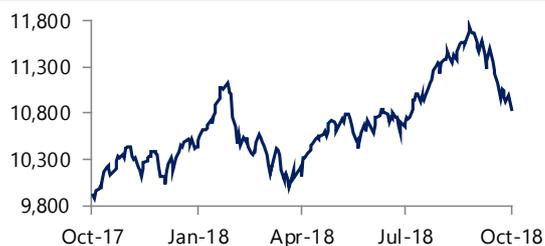


OCTOBER 4, 2018

	3-Oct	% Chg			
		1 Day	1 Mth	3 Mths	
Indian Indices					
SENSEX Index	35,976	(1.5)	(6.9)	2.0	
NIFTY Index	10,858	(1.4)	(7.0)	1.9	
NSEBANK Index	25,070	(1.2)	(10.7)	(4.4)	
NIFTY 500 Index	9,057	(1.2)	(9.4)	(0.6)	
CNXMcap Index	17,086	(1.2)	(14.2)	(5.4)	
BSESMCAP Index	14,424	0.2	(16.1)	(9.4)	
World Indices					
Dow Jones	26,828	0.2	3.4	11.0	
Nasdaq	8,025	0.3	(0.8)	7.0	
FTSE	7,510	0.5	0.7	(0.8)	
NIKKEI	24,111	(0.7)	6.0	10.8	
Hangseng	24,111	(0.7)	6.0	10.8	
Shanghai	27,091	(0.1)	(4.7)	(5.6)	
Value traded (Rs cr)					
	3-Oct	% Chg Day			
Cash BSE	3,303	(2.1)			
Cash NSE	39,051	1.0			
Derivatives	1,176,211	51.9			
Net inflows (Rs cr)					
	1-Oct	MTD	YTD		
FII	(1,608)	(1,608)	(16,670)		
Mutual Fund	1,441	1,441	89,696		
Nifty Gainers & Losers					
	Price	Chg	Vol		
3-Oct	(Rs)	(%)	(mn)		
Gainers					
Yes Bank Ltd	213	5.9	98.0		
Hindalco Ind	254	4.5	16.5		
Indiabulls Hous	944	4.2	12.6		
Losers					
Mahindra & Mahindra	792	(6.6)	6.7		
Eicher Motor	23,236	(6.1)	0.2		
Bharti Infra	252	(5.9)	3.0		
Advances / Declines (BSE)					
3-Oct	A	B	T	Total	% total
Advances	183	649	74	906	100
Declines	247	365	83	695	77
Unchanged	2	17	10	29	3
Commodity					
	3-Oct	% Chg			
		1 Day	1 Mth	3 Mths	
Crude (US\$/BBL)	86.1	(0.2)	10.2	10.1	
Gold (US\$/OZ)	1,197.4	(0.5)	0.5	(4.6)	
Silver (US\$/OZ)	14.6	(0.4)	3.1	(9.3)	
Debt / forex market					
	3-Oct	1 Day	1 Mth	3 Mths	
10 yr G-Sec yield %	8.1	8.0	8.0	7.9	
Re/US\$	73.3	72.9	71.2	68.6	

Nifty



Source: Bloomberg

News Highlights

- ▶ A day after farmer protests for better crop prices rocked the national capital, the Centre raised minimum support prices (MSP) for winter crops to ensure farmers get 50% more than what they spend on cultivation. (Mint)
- ▶ The Union cabinet chaired by Prime Minister Narendra Modi approved granting long leases of up to 99 years for land and airspace in and around railway stations to infrastructure developers in lieu of station redevelopment. (Mint)
- ▶ The Reserve Bank of India (RBI) allowed state-owned oil marketing companies (OMCs) to raise external commercial borrowings (ECBs) from lenders under the automatic route. (Mint)
- ▶ **Shriram Transport Finance Company** announced that the corporate guarantee given by the Company on 30 June 2015 in connection with Non-Convertible Debentures (NCDs) of face value aggregating to Rs6.5 bn issued by the SVL has been terminated with immediate effect. Consequently, the contingent liability of the Company with respect to redemption/ maturity of the said NCDs stands terminated. (BS)
- ▶ The dedicated bankruptcy court has admitted the insolvency petition filed by **ICICI Bank Ltd.** against absconding diamantaire Mehul Choksi-promoted Gitanjali Gems Ltd. (Mint)
- ▶ **Apollo Tyres** said its board would seek shareholders' guidance and independent counsel regarding the compensation for its managing director Neeraj Kanwar, whose reappointment was rejected by shareholders last month. (Mint)
- ▶ **Maruti Suzuki India** said it is recalling 640 units of its light commercial vehicle Super Carry sold in the domestic market to inspect and fix a possible defect in the fuel pump supply. (ET)
- ▶ **NCC** said it has received three new orders worth Rs 4.08bn in September from state government agencies. (ET)
- ▶ **Amara Raja Batteries Ltd** and Johnson Controls, Inc have signed a technology collaboration agreement to bring a new wave of battery technologies to India. (ET)
- ▶ International Finance Corporation, a World Bank group member, extended a seven-year long-term loan of Rs 10bn to **Aditya Birla Finance (ABFL)**. (ET)
- ▶ **VST's** power tillers sales in September 2018 stood at 1,152 units versus 1,855 units and tractors sales at 801 units versus 1,341 units (YoY). (Moneycontrol)
- ▶ **Larsen & Toubro** said that the buyback committee at its meeting has fixed the price of buyback of equity shares at Rs.1475 (BSE)

What's Inside

- ▶ **Management Meet Update:** VIP Industries Ltd

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, IE = Indian Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange, MC = Moneycontrol

Management Meet Update

Stock Details

Market cap (Rs mn)	:	58569
52-wk Hi/Lo (Rs)	:	647 / 252
Face Value (Rs)	:	2
3M Avg. daily vol (Nos)	:	690,953
Shares o/s (mn)	:	141

Source: Bloomberg

Financial Summary

Y/E Mar (Rs mn)	FY18	FY19E	FY20E
Sales	14,095	17,513	19,482
Growth (%)	10.5	24.3	11.2
EBITDA	1,917	2,456	2,755
EBITDA margin (%)	13.6	14.0	14.1
Net profit	1,277	1,673	1,863
EPS (Rs)	9.0	11.8	13.2
Growth (%)	50.4	31.0	11.4
Book value (Rs/share)	34.0	41.6	49.9
Dividend per share (Rs)	3.0	3.5	4.0
ROE (%)	26.5	28.4	26.4
ROCE (%)	37.3	39.2	36.8
EV/EBITDA (x)	28.3	22.4	20.1
P/E (x)	45.4	34.7	31.1
P/BV (x)	12.1	9.9	8.2

Source: Company, Kotak Securities - PCG

Shareholding Pattern (%)

(%)	Jun-18	Mar-18	Dec-17
Promoters	53.5	53.5	52.5
FII	11.0	11.0	10.3
DII	8.5	8.5	10.7
Others	27.1	27.1	26.5

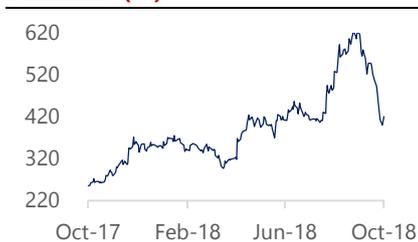
Source: Company

Price Performance (%)

(%)	1M	3M	6M
VIP Industries	(32.8)	(0.0)	28.2
Nifty	(7.0)	1.9	6.3

Source: Bloomberg

Price chart (Rs)



Source: Bloomberg

VIP INDUSTRIES LTD (VIP)

PRICE Rs.414

TARGET Rs.515

BUY

VIP Industries share price has declined by 32% in the past two months, post achieving our last target price on the back of unfavorable macro developments including depreciation of rupee, higher crude prices and increasing interest rates. We believe this steep recent correction offers another opportunity to invest in the stock which has been reporting strong quarterly performance on a sustained basis. Unfavorable macros force us to cut earnings (by 4%/7% respectively for FY19/FY20) and target multiple. However, we continue to have positive view on the stock as volume growth and delivery remains strong from the market leader. Recommend BUY with a target price of Rs 515 (versus Rs 570 earlier) at 39x FY20 earnings (versus 40x early).

Aviation industry is in bad shape

The domestic passenger traffic to continue to grow at a healthy pace of ~15% per annum due to conducive factors like relatively low penetration levels, lower yields, support from regulatory environment (i.e. regional connectivity scheme) and development of new airports. However, the recent spurt in crude prices, global increase in interest rates and depreciation in rupee can hurt the growth of the sector going forward. If the macro environment remains in bad shape for some more time, in H2FY19 we can see aviation companies deferring their capacity addition and also resorting to hike in ticket prices. This could hurt passenger air traffic going forward.

There is strong correlation between air traffic, air travel and demand for branded luggage and we would want to be cautious here given the current precarious state of the aviation industry.

Passengers flown by Indian airlines (in lakhs)



Source: DGCA

Level playing field post GST implementation

Before GST, VIP has been paying an effective indirect tax of 20% against our estimate of 12% paid by the unorganized players. GST of 18% is applicable now (reduced from 28% in November 2017) to the entire luggage industry which has maintained the indirect tax situation for organized players, but increased the tax burden of unorganized players.

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We estimate the unorganized players to have taken price increase for their products to recover the increased indirect tax impact, which has reduced the pricing gap between the organized and unorganized players creating a level playing field. Management indicated that this development has led to shift of volumes from the unorganized towards branded organized players like VIP with customers preferring to have branded luggage at similar prices. This has helped and would continue to help VIP to grow at faster pace over unorganized players and improve market share.

Level playing field post GST

Indirect tax	Rate for VIP	Unorganized player
Excise duty (%)	12.5	8
Sales tax (%)	5 to 13	3 to 7
Effective indirect tax (%)	20	12
Current GST (%)	18	18

Source: Kotak Securities – Private Client Research

Raw material situation is currently not healthy

Management indicated that the company has been experiencing increasing raw material trend (since Q4FY18) in both the 2 major categories of inputs - polypropylene (for hard luggage) and polycarbonate. Other raw material like polyester, canvas, denim, PU leather, copper, aluminum, zipper head and hardware accessories have also shown an inflationary trend.

VIP sources more than 70% of its soft luggage from China and its sourcing cost increases if Yuan appreciates against the rupee. YTD the Chinese Yuan has appreciated by 7% vs. the INR which has also contributed to cost inflation for VIP. VIP is trying to contain its margins under these adverse circumstance by increasing prices and also by reducing other cost.

Rupee depreciation vs. the Yuan

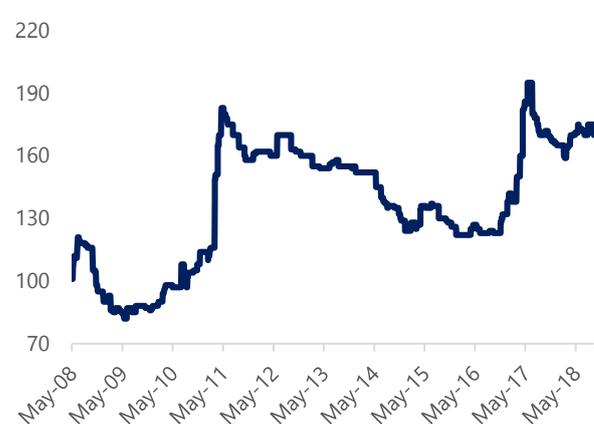
Further depreciation of rupee, increase in raw material prices and increase in operational expenditure in china have the potential to impact the margins for VIP over FY18-FY20E. However, we believe this would be off-setted by strong volume growth leading to operating leverage and economies of scale. We expect the sustainable EBIDTA of ~14% in a strong volume growth and high cost inflation environment.

Chinese Yuan versus INR (Rs)



Source: Bloomberg

Polypropylene prices imported from China (US\$/MT)



Source: Bloomberg

Sourcing from China gradually shifting to Bangladesh

Due to increasing labour costs and other reasons such as strengthening of the Yuan vs. INR, the company is gradually reducing its dependency on China and increasing its sourcing from Bangladesh through its wholly owned subsidiaries (total 3 subsidiaries) in Bangladesh set-up with an investment of Rs 150 mn. VIP has flexibility in increasing the capacities with minimum capex and within a short time-frame.

Going forward by FY20, we expect the sourcing of soft luggage to fall from China to 90% and with share of Bangladesh increasing to 10% (currently negligible) which would aid margins going forward. It is important to note that, revenues from Bangladesh has increased to Rs 250 mn (from Rs 128 mn YoY) with PAT of Rs 40 mn (from Rs 32 mn YoY) in Q1FY19.

Performance across Brands

Management of VIP indicated that each of its 5 brand have done well in FY18/Q1FY19 and share the same margins at net level.

- **Skybags** continues to do very well for the company and is now the largest luggage and backpack brand in the country. VIP claims to have more than 50% market-share in the backpack market with Skybags.
- **Aristocrat:** Aristocrat is the value brand of the company which saw an extremely good year and was the fastest growing brand. As per the management, there is a huge scope in the value segment of the market and the company is well poised to capture the same in value segment. VIP is also focusing on Aristocrat to face competition.
- **VIP brand** still enjoys a healthy market share and is on top of the mind brand when it comes to family travel. Management is focusing on reinventing the brand through campaigns.
- **Premium Brands: Caprese** and **Carlton** are high-margin brands and continue to grow well, though they are still a small proportion of revenues.

Performance across channels

The **Hypermarket channel** continues to witness the strongest growth amongst all channels suggesting that Indian consumers are showing preference towards affordable luggage and convenience of modern shopping formats which are clean and air conditioned. Management indicated that VIP enjoys market leadership in modern trade. **E-commerce** is another channel which is slowly picking-up for the company with Indian consumers not only in metros but also in tier 2 and 3 towns hooking on to e-com. **General Trade channel** has registered very good sales growth during the year due to focused efforts on each segment including distribution and direct dealers. The **Company-owned stores** and exclusive franchise stores also continue to do well. **Canteen Stores Department (CSD)** channel remain stable for the company.

Risk-reward favorable—upgrade to BUY

In recent years in India, luggage and handbags have managed to shed their traditional utilitarian tag and have now evolved as lifestyle products. Increasing business and leisure travels coupled with rising disposable income and organized retailing have led to increased demand for luggage. Within this category, the demand for brand names has grown, as consumers aspire for goods that are branded, durable and count as status symbol. We expect VIP to be one of the largest beneficiaries of this change in the country. However, the macro-economic variables can play spoilsport for the company.

Under current circumstances, for VIP, we estimate a revenue CAGR of 18% and earnings CAGR of 21% over FY18 to FY20E with strong operating margins and return ratios.

After recent correction in the stock price, VIP is now trading at ~31.1X FY20E earnings, down from 42X previously. We cut our FY19/20E earnings by 4.1% and 7% respectively, to account for lower volume growth and margins and upgrade the stock to BUY (from Accumulate earlier) with a price target of Rs 515 (versus Rs 570 earlier), valuing the stock at 39X FY20E earnings (versus 40x earlier)..

Company Background

VIP Industries, established in the year 1971, is a leading luggage maker in India offering a wide range of products in hard luggage and soft luggage segments including school bags, trolleys, backpacks, suitcases, executive cases, duffels and overnight travel solutions. Some of its brands include VIP, Caprese, Alfa, Aristocrat, Buddy and Carlton. The company is Asia's No.1 luggage manufacturer and transforming its business strategy from time to time. The company has manufacturing facilities located at Haridwar in Uttarakhand, Jalgaon, Nagpur and Nashik in Maharashtra. The company has set up a subsidiary in Bangladesh to manufacture and market luggage and bags. The company is maintaining its market share of 50% in the organized luggage industry by offering wide range of product mix like Carlton and VIP catering to high-end segment, Aristocrat caters to mid-segment, Skybags cater to mid and sub-mid segment and Alfa for lower-end price segment.

Financials: Consolidated

Profit and Loss Statement (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Revenues	12,752	14,095	17,513	19,482
% change YoY	4.8	10.5	24.3	11.2
Raw material cost	6,759	7,140	8,695	9,672
Employee cost	1,415	1,582	1,821	2,026
Other expenses	3,259	3,456	4,542	5,028
Total Operating expd	11,433	12,178	15,058	16,727
EBITDA	1,319	1,917	2,456	2,755
Depreciation	128	124	147	157
EBIT	1,191	1,793	2,308	2,598
Other income	59	104	100	100
Interest expense	6	0	0	0
Profit before tax	1,244	1,897	2,408	2,698
Tax	395.0	620.0	735.2	834.7
ETR (%)	31.8	32.7	30.5	30.9
Profit after tax	849	1,277	1,673	1,863
Minorities & Associates	0	0	0	0
Net income	849	1,277	1,673	1,863
% change YoY	25.2	50.4	31.0	11.4
Shares outstanding (m)	142	142	142	142
EPS	6.0	9.0	11.8	13.2
DPS	2.2	3.0	3.5	4.0

Source: Company, Kotak Securities – Private Client Research

Cash flow Statement (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
PAT	849	1,277	1,673	1,863
Depreciation	128	124	147	157
Changes in working capital	12	(372)	(732)	(396)
Cash flow from operations	989	1,029	1,089	1,624
Capex	(65)	(228)	(250)	(250)
Investments	(679)	79	100	-
Cash flow from investments	(744)	(149)	(150)	(250)
Equity issuance	-	-	-	-
Debt raised	(145)	(10)	(3)	-
Dividend Paid	(371)	(514)	(599)	(685)
Miscellaneous items	-	-	-	-
Cash flow from financing	(516)	(524)	(602)	(685)
Net cash flow	(271)	356	336	690
Opening cash	345	73	430	766
Closing cash	73	430	766	1,456

Source: Company, Kotak Securities – Private Client Research

Balance sheet (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Cash and cash equivalents	73	430	766	1,456
Debtors	1,209	1,520	1,900	2,020
Inventory	2,874	3,168	3,984	4,400
Loans and advances	558	666	833	900
Other current assets	46	56	66	76
<i>Total current assets</i>	<i>4,687</i>	<i>5,409</i>	<i>6,783</i>	<i>7,396</i>
LT investments	679	600	500	500
Net fixed assets	615	719	822	914
Total assets	6,054	7,158	8,871	10,266
Creditors	1,457	1,692	2,139	2,315
Provisions	113	257	304	289
Other current liabilities	425	397	544	601
<i>Total current liabilities</i>	<i>1,995</i>	<i>2,345</i>	<i>2,987</i>	<i>3,204</i>
LT debt	13	3	0	0
Minority Interest	0	0	0	0
Equity	283	283	283	283
Reserves	3,763	4,527	5,600	6,779
<i>Networth</i>	<i>4,046</i>	<i>4,810</i>	<i>5,883</i>	<i>7,062</i>
Total liabilities	6,054	7,158	8,871	10,266

Source: Company, Kotak Securities – Private Client Research

Ratio Analysis

(Year-end Mar)	FY17	FY18	FY19E	FY20E
EBITDA margin (%)	10.3	13.6	14.0	14.1
EBIT margin (%)	9.3	12.7	13.2	13.3
Net profit margin (%)	6.7	9.1	9.6	9.6
ROE (%)	21.0	26.5	28.4	26.4
ROCE (%)	29.3	37.3	39.2	36.8
Dividend payout (%)	43.8	40.2	35.8	36.8
BVPS (Rs)	28.6	34.0	41.6	49.9
Working capital turnover (days)	77.2	65.0	62.0	62.0
Debt Equity (x)	-	-	-	-
PER (x)	68.3	45.4	34.7	31.1
P/C (x)	59.4	41.4	31.9	28.7
Dividend yield (%)	0.5	0.7	0.9	1.0
P/B (x)	14.3	12.1	9.9	8.2
EV/Sales (x)	4.5	4.1	3.3	2.9
EV/ EBITDA (x)	41.6	28.3	22.4	20.1

Source: Company, Kotak Securities – Private Client Research

RATING SCALE

Definitions of ratings

- BUY** – We expect the stock to deliver more than 12% returns over the next 12 months
- ACCUMULATE** – We expect the stock to deliver 5% - 12% returns over the next 12 months
- REDUCE** – We expect the stock to deliver 0% - 5% returns over the next 12 months
- SELL** – We expect the stock to deliver negative returns over the next 12 months
- NR** – **Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
- SUBSCRIBE** – We advise investor to subscribe to the IPO.
- RS** – **Rating Suspended.** Kotak Securities has suspended the investment rating and price target for this stock, either because there is not a Sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.
- NA** – **Not Available or Not Applicable.** The information is not available for display or is not applicable
- NM** – **Not Meaningful.** The information is not meaningful and is therefore excluded.
- NOTE** – Our target prices are with a 12-month perspective. Returns stated in the rating scale are our internal benchmark.

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