

Monte Carlo Fashions

IPO Note – Subscribe from a two-year perspective

Monte Carlo Fashions Ltd. (MCFL) is one of the leading apparel brands in India which primarily caters to the premium and mid-premium branded apparel segment for men, women and kids. The company offers a comprehensive line of woollen, cotton and cotton-blended knitted and woven apparel and home furnishings under the 'Monte Carlo' brand.

Well established brand and distribution network: Monte Carlo is the flagship brand of the company which is a market leader in the woollen knitted apparel industry in India and has been recognized as a 'Superbrand' for woollen knitted apparel in each edition of Consumer Superbrands India since its first edition in September 2004. Monte Carlo enjoys significant premium and brand recall on a pan India basis. The company took the task of creating brand in a market largely dominated by unbranded products and is reaping rewards as well. Also, it has a strong distribution network comprising of 196 'Monte Carlo Exclusive Brand Outlets' and over 1,300 Multi Brand Outlet (MBOs) through which its products are sold.

Asset light business model; healthy balance sheet coupled with decent return ratios: The company has an asset light business model as it operates largely through the franchise network (178 franchise outlets as compared to 18 outlets owned by the company). Also, it outsources the manufacturing of cotton apparel, woollen woven apparel and home furnishing products to a network of job work entities. As a result, it has a low Debt/Equity (D/E) of ~0.2x and has the lowest employee cost as a percentage of sales in the industry. Further, the company has decent return ratios with ROE and ROCE of 14.6% and 16.6%, respectively (in FY2014).

Outlook and Valuation: The company's net sales have grown at a CAGR of 16.3% over FY2012 to FY2014. Although, the EBITDA margins have declined from 22% in FY2012 to 18.7% in FY2014, we believe they are at sustainable levels. The net profit has grown at a CAGR of 5.8% over FY2012-FY2014. At the lower end of the price band, the stock is valued at ~24.8x PE on FY2014 earnings which we believe is fair considering its i) strong brand image, ii) strong distribution network, iii) healthy balance sheet and iv) widening product portfolio.

We recommend Subscribe to the issue at the lower end of the price band from a two-year perspective. From a one-year perspective, we see limited upside potential as valuations seem to be fair.

Key Financials

Y/E March (₹ cr)	FY2012	FY2013	FY2014
Net Sales	372	404	504
% chg	-	8.7	24.5
Net Profit	49	50	55
% chg	0	1.2	10.6
EBITDA (%)	22.0	17.5	18.7
EPS (₹)	22.7	23.0	25.4
P/E (x)*	27.7	27.4	24.8
P/BV (x)*	19.7	9.2	7.8
RoE (%)	32.8	15.4	14.6
RoCE (%)	35.7	16.4	16.6
EV/Sales (x)*	3.8	3.2	2.6
EV/EBITDA (x)*	17.5	18.2	14.1

Source: Company, Angel Research; Note: *The above numbers are considering subscription at the lower end of the price band

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Issue Open: December 3, 2014
 Issue Close: December 5, 2014

Issue Details

Face Value: ₹10

Present Eq. Paid up Capital: ₹21.73cr

Offer Size: 0.54cr Shares

Post Eq. Paid up Capital: ₹21.73cr

Issue size (amount)**: ₹342cr - ₹350cr

Price Band**: ₹630-645

Post-issue implied mkt. cap**: ₹342cr-350cr

Promoters holding Pre-Issue: 81.06%

Promoters holding Post-Issue: 63.63%

Note:**at Lower and Upper price band respectively

Book Building

QIBs	At least 50%
Non-Institutional	At least 15%
Retail	At least 35%

Post Issue Shareholding Pattern

Promoters Group	63.63
MF/Banks/Indian FIs/FIIs/Public & Others	36.37

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Company Background

Monte Carlo Fashions Ltd. (MCFL) is a leading apparel brand in India. It was launched in 1984 as an exclusive woollen brand by Oswal Woollen Mills Ltd ('OWML'), one of its group companies. The company primarily caters to the premium and mid-premium branded apparel segment for men, women and kids, offering a comprehensive line of woollen, cotton and cotton-blended knitted and woven apparel and home furnishings through its '*Monte Carlo Exclusive Brand Outlets*' and MBOs, including a network of national chain stores under the '*Monte Carlo*' brand.

MCFL has introduced different ranges for different segments in the apparel industry under the umbrella '*Monte Carlo*' brand. '*Platine*' is its premium range for men, '*Denim*' is the exclusive range for denim apparel, '*Alpha*' is the exclusive range for women and '*Tweens*' is the exclusive range for kids. The company continues to broaden its product range including premium and economy cotton knitted and woven apparel products to appeal to a diversified customer base across India. The woollen products include sweaters and cardigans, whereas, cotton knitted garments include t-shirts and track suits. The woven garments portfolio includes shirts, trousers, suits, jackets and denims.

It has two manufacturing facilities in Ludhiana, Punjab, one for woollen apparel products and one for cotton apparel products. The manufacturing facilities include facilities for product development, a design studio and sampling infrastructure. Almost all woollen knitted products are manufactured in-house at its manufacturing facility. Also, it recently commenced in-house manufacturing of some of its cotton t-shirts and thermals in April 2014. For the remaining cotton and cotton-blended products, the company follows an asset-light model by outsourcing the production to a network of third-party manufacturers, also known as job work entities.

Issue Details

The issue comprises an offer for sale by promoters group and private equity (PE) firm Samara Capital of 0.54cr equity shares of face value of ₹10 each. There is no fresh issue of equity. MCFL has fixed the price band of the issue at ₹630 to ₹645. The offer constitutes 25% of the post offer paid-up equity share capital of the company.

Exhibit 1: Share Holding pattern

Particulars	Pre-Issue		Post-Issue	
	No. of shares	(%)	No. of shares	(%)
Promoter and promoter group	1,76,15,304	81.1%	1,38,28,708	63.6%
Total public holding	41,16,760	18.9%	79,03,356	36.4%
Total	2,17,32,064	100.0%	2,17,32,064	100.0%

Source: Company, Angel Research

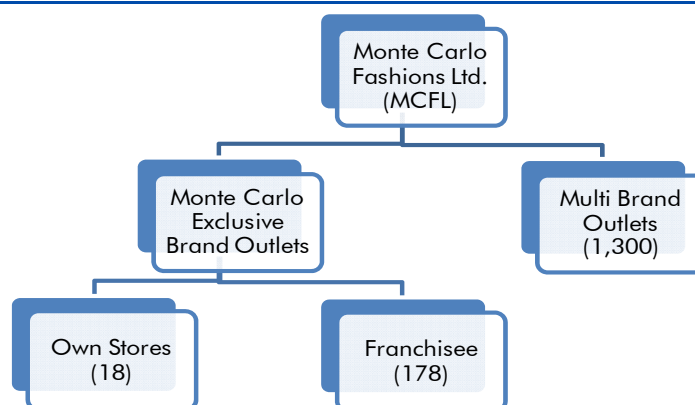
Objects of the Offer

The objects of the offer are to achieve the benefits of listing the equity shares on the stock exchanges and the sale of 5,433,016 equity shares by the Selling Shareholders. Further, the company expects that the listing of the equity shares will enhance its visibility and brand image among its existing and potential customers and provide liquidity to the existing shareholders. The company will not receive any proceeds of the offer and all the proceeds will go to the Selling Shareholders.

Investment Arguments

Well established brand to compliment network expansion: Monte Carlo is the flagship brand of the company with a portfolio of woollen apparel and cotton and cotton blended apparel. They are the leading woollen knitted apparel brand in India in the premium and mid-premium segment and enjoy significant premium and brand recall on a pan India basis. Monte Carlo brand has been built through advertising in print media, electronic advertising, television campaigns, fashion shows and through endorsement by famous Indian personalities (*Bipasha Basu*) and strategic associations with movies (*Barfi*, *Bhaag Milkha Bhaag*).

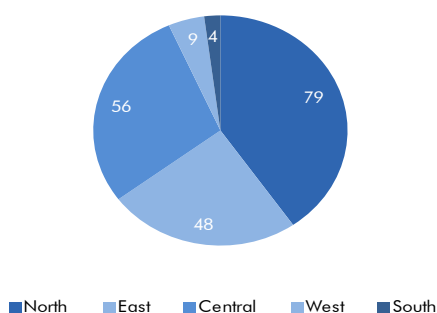
Exhibit 2: Products distribution model



Source: Company, Angel Research

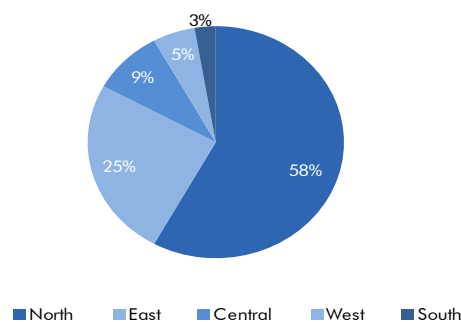
The company distributes its portfolio of products through 'Monte Carlo Exclusive Brand Outlets' and MBOs. As on June 30, 2014 there are 196 'Monte Carlo Exclusive Brand Outlets' in India, two in Dubai and one in Kathmandu, Nepal. The company plans to increase the outlets to 275 by fiscal FY2017 as a part of its growth strategy. While most of the outlets would be opened in North and Eastern India, the company would seek to penetrate further in the western and southern regions of India as well. Further, its products are supplied to over 1,300 MBOs (as of June, 2014) through its commissioned agents. Demographic and economic trends currently favour a fast growth of the organized branded industry. Moreover, MCFL has brands positioned to cater to different classes of customers. The company has also entered into distribution agreements with some of the leading Indian digital commerce platforms which would further aid growth.

Exhibit 3: Region wise Exclusive Brand Outlets



Source: Company, Angel Research

Exhibit 4: Region wise revenue contribution (FY2014)



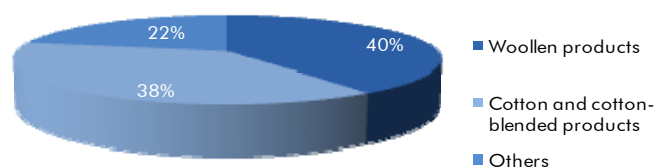
Source: Company, Angel Research

Asset light model to ensure healthy balance sheet going ahead: The company manufactures woollen knitted products and some of its cotton t-shirts and thermals at its own manufacturing facilities. For woollen woven apparel, cotton & cotton-blended products and home furnishing products, the company follows an asset light model by outsourcing the production to a network of third-party manufacturers, also known as job work entities with which it enjoys a long term relationship. The company sells the raw materials which include fabrics and/or yarns to the job worker entities who further sell the finished products back to the company. The company has 196 'Monte Carlo Exclusive Brand Outlets', of which 178 are owned and operated by different franchisees in India (including 21 discount stores or factory outlets). The franchisees lease the locations where they operate and staff costs and other operating expenses are borne by the franchisees. As a result, the company's employee cost as a percentage of sales is one of the lowest in the industry and its D/E is low at ~0.2x. Further it has around ₹175cr in cash and that has been set aside for future acquisitions which will ensure that balance sheet continues to be healthy.

Broadening of product portfolio to address seasonality concerns: The 'Monte Carlo' brand has historically been associated with winter-wear for its woollen knitted apparel. In order to position 'Monte Carlo' as an all-season pan-Indian brand, the company introduced cotton and cotton-blended apparel to the 'Monte Carlo' portfolio of products in 2006. The company is expanding its product range in the cotton and cotton-blended apparel segments and focusing on the production of cotton and cotton-blended shirts, trousers, t-shirts and denims to expand the all-season product range and increase penetration in the metros and expand presence in tier I and tier II cities in India.

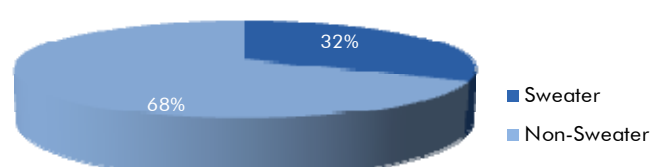
The portfolio of products under 'Monte Carlo' has primarily catered to the premium and mid-premium segments. The company recently launched an economy range 'Cloak & Decker' of cotton apparel products under the 'Monte Carlo' brand. It has also entered the high growth kids apparel segment under 'Tweens' range and has become a one-stop shop for the entire family. Further, it has entered into the niche home furnishing category with the product portfolio including mink blankets, bed sheets and quilts. Additionally, it sells thermal wear and other winter accessories including scarves, mufflers and woollen caps.

Exhibit 5: Revenue break-up products wise



Source: Company, Angel Research

Exhibit 6: Sweater and non-sweater break-up



Source: Company, Angel Research

Exploiting additional opportunity through acquisitions and focus on expansion of kids wear: The Management has guided at utilizing the available cash for inorganic acquisitions or strategic investments. The company is looking at opportunities in areas in which it is not present, ie in shoes, ethnic wears, suiting and women's western wear. The company also aims to increase production and supply of apparel products in the 'Tweens' range and also launch a dedicated marketing and branding exercise for kids wear products. The branded kids wear segment in India is under-penetrated and offers a compelling opportunity for growth. According to the Technopak Report, 2014, the kids apparel market contributes 20% to the total fashion market and is the fastest growing segment in the Indian market. The US\$8,222mn kids apparel market in India is expected to grow at a CAGR of 10.50% to reach US\$22,369mn in 2023. Branded kids' wear retail in itself is a high growth opportunity area as the market is dominated by local and unorganized players. The absence of a significant player in the mid-tier segment presents a huge prospect.

Industry Overview

According to the Technopak Report, 2014, the Indian branded apparel industry is estimated to be approximately US\$13,131mn in 2015 and is projected to grow to US\$34,182mn by fiscal 2020, driven by an increase in per capita income and increased penetration of organized retail across India. Though organized retail accounted for only 17% of the total apparel market in 2010, and is estimated to account for 25% of the total apparel market by the year 2015, its share is poised to grow sharply over the coming years and account for ~40% share of the total apparel market by 2020. The increased presence of multiple retail formats across speciality retail formats, hypermarkets and cash and carry is expected to drive this growth.

According to the Technopak Report, 2014, the current size of India's winter wear market is approximately US\$2,341mn and is growing at a CAGR of 9%. Between men, women and kids segment, men contribute as high as 51% of the entire segment. Most segments in winter wear, such as shawls, men's suits, jackets, blazers and sweaters are registering a double digit growth. Hence, winter wear is seen as a lucrative business proposition, despite facing various issues like infrastructure and labor costs to name a few. In India, the winter wear market is clearly segmented between branded and unbranded players. The ratio is 70:30 with 70% players being from the unbranded sector. The share of branded wool industry is about 12% of the total industry.

Outlook and Valuation

The company's net sales have grown at a CAGR of 16.3% over FY2012 to FY2014. Although, the EBIDTA margins have declined from 22% in FY2012 to 18.7% in FY2014, we believe they are at sustainable levels. The net profit has grown at a CAGR of 5.8% over FY2012-FY2014. At the lower end of the price band, the stock is valued at ~24.8x PE on FY2014 earnings which we believe is fair considering its i) strong brand image, ii) strong distribution network, iii) healthy balance sheet and iv) widening product portfolio. **We recommend Subscribe to the issue at the lower end of the price band from a two-year perspective. From a one-year perspective, we see limited upside potential as valuations seem to be fair.**

Key risks/concerns

Fluctuations in the prices of woollen yarn and cotton fabric: The company is exposed to fluctuations in the prices of woollen yarn and cotton fabric as well as its unavailability, as it does not enter into any supply agreements and purchases them from spot market.

High proportion of related party transactions: The company relies on certain group companies, including OWML and Nahar Spinning Mills Limited, for procurement of raw materials and outsourcing the manufacture of certain apparel. Hence any potential conflicts of interest pursuant to such related party transactions could have a material adverse effect on its business, financial condition and results of operations.

Credit risk of franchisees and MBOs: The company is exposed to payment delays and/or defaults by its franchisees who operate the company's 'Monte Carlo Exclusive Brand Outlets' and MBOs. MCFLs financial position and profitability therefore depend on the credit-worthiness of its franchisees and MBOs. In the past, for example, certain franchisees did not pay sales proceeds due to it, resulting in the termination of arrangements with such franchisees and to the closure of the exclusive brand outlets that they operated.

Profit & Loss (Standalone)

Y/E March (₹ cr)	FY2012	FY2013	FY2014
Gross sales	399	424	504
Less: Excise duty	26	20	0
Net Sales	372	404	504
% chg	0.0	13.3	25.8
Net Raw Materials	183	207	261
% chg	0.0	13.3	25.8
Power	5	6	8
% chg	-	15.2	45.9
Other Mfg costs	30	33	41
% chg	-	10.2	25.8
Personnel	14	19	27
% chg	-	37.6	43.0
Other	6	6	7
% chg	-	2.5	27.1
Total Expenditure	290	333	410
EBITDA	82	71	94
% chg	-	(13.3)	32.7
(% of Net Sales)	22.0	17.5	18.7
Depreciation & Amortisation	6	7	16
EBIT	76	64	78
% chg	-	(15.5)	21.5
(% of Net Sales)	20.4	15.9	15.5
Interest & other Charges	7	4	9
Other Income	3	12	15
(% of Net Sales)	0.9	3.0	3.0
PBT	73	72	84
Tax	23	22	28
(% of PBT)	31.9	31.0	34.0
PAT (reported)	49	50	55
Extraordinary Expense/(Inc.)	0	0	0
ADJ. PAT	49	50	55
% chg	-	1.2	10.6
(% of Net Sales)	13.3	12.4	11.0
Basic EPS (₹)	22.7	23.0	25.4
Fully Diluted EPS (₹)	22.7	23.0	25.4
% chg	-	1.2	10.6

Balance sheet (Standalone)

Y/E March (₹ cr)	FY2012	FY2013	FY2014
SOURCES OF FUNDS			
Equity Share Capital	19	22	22
Reserves & Surplus	132	303	358
Shareholders' Funds	151	325	380
Total Loans	62	67	89
Long term Provision	0	0	0
Other long term liabilities	6	8	9
Net Deferred Tax Liability	0	1	3
Total Liabilities	219	400	482
APPLICATION OF FUNDS			
Gross Block	100	163	241
Less: Acc. Depreciation	51	58	74
Net Block	49	105	167
Capital Work-in-Progress	19	23	20
Lease adjustment	0	0	0
Goodwill	0	0	0
Investments	0	40	50
Long term loans and adv.	17	13	12
Other non-current assets	0	0	45
Current Assets	191	305	331
Cash	1	107	82
Loans & Advances	7	13	17
Inventory	110	109	140
Debtor	72	74	89
Other current assets	0	1	3
Current liabilities	57	86	143
Net Current Assets	134	219	188
Misc. Exp. not written off	0	0	0
Total Assets	219	400	482

Cash flow statement (Standalone)

Y/E March (₹ cr)	FY2012	FY2013	FY2014
Profit Before Tax	73	72	84
Depreciation	6	7	16
Other Income	(3)	(12)	(15)
Change in Working Capital	-	21	6
Direct taxes paid	(23)	(22)	(28)
Cash Flow from Operations	52	65	63
(Incr)/ Decr in Fixed Assets	-	(60)	(35)
(Incr)/Decr In Investments	-	(44)	(11)
Other Income	-	12	15
Cash Flow from Investing	-	(91)	(32)
Issue of Equity/Preference	-	-	-
Incr/(Decr) in Debt	-	7	27
Dividend Paid (Incl. Tax)	-	-	-
Others	-	139	(29)
Cash Flow from Financing	-	(131)	56
Incr/(Decr) In Cash	52	106	(25)
Opening cash balance	-	1	107
Closing cash balance	-	107	82

Key Ratios

Y/E March	FY2012	FY2013	FY2014
Valuation Ratio (x)*			
P/E (on FDEPS)	27.7	27.4	24.8
P/CEPS	27.0	8.7	10.0
P/BV	19.7	9.2	7.8
Dividend yield (%)	-	-	-
EV/Net sales	3.8	3.2	2.6
EV/EBITDA	17.5	18.2	14.1
EV / Total Assets	6.5	3.2	2.8
Per Share Data (₹)			
EPS (Basic)	22.7	23.0	25.4
EPS (fully diluted)	22.7	23.0	25.4
Cash EPS	23.3	72.3	63.2
DPS	-	-	-
Book Value	69.4	149.4	174.8
DuPont Analysis			
EBIT margin	20.4	15.9	15.5
Tax retention ratio	0.7	0.7	0.7
Asset turnover (x)	1.9	1.8	1.5
ROIC (Post-tax)	26.1	19.2	15.6
Cost of Debt (Post Tax)	7.2	3.8	6.9
Leverage (x)	0.4	(0.2)	(0.1)
Operating ROE	33.6	15.4	14.6
Returns (%)			
ROCE (Pre-tax)	35.7	16.4	16.6
Angel ROIC (Pre-tax)	38.3	27.8	23.6
ROE	32.8	15.4	14.6
Turnover ratios (x)			
Asset TO (Gross Block)	3.7	2.5	2.1
Inventory / Net sales (days)	108	99	90
Receivables (days)	71	66	59
Payables (days)	17	27	37
WC cycle (ex-cash) (days)	130	141	115
Solvency ratios (x)			
Net debt to equity	0.4	(0.2)	(0.1)
Net debt to EBITDA	0.7	(1.1)	(0.5)
Int. Coverage (EBIT/ Int.)	11.6	17.4	8.4

Note: *Valuation Ratio at the lower price band

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Disclosure of Interest Statement	Monte Carlo
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹1 lakh for Angel, its Group companies and Directors

Ratings (Returns):	Buy (> 15%) Reduce (-5% to -15%)	Accumulate (5% to 15%) Sell (< -15%)	Neutral (-5 to 5%)
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