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Q3FY21 result review and
earnings revision

Consumer Staples & Discretionary

Target price Rs2,500

Earnings revision

(%)	FY21E	FY22E
Sales	↑ 8.8	↑ 2.0
EBITDA	↑ 23.1	↑ 4.1
PAT	↑ 30.5	↑ 8.4

Target price revision

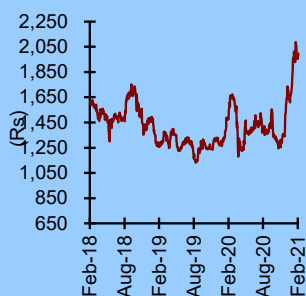
Rs2,500 from Rs2,300

Shareholding pattern

	Jun '20	Sep '20	Dec '20
Promoters	75.0	73.0	73.0
Institutional investors			
MFs and other	23.0	24.9	24.8
Banks, FI's, Insurance co	19.7	22.6	22.8
FIs	0.1	0.7	0.3
Others	3.2	1.7	1.7
	2.0	2.1	2.2

Source: BSE

Price chart



Research Analysts:

Manoj Menon

manoj.menon@icicisecurities.com
+91 22 6637 7209

Vismaya Agarwal, CFA

vismaya.agarwal@icicisecurities.com
+91 22 2277 7632

Karan Bhuwania

karan.bhuwania@icicisecurities.com
+91 22 6637 7351

Sheela Foam

BUY
Maintain

Robust recovery; long-term growth tailwind intact

Rs2,037

SFL's 3Q revenue grew 26%, a significant beat. We like (1) continued growth in branded mattress (+18%) and recovery in foam cores (+23%) and technical foam (+33%) in India, and (2) acceleration in growth in Australia and Spain subsidiaries (+35% and +100% respectively) – the best since IPO. Long-term growth opportunities are DCF-accretive and importantly embellish the narrative as well – (a) benefit from China+ strategy of buyers in US, Europe (grow exports from Spain and India – expect exports to cross Rs1bn in FY22), (b) opportunity in furniture cushioning and manufacturing (under SleepX brand), (c) sustained acceleration in India business growth (competitive edge through EBO network) and consumers realizing importance of good quality mattress. Price hikes in branded mattress and effective cost controls are likely to mitigate pressure from rising input costs. **Maintain BUY.**

- **Strong broad based performance:** Consolidated revenue / EBITDA / PAT grew 26% / 53% / 55%. This performance was broad based – branded mattresses (revenue +18%, volume +16%), foam core (+23%) and technical foam (+33%). However, furniture foam grew just 2% and home comfort recovered sequentially (+54%) but declined 26% YoY. Australia business revenue grew 35% YoY. Revenue from recently acquired Spain business doubled. Performance in B2C business was driven by some pent-up demand, change in consumer behavior towards better mattresses and industry formalization. The B2B business growth was driven by good traction in the auto sector.
- **Margin expansion despite steep input cost inflation:** Comparable gross margin declined 550bps to 43.5% due to input cost headwinds (TDI at Rs211/kg was up 64% YoY; Polyol at Rs216/kg was up 116% YoY). However, EBITDA margin expanded 310bps YoY to 17.4% driven by lower ad-spends, operating leverage and cost savings – lower employee costs (-110bps) and other expenses (-750bps). Australia and Spain business have EBITDA margins of 17.4% (+400bps YoY) and 18% (-200bps) respectively. We note that input costs have eased in Jan'21 – TDI at ~Rs170/kg and Polyol at ~Rs200/kg.
- **Valuation and risks:** We increase our FY22E earnings estimates by 8%; modelling revenue / EBITDA / PAT CAGR of 17% / 21% / 26% over FY20-23E. Maintain BUY with a DCF-based revised target price of Rs2,500 (was 2,300). At our target price, the stock will trade at 30x P/E multiple Mar-23E. Key downside risks are (1) adverse movement in prices of key inputs – TDI and polyol and (2) increase in competitive intensity from global players or Indian e-commerce.

Market Cap	Rs99bn/US\$1.4bn	Year to March	FY20	FY21E	FY22E	FY23E
Reuters/Bloomberg	SHVF.BO / SFL IN	Net Revenue (Rs mn)	21,736	23,755	31,100	34,980
Shares Outstanding (mn)	48.8	Net Profit (Rs mn)	2,063	2,485	3,243	4,114
52-week Range (Rs)	2344/1101	Dil. EPS (Rs)	42.3	50.9	66.5	84.3
Free Float (%)	27.0	% Chg YoY	54.2	20.5	30.5	26.8
FII (%)	1.7	P/E (x)	48.2	40.0	30.6	24.2
Daily Volume (US\$'000)	868	CEPS (Rs)	54.4	66.3	83.7	103.6
Absolute Return 3m (%)	61.3	EV/EBITDA (x)	32.0	25.3	21.2	17.9
Absolute Return 12m (%)	31.9	Dividend Yield (%)	0.0	0.0	0.1	0.1
Sensex Return 3m (%)	24.7	RoCE (%)	24.1	22.7	23.2	23.0
Sensex Return 12m (%)	25.6	RoE (%)	24.9	23.6	24.3	24.3

Table 1: Q3FY21 results review

(Rs mn)

	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Net Revenue	8,259	6,580	26	6,078	36	17,027	16,695	2
COGS	(4,664)	(3,356)	39	(3,108)	50	(9,206)	(8,505)	8
Gross profit	3,595	3,224	12	2,971	21	7,821	8,191	(5)
Staff cost	(645)	(586)	10	(583)	11	(1,681)	(1,693)	(1)
Other opex	(1,511)	(1,699)	(11)	(1,323)	14	(3,358)	(4,232)	(21)
Total opex	(2,156)	(2,285)	(6)	(1,907)	13	(5,039)	(5,925)	(15)
EBITDA	1,439	939	53	1,064	35	2,782	2,266	23
Other income	157	72	120	93	69	358	278	29
Finance Cost	(47)	(30)	58	(43)	10	(131)	(77)	70
D&A	(199)	(122)	63	(174)	14	(544)	(321)	70
PBT	1,351	859	57	941	44	2,465	2,147	15
Tax	(349)	(212)	65	(242)	44	(647)	(525)	23
Recurring PAT	1,001	647	55	698	43	1,818	1,622	12
EPS	20.5	13.3	55	14.3	43	37.3	33.2	12
Costs as a % of sales								
COGS	56.5	51.0	546 bps	51.1	534 bps	54.1	50.9	312 bps
Gross margin (%)	43.5	49.0	-547 bps	48.9	-535 bps	45.9	49.1	-313 bps
Staff cost	7.8	8.9	-111 bps	9.6	-179 bps	9.9	10.1	-28 bps
Other opex	18.3	25.8	-752 bps	21.8	-348 bps	19.7	25.3	-563 bps
EBITDA margin (%)	17.4	14.3	315 bps	17.5	-9 bps	16.3	13.6	276 bps
Income tax rate (%)	25.9	24.7	117 bps	25.7	10 bps	26.3	24.5	180 bps

Source: Company data, I-Sec research

Table 2: Q3FY21 segment results review

(Rs mn)

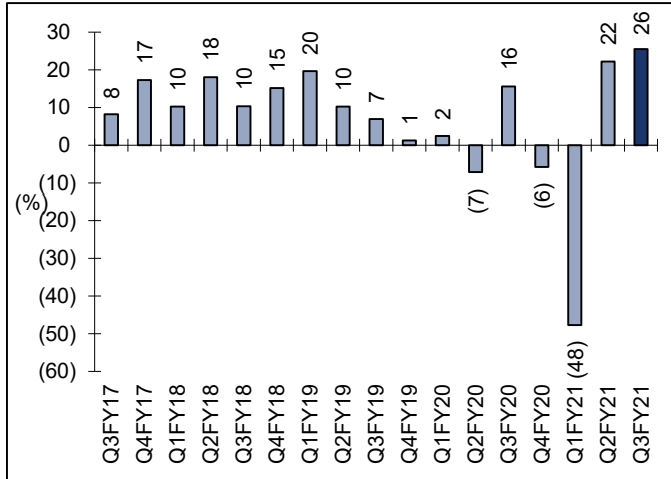
	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Segment Revenue								
Mattresses	2,846	2,410	18	1,840	55	5,356	6,086	(12)
Furniture Foam	802	790	2	680	18	1,652	2,094	(21)
Foam Core	1,058	860	23	780	36	2,068	2,314	(11)
Technical Foam	1,129	850	33	810	39	2,099	2,518	(17)
Home Comforts Products	200	270	(26)	130	54	370	631	(41)
Australia	1,210	897	35	1,040	16	3,069	2,550	20
Spain	1,000	500	100	820	22	2,420	500	
Segment Volume (Mattress in '000 Nos., others in Tons.)								
Mattresses	778	668	16	512	52	1,475	1,682	(12)
Furniture Foam	1,778	2,292	(22)	1,909	(7)	4,164	6,115	(32)
Foam Core	5,845	5,542	5	5,042	16	12,412	14,694	(16)
Technical Foam	3,412	3,034	12	2,918	17	6,913	8,985	(23)
Segment Realisation (Mattress in Rs/No., others in Rs/Kg)								
Mattresses	3,658	3,608	1	3,593	2	3,631	3,618	0
Furniture Foam	451	345	31	353	28	397	342	16
Foam Core	181	155	17	154	18	167	157	6
Technical Foam	331	280	18	278	19	304	280	8

Source: Company data, I-Sec research

Sheela Foam Q3FY21 call takeaways

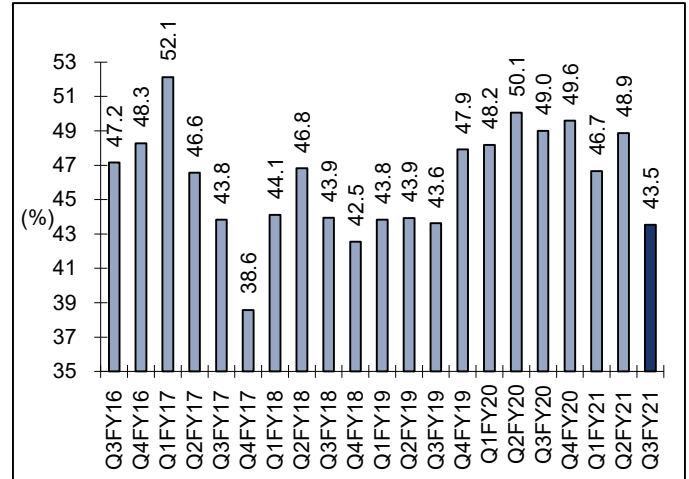
- **Consumer focus** is on health and channel preference is changing towards e-commerce.
- **Indirect benefits to SFL from the budget:** Affordable housing focus and increased allocation to railways means more business opportunity for Sheela Foam.
- **Raw material:** Fluctuating in the previous six months. Prices rose extremely high, but are reducing now. TDI is at Rs170/kg and Polyol at Rs200/kg. Management expects TDI to stabilize at Rs150-170 /kg levels by Feb-end. Contribution to input - 20% is Polyol and 30% is TDI; rest is spring and textile etc.
- **Ecommerce:** Reasonably present in e-commerce and are increasing presence. Segment is witnessing strong growth.
- **Exports:** Management estimates USD600mn opportunity for exports overall. This is primarily supplied by China as a bed in a box and buyers have been looking beyond China now. Competing with China and the Chinese manufacturers is tough but SFL has had many enquiries. In-fact, the company has been supplying to them (some from Spain, some from India). There are some challenges like shipping disruption and container availability which will go away soon. Next financial year, management expects exports will cross Rs1bn.
- **EBITDA margin:** Expect 17% to become the norm and hope to grow on this level.
- **Mattresses:** All three geographies have been a positive surprise. **Australia** – no travelling hence the consumer has greater disposable income, which led to higher purchases in household products and also China imports got restricted (sentimentally and even from government side). **Spain** – 1) Very small part of entire EU market, 2) mattresses market growth; **India** – benefitting from consumer shift from cotton to foam and from unorganized to organized market.
- **Decision on entry into Australia and Spain:** Each of the market entries had a different reason. Australia – developed market, learnings, raw material suppliers could be leveraged, Spain happened in 2019 – EU is the biggest market of PU foam in the world, SFL needed a foothold there, Spain subsidiary has only 1% share in EU, tech was similar between the two companies. Company is in a low cost area of Europe and now even exports business has opened up.
- **Demand improvement:** B2C – Driven by - 1) pent-up demand, 2) change in consumer behavior with consumers preferring good mattresses (when a category becomes importance, the largest player benefits the most), 3) industry formalization. B2B – experiencing good traction in auto where SFL has high market share.
- **ASP growth:** ASP grew as SFL did not pass the entire cost to the customers and it is also a function of product mix.
- **Pricing:** B2B - selling inputs to the other manufacturers in most cases, pricing is related to the input cost but in B2C, effort is to add value and charge for this value.
- **Channel:** EBO is more than 5000 outlets with a combination of display format and exclusive outlets. Sleepwell brand is only sold at exclusive outlets.

Chart 1: Revenue growth (consolidated)



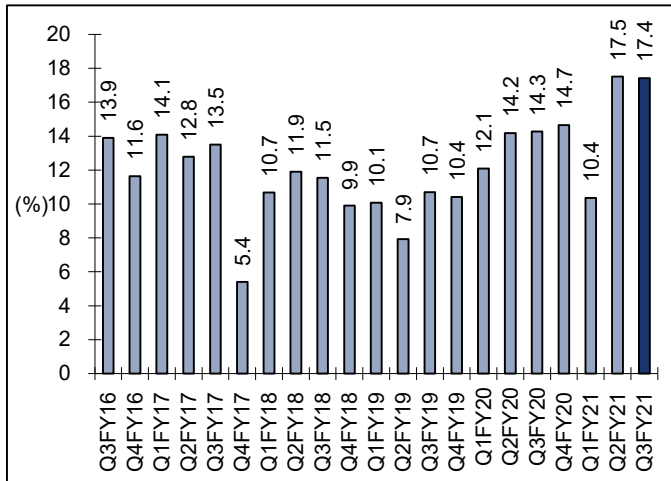
Source: Company data, I-Sec research

Chart 2: Gross margin (consolidated)



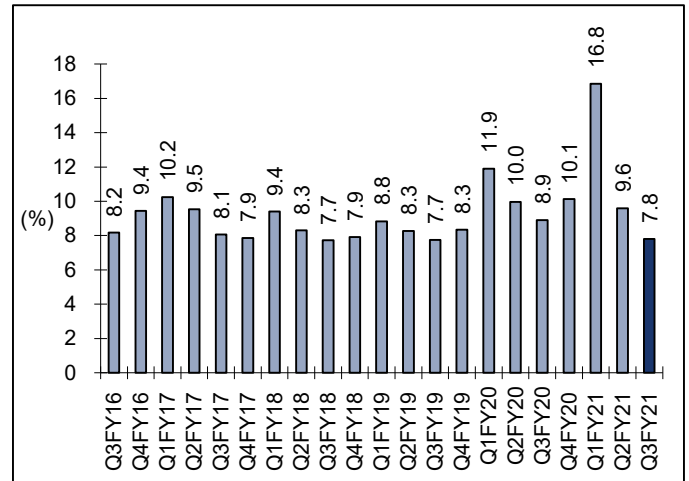
Source: Company data, I-Sec research

Chart 3: EBITDA margin (consolidated)



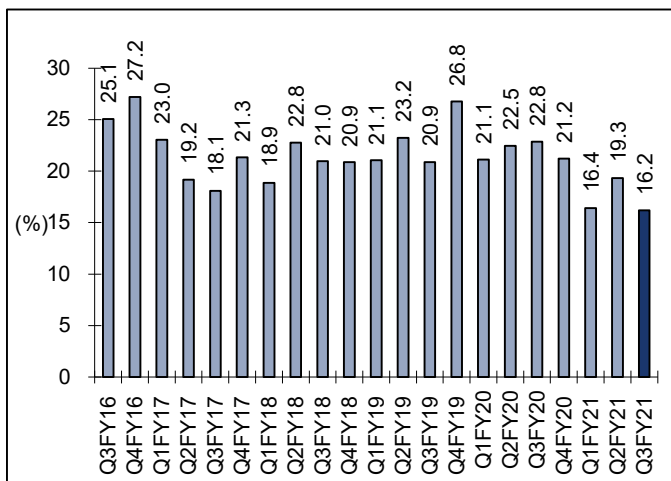
Source: Company data, I-Sec research

Chart 4: Staff cost as a % of sales



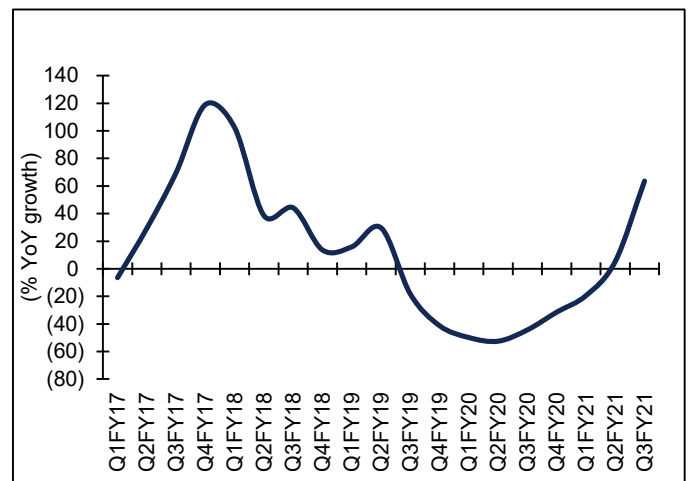
Source: Company data, I-Sec research

Chart 5: Other expenses as a % of sales



Source: Company data, I-Sec research

Chart 6: TDI price change



Source: Company data, I-Sec research

Financial summary

Table 3: Profit & Loss statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Net Revenues	21,736	23,755	31,100	34,980
Operating Expenses	18,732	19,954	26,556	29,616
EBITDA	3,004	3,802	4,544	5,364
% margins	13.8	16.0	14.6	15.3
Depreciation & Amortisation	590	749	839	938
Gross Interest	130	178	141	106
Other Income	400	446	770	1,177
Recurring PBT	2,684	3,321	4,334	5,497
Less: Taxes	621	836	1,091	1,384
Less: Minority Interest	-	-	-	-
Net Income (Reported)	1,943	2,485	3,243	4,114
Extraordinaries (Net)	(120)	-	-	-
Recurring Net Income	2,063	2,485	3,243	4,114

Source: Company data, I-Sec research

Table 4: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Assets				
Total Current Assets	7,569	10,350	14,053	18,374
of which cash & cash eqv.	446	2,596	5,858	9,435
Total Current Liabilities & Provisions	4,151	4,870	5,991	6,784
Net Current Assets	3,418	5,480	8,062	11,589
Investments	774	845	1,107	1,245
Net Fixed Assets	7,991	8,042	8,083	8,114
Capital Work-in-Progress	180	180	180	180
Goodwill	2,371	2,371	2,371	2,371
Total Assets	12,362	14,547	17,432	21,128
Liabilities				
Borrowings	2,915	2,615	2,315	2,015
Deferred Tax Liability	172	172	172	172
Minority Interest	-	-	-	-
Equity Share Capital	244	244	244	244
Face Value per share (Rs)	5	5	5	5
Reserves & Surplus*	9,032	11,517	14,701	18,698
Net Worth	9,276	11,761	14,945	18,942
Total Liabilities	12,362	14,547	17,432	21,128

Source: Company data, I-Sec research

Table 5: Quarterly trends

(Rs mn, year ending March 31)

	Mar 20	Jun 20	Sep 20	Dec 20
Net Revenues	5,041	2,690	6,078	8,259
% growth (YoY)	(5.7)	(47.7)	22.2	25.5
EBITDA	739	278	1,064	1,439
Margin (%)	14.7	10.4	17.5	17.4
Other income	122	108	93	157
Extraordinaries (Net)	(120)	-	-	-
Adjusted Net profit	442	118	698	1,001

Source: Company data, I-Sec research

Table 6: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Operating Cash flow	2,730	2,894	3,192	3,842
Working Capital	(1,094)	88	680	49
Changes				
Capital Commitments	(1,834)	(800)	(880)	(968)
Free Cash Flow	(199)	2,182	2,992	2,923
Cash flow from	(2,946)	(532)	(251)	103
Investing Activities				
Issue of Share Capital	70	-	-	-
Inc (Dec) in Borrowings	1,686	(300)	(300)	(300)
Dividend paid	-	-	(59)	(117)
Change in Deferred Tax Liability	273	2,150	3,262	3,577
Chg. in Cash & Bank balance	446	2,596	5,858	9,435

Source: Company data, I-Sec research

Table 7: Key ratios

(Year ending March 31)

	FY20	FY21E	FY22E	FY23E
Per Share Data (Rs)				
EPS	42.3	50.9	66.5	84.3
Cash EPS	54.4	66.3	83.7	103.6
Dividend per share (DPS)	-	1.0	2.0	3.0
Book Value per share (BV)	190.2	241.1	306.4	388.3
Growth (%)				
Net Sales	1.5	9.3	30.9	12.5
EBITDA	42.4	26.5	19.5	18.0
PAT	54.2	20.5	30.5	26.8
DPS	-	-	-	-
Valuation Ratios (x)				
P/E	48.2	40.0	30.6	24.2
P/CEPS	37.4	30.7	24.3	19.7
P/BV	10.7	8.4	6.6	5.2
EV / EBITDA	32.0	25.3	21.2	17.9
EV / Sales	4.4	4.0	3.1	2.7

Operating Ratios

Raw Material / Sales (%)	50.8	53.8	52.7	52.1
Employee cost / Sales (%)	10.1	9.5	8.3	8.2
SG&A / Sales (%)	25.2	20.8	24.4	24.3
Other Income / PBT (%)	14.9	13.4	17.8	21.4
Effective Tax Rate (%)	23.1	25.2	25.2	25.2
Working Capital (days)	14.1	11.7	1.2	0.7
Inventory Turnover (days)	38.1	40.0	32.0	32.0
Receivables (days)	36.2	37.0	30.0	30.0
Payables (days)	25.8	30.0	25.0	25.0
Net D/E Ratio (x)	(0.1)	(0.3)	(0.4)	(0.6)

Profitability Ratio (%)

Net Income Margins	9.5	10.5	10.4	11.8
RoACE	24.1	22.7	23.2	23.0
RoAE	24.9	23.6	24.3	24.3
Dividend Payout	-	2.4	3.6	4.3
Dividend Yield	-	0.0	0.1	0.1
EBITDA Margins	13.8	16.0	14.6	15.3

Source: Company data, I-Sec research

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