Edel Invest Research

BUY

Indo Count Industries Ltd

Counting Well

CMP INR: 339

Target: INR 542

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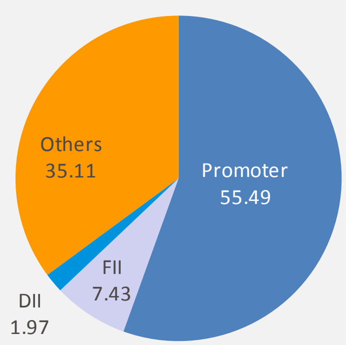
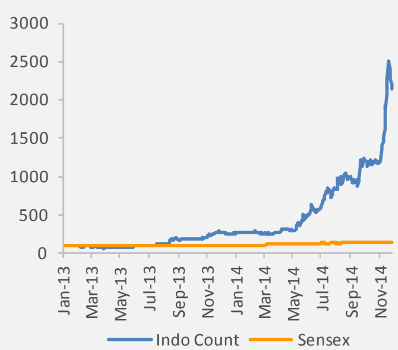
Bloomberg:	**ICNT:IN**
52-week range (INR):	391 / 35
Share in issue (Crs):	3.65
M cap (INR crs):	1,209
Avg. Daily Vol. BSE/NSE :('000):	139

SHARE HOLDING PATTERN (%)





Date: 30th December, 2014

About the Company:

Indo Count Industries Ltd. (ICIL) is a leading manufacturer and exporter of Home Textiles. The company undertook forward integration in 2007 and with that it went from spinning to weaving to processing. ICIL boasts of marquee global clients like Walmart, JC Penney and Bed Bath & Beyond. Currently, 85% of ICIL's revenue comes from exports (70% to the US). The company is diversifying its product mix from bed linen to Fashion, Utility and Institutional segments. ICIL's strong clientele, expanding product bouquet, entry into new export markets, shift in product mix towards premium products, superior return ratios, asset light model and exit from CDR leading to superior return ratios - 24% RocE and 44% RoE in FY14. At CMP, the company is trading at 6.1x FY17E EPS of INR 54.2/share.

Investment Rationale

1) **India competitiveness to sustain:** Indian Textile exporters are in a favorable position over competitors due to our competitive cost dynamics, skilled labour advantage and supportive government policies & subsidies. Also, India's cotton surplus status allows easy availability of raw material (India is now the world's largest cotton producer with 22% market share).

2) **Made-to-Order business with an expanding product bouquet:** ICIL derives ~70% of its overall revenue from the US and has a ~20% share in India's bed linen exports to that country. It is expanding into new international geographies such as UK, Australia, New Zealand, Japan etc. ICIL exports bed linen on a made-to-order basis, resulting in effective management of the company's inventory. Going ahead, the company plans to foray into other product segments like Fashion, Institutional and Utility Bedding. ICIL exports to international clients such as Walmart, JC Penney, Target, Bed Bath & Beyond, John Lewis and House of Fraser.

3) **ICIL to exit CDR by FY15:** During 2008, ICIL went into corporate debt restructuring (CDR) due to series of events. In 2007company undertook a cap-ex of INR 210 crores and forayed in Home Textiles however due to global meltdown the utilization levels remained subdued leading to huge financial loss to the company. In addition, it takes around five years to get an entry into the global retailer's suppliers' list and scale up from there. Moreover, the company lost around INR 70 crores in currency derivatives. It will be out of CDR before March 2015.

4) **Superior return ratios:** One of the key reasons for low return ratios in the Indian textile industry is the low asset turnover. But, unlike its peers, ICIL has done cap-ex in building the front end capacity i.e. processing capacity. The company has the ability to outsource yarn and grey fabric from the open market. This led to high asset turnover, which in turn pushed the return on capital employed (RoCE) higher to 24% in FY14. It also continues to generate healthy ROEs (45% in FY14 from 5.6% in FY11).

Valuation

We believe that ICIL's strong clientele, expanding product bouquet, entry into new export markets, shift in product mix towards premium products, superior return ratios, asset light model and exit from CDR are the key positives. At CMP, the company is trading at 6.3x FY17E EPS of INR 54.2/share. We recommend buy with target price of INR 542 (10x FY17 price to earnings multiple).

Financials

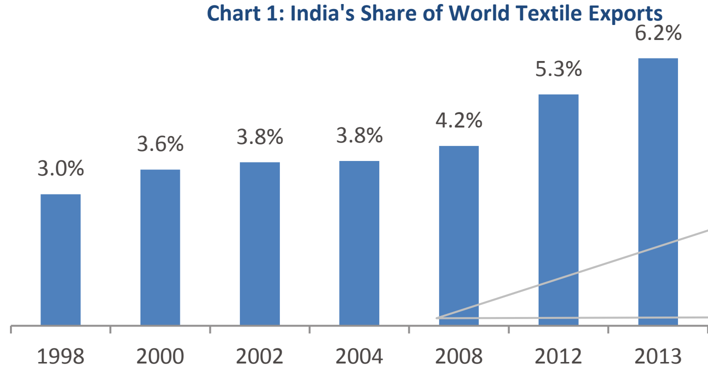
Year to March	FY13	FY14	FY15E	FY16E	FY17E
Revenue	1,208	1,489	1,671	1,936	2,272
Rev. growth (%)	*50.0*	*23.2*	*12.2*	*15.9*	*17.4*
EBITDA	96	180	266	313	384
Net profit	30	110	155	170	222
Shares outstanding (crs)	*3.8*	*3.8*	*4.1*	*4.1*	*4.1*
Diluted EPS (INR)	7.8	29.1	38.0	41.7	54.2
EPS growth (%)	*1,377.5*	*274.0*	*30.7*	*9.6*	*30.1*
Diluted P/E (x)	*43.8*	*11.7*	*8.9*	*8.2*	*6.3*
EV/ EBITDA (x)	17.7	9.4	6.4	5.1	4.1
ROE (%)	*15.7*	*44.7*	*42.9*	*33.6*	*32.0*
ROCE (%)	14.1	24.0	32.4	36.1	35.7

Textile Industry

I) India gaining market share in textile exports

For many centuries India has been a global textile hub. The textile industry in India is one of the crucial segments of the Indian economy, accounting for 14% of industrial production (which translates into 4% of GDP). Textile industry employs 45 million people and accounts for 12% (USD 19bn)of the country's total exports basket. India has been steadily gaining market share in the global textile exports market, improving its share from 3.8% in 2004 to 6.2% in 2013, and ranking only second to China.

Chart 1: India's Share of World Textile Exports



India's share of world textile exports has been growing steadily since 2005 post the expiry of **Multi Fibre Agreement (MFA)** as cotton prices are now fully integrated with the global prices. However, India lost out in the initial years post MFA expiry as Chinese textile exporters gained world market share due to a higher degree of

Source: Edel Invest Research

India: a strong player in global textiles market

India is currently in an advantageous position, as it is the largest producer of cotton globally (2014-15E) with a 22% share. It has the second largest spindles capacity globally with a 22% market share and is currently one of the largest yarn exporters in the world. India is present across the entire textile value chain with production projected to grow significantly over the next few years. India is cotton surplus in comparison to the competitors viz, textile centres like Vietnam, Bangladesh, Indonesia and Thailand (these are net importers of cotton).

Table 1: India's Consumption and availability

Cotton Season	2010-11	2011-12	2012-13(E)	2013-14(P)**
Domestic Consumption (bn Kg)	4	4	5	5
Total Availability (bn Kg)	6	7	7	7
Consumption to Availability Ratio	68%	60%	67%	70%

Source: Edel Invest Research

India is cotton surplus with consumption to availability margin of 60-70% from the past few years. This implies low raw material availability concerns for Indian textile manufacturers

II: India: Increasing its presence in Made-Up Textile exports

Global Made-Ups export market is estimated at ~USD 96bn and grew by 14.9% in 2013-14.

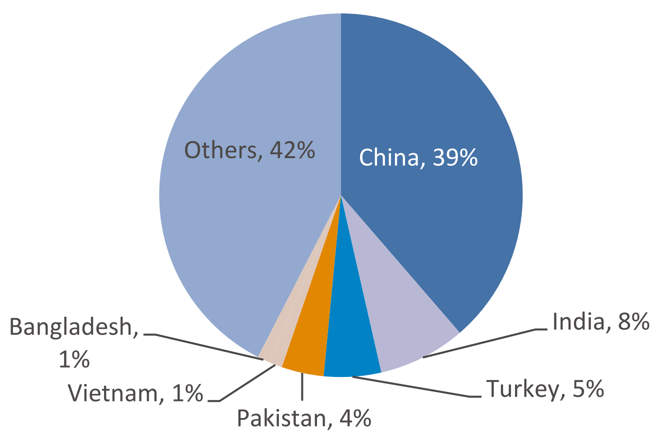
China dominates global home textile exports with a 39% market share followed by India (market share of 7.8%). China is currently 5x the size of Indian Made-Up exports, leaving huge future growth potential for India since India has become more cost competitive than China. India's Made-Ups export market stood at USD 7.48bn and has been growing consistently. Indian Made Up exports grew by 4.6% in 2012-13 and 11% in 2013-14.

Table 2: Global Made Up Exports

Global Made Up Exports(USD bn)				Growth %	
	2012	**2013**	**2014**	**2012-13**	**2013-14**
World	**83.3**	**83.6**	**96.1**	**0.4%**	**14.9%**
China	32.2	33.9	37.1	5.3%	9.5%
India	6.4	6.7	7.4	4.6%	11.6%
Turkey	4.1	4.4	4.9	6.0%	10.6%
Pakistan	3.6	3.3	3.6	-10.3%	9.7%
Vietnam	0.9	0.9	1.1	4.1%	15.3%
Bangladesh	1.0	0.9	1.0	-2.8%	7.6%

Source: Edel Invest Research

Chart 2: Global Made-Up Exports Market Share (%) -2014



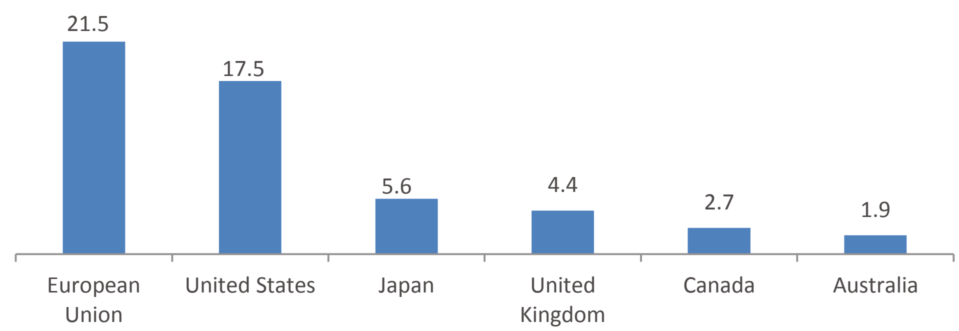
Source: Edel Invest Research

US and EU key markets for Made-Ups with a combined market share of 50%

Global Made-Up imports are dominated by The US and the European Union (EU), with the former alone accounting for USD 16.9bn i.e. 17.5% of the total global Made-Up imports.

Superior quality makes textile companies in India key players in major home textiles markets of the US, Europe and the UK.

Chart 3: Global Made-Ups Market Share Imports-2014 (%)



Source: Edel Invest Research

Indian Made-Up exports to the US increasing

The US accounts for 40% of India's total Made-Up exports whereas India accounts for 17% of total Made-Up imports by the US, growing from 15% in 2012. India's Made Up exports have been growing at 10% while US imports have grown at 4% for the corresponding time period.

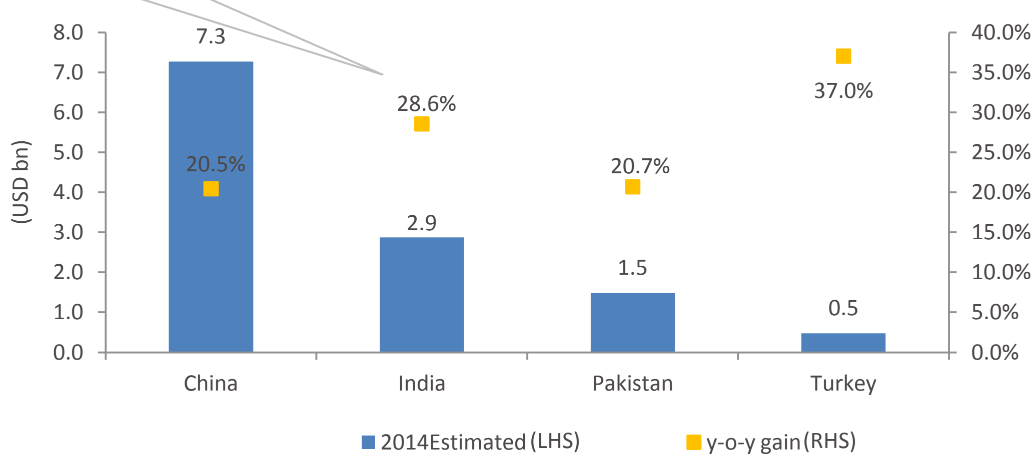
Table 3: Indian Made-Up exports to the US

USD bn	2012	2013	2014E	2012-14 Growth
Indian exports to US	2.4	2.6	2.9	10%
US imports	15.7	16.1	16.9	4%
As a % of US imports	15%	17%	17%	

Source: Edel Invest Research

As an exporting nation to world's biggest Made Ups importing nation- USA, India has reported a 28.6% y-o-y growth surpassing its world Made Ups exports y-o-y growth of 11%

Chart 4: Made Up exporting countries to US



Source: Otexa, Edel Invest Research

Cotton Made-Ups account for 49% of total Made-Ups exports

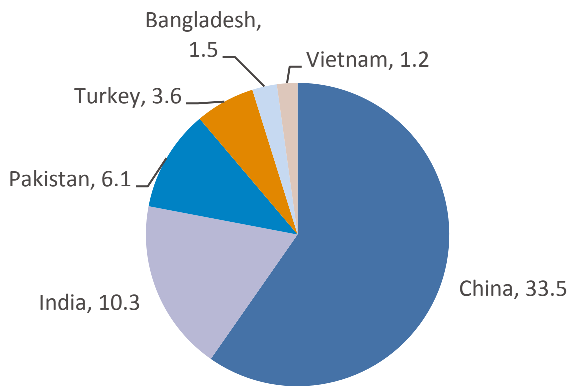
Cotton Made-Ups at USD 46bn account for 49% of the global Made-Up exports. Global exports in the Cotton Made-Ups segment have reported 18% growth from 2013 to 2014. India has witnessed a steady growth in Cotton Made-Up exports, with its global share presently at 10.3%.

Table 4: Global Cotton Made Up Exports

(USD bn)				Growth %	
	2012	2013	2014	2012-13	2013-14
World	**39.3**	**39.6**	**46.7**	**0.7%**	**17.9%**
China	14.08	14.6	15.6	4.1%	6.7%
India	**4.08**	**4.4**	**4.8**	**7.8%**	**9.1%**
Pakistan	2.93	2.5	2.8	-12.1%	10.1%
Turkey	1.51	1.4	1.6	-1.9%	12.2%
Bangladesh	0.66	0.5	0.6	-11.6%	19.3%
Vietnam	0.48	0.5	0.5	5.9%	12.6%

Source: Edel Invest Research

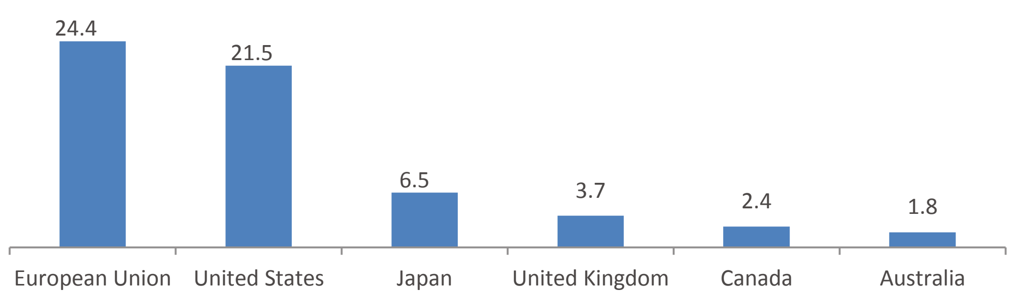
Chart 5: Global Cotton Made Up Exports Market Share (%) 2014



Source: Edel Invest Research

Global Cotton Made-Up imports are dominated by the US and the EU. The US alone accounts for USD 10bn i.e. 21.5% of the total global Cotton Made Up imports.

Chart 6: Global Cotton Made Ups Market Share Imports-2014 (%)

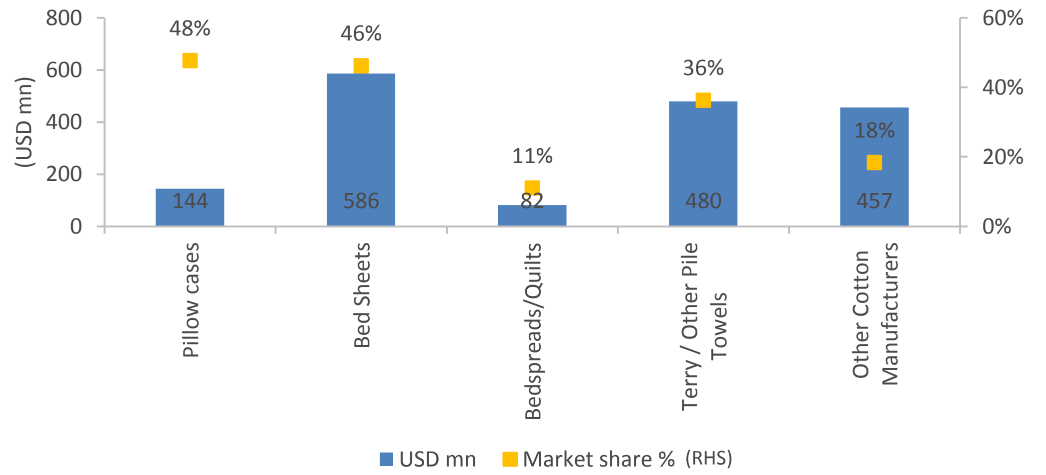


Source: Edel Invest Research

The US is a key importer of India's Cotton Bedsheets and Bedpsreads

Till Oct. 2014, the US imported USD 6.1bn cotton Made-Ups. India exported USD 1.74bn cotton Made-Ups to the US during the same timeframe. Three main segments of Cotton Made-Ups are: Cotton Bed Sheets & Pillow, Cotton Bedspreads & Quilts and Cotton Terry Towels. India accounts for 46.5% of the US' total Cotton Bed Sheets/Pillow imports, 11% of Cotton Bedspreads/Quilts imports and 36.3% of Cotton Terry Towels imports.

Chart 7: US Imports of Cotton Made Ups segmentations



Source: Otexa, Edel Invest Research

ICIL is currently present in the Pillow Cases and Cotton Bed Sheets category. It is planning to enter the top-of-bed i.e. Bedspreads and Quilts category.

III: China's Cotton Policy a boost for Indian Cotton Textile manufacturers

China introduced a Cotton Policy in 2011 and ran till the beginning of 2014 in order to help domestic cotton farmers through minimum support price (MSP). The MSP was set at USD 1.4/pound as opposed to global price of over USD 2 per pound. However, within a span of few months, international cotton prices crashed to sub-USD 1.0/pound levels and remained at that level for a considerably longer time. But, the China government continued to buy cotton from local farmers at a higher MSP vis-à-vis world cotton prices, forcing domestic Chinese mills to initially resort to cotton imports. As a result of the reduced domestic off-take of cotton and higher imports by local mills, the Chinese cotton reserve stocks ballooned and cotton imports doubled. To curb cotton imports by local mills, the Chinese government imposed import quota on cotton and cotton yarn. Consequently, Chinese mills were forced to buy high-cost cotton from local farmers, leading to a significant decline in their competitiveness. This in turn resulted in many low count yarn producing mills in China shutting down.

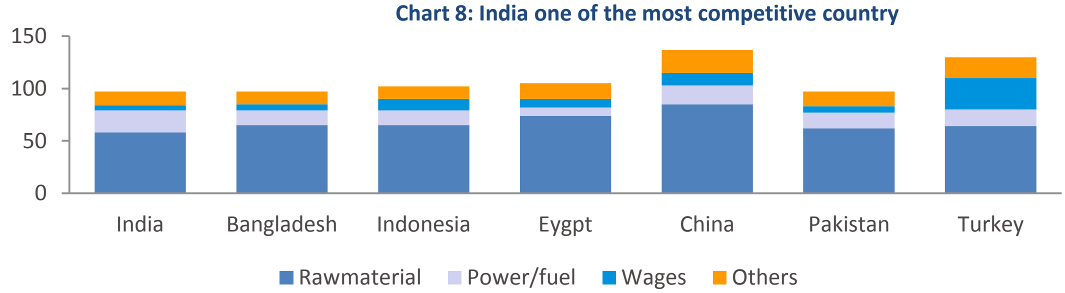
Since India exports 40% of its total cotton yarn to China, there was a huge margin improvement for Indian cotton yarn manufacturers in FY13 and FY14. By capitalizing on this opportunity, the Indian cotton yarn players upgraded their spindle technology while also reducing their debt, resulting in marked improvement in their competitiveness.

However, with China altering its cotton policy this year with direct subsidies for its domestic cotton farmers (cotton reserves as on July'14 stood at average 11.5bn kg), Chinese cotton imports are expected to reduce by 30%. While this could impact Indian cotton yarn exporters to some extent, it will be mitigated by softening cotton and cotton yarn prices. We believe softening of cotton and cotton yarn prices would benefit the Indian textile industry going forward.

IV: India's Competitiveness to boost Textile Exports

In addition, India's cotton surplus status allows easy availability of raw material (India is now the world's largest cotton producer). Indian textile exporters are in a favorable position due to the competitive cost dynamics, skilled labour advantage and supportive government policies & subsidies. These factors, along with a whole host of issues faced by competing countries such as labour unrest (Cambodia) high cost of credit (Vietnam), currency appreciation (Indonesia) etc leaves a fertile ground for India to improve its share of the world 'Textile' exports pie.

Chart 8: India one of the most competitive country

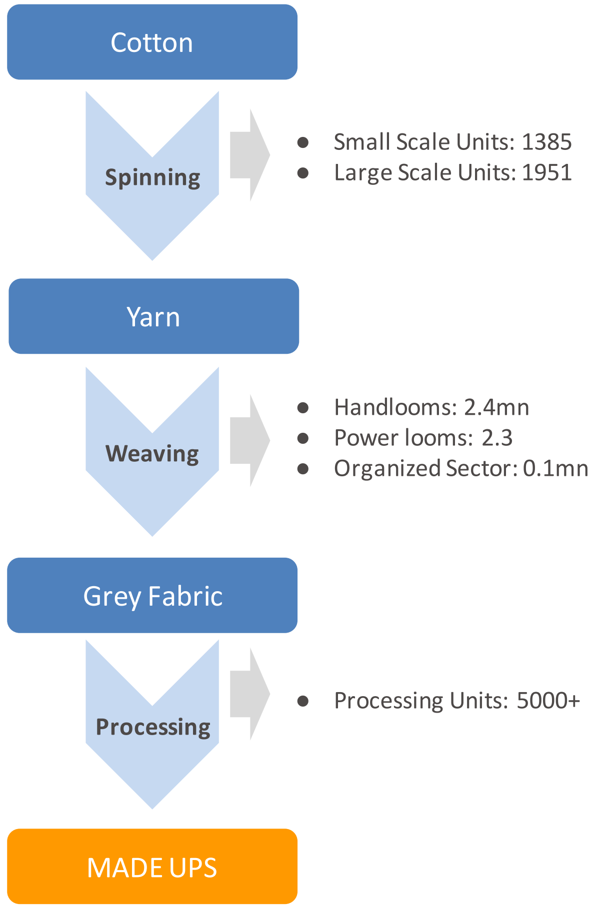


Source: Edel Invest Research

V: Government support to aid growth in textile sector

The Indian government launched the Technology Upgradation Fund (TUF) scheme in FY2000, which led to successful upgradation and modernization of the Indian Textile industry. The scheme offers interest subsidy of 2% for standalone spinning, 5% for integrated facility, processing, garmenting, and technical textiles and 6% for weaving. In addition to TUF scheme, many states offer 5-6% interest subsidy for capital investment. The Indian government also offers zero excise duty for cotton textile and man-made textile segments at yarn, fabric and garment stages and reduction in duty for imported textile machinery and parts.

The Indian Textile Value Chain



Source: EdelInvest Research, Confederation of Indian Textile Industry

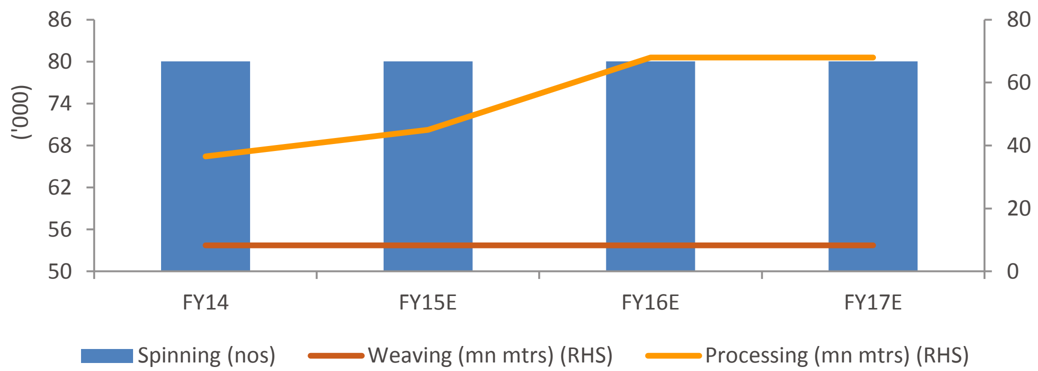
The Indian textile industry has presence across industry value chain. India being a cotton surplus nation is in an enviable position to support its cotton textile industry. India is the largest exporter of yarn in the international market and commands 25% share of global cotton yarn exports. It accounts for 12% of the world's production of textile fibers and yarn. Fabric production in India has witnessed a CAGR of 2.7% between 2006 and 2013.

Investment Rationale

Strong revenue visibility:

Capacity addition: ICIL is increasing the processing capacity from 45 mn meters to 68 mn meters. The new capacity will be operational by Q4FY15. For the same, the company has incurred the capex of INR 70 cr. The new capacity will suffice for the next two years. Post the current expansion, the company will go for Greenfield expansion in FY17. In the second phase, not only processing capacity but the weaving capacity will also be increased. The rationale behind the same is that the company wants to maintain the 25% ratio of in-house weaving.

Chart 9: Capacity addition to enhance growth



Source: Edel Invest Research

Expanding product bouquet: Home Textiles presently is USD 18bn market in the US (ICIL's major market). ICIL currently caters to only one segment i.e. bed linen market (market size: USD 1.8bn). Going forward, the company plans to make an entry into the remaining three segments i.e. Fashion (top-of-the-bed i.e. bed dressing, quilts, comforters etc), Utility and Institutional. The combined opportunity in the balance three segments i.e. Fashion, Utility and Institutional is ~3x the Bed Sheets segment. Currently, China's share of total US imports in the three segments is 90%.

The company's existing facility can be used for the export of new products, but it will need to make a minor investment in terms of stitching machines etc. The clients for the Fashion and Utility segments will remain the same but the Institutional segment clientele will be different. The company plans to increase the share of non Bed Sheets products in Home Textiles from the current level of under 5% to 20% over the next four years.

Expanding geographic reach: ICIL exports account for ~85% of its revenue (~70% of exports to the US). ICIL is currently the third largest exporter of bed linen from India, fourth-largest Bed Sheet exporter to the UA and the 14th largest Home Textiles supplier to the US. The company has a ~20% share in the Indian bed linen exports to the US. The contribution of Home Textiles in ICIL's revenue is expected to increase going ahead, as the company plans to expand into new international geographies such as UK, Australia, New Zealand, Japan etc. The company has already set up offices in Australia. Due to non-FTA agreement with EU, export to that region is relatively lower. This has led to Indian companies being at a disadvantage over other Asian countries like Bangladesh and Pakistan. There is expectation that India and EU will soon sign FTA. Post the FTA, the European market will also open up for ICIL.

Global retailers among top clients: ICIL exports to some of the world's leading clients such as Walmart, JC Penney, Target, Bed Bath & Beyond and Macy's in the US. In Europe, ICIL supplies bed linen to John Lewis, House of Fraser and Debenhams whereas in Dubai it sells to the Lifestyle group. Presently, ICIL's UK clientele strength stands at 4-5, which the company plans to double in the next few years. No single retailer contributes more than 15% of the company's total revenue and the top 10 clients together account for 45-50% of total revenue. Currently, ICIL products make up 20% of the retailers' bed linen requirement, making the company a key supplier for top global retailers.

High lead time required to be named supplier acts as a buffer: Being a supplier to major global retailers requires around three years of gestation period. This results in high gestation period for any new player wanting to supply to the global retail giants. Also, scaling up of the business takes years.

Margin improvement: Till 2005, ICIL was focused on the spinning business. The spinning business is capex intensive and has low return ratios. During 2005, the company planned forward integration with weaving, processing and made-ups facility. The production shifted from yarn manufacturing to bed linen manufacturing. In addition, the company focused on high margin exports markets. The current revenue share of Home Textile is 70% as against nil in FY05. This shift in revenue led to improvement in margins. In addition, the capacity utilization of around 95% in Home Textiles in FY14 also led to increase in operating leverage. The gross profit margin increased from 20% in FY05 to 24% in FY14 while EBITDA margins expanded from 8.2% in FY05 to 12.1% in FY14.

India's cost competitiveness in textiles vis-à-vis other Asian countries, high gestation period to get entry into global retailers, expectation of sustainably soft cotton prices and move towards high value added products like fashion will help ICIL to maintain current margins going forward.

Chart 10: Segmental Revenue & EBITDA Margin

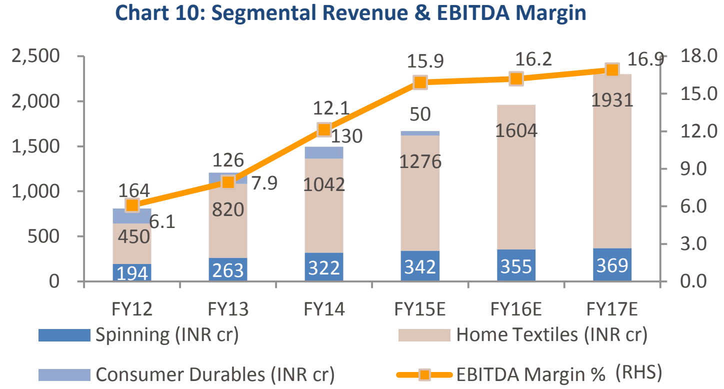
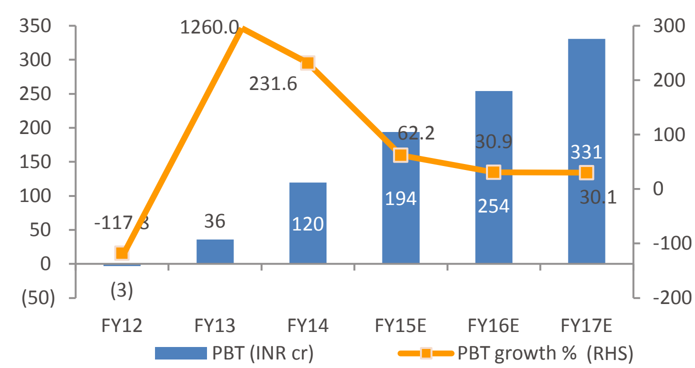


Chart 11: Sustainable PBT



Source: Edel Invest Research

Asset light model – capex on front end: Traditionally, the Indian textile industry has reported low return ratios. The key reason for the same is low asset turnover. Within the textile industry value chain, spinning and weaving segments are capital intensive businesses. But, unlike its Indian peers, ICIL's incremental capex majorly caters to building the front end capacity i.e. processing capacity. The company outsources yarn and grey fabric requirements to the open market. This has led to high asset turnover, which in turn will lead to higher RoCE.

At the current capacity, around 24% of grey fabric is manufactured in house. Post the increase in processing capacity from 45 mn meters to 68 mn meters, the proportion of in-house weaving will fall to around 15%. The company targets to keep around 25% of weaving facility in-house. At the time of next capex cycle, the company will increase the weaving capacity also to maintain the 25% ratio of in-house weaving sourcing.

The outsourced raw material model leads to better return ratios but also exposes the company to outside control over the availability of raw material.

Chart 12: Improving ROCE

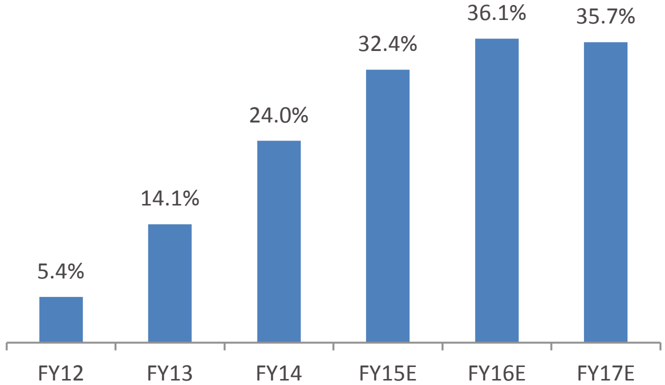
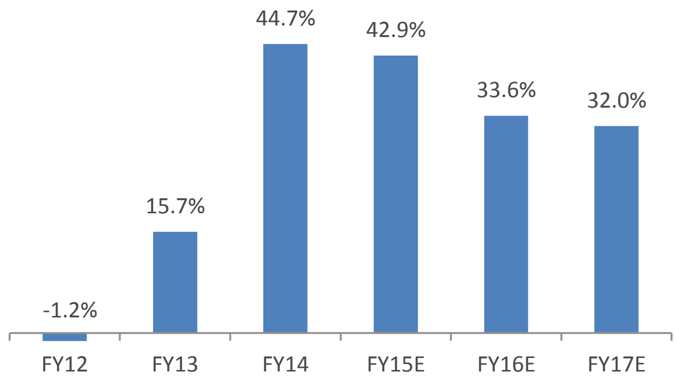


Chart 13: Sustainable ROE



Source: Edel Invest Research

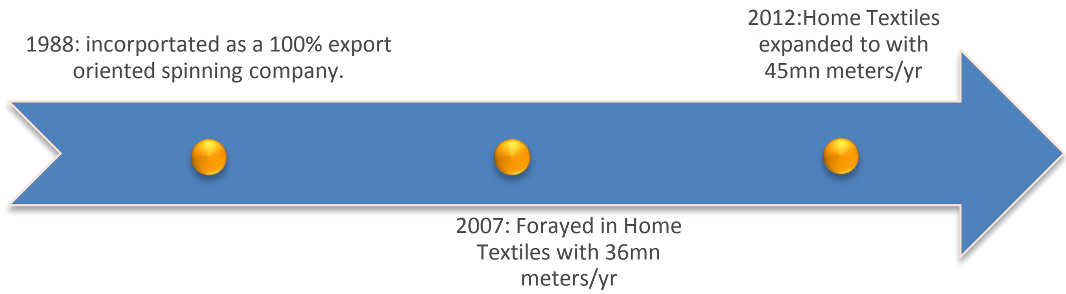
What drove ICIL into CDR: ICIL witnessed liquidity pressure in FY09 due to which the company went into CDR. Derivative losses, coupled with a volatile currency and a hostile macro-economic environment (which adversely impacted consumer sentiment) led to severe financial stress. The company suffered derivative losses to the tune of INR 80 cr in 2009, led by volatile and adverse rupee movement. Also, ICIL's foray into Home Textiles in 2007 led to an enhanced capacity (cap-ex incurred INR 2.1bn funded by debt). However, the capacity expansion did not result in higher utilisation due to depressed consumer sentiment in the aftermath of the 2008 global financial turmoil. These factors resulted in liquidity crunch for the company, in turn driving it into CDR. ICIL revalued its assets to the tune of INR 150.9 cr and INR 21.2 cr in FY09 and FY10, respectively, as one of the requirements under CDR scheme.

The management introduced efficient business strategies which have led to a marked improvement in the health of ICIL's balance sheet. Management has been prudent in improving its balance sheet post FY08-FY09. The company is expected to come out of CDR in the next 1-2 months. Post that we expect a marginal dip in the interest cost of the company.

About the Company

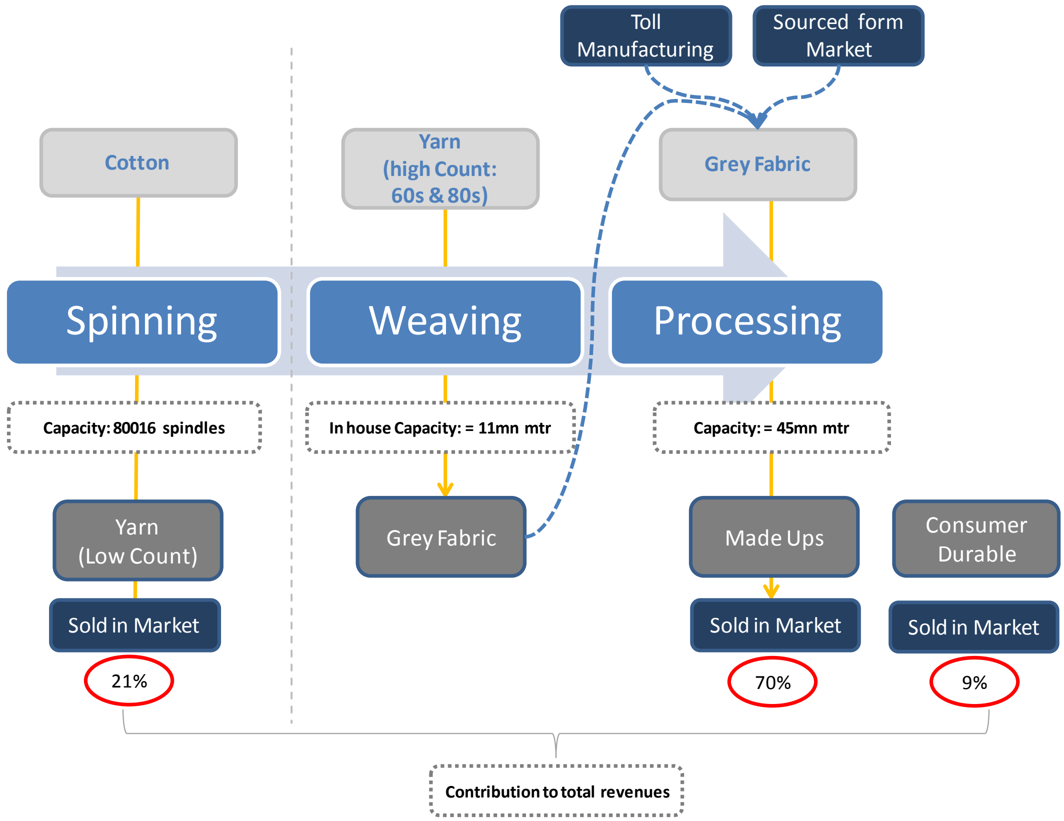
Incorporated in 1988, Indo Count Industries Ltd. (ICIL) is a vertically-integrated textile player with a presence across the entire value chain (from spinning & weaving to processing). The company is promoted by Mr. Anil Kumar Jain. It has three businesses – Home Textiles, Yarn and Consumer Durables. It manufactures and exports cotton yarn, grey knitted fabrics and Made Ups. The company diversified into Home Textiles in 2007. Currently, ICIL has emerged as the third largest manufacturer and exporter of bed sheets from India. The company is a net exporter, with ~70% of its clientele in the international markets.

Its Home textiles plant is located in Kolhapur, Maharashtra and is equipped with the state-of-the-art imported machinery. The plant is equipped with 80,016 spindles, 8 knitting machines and 33 doublers. The Processing facility is equipped with state-of-the-art continuous Bleaching, Dyeing and Finishing machinery.
The company has a showroom and design studio in New York, which was established in 2011 and a warehousing facility in Charlotte, USA. ICIL also established a showroom, design studio and warehouse in Manchester, UK as well as in Melbourne, Australia in July 2014.



Source: Edel Invest Research

Business Overview



Source: Edel Invest Research

ICIL's textiles vertical has two divisions, 1) Spinning and 2) Home Textiles.

Spinning Division: The company produces low count cotton yarn (low count) from its spinning division (capacity: 80,016 spindles). The company sells yarn in the open market wherein 30% revenue is from domestic sales and 70% from exports to South East Asian markets.

Home Textiles Division: Its second division of Home Textiles manufactures bed linen. This division comprises two processes - weaving (capacity of 11mn mtrs) and processing (capacity 45mn mtrs). High count yarn of 60s and 80s count is procured from the markets as a raw material for weaving. At current capacity, around 24% of grey fabric is manufactured in house. The company outsources grey fabric from open market either through toll manufacturing or directly sourced from the market.

Products

Bed Linen

Pillow Covers

Fashion Bedding: Comforter/Quilt

Top-Of-Bed: Fashion Bedding

Institutional Bedding

Utility Bedding

Management Profile

Name	Designation
Anil Kumar Jain	*Chairman and MD*
Mr. R.N. Gupta	*Joint Managing Director*
K.R.Lalpuria	*Executive Director*
Kamal Mitra	*Director*
J.G Arora	*President Home Textiles*
R. Sundaram	*CFO& CS*
Mr. S.K. Mohanty	*SVP-Operations*

Valuation

We believe that the company's strong clientele, expanding product bouquet, entry into new export markets, shift in product mix towards premium products, superior return ratios, asset light model and exit from CDR are the key positives. At CMP, the company is trading at 6.3x FY17E EPS of INR 54.2/share. We recommend buy with target price of INR 542 (10x FY17 price to earnings multiple).

Chart 14: Price-Book

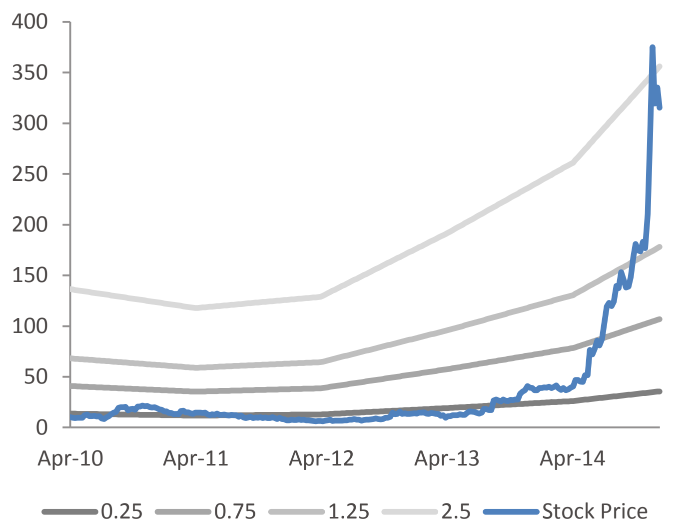


Chart 15: Price-Earnings

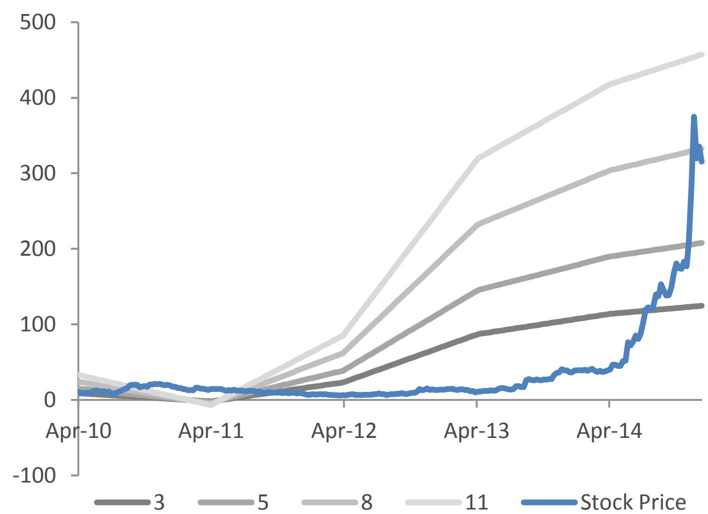


Chart 16: EV/EBITDA

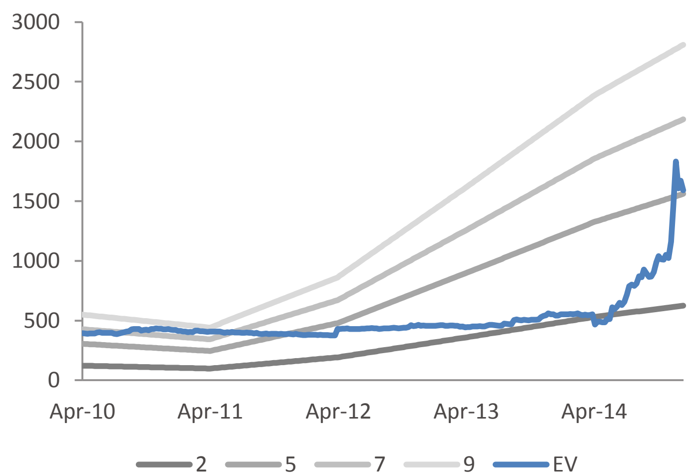
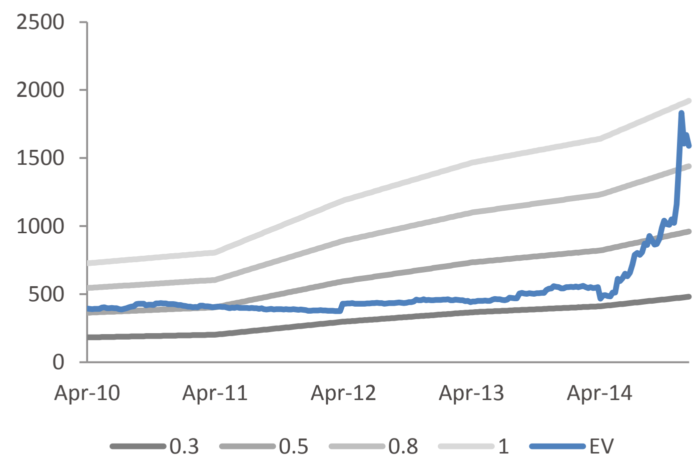


Chart 17: EV/Sales



Source: Edel Invest Research

Investment Risk:

Raw material volatility: Any volatility in prices of cotton and cotton yarn can lead to inventory losses

Losing Suppliers: ICIL sources Yarn from the market and grey fabric either through toll manufacturing or from the market. Although this model is cost effective, it exposes the company to supplier driven risks.

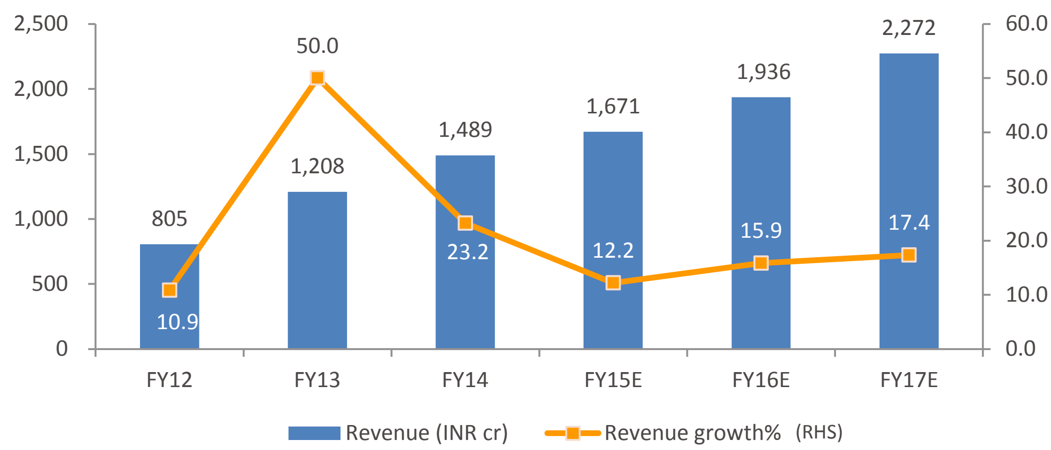
Geographic exposure: Currently, the US accounts for ~70% of ICIL's revenues. Any change in import norms or any import restrictions by the US would adversely affect the company's revenue.

Financials

Sales expected to grow at a CAGR of 15% over FY14-FY17E

The company's revenue grew at a CAGR of 27% over FY11-FY14, backed by growth in the Home Textiles division, which accounts for ~71% of its topline. We expect ICIL to continue recording steady revenue growth going ahead, backed by its shift towards high-value items and expansion of into newer geographies. We expect ICIL to continue growing at a CAGR of 15% over FY14-17E.

Chart 18: Revenue and Revenue Growth



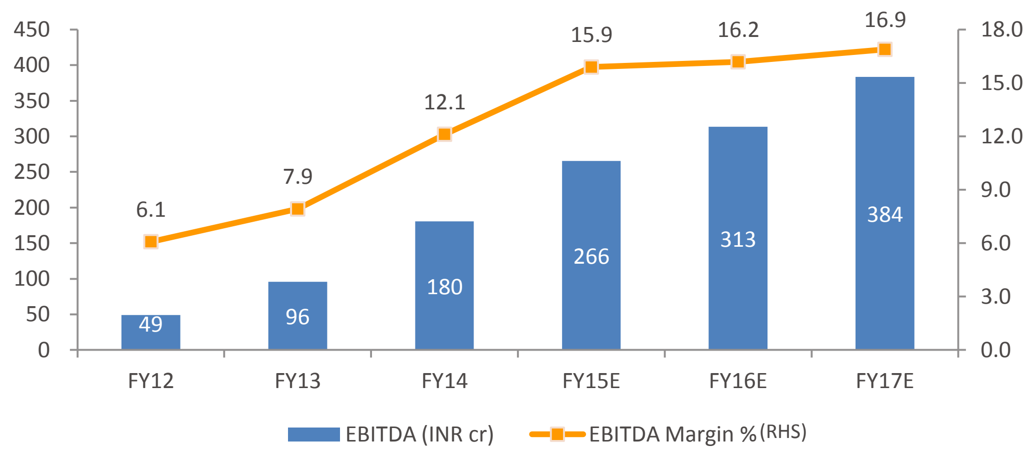
Source: Edel Invest Research

EBITDA margins to sustain above 16% in FY17E

The change in product mix towards high value items supported by a product mix shift towards Home Textiles and a declining contribution of the Consumer Durables segment from 8.8% in FY14 to nil in FY17E will lead to improvement in margins. Home Textiles recorded EBITDA margin of 16% in FY14 compared to 11.6% in FY11 whereas Consumer Durables reported 3% EBITDA margin in FY14 compared to 6% in FY11.

We expect gross margins to be maintained in a range of 27%. EBITDA is expected to record a 29% CAGR over FY14-17E. We expect EBITDA margins to remain steady above 16% over the next three years.

Chart 19: EBITDA and EBITDA Margins

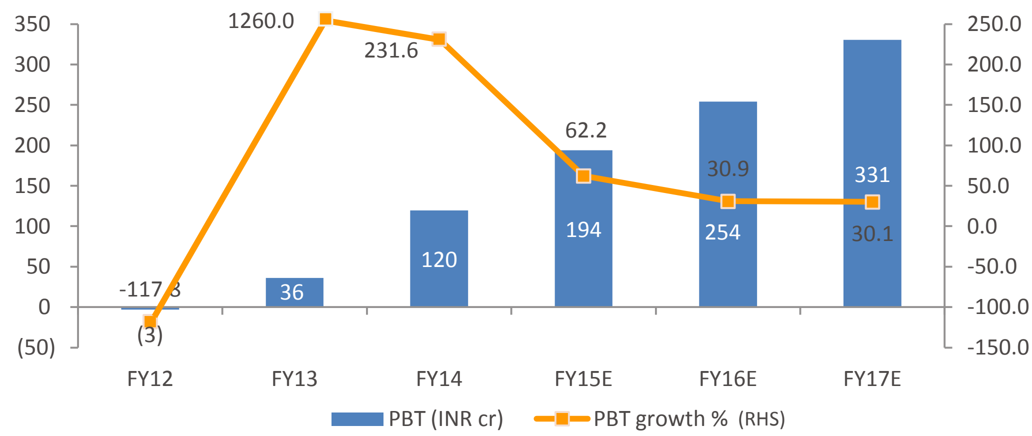


Source: Edel Invest Research

PBT to grow at a CAGR of 40% for FY14-17E

We expect PBT to grow at a CAGR 40% for FY14-17E. Interest costs are expected to reduce due to the company's impending exit from CDR.

Chart 20: Improving PBT



Source: Edel Invest Research

PAT is expected to grow at a CAGR of 26% over FY14-17E. Till FY14, the tax rate was nil due to MAT credit. The effective tax rate for FY15E would be 20% and the company would be paying tax as per the full tax rate from FY16E onwards.

Debt-Equity to remain stable; Operating cash flows to remain strong

ICIL management has been prudent in improving its balance sheet post FY08-FY09. Debt:Equity has reduced from 3.7x in FY08 to 1.5x in FY14 owing to lean working capital and improvement in debtor days (from 51 days in FY08 to 27 days in FY14). The company has initiated the process of exiting CDR and would exit CDR by March 2015. We believe the company would successfully maintain its debt equity ratio at sub-1x going ahead.

Operating cash flows are expected to remain strong on the back of good revenue visibility and efficient working capital management.

Chart 21: Debt Equity

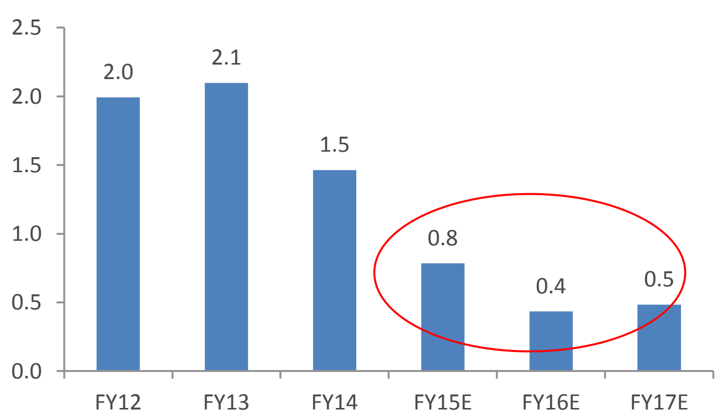
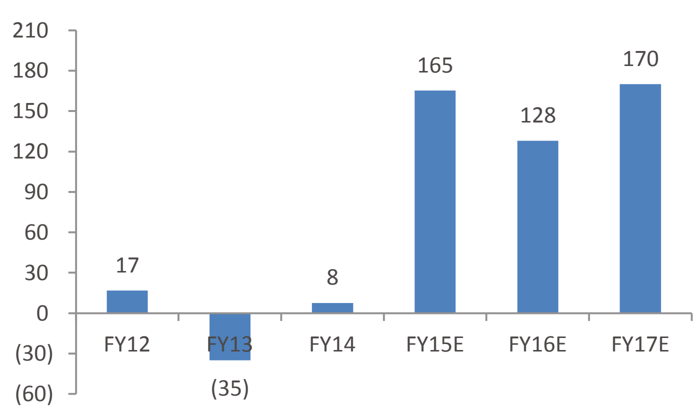


Chart22: Operating Cash Flow



Source: Edel Invest Research

Superior Ratios:

ICIL has reported improvement in its ROCE from 5.4% in FY12 to 24% in FY14. It also continues to generate healthy ROEs (45% in FY14 from -1.2% in FY12). We expect the company to sustain ROCE in excess of 35% in FY17E and ROE to remain in excess of 30% with expanding operating margins and minimal addition in leverage, making it an attractive business to look at going forward.

Chart 23: Improving ROCE

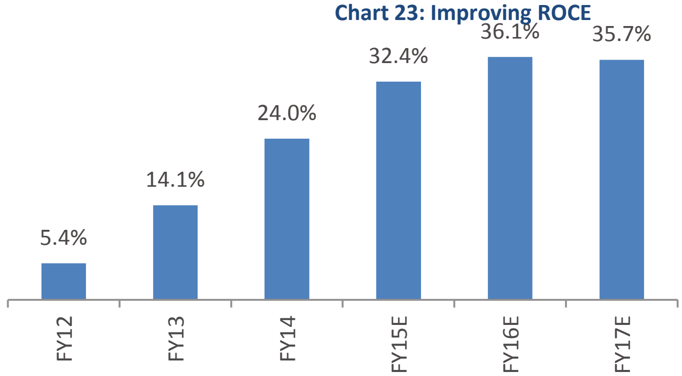
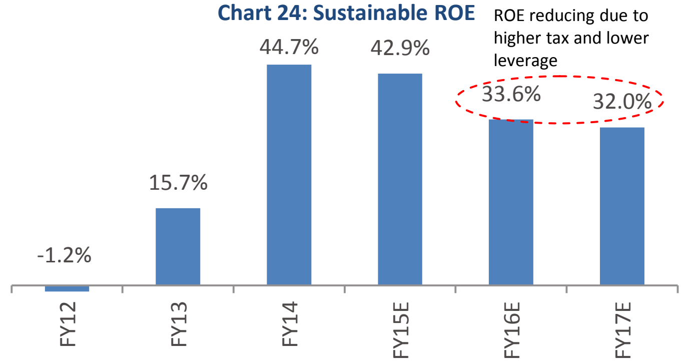


Chart 24: Sustainable ROE

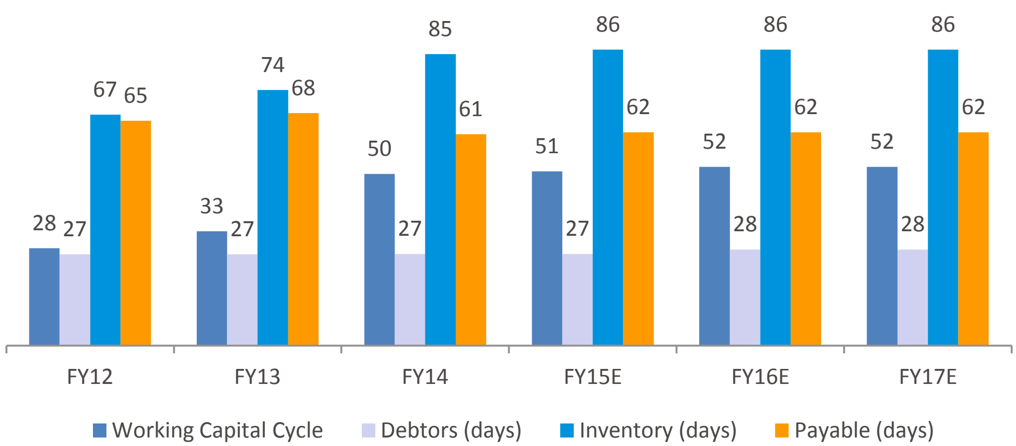


Source: Edel Invest Research

Working Capital Cycle:

The company has been successfully maintaining a lean working capital cycle. Debtor days have reduced from a peak of 51 days in FY08 to a constant 27 days.

Chart 25: Stable Working Capital

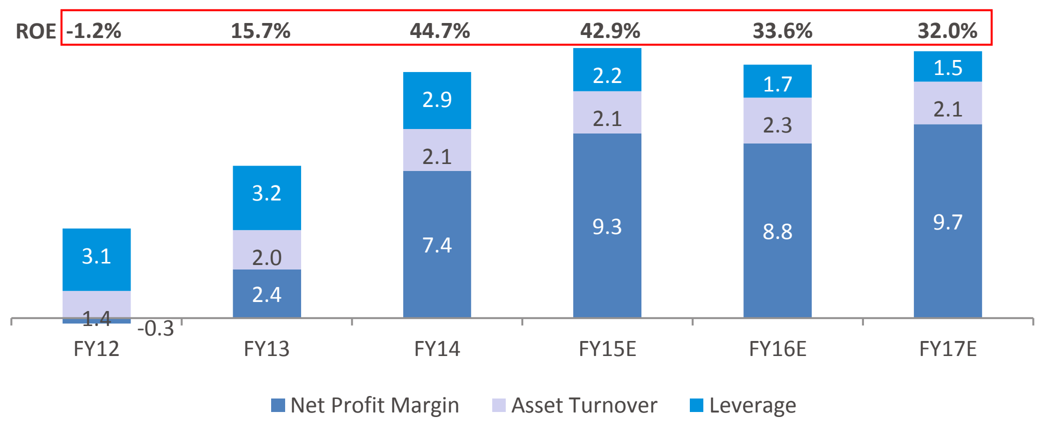


Source: Edel Invest Research

Du Pont Analysis: Composition of ROE to improve led by higher asset turns

With net profit margins at 7.4%, asset turnover at 2.1x and leverage at 2.9x, ROE is currently healthy at 45%. Going forward, we expect ROE and the quality of ROE to improve with steady asset turns, stable operating margins and reducing leverage.

Chart 26: Du Pont Analysis



Source: Edel Invest Research

Hedging Policy

The company entered into derivatives contracts during FY06 - 07. Those contracts led to derivative losses of INR 70 cr in FY08. This was one of the reasons for ICIL entering CDR. Post the debacle, ICIL formed policy not to keep forex risk open. As soon as the company gets contract confirmation from the client, it hedges the currency risk by entering into forward contracts with banks. As a part of the company's accounting policy, sales are shown on actual realization and the gain/(loss) on the forward is shown as part of other income/expenses.

TUF Loan subsidy

During FY14, ICIL had total long term loan of INR 113 cr. The total interest on long-term loan charged to P&L is INR 12.6 cr. This translates into interest rate of 10.25% but post the adjustment of TUF subsidy of INR 5.57 cr, the effective interest cost on term loan turns out to be 6.25%. Post the company's exit CDR going forward, the effective interest cost will come down by ~1-1.5%.

Future cap-ex will be eligible for Centre TUF subsidy and subsidy from the Maharashtra govt. This will lead to effective interest cost for new cap-ex to be around 1-2.5%.

Table 5: Break up of Debt

	FY12	FY13	FY14
Term loan	172	150	113
Working capital loan	163	244	310
Term loan rate		10%	10%
Term loan rate (adj. for TUF subsidy)	5%	6%	6%
Working capital loan rate	11%	11%	9%

Financials

Income statement (INR cr)

Year to March	FY13	FY14	FY15E	FY16E	FY17E
Net Sales	1,187	1,468	1,642	1,928	2,264
Other Operating Income	22	22	29	8	8
Income from operations	1,208	1,489	1,671	1,936	2,272
Direct costs	938	1,121	1,215	1,418	1,652
Employee costs	51	58	65	74	86
Other expenses	174	187	191	205	236
Total operating expenses	1,113	1,309	1,406	1,623	1,889
EBITDA	96	180	266	313	384
Depreciation and amortisation	18	20	20	22	26
EBIT	77	161	245	292	357
Interest expenses	50	50	60	50	47
Other income	9	9	9	13	20
Profit before tax	36	120	194	254	331
Provision for tax	7	9	39	84	109
Core profit	30	110	155	170	222
Extraordinary items	(0)	0	(15)	0	0
Profit after tax	29	111	140	170	222
Minority Interest	0	0	0	0	0
Share from associates	0	0	0	0	0
Adjusted net profit	29	111	140	170	222
Equity shares outstanding (mn)	3.8	3.8	4.1	4.1	4.1
EPS (INR) basic	7.8	29.1	38.0	41.7	54.2
Diluted shares (mn)	3.8	3.8	4.1	4.1	4.1
EPS (INR) fully diluted	7.8	29.1	38.0	41.7	54.2
Dividend per share	0.0	0.0	0.0	0.0	0.0
Dividend payout (%)	0.0	0.0	0.0	0.0	0.0

Common size metrics- as % of net revenues

Year to March	FY13	FY14	FY15E	FY16E	FY17E
Operating expenses	92.1	87.9	84.1	83.8	83.1
Depreciation	1.5	1.3	1.2	1.1	1.2
Interest expenditure	4.1	3.4	3.6	2.6	2.0
EBITDA margins	7.9	12.1	15.9	16.2	16.9
Net profit margins	2.4	7.4	8.4	8.8	9.7

Growth metrics (%)

Year to March	FY13	FY14	FY15E	FY16E	FY17E
Revenues	50.0	23.2	12.2	15.9	17.4
EBITDA	95.3	88.5	47.2	18.0	22.4
PBT	1,260.1	231.6	62.2	30.9	30.1
Net profit after minority interest	1,302.0	277.8	26.6	21.4	30.1
EPS	1,377.5	274.0	30.7	9.6	30.1

Profit & Efficiency Ratios

Year to March	FY13	FY14	FY15E	FY16E	FY17E
ROAE (%)	15.7	44.7	42.9	33.6	32.0
ROACE (%)	14.1	24.0	32.4	36.1	35.7
Debtors (days)	27	27	27	28	28
Current ratio	2.0	2.3	2.3	2.3	2.7
Debt/Equity	2.1	1.5	0.8	0.4	0.5
Inventory (days)	74	85	86	86	86
Payable (days)	68	61	62	62	62
Cash conversion cycle (days)	33	50	51	52	52
Debt/EBITDA	4.3	2.4	1.3	0.8	1.0
Adjusted debt/Equity	2.1	1.4	0.7	0.4	0.2

Valuation parameters

Year to March	FY13	FY14	FY15E	FY16E	FY17E
Diluted EPS (INR)	7.8	29.1	38.0	41.7	54.2
Y-o-Y growth (%)	*(1,377.5)*	*274.0*	*30.7*	*9.6*	*30.1*
CEPS (INR)	12.6	34.2	42.9	47.0	60.7
Diluted P/E (x)	43.8	11.7	8.9	8.2	6.3
Price/BV(x)	6.6	4.3	3.3	2.4	1.7
EV/Sales (x)	1.4	1.1	1.0	0.8	0.7
EV/EBITDA (x)	17.7	9.4	6.4	5.1	4.1
Diluted shares O/S	3.8	3.8	4.1	4.1	4.1
Basic EPS	7.8	29.1	38.0	41.7	54.2
Basic PE (x)	43.8	11.7	8.9	8.2	6.3
Dividend yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%

Balance sheet (INR cr)

As on 31st March	FY13	FY14	FY15E	FY16E	FY17E
Equity share capital	38	38	41	41	41
Warrants	1	2	0	0	0
Reserves & surplus	157	251	381	540	751
Shareholders funds	195	289	422	581	792
Secured loans	364	396	335	255	385
Unsecured loans	47	38	0	0	0
Borrowings	413	435	335	255	385
Minority interest	1	5	5	5	5
Sources of funds	**610**	**732**	**762**	**841**	**1,182**
Gross block	630	642	712	737	887
Depreciation	271	296	316	338	364
Net block	360	346	396	399	523
Capital work in progress	2	0	2	2	2
Total fixed assets	361	347	398	401	525
Goodwill	0	0	0	0	0
Investments	0	0	0	0	0
Inventories	246	346	394	456	535
Sundry debtors	88	109	122	149	174
Cash and equivalents	9	31	34	47	186
Loans and advances	112	160	167	194	227
Other current assets	3	6	0	0	0
Total current assets	457	651	717	845	1,123
Sundry creditors and others	224	251	284	329	386
Provisions	6	28	30	31	33
Total CL & provisions	229	279	314	360	419
Net current assets	227	372	404	485	704
Net Deferred tax	(37)	(37)	(40)	(45)	(47)
Misc expenditure	0	0	0	0	0
Uses of funds	**552**	**682**	**762**	**841**	**1,182**
Book value per share (INR)	52	78	104	143	195

Cash flow statement (INR cr)

Year to March	FY13	FY14	FY15E	FY16E	FY17E
Net profit	30	110	170	170	222
Add: Depreciation	18	20	20	22	26
Add: Misc expenses written off	0	0	0	0	0
Add: Deferred tax	0	0	3	5	2
Add: Others	0	0	0	0	0
Gross cash flow	49	130	194	197	250
Less: Changes in W. C.	84	122	28	69	80
Operating cash flow	(35)	8	165	128	170
Less: Capex	10	5	72	25	150
Free cash flow	**(45)**	**3**	**93**	**103**	**20**

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