adj Net Profit	**278**	**279**	**450**	**557**	**646**

Source: Company, Centrum Research Estimates

Exhibit 76: Key Ratios

Y/E Mar	FY14	FY15	FY16	FY17E	FY18E
Growth ratios (%)					
Revenues	*1.2*	*19.2*	*-4.6*	*12.3*	*10.6*
EBIDTA	*(0.1)*	*6.2*	*20.3*	*40.0*	*16.4*
Adj Net Profit	*(0.9)*	*0.6*	*61.2*	*23.7*	*15.8*
Margin ratios (%)					
EBIDTA Margins	*17.9*	*15.9*	*20.0*	*25.0*	*26.3*
PBIT Margins	*13.6*	*11.3*	*14.9*	*19.8*	*21.3*
PBT Margins	*14.4*	*12.9*	*17.1*	*21.0*	*22.5*
PAT Margins	*10.6*	*9.0*	*15.1*	*16.7*	*17.5*
Return Ratios (%)					
ROCE	*9.5*	*7.1*	*9.8*	*10.8*	*11.3*
RoNW	*17.8*	*14.0*	*18.3*	*19.7*	*19.6*
RoIC	*14.3*	*14.1*	*17.4*	*20.8*	*23.2*
Turnover Ratios (Days)					
Inventory period	99	100.9	113.6	110.0	110.0
Collection period	105	92.1	95.6	97.0	97.0
Payment period	55	53.9	75.1	55.0	55.0
Net Working Capital	176	189.0	161.2	176.4	174.2
Solvency Ratio					
Debt-equity	1.4	1.1	1.0	1.0	0.8
Net Debt-equity	0.8	0.5	0.3	0.3	0.2
Current ratio	4.5	5.5	4.6	6.1	6.3
Interest coverage ratio	5.2	5.5	6.8	8.3	9.2
Dividend					
Dividend (Rs)	0.8	0.8	1.1	1.4	1.8
Dividend yield (%)	*1.2*	*1.3*	*1.7*	*2.2*	*2.8*
Dividend Payout (%)	*22.0*	*28.4*	*23.3*	*22.2*	*24.9*
Per Share (Rs)					
Basic (end pt) EPS - Rep	4.0	3.3	5.4	6.7	7.7
FDEPS (Adjusted)	3.3	3.3	5.4	6.7	7.7
Basic (end pt) EPS - Adj	4.0	3.3	5.4	6.7	7.7
FDEPS (Reported)	3.3	3.3	5.4	6.7	7.7
CEPS	5.6	5.1	7.3	8.8	10.0
Book Value	24.3	27.5	31.4	36.6	42.4
Valuations (x)					
PER	4.5	11.1	11.7	9.3	8.0
P/BV	0.7	1.3	2.0	1.7	1.5
EV/EBIDTA	5.7	8.4	10.1	7.2	5.9
AOCF/EV Yield (%)	*10.5*	*(1.1)*	*12.8*	*5.2*	*9.4*
EV/Sales	1.0	1.3	2.0	1.8	1.6
M-cap/Sales	0.3	1.5	0.2	0.2	0.2

Source: Company, Centrum Research Estimates

Exhibit 77: Balance Sheet

Y/E Mar(Rs mn)	FY14	FY15	FY16	FY17E	FY18E
Share Capital	70	84	84	84	84
Reserves & Surplus	1,622	2,215	2,536	2,969	3,454
Total Shareholders Funds	**1,692**	**2,298**	**2,619**	**3,053**	**3,538**
Loan Funds	2333	2,589	2,683	2,963	2,963
Minority Interest	0.0	(3)	(2)	(2)	(2)
Deferred Tax Liabilities	150	142	77	80	71
Total Capital Employed	**4,175**	**5,026**	**5,377**	**6,093**	**6,569**
Gross Block	2,581	2,667	3,036	3,496	3,716
Less:- Accumulated Depreciation	620	775	929	1,103	1,289
Net Block	1,961	1,893	2,107	2,392	2,427
Capital WIP	8	-	-	-	-
Total fixed assets	**1,969**	**1,893**	**2,107**	**2,392**	**2,427**
Investments	548	576	852	852	852
Inventory	708	863	927	1,007	1,114
Debtors	756	787	780	888	982
Loans & advances	220	436	196	206	216
Other Current Assets	38	80	59	59	59
Cash & bank balances	369	941	1,101	1,232	1,525
Total current assets	**2,091**	**3,106**	**3,063**	**3,393**	**3,897**
Current liabilities and provisions	458	550	647	546	607
Net current assets	1,632	2,556	2,416	2,847	3,289
Mis Expenses	24.6	1	1	1	1
Total	**4,175**	**5,026**	**5,377**	**6,093**	**6,569**

Source: Company, Centrum Research Estimates

Exhibit 78: Cash Flow

Y/E Mar(Rs mn)	FY14	FY15	FY16	FY17E	FY18E
CF from operations					
Profit before tax	377	404	508	700	831
Depreciation & amortisation	110	145	155	175	186
Others	38	17	(14)	(40)	(44)
CF before WC changes	**525**	**565**	**649**	**835**	**972**
Working capital changes	(83)	(425)	312	(300)	(149)
Cash inflow from operations	**443**	**141**	**961**	**535**	**823**
Income tax paid	(94)	(121)	(128)	(140)	(194)
Cash from Operations	**349**	**20**	**833**	**395**	**629**
Adj. OCF (OCF-Interest)	**280**	**(45)**	**768**	**315**	**544**
Adj. FCF (AOCF-Capex)	**(520)**	**(120)**	**398**	**(145)**	**324**
Cash From Investing					
Capex	(787)	(76)	(369)	(460)	(220)
Investments	(520)	(27)	(277)	(0)	0
Others	25	48	78	120	130
Cash from investing	**(1,282)**	**(55)**	**(567)**	**(340)**	**(90)**
Cash from Financing					
Borrowings/ repayments	1,190	257	93	280	0
Interest paid	(69)	(64)	(65)	(80)	(86)
Equity Share Capital	0	467	0	0	0
Dividend and Dividend Tax	(38)	(51)	(133)	(124)	(161)
Cash from financing	**1,084**	**608**	**(104)**	**76**	**(247)**
Net change in cash	**150**	**572**	**162**	**131**	**293**

Source: Company, Centrum Research Estimates

Appendix A

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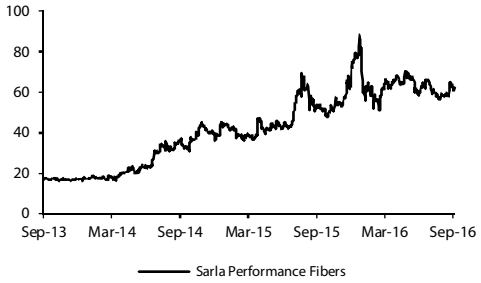
Sarla Performance Fibers price chart



Source: Bloomberg

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