

# NANDAN DENIM LTD

## FUTURE PERFECT



Retail Desk

09 April 2015

<b>Rating</b>	Buy
CMP (₹)	73
Target Price (₹)	110
Upside (%)	50

<b>Key Data</b>	
BSE Code	532641
NSE Code	NDL
Reuters code	NANE.BO
Bloomberg Code	NAND IN
Sensex	28708
Face Value (₹)	10
Mcap (₹ Cr.)	332
52 week H/L (₹)	94/32
2 Wk Avg Qty	123000

<b>Share holding, December '14</b>	<b>Holding %</b>
Promoters	60.26
FII	3.82
DIs	0.02
Public	35.90

<b>Performance (%)</b>	<b>3M</b>	<b>6M</b>	<b>12M</b>
Stock-NDL	0	73.8	102.8
BSE 200	6.6	13.7	35.8
BSE 500	6.6	13.7	37.1

## Price Chart: (One-Year)


<http://www.nandandenim.com>

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**The Case in Point:**

The western lifestyle and western fashion has boosted the consumption of casual fashion apparel like denims, dress shirts, tees, casual shirts among both men and women consumers in all developing countries including India.

The average number of denim items owned by Indian consumer is much lower in comparison to consuming market of the United States, Europe etc. The number is even lower than countries like Brazil and China. This difference in the number demonstrates the huge potential that exists for denim in the domestic market.

Per capita denim jeans consumption in India is only 0.3 compared to USA's 9, UK's 8, Brazil 7, Thailand 7, Japan 6 and China's 2.

The 78% of Indian population is less than 45 years of age.

The rising disposable incomes and fashion consciousness, increasing demand from womenswear segment and the growing acceptance of denim jeans as an officewear coupled with the expanding demand from Tier II & III cities driven by expanding organised retail industry will lead the growth of denim in India.

The movement towards casual comfortable dressing, growth in the women/children segment, rapidly increasing incomes, more organized retail and penetration of brands into smaller towns and cities, the advent of international buying houses, more garment exports and other positive factors.

As the penetration of denim category and the awareness of denim quality increases in those cities and rural India, their share in market value will start increasing with more number of consumers willing to pay premium for the quality, design and fit.

The latest trend in the denim fashion augurs well for the denim companies in India and the case in point is Nandan Denim (NDL), which is the second largest manufacturer of denim in India and the 5<sup>th</sup> largest in the global arena.

**Key Financial:**

(₹ crore)

Year-March	9MFY15A	9MFY14A	FY14A	FY15E	FY16E	FY17E
Sales	818.23	654.91	893.75	1100.0	1250.0	1370.0
PBIDT	130.54	109.97	136.67	173.8	209.5	264.2
Interest	29.63	27.68	32.03	33.7	40.6	20.0
PBDT	100.92	82.29	104.64	140.1	168.9	244.2
Depreciation	45.82	36.77	49.73	66.2	84.6	86.3
PBT	55.10	45.52	54.91	73.9	84.3	157.9
Tax	19.03	18.6	15.6	24.4	27.8	52.1
PAT	36.07	26.92	39.31	49.5	56.5	105.8
Equity			45.5	45.5	45.5	45.5
Reserves			171.0	220.5	277.0	382.8
Book Value (₹)			47.6	58.5	70.9	94.1
EPS (₹)	7.9	5.9	8.6	10.9	12.4	23.3
Cash EPS (₹)	18.0	15.9	19.6	25.4	31.0	42.2
OP Margin (%)	16.0	16.8	15.3	15.8	16.8	19.3
NP Margin (%)	4.4	4.1	4.4	4.5	4.5	7.7
P/E				6.7	5.9	3.1



**Company Description**

Incorporated on August 9, 1994, the Ahmedabad-based Nandan Denim (NDL) formerly Nandan Exim) is engaged in textile business. Initially, NDL was in the business of trading of fabrics in domestic and international markets. During FY04, NDL commenced implementation of Weaving (Grey) project.

NDL is engaged in manufacturing of denims, gray cotton fabrics and khakhis. It also manufactures fabrics of different weaves, dyes, combination of yarns and weights. Currently, the exports account for nearly 10% of sales.

NDL is the largest denim suppliers to global brands such as Carrefour, Ralph & Lawen, Polo, A/X, Tomy Hilfiger, Gini & Jony, CP Colorplus, Mufti, Killer, Spykar etc.

**Promoters**

NDL is a part of a leading conglomerate, Chiripal Group, which was established in 1972 and is currently diversified across several businesses like Textiles, Petrochemicals, Chemicals, Packaging, Infrastructure and Education.

Chiripal group is widely recognized as the Textile House with manufacturing facilities for POY, Texturising, Cotton Spinning, Denim Weaving, Knitting and Processing, Home Furnishing. With clear focus and ambitious growth plans on the anvil, the Group has been gearing itself to take on the future challenges.

The Chirpal group had a turnover of ₹2900 crore with EBITDA of ₹321 crore and a PAT of ₹83 crore in FY14. The employee strength is 5000.

**Installed Capacity & Utilisation**

**Installed Capacity:**

Denim - 110 MMPA

The capacity will be fully operational post expansion in FY16.

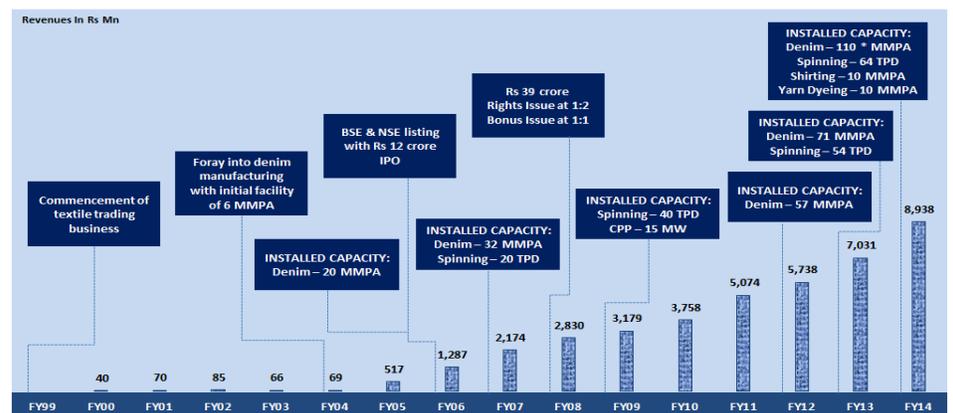
Spinning - 64 TPD

Yarn Dyed Shirting - 10 MMPA

**Capacity Utilisation:**

80% denim capacity utilization

**Milestones**



Particulars	Pre-expansion Capacity	Post Expansion Capacity	Status
Open-end Spinning	38 TPD	84 TPD	6 TPD Commissioned
Ring Spinning	16 TPD	40 TPD	4 TPD Commissioned
Total Spinning	54 TPD	124 TPD	10 TPD Commissioned
Yarn Dyeing	-	Integrated	Commissioned
Shirting Fabric	-	10 MMPA	Commissioned
Denim	71 MMPA	110 MMPA	Ongoing



### *Technology*

State of art manufacturing facility with latest machinery & technology sourced from across the globe. The machinery is capable of producing wide range of denim fabrics - 100% cotton, cotton spandex, cotton poly, cotton poly spandex, cotton modal, cotton tencel etc. The technology enables the company to meet the latest trends and requirements of denim fabric.

### *Locational Advantage*

NDL plant is located in Gujarat, which is a textile hub of India, largest exporter of denim fabric, largest producer of cotton etc. Close proximity to machinery vendors, fabric dealers and leading garment manufacturers result in faster delivery and service and lower overheads. NDL has easy access to the raw material like cotton as Gujarat meets 70% requirement and provides skilled & unskilled labour.

### *Easy Availability of Raw Material*

Cotton is the key raw material used for manufacturing denim fabric. It is a seasonal commodity and production is heavily dependent on monsoon. India, under a normal monsoon condition remains a major source of cotton to the national consumers as well as International market.

With production of cotton having stabilized around 37-38 million bales and domestic consumption to the tune of 30 million bales, the country is prepared to take advantage of any volatility in the commodity market.

Any volatility in cotton market impacts the yarn manufacturers the most whereas the value added manufacturers are reasonably hedged due to the market conditions, i.e. non-commoditised product.

### *Marketing Network*

Leveraging the strong agent-based domestic & global network of the Chiripal group

Strong pan-India network of around 35 - 40 distributors associated with NSL for close to a decade.

Strategic tie-ups with 10 firms for exclusively selling Nandan products

Around 2/3rd of the orders are confirmed through long term agreements involving minimum yearly quantity commitment.

Strong global network of around 15 distributors spread across 8 countries - Peru, Mauritius, Hong Kong, Dubai, Thailand, Bangladesh, New York, Columbia.

NDL exports its denim fabric to over 22 countries across the globe through its strong global dealer-distribution network.

Merchant exports through various star export houses give an additional boost to exports. Currently, exports constitute over 10% of total turnover in next three to four years taking benefit from decreasing competitiveness Chinese players.

### *Capacity Expansion Plan*

NDL is implementing capacity expansion in denim fabric, spinning and shirting segments. The total Capex requirement of ₹612 crore is funded with a D/E ratio of 2.4:1.

**Phase I expansion:** (a) Expansion of denim fabric capacity will help the company to increase its domestic market share as well as diversify its operations on a global scale through a rising share of exports, b) Addition of new shirting capacity to further diversify its operations, and (c) Capex already incurred stands at ₹262.5 crore as on 31 December 2014.

**Phase II expansion:** (a) Expansion of spinning capacity to support the increased denim fabric capacity of 110 MMPA, (b) Incremental capex to be incurred stands at ₹349.5 crore. NDL will backward integrate by expanding its spinning capacity from 64 tpd (tonne per day) to 124 tpd over FY15E-FY16E. Backward integration will help NDL to improve operating flexibility and margins.



### *Improved Operational Flexibility*

Integrated facility will improve the overall operational flexibility, helping the company to absorb the increasing market demand with faster delivery and timely execution due to limited dependency on external factors along the value chain. NSL will achieve optimum capacity utilization and maintain consistency and high quality standards.

With the backward integration in place, the average cost of raw materials stands at ₹150/kg compared to ₹170/kg when outsourced from the open 10%-15% compared to purchase of yarn from market. Integrated facility to help in better management of the working capital and improve the operational efficiencies.

Better market response, efficient capacity utilisation and cost savings on captive yarn would result in EBITDA margin improvement from current 14% - 15% to around 19% - 20% in the next two years. This backward integration will also result in improved return ratios.

Furthermore, with improved operating flexibility, the company would be better placed to increase its share of exports, -which have strict quality and timeline requirements. The company envisages increasing its share of exports from 10% in FY14 to around 30% by FY18.

Overall, this should further help the company to increase its EBITDA margins to more than 20% beyond FY17.

Additionally, the company would also focus to increase its share of value added products post completion of expansion. As a part of this expansion, the company would also be adding a few processing facilities, which would help it to manufacture a wide range of high quality denim fabric, which would help fetch higher realizations. Thus, the company would look to increase its share of value added products from 5-8% in FY14 to 30% by FY18.

### *Favourable Policies*

#### **Technology Upgradation Fund Scheme (TUFS):**

TUFS was introduced in 1999 to catalyse investments in textiles and jute industry. TUFS has facilitated an increase in productivity, cost and waste reduction and improved quality across the value chain.

The total subsidy allocation for revised and restructured TUFS under the 12th Five Year Plan (2012-2017) is ₹1,19,528 million resulting in an expected investment of ₹15,10,000 million. For 2014-15, budgetary allocation under the TUFS increased to ₹23 billion from the revised estimate of ₹19.5 billion in 2013-14. Nandan Denim is entitled to 5% interest subsidy and 15% capital subsidy for period of 7 years.

**Gujarat textile policy:** 5% (7% - spinning facility) interest subsidy and power subsidy @₹1/unit for 5 years, VAT/Entry Tax reimbursement for 8 years, 100% stamp duty reimbursement.

**TUFS (Central textile policy):** 5% interest subsidy and 10% capital subsidy for period of 7 years. VAT/Entry Tax reimbursement is for 8 years and 100% stamp duty reimbursement.

With the overall interest subsidy of 10-12%, PAT will also witness a significant jump from 4%-5% to 7%-8% from FY17E onwards.

The management has not included any benefit of VAT refund to which it is entitled under the Gujarat government textile policy. NDL is entitled for VAT refund only on the machinery excluding land and other costs.

Thus, out of ₹612 crore, NDL will enjoy the benefit of VAT refund of ₹450 crore.



### Q3FY15 & 9MFY15 Results

During Q3FY15, net profit rose 38% to ₹12.6 crore on 26% higher sales of ₹278 crore. OPM and NPM stood at 16.2% and 4.6% Vs 17.4% & 4.1% respectively in Q3FY14. Q3FY15 EPS works out to ₹2.8 Vs ₹2.0 in Q3FY14.

During 9MFY15, net profit climbed 34% to ₹36.1 crore on 25% to ₹818.2 crore. OPM and NPM stood at 16.0% and 4.4% Vs 16.8% & 4.1% respectively in 9MFY14. 9MFY15 EPS is ₹7.9 Vs ₹5.9 in 9MFY14.

### Financial

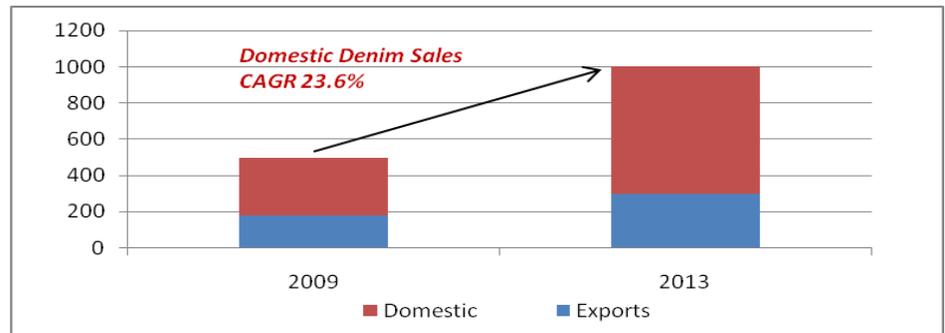
Equity capital is ₹45.5 crore. With reserves of ₹171 crore, the book value of the share works out to ₹ 48. In three years from FY11, debts have gone up by ₹192 crore from ₹268 crore to ₹452 crore while the gross block has moved up by ₹303 crore to ₹670 crore in FY14. DER works out to 2.1:1. Cash/Loans and other current assets etc were ₹75 crore (₹16.5/share).

### Issue of Warrants

NDL is in the process of issuing convertible warrants. This will largely go to the Capex funding.

### Advantage Indian Denim Market

According to Technopak, the Indian denim apparel demand has witnessed a robust growth over the past 4 years and grew at a CAGR of 23.6%. The denim market is expected to grow at a CAGR of 14-15% in the next 5 years, which will significantly outpace the global denim apparel market CAGR growth of 3-5%.



Denim is of the most promising category in India’s apparel market. In 2013, the denim market of India was worth ₹13,500 crore which accounts for 5 percent of the total apparel market of the country. The market is projected to grow at a CAGR of 15 percent to become ₹27,200 crore market in 2018 according to Technopak.

The denim market in India is skewed towards men’s segments with 85 percent contribution coming from it. Women’s denim segment contributes 9 percent to the market and the kids segment the rest 6 percent. The women’s and kid’s denim segments are expected to witness higher growth rates due to their lower base and increasing focus of brands and retailers on those segments.

### Growing Popularity of Denim

In India most of the denim manufacturers focus on the domestic markets given the huge market potential. In the recent times the industry has witnessed entrance of new fabric manufacturers which is expected to make the market for denim fabric more price competitive in the coming years.

Cotton remains the fibre of choice in denim apparel. In blended denim fabrics polyester is being used as weft threads. The demand for stretch denim is growing at a faster rate in India market due to its comfort and fit characteristics. The colour of denim jeans is no longer limited to traditional blue colours. Indian youth has started accepting denim in different colours including green, red, yellow etc.

Denim Jeans has seen a growing popularity as a casual/ leisure wear in almost all large cities in India. The primary reason for the initial growth in the metros and large cities was availability. Most brands started retailing from the large cities and metros.



The earlier phase of scalability also happened in the same cities making it easily available to consumers. The popularity among youth makes it a day wear for college and for other non formal occasions. People have also used denim in semi formal occasions. Brands have been able to create the high aspiration of denim wear by catchy advertisements made with big stars. There is also an increasing aspiration of the youth to engage with premium brands.

### Prospects

The Indian denim apparel market has grown from ₹72 billion in FY2011 to ₹108 billion in FY2013 and is expected to expand to ₹132 billion in FY2017.

The Indian denim apparel market has been growing at a CAGR of 14%-15% which has fast outpaced the global denim apparel market growing at a CAGR of 3%-5%. The domestic denim apparel market has witnessed faster growth vis- à-vis export in terms of volume over a period of five years FY2009-FY2013.

In addition, India is the fourth largest exporter of denim fabrics in the world after China, Pakistan and Turkey. World trade in denim fabric averaged 670,000 tonnes over the past one decade, while in value terms, it fluctuated between \$3 billion and \$3.5 billion. India accounts for 5% of this trade.

Going forward, a large part of the growth of denim apparel shall be driven by deeper penetration in the smaller cities with increasing acceptance of denim within India. On comparing the current population spread and compare it with the contribution in the denim wear market, it becomes very evident on the largest market size between Metros and Mini metros.

As per the Ministry of Textiles, annual production of textile goods is expected to touch US\$220 billion by 2020 (Technopak Advisors) from the current US\$90 billion and China has about 33% share of the global textile market. India's share is just 4.5%. Since China is diverting its focus to other sectors, this is a great opportunity for the Indian Textile Industry.

The global textile and apparel trade of US\$510 billion in 2009 is expected to touch US \$800 billion by 2015 and \$1 trillion in 2020.

The Technopak report states that India has the potential to boost its export share in world trade from the current 4.5% to 8% to reach \$80 billion by 2020 while the global textiles and apparels industry could grow at a CAGR of 6.3% over the next 8-10 years to touch US\$1 trillion.

### Phenomenal Growth Triggers

Acceptance of denim as a fabric has registered perhaps the highest growth over the years in Indian textile scenario. While metro cities have led the growth in the past, with the larger potential penetration in tier-II and tier-III towns, the growth is expected to explode.

While denim story started elsewhere in the world as workwear, it started as a fashion statement of youth in India. It reflected the fashion statement, style quotient and comfort wear anywhere for the youth.

With more than 70% of Indian population aging around 26 years and the median age remaining under 30 years even after 10 years, huge potential exist for denim, a fabric with the target Indian age bracket of 14-40 years.

Current share of male segment within denim wear is almost 75-80% with the female gender catching up faster than the growth registered in the male segment.

The young generation, either gender, has accepted denim as "normal" wear rather than a "functional" wear. Current domestic market is dominated by metro cities that account for almost two-third of consumption while having got less than 10% of national population.



With ever expanding retail network of distribution and higher per capita income at disposal of the tier-II and tier-III towns, the denim availability would register requisite improvement leading to higher penetration. Multiple price-point strategy of branded jeans is further fueling the growth. With affordable availability of better fabrics to erstwhile deprive 90% of the Indian population, the segment is bound to register phenomenal growth.

### *Export Potential*

Of the total denim fabric produced in India, about 25%-30% (200 MMPA) is exported. In recent times, fabrics exported from China have become costlier than those from India owing to multiple reasons including the Cotton Policy and Yuan disparity apart from the ever rising cost of power and manpower. Owing to these factors, denim fabric manufactured in China costs \$2.6-\$2.65/metre compared with \$2.5/metre in India, making India a more lucrative destination for international buyers.

Geopolitical instability of Pakistan, another major denim fabric exporter, has also worked in India's favour. Additionally, the emergence of Bangladesh, which imports bulk of its denim fabric from India, as a favoured destination for RMG manufacturing has boosted India's exports. Owing to these factors, India's share in the world trade of denim fabric is expected to improve, benefitting domestic players.

### *Top Global Denim Manufacturers*

Name	Capacity (MMPA)	Country
Vicunha Textil	230	Brazil
ISKO	200	Turkey
Tavex Corporation	160	Spain
Arvind Ltd	130	India
Nandan Denim	110	India

Aarvee Denim is the third-largest with a capacity of 85 MMPA in India followed by Sudarshan Jeans with a capacity of 70 MMPA followed by Etco Denim and Jindal Worldwide with a capacity of 50 MMPA each.

### *Valuation & Recommendation*

Given India's demographics, the decade ahead will offer even better prospects for the Indian Textile Industry as it is set for strong growth buoyed by both rising domestic consumption as well as export demand.

Abundant availability of raw materials and a skilled workforce, uncertainties & rising costs in competing neighboring countries augurs well for India becoming a global sourcing hub. Looking at this potential of development of the textile industry, the Government of India has extended TUF Scheme for next Plan period and the State Governments have also launched special schemes to promote investment in textiles.

As per a recent study by the industry experts, the denim market in India is set to touch over ₹16,000 crore in the next three years by 2017 owing primarily to youngsters' obsession for the cult fabric.

The boom will be fuelled by not only an increasing demand from small cities and rural areas, but also acceptance of the fabric at workplaces, the study adds. In terms of volumes, the denim market is estimated at 300 million pairs of jeans, which is projected to grow to 550-600 million by 2015. The huge opportunity in denim market augurs well for the future prospects of ND.



NDL has a vision of future growth through diversification in order to survive in a highly competitive environment. This is supported with quality products manufactured by NSL along with fully integrated textile plant to cater to the needs of customers by providing a variety of products under one roof. Further, it has targeted to achieve high volume in terms of quantity and value and also adding the capacity to improve its performance and thereby its share in the market. NDL is also in dialogue with the international brand players for the supply of its products.

NDL has one of the largest denim fabric manufacturing capacities in the world. It is the second largest Denim manufacturer in India and 5th largest in the world. With the recent capacity addition, NDL is well placed to capitalize on the soaring demand of Denim Apparel. The ongoing expansion in its denim fabric capacity and backward integration by expanding its spinning capacity in FY15-16 will result in higher operating margins and improved return ratios.

At the CMP of ₹73, the share is trading at a P/E of 5.9x on FY16E and 3.1x on FY17E. We recommend BUY with a revised upward target price of ₹110 (at a P/E of about 4.8x on FY17E) in the medium-to-long term.

**Key Risk**

Fluctuation in raw material prices and foreign currency & change in government policies if any are key risks.

**Risk Mitigation**

NDL has an Internal Risk Monitoring Committee that strives to put in place specific policies, frameworks and systems for effectively managing various risks. These policies and procedures are reviewed and updated at regular intervals.

**Nandan Denim - Technicals**

**NANDAN DENIM**

NANDAN DENIM (83.5000, 83.7000, 61.5500, 62.7000, +0.85000)



The stock of Nandan Denim had witnessed a deep correction after topping out above ₹90 in early-2015. Prices corrected upto ₹56. At around ₹56, prices formed a bullish ‘double bottom’ pattern. The correction in the stock of Nandan Denim seems to be over. Prices can be expected to target ₹100-110 on the upside.



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