



Mayur Uniquoters Ltd

Independent Research - Equities

30 Aug 2010

For Private Circulation Only
Important disclosure on the last page

India's largest manufacturer of artificial / synthetic leather, Mayur Uniquoters is growing rapidly, expanding capacity, integrating backward. After making marquee names like Bata, Maruti, Hero Honda as its customers, it has now set its sights on global auto majors like BMW, Mercedes, GM, Ford & Chrysler. A bet on domestic consumption growth and domestic & global automobile growth, at 5x current year earnings, is worth playing.

DCF Value Rs.535

Current Price Rs.235

Potential 2.3x

The stock currently trades at 6.2 times and 4.4 times the estimated EPS for FY11 (Rs.38) and FY12 (Rs.53) respectively. We expect EPS to grow at 40% in each of the next two years. Our DCF value estimate comes to around Rs.535 (CoE & WACC at 15.8%). We estimate its RoCE and RoE to be maintained at 35-40%.

Key Data

Market Cap	Rs.1.27bn US\$27mn
Shares Outstanding	5.4mn
52 week High-Low	289 – 51
Avg Trading Vol	No. of shares
1 month	20,400
3 months	10,400
1 year	8,300
BSE Scrip Code	522249
BSE Group	S

Shareholding 30 Jun10 %

Promoters	74.96
Institutions	00.20
Others	24.84

Multiple Valuation FY11E

EV/ EBIT Market	3.6x
Cap/Sales	0.6x
P/E	6.2x

Products

Artificial / Synthetic Leather (PU/PVC-coated fabrics)

Key Investment Points

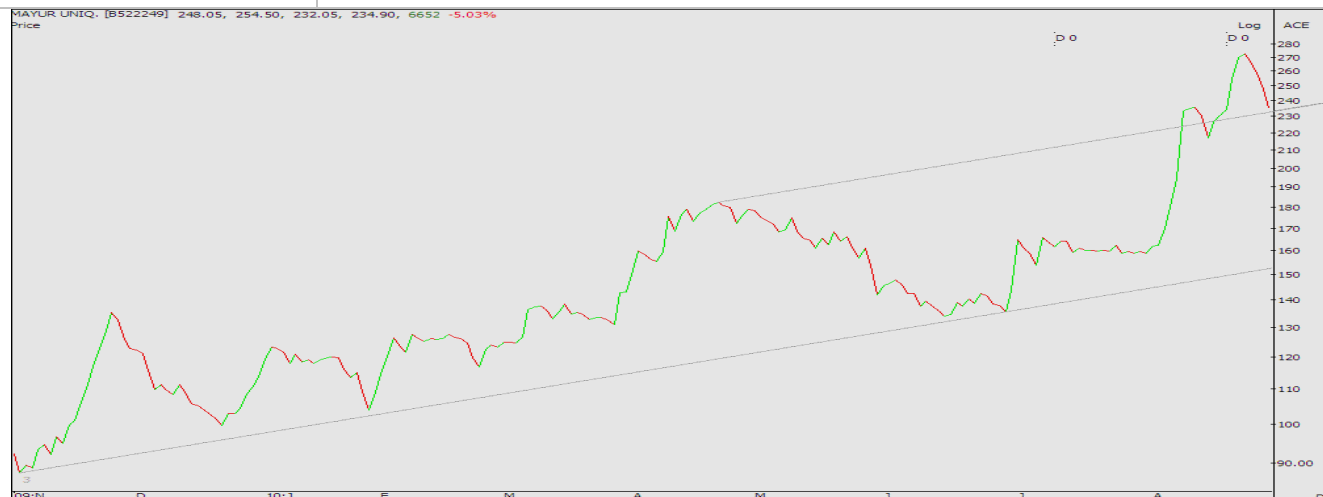
- The market leader in Synthetic Leather is way ahead of its competitors. It's twice as large as its nearest competitor.
- Continued strong growth in consumer spending and auto sector to drive growth. Footwear sector is the largest user sector followed by auto sector. Artificial leather also finds application in numerous fashion products.
- Proportion of high-value added high-margin products rising
- Marquee clients like Bata, Liberty, Maruti, Honda, M&M, Eicher
- Started supplying to US auto majors like Ford & Chrysler. To start supplies shortly to European auto majors like Mercedes Benz & BMW
- Sustained volume growth in US auto sector augurs well
- Operating at full capacity, expanding capacity gradually in phases
- Integrating backward into knitted fabric to ensure better quality inputs for high-quality products – to cause margin improvement
- Cash surplus company. The surplus to grow despite capex & backward integration.
- Extremely low Beta makes it a defensive bet

Value Kickers

- Successful scale up of supplies to global automotive OEMs

Points of Concern

- Rising input costs may impact margins in short term
- Depreciation of rupee vis-a-vis USD to impact margins in short term
- Production shut-downs for capacity expansion may impact performance in short term





Introduction

Mayur Uniquoters Ltd (Mayur) is India's largest manufacturer of synthetic / artificial leather with annual revenues of around Rs.1.86bn. Its plant is located near Jaipur. It coats/laminates various kinds of fabrics with PU/PVC to make synthetic leather. The product range includes single-side coated, both-side coated, coated on knitted fabric, coated on non-woven fabric, coated on synthetic fabric, coated on cotton fabric. The synthetic leather finds application in footwear, automobile seats, upholstery, furnishings, sports goods, apparel, ladies bags, and a plethora of fashion accessories. The products are customized to suit various applications. Synthetic leather is available in a very wide price range depending on application, inputs that goes into it, order size, etc. Mayur's average realizations in various product ranges mentioned above varies from Rs.120/meter to Rs.325/meter.

Investment Arguments

Domestic consumption surge helps Mayur's growth

Consumption growth in India has been outstanding over the last five years across product categories. We expect this consumptions surge to continue going forward driven by rising disposable income & improving standard of living.

Footwear sector is the largest user industry for Mayur's synthetic leather. Footwear is a large industry and continues to witness significant growth year after year. With ever increasing number of premium brands in footwear, demand for high margin premium synthetic leather is rising faster. It supplies to footwear makers like Bata, Action, and Liberty. Footwear makers in South India are major customers of Mayur. The beauty of this segment is that it is price insensitive as far as artificial leather is concerned, as artificial leather contributes very little to total footwear cost.

Auto replacement market is another significant market segment for the company. Unlike cyclicity of auto OEM market, the replacement market is a stable market and displays characteristics of a consumer market.

The whole gamut of fashion products including garments, bags, and furnishings are not only driving growth but also causing margin expansion, as these products require more customization and better quality.

Strong growth in domestic automobile sector

Domestic automobile sector, especially the passenger vehicles, continues to grow very strongly and have not shown much cyclicity. The strong auto sales growth continue to drive Mayur's sales growth. In automotive OEM space, Mayur supplies to companies like Maruti, Honda Motors, Hero Honda, Eicher Motors, and M&M. In this customer segment, it mainly supplies for low margin products for low end cars.

Market leader, way ahead of competition

Mayur is the largest producer of Synthetic Leather in India with revenues of Rs.1.76bn and capacity of 1.3mn meters per month (mpm). The second largest is half the size of Mayur. Others in this business are Fenoplast Hydearabd (capacity 600-700,000 mpm), Polynova Industries Goa, Manish Vinyl, Jasch Industries (Listed, FY10 Revenue Rs.540mn, EBIT Rs.26mn).

Mayur uses coating process to make Synthetic Leather. Many of its competitors use calendaring process. We understand that coating process is significantly better than calendaring process.



Mayur's source of competitiveness is its lower cost of production and ability to produce products to meet clients' application needs.

International Automobile Makers – huge untapped potential

Export was 9.5% of its total revenues in FY10. This was for miscellaneous usages. We expect proportion of exports in revenues to go up sharply over the next few years driven by sales to automobile OEMs. The company has lately started supplying to US auto majors (Ford & Chrysler) and is expected to supply to GM also. In Germany, Mercedes Benz has already approved its products. Approval process is on at BMW. The company expects to begin supplying to these European auto OEMs over the next six months. These are high quality products and carry significantly higher margin. We estimate margin/meter here to be more than its average realization/meter in FY10. These auto majors use artificial leather at places that are not body-touching. Sourcing from India is expected to be 15-20% cheaper for these companies. Mayur claims to be the first company from India to develop such products for these auto majors.

Besides auto OEMs, general exports would continue and grow to countries like Middle East, UK, Russia, Italy, Sri Lanka, and Bangladesh.

US Automobile sales shows sustainable improvement

US automobile sales have shown sustainable improvement. It was widely believed that growth in the US auto sector would taper off after the cash for clunker program. However, the growth continues unabated.

Following is the chart of seasonally-adjusted US Auto Sales. The spikes in Jul & Aug-09 are due to cash for clunkers program. It was being feared that C-for-C program would only pull the sales forward without any lasting impact. However, sales continue to grow 20% YoY despite the spiked-up sales in Jul-Aug09.



The buoyancy in the US Auto sector augurs well for Mayur's foray there in OEM space. We would like to emphasize here that while volume growth continues, the US OEMs are still looking for ways to cut costs to be competitive and strengthen their financials. Their efforts to source from India are aimed at cutting costs.



Marquee client set – an indicator of product quality & continued sales

Mayur has a marquee set of clients like Bata, Liberty, Action, Maruti, Hero Honda, Honda Motors, Eicher Motors, M&M, and now Chrysler & Ford. Shortly, it expects to start supply to GM, BMW and Mercedes Benz. This surely is an indicator of quality of its products and sustainability of its revenues, as these clients are large names with foreseeable revenues streams.

Expansion of manufacturing capacity

Mayur is currently operating at full capacity. It's currently producing 1.25-1.35mn mpm with capacity of 1.3mn mpm. It has three production lines and it is expanding all three lines' capacity by 100,000 mpm. This will take total capacity to 1.6mn mpm (up 23%). Capacity expansion at one of the lines was completed a few days back. Capex at other two lines are expected to be completed by Oct-10 and Dec-10. The company had to take 11 days shutdown of the line for the capex. Second line capex may also require a couple of weeks' shutdown. The third line's capex would require three weeks' shutdown. These shutdowns may impact the company's performance during such periods due to loss of production. Total capex of Rs.50-60mn is expected for this.

We expect the production to hit the expanded capacity of 1.6mn mpm by FY12/FY13. The company will need another round of capex before it hits capacity. We have built in suitable capex towards this in our model.

Backward integration into knitted fabrics

Mayur is integrating backward into manufacturing of synthetic knitted fabric. Knitted fabric is the largest input value-wise (15% of total input cost) after chemicals like PU, PVC, etc (60% of total input cost). The biggest advantage with backward integration would be availability of good quality knitted fabric. This would support production of high quality products. Land for this purpose has already been acquired about 15-20 km from existing plant site. This would entail a further capex of Rs.150mn.

Cash Surplus Company – to remain so despite capex and backward integration

Mayur had Rs.144mn (Rs.27/share) of surplus cash at the end of Mar10. We estimate the surplus to rise to Rs.412mn (Rs.76/share) at the end of Mar13 assuming dividend payout at current level of 15-20% of PAT and after considering planned & expected capex.

Very low beta stock

We calculated Mayur's beta against Sensex using data over multiple periods with both simple and log returns. The maximum beta amongst the all betas is 0.26. The low beta makes it an extremely defensive stock for portfolios. Yet, we chose to use beta of 1.0 for valuation to build in conservatism.

Risks / Concerns

Sharp rise in input costs

Key inputs for the company are PU, PVC, knitted & other fabrics, and release paper. PU, PVC, & synthetic fabric prices are a function of crude oil prices among others. There has been a sharp rise in input prices in QE Mar-10. This led to five percentage point margin contraction in the quarter. However, the impact on margins due to change in input costs are transient. The rise in costs is passed on to customers, though with a lag. The lag varies from one to three months for different segment of customers. Auto OEMs price is changed every quarter based on input prices in previous quarter. Input suppliers, however, change prices every fortnight. In response to rising input costs, Mayur took three product price increases of 5% each in Sep-09, Jan-10 and Apr-10. QE Jun10 saw 310bps contraction in material cost to sales ratio.



Therefore, rise in input costs is likely to impact margins in the interim. This may have a transitory impact on stock price performance.

Rupee depreciation vis-à-vis USD

Depreciation of rupee vis-à-vis USD is likely to have a transient adverse impact on it. It imports about 40% of its raw material while 90% of sales are in domestic market at present. Rupee depreciation increases material cost, which is passed on but with a lag as explained above.

Our view on INR/USD is that of rupee appreciation at least till 43.50. If our view plays out as it has been since Rs.51/USD, synthetic leather demand will get additional impetus as lower input costs are likely to be passed on.

Ownership & Management

The company is owned 75% by promoters – Poddars from Jaipur. There is negligible holding by institutional investors at present. Mr Suresh Poddar, Mr Manav Podar and Mr Arun Bagaria (all part of promoters) are executive directors of the company. Mr Suresh Poddar, a science graduate, started the company in 1992.

Valuation and key underlying assumptions

We estimate fair value per share to be around Rs.535 using the discounted free cash flows. Key assumptions for the valuation are 5% terminal growth rate in NOPLAT, 2% terminal ROIC spread over WACC, Cost of equity at 15.8% based on beta of one (though the calculated beta is mere 0.26), risk free rate of 7.8% and market risk premium of 8%.

At the current price of Rs.235, the stock trades at 8.7 times FY10 actual EPS of Rs.27. It trades at 6.2x and 4.4x expected EPS for FY11 (Rs.38) and FY12 (Rs.53) respectively. The company has no net debt and is cash positive. At our fair value of Rs.535, the stock will trade at 10x FY12 EPS and 8x FY13 EPS.



Financials

Income Statement

Rs. Mn.	FY10	FY11	FY12
Revenues	1,761	2,141	2,586
EBIT	245	321	442
PBT	255	323	450
PAT	146	205	287
EPS Rupees	27.06	37.90	53.09

Ratios

%	FY10	FY11	FY12
Revenue Gr%	43.1	21.5	20.8
EPS Growth %	51.0	40.1	40.1
RoE %	39.5	39.2	39.3
D/E x	0.1	-	-
Debtor days	53	53	53
L&A/Rev %	1.5	1.5	1.5
Creditors days	79	79	79

Balance Sheets

Rs. Mn.	31Mar10	31Mar11	31Mar12
Assets			
Net Block	231	302	452
Capital WIP	11	75	60
Net Curr. Assets	96	141	180
Surplus Funds	144	98	180
Liabilities			
Equity Capital	54	54	54
Reserves	366	534	777
Debt	44	-	-

Interim Performance

Rs. Mn.	Sep09	Dec09	Mar10	Jun10
Months	3	3	3	3
Revenues-Net	398	451	475	539
EBITDA	62	87	51	87
EBIT	55	81	45	81
PBT	55	82	52	82
PAT-Adjusted	33	51	35	55
Eq Capital	54	54	54	54
EPS Rs.	6.11	9.41	6.43	10.08
EBIT Margin %	13.9	18.0	9.6	15.0
Other income/PBT %	2.2	2.4	14.0	3.5
Tax/PBT %	39.9	37.6	31.6	34.1

Multiple Valuation

	FY10	FY11	FY12
EV/EBITDA x	3.5	2.7	2.0
EV/EBIT x	3.8	2.9	2.1
Mkt. Cap/Sales x	0.6	0.5	0.4
P/E x	7.2	5.1	3.7
Price/Book x	2.5	1.8	1.3

Free Cash Flow

Rs. Mn.	FY10	FY11	FY12
NOPLAT	152	204	282
Change in Net Working Capital	1	49	42
Operating Cash Flows	151	155	240
Net Capex & others	4	124	122
Free Cash Flow	147	31	118
Non-opr. Cash flow	21	4	5
Cash Flow to Investors	168	35	123

Financing Cash Flow

Rs. Mn.	FY10	FY11	FY12
Post-tax Interest	9	3	-
Repayment/ (issue) of Debt	34	44	-
Equity Share Dividend	25	34	40
Inc / (Dec) in surplus cash/Investments	100	(46)	83
Financing Cash Flow	168	35	123

DCF Valuation

Key Assumptions	%
Terminal Growth Rate	5.0
WACC	15.8
Cost of Equity	15.8
Terminal ROIC	17.8
Outcome	Rs.
Fair Value Per Share (Rs.)	535



Important Disclosure

This material has been prepared by Impetus Advisors, Mumbai, India.

The views expressed herein correctly reflect Impetus Advisors' views. Owners, analysts, and/or employees of Impetus Advisors hold long position in the stock mentioned in this report.

This document is not for public distribution and has been furnished to you solely for your information and may not be reproduced or redistributed to any other person. Persons into whose possession this document may come are required to inform themselves of, and to observe such restrictions.

This material is for the personal information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. No person associated with Impetus Advisors is authorized to call or initiate contact with you for the purposes of elaborating or following up on the information contained in this document. The material is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon as such.

Neither Impetus Advisors, nor any person connected with it, accepts any liability arising from the use of this document. The recipient of this material should rely on their own investigations and take their own professional advice. Opinions expressed are our current opinions as of the date appearing on this material only. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice.

No part of this material may be duplicated in any form and/or redistributed without Impetus Advisor's prior written consent.

About Impetus Advisors

Impetus Advisors, based at Mumbai, is an independent business & investment research firm, which specializes in identifying multi-bagger stock ideas among Indian equities. It provides equity research to high net-worth, proprietary, and institutional investors. It also provides research on forex and commodities to business firms and investors.

Besides its own stock picks, Impetus Advisors also provides customized investment research outsourcing services to stock brokers, investment bankers, business firms, and investors. As an independent research outfit, it is into neither broking nor investment banking nor any other activity that can potentially conflict with objectivity of its research.

Office:

A-604 Oberoi Woods | Oberoi Garden City | Off Western Express Highway | Goregaon-E | Mumbai.

Telefax 91 22 28405766 | Email research@impetusadvisors.com

Websites: www.impetusadvisors.com | www.independentresearch.in
