

SINCE 1986

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October 2017



## The Trick Is To **Spot Them** At The **Larval Stage**

BSE Code	: 540048
Time Duration	: 1 year
CMP	: ₹389 (as on 26 October, 2017)
Target Price	: ₹526

## S P Apparels

# SPINNING CAPACITY AND CROCODILE STORE ADDITION TO WEAVE GROWTH

Our Tiny Treasure for the month of October is S P Apparels Ltd. (SPAL). It was established in 1989 and is a leading manufacturer and exporter of knitted garments for infants and children in India. The company supplies these products to leading global children's wear retailers like Tesco, Primark, Mothercare and Dunnes stores. It also manufactures and retails the menswear garments in India under brand name of 'Crocodile'. Currently, it has 23 manufacturing units in and around Avinashi, Tamil Nadu. The company was listed on BSE and NSE through a successful IPO in 2016.

### Robust capacity expansion

SPAL is planning integration and expansion of its manufacturing facilities to increase its operational efficiency. During FY17, the company installed 19 knitting machines and 300 sewing machines. It is expanding the yarn capacity to source all yarn requirements internally and have established a knitting facility to reduce third-party dependence for manufacturing. This will include the expansion of spinning facility from 16,896 spindles to 22,272 spindles and increasing the blow-room capacity from the current 3,200 kg of cotton per day to 15,015 kg per day. The company incurred capex of Rs 47.24 crore for this expansion. We expect this would aid revenue by 10-15% and improve margins which were affected by GST roll-out. It is also setting up a new knitting facility in the spinning facility with capex of Rs 16.86 crore. All of the capex would be sourced from net proceeds received from the IPO last year.

### Getting strong in international market

SPAL is showing persistent growth in export markets by adding new customers and is building a leadership position in all children wear apparel categories. It has forayed into new geographies and has also penetrated the US region. Till now, its top five customers were based out of the EU region, primarily from the UK. Recently, it has added three major customers based out of the US region and France. All the three additions are volume customers and the company has already started production for them. The company is expecting large volume of orders from these customers in the upcoming quarters. Exports are expected to grow by 12-15% YoY. These orders will help generate revenue and improve the growth rate.

### Promotion and expansion of 'Crocodile' brand

SPAL manufactures and retails wide range of menswear products such as shirts, T-shirts, polo shirts, jeans, trousers, jackets, etc. as also the innerwear products. It operates through large format stores like Central, D-Mart, Star Bazaar, Walmart, Brand Factory and many more. These products are also available on leading e-commerce platforms such as Flipkart, Amazon and Jabong. Currently, it has presence in nine states of India. The awareness and preference for branded products is rising in semi-urban and rural areas. So, the company is focusing to expand in Tier-II, Tier-III and Tier-IV cities in India. With capex of Rs 27.85 crore, SPAL is establishing 70 new retail COCO stores and 160 large format stores and expanding to nine more states in India in the upcoming three years.

### Strong prospects for Indian textile and apparel industry

The textile sector contributes roughly 11% of the total exports from India amounting to USD 40bn in FY16. The Indian textile industry contributes ~5% to the GDP. Some key growth drivers for exporting apparels from India could be expertise of Indian manufacturers to produce garments at lower costs, acceptance and understanding of global brands with continuous efforts to maintain innovation and creativity, increasing government initiatives to promote exports from India, rising demand from retailers which are preferring Indian products over China. The Indian government has allowed 100% FDI in the textile sector and in the Budget 2017-18, it has allocated major chunk of funds for this sector. For encouraging new entrepreneurs, the government has allocated Rs 244,000 crore to Mudra Bank.

### Positive impact of GST on textiles in the long run

The implementation of the GST saw the textile industry facing utmost pressure. It was because tax rate under the GST is higher than the pre-GST tax rate. Natural fibres, which were earlier exempt from tax, have now been brought under the ambit of GST. But GST is going to benefit the industry in the long run as the input credit chain would break, manufacturing costs would reduce and input credit would be allowed on capital goods. The

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GST would also curb duty drawbacks, which would boost textile exports from the country. We see that textile and apparel companies would benefit from this tax reform and would contribute more than 11% towards the total exports.

### Financial Performance

The company's revenue has grown at a CAGR of 10% during FY13-17. Its profit has grown at a CAGR of 110.23% over FY13-17. It recorded total revenue of Rs 656.68 crore for FY17, as against Rs 537.75 crore in FY16, showing growth of 22.12% YoY. Its EBITDA in FY17 grew 42.3% YoY to Rs 128.36 crore from Rs 90.24 crore in FY16. Its PAT jumped 225.26% YoY to Rs 60.66 crore in FY17 from Rs 18.65 crore in FY16. The company's debt-equity ratio for FY17 stood at 0.4x which improved from 2.7x in FY14. It has paid off debt of Rs 63 crore from the IPO proceeds. The interest coverage ratio was 7.7x in FY17. The company paid dividend of 5% in FY17.

Although in Q1FY18, the company's revenue de-grew by 5% YoY due to the Brexit issue, its EBITDA margin improved from 17.9% to 18.2% YoY and PAT margin grew marginally from 7% to 7.1% YoY. We expect to see some pressure on margins in Q2FY18 due to GST.

### Valuation

The company is trading at TTM P/E of 17.6x with TTM EPS of Rs 22.48. It has delivered ROE and ROCE of 25.12% and 22.69%, respectively, for FY17. Due to growing awareness and need for quality products, the demand for branded children's wear is increasing globally and SPAL is efficiently meeting this demand. Its robust spinning capacity expansion will boost its revenues. Its foray into new geographical areas and aggressive expansion of its stores for Crocodile brand will stimulate the margins. We expect an upside of 35% with target price of Rs 526 over a period of one year.

### Inc/Exp Statement(Consolidated) (Rs in Crore)

Description	201703	201603	201503	201403	201303
Net Sales	635.65	532.83	472.57	450.87	428.50
Total Income	656.68	537.75	481.51	453.10	436.73
Total Expenditure	528.31	447.52	406.14	388.30	377.96
PBIDT	128.37	90.24	75.36	64.80	58.77
PAT	60.66	18.65	9.68	6.46	2.03
Dividend %	10.00	--	--	--	--
Adj. EPS(Rs)	23.81	8.41	5.59	3.97	1.41

### Quarter On Quarter (Consolidated) (Rs in Crore)

Particulars	201706	201703	Q on Q Var%	201606	Y on Y Var%
Net Sales	150.61	158.10	-4.74	162.21	-7.15
Total Expenditure	131.85	132.08	-0.17	134.66	-2.08
PBIDT (Excl OI)	18.76	26.02	-27.89	27.55	-31.91
PAT	11.05	16.11	-31.41	11.51	-3.99
PBIDTM% (Excl OI)	12.46	16.46	-24.30	16.99	-26.66
PBIDTM%	19.40	20.02	-3.10	18.25	6.30
PATM%	7.34	10.19	-27.97	7.09	3.53
Adj. EPS(Rs)	4.46	6.47	-31.07	7.22	-38.23

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