



INDEPENDENT **EQUITY** **RESEARCH**

Nahar Spinning Mills Ltd

Initiating coverage

Enhancing investment decisions

Explanation of CRISIL Fundamental and Valuation (CFV) matrix

The CFV Matrix (CRISIL Fundamental and Valuation Matrix) addresses the two important analysis of an investment making process – Analysis of Fundamentals (addressed through Fundamental Grade) and Analysis of Returns (Valuation Grade) The fundamental grade is assigned on a five-point scale from grade 5 (indicating Excellent fundamentals) to grade 1 (Poor fundamentals) The valuation grade is assigned on a five-point scale from grade 5 (indicating strong upside from the current market price (CMP)) to grade 1 (strong downside from the CMP).

CRISIL Fundamental Grade	Assessment	CRISIL Valuation Grade	Assessment
5/5	Excellent fundamentals	5/5	Strong upside (>25% from CMP)
4/5	Superior fundamentals	4/5	Upside (10-25% from CMP)
3/5	Good fundamentals	3/5	Align (+-10% from CMP)
2/5	Moderate fundamentals	2/5	Downside (negative 10-25% from CMP)
1/5	Poor fundamentals	1/5	Strong downside (<-25% from CMP)

Analyst Disclosure

Each member of the team involved in the preparation of the grading report, hereby affirms that there exists no conflict of interest that can bias the grading recommendation of the company.

Additional Disclosure

This report has been sponsored by NSE - Investor Protection Fund Trust (NSEIPFT).

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Nahar Spinning Mills Ltd

Knitting large growth patterns

Fundamental Grade 3/5 (Good fundamentals)
Valuation Grade 5/5 (CMP has strong upside)

Industry Textiles, Apparel & Luxury Goods

Nahar Spinning Mills Ltd (Nahar Spinning) manufactures cotton yarn and knitted garments. It is the largest exporter of cotton yarn in India. Given its large-scale operations, relatively low gearing among peers and healthy demand prospects in the cotton yarn industry, we assign Nahar Spinning a fundamental grade of '3/5', indicating that its fundamentals are 'good' relative to other listed securities in India.

Capacity expansion to feed growing demand

Nahar Spinning, with a capacity of 3,46,096 spindles and 720 rotors, is the second largest player in the highly fragmented domestic cotton yarn industry. The company is in the process of adding 90,000 spindles over the next two years in a phased manner. We believe that the expanded capacity will help it better capitalise on the healthy demand prospects in the cotton yarn segment.

Higher bargaining power lowers material costs

Nahar Spinning and Nahar Industrial, a group company, together purchase their cotton requirement, which accounts for ~3% of India's cotton production, resulting in higher bargaining power. Further, the company has also forward integrated into the manufacturing of garments. The entire cotton yarn requirement for manufacturing of garments is met indigenously. Integrated operations, large scale of procurement and an efficient procurement strategy have translated into operating efficiencies for Nahar Spinning.

Garments segment - high client concentration risk

Majority of garment revenues (~94% in FY10) is earned through exports to the US. Nahar Spinning caters to three customers in the US - GAP, Philippe Van-Heusen and CHAPS which results in high business concentration risk. Its dependence on few clients reduces its bargaining power and limits its ability to pass on hikes in input prices.

Expect three-year revenue CAGR of 23%

We expect revenues to register a three-year CAGR of 23% to Rs 20 bn in FY13 largely driven by higher realisations in the cotton yarn segment and recent increase in export demand due to tight supply of cotton in the global market. PAT margin is expected to expand to 6.7% in FY13 with an ROE of 16.8%.

Valuations – the current market price has 'strong upside'

CRISIL Equities has used the discounted cash flow method to value Nahar Spinning and arrived at a fair value of Rs 136 per share. This fair value implies P/E multiples of 3.8x FY11E and 4.3x FY12E earnings.

KEY FORECAST

(Rs mn)	FY09	FY10	FY11E	FY12E	FY13E
Operating income	10,008	11,093	14,966	17,031	20,472
EBITDA	1,346	1,928	3,202	3,331	3,741
Adj net income	(165)	539	1,276	1,175	1,376
Adj EPS-Rs	(4.6)	14.9	35.3	32.6	38.1
EPS growth (%)	(238.3)	(421.6)	138.5	(7.8)	17.0
Dividend yield	0.4	0.8	5.6	5.1	7.2
RoCE (%)	4.7	9.6	16.1	13.7	14.5
RoE (%)	(3.2)	10.1	21.0	16.5	16.8
PE (x)	(28.8)	15.6	2.7	2.9	2.5
P/Bv (x)	0.9	1.5	0.5	0.4	0.4
EV/EBITDA (x)	8.1	8.7	4.3	4.4	4.1

NM: Not meaningful; CMP: Current Market Price

Source: Company, CRISIL Equities estimates

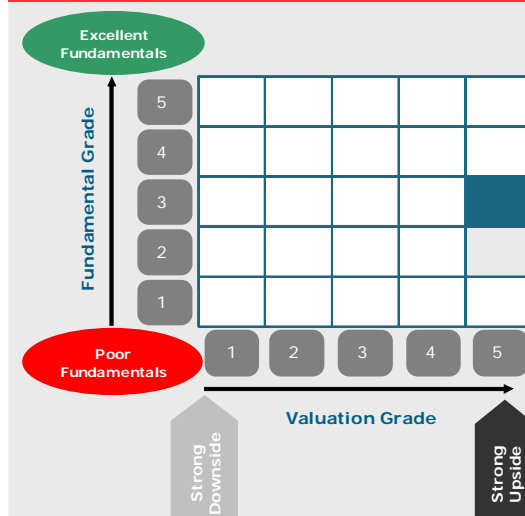


February 25, 2011

Fair Value Rs 136

CMP Rs 95

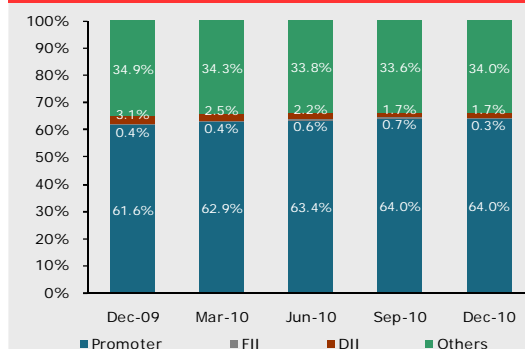
CFV MATRIX



KEY STOCK STATISTICS

NIFTY	5604
NSE ticker	NAHARSPING
Face value (Rs per share)	5
Shares outstanding (mn)	36
Market cap (Rs mn)/(US\$ mn)	4,404/96
Enterprise value (Rs mn)/(US\$ mn)	12,780/280
52-week range (Rs) (H/L)	160/71
Beta	1.25
Free float (%)	36.0%
Avg daily volumes (30-days)	194,510
Avg daily value (30-days) (Rs mn)	24.3

SHAREHOLDING PATTERN



PERFORMANCE VIS-À-VIS MARKET

	Returns			
	1-m	3-m	6-m	12-m
NAHARSPING	-1%	-9%	5%	33%
NIFTY	-5%	-7%	5%	14%

ANALYTICAL CONTACT

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Table: 1 Nahar Spinning: Business environment

Product / Segment	Cotton yarn	Knitted and woollen garments
Revenue contribution (FY10)	76.2%	14.9%
Revenue contribution (FY12)	79.8%	13.0%
Product / service offering	Manufacturing of cotton, synthetic and blended yarn (~90% of the yarn manufactured is cotton yarn)	Manufacturing of knitted cotton and blended garments
Geographic presence	Exports: 73.1% of revenues as of FY10; major export destinations are Bangladesh, Brazil and Korea	Exports: 94% of revenues as of FY10; major export destination is the US
Market position	<ul style="list-style-type: none"> Second largest cotton yarn manufacturer in India in terms of capacity Overall market share of ~2% as of FY10 in terms of total production, indicating that the cotton yarn segment in India is highly fragmented 	<ul style="list-style-type: none"> Mid-sized player in the readymade garments (RMG) segment; however, does not house its own brands Approved supplier to reputed international US brands
Industry growth expectations	<ul style="list-style-type: none"> CRISIL Research expects domestic cotton yarn demand to grow at a CAGR of 6.5% from 2010-11 to 2015-16 	<ul style="list-style-type: none"> CRISIL Research expects RMG exports to grow at a CAGR of 7.6% from 2010-11 to 2015-16
Sales growth (FY08-FY10 – 2-yr CAGR)	8.1%	11.8%
Sales forecast (FY10-FY12 – 2-yr CAGR)	23.4%	12.7%
Demand drivers	<ul style="list-style-type: none"> Tight supply of cotton in the global markets will drive cotton yarn exports in the medium term Recovery in the global RMG segment 	<ul style="list-style-type: none"> Rising income levels and increase in discretionary spending
Key competitors	Vardhman Textiles, KPR Mills, Nahar Industrial Enterprises and Super Spinning Mills	Gokuldas Images, Network Clothing and Arvind Mills
Key risks	<ul style="list-style-type: none"> EBITDA margins are susceptible to volatile cotton prices Exposed to fluctuations in foreign exchange 	<ul style="list-style-type: none"> Client concentration risk is high as three customers account for ~90% of revenues from apparel exports Exposed to fluctuations in foreign exchange

Source: Company, CRISIL Equities

Grading Rationale

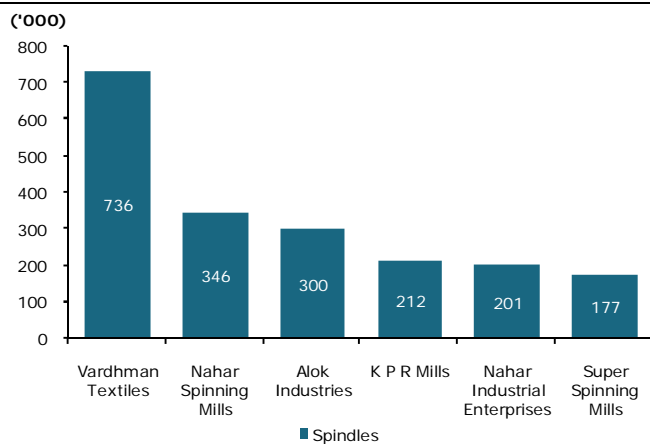
Large player in the textile industry

Nahar Spinning, with a capacity of 3,46,096 spindles and 720 rotors, is the second largest player in the highly fragmented domestic cotton yarn industry. Including the other promoter group company, Nahar Industrials, the Nahar group was the largest cotton yarn player in India in revenue terms in FY10.

The cotton yarn segment constituted ~76% of total revenues in FY10, of which ~73% was earned through exports to Brazil, China/Hong Kong, Bangladesh, Egypt and Korea. Nahar Spinning is also present in the RMG space, manufacturing knitted and woollen garments. Majority of garment revenues (~94% as of FY10) is earned through exports to the US.

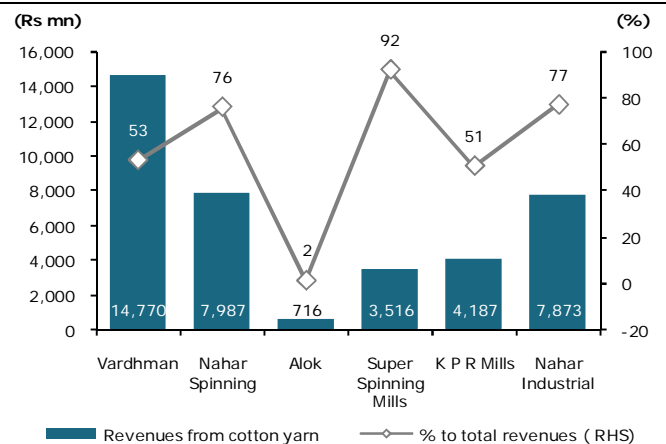
Nahar Spinning is the second largest cotton yarn manufacturer in India

Nahar has the second largest spindleage capacity



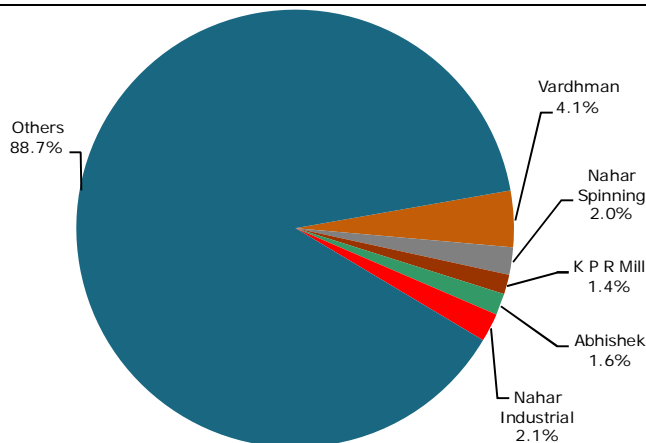
Source: Prowess

Revenues from cotton yarn as of FY10



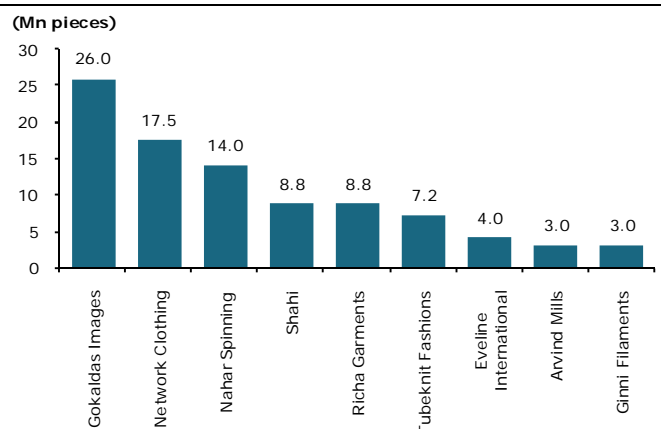
Source: Prowess

Market share: production as of FY10



Source: Prowess

Peer comparison: garments manufacturing capacity



Source: Prowess

Expansion in spindleage capacity to cater to...

Nahar Spinning is in the process of adding ~90,000 spindles (30,000 spindles each in three of its manufacturing units) in a phased manner over the next two years. The combined capex of the entire expansion plan is ~Rs 3,500 mn, of which Rs 1,930 mn is funded through TUFF loans at the rate of 6.6%. The expanded capacity is expected to become operational in FY12. Post expansion,

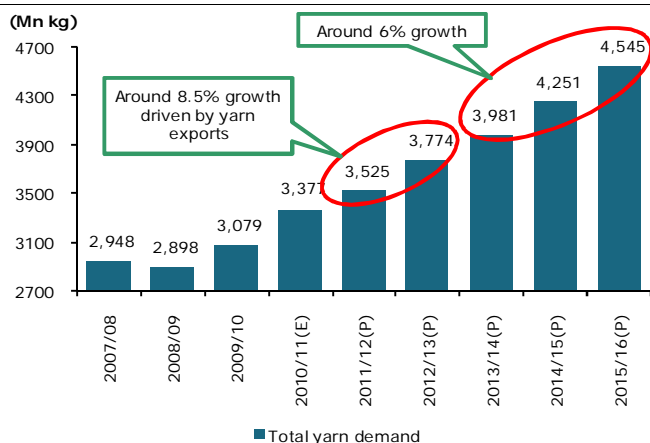
Nahar Spinning plans to add ~90,000 spindles in the next two years

Nahar Spinning will have a total capacity of ~440,000 spindles and 720 rotors. We believe that the expanded capacity will help Nahar Spinning better capitalise on the healthy demand prospects in the cotton yarn segment.

... pick-up in cotton yarn, RMG demand

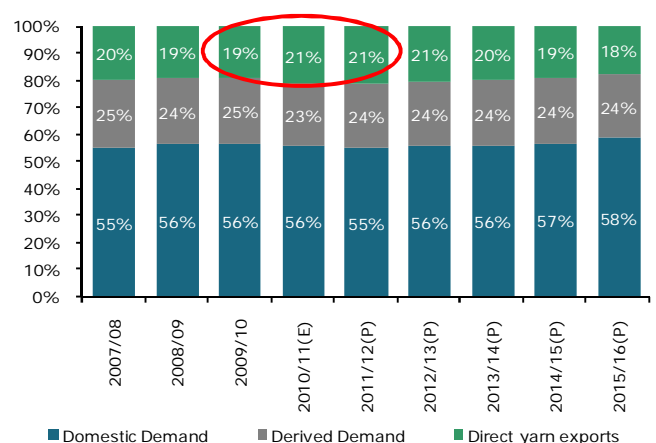
The demand for cotton yarn declined by ~2.8% during 2008-09 following the economic slowdown which adversely affected exports and local demand. However, with the speedy recovery in the domestic economy and improving consumer sentiments, the demand for cotton yarn is estimated to have improved by 6% during 2009-10. CRISIL Research expects cotton yarn demand to grow at a CAGR of 6.5% from 2010-11 to 2015-16. The main driver of the growth in the long term is expected to be domestic demand, which is expected to grow at a CAGR of 8.5% between 2010-11 and 2015-16. The share of cotton yarn exports is expected to increase in 2010-11 and 2011-12 on account of the spurt in export demand for cotton yarn following the tightened supply of cotton in the global market.

Figure 1: Cotton yarn demand on a growth trajectory



Source: Office of Textile Commissioner, CRISIL Research

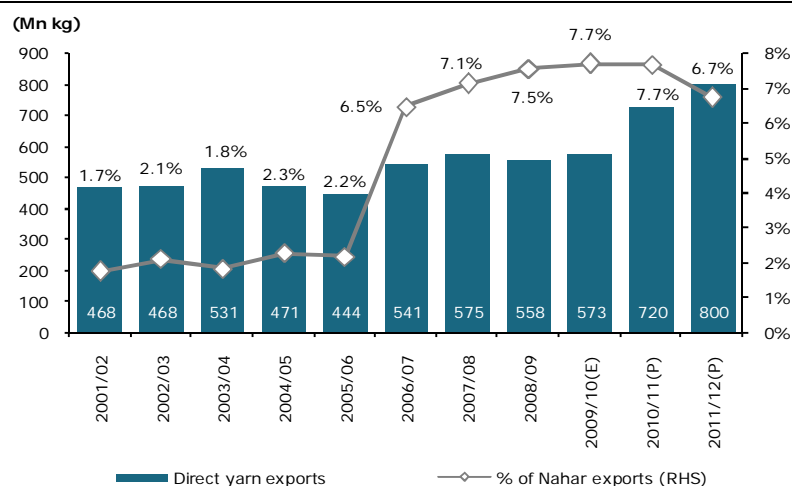
Figure 2: Share of yarn exports to increase



Source: Office of Textile Commissioner, CRISIL Research

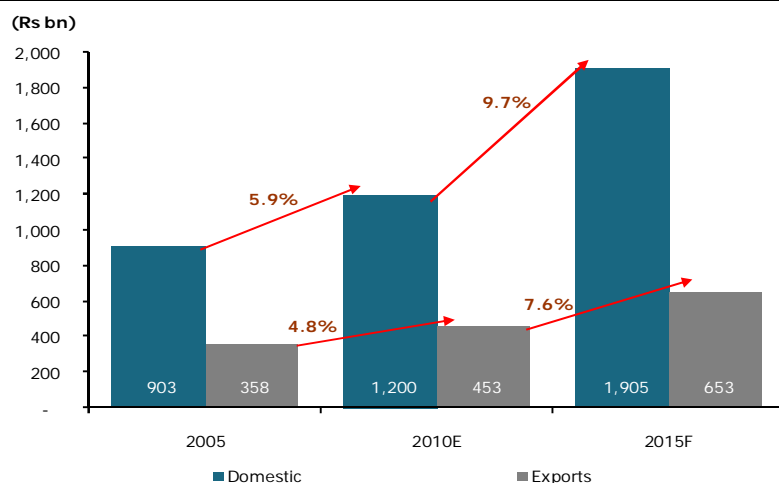
After declining by 3% in 2008-09, yarn exports rebounded sharply with 5.8% growth to 590 mn kg in 2009-10. The growth was driven mainly by higher imports from countries such as China and Korea. These countries had to temporarily increase their yarn imports from India due to restricted supply from Pakistan - a major yarn exporter - on account of floods in 2009-10. Pakistan had imposed a restriction of 35,000 tonnes per month and 15% duty on export of cotton yarn in order to meet rising domestic consumption. Going forward, post the stabilisation of production from Pakistan and other countries, cotton production is expected to increase and, hence, export demand for Indian cotton yarn will moderate.

Figure 3: Spurt in direct yarn exports in 2010-11



Source: Company, CRISIL Research

Figure 4: RMG exports growth slower than domestic market's



Source: CRISIL Research

Higher bargaining power lowers material costs

Nahar Spinning, being one of the largest manufacturers of cotton yarn in India, consumed ~83 mn kgs of raw cotton in FY10. Nahar Industrial Enterprises, another group company, consumed ~68 mn kgs in FY10. Nahar Industrial Enterprises and Nahar Spinning purchase their cotton on a combined basis, resulting in a higher bargaining power and cost savings for the company. They together consumed 0.15 bn kgs of cotton in FY10, 3% of the total cotton yarn production in the country during the same period. Majority of its cotton procurement takes place from October to April, which is the cotton season in India. Nahar Spinning maintains an average seven to eight months of cotton inventory.

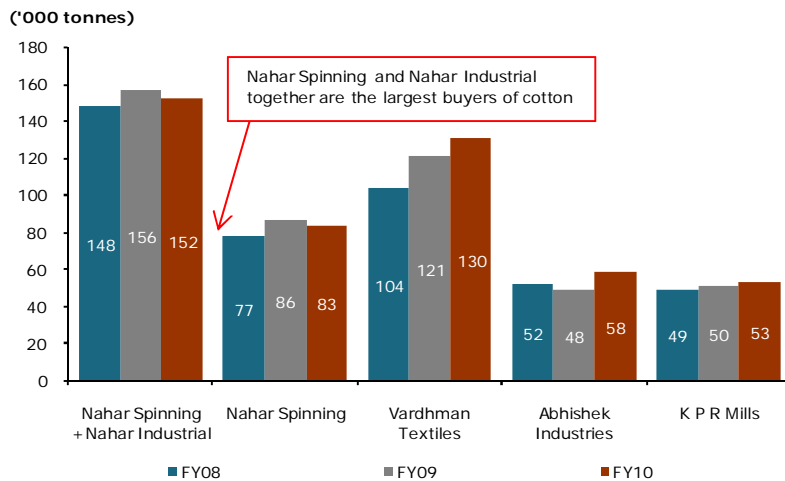
Anticipating a higher cotton price increase during 2009-10, the company procured cotton in bulk at lower prices. Consequently, older inventory of cotton at low prices and higher cotton yarn prices have enabled the company to report EBITDA margins of 17.4% in FY10 and ~22% as of nine months ended

Nahar Spinning accounts for a healthy ~7.7% of the total direct yarn exports; thereby emerging as the largest yarn exporter in India

Recovery post the global downturn has been slow in the export market; Nahar Spinning accounted for ~0.3% of total exports in FY10

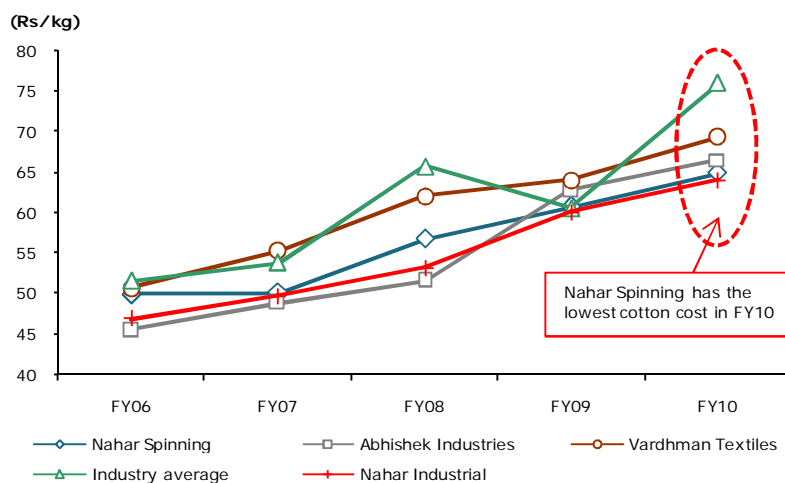
December 2010 in spite of a surge in cotton prices. Further, the company has also forward integrated into the manufacturing of garments. The entire cotton yarn requirement for manufacturing of garments is met through in-house production, thereby resulting in savings by avoiding external purchases of costlier yarn. Integrated operations, large-scale procurement and an efficient procurement strategy have translated into operating efficiencies for Nahar Spinning.

Figure 5: Peer comparison - quantity of cotton procured



Source: Prowess, CRISIL Equities

Figure 6: Cotton cost comparison amongst peers

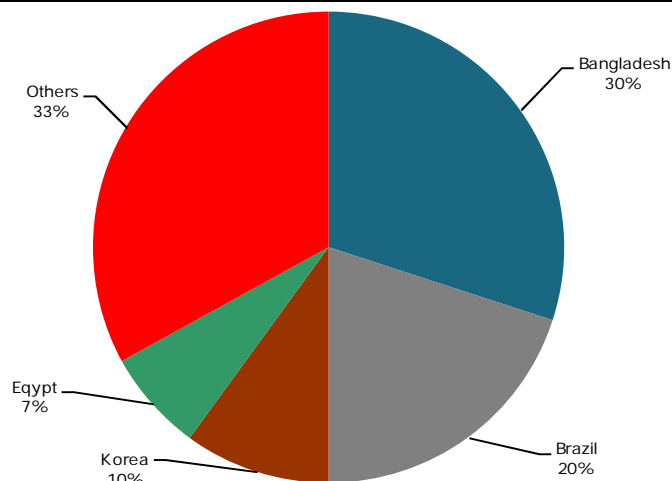


Source: Prowess, CRISIL Equities

Well placed in the cotton yarn export market

The company earned ~73% of its yarn segment revenues through yarn exports in FY10, of which ~30% was to Bangladesh. Recently, the government imposed a cap on exports of cotton yarn at 720 mn kgs. This cap is not expected to affect Nahar Spinning going by its FY10 export volumes that amounted to ~44 mn kgs or ~6% of the total cap on exports.

Figure 7: Geographic mix of clients in the yarn segment



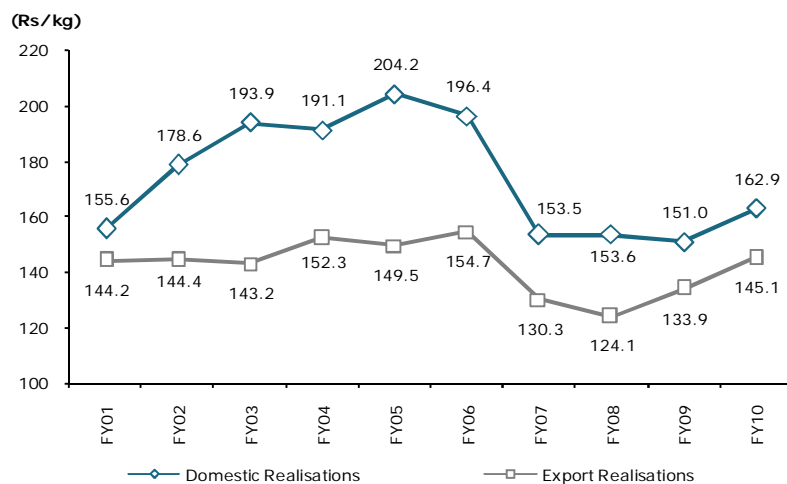
Source: Company, CRISIL Equities

Bangladesh is one of the major manufacturing destinations of garments and one of the largest importers of cotton yarn. However, few weavers in Bangladesh have backward integrated to producing yarn from cotton and hence importing higher quantities of cotton.

Bangladesh has added 5.2 mn spindles between 2000 and 2008, which is only ~20% of India's (36.8 mn) spindleage capacity, indicating that cotton yarn imports from Bangladesh will not be impacted significantly. Further, the incremental capacities are expected to be absorbed in the country itself, as demand is growing at a steady pace. We believe that Nahar Spinning is well positioned to cater to the growing demand in Bangladesh, given that it has established its presence in that region over many years. However, if players in Bangladesh continue to backward integrate, Nahar Spinning's ability to shift focus to other countries and attract clients in new geographies will be key in maintaining export revenues.

Nahar Spinning follows the strategy of exporting coarser counts (30s to 40s) to Bangladesh, Brazil and Korea, and selling finer counts (60s to 80s) in the domestic market. Hence, Nahar Spinning's domestic realisations are higher than that from the export markets. The type of counts sold depend on the customer's requirements. In Bangladesh, clients demand a higher proportion of coarse counts as it is used to make denim fabric and other cotton garments. Given the competition in the export market, we believe the company has so far been able to export to Bangladesh due to its competitive pricing. The company has one of the lowest cotton procurement prices due to its large size. Hence, we believe that competitive pricing could be sustainable in the medium term.

Figure 8: Domestic realisations of yarn > export realisations



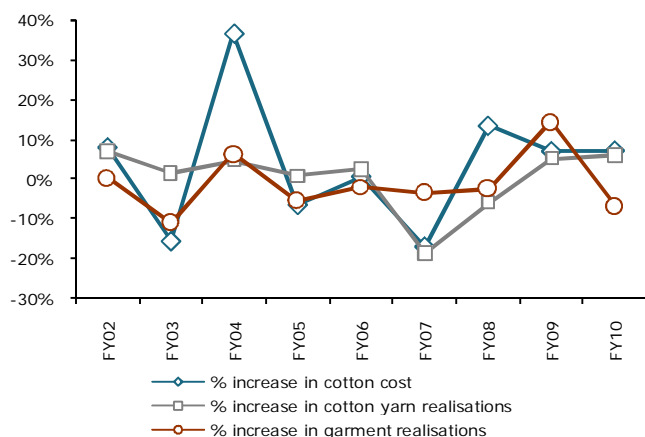
Source: Company, CRISIL Equities

Garments segment - high client concentration risk

Nahar Spinning is also present in the RMG space. Majority of garment revenues (~94% in FY10) is earned through exports to the US. Nahar caters to three customers in the US - GAP, Philippe Van-Heusen and CHAPS. They outsource the manufacturing of knitted garments like T-shirts, sweat shirts and jackets to the company. The garment exports cater entirely to the US, thereby exposing the company to the risk of geographic concentration; any downturn in the US will adversely impact the company's profitability.

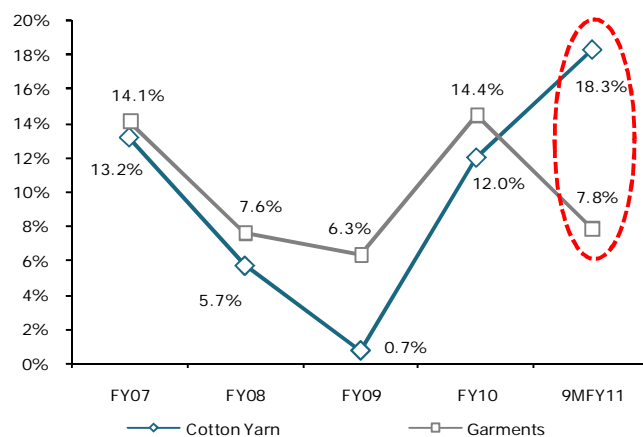
Nahar Spinning has a limited focus on the garments segment. With business from only three customers, the company runs a high business concentration risk. Its dependence on few clients reduces its bargaining power and limits its ability to pass on hikes in input prices. Further, the orders for the garment segment are booked on a quarterly basis against yarn orders that are booked on daily basis. As there is a time lag in the bookings for garments, the company finds it difficult to react promptly to hikes in input prices. Additionally, strong resistance to price hikes from international clients further adds to the woes. This has resulted in the company making EBIT margin of 8% in the garments segment against 18% margins in the yarn segment for the nine months ended December 2010.

Figure 9: Flexibility in passing on input price hikes



Source: Company, CRISIL Equities

Figure 10: Yarn and garment segment comparison



Source: Company, CRISIL Equities

Competitive landscape

Operating indicators

Operating indicators (FY10)	Nahar Spinning		Nahar Industrial		Bannari Amman		Precot Meridian		Vardhman Textiles		Super Spinning Mills		KPR Spinning Mills	
	Punjab		Punjab		Tamil Nadu		Tamil Nadu		Punjab		Tamil Nadu		Tamil Nadu	
Spindles	346098		201408		137232		217632		736168		177408		212064	
Output per spindle (kgs)	181		323		140		130		171		118		205	
Yarn price per (kgs)	140		115		138		138		162		160		127	
Market share by capacity %	0.8%		0.5%		0.3%		0.5%		1.8%		0.4%		0.5%	

Source: CRISIL Research, Prowess

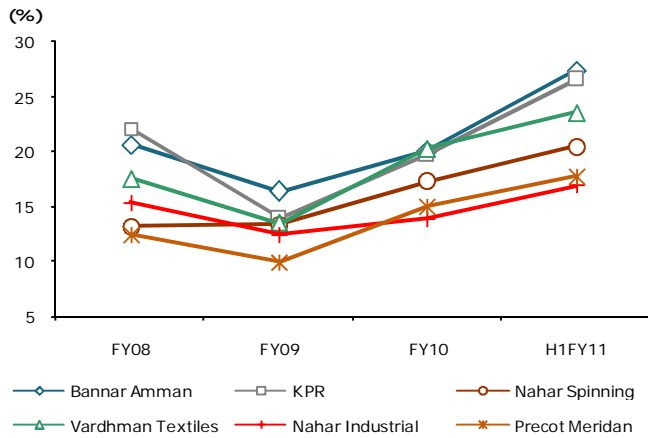
Working Capital indicators

	Nahar Spinning				Vardhman Textiles Ltd.				Kandagiri Spinning Mills				Nahar Industrial Enterprises			
	FY07	FY08	FY09	FY10	FY07	FY08	FY09	FY10	FY07	FY08	FY09	FY10	FY07	FY08	FY09	FY10
Debtor Days	55	83	83	79	40	41	40	44	28	42	50	41	35	41	44	48
Creditor Days	28	32	23	37	55	43	40	38	52	65	41	45	25	60	35	32
Inventory days	177	246	188	202	182	195	166	186	135	167	104	113	193	222	175	185
Cash Conversion Cycle	204	297	248	244	167	192	167	192	112	145	112	109	203	204	184	201
Operating Cash Flows (in Rs. mn)	1271	(345)	2680	(908)	1948	50	7050	(797)	122	225	156	76	136	1070	1990	(591)

Source: Prowess

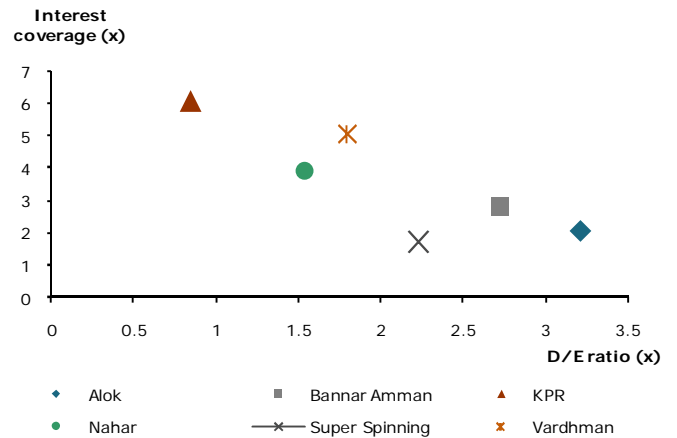
Financial indicators

EBITDA margins expand for all spinners in H1FY11



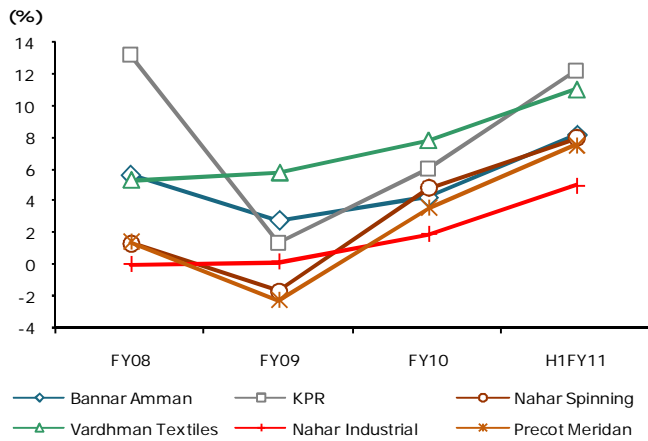
Source: Prowess, CRISIL Equities

Nahar has a relatively low gearing..



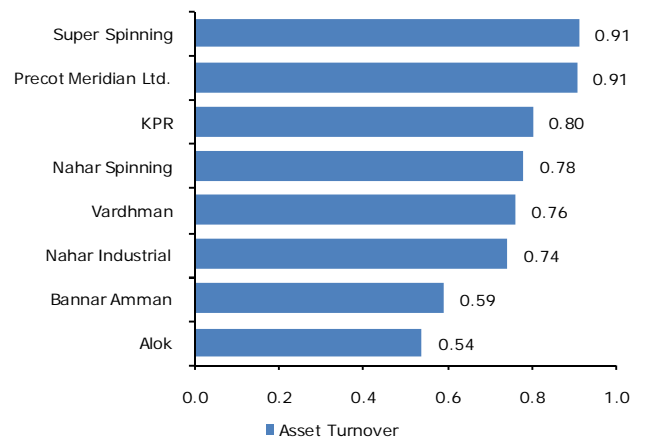
Source: Prowess, CRISIL Equities

...leading to better PAT margins



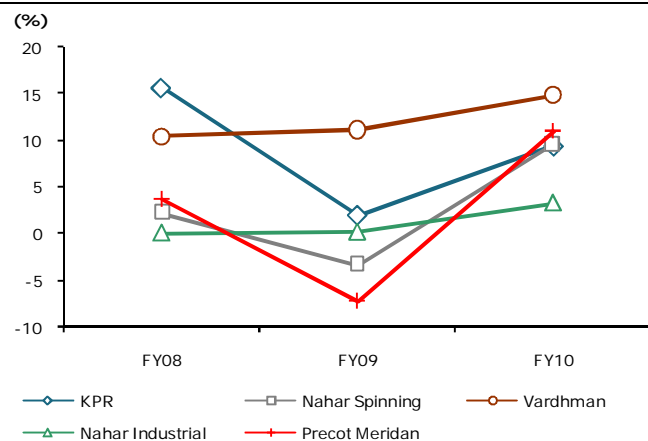
Source: Prowess, CRISIL Equities

Asset turnover steady at 0.8x in FY10



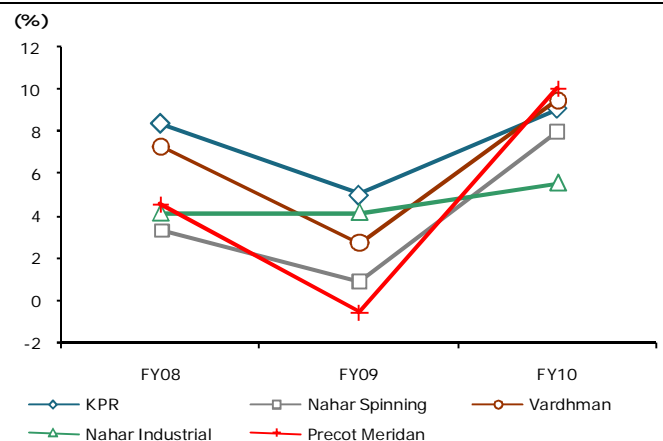
Source: Prowess, CRISIL Equities

Low D/E ratio has resulted in a low RoE



Source: Prowess, CRISIL Equities

RoCE in the range of 8-10%



Source: Prowess, CRISIL Equities

Key risks

Concentrated product mix

Nahar Spinning earns ~76% (as of FY10) of its revenues through the sale of cotton yarn. In the absence of a diversified product mix, a downturn in the cotton yarn segment will adversely impact its financial health. For instance, the economic slowdown in FY09 impacted its financial performance; it reported a loss of Rs 166.3 mn at the PAT level.

Volatile cotton prices

Price of cotton, the main raw material in the manufacturing of cotton yarn, is inherently volatile. Further, spinners generally find it difficult to pass on the increase in cotton prices as the downstream players such as weavers and garment manufacturers enjoy a higher bargaining power than spinners. Raw material forms ~68% of the total operating costs for Nahar Spinning. Thus, the company's EBITDA margins are susceptible to movement in cotton prices.

Exposed to currency fluctuations...

Exports are expected to contribute about 70% of Nahar Spinning's revenues. While the company hedges ~50% of its total foreign exchange exposure through simple forward contracts, any sharp appreciation in the rupee will impact the company's top and bottom lines.

... and changes in regulatory policies

The government has capped cotton yarn exports to 720 mn kgs for the year 2010-11 to protect the domestic weavers and garment manufacturers. Till date, ~680 mn kgs have been already exported. If the cap on exports continues, Nahar Spinning will face huge competition as there are a number of smaller players vying to book their export contracts before the quota is exhausted.

Concentrated product mix, volatile cotton prices, exposure to exchange rate fluctuations and government policies are key risks

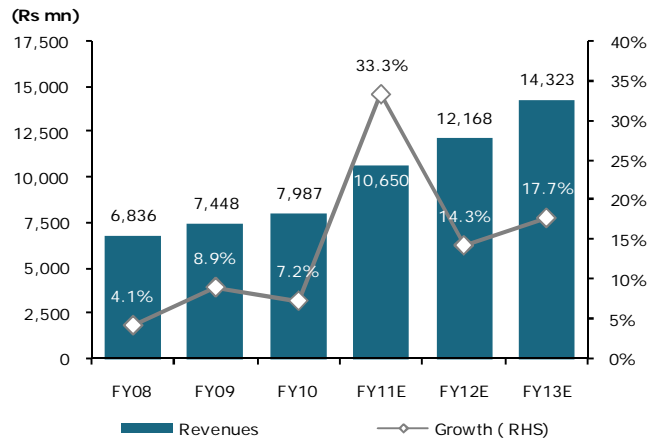
Financial Outlook

Revenues to grow at three-year CAGR of 23%

Nahar Spinning's revenues are expected to increase at a three-year CAGR of 23% to Rs 20 bn by FY13 driven by higher realisations in the cotton yarn segment following the spurt in demand in the export market. Incremental revenues from the capacity expansion is also expected to aid revenue growth in FY13.

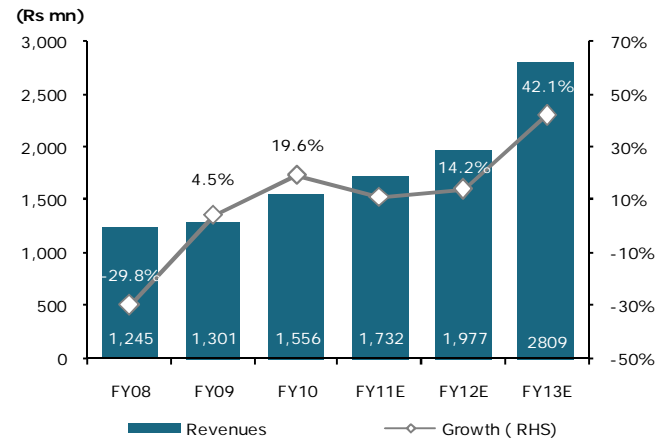
Revenues to grow at a CAGR of 23% to Rs 20 bn in FY13

Figure 11: Cotton yarn revenues up



Source: Company, CRISIL Equities

Figure 12: Garment revenues also up



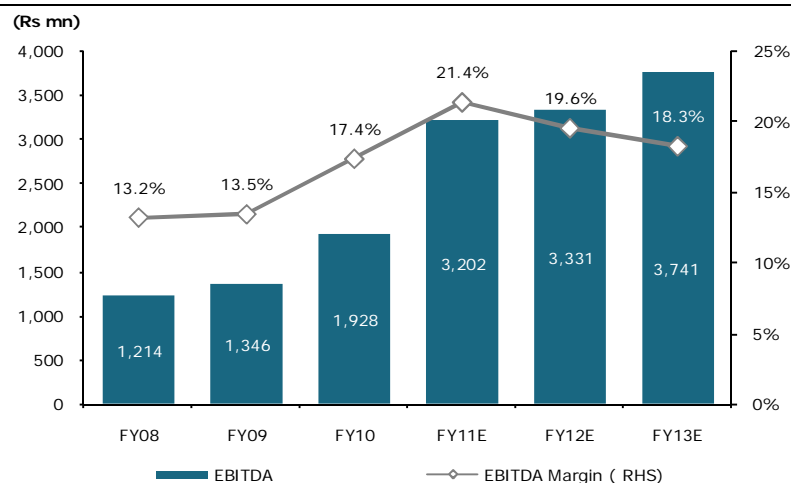
Source: Company, CRISIL Equities

EBITDA and PAT margin to expand in FY11, moderate thereafter

Nahar Spinning's EBITDA margin is expected to expand to 21.4% in FY11 following robust demand in the cotton yarn segment which will enable the company to pass on the hike in cotton prices. However, due to lower bargaining power vis-a-vis the downstream segment consisting of weavers, the company will find it difficult to increase realisations on a sustained basis. Additionally, cotton prices are expected to continue to move up. Consequently, we expect the EBITDA margin to contract to 19.6% in FY12.

EBITDA margin to expand to 21.4% in FY11 but contract to 19.6% in FY12

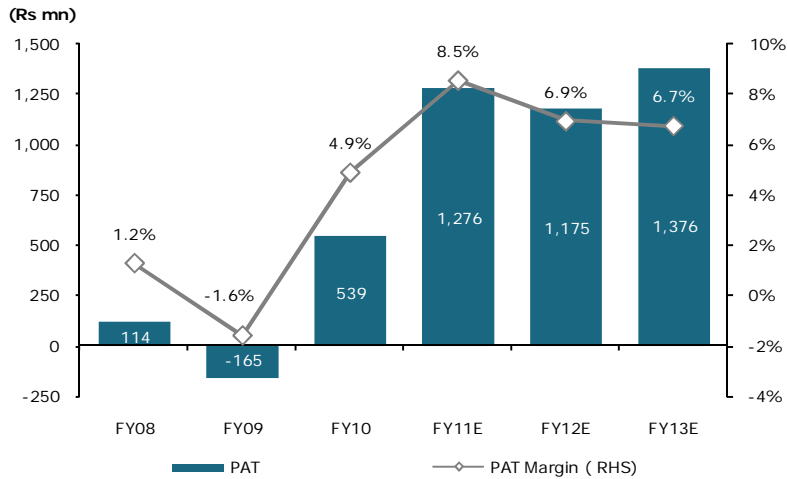
Figure 13: EBITDA margin to expand to 21.4% in FY11



Source: Company, CRISIL Equities

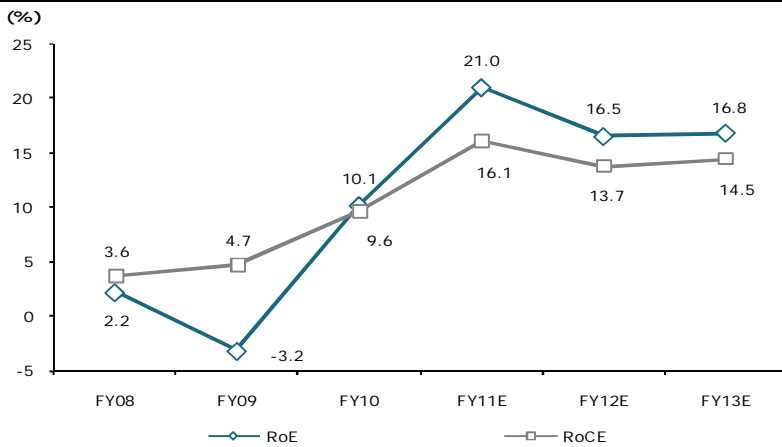
PAT margin is expected to expand to 8.5% in FY11 following the expansion in operating margins. However, the PAT margin is expected to decline to 6.9% in FY12 and 6.7% in FY13 on account of higher interest and depreciation costs following the capacity expansion. EPS is expected to increase from Rs 14.9 in FY10 to Rs 38.1 in FY13.

Figure 14: PAT margin to expand to 8.5% in FY11



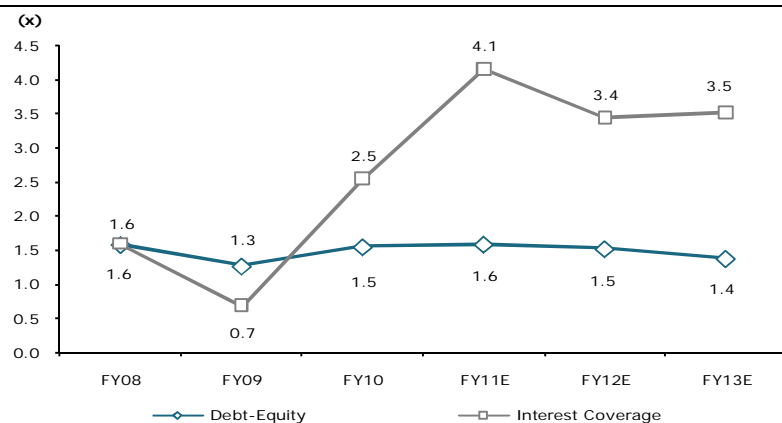
Source: Company, CRISIL Equities

Figure 15: RoCE and RoE to improve over a period of time



Source: Company, CRISIL Equities

Figure 16: Gearing to increase marginally with proposed expansion



Source: Company, CRISIL Equities

ROE on the lesser side on account of low gearing

Gearing to increase marginally following debt-funded capacity capex

Management Overview

CRISIL's fundamental grading methodology includes a broad assessment of management quality, apart from other key factors such as industry and business prospects, and financial performance.

Second generation of family run business

Led by Mr. Jawahar Oswal, chairman, Nahar Spinning is the flagship of the Nahar group of companies. He is supported by his sons Mr. Dinesh Oswal and Mr. Kamal Oswal and son-in-law Mr. Sandeep Jain. Mr. Jawahar Oswal is vastly experienced in the textile industry and is currently also on the board of the Textile committee (Ministry of Textile-Government of India). Mr. Dinesh Oswal and Mr. Kamal Oswal, both have over 25 years of experience in the textile industry.

Based on our interactions and assesment, we believe the company has a reasonably good second line of management. The second line of management also has experience of over 25 years in their respective domains. The company is highly dependent on the promoters for all important strategic decisions. We believe that the top management posts are likely to remain with the family members since Nahar Spinning is fundamentally a promoter-driven company.

Table 2: Details of group companies

Company Name	Incorporation	Industry Name	Chairman	Managing Director
Nahar Industrial Enterprises Ltd	1996	Cotton Yarn, Fabrics	Jawahar Oswal	Kamal Oswal
Nahar Poly Films Ltd	1988	BOPP films	Jawahar Oswal	Dinesh Oswal
Nahar Spinning Mills Ltd	1980	Cotton & blended yarn	Jawahar Oswal	Dinesh Oswal
Nahar Capital & Financial Services Ltd	2006	Financial services	Jawahar Oswal	Dinesh Oswal
Oswal Woollen Mills Ltd	1949	Woollen textiles	Jawahar Oswal	Sandeep Jain (ED)

Source: Prowess

Nahar Spinning has an experienced management

Corporate Governance

CRISIL's fundamental grading methodology includes a broad assessment of corporate governance and management quality, apart from other key factors such as industry and business prospects, and financial performance. In this context, CRISIL Equities analyses the shareholding structure, board composition, typical board processes, disclosure standards and related-party transactions. Any qualifications by regulators or auditors also serve as useful inputs while assessing a company's corporate governance.

Nahar Spinning maintains adequate corporate governance practices regarding its board constitution and has audit and other committees in place, which support board processes. The attendance record of independent directors in the board meetings is high.

Board composition

Nahar Spinning's board consists of 10 members, of whom five are independent directors, which meets the requirement under Clause 49 of SEBI's listing guidelines. Three of the five independent directors have a teaching background at business schools and hold directorships in other Nahar group companies. Three members of the board are from the promoter group. Mr. Dinesh Gogna and Mr. Amarjeet Singh, who also have directorships with other Nahar Group companies, are the two other board members. Given the background of the directors, we believe the board is well experienced.

Board's processes

The company's quality of disclosure can be considered reasonably good judged by the level of information and details furnished in the annual report, websites and other publicly available data. The company has all the necessary committees – audit, remuneration, nomination and investor grievance - in place to support corporate governance practices. The audit committee is chaired by an independent director, Mr Amarjeet Singh.

Inter corporate transactions – at arm's length

Nahar Spinning and Nahar Industrial Enterprises, both part of the Nahar Group, are involved in the same line of business - manufacturing and selling cotton yarn. Nahar Spinning focusses on the export market while Nahar Industrials caters to the domestic market. There are no related party transactions between the companies. The transactions between the group companies are miniscule and at market rates.

Nahar Spinning has maintained adequate corporate governance practices

Valuation

Grade: 5/5

We have used the discounted cash flow (DCF) method to value Nahar Spinning and arrived at a fair value of Rs 136 per share. The stock is currently trading at Rs 95 per share. Consequently, we initiate coverage on Nahar Spinning with a valuation grade of '5/5', indicating that the current market price has strong upside.

Key DCF assumptions

We have considered the discounted value of the firm's estimated free cash flow from FY13 to FY17.

We have included capital expenditure of Rs 2,900 mn together for FY11 and FY12 and a maintenance capex of Rs 325 mn per annum thereafter.

We have assumed a terminal growth rate of 3% beyond the explicit forecast period until FY17.

WACC computation

	FY13-17	Terminal value
Cost of equity	17.8%	17.8%
Cost of debt (post tax)	5.3%	8.0%
WACC	10.2%	11.4%
Terminal growth rate		3.00%

Sensitivity analysis to terminal WACC and terminal growth rate

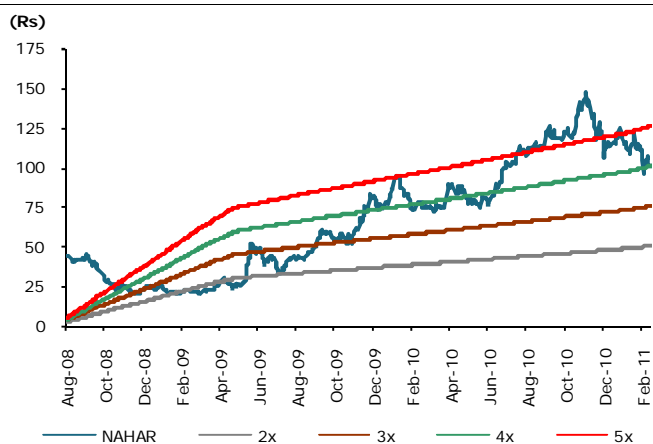
		Terminal growth rate				
		1.0%	2.0%	3.0%	4.0%	5.0%
Terminal WACC	9.5%	155	194	246	317	420
	10.5%	115	145	183	233	302
	11.5%	83	107	136	173	221
	12.5%	58	76	99	127	163
	13.5%	37	52	70	92	119

Source: CRISIL Equities estimates

We assign a fair value of Rs 136 per share to Nahar Spinning and initiate coverage with a valuation grade of "5/5"

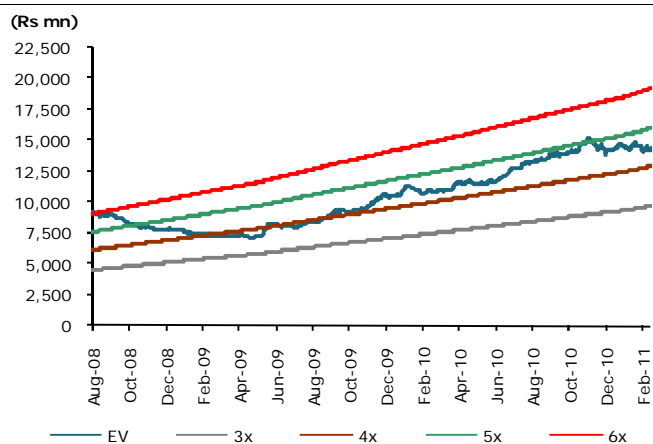
The fair value implies P/E multiple 3.8x FY11 EPS of Rs 35.3, and 4.3x FY12 EPS of Rs 32.0

One-year forward P/E band



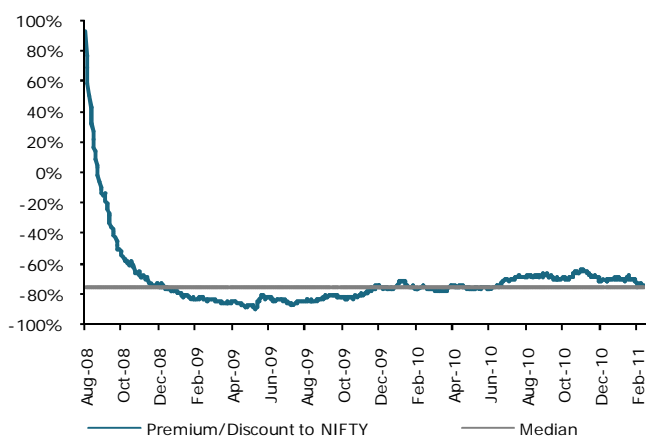
Source: NSE, Company, CRISIL Equities

One-year forward EV/EBITDA band



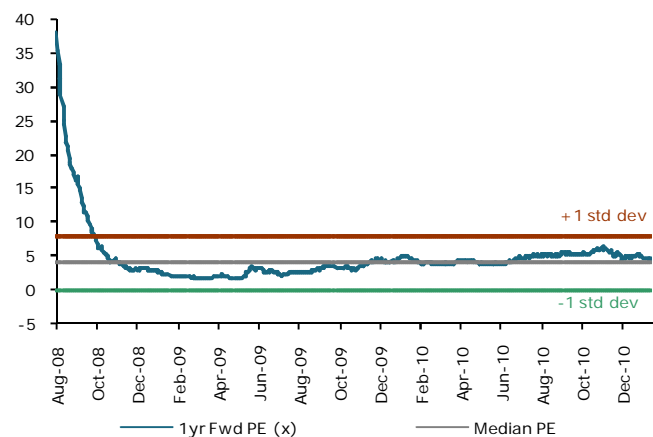
Source: NSE, Company, CRISIL Equities

P/E – premium / discount to NIFTY



Source: NSE, Company, CRISIL Equities

P/E movement



Source: NSE, Company, CRISIL Equities

Peer comparison

Companies	M.cap (Rs mn)	Price/Earnings (x)			Price/Book (x)			EV/EBITDA			RoE (%)		
		FY10	FY11E	FY12E	FY10	FY11E	FY12E	FY10	FY11E	FY12E	FY10	FY11E	FY12E
Nahar Spinning Mills	4128	15.6	4.7	5.3	1.5	0.6	0.6	8.7	5.5	6.0	10.1	14.4	11.6
Vardhman Textiles Ltd	18241	5.7	6.1	6.13	0.9	0.8	0.7	5.7	NM	NM	17.5	14.4	12.4
Bannari Amman Spinning Mills	1164	10.5	NM	NM	0.9	NM	NM	8.6	NM	NM	9.1	NM	NM
Super Spinning Mills	748	76.2	NM	NM	0.7	NM	NM	5.7	NM	NM	NM	NM	NM
KPR Mill Ltd	6564	8.3	4.5	3.5	0.8	4.5	3.5	5.2	2.7	2.1	NM	20.2	21.5
Abhishek Industries Ltd	3367	5.6	NM	NM	0.6	NM	NM	5.6	NM	NM	11.9	NM	NM
Malwa Cotton Spinning Mills	372	NM	NM	NM	8.3	NM	NM	27.0	NM	NM	-146.9	NM	NM

NM=not meaningful

Source: CRISIL Equities

Company Overview

Incorporated in 1980, Ludhiana-based Nahar Spinning is the flagship of the Nahar group of companies. Promoted by Mr Jawahar Lal Oswal, Nahar Spinning manufactures cotton, synthetic and blended yarn and cotton and woolen knitted garments. The company went public in 1985, with a public issue of equity shares at par.

Nahar Spinning has eight weaving units spread around seven locations in Punjab and one unit at Mandideep in Madhya Pradesh. The company exports its products from the ports of Ludhiana and Mumbai. It has the status of a “Star Trading House” from the Ministry of Commerce and Industry, and has been awarded the Gold Trophy for highest cotton yarn exports by the Cotton Textiles Export Promotion Council in FY08 and FY09.

It has grown from a capacity of 90,480 spindles in FY01 to 117,408 spindles in FY06. During FY06, the company entered into a composite scheme of demerger and arrangement with Nahar Exports Ltd (now known as Nahar Poly Films Ltd) and Nahar Capital and Financial Services Ltd, in order to consolidate its textile business. As per the arrangement, Nahar Exports’ textile business was demerged and transferred to Nahar Spinning and the investment business of Nahar Spinning was demerged and transferred to Nahar Capital, a company formed specifically for the investment business. After the demerger and transfer, the face value of shares of Rs 10 each of Nahar Spinning was reduced to Rs 5 each and the capital was reorganised accordingly. The shareholders of Nahar Spinning and Nahar Exports were given one share each of Nahar Spinning and Nahar Capital.

The company also has the capacity to manufacture 14 mn pieces of knitted garments. The company’s T-shirts are being exported to reputed international brands such as GAP, Arrow, Old Navy, Philips Van Heusen, Izod, and PriceCostco.

Business segment	Contribution to revenues		
	FY08	FY09	FY10
Cotton and synthetic yarn	77.8%	77.8%	76.2%
garments	14.2%	13.6%	14.9%

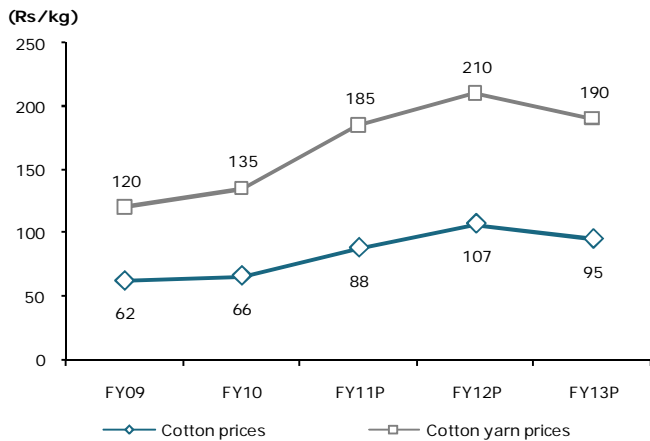
Milestones

1980	Incorporated as a private ltd company
1984	Recognised as an export house by the Indian government
1985	Raised funds through IPO to finance modernisation & expansion
1992	Set up a spinning mill with 50,400 spindles. Raised capital through rights issue
1994	Increased spindleage capacity by another 25,000 spindles
1996	Received ISO 9002 certification
2000	Mercerising and dyeing plant and an 100% EOU spinning unit with 28,224 spindles
2007	The Apparel Export Promotion Council (AEPC) awarded achievement award to the company for the highest cotton garment export
2008	AEPC awarded gold trophy for achieving highest export of cotton garments
2009	The Cotton Textiles Export Promotion Council (TEXTPROCIL) awarded gold trophy for highest export of cotton yarn (counts 50s and below).
2010	Plans to increase capacity by another 90,000 spindles

Source: Company

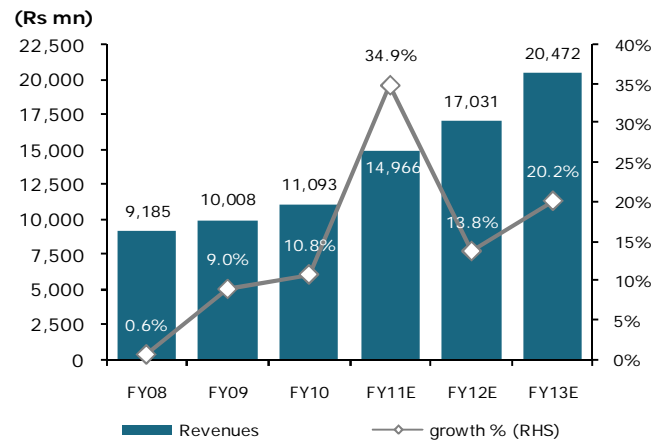
Focus Charts

Cotton and Cotton yarn price trend



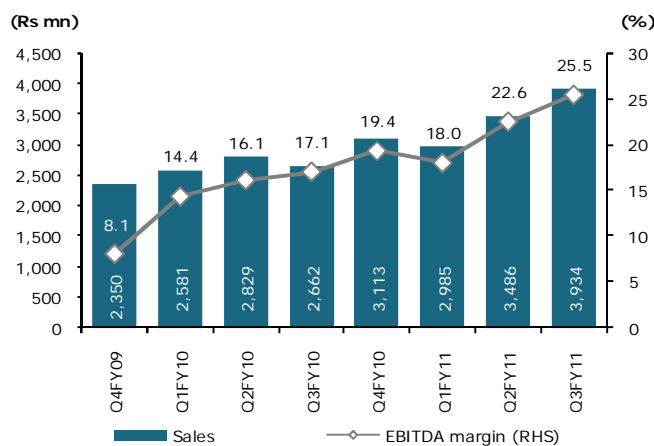
Source: CRISIL Research

Revenue and growth trend



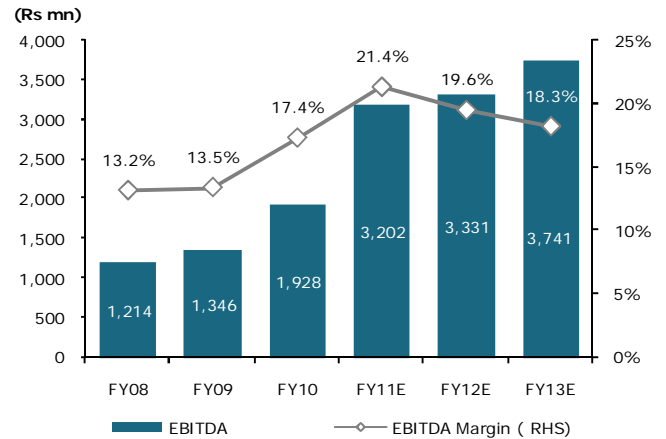
Source: Company, CRISIL Equities

Quarterly sales and EBITDA margin trend



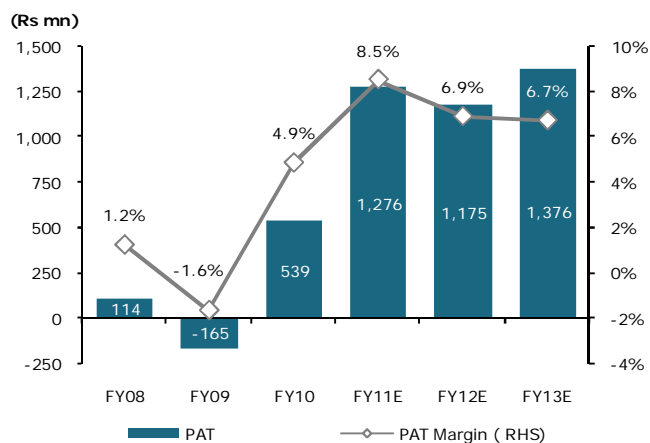
Source: Company, CRISIL Equities

EBITDA and EBITDA margin trend



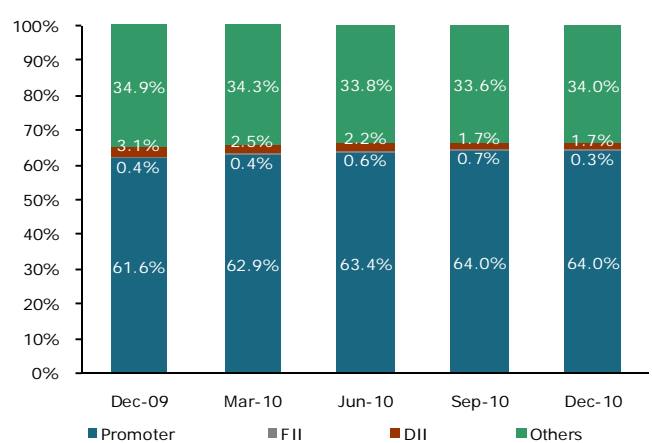
Source: Company, CRISIL Equities

PAT and PAT margin trend



Source: Company, CRISIL Equities

Shareholding pattern over the quarters



Source: NSE

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