BED, BATH AND BEYOND

Will Trident's accelerated push in the home-textiles business sustain its next leg of growth?

"Our focus is to ramp up utilisation and strengthen marketing to reach new customers, besides increasing our market share

— **RAJINDER GUPTA**
Chairman, Trident Group

PHOTOGRAPHS BY VISHAL KOUL

Jash Kriplani

There aren't too many businesses in which India can boast of a significant lead over China. However, home textiles is one such sector where India is in the lead, thanks to its cotton surplus position and relatively low cost of labour. With a 40% share in the US terry towel market and 48% share in the US bed sheet market, India towers over China which has a 23% share in the terry towel market and 22% of the bed sheet market. The US accounts for $7.5 billion or about 17% of the $45 billion global home textiles market.

Making the most of this significant advantage is the Ludhiana-based Trident, which has snapped up around 16% of the US market. The company, which started as a yarn manufacturer in the early 1990s, has moved up the value chain to manufacture terry towels in 1998 and bed linen in the last quarter of FY16. Over the past two years, the company has invested significantly in expanding its capacity across these two products to capture a larger share of both the international and domestic markets and is now looking to build on its position of strength.

MOVING UP THE VALUE CHAIN

Trident moved into the terry towel business in 1998 by setting up a plant in Barnala, Punjab. A bitter experience with the Punjab government when it acquired land for expanding capacity in 2008 forced Trident to look beyond its home turf for its future expansion plans. In FY09, Tri-

A rich tapestry

Over the years, Trident has invested significantly to cater to global demand

Bed Sheet
Budhni, MP
1 Unit | 500 Looms
43.2 Mn Mtrs/pa

Paper
Barnala, Punjab
2 Units |
175,000 MT/pa

Bath Linen
Budhni, MP
1 Unit | 300 Looms
48,000 MT/pa

Barnala, Punjab
3 Units | 388 Looms
42,000 MT/pa

Yarn
Budhni, MP
5 Units | 3.8 Lac Spindles
1,920 Rotors

Barnala, Punjab
5 Units | 1.8 Lac Spindles
3,584 Rotors

dent set up its first facility outside of Punjab in Budhni, Madhya Pradesh to manufacture yarn. This was followed by a terry towel plant that was set up in FY15 with a capacity to produce 48,000 tonne per annum—which incidentally is the largest terry towel unit in the world, according to the company.

Trident's new plant at Budhni is highly automated making it less labour intensive. For instance, while in Punjab the cutting still takes place manually, in Budhni, it is an automated process. And instead of following a batch process, the Budhni plant follows a continuous processing of fabric. "These automated processes save time, reduce errors, control costs and also improve quality," says Rajinder Gupta, chairman, Trident Group.

The company currently gets 85% of its bed and bath linen revenues from exports, while the remaining comes from the domestic market

After the Budhni plant was set up, the combined towel capacity of Trident increased to 90,000 tonne per annum. In FY16, Trident added bed linen to its product mix by setting up another plant at Budhni with a capacity of 43 million metres. The company spent around ₹2,700 crore to expand capacity in terry towels (₹1,200 crore), spinning (₹700 crore) and bed linen (₹750 crore) and the focus is to now leverage the beefed-up capacity. "Our capex cycle that started two years ago is finally over. From FY17, we have been in a consolidation mode. Our focus is to ramp up utilisation and strengthen marketing, to reach new customers besides increasing market share," says Gupta.

At present, Trident's terry towel plants across Punjab and Madhya Pradesh have a capacity utilisation of 50%, and the bed linen unit is operating at 30% since it is a relatively new facility. The management expects the utilisation in its terry towel and bed linen facilities to improve to 60% and 45% respectively in FY18 as they ramp up their marketing efforts.

The company is banking on its long list of marquee clients, both in the international and domestic markets, to drive overall volumes higher. It has a long standing relationship with retail giants such as Wal-Mart, JC Penny, Target, IKEA, etc. While in the domestic market, Trident has a relationship with leading hotel chains such as Taj, Oberoi, Hyatt Regency, Inter-Continental, ITC and large retail chains such as Shoppers Stop, Metro Cash & Carry, Big Bazaar and D-Mart. The company currently gets 85% of its bed and bath linen revenues from exports, while the balance comes from the domestic market.

Apart from expanding its global footprint, Trident is also looking to increase its share of the domestic market. As Gupta points out, "About 70% to 80% of the domestic home textile market is still unorganised. Large players don't have a significant market share here. We are globally competitive but in the domestic market we still face certain distribution channel issues. Despite that, over the past two years we have been trying to expand our presence in the domestic market as well."

While the company has moved up the textile value chain, its legacy yarn business still contributes about 34% of overall revenues. Around 35% of total yarn produced is consumed in-house, while the rest is sold in the market. Analysts believe that as Trident increases its sales from terry towel and bed linen, yarn's contribution to sales could come down to as low as 21%. At the same time, increased terry towel and bed linen production will ensure that internal consumption of yarn remains robust. Bhavesh Chauhan, analyst at IDBI Capital, sees 45% of the yarn produced being consumed by the company in FY18. As the contribution from yarn to overall revenues declined from 75% in 1999 to 34% in 2016 and the share of value-added products increased, the company's stand-alone margins almost doubled from 11% to 20% during the same period.

BETTER DAYS AHEAD

With all the planned capacity expansion complete, analysts expect improving operating leverage to drive earnings. "If demand momentum continues to sustain in the overseas markets, Trident will see increased capacity utilisation as it continues to tap new geographies and new customers," says Deepak Jasani, head – retail research, HDFC Securities. IDBI Capital's Chauhan breaks down how this operating leverage could play out in the near to medium term. "At present, utilisation of the bed-linen capacity at 30% is yet to reach break-even. We expect to see a significant improvement in its return ratios by FY20 once it starts to operate at its optimal capacity." By 2020, he estimates the terry towel business to generate revenues of ₹1,794 crore and bed linen business to bring in sales of ₹1,000 crore which is nearly double its current (FY16) revenues. Consequently, he expects the RoE

What's in store

Higher capacity utilisation will lead to better operating margin and return ratios

₹Cr	Revenue	EBITDA	EBITDA(%)	Adj.PAT	EPS (₹)	PE(x)	EV/EBITDA (x)	ROE (%)	ROCE (%)
FY15	3,755	661	17.6	118	2.3	30	7.4	9.9	14.1
FY16	3,684	719	19.5	229	4	17	8.4	14.2	10.7
FY17E	4,642	952	20.5	338	6.6	10.5	5.4	18.1	13.5
FY18E	5,046	1,058	21	417	8.2	8.5	4.2	19.7	17.2

Source: IDBI Capital

"The high-margin paper business will be a steady source of revenue in the coming years

—VINAY KHATTAR
Head of research - Equity, Edelweiss

"With rising sales and no major capex, we expect free cash flows to be utilised to deleverage the balance sheet

—BHAVESH CHAUHAN
Research analyst, IDBI Capital

"If demand sustains in the overseas markets, Trident will see increased capacity utilisation as it taps new geographies

—DEEPAK JASANI
Head - retail research, HDFC Securities

Analysts believe that as Trident increases its sales from terry towels and bed linen, yarn contribution to revenue could come down to as low as 21%

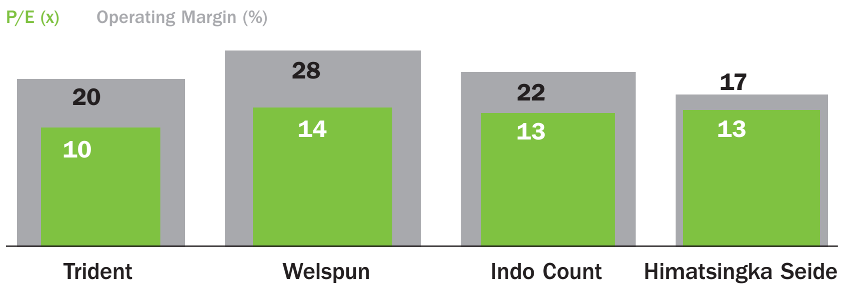
to more than double from 14.2% to 42% and RoCE to move up from 10.7% to 18% respectively. Over the past three years (FY14-FY16), the RoCE has declined from 27% to 10.7% as the company made significant investments in expanding its capacity. But as utilisation levels pick up, the assets should start generating better returns.

Also, efforts to improve its overall profitability is reducing the company's overall debt burden. Trident repaid a total of ₹445 crore during the first nine months of FY17, including ₹159 crore of high-cost debt. As on December 31, 2016, the company had a long-term debt of around ₹2,072 crore, of which more than 75% is covered under the Technology Upgradation Fund (TUF) scheme. The average interest cost for the loans under TUF is less than 3%. The fact that the company has managed to bring down its debt-equity ratio from 3x in FY13 to 1.89x in FY16 and improve its interest coverage ratio, which has gone up from 1.3x to 3.03x during the same period, is definitely an indication that the company is well placed to manage its debt burden. In FY16, the company paid ₹136 crore as interest costs, which accounted for 3.7% of its net sales. With the company aiming to pay off loans worth ₹450 crore in FY18, the interest burden is likely to come down to ₹125 crore. "The repayment of some of its high-cost debt ahead of the repayment schedule will lead to a stronger balance sheet and reduce its leverage risk," says Prasanth Victor, analyst, Karvy Stock Broking.

Apart from enjoying a formidable position in home textiles, Trident is also the largest wheat straw-based paper producer in the world with a capacity of 175,000 metric tonne per annum (mtpa). Wheat-straw, which is an agro waste, is easily available in Punjab, one of the largest producers of wheat in India. The paper business currently operates at more or less full capacity (around 92%). But, the company has no further plans to increase capacity, as its near-term focus will be on scaling up the textile business. Within the paper business, the company is focusing on increasing the contribution of branded copier paper that enjoys higher margins and makes up about 50% of the segment's revenues. The company currently derives 19% of its revenues from the paper business, which was merged with the textiles business in 2002. Vinay Khattar, head of research at Edelweiss believes the company's paper business will be a steady source of revenue for Trident given its ability to generate cash at higher margins (36.3%).

Going cheap

Trident seems relatively cheap compared to its peers



Source: Brokerage reports, Ace Equity

STILL SOME STEAM LEFT

At current prices, Trident is trading at 10x its one-year-forward earnings. The stock looks relatively inexpensive even when compared with its peers. For instance, Welspun, Indo Count and Himatsingka Seide trade at valuations that are as much as 37% premium to Trident's multiple (*See: Going cheap*). While each of the large companies have their own niches, Trident's valuation looks attractive on a relative basis given its expected earnings growth. Indo Count Industries has an asset-light model and operates a tightly-run manufacturing capacity. Himatsingka Seide also has an asset-light model and comes with a strong portfolio of brands such as Calvin Klein Home, Espirit, Peacock Alley and Atmosphere. While Welspun did take a beating last year when its bed linen products didn't meet requisite standards, it enjoys a premium position with a market share of about 10% and 20% share in bed sheets and terry towel in the US home textiles market.

Over the past five years, Trident's revenues have grown at an average of 8% and profits have grown at a faster clip at 28%, given the expansion in margins

Over the past five years, Trident's revenues have grown at an average of 8% and profits have grown at a faster clip at 28%, thanks to higher margins. According to Chauhan at IDBI Capital, Trident's revenue is likely to grow at an average of 15.5% over FY16-FY19 and net profit will see a healthier increase at 34.5% as capacity utilisation improves and operating leverage kicks in. "With rising sales of terry towel and bed linen and no major capex in the near future, we expect free cash flow to be utilised to deleverage the balance sheet and pay dividends. Hence, we expect the stock to trade at higher-than-historical multiples," he says. Over the past one year, the stock has gained by 65% compared to an 18% gain by the benchmark Sensex. Despite the run-up, with several triggers yet to play out and a relatively inexpensive valuation. Trident does make for an interesting cut.