



**Invest & “SLEEP-WELL”**

**BUY**

Target Price: Rs. 2,039

# Sheela Foam Ltd

Polyurethane Foam and Mattresses

CMP : Rs 1,650  
Potential Upside : 24%

**MARKET DATA**

No. of Shares : 4.88 Cr.  
Market Cap : Rs. 8,049 Cr.  
Free float : 14%  
Avg. daily vol (6mth) : 17588  
52-w High / Low : 1850/1275  
Bloomberg : SFL:IN  
Promoter holding : 85.68%  
FII / DII : 11.05%

**Price performance****Financial Summary**

Y/E	Sales (Rs Cr)	EBITDA (Rs Cr)	PAT (Rs Cr)	EPS (Rs)	Change (%)	P/E (x)	RoE (%)	RoCE (%)	EV/EBITDA
March									
FY16	1,696	176	105	32.2	145.4	-	35.9	42.1	-
FY17	1,912	195	125	25.6	(20.5)	-	31.1	39.0	-
FY18	2,004	216	134	27.4	7.1	-	25.2	33.2	-
FY19E	2,202	285	180	36.8	34.3	44.8	26.1	35.0	27.4
FY20E	2,478	387	249	51.0	38.5	32.4	27.6	37.7	19.7

Source: Company, Axis Securities; CMP as on 18 SEP 2018

**Shareholding pattern**

	Jun-18	Mar-18
Promoter & Promoter group	85.7%	85.7%
MFs/UTI	9.0%	8.9%
FPI	2.5%	2.6%
Public	2.8%	2.9%
Others	0.0%	0.0%
Banks/FIs	0.0%	0.0%

## Investment Rationale

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Incorporated in 1971, Sheela Foam Ltd. (SFL) is India's largest Polyurethane foam (PU) manufacturer. They are also amongst the leaders in mattress market and sell under the flagship brand of 'SLEEPWELL'. The Company manufactures other foam-based home comfort products focusing primarily at Indian retail consumers, as well as technical grades of polyurethane (PU) foam for end use in a range of industries. It has 10 manufacturing units Pan India and 5 units in Australia. 85% of the revenue comes from Indian operation whereas 15% is contributed by Australian subsidiary. It has extensive distribution network with more than 6360 exclusive distributor, retail dealers and multi-brand outlets cumulatively.

Sheela Foam is expected to be big beneficiary of the shift in taste following urbanization and changing lifestyle. Being one of the top 3 players, SFL would be riding the growth wave due to shift from unorganized to organized segment, product innovation and under penetration. We estimate revenue to grow at CAGR of 11% over FY18-FY20E and PAT to grow at CAGR of 36% over FY18-FY20E driven by:

- Strong brand awareness among the consumers giving the company competitive edge over its peers
  - Pan India distribution network along with manufacturing plants situated in proximity to market
  - Product expansion, introduction of low price products with sub-brands and utilizing the knowhow to produce higher margin products
  - New plant setup and investment in existing plants to be supported by strong cash flow position
  - Expected fall in price of major raw material TDI to further increase the EBITDA margin from existing 10-11%
- ♦ We initiate coverage with "BUY" rating with a target price of Rs 2,039 i.e 24% upside (implies 40x FY20E)

## Investment Rationale

### Growing industry

- The Rs 10,000 Crore mattress industry is growing at 11% CAGR and a shift from unorganized to organized market in mattress industry would provide opportunities for Sheela Foam to grow. Population growth, nuclearisation, increase in disposable income, urbanization as well as growth in end user industry (household, hospitality and hospital) would be the factors driving mattress sales growth.

### Brand recognition

- Mattress and Home comfort products of Sheela Foam sells under the flagship brand SLEEPWELL which is well recognized by the consumer. The Company is looking forward to consolidate customer recall of various customized product sub-brands such as My Mattress and Perfect Match. This will result in increase in customer and revenue.

### Pan India distribution network

- Sheela Foam has a wide distribution network of more than 110 exclusive distributors, 3,350 plus exclusive retail dealers and upwards of 3,250 multi-brand outlets. The company targets to have more than 4000 Exclusive brand outlets (EBO) by FY20. During Q1FY19 company added 685 EBO's.

### Proximity to market

- Sheela Foam has pan India manufacturing facility to enable it save on freight cost as its product is voluminous in nature and freight cost eats into profits beyond certain radius. SFL has 10 manufacturing plants are well spread across the country with 1 plant in west, 2 in east, 5 in north and 2 in South. This enables the company to **service the markets better**. The company enjoys higher sales compared to peer because of manufacturing plants in proximity to market.

## Investment Rationale

### Product portfolio

- Sheela Foam introduced **economy model mattress** "Starlite" and **Mid Level Mattress** "Feather Foam" in July 2017 and Feb. 2018 respectively. The Company intends to leverage the existing range of products, the knowhow and manufacturing capabilities to produce **niche and higher-margin products**, including more sophisticated grades of technical PU foam. They are also planning to create baseline products at lower price points, targeting the rural customer. On the furniture side of the business, the Company has tied up with **carpenters & upholsters** under "Anmol Bandhan Scheme".

### Raw material cost

- The overall foam based industry has been facing stress because of rising price of one of the important raw material i.e. TDI in foam production. Sheela Foam has performed well during these stressed period with 10-11% EBITDA Margin. With TDI supply getting back on track, **TDI prices have eased from Rs 310/Kg in June'18 to Rs 250/Kg in August'18**. Demand and supply is discussed on page 13. While some of the benefits would be passed on to customers, branded mattresses would gain margins owing to SFL's pricing power.

### Focus on R&D

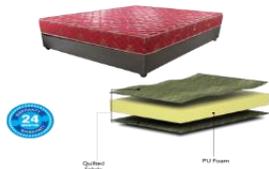
- Sheela foam has been able to continuously increase foam yield. The foam produced from **Vertical Variable Pressure Foaming plant** is used for quilting to provide extra comfort, to all kinds of Sleepwell Mattresses. This Award winning technology has proved to be a game changer for quilting comfort for Sheela Foam.

# Mattress Industry

## Major Types of Mattress



Rubberised Coir



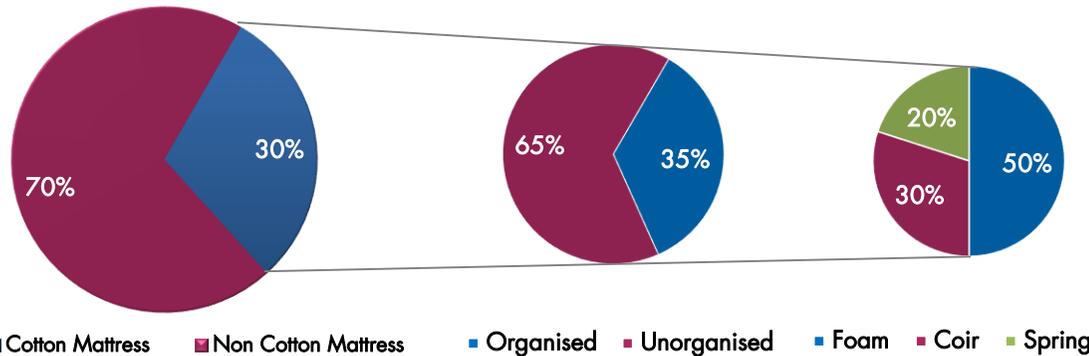
PU Foam



Spring

✓ Cotton Mattress which is roughly estimated to be used by 70% of the population is considered as an alternative to mattress and has not been accounted in the Mattress Industry

## Market Classification



Source: Company, Axis Securities

✓ The Size of Indian Non-Cotton mattress market at present is ~ Rs 10,000Cr comprising Polyurethane(PU) foam, Rubberized coir and Spring mattresses

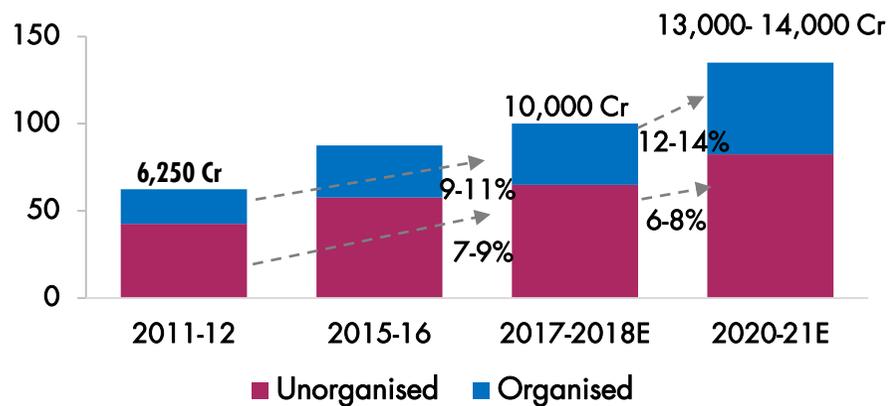
✓ Around Rs 6500 Cr of total mattress market belongs to unorganized sector and Rs 3500 Cr is organized

✓ PU foam mattresses dominated the overall organized market capturing 50% share followed by coir and spring mattresses constituting 30% and 20% share respectively

**PU Foam mattress is growing fast with consumer understanding the need for comfortable sleep & is replacing coir mattress with the Foam mattress**

## Mattress Market

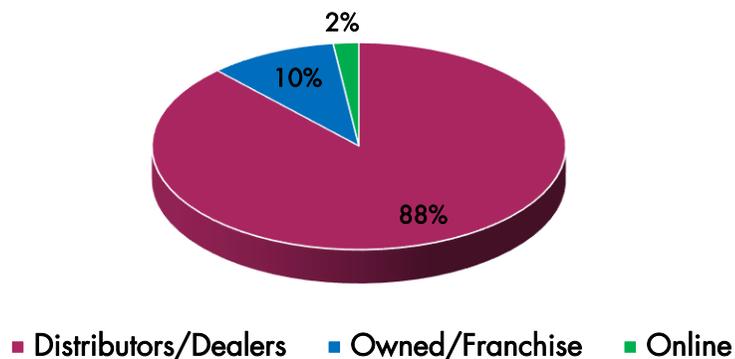
### Mattress Market Growth



### Growth : Organized Sector to capture share in growth

- ◆ The non-cotton mattress market is estimated to reach the market size of Rs 13000-14000 Cr by 2021 growing at a CAGR of 8-10%
- ◆ Organized sector would gain market share from 35% at present to **40% in FY21E**, growing at a CAGR of 11-13%
- ◆ Unorganized sector which accounts for 65% of the market would loose its share and grow at CAGR 6-8%
- ◆ Implementation of **GST narrowed down the pricing gap** enabling organized player to capture the share of unorganized market

### Distribution Channels

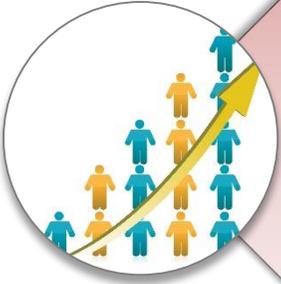


### Distribution Channel: Dependence on Distributor and Retailers

- ◆ Based on distribution channel, the mattress market is dominated by **distributor/dealer network** followed by own/franchisee stores and online mode accounting for nearly 88%, 10% and around 2% of the total sales respectively
- ◆ Organized players have started online sales by way of **partnerships with online portals** and also by establishing their own websites
- ◆ Owing to demographic factors such as rising youth population and rising standard of living, the demand for mattress from **e-commerce portals is expected to increase**

Source: Company, Axis Securities

## Mattress Industry: Growth Prospects



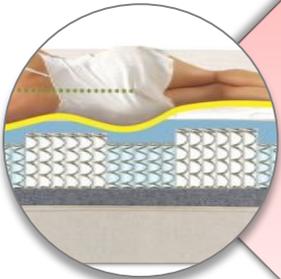
### Population growth and nuclearisation of families

Population of India is expected to be at **138 cr by CY20** which will increase the consumption. The new India is slowly shifting towards nuclearisation of families due to job prospects, standard of living and urbanization which will drive the demand for mattress



### Urbanization and increase in disposable income

About 34% of India's population is now urbanized ( 3% increase since the 2011 Census) and would reach **36% by CY20**. This is likely to shift the consumer preference from cotton mattress to the non-cotton mattress. Rural income level and disposable income is also on the rise which is envisaged to increase the affordability thereby leading to rise in consumption of lifestyle products



### Increase in awareness

As people are becoming more **health conscious and aspiring luxury lifestyle**, there is an evident rise in the awareness of the relation between good sleep and a good quality mattress especially among the youth. Urban consumers are moving towards quality mattress as a measure to compensate for the increasing stress

Source: Company, Axis Securities

## Mattress Industry: Growth Prospects

### Growth in End User Industry



#### Housing Segment

- ◆ 18 lakh houses to be built across top 10 cities
- ◆ 11 lakh units (approx.) are expected to be ready for possession by CY18
- ◆ Housing growth represents a significant potential demand for the mattress industry



#### Hospitality segment

- ◆ Premium hotel rooms inventory to significantly increase by 28% to reach 66,400 rooms by FY20
- ◆ Leisure destinations supply is envisaged to increase from 14,200 rooms in FY16 to 17,300 rooms by FY20
- ◆ Growth in the Indian hospitality sector is expected to affect mattress sales



#### Healthcare segment

- ◆ Bed density in the hospitals of India is lower than its peer developing countries
- ◆ Potential exists for mattress sales as the current density of 1.3 beds (per 1000 people) gets rectified to 3.5 beds defined by WHO
- ◆ Govt. to establish 1.5 lakh Health and Wellness Centers over next 5-10 years

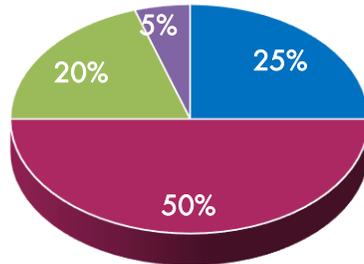
**The hospitality sector in India is expected to grow at 16% CAGR to reach at Rs 28 lakh crore by 2022.  
This portends tremendous growth potential for mattress industry**

Source: Company, Axis Securities

## Mattress Industry: Growth Prospects

### Potential for Non-Cotton Mattress to replace Cotton Mattress

Economy segment at presents account for 25% of Non-cotton mattress



- Economy (up to Rs 8,000)
- Mid-segment (Rs 8,000-30,000)
- Premium (Rs 30,000-75,000)
- Luxury (Above Rs 75,000)

Cotton mattress estimated price chart\*

Price per unit	Quantity used	Single Bed		Double Bed	
		10Kg/5M	15Kg/5M	20Kg/8M	30Kg/8M
Rs90#/Rs80*		2500	2950	3640	4540
Rs100/Rs100		2700	3200	4200	5000
Rs110/Rs120		2900	3450	4360	5460
Rs120/Rs150		3150	3750	4800	6000

#Cotton price per Kg/ \* Cloth price per meter

Note: Inclusive of average labor cost of Rs 1200 per mattress (Mumbai)

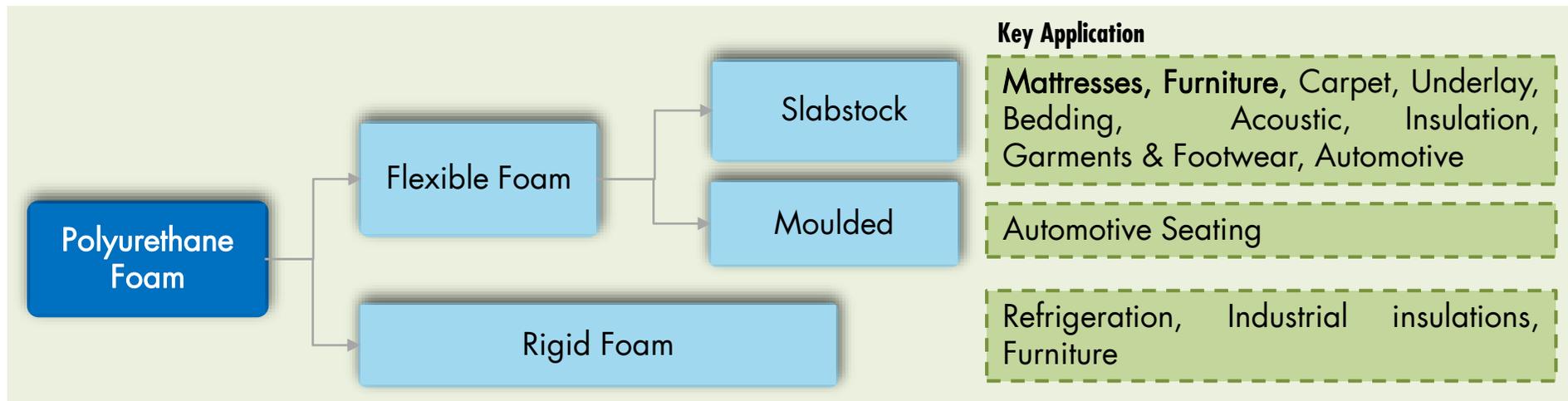
### 'Economy model' Non-cotton mattress to take away cotton mattress market share

- ◆ Economy model Non cotton mattress are available at Rs 2,500 onwards giving competition to Cotton mattresses
- ◆ Infrastructure development would increase the market penetration for Non-cotton mattress which are more durable
- ◆ Health awareness and Rural development would be driving consumer towards Non-cotton mattress
- ◆ Non-Cotton stuffed mattresses do not develop clots or de-shape after a certain period thus relaxing the spine

**The share of Non-cotton economy model mattress would significantly increase as price differentiation with cotton mattresses is reducing**

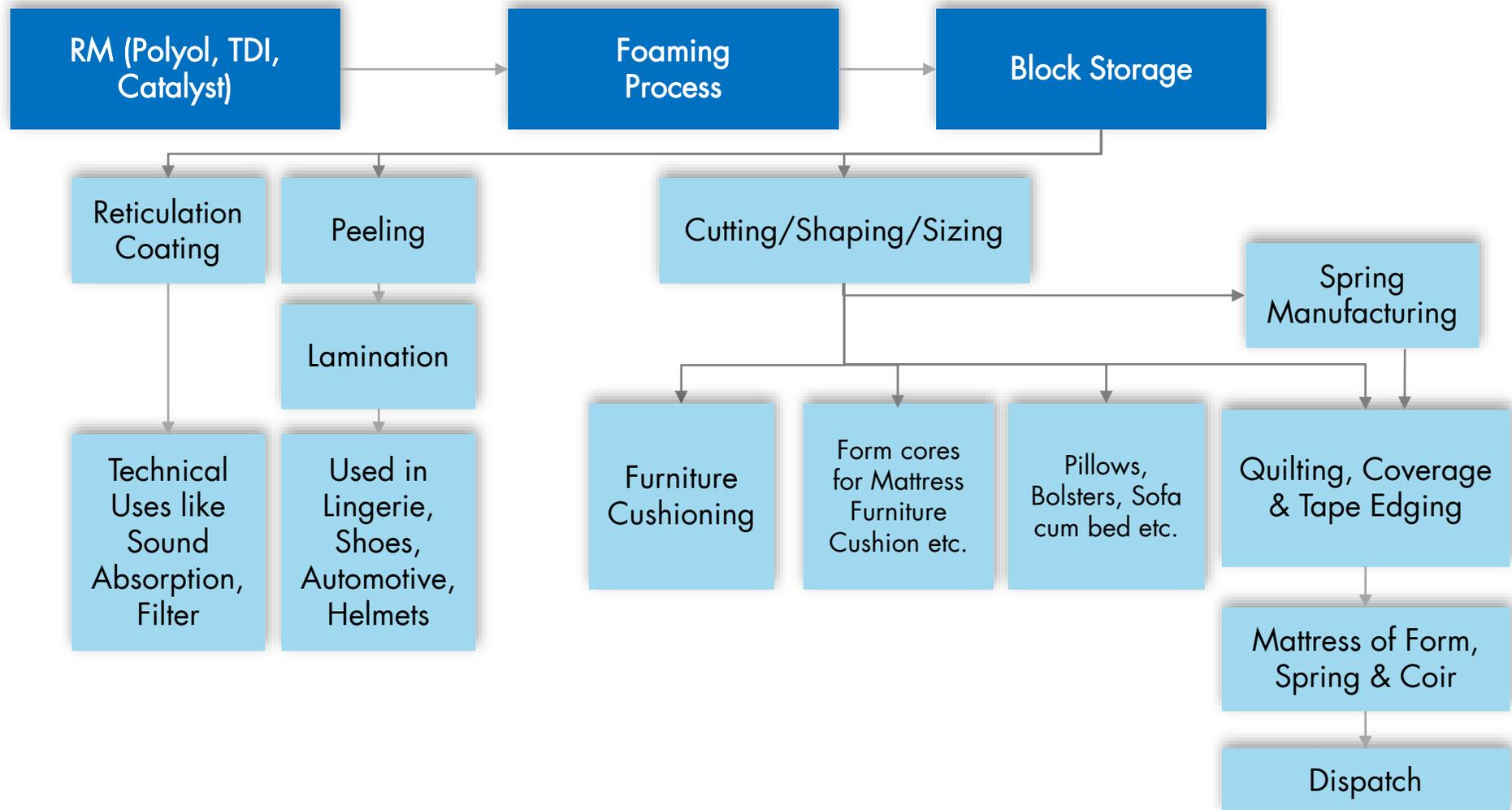
Source: Company, Axis Securities

## Polyurethane Foam Industry



- ◆ Global PU foam market is expected to reach USD 25.1bn in 2020 from USD 17.3bn in 2015 growing at 7.8% CAGR. Asia Pacific is the dominant market, with China being the leading manufacturer and consumer of PU foam. Increasing demand from bedding & furniture industry owing to rising urban population in emerging economies of Asia Pacific such as China, India, and Indonesia is anticipated to drive growth over the forecasted period
- ◆ The Indian flexible PU Foam industry is significantly unorganized; market is dominated by small and medium scale manufacturers in every region, mainly owing to transporting issues
- ◆ The Indian flexible PU foam industry is estimated at Rs 6500 Cr. The flexible PU foam is manufactured as Slabstock Foam and Moulded Foam. Major part of the PU foam market is dominated by Slabstock foam (around 65-70%). Flexible Slabstock foam mainly finds application in mattress and furniture, whereas Moulded Foam is mostly used in automotive Industry

## PU Foam making process

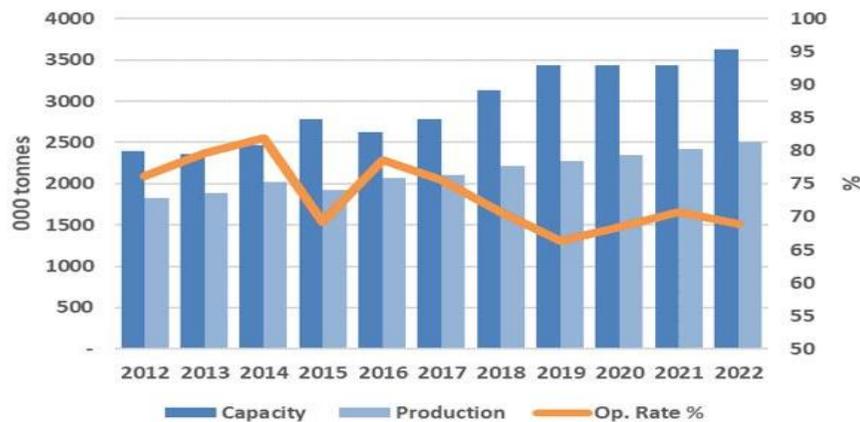


Source: Company, Axis Securities

## Raw Material - TDI

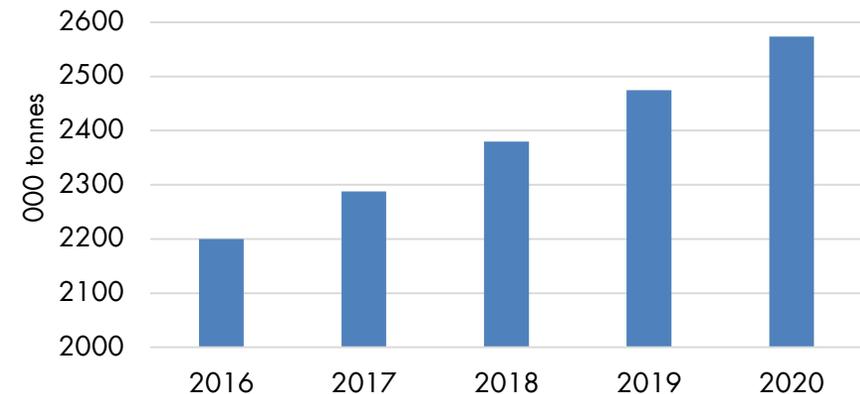
**Toluene di-isocyanate (TDI) is a major raw material used in the production of Foam. Price of TDI is highly volatile and price movement depends on demand-supply gap.**

### Global Supply: 3.1 MT (FY18) operating at 70-75%



Source: Axis Securities, ICIS

### Global Demand : 2.3 MT (FY18)



Source: Axis Securities

### Reasons for TDI price rise during 2016-2018

- ◆ While Global capacity is around 3 MT, **operating rate is around 70-75%** causing tightness in market
- ◆ Hazardous nature of TDI results in **frequent shutdown** of plants in case of leakages
- ◆ **Low operating rate** created supply pressure and price rose during 2016-2018

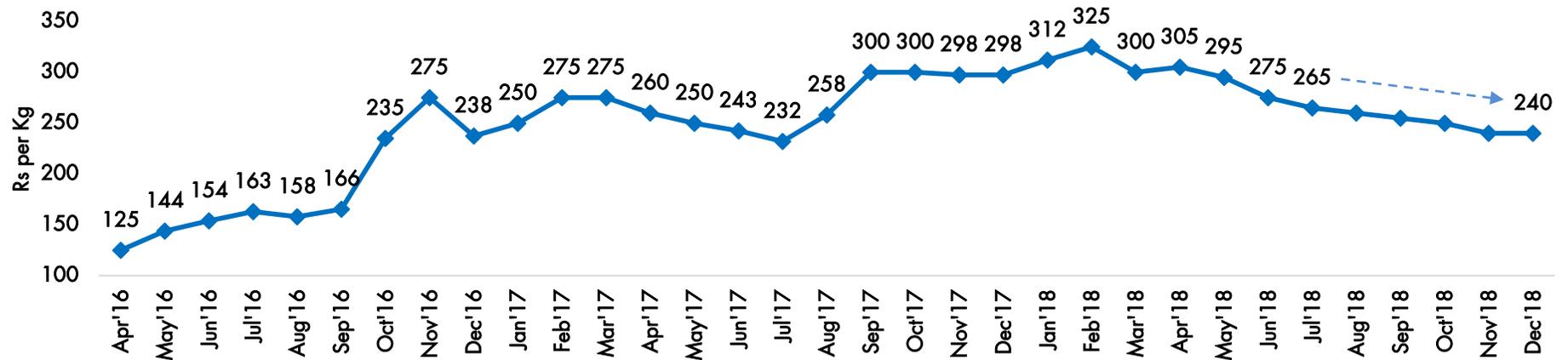
Source: Company, Axis Securities

### Additional supply to ensure lower TDI price

- ◆ Global TDI player BASF re-started **300,000 tonne/year** capacity from Q2FY19
- ◆ **200,000 tonnes/year** Sadara facility in Saudi Arabia is also to be operational soon
- ◆ Expected demand of 2.6 MT by 2021 would be comfortably supplied by expected capacity of 3.6 MT even at 70% operating rate

## Raw Material - TDI

### Average monthly TDI price



Source: Company, Axis Securities

- ◆ During April'16 and June'18, a series of **shutdowns** and force majeure added to the supply tightness causing prices to soar. TDI price rose sharply from Rs 118/Kg on April 1, 2016 to Rs 300/Kg on April 1, 2018
- ◆ TDI price saw its peak in February 2018 when it reached to the level of **Rs 335/Kg** due to multiple plants being shutdown for different period during years mentioned above
- ◆ From June'18, prices have started to fall in anticipation of Northeast Asian plants to restart from their shutdowns. TDI price stands at **Rs 255/Kg** as on 24<sup>th</sup> July 2018
- ◆ Toluene di-isocyanate (TDI) prices globally are likely to fall further as the market moves from a sustained period of tightness into overcapacity. The company management expects TDI to be around **Rs 240** by the end of 2018

Source: Company, Axis Securities

## Sheela Foam

### Introduction

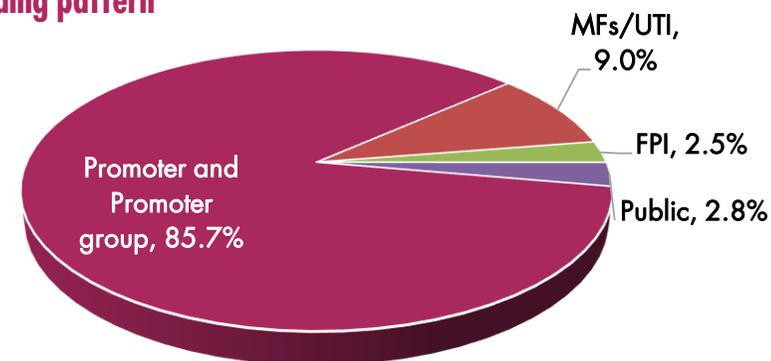
- Established in 1971, Sheela Foam Limited manufactures mattresses, other foam-based home comfort products and technical grades of PU Foam:
  - Its home comfort line consists of products, such as furniture-cushioning, cushions and sofa-cum-beds, as well as PU Foam
  - Its mattress line, offered under its 'Sleepwell' brand, includes pure foam mattresses, as well as hybrids of spring and coir
  - Its furniture-cushioning line, offered under 'Sleepwell' and 'Feather Foam' brands, consists of PU Foam that constitutes upholstery material of various densities
- Sheela Foam has a strong presence in Australia through its wholly owned subsidiary, Joyce Foam Pty Ltd and manufactures PU foam.

### Distribution network

- Strong retail presence with 110+ exclusive Distributors, 3,350+ exclusive retail dealers and 3,500+ multi-brand outlets. SFL targets to have 4,000+ exclusive outlet by FY20

Source: Company, Axis Securities

### Shareholding pattern



### Manufacturing Plants

- SFL has 10 plants in India for foam production out of which it manufactures foam in 5 plant for a total of 1,23,000 tonne p.a. capacity. SFL also has annual foam production capacity of 10,500 tonnes in Australia.

Location	Capacity (Tonne)
Greater Noida (U.P.)	60,000
Hyderabad (Telangana)	13,000
Erode (Tamil Nadu)	16,000
Talwada (Gujarat)	28,000
Jalpaiguri (West Bengal)	6,000
<b>Total</b>	<b>123,000</b>

## Sheela Foam - Experienced Management Team

### Mrs. Sheela Gautam

- She is an avid entrepreneur, renowned social worker & philanthropist. She founded Sheela Foam in 1971 and has been actively involved in growing the organization

### Mr. Rahul Gautam

- Managing Director, Chemical Engineer from IIT, Kanpur with Masters Degree in Chemical Engineering from Polytechnic Institute of New York, USA and 40+ years of experience in home comfort products

### Mrs. Namita Gautam

- Executive Director, a professionally qualified and experienced Human Resource Specialist with extensive knowledge and skills in Training and Development, Project Management, Media and Communication

### Mr. Tushar Gautam

- Executive Director, a bachelor of Industrial Management and Industrial Engineering from Purdue University, USA. He have 14+ years of experience in heading production and research and development

### Dr. Mahesh N. Gopalamudram

- COO, is a bachelor of Science from Sri Sathya Institute of Higher Learning, Master of Science (Chemistry) from University of Madras and a PhD in Chemistry from University of Madras. He has more than 15 years of experience in chemical industry

### Mr. Dhruv Mathur

- CFO, a fellow member of Institute of Chartered Accountants of India and Institute of Cost Accountants of India. He has more than 36 years of experience in various industries

### Mr. Rakesh Chahar

- Director- Sales and Marketing, has more than 20 years of experience in designing and marketing of P.U. Foam products

### Mr. Frank Van Gogh

- CEO, Joyce Foam, is a bachelor of Mechanical Engineering from University of New South Wales, Master of Business Administration from University of Technology, Sydney

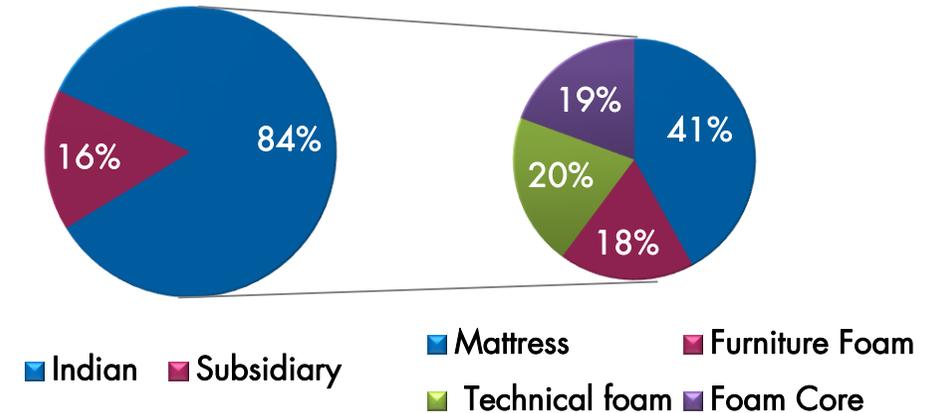
Source: Company, Axis Securities

## Diversified revenues segments

### Mattress & Home Comfort

- ◆ Mattress Segment accounted for 41% of revenue in FY18
- ◆ Sheela Foam have highest share in Premium & Mid Segment
- ◆ Sheela Foam has introduced two models Starlite(Aug 2017) and Feather foam(Feb 2018) to take on unorganized market of foam and spring mattress
- ◆ Economy model would drive the volume by 5% whereas push for ultra premium products will increase realization by 3-4%

### Revenue Breakup (FY18)



### Technical Foam

- ◆ The Company has increased sale of Technical Foam by increasing its customer base
- ◆ The Company has been able to develop different kinds of high quality technical foams through constant Research & Development
- ◆ Demand driver would be end user industry which are Automotive Industries, Sound Industry, Garment & Shoe industry

### Furniture Foam

- ◆ Furniture market has also been unorganized so far
- ◆ Sleepwell is associating with carpenters to influence its foam sales for Furniture cushioning and partners with smaller furniture manufacturers
- ◆ The market is expected to expand at a CAGR of 13% during the forecast period of 2016-2023
- ◆ Furniture Segment for the company is expected to grow at 18-20%

**Being a leading foam supplier, Sheela Foam would be ultimate beneficiary of highly growing furniture market**

Source: Company, Axis Securities

## Subsidiaries' performance expected to improve in near future

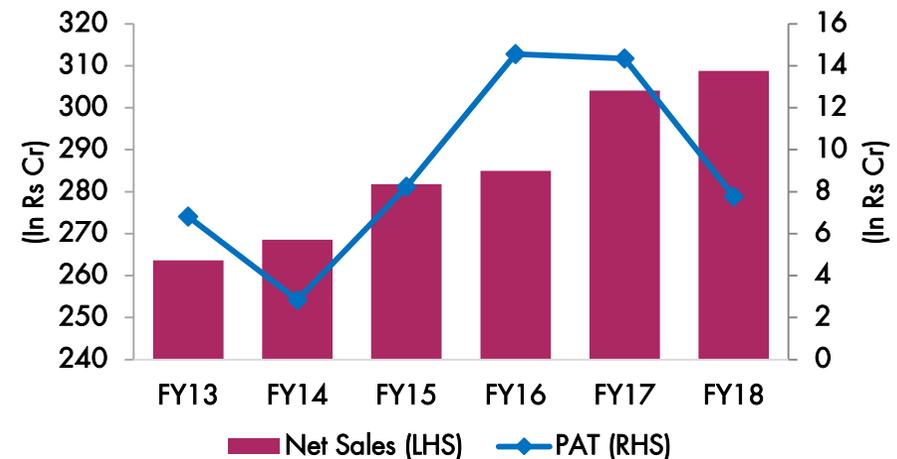
### Foam Core

- ◆ Foam Core is the Unbranded Foam of Sheela Foam that is sold to local manufactures who further repackage it and sell as finished mattress product
- ◆ This provides company the opportunity to capture a substantial unorganized market
- ◆ With consumer awareness of using foam mattress as compared to traditional one, this segment will also attract good demand in future

### Joyce Foam

- ◆ Joyce Foam is a leading manufacturer of flexible polyurethane foam with more than 35% market share in Australia
- ◆ Supplies its high quality Foam to Global Mattresses and Furnishing Companies
- ◆ Joyce recorded a turnover of 63.28 Million Australian Dollars (AUD) in FY 2017-18, recording a growth of more than 2%
- ◆ Margins contracted in FY18 as TDI price were constantly rising, with expected fall in TDI price Joyce bottom line is likely to improve in near future

### Subsidiaries Performance \*



Note: Figures are arrived by subtracting standalone numbers from consolidated

**Export operations would be leveraged to sell higher volumes of technical foam to manufacturers in SAARC nations**

Source: Company, Axis Securities

## Strong Brand Recognition

The brand Sleepwell was launched in 1993. Sleepwell has consistently built its brand over these year and has a strong brand recall. It is associated with comfortable sleep and is expected to reap its benefit when consumers are realizing the importance of quality mattress required for better sleep and health

**Sleepwell branded mattresses enjoy ~20-23% share in the organized Indian mattress market as of FY16**



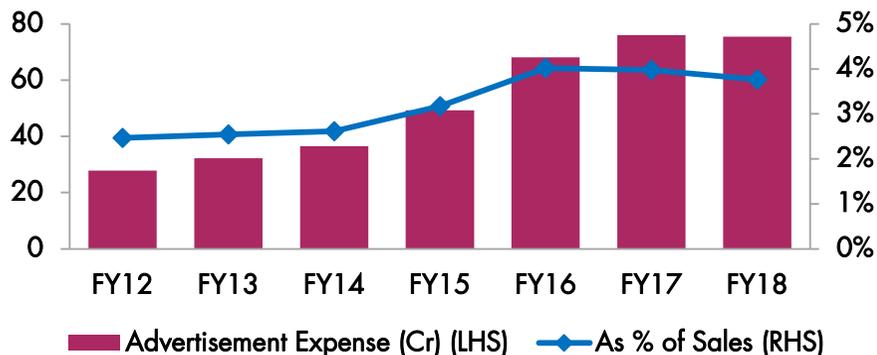
The other winning brands of Sheela Foam are: **Feather Foam**, a pure PU Foam and **Lamiflex**, a superior quality Polyester foam for lamination. These are ranked as largest selling PU foam in the country.

It has launched **Sleepwell Perfect match**: An initiative whereby mattresses are suggested that are best suited to an individual's body structure, weight and pressure distribution, based on diagnostic and statistical sleep measurements recorded on a senso-bed.

Sheela Foam is changing the dynamics of Industry, where mattress were mainly pushed by dealers it is now driven by consumer demand because of strong brand built by the company.

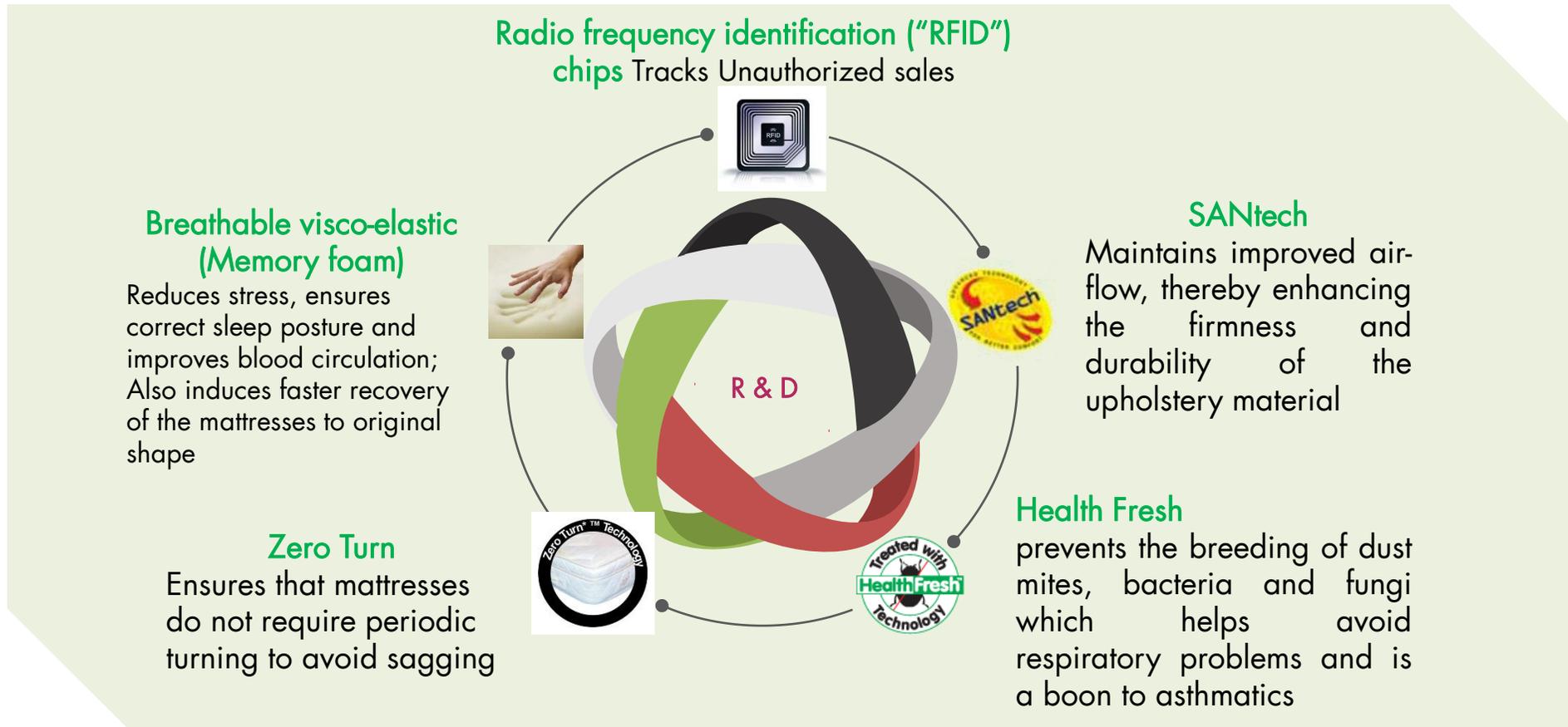
Company plans to further invest in **advertisement** to increase footfalls in its outlets and be ahead in brand recognition in the competitive market

### Advertisement Expense (Cr)



Source: Company, Axis Securities

## Innovation through R&D



- ◆ The Company has launched Comfort Cell technology to raise the comfort quotient of the consumer
- ◆ The foam produced from Vertical Variable Pressure Foaming plant is used for quilting to provide extra comfort, to all kinds of Sleepwell Mattresses. This Award winning technology has proved to be a game changer for quilting Comfort

Source: Company, Axis Securities

## Distribution Network

### Prominent retail presence

**110+**  
Exclusive distributors

**3350+**  
Exclusive retail dealers

**3500+**  
Multi Brand outlet

- ✓ Sheela Foam has been associated with most of its distributors for over 20 years
- ✓ Exclusive distributors are in strategic proximity to the manufacturing facilities, which helps reduce carriage expenses and minimizes product damage
- ✓ The distribution network is well integrated with the Company's IT platforms, that enables tracking secondary sales made by distributors and dealers in real time
- ✓ Around 150 sales personnel are actively engaged with key distributors
- ✓ As against 1101 EBO (Exclusive Branded Outlets) in 2012, Sheela Foam have 3,558 EBO as on August 2018 and planned to reach 4000+ by March 2020

### Exclusive Sleepwell brand outlets



**Sleepwell Shoppes**  
Average Size 200 Sq. Ft /1159 Outlets



**Sleepwell Galleries**  
Average Size 600 Sq. Ft/535 Outlets

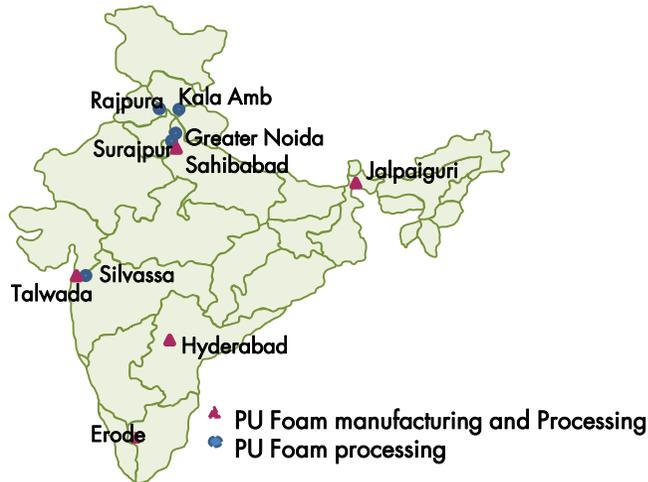


**Sleepwell World**  
Average Size 1000 Sq. Ft/321 Outlets

Source: Company, Axis Securities

## Manufacturing in Proximity to Market

### India: 10 Plants



- ◆ The plants are situated in **close proximity to market** which enables fast and better serviceability to customers.
- ◆ Company targets plants to be situated within radius of 300-400 km to ensure low freight cost and SFL is planning to install **2 new plants by FY20** in the location such as Indore, Raipur, Rohtak, which are growing as new market
- ◆ Total capacity of 123,000 tonne/year is sufficient to meet any spike in additional demand from the respective region

### Australia: 5 Plants



- ◆ Joyce Foam, Australia - Joyce foam, Australia is a 100% subsidiary of the Sheela Group.
- ◆ Joyce Foam is a leading manufacturer of flexible polyurethane foam with more than **35% market share** in Australia
- ◆ Manufacturing capacity of Joyce Foams stands at 10,500 tonne/year

**Proximity to market is one of the competitive edge for Sheela Foam due to the nature of product. Sheela Foam's strategy to penetrate the market further includes both organic as well as inorganic growth prospects**

Source: Company, Axis Securities

## Product Portfolio

Home comfort products

### Mattresses



My Mattress, Spring range, Technology range, Back support range, Flexi PUF range, Showroom range, Economy Range

### Furniture-cushioning material



Sleepwell Resitec, Sleepwell Cool Gel, Primo, Feather Foam

### Pillows



Fibre range, Flexi PUF range, Premium range

### Bolsters, cushions and other



Comfort range accessories

### Sofa-cum beds



Sofa and Bed

Technical foam products

### Automotive foams



Seat covers, Sound absorption systems, Sun visors, Headliners, Door trims, Lamination systems

### Reticulated foam



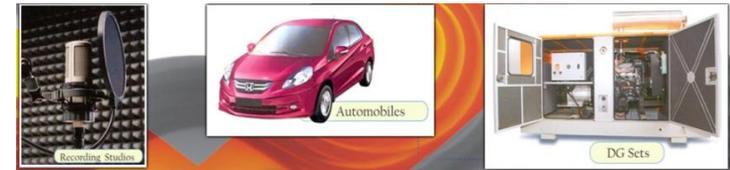
Filtration systems, Ceramic foam filters, Outdoor furniture, Microphones and headphones, Safety fuel tanks, Ink cartridges

### Ultra Violet Stable foam



Sportswear, Innerwear and lingerie, Clothing, Swimwear, Comfort accessories for shoes

### Silentech foam



Automotive, Diesel generator canopies, Theatres, auditoriums, indoor stadiums, Broadcasting rooms and recording studios, Industrial silencers, Acoustic enclosures, Engine testing rooms

**Sheela Foam is leveraging the existing suite of products and manufacturing capabilities to produce niche, more sophisticated and higher-margin products**

Source: Company, Axis Securities

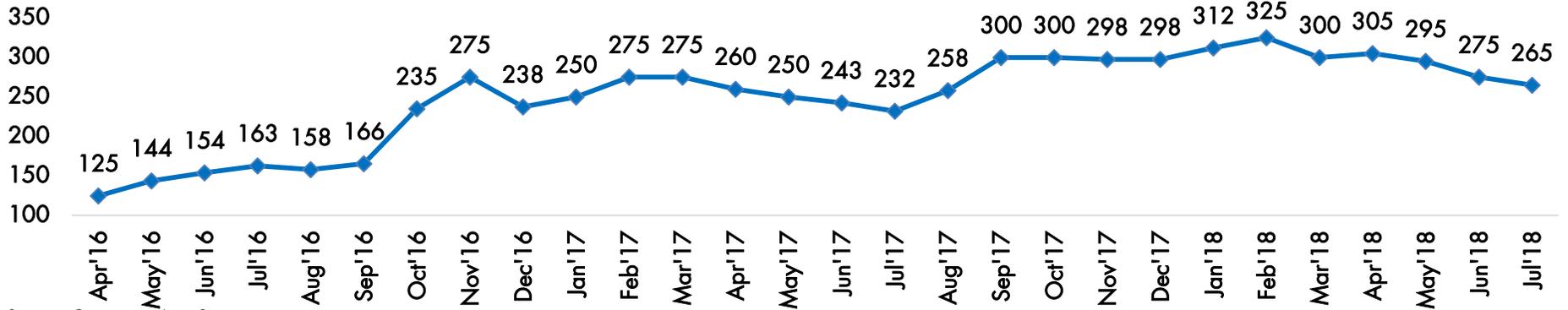
## Strategic Direction Ahead

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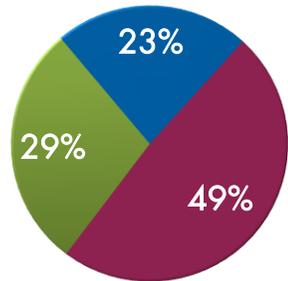
## Correcting TDI prices to help improve margins

### TDI price hiked during 2016-18

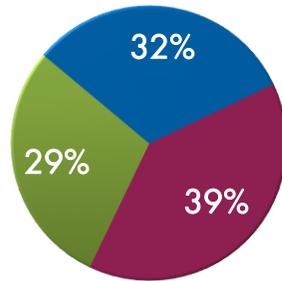


Source: Company, Axis Securities

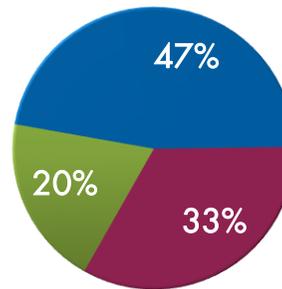
### RM cost breakup (%) : TDI share rose sharply due to price hike



FY2016



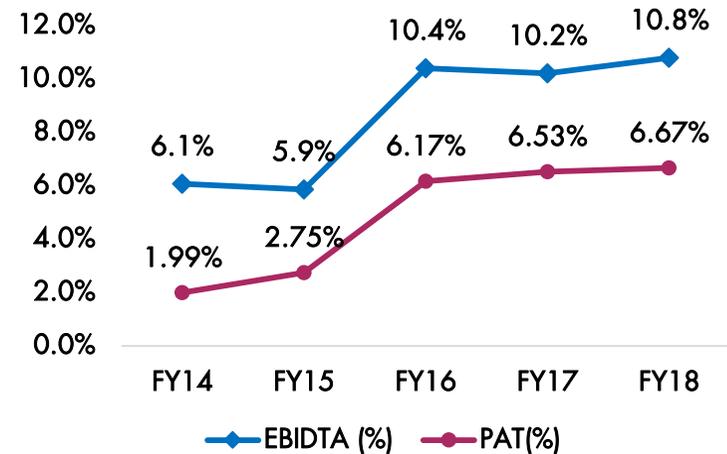
FY2017



FY2018

■ TDI ■ Polyol ■ Other (Coir sheet, chemical, clothe)

### Margins maintained despite TDI price rise

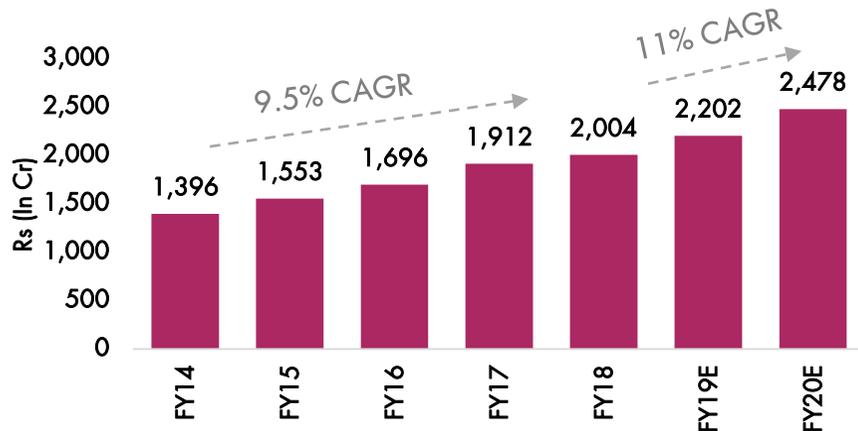


**TDI share in RM cost would reduce with fall in TDI price, giving boost to SFL's branded products margins owing to its pricing power**

Source: Company, Axis Securities

## Revenues, realizations to grow at healthy pace

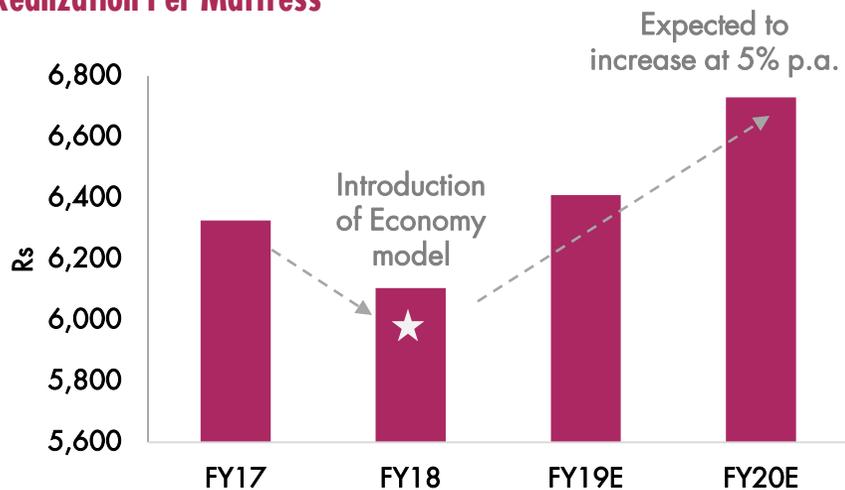
### Revenue



**Revenue Growth:** SFL has CAGR of 9.5% over FY14-FY18. We expect revenue to grow at 11.2% CAGR over FY18-FY20 led by increase in target market and growing End-User Industry

- ◆ Mattress Segment is expected to grow 5% in volume whereas company takes 3-4% price increase annually
- ◆ We expect Furniture Foam segment to grow substantially at 20% on a low base
- ◆ Technical PU foam is expected to grow at 12% CAGR as SFL has developed high quality products through R&D

### Realization Per Mattress

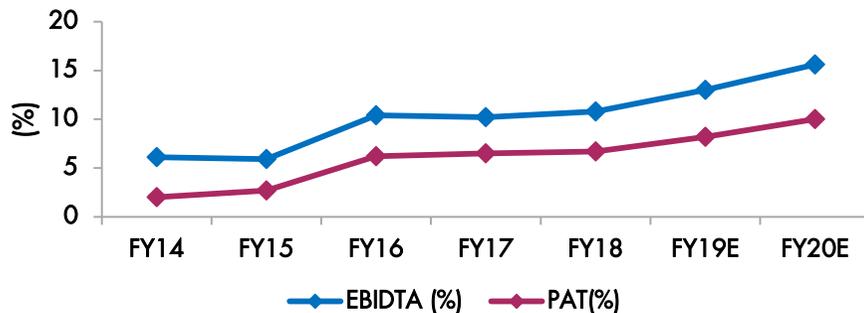


**Realization on increasing trend:** FY18 saw slight decline in mattress realization due to introduction of Economy class brand. SFL increases price twice a year without facing pressure on demand

- ◆ Realization growth on mattresses was 3.5% in FY18 (excluding economy model). Going forward we expect 5% realization growth yearly
- ◆ SFL has strong hold in premium and mid-range segment
- ◆ The launch of premium outlets, Sleepwell Emporios would help realization growth

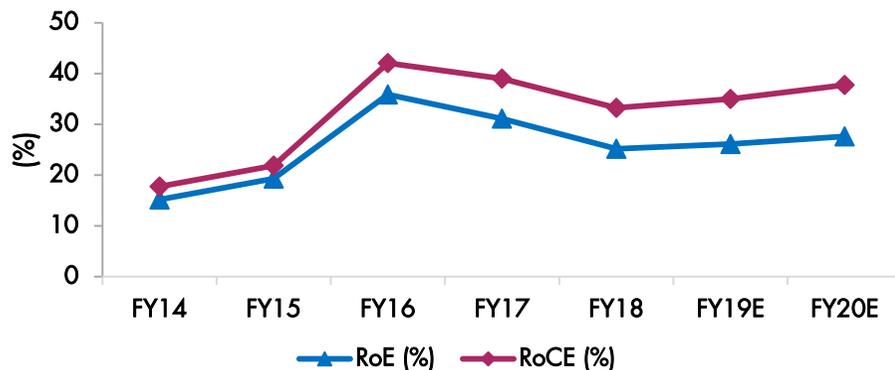
Source: Company, Axis Securities Ltd.

## Debt free company; strong cash flows to back capex



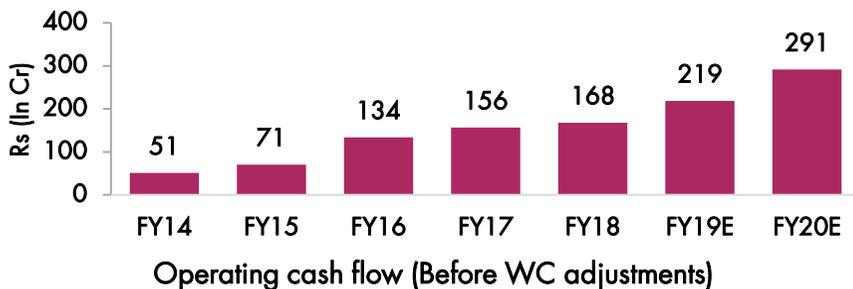
### Margins on increasing trend

- ◆ We estimate EBITDA margin to be 15.6% by FY20E and PAT to be at 10.3% by FY20E on back of and incremental production and sales along with increasing efficiency
- ◆ Going forward we expect TDI price to ease which would further improve the margins



### Improving return ratios

- ◆ SFL generated RoE of 25.2% and RoCE of 33.2% in FY18. We expect SFL's RoE to be at 27.6% and RoCE to be at 37.7% by FY20E on back of improving margins and operational efficiency.
- ◆ We expect the return ratios to get better on account of improving NPM. The asset turn is currently subdued and as the capacity utilization improves, we expect asset turn to pick up thus further pushing the return ratios nearer to its historical highs.



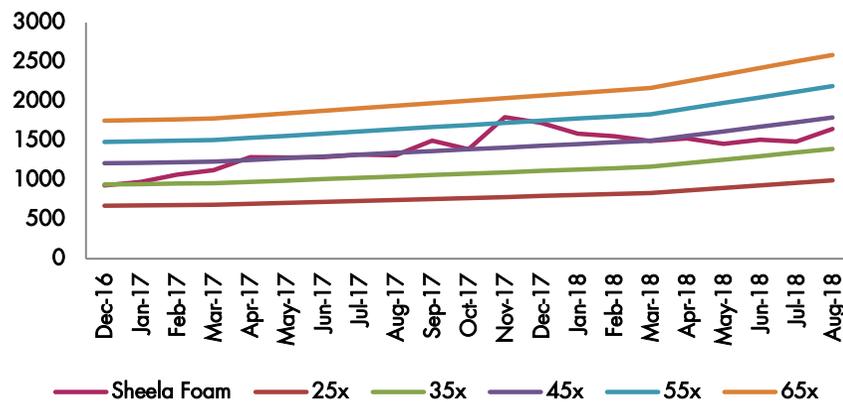
### Strong Cash flow to back Capex

- ◆ SFL has also reduced its long-term debt and is currently debt free
- ◆ Operating Cash flows would be enough for capex requirements
- ◆ We expect operating cash flows (before WC changes) to grow at a CAGR of 32 % over FY18-20E

Source: Company, Axis Securities

## Growth to drive valuations

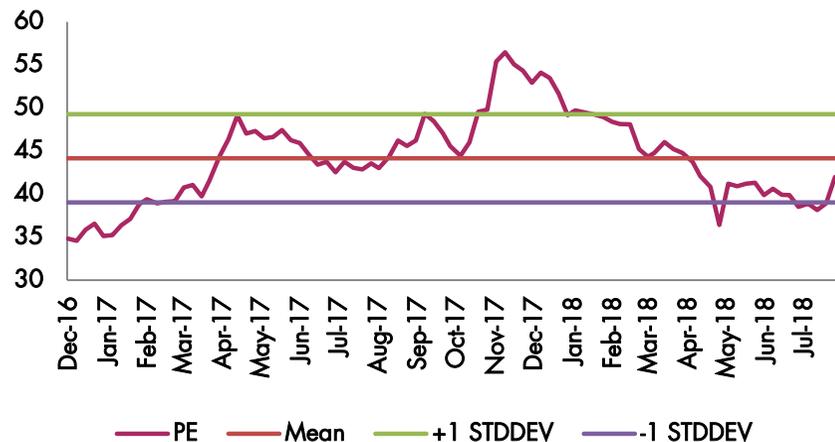
### PE Band



### Valuations

- ◆ We estimate SFL to post revenue growth at a CAGR of 11% and profits at CAGR of 36% over FY18-20E
- ◆ SFL is well positioned with 20-23% share in mattress market, strong brand recognition, robust margins and solid financials to support market expansion.
- ◆ We value SFL at 40x FY20E given the growth prospects to arrive at a target price of Rs 2039 (24% upside)

### 12mth fwd P/E (x)



### Key Risks

- ◆ TDI which accounts for ~1/3 of SFL's raw material cost is highly volatile. Any obstacle in the operation of upcoming capacity as well as existing capacity could push the price up
- ◆ Mattress market is highly competitive with more than 20 players in the organized sector. Competitors are looking for funding to expand their market share which could impact SFL profits

Source: Company, Axis Securities

## Financials (Consolidated)

### Profit & Loss

(Rs Cr)

YE March	FY16	FY17	FY18	FY19E	FY20E
Net sales	1,696	1,912	2,004	2,202	2,478
Total income	1,696	1,912	2,004	2,202	2,478
Cost of goods sold	1,187	1,348	1,377	1,467	1,595
Contribution (%)	30.0%	29.5%	31.3%	33.4%	35.6%
Other Expense	332.4	368.7	411.4	449.2	495.7
<b>Operating Profit</b>	<b>176</b>	<b>195</b>	<b>216</b>	<b>285</b>	<b>387</b>
Other income	16	22	21	21	23
PBIDT	<b>193</b>	<b>217</b>	<b>237</b>	<b>306</b>	<b>410</b>
Depreciation	29	30	35	39	43
Interest & Fin Chg.	12	10	9	9	10
Pre-tax profit	<b>152</b>	<b>177</b>	<b>193</b>	<b>258</b>	<b>358</b>
Tax provision	47	52	60	79	109
(-) Minority Interests	0	0	0	0	0
Associates	0	0	0	0	0
<b>Adjusted PAT</b>	<b>105</b>	<b>125</b>	<b>134</b>	<b>180</b>	<b>249</b>
Reported PAT	<b>105</b>	<b>125</b>	<b>134</b>	<b>180</b>	<b>249</b>

Source: Company, Axis Securities

### Balance Sheet

(Rs Cr)

YE March	FY16	FY17	FY18	FY19E	FY20E
<b>Total assets</b>	<b>499</b>	<b>564</b>	<b>705</b>	<b>882</b>	<b>1,136</b>
Net Block	288	317	347	403	481
CWIP	11.4	37.5	53.3	78.0	78.0
Investments	23.0	16.0	47.5	47.5	47.5
Wkg. cap. (excl cash)	(41)	(16)	99	111	125
Cash / Bank balance	217.2	209.4	158.2	242.5	405.7
<b>Capital employed</b>	<b>499</b>	<b>564</b>	<b>705</b>	<b>882</b>	<b>1,136</b>
Equity capital	16.3	24.4	24.4	24.4	24.4
Reserves	322	439	573	752	1,001
Minority Interests	0.0	0.0	0.0	0.0	0.0
Borrowings	158	99	106	103	108
Def tax Liabilities	1.9	1.6	2.0	2.5	3.1

## Financials (Consolidated)

Cash Flow	(Rs Cr)				
	YE March	FY16	FY17	FY18	FY19E
<b>Sources</b>	<b>79</b>	<b>(54)</b>	<b>175</b>	<b>211</b>	<b>292</b>
Cash profit	146	165	178	227	301
(-) Dividends	0	0	0	0	0
Retained earnings	146	165	178	227	301
Issue of equity	(0.0)	8.1	0.0	0.0	0.0
Change in Oth. Reserves	(11.0)	(9.1)	0.8	0.0	0.0
Borrowings	(38)	(13)	(14)	(8)	0
Others	(17)	(205)	10	(8)	(9)
<b>Applications</b>	<b>79</b>	<b>(54)</b>	<b>175</b>	<b>211</b>	<b>292</b>
Capital expenditure	11.8	(116.9)	82.4	120.0	120.0
Investments	22.1	(6.9)	92.0	0.0	0.0
Net current assets	(54.8)	77.9	51.3	6.9	8.8
Change in cash	100.2	(7.8)	(51.1)	84.3	163.2

Source: Company, Axis Securities

Ratio Analysis	(%)				
	YE March	FY16	FY17	FY18	FY19E
Sales growth	9.2	12.7	4.9	9.9	12.6
Oper. profit growth	10.4	10.2	10.8	13.0	15.6
COGS / Net sales	93.7	10.7	10.8	31.9	35.8
Overheads/Net sales	70.0	70.5	68.7	66.6	64.4
Depreciation / G. block	19.6	19.3	20.5	20.4	20.0
Effective interest rate	6.0	8.8	8.5	7.7	6.8
Net wkg.cap / Net sales	(0.02)	(0.02)	0.02	0.05	0.05
Net sales / Gr block (x)	3.5	5.5	4.9	4.3	3.9
RoCE	<b>42.1</b>	<b>39.0</b>	<b>33.2</b>	<b>35.0</b>	<b>37.7</b>
Debt / equity (x)	0.34	0.10	0.06	0.04	0.04
Effective tax rate	31.1	29.4	30.9	30.5	30.5
RoE	<b>35.9</b>	<b>31.1</b>	<b>25.2</b>	<b>26.1</b>	<b>27.6</b>
Payout ratio (Div/NP)	0.0	0.0	0.0	0.0	0.0
EPS (Rs.)	<b>32.2</b>	<b>25.6</b>	<b>27.4</b>	<b>36.8</b>	<b>51.0</b>
EPS Growth	145.4	(20.5)	7.1	34.3	38.5
CEPS (Rs.)	41.2	31.8	34.6	44.8	59.7
DPS (Rs.)	0.0	0.0	0.0	0.0	0.0

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SELL	Less than -10%

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