Initiating Coverage

GHCL

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Strong business fundamentals are neglected in current valuations

CMP	Target Price
Rs171	Rs228
Rating	**Upside**
BUY	33.6 %

- GHCL is among the key domestic soda ash players (23% market share) and benefits from fully integrated plant and various distinct cost advantages which helps it to enjoy highest margins in the industry (EBIT margins 28-31%) and strong return ratios
- It's textile business (40% of sales and 20% of EBIT) is also backward integrated from yarn to home textiles, however thrust in this segment is to drive margins (from EBIT margins of 11% in FY16 to 13%/15% in FY17/FY18) by changing customer and product mix
- We believe that GHCL's strong free cash flow generating business (FCF yield of ~30%), falling D/E to 0.6x (from 1.2x) and its ability to protect its margins in soda ash in a weak market driven by cost leadership is not truly reflected in its current valuations
- Ongoing capex in soda ash and potential ramp up in textile segment margins to drive company's earnings at a CAGR (FY16-18E) of 21% with RoE of 28%. We see significant re-rating potential in the stock and initiate coverage with 'Buy' recommendation with target price of Rs 228 (based on 6x FY18E EPS of Rs 38)

Cost leadership in soda ash business

GHCL is one of the key soda ash players with market share of about 23%. Company enjoys EBIT margins in the range of 28-31%, which is 400-800bps higher than its peers driven by its cost leadership and backward integration. The segment contributes approximately Rs 4-4.5bn pa to cash flows and ongoing capex to boost it further to Rs5bn with RoCE of 36%.

Textiles business has significant potential of margin expansion

GHCL's textile business also benefits from backward integration (in yarn) however its late entry in the home textiles division has led to lower margins (11% at EBIT level) compared to other players in the industry. The domestic textile industry is going through structural changes and is benefitting from increased outsourcing from the US and European countries. GHCL's thrust on improving its product mix, changing customer profile and ramp up in capacity utilization is expected to improve its EBIT margins from 11% in FY16 to 13%/15% in FY17E/FY18E, respectively.

Initiate with BUY as cash flow generation remains strong

We believe, GHCL will continue to generate steady cash flows on the back of its cost leadership in soda ash business and improvement in performance of its textiles segment. We expect revenue/EBITDA/PAT to clock 6%/10%/21% CAGR during FY16-18E. After meeting future capex requirements, company will be able to focus on significant debt reduction from FY18E. Valuations look attractive as at CMP of Rs 171, the stock is trading at 4.5x FY18E EPS. Valuing the stock at 6xFY18E EPS with target price of Rs 228, we initiate coverage on GHCL with a 'Buy' rating.

Financial Snapshot (Consolidated)

(Rs mn)	FY14	FY15	FY16	FY17E	FY18E
Net Sales	22,343	23,616	25,458	26,302	28,673
EBITDA	4,370	5,328	6,334	6,734	7,725
EBITDA Margin (%)	19.4	22.4	24.8	25.5	26.8
APAT	1,431	2,138	2,685	3,055	3,800
EPS (Rs)	14.3	21.4	26.8	30.5	38.0
EPS (% chg)	7.5	49.4	25.6	13.8	24.4
ROE (%)	24.8	31.5	30.6	27.6	27.5
P/E (x)	11.9	8.0	6.4	5.6	4.5
EV/EBITDA (x)	7.0	5.5	4.5	4.2	3.2
P/BV (x)	2.9	2.2	1.7	1.4	1.1

Source: Company, Emkay Research

Change in Estimates	
EPS Chg FY17E/FY18E (%)	NA/NA
Target Price change (%)	NA
Previous Reco	NA

Emkay vs Consensus

EPS Estimates	FY17E	FY18E
Emkay	30.5	38.0
Consensus	-	-
Mean Consensus TP		-

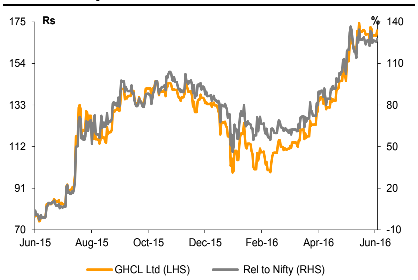
Stock Details	
Bloomberg Code	GHCL IN
Face Value (Rs)	10
Shares outstanding (mn)	100
52 Week H/L	176 / 75
M Cap (Rs bn/USD bn)	17 / 0.25
Daily Avg Volume (nos.)	486,588
Daily Avg Turnover (US$ mn)	1.2

Shareholding Pattern Mar '16	
Promoters	18.5%
FIIs	17.8%
DIIs	5.5%
Public and Others	58.2%

Price Performance

(%)	1M	3M	6M	12M
Absolute	10	52	26	128
Rel. to Nifty	2	43	21	132

Relative price chart



Source: Bloomberg

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Investment rationale

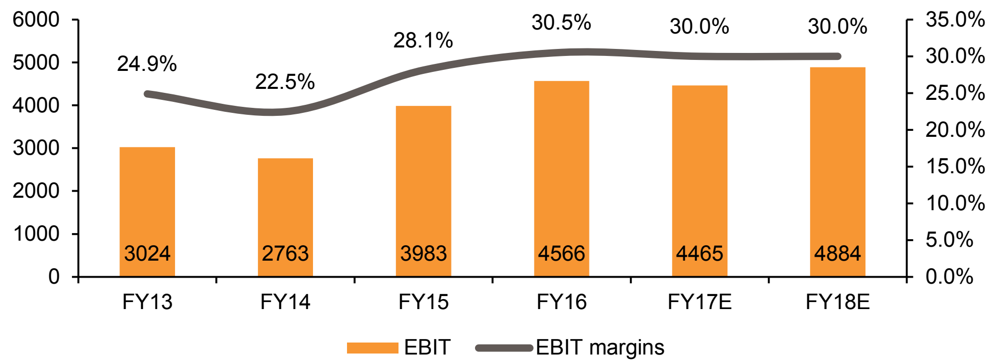
Soda ash business a steady cash generator

GHCL is one of the key soda ash players in India, with a capacity of 0.85 mn tpa, accounting for 23% of the country's total demand. GHCL's soda ash business contributes 58% to revenues and 80% to its profitability. The segment is a cash cow for the company with largely stable volumes and high profitability. Demand for soda ash is likely to grow at a steady pace of 5% CAGR over the next few years, similar to the rate seen in the last decade. Prices for soda ash have also increased at a steady pace with increase in input costs. On the back of strong contribution margins and company's depreciated plant, its soda ash business supports strong free cash flow generation.

GHCL's soda ash business is the cash cow for the company with highest margins in the industry

With steady demand-supply dynamics going forward, the business is likely to continue generating steady cash flows for the company. We expect revenues from this segment to increase at 4% CAGR over FY16-18E. Further, margins in this segment are expected to stay healthy at 30%.

Exhibit 1: Soda ash segment's EBIT (Rs mn) and EBIT Margins (%)

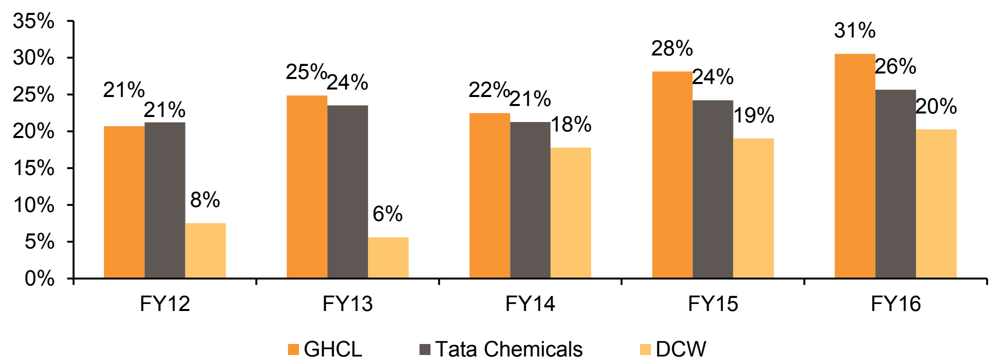


Source: Company, Emkay Research

Cost leadership in Soda ash business

GHCL is the cost leader in soda ash manufacturing, with EBITA margins ranging between 25-31%, 400-800 bps higher than closest peers. Higher margins in this segment are on the back of highest utilisation in the industry and well integrated business model with captive availability of raw materials, leading to cost leadership in the industry.

Exhibit 2: EBIT margins comparison



Source: Company, Emkay Research

Exhibit 3: GHCL enjoys better operating metrics amongst its peers in soda ash

	GHCL	Tata Chemical	Nirma*	DCW
EBIT %	*31%*	*26%*	*13%*	*20%*
ROCE	36%	69%	11%	23%

Note: Based on FY16 numbers
Tata Chemicals segment results also includes its branded salt and cement business
**Nirma segment performance is based on overall consolidated results*

GHCL's Textiles segment to benefit from increasing export opportunities

GHCL's textiles segment is a beneficiary of the increasing export opportunities in home textiles sector for India. India has a competitive advantage in the 'Bed linen' space, given the focus on capability and capacity and acceptance of smaller volume quantity as against China (where focus is more on bulk quantities). Further, most of the players present in thin margin spinning business have forward integrated into high margin home textiles segment.

GHCL's Home Textiles segment is benefitting from increase in exports opportunities

As per the data released by the Office of Textiles and Apparels, India's share of cotton bed sheet exports to the US has grown from just 27% in 2009 to almost 50% currently. This has given an edge to Indian exporters, especially to players like GHCL. The company has a strong presence in the exports market, mainly in the US and has marquee customers like Bed Bath & Beyond and TARGET.

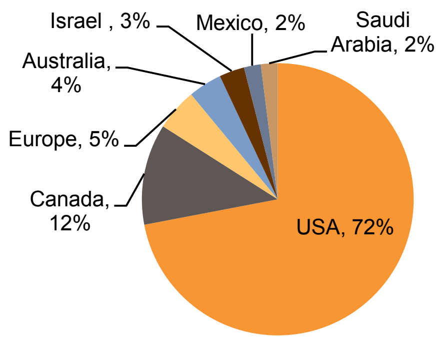
With positive outlook for the US economy, Indian players are likely to benefit from increasing exports in the home textiles division. Further, abundant availability of raw material (India is the world's largest cotton producer) will help it have a competitive edge over other countries.

Exhibit 4: US imports by country in Cotton Sheets

Country	2009	2010	2011	2012	2013	2014	2015
India	**27%**	**33%**	**38%**	**45%**	**47%**	**47%**	**48%**
China	29%	30%	24%	22%	24%	23%	23%
Pakistan	26%	21%	22%	18%	17%	17%	16%
ROW	18%	16%	16%	15%	13%	13%	13%

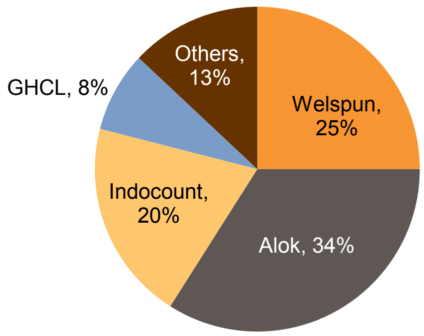
Source: Otexa, Emkay Research

Exhibit 5: GHCL's presence across all the leading export markets



Source: Company, Emkay Research

Exhibit 6: GHCL amongst large suppliers to US markets



Source: Industry, Emkay Research

One of the lowest margins in home textiles- Provides immense scope for improvement

GHCL is one of the late entrants in the home textile segment. It generally takes time in this segment to acquire quality customers with healthy volumes and pricing. Company supplies its fabrics to private label brands in exports markets. In this segment, GHCL competes with established players like Welspun and Indo Count. Being the late entrant, GHCL's margins are also one of the lowest in the business, mainly due to low utilization rates.

Exhibit 7: EBIT margins of Home textile players

Company	FY12	FY13	FY14	FY15	FY16
Himatsing. Seid	6.9%	7.0%	7.3%	9.2%	14.6%
GHCL	**1.4%**	**4.2%**	**8.2%**	**7.1%**	**10.7%**
Indo Count Inds.	4.1%	7.2%	11.6%	15.8%	20.9%
Welspun India	6.1%	13.6%	7.8%	19.5%	21.3%
Trident	4.1%	9.5%	12.3%	10.0%	11.2%
Alok Inds.	16.4%	16.8%	-	16.5%	-23.1%

Source: Company, Industry, Emkay Research

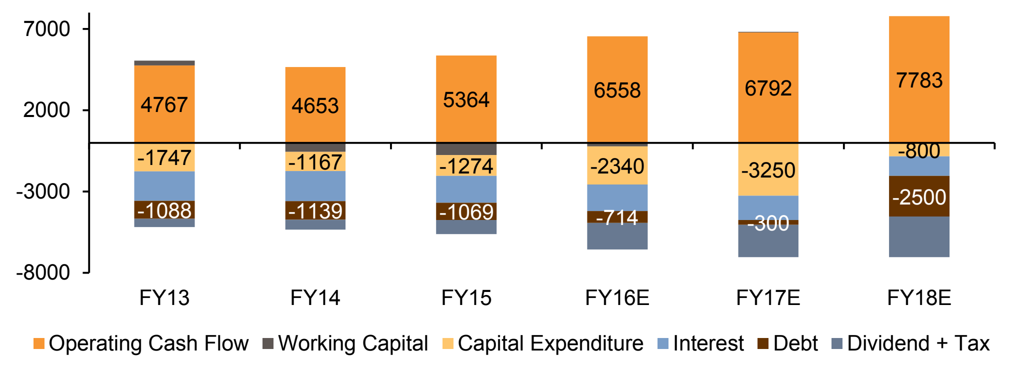
Going forward, company plans to focus on improving margins from the current 11% to 13%/15% in FY17/18 with improvement in utilization rates, change in customer mix and bringing various cost efficiencies.

Future cash flows will be utilized for debt repayments

Strong cash flow generation coming back to investors now

Over the past 4 to 5 years, the company has utilized significant amount of cash flows for paying off overseas debt (due to write-offs taken on overseas retail investments). Moreover, in the last two years, GHCL has embarked on a capacity expansion plan, wherein the company is expanding capacity in soda ash segment, textiles and has also installed wind turbine systems. With write-off of losses in overseas subsidiaries and major capex in both the businesses nearing completion, the major focus for the company from FY18 will be debt reduction and paying back investors, either in the form of dividend or shares buyback.

Exhibit 8: Cash flows to be utilized for debt repayments



Source: Company, Emkay Research

Dividend distribution policy, ESOPs are the steps in right direction

GHCL's steps towards creating shareholder wealth to bode well in the long term

The company has taken various steps to reward shareholders over the past one year. In FY16, the company declared a dividend of Rs 420 mn, which is a 16.4% gross payout. Company has also announced its dividend distribution policy, wherein it will maintain 15%-20% gross payout of standalone profits. Further, the company has also introduced ESOPs to reward internal stakeholders. ESOPs will be to the extent of 1.2% of share capital allocated in 1st year and will be issued at Rs 100 per share. Further, the company has also appointed S R Batliboi (E & Y) as auditors. We believe all these steps are in the right direction and will create value for shareholders in the long run.

Initiate with Buy on compelling valuations

We believe, GHCL will continue to generate steady cash flows on the back of its cost leadership in soda ash business and improvement in performance of its textiles segment. We expect revenue/EBITDA/PAT to clock 6%/10%/21% CAGR during FY16-18E. After meeting future capex requirements, company will be able to focus on significant debt reduction from FY18E. Valuations look attractive as at the CMP of Rs 171, the stock is trading at 4.5x FY18E EPS of Rs 38, EV/EBIDTA of 3.2x and P/BV of 1.1x. Given company's strong earnings growth of 21%, RoCE / RoE of 26%/28% and strengthening balance sheet with D/E of 0.6x (FY18E) we believe that company's stock has significant re-rating potential.

Valuing the stock at 6xFY18 our fair value for the stock works out to be Rs 228. We initiate coverage on GHCL with Buy rating. Given company's dividend policy in placed with growing EPS, stock offers dividend yield of 3.8% (FY18E) and further protects downside risk.

Exhibit 9: Valuations Summary

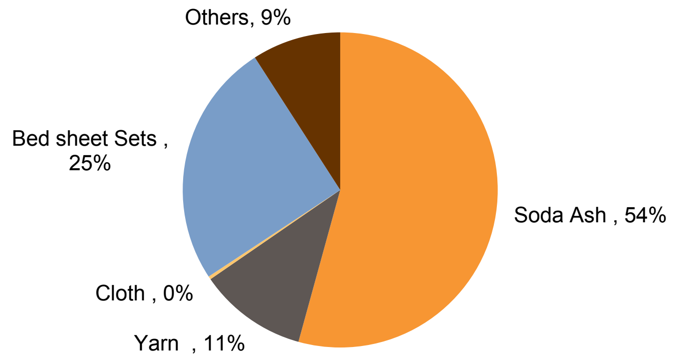
Company Name	Price (Rs)	Mkt Cap (Rs bn)	Reco	Target Price (Rs)	EPS Growth (%)		Net Debt/ Equity (x)	ROE (%)	PE (x)		EV/EBITDA (x)		PB (x)		Dividend Yield (%)
					FY17e	FY18e	FY18e	FY18e	FY17e	FY18e	FY17e	FY18e	FY17e	FY18e	FY18e
Tata Chemicals	426	109	Accumulate	500	26.4	7.4	0.6	14.4	11.0	10.2	6.7	6.0	1.6	1.4	2.3
GSFC	75	30	Hold	74	11.4	33.1	0.3	7.8	10.0	7.5	8.8	7.2	0.6	0.6	2.9
Deepak Fertilisers	163	14	Buy	217	46.6	7.9	1.0	10.8	8.1	7.5	6.7	6.2	0.8	0.8	3.4
DCM Shriram	200	32	Buy	260	34.5	16.6	0.2	17.9	8.2	7.0	5.8	4.8	1.3	1.2	2.5
GHCL	**171**	**17**	**Buy**	**228**	**18.6**	**24.4**	**0.5**	**27.5**	**5.6**	**4.5**	**4.2**	**3.2**	**1.4**	**1.1**	**3.8**

Source: Emkay Research

Company background

GHCL Ltd (formerly known as Gujarat Heavy Chemicals Ltd) was incorporated in 1983, jointly by the Gujarat Industrial Investment Corporation, GTC Industries Limited and Dalmia Dairy Industries Limited. The company has established itself as a well-diversified group with major presence in chemicals and textiles. Further, GHCL's consumer products business involves manufacturing and selling Edible salt, Industrial grade salt and Honey.

Exhibit 10: Revenue by segment (FY16)



Source: Company, Emkay Research

Exhibit 11: Steadily expanding capacity across segments

1988-2000	2001-03	2006-08	2012-15	2016-18
Production of Soda Ash commences with an installed capacity of 420,000 tonnes/ year	Soda Ash production increased to 600,000 tonnes/ year	Soda Ash production increased to 850,000 tonnes/ year	Spindles capacity increased to 175,000	Soda Ash capacity expansion by 0.1 mn tpa
Production capacity increased to 525,000 tonnes/ year	Entered into Spinning business - 65,000 spindles	Spindles capacity increased to 83,000 and subsequently to 140,000	Air jet looms capacity increased to 134 and subsequently to 162 looms (present weaving capacity - 12 mn meters)	De-bottlenecking at Home textiles and increase in cut and sew capacity
	Spindles capacity increased to 83,000	Home textile production commences with 36 mn meters processing capacity and 8 mn meters weaving capacity		

Source: Company, Emkay Research

Management team

Mr. RS Jalan (MD)

- Mr. Ravi S Jalan is the managing director of the company with over three decades of business experience
- His unique leadership style have been a driving force for GHCL's businesses
- A Qualified Chartered Accountant, he possesses deep business understanding and excellent analytical skills

Mr. Raman Chopra (CFO & ED Finance)

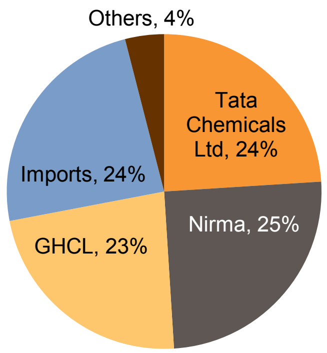
- Spear heading GHCL's Finance and IT functions
- Experience of 25 years in Mergers & Acquisitions, Taxation, Finance and Project implementation
- A Qualified Chartered Accountant having sharp financial acumen, negotiation skills and a great passion for technological advancements

Soda ash segment – Cash cow business

Key soda ash player in the country

GHCL enjoys a dominant position in the concentrated soda ash industry in the country. The domestic soda ash industry is dominated by a few large players like Nirma (25% market share), Tata Chemicals (24%) and GHCL (23%), with imports catering to another 24% of demand. However, due to significant logistics cost, imports are limited to coastal areas only (South and East).

Exhibit 12: Market share of Soda Ash players



Source: Industry, Emkay Research

Soda ash contributes ~80% to company's profitability and enjoys high returns

GHCL is one of the largest focused soda ash players, as soda ash accounts for approximately 58% of revenues and 80% of company's profit. Other players like Tata Chemicals, Nirma and DCW have lower contribution from soda ash due to their diversified business presence.

Exhibit 13: Soda ash players and their business profile

Player	Soda ash presence	Presence in other businesses	Significance of soda ash in total revenue pie	Future capex initiatives
Tata Chemicals	Key player in soda ash in the country, with 24% market share; World's 3rd largest soda ash player	Tata Chemicals, apart from soda ash has diversified business with presence in fertiliser, pesticides and consumer businesses like salt and pulses	Soda ash contributes ~50% to revenues and 75% to profitability	Company does not have any significant capex plan in soda ash. It is primarily focusing on its consumer business
NIRMA	Nirma is the leader with 25% market share in India.	Nirma is a key player in detergent, toilet soaps etc	Soda ash contributes 1/3rd to revenues.	Company is in the process of increasing soda ash manufacturing capacity by 0.2 mn tpa, that is likely to get completed by FY17
DCW	Relatively small player in soda ash with less than 2-3% market share	DCW has presence in caustic soda, PVC and other chemicals	Soda ash contributes only 15% to company's revenues and ~45% to profitability	Company has no firm plans to increase its capacity in soda ash
GHCL	Key player in soda ash in the country with 23% market share	GHCL has presence in textile and home fabrics with focus on exports	Soda ash contributes ~60% to revenues and 80% to profitability	Company is in the process of increasing soda ash manufacturing capacity by 0.1 mn tpa, that is likely to get completed by FY17

Source: Industry, Emkay Research

Presence in Sodium Bicarbonate and Edible salt

The other product that the company offers is **Sodium Bicarbonate** (0.7 tonnes of soda ash required to make 1 tonne of sodium bicarbonate). The realisation for this product is almost similar to soda ash realisations. The product is mainly used for cooking. The company has a total capacity of 70 TPD and currently enjoys a 13% market share in India.

The company is also present in the **edible salt** segment. The capacity for this product is located in South India with raw salt manufacturing capacity of 0.15 mn tpa and refined salt capacity of 75 thousand tpa. GHCL sells salt through brands like Sapan & i-FLO.

Capacity additions to drive soda ash revenues and profitability

Capacity expansions to further boost profitability

Incremental soda ash production to provide EBITDA margins upward of 50%

GHCL plans to increase its soda ash capacity by 0.1 mn tpa through a brownfield expansion with investment of Rs. 3.75 bn that is likely to be completed by March 2017. This brownfield plant comes at a capital cost of Rs 37,500/mt as against an estimated Rs 50,000/ mt for a Greenfield plant. New plant will have EBITDA margins above 50%, as it will not lead to any increase in fixed cost. Thus, the expansion in soda ash segment will further boost the company's profitability and return ratios.

Exhibit 14: Economies of existing soda ash plant

Particulars	Amount (Rs per tonne)
Soda ash realisations	19,200
EBITDA (Based on 34% EBITDA margin in FY16)	6,528
Total cost	**12,672**
of which:	
Variable cost (40%)	7,740
Fixed overhead cost (60%)	5,069

Source: Company, Emkay Research (The above data is gathered from our recent plant visit)

Exhibit 15: Economies of new soda ash plant

Particulars	Amount (Rs per tonne)
Soda ash realisations	19,200
Variable cost	7,740
EBITDA	11,460
Resulting EBITDA margins	*60%*

Source: Company, Emkay Research (The above data is gathered from our recent plant visit)
Note – Above calculation is based on assumption that it is a brownfield capex and will not result into similar increase in overhead cost.

Exhibit 16: Variable cost break-up

Raw materials	Requirement per tonne	Cost (Rs per tonne)	Total cost (Rs per tonne)
Salt	1.8 tonnes	700 per tonne	1260
Limestone	1.8 tonnes	700 per tonne	1260
Coal	430 kg		2500
Briquette	150 Kg		1800
Packing			270
Ammonia and other minor raw material			300
Internal usage of soda ash ~5-7%			350
Total			**7740**

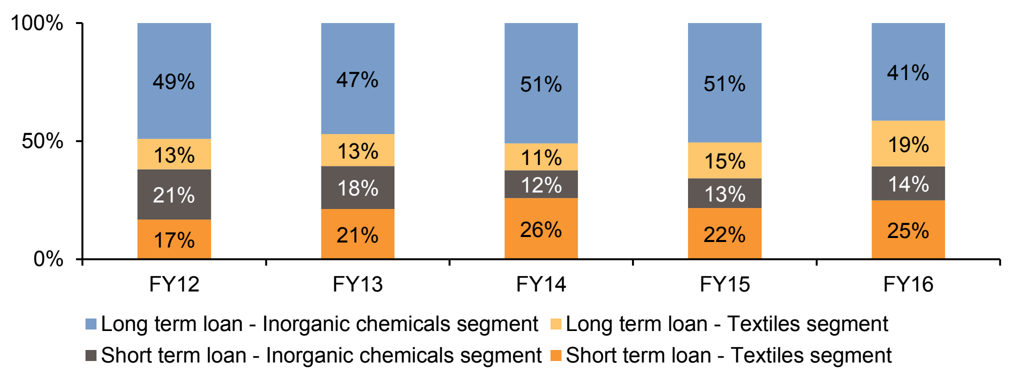
Source: Company, Emkay Research (The above data is gathered from our recent plant visit)

Low working capital of soda ash business supports bottom-line profitability

Low working capital requirement in soda ash business

The company generally does not keep soda ash inventory as it is directly sold from factories. However, company maintains inventory of salt (key raw material for soda ash) i.e. about 0.3 mn tonnes at its plant i.e. roughly 2.5-3 months requirement. We believe the incremental 0.1 mn tonne soda ash production with limited inventory will also support higher profits in this business.

Exhibit 17: Low working capital requirement for soda ash business



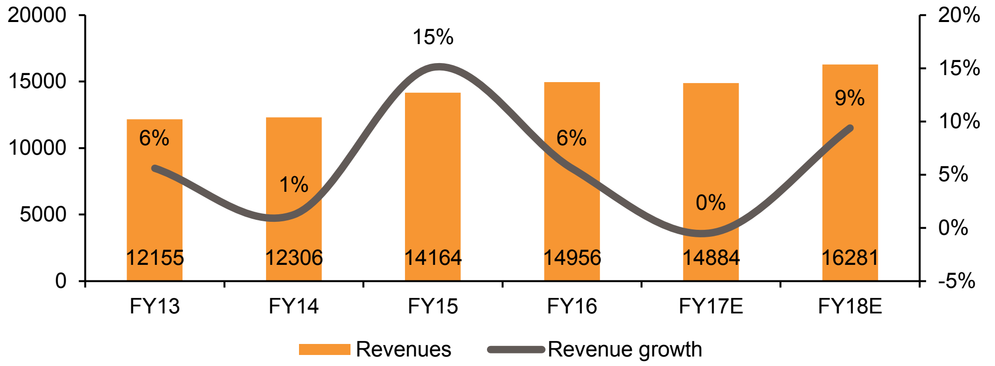
Source: Company, Emkay Research

Ongoing capex unfolds revenue growth in FY18

Increase in soda ash capacity to provide revenue growth potential in FY18

GHCL is currently operating at around 88% utilization rate, which is the highest ever utilisation achieved by the company. Further, such utilisation rate is also one of the benchmarks in the domestic as well as global markets. With GHCL operating at optimum utilization level, we do not expect any volume growth in FY17. Company is in the process of expanding capacity to 0.95 mn tpa from 8.5 mn tpa currently. The capacity is likely to get commissioned by March 2017 and is expected to drive revenue growth for FY18. We expect soda ash prices to remain largely stable over the next two years and thus, revenues will be driven by volume growth in FY18.

Exhibit 18: Inorganic Chemical Revenues (Rs mn) and Revenue growth (%)



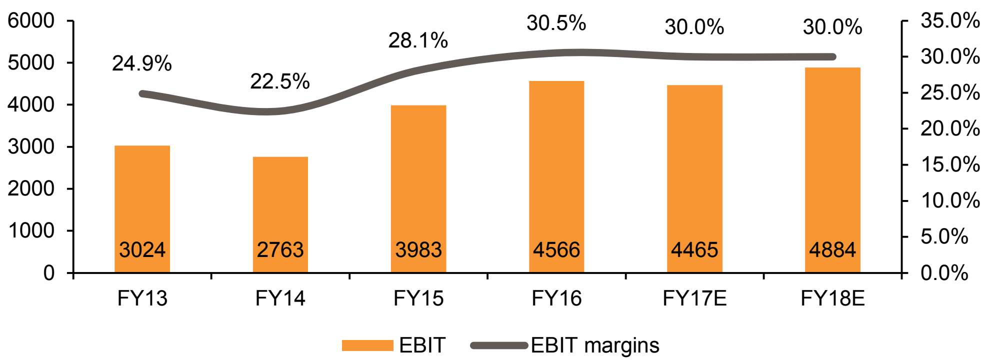
Source: Company, Emkay Research

Margins are likely to remain healthy

GHCL will continue to be cost leader with highest margin in the industry

Amid seasonality, GHCL has been constantly earning higher margins compared to its peers led by higher operating efficiency. We believe, this trend is likely to continue with company achieving EBIT margins of around 30% in the next two years.

Exhibit 19: EBIT (Rs mn) and EBIT Margins (%)



Source: Company, Industry

We have not assumed margin expansion in FY18, despite higher margins from the brownfield project mainly because the expanded capacity will not operate at optimum capacity from first year of operation.

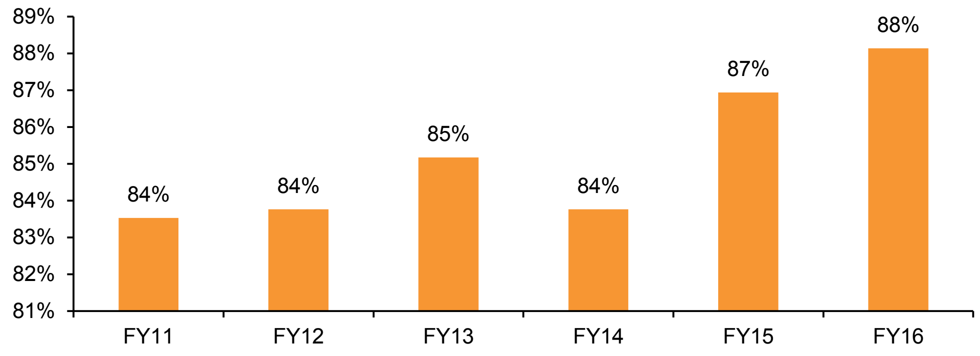
What makes GHCL enjoy highest margins in the industry?

i) Highest utilisation rate in the industry

GHCL benefits from higher capacity utilization of ~88% compared to 80-85% utilization rate in industry

GHCL enjoys higher capacity utilization at its soda ash plant compared to industry. Capacity utilization at 88% in FY16, was the highest in the domestic soda ash industry, which was operating at about 80-85%. The utilization rate of GHCL's soda ash plant is also one of the benchmarks in the domestic as well as global market. Production in Soda ash plants suffers from seasonal volatility and adversely affects utilization rates, hence making 88-90% utilization level optimal. GHCL's backward integration, efficient management of raw materials and sustained investment in maintenance of plants and machinery has helped the company to operate the plant at optimum utilization level, thereby leading to higher operating leverage.

Exhibit 20: GHCL Soda ash plant utilization rate



Source: Company, Emkay Research

ii) Captive availability of raw material and integrated plant supports cost efficiency

Typically, Soda ash industry entails significant use of raw material due to adverse input / output ratio. One tonne of Soda ash requires approximately 5 tonnes of inputs, making logistics cost a key driving factor of the total cost. Hence, proximity to raw materials becomes a key success criteria. GHCL has successfully created a well-integrated business model with captive availability of raw materials, leading to cost leadership in the industry. As a result, it enjoys 400-800bps higher margins than its peers.

Exhibit 21: GHCL: Captive integration

Input	Captive (%)
Salt	56%
Limestone	33%
Briquette	74%
Lignite	20%

Note: All limestone mines are within 40km distance
Source: Company, Emkay Research

iii) Distinct cost advantage

GHCL is the only player to have its own lignite mines, which gives the company a strategic edge

GHCL is the only player to have its own lignite mines, which gives the company a strategic edge, ensuring cost advantage in utilities. Further, the company has a unique advantage, where in it has replaced Met Coke with in-house developed Briquette coke. Thus, the company also benefits from lower briquette cost compared to coke. Recently, the company has also invested in condensing turbine resulting in decline in utility cost.

iv) Built in operational efficiencies

Over the past many years, GHCL is running various cost efficiency programs comparable to Six Sigma projects and other cost reduction projects. Apart from these cost reduction programs, the company regularly spends Rs. 400-500 million every year on its plants and machinery as maintenance capex to increase the efficiency of plants. These efficiencies in their plants have led to highest utilization rate in the industry.

Concerns – Soda ash segment

i) Anti-dumping duty on Soda ash coming off

Domestic soda ash industry continues to be protected by anti-dumping duties levied on various nations. Anti-dumping duty on Soda ash came into force in July 2012. The duty ranges from $9 per tonne for European Union to $39 for US. The duty on most of these countries will be valid till July 2017. Despite anti-dumping duties on these countries, around 24% of total demand in India is being imported given the high cost of transportation from the West to East or South.

Domestic soda ash industry is currently protected by anti-dumping duty on various countries

Exhibit 22: Anti-dumping duty list

Countries	Duty range ($ per tonne)	Valid till
China	36.26	3rd July, 2017
European Union	9.17	3rd July, 2017
Iran	28.86	3rd July, 2017
Kenya	20.35-28.86	3rd July, 2017
Pakistan	2.38-10.34	3rd July, 2017
USA	38.79	3rd July, 2017
Ukraine	15.64	3rd July, 2017
Russia	35.99	18th April, 2018
Turkey	18.39-75.16	18th April, 2018

Source: Ministry of commerce, Emkay Research

Our analysis suggests less than 5% decline in prices

Major imports in India are from Europe, accounting for around 50% of total imports, while China accounts for 15-20% of total imports. Across geographies, Soda ash has remained primarily a domestic commodity, wherein only surplus volumes are exported. Even for China, exports accounts for roughly 8-10% of production. Generally, prices in domestic markets for these countries are higher than in India and exporters match domestic prices prevailing in the importing country. Since the lowest anti-dumping duty on major exporter of Soda ash (European Union) is $9 per tonne i.e. less than 5% of prices, maximum destruction on prices can only be in that range, as the remaining producers will try to match the prices at that level.

Our analysis suggest less than 5% decline in soda ash prices due to removal of anti-dumping duty

Exhibit 23: Sensitivity analysis for drop in soda ash prices

Drop in soda ash price (Rs/tonne)	-500	-1000	-1500	-2000
For FY17				
Assumed Sales Volume -748340 MT				
Decline in value terms (Rs mn)	-374	-748	-1123	-1497
Impact on PBT (as a % of PBT)	-8%	-17%	-25%	-34%
For FY18				
Assumed Sales Volume -766170 MT				
Decline in value terms (Rs mn)	-383	-766	-1149	-1532
Impact on PBT (as a % of PBT)	-7%	-14%	-21%	-28%

Source: Emkay Research

Margins in soda ash likely to remain protected

Anti-dumping duty for soda ash came in July 2012. Even after the duty was imposed, domestic industry players did not take any price hike for one year. We believe soda ash will continue to remain a domestic commodity, wherein supply threat from other countries will be limited to coastal areas because of huge logistics cost.

ii) Commissioning of 3 mn tonnes of capacity in Turkey

Turkey is planning to come with natural soda ash capacity of 3 mn tonnes, which is equal to total demand in India. The capacity is likely to come up in 2018, post the addition of 300,000 tonnes combined by Nirma and GHCL in FY17. Further, the anti-dumping duty ranging from $18-75 on imports from Turkey is also valid till April, 2018. Thus post the expiry of this anti-dumping duty, imports from Turkey can increase sharply and impact utilization rates in domestic market. However, we do not envisage this situation as the incremental soda ash will be first supplied to European markets and then to Asian countries.

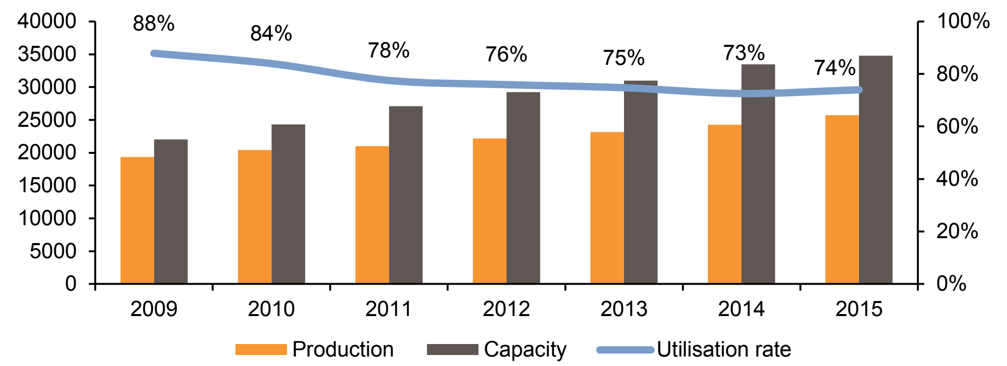
iii) Slowdown in China can see dumping of soda ash in India

China with a capacity of around 33.5 mn tpa, is the largest producer and consumer of soda ash. Due to slowdown in its domestic market, the country is dumping its excess production in the global market. This is also visible from aggressive exports of soda ash from China. Going forward, weak domestic consumption in China may push exports to various nearby countries like Middle East and some other Asian countries, which may put pressure on realisations.

China does not enjoy any cost advantage over India, since it has been witnessing cost pressures like rising fuel and power cost. Also, soda ash being bulky material, suffers from huge logistics cost, which affects long movement on roads / inland transportation. However, increase in dumping to enjoy higher utilisation rates may disrupt pricing in domestic market.

Further slowdown in China can add pressure on prices

Exhibit 24: Demand-supply in China



Source: Industry, Emkay Research

Following are the key reasons for increase in exports from China:

- **Slowdown in the domestic market:** China is the largest producer and consumer of soda ash, having almost 50 per cent of the world's total soda ash capacity and consuming about 41 per cent of the world's total soda ash consumption. The engine for growth on a global basis has been driven by China and latest data is showing a slight decline in demand in their domestic markets. From January to June 2015, domestic demand in China was down by 1.1 per cent on a y-o-y basis, primarily due to drop in domestic glass production. This has also led to decline in domestic soda ash prices in China. As a result, the country's producers are looking for external markets to offload material that cannot be consumed domestically.
- **Increase in ammonium chloride prices**: In 2014, China produced around 45 per cent of its total soda ash production via the Hou process. Under the Hou combined-soda process, the output ratio of soda ash to ammonium chloride is 1:1. Ammonium chloride prices have been very weak for a number of years. Recently, relaxation in Chinese export policies and the introduction of a 5% flat export tax replacing a seasonally variable rate, has led to increase in prices of ammonium chloride and thus boosted soda ash output. Further, the rising price of ammonium chloride has pushed previously loss-making producers of soda ash into profit. This is also leading to increase in soda ash production from China, world's largest producer of soda ash.
- **Decline in freight rates:** As per the Chinese Containerized Freight Index (CCFI), there has been a collapse in freight rates for containers from China to large number of destinations worldwide. The drop in freight rates is due to weak demand for Chinese goods around the world and a huge over supply of containers ships. Thus, along with decline in soda ash prices from China, the sharp drop in freight rates has meant even lower prices on a CFR basis to a number of destinations.
- **Depreciation of Chinese currency:** China has recently carried out the biggest devaluation of its currency (Yuan Renminbi) in decades. The sharp and recent fall in Yuan is likely to support continuing strong soda ash exports from China.

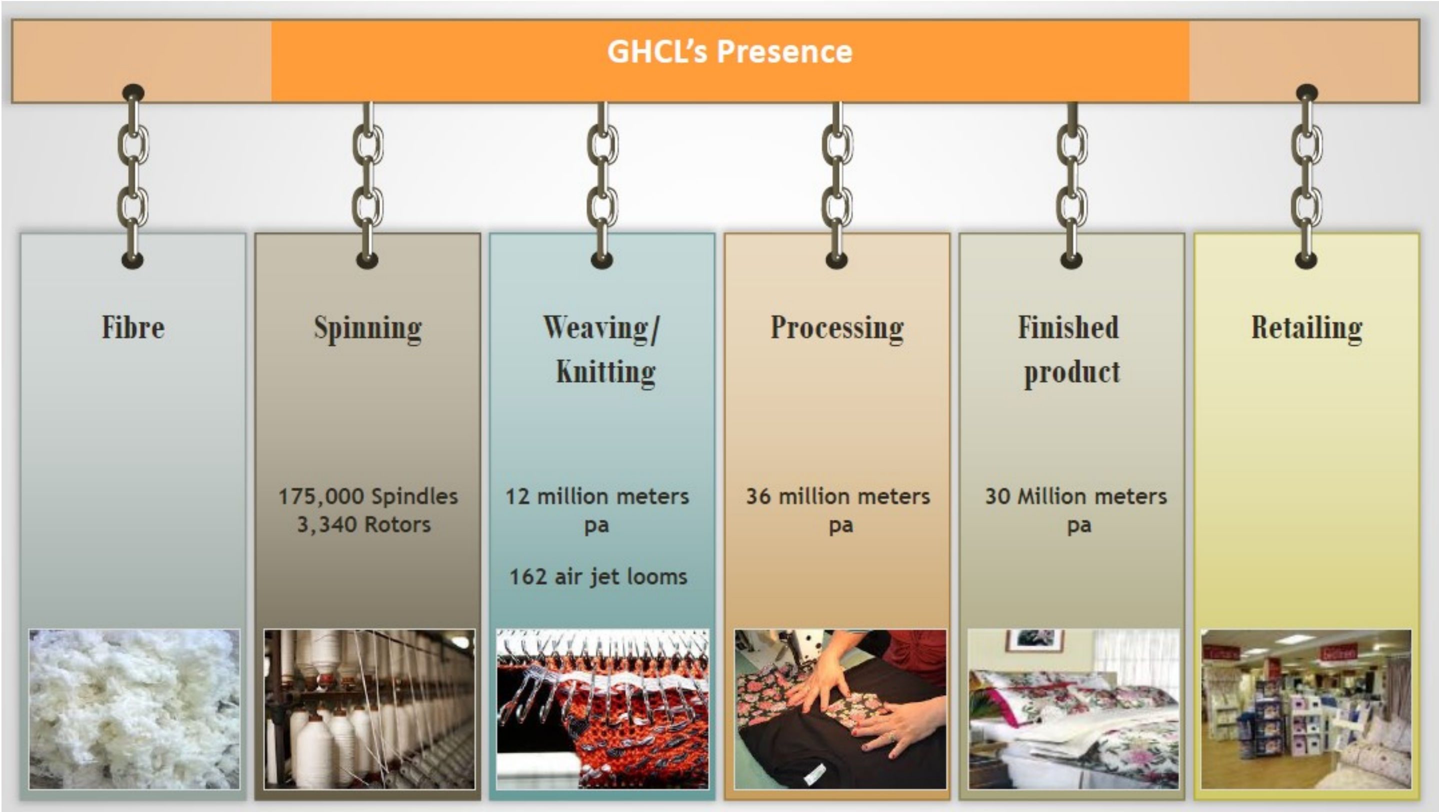
Textiles – Key growth driver

GHCL – An integrated player in textiles

GHCL is one of the largest integrated textile manufacturers in India with presence in both spinning and home textiles business. The company has an integrated vertical set up- right from spinning of fiber (yarn), weaving, dyeing, printing till the finished products, like sheets & duvets, take shape, which are primarily exported worldwide.

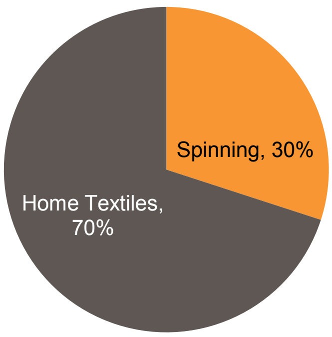
GHCL's spinning unit with installed capacity of 175,000 spindles is located near Madurai in Tamil Nadu, India. The company manufactures multiple varieties of yarn, ranging from 16s to 21s in open end, 30s to 100s in ring spun counts in 100% cotton and 30s to 70s counts in blended yarns. Further, company's home textiles manufacturing is located near Vapi in Gujarat, India. Here, yarn is woven into fabric, which is then dyed, printed and finished into final products like bed sheets, which are then exported.

Exhibit 25: Presence across the textile value chain



Source: Company, Emkay Research

Exhibit 26: GHCL's textiles segment revenue break-up



Source: Company, Emkay Research

Immense scope for improvement in textiles business

GHCL's margins are also one of the lowest in the home textile's industry

GHCL is one of the late entrants in the home textile segment. This segment generally takes time to acquire quality customers (who can ensure healthy volumes and pricing). Company supplies its fabrics to private label brands in export markets. In this segment, GHCL competes with established players like Welspun and Indo Count. Being the late entrant, GHCL's margins are also one of the lowest in the industry, mainly due to low utilization rates.

Exhibit 27: Textiles: Peer comparison

Company Name	Presence	Capacity (mn meters)	Planned Expansion (mn meters)	Capacity Post Expansion (mn meters)
Alok	Spinning / Weaving/ Processing /Made-ups/ Others	150	-	150
Welspun India	Spinning / Weaving/ Made-ups/ Distribution / Captive Thermal Plant/Others	72	18	90
Indo Count Industries	Spinning / Weaving/ Processing /Made-ups/ Others	68	22	90
GHCL	**Spinning / Weaving/ Processing /Made-ups/ Captive Wind Mills / Others**	**36**	**4**	**40**
Himasingka Scide	Weaving/ Processing / Made-ups/ Distribution / Captive Thermal Plant	25	-	25
Trident	Spinning / Weaving/ Processing /Made-ups	-	43	43

Source: Industry, Emkay Research

Exhibit 28: Spinning Business comparison

Company Names	Capacity (No. of Spindles)
Vardhman Textiles	10,00,000
RSWM	4,68,152
KPR Mills	3,53,568
GHCL	**1,75,000**

Source: Industry, Emkay Research

Exhibit 29: Revenues (Rs mn)

Company	FY12	FY13	FY14	FY15	FY16
Revenues					
Himatsingka. Seide	14,287	16,894	20,282	19,406	18,088
GHCL	**8,236**	**10,595**	**10,170**	**9,572**	**10,634**
Indo Count Inds.	7,797	11,868	14,676	17,169	21,737
Welspun India	32,205	36,473	43,730	53,025	59,795
Trident	27,323	33,352	38,690	37,553	36,840.2
Alok Inds.	97,847	2,13,884	-	2,41,531	1,29,188.3
Revenue Growth					
Himatsingka. Seide	16%	18%	20%	-4%	-7%
GHCL	**46%**	**29%**	**-4%**	**-6%**	**11%**
Indo Count Inds.	10%	52%	24%	17%	27%
Welspun India	52%	13%	20%	21%	13%
Trident	52%	22%	16%	-3%	-2%
Alok Inds.	48%	-	-	-	-
EBIT					
Himatsingka. Seide	990	1,189	1,482	1,787	2,634
GHCL	**114**	**448**	**830**	**681**	**1,133**
Indo Count Inds.	321	859	1,695	2,719	4,547
Welspun India	1,949	4,958	3,389	10,362	12,740
Trident	1,127	3,163	4,755	3,739	4,130
Alok Inds.	16,015	35,926		39,838	-29,838
EBIT Margins					
Himatsingka. Seide	6.9%	7.0%	7.3%	9.2%	14.6%
GHCL	**1.4%**	**4.2%**	**8.2%**	**7.1%**	**10.7%**
Indo Count Inds.	4.1%	7.2%	11.6%	15.8%	20.9%
Welspun India	6.1%	13.6%	7.8%	19.5%	21.3%
Trident	4.1%	9.5%	12.3%	10.0%	11.2%
Alok Inds.	16.4%	16.8%	-	16.5%	-23.1%

Source: Company, Industry, Emkay Research
Note: ** Alok Industries results in FY13 are for 18 months from 1st Apr 2012 to 30th Sept 2013. Similarly, FY15 numbers results are from 1st Oct 2013 to 31st March 2015.*

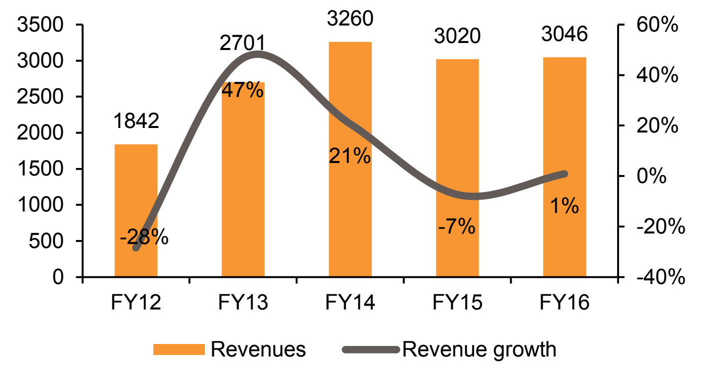
Home textiles business to drive growth

Revenues to be driven by higher capacity utilization

Increase in capacity utilization to drive revenue growth

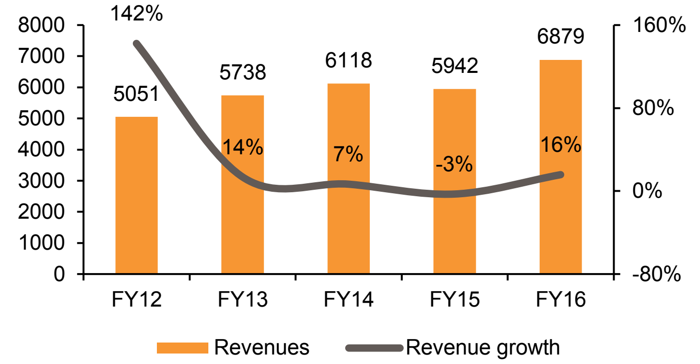
In FY16, GHCL's textiles segment revenues increased by 11% mainly led by increase in revenues of home textiles segment. During the year, the home textile segment's revenues increased by 16% yoy, mainly led by higher utilization rate, increase in exports and improvement in customer mix. On the other hand, the growth in spinning segment was impacted due to low yarn prices.

Exhibit 30: Spinning segment's revenue (Rs mn) and Growth (%)



Source: Company, Emkay Research

Exhibit 31: Home textiles revenues (Rs mn) and Growth (%)



Source: Company, Emkay Research

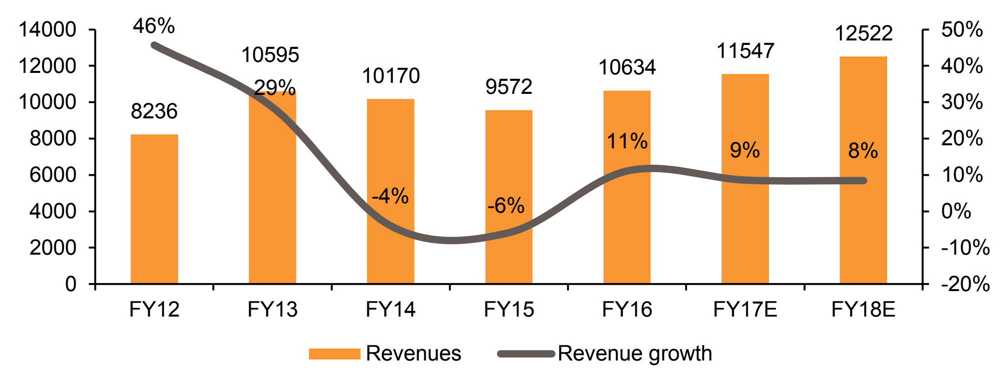
Going forward, we expect textiles segment revenues to increase by 9%/8% in FY17/FY18, led by continued increase in exports. Out of the total textile business production, GHCL sells only 2 per cent in the domestic market, while rest is exported.

GHCL benefitting from increase in export opportunities from the US and European countries

The demand in exports market is primarily driven by:

- **Production Shift:** Textile manufacturing continues to shift to low cost Asian countries
- **De-Risking from China** - Overseas buyers are looking to add India as an alternate supplier in order to de-risk their sourcing arrangements from China
- **Advantage India** – Major advantage with India is availability of raw materials, especially cotton. Further. integrated operations and design skills provide a competitive edge to Indian producers

Exhibit 32: Textiles segment's revenues (Rs mn) and Revenue growth (%)



Source: Company, Emkay Research

Capex plans to boost margins and improve return ratios

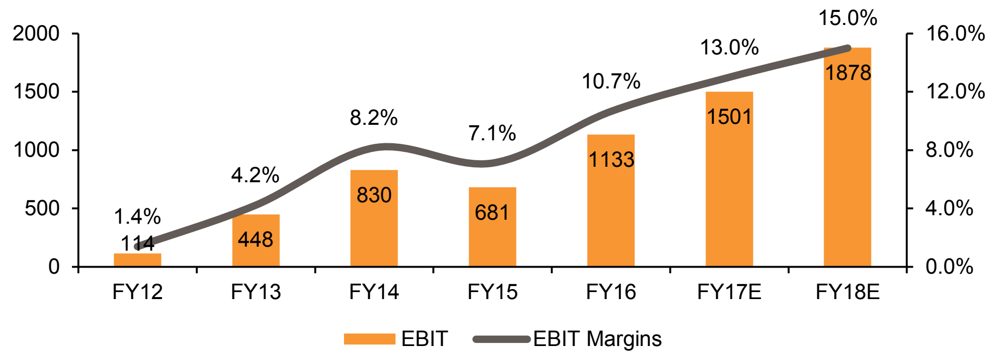
GHCL's operating margins in the textiles segment have been subdued compared to its peers. However, company is constantly investing in improving and modernising this segment in order to improve margins. In FY16, the company invested Rs 810 mn in increasing windmill capacity and Rs 710 million in its home textiles division, including investments in in-house stitching capacity with estimated cost of Rs 250-260 million, which got commissioned in quarter ending March, 2016. The company will further spend Rs. 500 million in FY17 on modernising its textiles plant.

Journey of margin improvement to continue

Margin expansion will be on the back of higher utilization rate, improved customer mix, wind mill installation and other cost optimisation

In the last 1-2 years, company has been constantly working on improving margins in this segment. As a result, EBIT margins in this segment have improved from 7% in FY15 to 11% in FY16. Further, with continued efforts, we expect margins in this segment to increase to 13%/15% in FY17/18. The margins improvement in this segment is likely to continue on the back of the following factors:

Exhibit 33: EBIT (Rs mn) and EBIT margins (%)

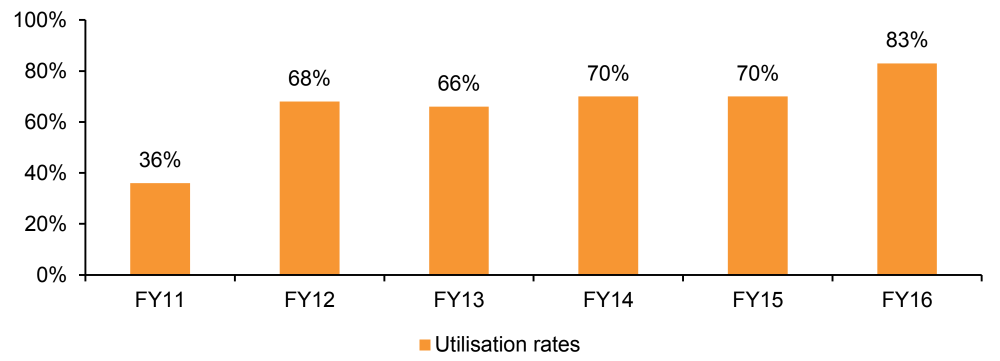


Source: Company, Emkay Research

i) Focus on higher capacity utilization

With focus on increasing presence in the exports market, GHCL has increased its utilization rate from 70% in FY15 to 83% in FY16. Further, with improving visibility from same customers and additions of new customers, company plans to increase its utilization rate to 95% in FY17 and achieve optimum utilization in FY18.

Exhibit 34: Increasing utilisation rates for textile segment



Source: Company, Emkay Research

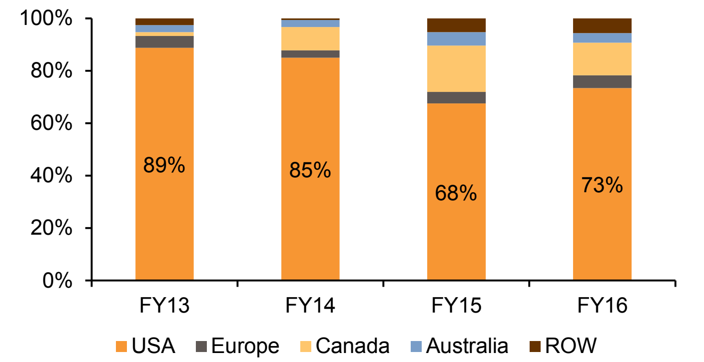
ii) Improved customer mix to drive margins

GHCL is a late entrant in home textiles segment compared to established peers like Welspun & Indo Count. The company in the recent years has started focusing on exports market by supplying to marquee customers like Bed Bath & Beyond, JC Penny and TARGET. Further, the proportion of replenishment programs from these customers have increased from 59% in FY13 to 68% in FY16. GHCL's major exports market is the US, followed by Canada, Europe and Australia.

Exhibit 35: GHCL Customer Profile

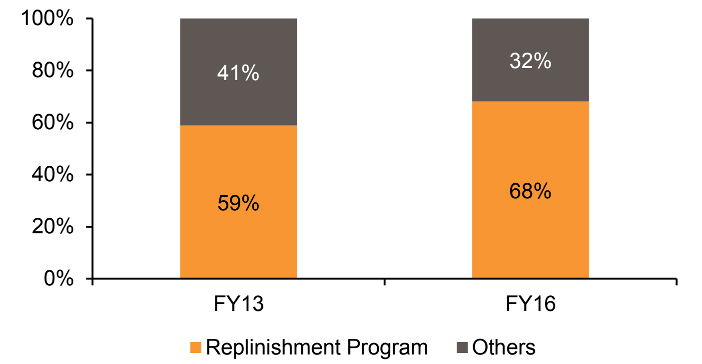
Source: Company, Emkay Research

Exhibit 36: GHCL's exports market share



Source: Company, Emkay Research

Exhibit 37: Proportion of replenishment programs

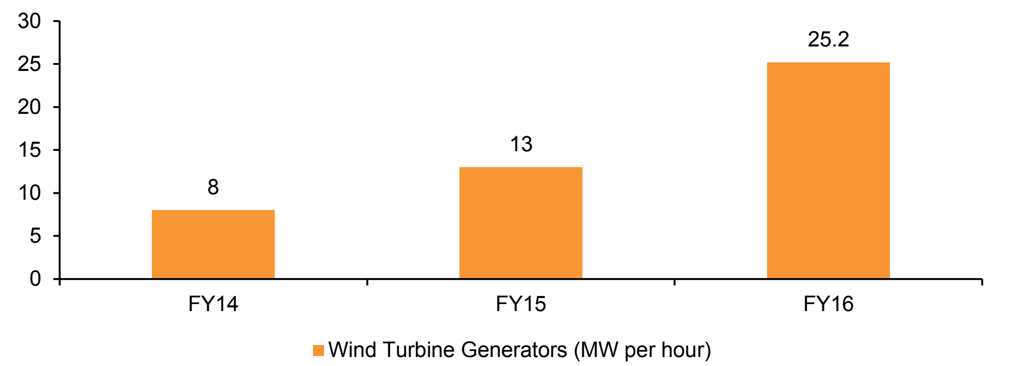


Source: Company, Emkay Research

iii) Benefit of wind mill installation

In the last two-three years, company has invested immensely in Green energy by installing wind turbine generators. The company increased power capacity generated though wind mills from 8 MW per hour in FY14 to 13 MW per hour in FY15. The company further invested Rs 810 mn in FY16 to increase this capacity to 25.2 MW per hour. The management anticipates increased cost savings from these capacity installations and expects 1% increase in margins in textiles segment, only because of investments in green energy.

Exhibit 38: Increased wind energy capacity



Source: Company, Emkay Research

iv) Cost optimization

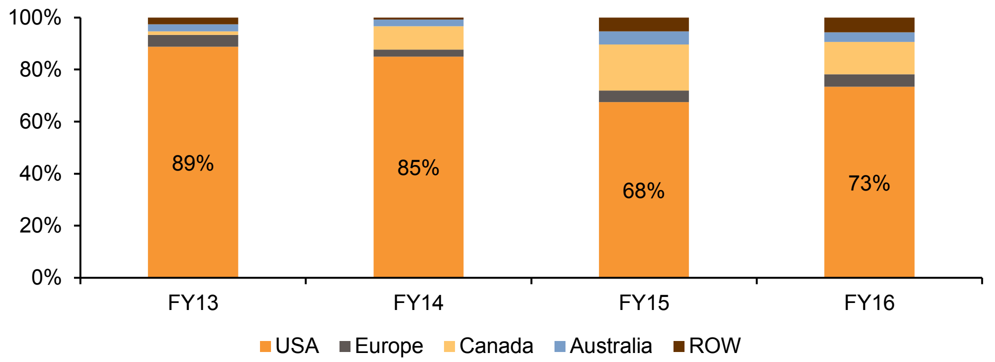
GHCL is the cost leader in soda ash segment with highest margins in the industry. Company plans to achieve similar cost efficiencies even in its textiles segment with continued spending on modernization and maintenance of its unit.

Concerns – Home Textile segment

i) Slowdown in US market

GHCL's revenues in home textiles segment are largely concentrated in US market. Thus, any slowdown in demand from US can significantly impact the utilization of its home textiles unit, resulting in lower profitability.

Exhibit 39: GHCL Home Textile export markets presence



Source: Company, Emkay Research

ii) Increase in competitive intensity

GHCL faces competition from well established players like Welspun, Indo Count, Himatsingka Seide, Alok and Trident in the home textile segment. Most of these players have focused on exports market, mainly US and Europe. Further, majority of these players are in the process of expanding capacity or have recently increased their capacity. These players also operate on higher margins compared to GHCL. Thus, increase in competitive intensity amongst these players can impact GHCL's pricing and thus, margins.

iii) Significant appreciation of rupee

Majority of GHCL's home textiles revenues come from exports. In the last few years, rupee depreciation has helped the company gain a competitive edge in the exports market. Any significant appreciation in rupee vs dollar can impact the competitive advantage of India (in particular GHCL) vs other competitor countries like China and Pakistan. Thus, pricing and margins of the company can get squeezed with significant appreciation of rupee.

iv) Further slowdown in the spinning sector

Indian spinning sector has been impacted because of increased availability and relatively low prices of manmade fibre. Further, the profitability of yarn spinners is under huge pressure due to volatile demand and prices of cotton and cotton yarn. Thus, with further fall in yarn prices, spinning industry will face huge pressure on profitability. GHCL is having larger presence on spinning side and thus, further fall in yarn prices can impact company's profitability significantly.

v) Interest rate risk

Cotton yarn industry requires huge working capital due to high inventory of cotton on account of its seasonal availability. Indian yarn spinners stock 2-3 months of cotton inventory due to its seasonal availability leading to high working capital requirement. This is largely funded by external borrowings, leading to high interest cost. Thus, a small increase in interest rate can impact the net margins of the company adversely.

vi) Changes in Government Regulations

Textile industry in India is getting many export incentives including ~7% duty drawback and ~2% MEIS. As per the WTO agreement, the incentives offered should be taken off over a period of time, when the exports of particular product from developing country gains significant share in global trade These changes in regulations pose a risk for the sector, as many countries have gained competitive advantage in exports market because of such incentives.

Done away with past losses

In the past, GHCL had entered into textile retail and distribution businesses by acquiring and setting up subsidiaries in UK, US and India. However, company had incurred losses of around Rs. 10 bn in these companies which led to shut-down of these businesses.

Exhibit 40: Summary of various subsidiaries

Subsidiary Names	Location	Business Description
Subsidiaries that are closed down		
Colwell & salmon Communication Inc	USA	The operations of subsidiary company engaged in the IT outsourcing business, have been stopped as the same were not viable.
Indian Britain B.V.	Netherlands	Textiles retail division in India was closed down as the company was making losses
Rosebys Interior India Limited	India	Was into the business of home furnishing retail in India
Indian England N.V.	Netherlands	Special purpose vehicle holding GHCL Upsom (SA Romania)
Indian Wales N.V.	Netherlands	Special purpose vehicle holding Textile retail in UK (Rosebys Operations Limited)
SC GHCL Upsom SA	Romania	The soda ash production of GHCL Upsom, Romania, a step down subsidiary of the Company was closed down due to outstanding issues with gas supplier that were creating troubles with production.
GHCL INC. USA.	USA	Special Purpose vehicle holding Home textile business in USA under DAN RIVER INC.
GHCL Rosebys Limited	UK	Special purpose vehicle
Rosebys UK Ltd	UK	Textiles retail division in UK was closed down as the company was making losses
Teliforce Holding India Ltd	Cyprus	Special purpose vehicle
Textile & Design Limited	UK	Was into the business of home textile retail in UK.
Fabient Textile Limited	India	Incorporated for textile business in India however remained dormant
Rosebys International Limited	India	Incorporated for textile business in India however remained dormant
GHCL International Inc. U	USA	Special Purpose vehicle holding Home textile business in USA under DAN RIVER INC.
Fabient Global Limited	India	Incorporated for textile business in India however remained dormant
Old Apparel Inc.	USA	Part of DAN RIVER Group, During the acquisition
Old Apparel Property Inc.	USA	Part of DAN RIVER Group, During the acquisition
GHCL Global Sourcing Limited	Isle of Man	Incorporated for textile business in India however remained dormant
Existing Subsidiaries		
Grace Home Fashion LLC	USA	Strategic subsidiary of the company with continued operations
Dan River Properties LLC	USA	Associate of DAN RIVER INC holding its real estate, Continuing till date

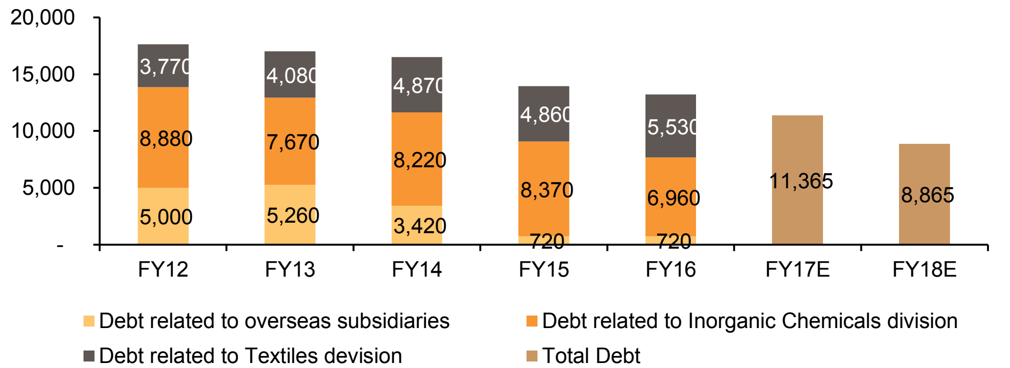
Source: Company, Emkay Research

Losses in overseas subsidiaries written-off; now the focus on standalone debt reduction

Over last 4-5 years, GHCL has substantially paid all its debt related to subsidiary

Over the past 4-5 years, in line with the strategy of closing down the retail divisions, the company had taken substantial write-offs. These write-offs in the overseas subsidiaries were funded by strong cash flows from its core businesses. As a result, the company's standalone business did not see any debt reduction. As the losses in overseas subsidiaries have been written-off and major capex in both the businesses are nearing completion, the major focus for the company from FY18 will be debt reduction.

Exhibit 41: Reduction in overseas debt (Rs mn)



Source: Company, Emkay Research

The only two subsidiary that remains with the company now is Grace Home Fashion LLC and Dan River Properties LLC, located in the US. Grace Home Fashion LLC, a 100% subsidiary of GHCL is the strategic arm which takes care of all the billings in the US.

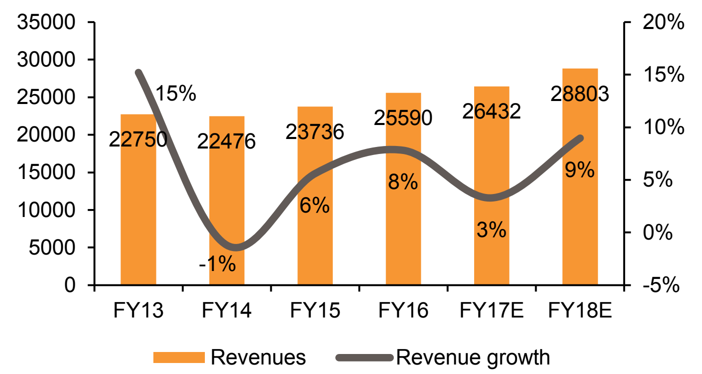
Financial Analysis

Soda ash will contribute to revenue growth in FY18

Capacity expansion in soda ash to add to revenue growth in FY18

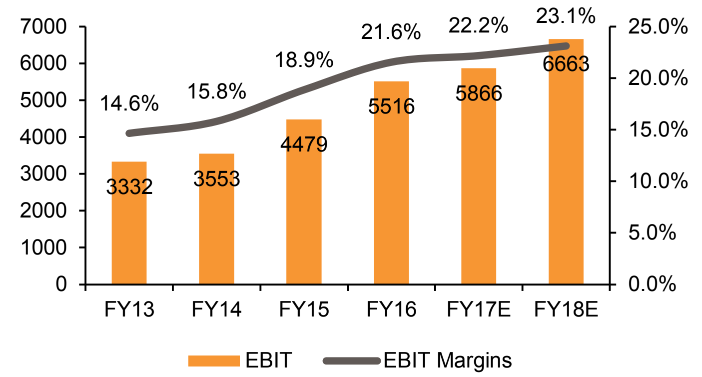
We expect GHCL's revenue growth in FY17 to be driven by the 9% growth in textiles segment due to increasing export opportunities. Further, in FY18, along with continued improvement in textiles segment, the company will benefit from increase in soda ash capacity from 0.85 mn tpa to 0.95 mn tpa. We expect GHCL's revenues to increase at 6% CAGR over FY16-18E.

Exhibit 42: Revenue (Rs mn) and Revenue growth (%)



Source: Company, Emkay Research

Exhibit 43: EBIT (Rs mn) and EBIT margins (%)



Source: Company, Emkay Research

Textile segment to drive margin expansion

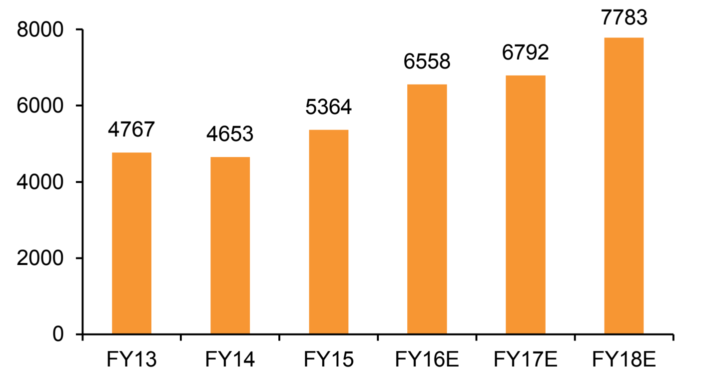
Margin expansion will be driven by improvement in textiles segment

GHCL's margins in Soda ash segment have remained healthy led by cost leadership in the segment. Going forward, we believe that GHCL's margin growth will be led by margin expansion in the textiles segments from 11% in FY16 to 15% in FY18. Overall margins of the company will improve by ~160 bps to 23%. We expect EBIT to increase at a CAGR of 10% over FY16-18E.

Healthy cash flows to translate into debt reduction in FY18

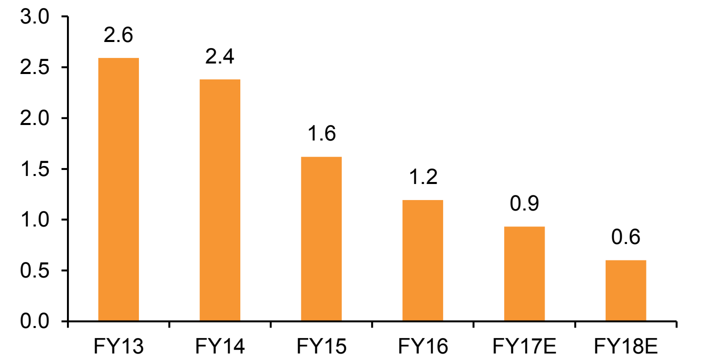
In the year FY16, strong cash flow generation has helped them finance capex of Rs. 2.5 bn (Rs1 bn towards inorganic chemicals and Rs. 1.5 bn towards textiles) along with debt reduction of Rs 700 mn. In FY17, despite major capex, company plans to repay Rs.300-500 mn debt. We believe FY18, will be the year for major debt repayment, as company does not have any capex plans in FY18. This will help company bring down its debt-equity ratio to 0.6 in FY18.

Exhibit 44: Healthy cash flow generation (Rs mn)



Source: Company, Emkay Research

Exhibit 45: Declining Debt-Equity ratio



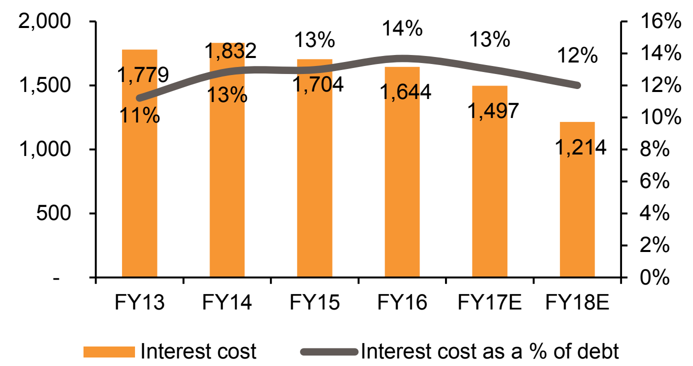
Source: Company, Emkay Research

Debt repayment and improvement in debt rating would translate into higher bottom-line growth

Lower interest cost will translate into higher bottom-line profitability

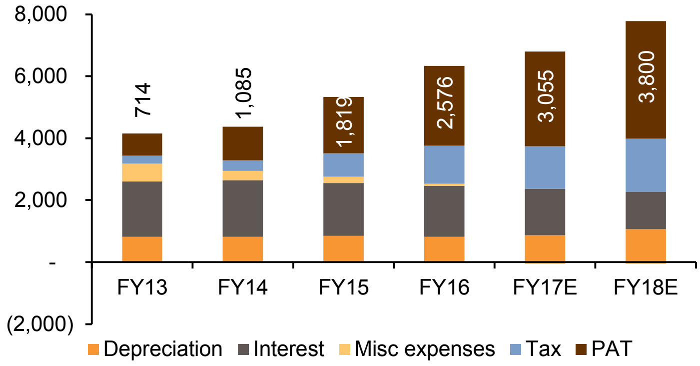
Followed by debt reductions and healthy cash flow generation, company's long term debt ratings have improved from –BBB to +BBB and with continued robust cash generations and debt reductions, the ratings are likely to improve further. The improvement in ratings, decline in overall interest rates along with substantial reduction in debt will lead to decline in interest cost by 9%/19% in FY17/18E. Thus, with improvement in operating profits and reducing interest cost, we expect PAT to increase at CAGR of 21% over FY16-18E.

Exhibit 46: Interest cost (Rs mn) and interest cost as a % of debt



Source: Company, Emkay Research

Exhibit 47: EBITDA break-up (Rs mn)

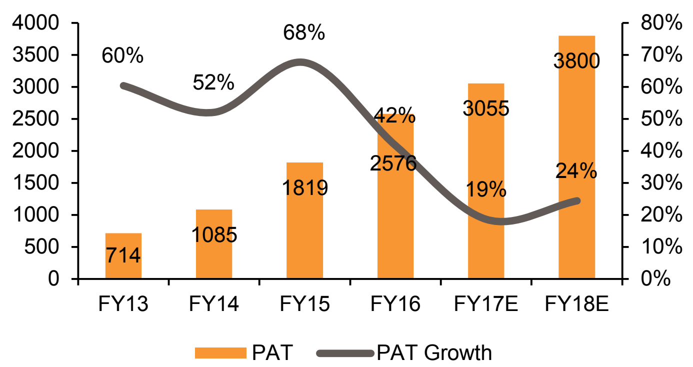


Source: Company, Emkay Research

Return ratios to remain healthy going forward

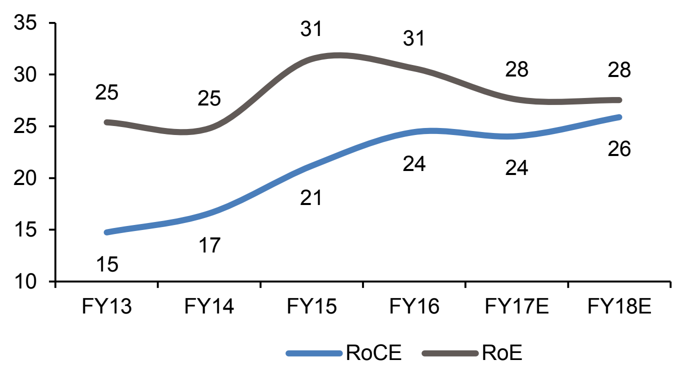
With increase in margins and improvement in balance sheet, GHCL's RoCE has improved from 15% in FY13 to 25% in FY16. Further, RoE has also increased from 25% in FY13 to 32% in FY16. Going forward, we expect return ratios to remain healthy, given the improvement in margins and continued debt reduction.

Exhibit 48: PAT (Rs mn) and PAT growth (%)



Source: Company, Emkay Research

Exhibit 49: Improved return ratios (%)



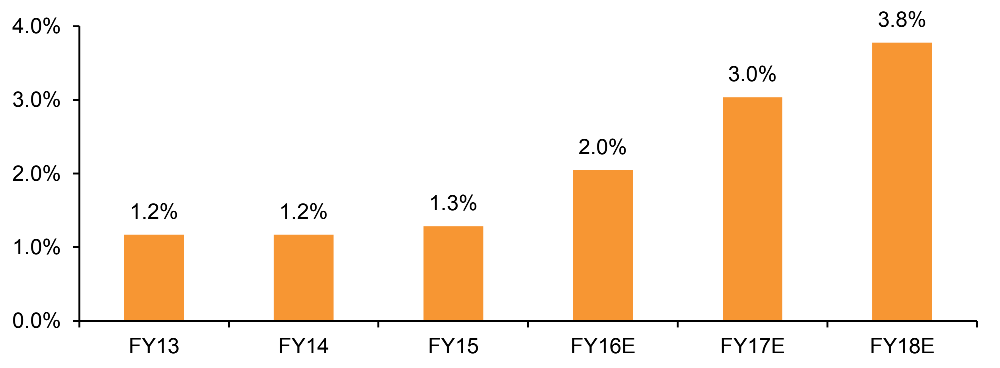
Source: Company, Emkay Research

Initiate with Buy on compelling valuations

We believe, GHCL will continue to generate steady cash flows on the back of its cost leadership in soda ash business and improvement in performance of its textiles segment. We expect revenue/EBITDA/PAT to clock 6%/10%/21% CAGR during FY16-18E. After meeting future capex requirements, company will be able to focus on significant debt reduction from FY18E. Valuations look attractive as at the CMP of Rs 171, the stock is trading at 4.4x FY18E EPS of Rs 38, EV/EBIDTA of 3.2x and P/BV of 1.1x. Given company's strong earnings growth of 21%, RoCE / RoE of 26%/28% and strengthening balance sheet with D/E of 0.6x (FY18E) we believe that company's stock has significant re-rating potential.

Valuing the stock at 6xFY18 our fair value for the stock works out to be Rs 228. We initiate coverage on GHCL with Buy rating. Given company's dividend policy in placed with growing EPS, stock offers dividend yield of 3.8% (FY18E) and further protects downside risk.

Exhibit 50: Dividend Yield



Source: Company, Emkay Research

Key risks / Concerns

Change in industry dynamics for soda ash

Historically, soda ash has been a domestic commodity, where exports are limited to excess production. The industry also has a number of entry barriers including high capital investments and various raw material constraints. This is the reason why supply generally follows demand and new players have not entered this business in the past decade.

However, growing share of natural soda ash globally, can be a threat to synthetic soda ash producers. We believe, as seen in the past, the natural soda ash producers will first gain market share from high cost producers in Europe, where increasing costs are leading to shut-downs of soda ash plants in Europe in the past 2-3 years. Further, there is a 3 mn tonnes per annum natural soda ash capacity coming up in Turkey, which is closer to total capacity in India. Capacity expansion globally along with increase in capacity in domestic market can create temporary pressure on soda ash prices.

Slow margin expansion in textile business

In FY16, GHCL's EBIT margins expanded by ~400 bps from 7% to 11% in line with expansion of margins for other players in home textiles segment. In the last two-three years, the Indian home textiles players have benefited from increasing export opportunities, mainly to US and Europe. However, any slowdown in exports can lead to drop in margins for all the players.

Exhibit 51: EBIT margins of Home textile players

Company	FY12	FY13	FY14	FY15	FY16
Himatsing Seid	6.9%	7.0%	7.3%	9.2%	14.6%
GHCL	**1.4%**	**4.2%**	**8.2%**	**7.1%**	**10.7%**
Indo Count Inds.	4.1%	7.2%	11.6%	15.8%	20.9%
Welspun India	6.1%	13.6%	7.8%	19.5%	21.3%
Trident	4.1%	9.5%	12.3%	10.0%	11.2%
Alok Inds.	16.4%	16.8%	-	16.5%	-23.1%

Source: Company, Industry, Emkay Research

Historical investments in overseas subsidiary that were written-off

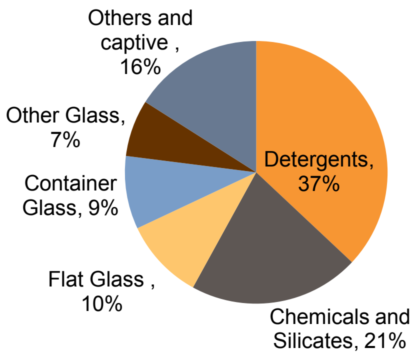
In the past, GHCL had invested immensely in the retail textiles division both globally and in India. Due to huge losses in all these investments, the company decided to close down all overseas ventures. In the last 4-5 years, the strong cash flows that were generated by existing domestic business were used to pay off the overseas debt that were used to write-off those businesses. Thus, the real repayment of standalone debt will now come in as the company is done away with writing off losses and all the required capex.

While the company has written-off all the losses made in the overseas subsidiaries, any future investments in unrelated businesses can adversely impact company's cash flows.

Is soda ash a commodity?

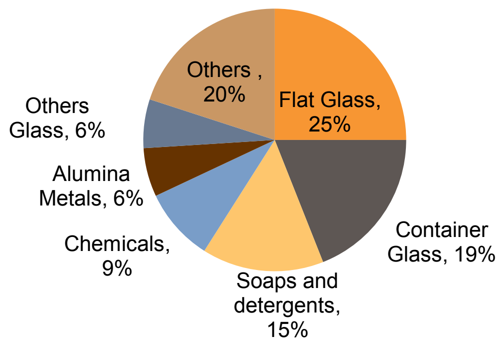
Soda ash is the basic raw material to manufacture soaps and detergents, glass and other sodium salts. Companies like HUL, Ghari, P&G, HNG, Videocon Industries, Piramal Glass Limited, St Gobain Glass are the major customers for GHCL in the soda ash segment.

Exhibit 52: India' Soda Ash demand by segment



Source: Industry, Emkay Research

Exhibit 53: Global Soda ash demand by segment



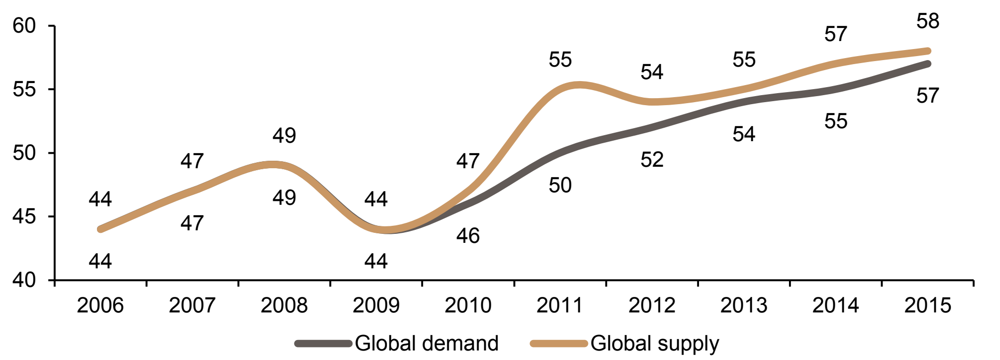
Source: Industry, Emkay Research

Soda Ash – a resilient commodity

Despite sharp volatility in other commodity markets, soda ash is one of those rare commodities whose prices have remained largely stable, mainly led by vigorous demand across the world. Also, number of plant closures due to rising production costs have restricted decline in soda ash prices. There have been a series of plant closures since 2000, which have reduced global soda ash capacity by 7 million tons.

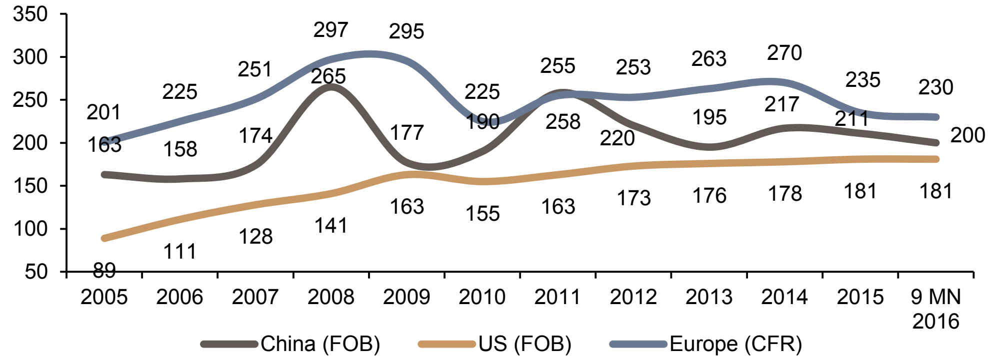
In 2014, there were series of plant closures in the UK and Kenya (Tata Chemicals), Portugal (Solvay group) and Australia (Penrice Holdings), primarily due to increased energy and raw material costs. At the same time, demand remained healthy, in particular from container glass, detergents and chemical industries, which led to firm prices. In 2015, prices were holding strong due to elimination of sizable capacity due to shutdowns and steady increase in global demand.

Exhibit 54: Global Demand and Supply for Soda ash (Mn MT)



Source: Industry, Emkay Research

Exhibit 55: Export price trend for soda ash ($ per tonne)



Source: Industry, Emkay Research

Soda Ash – Dynamics driven by domestic demand – supply rather than global

High freight cost makes long distant travel uneconomical

Soda ash can rather be termed as domestic commodity since freight cost plays a big role in setting the prices of products. Despite lower prices in other countries, namely US and China, high freight cost makes distant travel uneconomical. Freight cost, is thus a very big component in total soda ash cost.

Exhibit 56: Freight cost from various countries

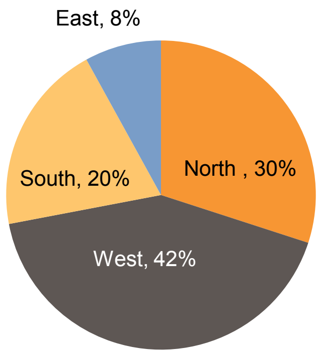
Countries	Freight Cost
US	$50 per tonne
Europe	$40 per tonne
China	$30 per tonne

Source: Industry, Emkay Research

Most of the produce is consumed either locally or in natural markets

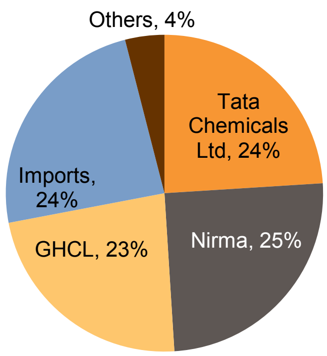
96% of soda ash capacities in India are located in Gujarat, where raw materials are easily available. On the other hand, demand for soda ash is scattered across India making transportation to North East and Sothern region expensive. Thus, around 24% of total demand in India is being met through imports due to high cost of logistics from West to North East and South.

Exhibit 57: Domestic demand scenario



Source: Industry, Emkay Research

Exhibit 58: Market share in domestic market

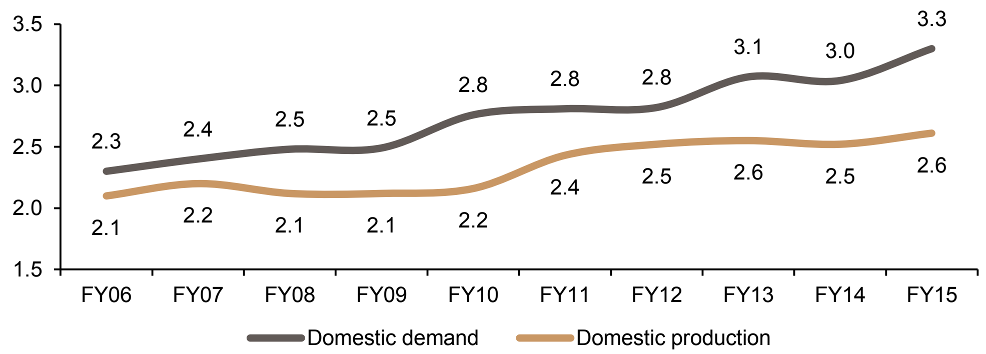


Source: Industry, Emkay Research

Supply follows Demand – No major mismatch

Over the years, it has been seen that supply follows demand for soda ash. In India, historically it has been seen that demand for soda ash is more than the supply in Indian market, thus creating positive pricing. Further, around one fourth of demand in India continues to be supplied by imports as the cost of transportation from West to East and South is very high.

Exhibit 59: Domestic Demand and Supply (mn MT)



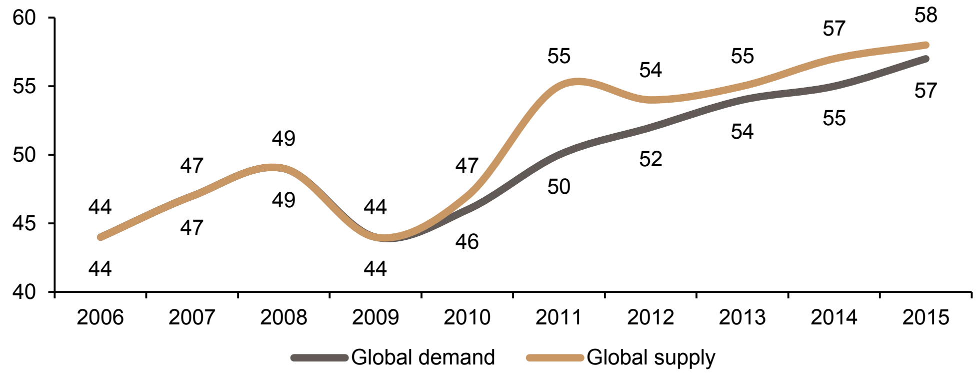
Source: Industry, Emkay Research

Soda ash demand to increase at a healthy pace

Steady growth in demand for soda ash over the years

Globally, there has not been any major mismatch in demand and supply of soda ash, thereby giving it stability. The last 10 years of data suggests that both demand and supply for soda ash globally as well as in domestic market have increased at a steady pace of about 4-5%.

Exhibit 60: Global Demand and Supply (mn MT)



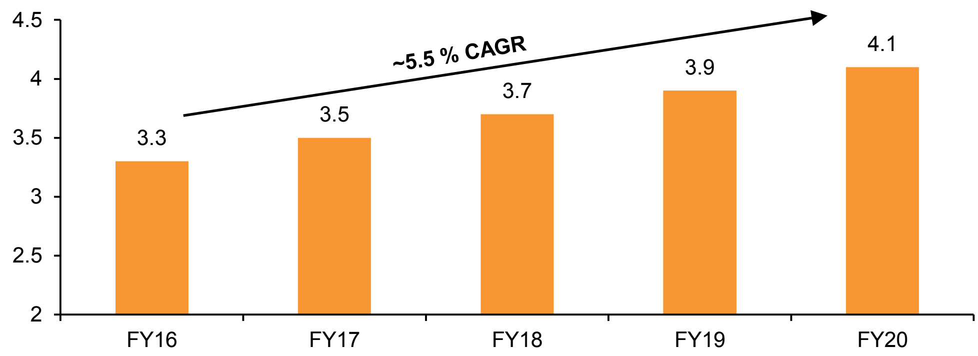
Source: Industry, Emkay Research

Soda ash demand will continue to grow at healthy pace

Demand is expected to increase at a steady pace of 4-5% CAGR over the next five years, largely driven by improvement in economic activity.

- **Detergents:** The detergents segment currently accounts for about 37-38 per cent of soda ash demand. Soda ash is mainly used as a filler in detergents, source for alkalinity and softening of water. Demand from soaps and detergents segment is expected to grow at a steady pace of 5-6 per cent CAGR on the back of higher disposable income and increase in penetration.
- **Glass:** The glass segment currently accounts for about 26-27 per cent of soda ash demand. Soda ash is the vital raw material in the manufacturing of glass (both flat glass and container glass). Demand from flat glass segment is expected to increase at a healthy pace led by growth in construction and automobile sector. Moreover, demand from container glass is also expected to grow at healthy pace, given the rise in consumption from end-user industries like pharmaceuticals and beverages.

Exhibit 61: Soda ash demand will continue to increase at a healthy pace (mn MT)



Source: Company, Emkay Research

Why many players do not enter this business?

As seen in the past few years, not many capacities have come in the soda ash industry. Thus, Indian soda ash industry remains fairly consolidated due to high entry barriers like:

i) Significant capex requirement

The cost of setting up Greenfield capacity is close to Rs. 50,000 per tonne in comparison with realisation of approx. Rs. 20,000 per tonne. This leads to high gestation period of about 4 to 5 years. Thus, adverse capital turnover ratio leaves no major incentive to add capacities in soda ash business.

ii) Huge logistics cost

Soda ash is a raw material extensive business. It takes about 5 tonnes of raw material to produce 1 tonne of soda ash. Thus, due to importance of logistics cost in the soda ash business, 96 per cent of capacities in India are located in Gujarat, where raw materials are easily available.

Exhibit 62: Raw material required for making 1 tonne of soda ash

Raw material	Requirement	Procurement
Salt	1.8 tonnes	50-60% from captive salt pans within 100 kms
Limestone	1.8 tonnes	Around 30-35% from captive limestone mines (located at Bhav Nagar), remaining from local market and imports.
Coal	430 kg	Imported from Indonesia
Briquette*	150 Kg	
Power	250 units	Captive power plant

Source: Company, Emkay Research (The above data is gathered from our recent plant visit)

***Note:** *The company has a unique advantage where in it has replaced imported Met Coke with in-house developed Briquette coke. Thus, the company also benefits from lower briquette cost compared to coke. The company is currently using briquette in its plant.*

iii) Raw material constraints

Salt, Limestone and Coke are the key raw materials for the soda ash industry. Being a raw material intensive industry, it requires nearness to raw material availability. Thus, domestic soda ash industry suffers from concentration risk as 96 per cent of the soda ash capacity in India is concentrated in Gujarat, mainly due to availability of key raw material.

While a large portion of these raw materials are captively produced by present companies, given the large requirements, sizable volumes still have to be sourced from the open market, where availability of good quality salt and limestone is a major problem.

- **Salt:** Salt prices have been consistently going up over the years. Since the last two-three years, with poor monsoon in the country, salt prices and availability has been in favor of the industry.

  Further, export of salt to countries like China, Japan, etc., who offer higher price, leads to periodic shortfall in salt availability. As a result, the companies have to travel longer distances to procure salt, making this key raw material more expensive. Further, incremental salt mines are not being allocated by the government, restricting entry of new players in the industry.

- **Limestone**: In the case of limestone, no fresh mining leases have been allotted to the industry in the last many years due to the tough mining regulations imposed by the government. This has forced companies to import a sizable portion of this basic raw material from West Asia which has led to increase in cost of limestone. However, many companies prefer certain amount of imports despite higher prices mainly because of:
  - Higher efficiency by using imported limestone
  - Saves logistics cost
  - It helps control domestic prices
  - Less grinding hours required for imported limestone (saves time as well as cost)

These are the reasons why new players are not able to enter the market. Moreover, due to these challenges, existing players in the industry are going slow on capacity expansion. Even one of the largest soda ash players, Tata Chemicals has not announced capacity expansion in the domestic market. However, GHCL, having highest margins in the soda ash segment is going for brownfield capacity expansion mainly due to higher captive raw material availability. Thus, the expansion will help the company expand its market presence in the soda ash segment.

Exhibit 63: Expansion plans of domestic soda ash players

Company name	Category	Capacity	Commissioning
GHCL Ltd	Brownfield	1,00,000	2016-17
Nirma Ltd	Brownfield	2,00,000	2016-17
RSPL	Greenfield	5,00,000	2019-20

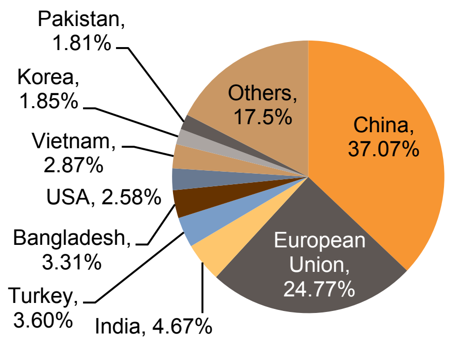
Source: Industry, Emkay Research

Textiles segment benefiting from increasing export opportunities

As per the data published by WTO, the global Textile and Clothing trade has reached US$ 766 bn in CY2013.This implies 10% CAGR increase from the 2009 level. Of this overall trade, Clothing or Apparel trade was close to US$ 460 bn, while the balance was on account of textile trade, which was US$ 306 bn.

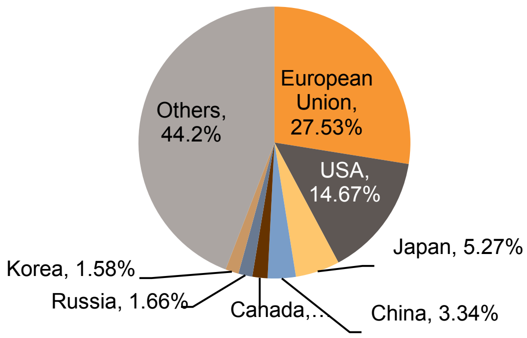
Indian Textiles Industry has emerged as a significant source for the global market during the last five years. India along with China, is amongst the major exporters while developed economies such as US and Europe continue to be the major importers.

Exhibit 64: Textile & Apparel Exporters



Source: Industry, Emkay Research

Exhibit 65: Textile & Apparel Importers



Source: Industry, Emkay Research

Increasing competitive position of India's textile sector

The competitive position of India's textile sector has been gradually improving over the last few years, given that its key competitors namely China and Pakistan are facing several issues:

Exhibit 66: India's competitive advantage in Textiles market

India	China	Pakistan
Largest producer and 2nd largest exporter of cotton	Major importer of cotton and yarn	Cotton Importer
Exporter of yarn	Yuan appreciation	Energy issues
Competitive costs	Wage inflation	Geopolitical issues
Robust ecosystem for textiles	Rising power costs	Compliance issues
Democracy with stable government	Stricter environmental compliance	
Better environmental and labor law compliance	Focus on domestic consumption	
	Yarn capacity closures	

Source: Industry, Emkay Research

India is having strong presence in the global Home Textiles market

Based on the industry estimates, the global home textiles market is estimated at $45 billion, wherein the major consuming places are US and Europe, each accounting for about one-third of the world's total demand. The segment includes towels, bed sheets, top of the beds, curtains, pillow cases, rugs, carpets etc used for home furnishings. India, along with China and Pakistan, are the biggest exporters, together constituting more than 50% of world trade.

The share of India in total home textile trade is 11%, which is more than double its share in textiles. Further, the share of "cotton" Home Textiles is even higher and better than China in many products. As per the data released by Office of Textiles and Apparels, India's share of exports of cotton bed sheets to the US has grown from just 27% in 2009 to almost 50% currently.

Key Financials (Consolidated)

Income Statement

Y/E Mar (Rs mn)	FY14	FY15	FY16	FY17E	FY18E
Net Sales	**22,343**	**23,616**	**25,458**	**26,302**	**28,673**
Expenditure	**18,106**	**18,408**	**19,256**	**19,698**	**21,078**
EBITDA	**4,370**	**5,328**	**6,334**	**6,734**	**7,725**
Depreciation	817	849	817	868	1,063
EBIT	**3,553**	**4,479**	**5,516**	**5,866**	**6,663**
Other Income	50	113	40	58	58
Interest expenses	1,832	1,704	1,644	1,497	1,214
PBT	**1,771**	**2,887**	**3,912**	**4,428**	**5,507**
Tax	340	749	1,226	1,373	1,707
Extraordinary Items	(346)	(319)	(109)	0	0
Minority Int./Income from Assoc.	0	0	0	0	0
Reported Net Income	**1,085**	**1,819**	**2,576**	**3,055**	**3,800**
Adjusted PAT	**1,431**	**2,138**	**2,685**	**3,055**	**3,800**

Balance Sheet

Y/E Mar (Rs mn)	FY14	FY15	FY16	FY17E	FY18E
Equity share capital	1,000	1,000	1,000	1,000	1,000
Reserves & surplus	4,873	6,701	8,857	11,288	14,313
Net worth	**5,873**	**7,702**	**9,857**	**12,288**	**15,313**
Minority Interest	**0**	**0**	**0**	**0**	**0**
Loan Funds	**13,979**	**12,464**	**11,769**	**11,469**	**8,969**
Net deferred tax liability	1,620	1,727	1,951	1,951	1,951
Total Liabilities	**21,472**	**21,893**	**23,576**	**25,708**	**26,233**
Net block	**18,694**	**19,339**	**20,861**	**23,243**	**22,981**
Investment	**75**	**15**	**15**	**15**	**15**
Current Assets	**11,247**	**9,090**	**8,630**	**8,849**	**9,961**
Cash & bank balance	417	339	427	211	971
Other Current Assets	1,579	1,433	1,247	1,031	1,031
Current liabilities & Provision	**8,668**	**6,622**	**5,930**	**6,399**	**6,724**
Net current assets	**2,579**	**2,468**	**2,700**	**2,450**	**3,237**
Misc. exp	0	0	0	0	0
Total Assets	**21,472**	**21,893**	**23,576**	**25,708**	**26,233**

Cash Flow

Y/E Mar (Rs mn)	FY14	FY15	FY16	FY17E	FY18E
PBT (Ex-Other income) (NI+Dep)	**1,721**	**2,774**	**3,872**	**4,370**	**5,449**
Other Non-Cash items	(990)	(45)	(110)	0	0
Chg in working cap	398	140	80	34	(27)
Operating Cashflow	**3,438**	**4,673**	**5,077**	**5,396**	**5,991**
Capital expenditure	(565)	(1,440)	(2,269)	(3,250)	(800)
Free Cash Flow	**2,872**	**3,233**	**2,807**	**2,146**	**5,191**
Investments	(20)	59	0	0	0
Other Investing Cash Flow	0	0	0	0	0
Investing Cashflow	**(535)**	**(1,268)**	**(2,230)**	**(3,192)**	**(742)**
Equity Capital Raised	0	0	0	0	0
Loans Taken / (Repaid)	(710)	(1,515)	(695)	(300)	(2,500)
Dividend paid (incl tax)	(234)	(265)	(420)	(623)	(775)
Other Financing Cash Flow	0	0	0	0	0
Financing Cashflow	**(2,776)**	**(3,484)**	**(2,759)**	**(2,420)**	**(4,489)**
Net chg in cash	**126**	**(78)**	**88**	**(216)**	**760**
Opening cash position	291	417	339	427	211
Closing cash position	**417**	**339**	**427**	**211**	**971**

Key Ratios

Profitability (%)	FY14	FY15	FY16	FY17E	FY18E
EBITDA Margin	19.4	22.4	24.8	25.5	26.8
EBIT Margin	15.8	18.9	21.6	22.2	23.1
Effective Tax Rate	19.2	26.0	31.4	31.0	31.0
Net Margin	6.4	9.0	10.5	11.6	13.2
ROCE	16.6	21.2	24.4	24.0	25.9
ROE	24.8	31.5	30.6	27.6	27.5
RoIC	16.8	21.2	24.7	24.1	26.3

Per Share Data (Rs)	FY14	FY15	FY16	FY17E	FY18E
EPS	14.3	21.4	26.8	30.5	38.0
CEPS	22.5	29.9	35.0	39.2	48.6
BVPS	58.7	77.0	98.5	122.9	153.1
DPS	2.0	2.2	3.5	5.2	6.5

Valuations (x)	FY14	FY15	FY16	FY17E	FY18E
PER	11.9	8.0	6.4	5.6	4.5
P/CEPS	7.6	5.7	4.9	4.4	3.5
P/BV	2.9	2.2	1.7	1.4	1.1
EV / Sales	1.4	1.2	1.1	1.1	0.9
EV / EBITDA	7.0	5.5	4.5	4.2	3.2
Dividend Yield (%)	1.2	1.3	2.1	3.0	3.8

Gearing Ratio (x)	FY14	FY15	FY16	FY17E	FY18E
Net Debt/ Equity	2.3	1.6	1.2	0.9	0.5
Net Debt/EBIDTA	3.1	2.3	1.8	1.7	1.0
Working Cap Cycle (days)	35.1	32.7	32.4	30.9	28.7

Growth (%)	FY14	FY15	FY16	FY17E	FY18E
Revenue	(1.0)	5.7	7.8	3.3	9.0
EBITDA	5.2	21.9	18.9	6.3	14.7
EBIT	6.6	26.1	23.2	6.3	13.6
PAT	52.1	67.6	41.6	18.6	24.4

Quarterly (Rs mn)	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16
Revenue	6,410	5,869	6,567	6,651	6,504
EBITDA	1,565	1,508	1,500	1,542	1,748
EBITDA Margin (%)	**24.4**	**25.7**	**22.8**	**23.2**	**26.9**
PAT	498	613	512	663	790
EPS (Rs)	**12.8**	**15.8**	**13.2**	**17.1**	**20.3**

Shareholding Pattern (%)	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16
Promoters	18.4	18.4	18.4	18.5	18.5
FIIs	13.4	12.5	14.0	17.5	17.8
DIIs	6.4	6.5	6.6	5.4	5.5
Public and Others	61.9	62.6	61.1	58.6	58.2

Emkay Rating Distribution

BUY	Expected total return (%) (Stock price appreciation and dividend yield) of over 25% within the next 12-18 months.
ACCUMULATE	Expected total return (%) (Stock price appreciation and dividend yield) of over 10% within the next 12-18 months.
HOLD	Expected total return (%) (Stock price appreciation and dividend yield) of upto 10% within the next 12-18 months.
REDUCE	Expected total return (%) (Stock price depreciation) of upto (-) 10% within the next 12-18 months.
SELL	The stock is believed to underperform the broad market indices or its related universe within the next 12-18 months.

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