CRISIL RESEARCH

Independent Equity Research

Enhancing investment decisions

In-depth analysis of the fundamentals and valuation

KLRF Limited

CRISIL Independent Equity Research Team

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CRISIL's Equity Offerings

The Equity Group at CRISIL Research provides a wide range of services including:

- Independent Equity Research
- IPO Grading
- White Labelled Research
- Valuation on companies for use of Institutional Investors, Asset Managers, Corporate

Other Services by the Research group include

- CRISINFAC Industry research on over 60 industries and Economic Analysis
- Customised Research on Market sizing, Demand modelling and Entry strategies
- Customised research content for Information Memorandum and Offer documents

Explanation of CRISIL Fundamental and Valuation (CFV) matrix

The CFV Matrix (CRISIL Fundamental and Valuation Matrix) addresses the two important analysis of an investment making process – Analysis of Fundamentals (addressed through Fundamental Grade) and Analysis of Returns (Valuation Grade)

Fundamental Grade

CRISIL's Fundamental Grade represents an overall assessment of the fundamentals of the company graded in relation to other listed equity securities in India. The grade facilitates easy comparison of fundamentals between companies, irrespective of the size or the industry they operate in. The grading factors in the following:

- Business Prospects: Business prospects factors in Industry prospects and company's future financial performance
- Management Evaluation: Factors such as track record of the management, strategy are taken into consideration
- Corporate Governance: Assessment of adequacy of corporate governance structure and disclosure norms

The grade is assigned on a five-point scale from grade 5 (indicating Excellent fundamentals) to grade 1 (Poor fundamentals)

CRISIL Fundamental Grade	Assessment
5/5	Excellent fundamentals
4/5	Superior fundamentals
3/5	Good fundamentals
2/5	Moderate fundamentals
1/5	Poor fundamentals

Valuation Grade

CRISIL's Valuation Grade represents an assessment of the potential value in the company stock for an equity investor over a 12 month period. The grade is assigned on a five-point scale from grade 5 (indicating strong upside from the current market price (CMP)) to grade 1 (strong downside from the CMP).

CRISIL Valuation Grade	Assessment
5/5	Strong upside (>25% from CMP)
4/5	Upside (10-25% from CMP)
3/5	Align (+-10% from CMP)
2/5	Downside (negative 10-25% from CMP)
1/5	Strong downside (<-25% from CMP)

Analyst Disclosure

Each member of the team involved in the preparation of the grading report, hereby affirms that there exists no conflict of interest that can bias the grading recommendation of the company.

Additional Disclosure

This report has been sponsored by NSE - Investor Protection Fund Trust (NSEIPFT).

List of companies under coverage

Sl. No.	Report Date	Company Name	Sector	CMP	M. Cap (Rs. Mn)	Initiating Coverage Fundamental value	Initiating Coverage Fundamental grade	3QFY10 Update Fundamental value	3QFY10 Update Fundamental grade
1	02-Feb-10	Aarti Industries	Chemicals	49	3,757	56	3/5	56	3/5
2	31-Jan-10	ABG Shipyard	Shipping	315	10,286	242	3/5	259	3/5
3	01-Feb-10	Apollo hospitals	Hospitals	712	44,102	642	4/5	724	4/5
4	04-May-10	Beardsell Limited	Packaging/Expanded Polystyrene	64	245	54	3/5	-	-
5	06-Apr-10	Dhanuka Agritech Ltd	Pesticides	271	2,483	283	3/5	-	-
6	29-Jan-10	DLF	Real Estate	335	568,495	356	3/5	356	3/5
7	27-Jan-10	Dolphin Offshore	Oil & Gas	385	6,060	315	3/5	417	3/5
8	05-Feb-10	EID Parry	Sugar	348	30,050	394	4/5	395	4/5
9	01-Feb-10	Everest Kanto	Manufacturing	131	13,252	270	4/5	135	4/5
10	11-May-10	GKB Ophthalmics Ltd	Ophthalmic Lens	48	199	52	2/5	-	-
11	23-Feb-10	Havells India Ltd	Capital Goods	533	32,070	614	4/5	-	-
12	29-Jan-10	Hero Honda	Automobiles	1,889	377,240	1,747	5/5	1937#	5/5#
13	02-Mar-10	Hindusthan National Glass & Industries Ltd.	Packaging/Glass	240	21,049	314	4/5	-	-
14	13-May-10	Hydro S&S Industries Ltd.	Petrochemicals | Plastic Compounds	71.5	465	32.5	3/5	-	-
15	11-Feb-10	Indiabulls Securities	Financial Services	31	7,932	60	4/5	48	4/5
16	05-Feb-10	JBF Industries	Textiles	111	6,882	119	3/5	129	3/5
17	05-Feb-10	JM Financial	Financial Services	39	30,550	57	4/5	57	4/5
18	21-Jan-10	KKCL	Fashion and apparels	265	3,292	336	3/5	-	-
19	20-May-10	KLRF	Flour milling, yarn spinning, castings	32	161	35	2/5	-	-
20	01-Feb-10	KRBL	Agriculture/Rice	194	4,716	340	3/5	340	3/5
21	11-May-10	KSE Limited	Animal Feed	210	673	200	3/5	-	-
22	31-Jan-10	NTPC	Power	214	1,764,537	228	5/5	231	5/5
23	29-Jan-10	Pantaloon Retail (India)	Retail	406	77,282	*	4/5	*	4/5
24	04-Feb-10	Phoenix Mills	Real Estate	203	29,404	160	2/5	183	2/5
25	22-Apr-10	Polaris Software	Information Technology	186	18,407	247	4/5	-	-
26	19-Apr-10	Sangam (India) Ltd	Textiles	33	1,380	46	3/5	46	5/5
27	03-Feb-10	UTV Software	Media and Entertainment	498	17,066	548	3/5	538	3/5
28	07-May-10	Zylog System	Information Technology	456	7,494	530	3/5	-	-

CMP - Current Market Price (as on date of respective report)

M Cap - Market Capitalisation (as on date of respective report)

*NA - Not Applicable (Company has requested for a fundamental grading only)

Includes Q4FY10 result update

Independent Research Report - KLRF Ltd

Casting about for higher profitability

Industry: Wheat flour milling, textiles, castings
Date: May 21, 2010

CRISIL RESEARCH

Tamil Nadu-based KLRF (formerly known as Kovilpatti Laxmi Roller Flour Mills Ltd) is a small South India-focused player. It commenced operations in 1964 with the setting up of a roller flour mill. Over time, it has diversified into sheet metal fabrication, textiles and manufacturing of grey iron castings.

Success of castings business key to growth and profitability

KLRF entered the castings business through the acquisition of the loss-making Eltex Super Castings Ltd in 2007. We expect the company to turn around the business over the next two years, since: (a) Eltex Group's brand equity is intact; (b) the company has recruited senior staff from the castings industry to manage its operations; and (c) KLRF is well established in Coimbatore, the foundry capital of Tamil Nadu, which is the auto, pumps and valves, and electronics hub of southern India.

Flour milling, yarn segments lead to moderate growth and cash surplus

The company's wheat flour and cotton yarn businesses are now in a steady state of operations and are expected to continue to generate operating cash surplus. The company's flagship brand "Kuthuvilakku" enjoys premium pricing in the wheat flour markets of Tamil Nadu and Kerala. It claims a market share of ~15% in southern Tamil Nadu and Kerala. However, these businesses are low margin businesses and offer limited opportunities for growth.

Spindle overcapacity, power cuts limit growth and margins in yarn segment

CRISIL Research expects the overcapacity of spindles in southern India to impact players like KLRF. The company may not be able to pass on the complete price increase in cotton to its customers, thereby impacting margins. Tamil Nadu is a power deficit state and manufacturers are compelled to bear up to 30% power cuts, adversely affecting utilisation rates and sales volumes.

Revenues to grow to Rs 1.8 bn by FY12 at a two-year CAGR of 7.7%

We expect revenues to grow at a CAGR of 7.7% to Rs 1.8 bn in FY12 led by growth across business lines. EBITDA margin is expected to be 9.5% in FY12 vs. an estimated 9.2% in FY10. PAT margin is expected to turn positive in FY10 to 1.3% and rise to 2.2% in FY12. RoE is forecast at 16.1% in FY12, while EPS is expected to be Rs 7.9 in FY12.

Debt-equity ratio to improve to 2.2x by FY12 from 3.4x in FY10E

We expect KLRF's debt-equity ratio to improve from 3.4x in FY10E to 2.2x in FY12, considering higher cash flows from the castings division and steady stream of cash flows from the flour milling and textiles divisions.

We assign KLRF 2/5 on fundamentals and 3/5 on valuation

We assign KLRF a fundamental grade of **2/5**, indicating that its fundamentals are **'moderate'** relative to other listed securities in India. While an established brand in flour milling and expected revenue growth from the castings business positively influence our grading, the overall spindle overcapacity in Tamil Nadu, geographical concentration across business lines and paucity of power weigh down on our overall grade. CRISIL Equities has assigned a valuation grade of **3/5**, indicating that the fair value of the stock is aligned with the current market price of Rs 32 (as on May 20, 2010). Our one-year fair value for the stock is Rs 35.

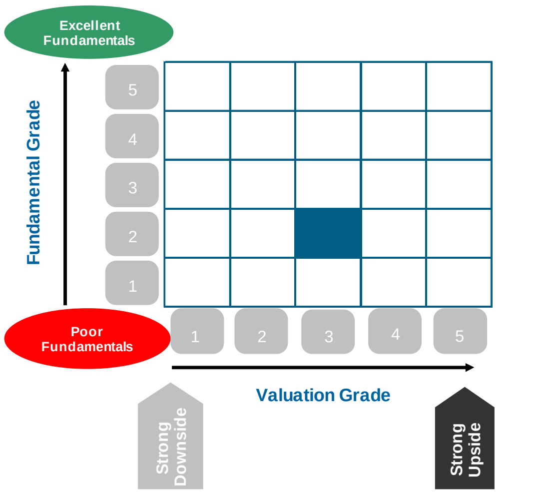
Key forecast

(Rs Mn)	FY08	FY09	FY10E	FY11F	FY12F
Operating income	1,403	1,423	1,553	1,694	1,802
EBITDA	124	70	144	167	171
Adj Net income	30	(43)	20	36	40
EPS-Rs	5.9	(8.7)	4.0	7.2	7.9
EPS growth (%)	78.6	n.m.	47.7	76.7	10.0
PE (x)	4.8	(1.5)	7.9	4.5	4.1
P/BV (x)	0.7	0.4	0.8	0.7	0.6
RoCE(%)	11.0	2.0	11.1	13.5	13.6
RoE(%)	15.6	(23.3)	11.4	17.3	16.1
EV/EBITDA (x)	7	10	6	5	4

n.m. - Not meaningful

Source: Company, CRISIL Equities Forecast

CFV Matrix



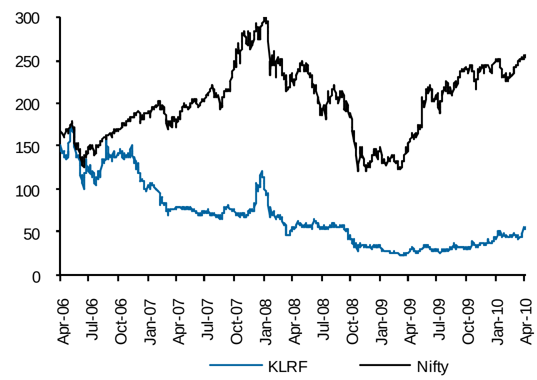
- Fundamental grade of '2/5 indicates moderate fundamentals
- Valuation grade of '3/5' indicates aligned valuation w rt CMP

Key stock statistics

NSE Ticker	KLRFLTD
Fair Value (Rs per share)	35
Current market price (Rs per share)*	32
Shares outstanding (Mn)	5.0
Market cap (Rs Mn)	161
Enterprise value (Rs Mn)	809
52-week range (Rs) (H/L)	36/14
P/E on EPS estimate (FY11F)	4.5
Beta	1.90
Free float (%)	60.98%
Average daily volumes	4,360

** as on May 20, 2010*

Share price movement



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Grading Rationale

Small player focused on the southern market

45-year-old flour-to-foundry player

KLRF commenced operations as a roller flour mill player in 1964. Over the years it has diversified into textiles, sheet metal fabrication and manufacturing of grey iron castings. It currently derives 50% of its revenues from flour milling, 33% from textiles and 17% from the engineering division (which includes sheet metal fabrication and ferrous castings). The company has been facing operational constraints in the textiles and engineering divisions on account of inadequate power supply.

Revenue break up for the past five years

	FY05	FY06	FY07	FY08	FY09
Food Division	49%	51%	55%	52%	50%
Textile Division	50%	49%	40%	32%	33%
Engineering Division	0%	0%	5%	16%	17%
Total Revenues (Rs mn)	**964**	**928**	**1,196**	**1,431**	**1,449**

Source: Company data

Success of castings business key to growth and profitability

Castings business – in the right place, at the wrong time

KLRF's engineering business comprises the sheet metal fabrication division (which is a small unit) and a foundry manufacturing grey iron castings. KLRF entered the business in 2007 with the acquisition of Eltex Super Castings Ltd, a sick unit formerly owned by a relative of the promoter. Under the former management, the company had enjoyed good patronage of its clients such as L&T Komatsu, Audco India Ltd, BHEL, TVS Group, Rane Group, Amalgamation Group and BEML among others. It was referred to the BIFR in 1998 owing to management issues and lack of working capital. After incurring a loss in FY09, the foundry has achieved break-even at the EBITDA level in FY10.

The installed capacity of the foundry is 7,200 tonnes per annum (TPA). Currently, 85% of the foundry's output comprises the low value-added raw castings and the balance is the higher-end machined castings, which offer better margins. Going forward, the management intends to increase the share of machined castings, leading to higher realisations and margins.

The company is well established in Coimbatore, the foundry hub of Tamil Nadu, which is the auto, pumps and valves, and electronics hub of southern India. To run the business, the company has appointed senior staff from the casting industry. Also, Eltex Group's brand equity is still intact, which is visible in the willingness of the old clients to resume business with the company. Hence, we believe that the company can turn around the division over the next couple of years. However, power will continue to be a cause for concern in Tamil Nadu. KLRF will also need to reduce its dependence on a few major clients, which currently poses a significant concentration risk. We expect revenue from the castings division to grow at 15.1% to Rs 336 mn in FY12 with EBITDA margins of 7.5%.

Castings industry snapshot

Statistics	
Estimated industry size	Rs 130 bn
Estimated production of castings	6.9 mn tonnes per annum produced by around 4,500 units
Market share	• 75% of the output is produced by 500 large and globally competitive players • 25% is produced by small-scale family-owned operations
Industry characteristics	• A majority of the large foundries are captive foundries with capacities ranging from 30,000 to 60,000 metric tonnes per annum and utilisation rates from 85% to 90%. They mainly cater to mass producers of engine blocks or related equipment in the automotive and agricultural equipment industries • Capacity utilisation of smaller players is around 55% and they cater to the local pumps and valves, automobile and textile industries
End use industries	Pumps/valves - 46% Food processing industry - 7% Textile machinery - 6% Electric motors - 6% Automotive - 4% Others - 31%

The foundry cluster of Coimbatore – An overview

Statistics	
Total capacity	30,000 tonnes per month
Exports	10% of output
Industry characteristics	• Good connectivity with all major industrial towns in India especially Chennai and Bangalore • Concentration of revenues with large customers leading to technological and transactional dependence as well as weak bargaining strength • Strong vertical linkages with suppliers, subcontractors and customers due to proximity to the local pumps industry and textile industry, which are the main customers • 60% of the units are proprietary concerns, the remaining partnership and private limited units are closely-held family concerns • 80% of the units use the old cupola system (metal melting system), due to which thermal efficiency is lower and pollution is higher • Most of the foundries are engaged in the manufacturing of low value raw castings

Flour milling – steady state ahead

Established flour milling business to ensure steady stream of revenues…

KLRF has a roller flour mill with installed capacity of 74,000 TPA. The main products include atta (wheat flour), maida (refined flour) and sooji (semolina), which are supplied in bulk to bakeries, parotta makers, etc. The company's flagship brand is "Kuthuvilakku", a premium brand in specific parts of Tamil Nadu and Kerala. As wheat flour is a low margin business, it can cater to markets within 150 kms of the plant location, beyond which high transportation costs renders it uneconomical. There are about 35 roller flour mills in Tamil Nadu with a cumulative installed capacity of 1.68 million TPA.

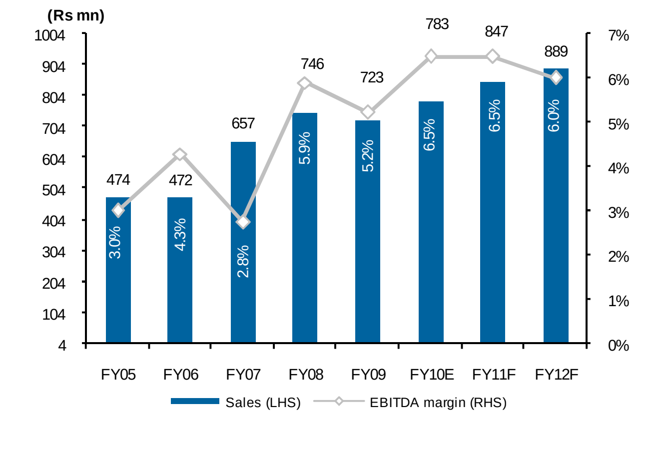
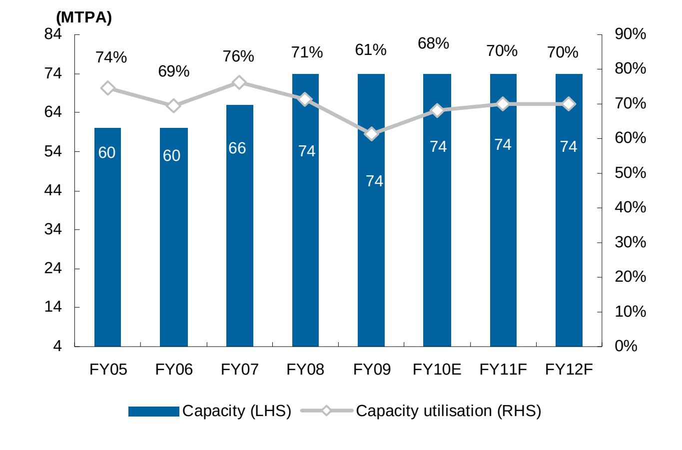
Wheat flour milling - Industry snapshot

Statistics	
Estimated industry size	1,000 roller flour mills having capacity of around 20 Million TPA per annum)
Estimated industrial production of flour milling products	12-14 Million TPA
Market concentration	▪ 20% organised. ▪ Balance wheat flour distributed through small chakki (unorganised) players
Industry characteristics	▪ Low value adding, volume-driven business ▪ Addressable market for a flour mill remains concentrated ▪ Cost of freight over distances longer than 200 km renders the product uncompetitive on pricing ▪ Demand for a particular variety of wheat flour product varies according to local tastes ▪ Limited entry barriers ▪ Limited pricing power
Key market for roller mill products in Tamil Nadu and Kerala	▪ Bakeries (for bread and biscuits) ▪ Parotta makers ▪ Hoteliers ▪ Confectioneries
Revenue drivers	▪ Steady market growth ▪ End market of wheat flour is price elastic in rural southern markets
Key competitors	Other small and medium sized regional players

…but less power means less flour

The demand for bread and biscuits is expected to grow at a CAGR of 10-15%, translating into growing demand for wheat flour. The company's current capacity utilisation is 70% and can operate at a maximum utilisation of ~80%, as switching between products necessitates a pause in production. To improve utilisation rates, the company has identified institutional sales to FMCG players such as Parle and Britannia. However, KLRF may have to be content with lower margins in this segment as it will have no pricing control over the FMCG giants.

We expect the flour milling business to grow at a two-year CAGR of 9% to Rs 889 mn in FY12. We anticipate the segment will have EBITDA margin of about 5.5-6%.

Milling revenue to grow, margins to remain low	Utilisation rate for flour milling to rise with demand
	
Source: Company data, CRISIL Equities estimate	Source: Company data, CRISIL Equities estimate

Yarn segment – overcapacity to squeeze margins

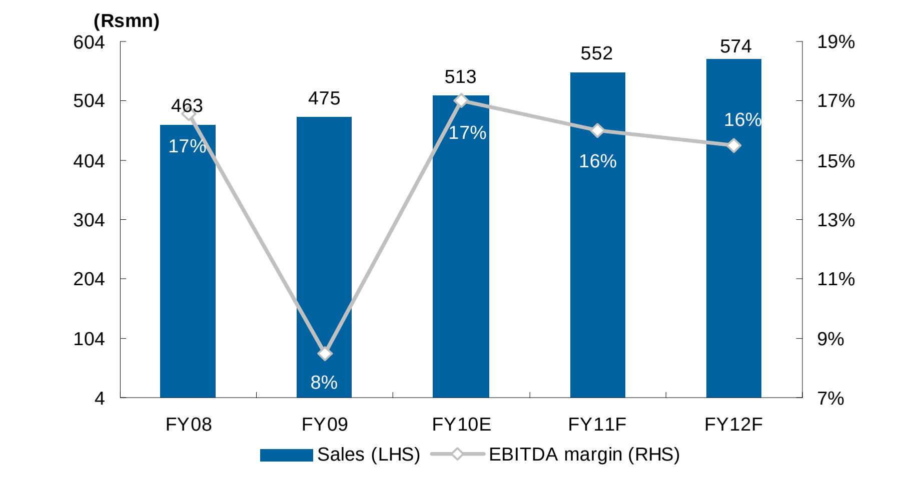
Too many spinners to spoil the margins in Tamil Nadu

KLRF's textile division manufactures cotton yarn which it markets primarily to clothing units in Maharashtra and Tamil Nadu. It exports a small quantity (3-5%) to East Asian countries such as Korea, Malaysia and Singapore. The company has an installed capacity of 29,520 spindles and 2,760 rotors.

The cotton yarn segment is a commodity play with 90% represented by unorganised small-scale units, which inherently restricts the company's ability to pass on the cotton price increases. Further, the operating rates in Tamil Nadu are constrained by high capacity and the power cuts imposed by the Tamil Nadu Electricity Board.

We expect revenues to grow at a two-year CAGR of 5.8% to Rs 574 mn by FY12 with EBITDA margin of 15.5%.

Higher sales due to higher yarn prices; EBIDTA margin to be constrained



Source: CRISIL Equities

High gearing limits growth potential

KLRF's capex cycle is behind it, strengthening of businesses key to profitability

KLRF's gearing is high at 3.4x in FY10 as a fall out of debt taken under TUFS (Technology Upgradation Fund Scheme) for expanding the textile business in FY06, and for acquiring the foundry business in FY08. The company's capex cycle is over and it is looking to stabilise its business over the next two-three years. Consequently, the debt-equity ratio is expected to decline to 2.2x in FY12, which is still high as the company operates in capital intensive industries. To fuel growth beyond this period, the company would have to resort to additional borrowing or equity dilution.

Shortage of electricity is a key concern for growth

The state of Tamil Nadu suffers from severe shortage of electricity. Companies do not get power for three hours daily during the peak hours. Over and above that, they need to choose between: (a) 60% power of the allotted KVA; or (b) eight days power cut during a month. CRISIL Research expects the power deficit to continue beyond FY12. Given the power intensive nature of businesses KLRF operates in, this is a key concern for growth. Alternatively, if the company wants to have continuous power it will have to incur additional capex, which it can ill afford.

Significant land reserves – a silver lining

KLRF's foundry is located on 12.3 acres of land in one of the prime industrial areas of Coimbatore, which could be valued in excess of Rs 200 mn. The company may choose to relocate the foundry to the outskirts of the city and sell the land, and infuse the resulting funds into the business. While the management is exploring such options, no concrete steps have been taken. If this materialises, the company will be able to expand its operations without additional equity or debt funds.

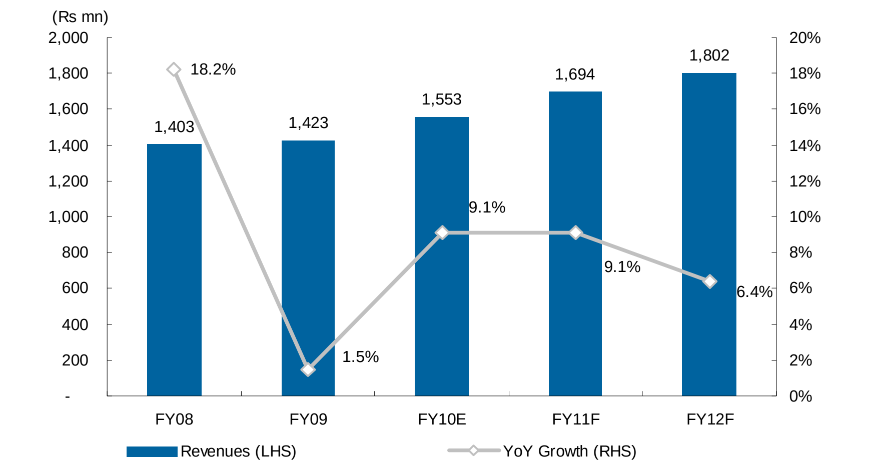
Financial Outlook

Revenues to grow to Rs 1.8 bn by FY12 at a two-year CAGR of 7.7%

Flour milling and textiles to experience steady growth, castings to augment top line

We expect KLRF's revenues to register a two-year CAGR of 7.7% to Rs 1.8 bn in FY12 from an estimated Rs 1.6 bn in FY10 (Rs 1.4 bn in FY09). The growth is expected to be led by steady rise in revenues from textiles and flour milling divisions, supported by rise in level of operations from the castings division.

Top line growth to be fuelled by castings business



Source: Company, CRISIL Equities estimate

EBITDA and PAT margins to remain range-bound

EBIDTA margin of castings business to lend little support to overall margin

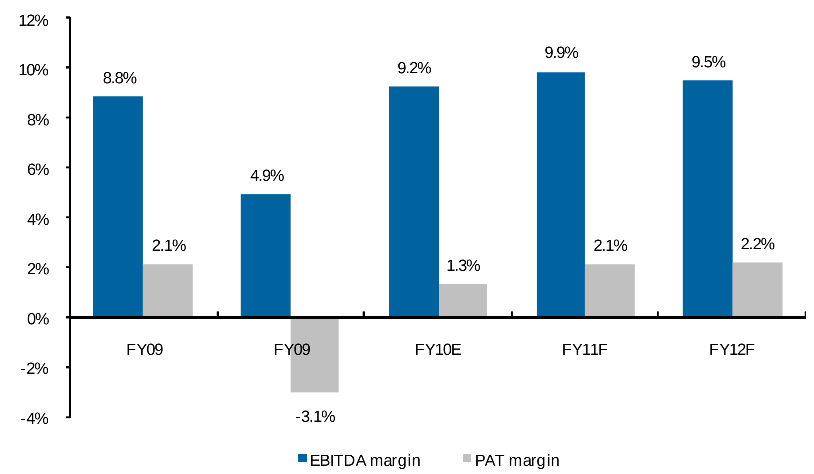
Overall PAT margin for KLRF turned negative in FY09 mainly due to a rise in cotton prices and a concurrent inability to pass on the higher costs to yarn customers due to overcapacity. Yarn prices have since recovered. PAT margins are estimated at 1.3% in FY10. They are expected to rise to 2.1% in FY11 and 2.2% in FY12.

We expect EBIDTA margin in the low value-added flour milling division to remain at about 5.5-6.5%. For the castings division, we expect it to rise from an estimated 0.9% in FY10 to 7.5% in FY12 as the foundry enters the business-as-usual phase of operations.

EBIDTA margin for the textiles business has improved from 8.5% in FY09 to an estimated 17% in FY10. It is likely to remain between 15% and 16% thereafter in line with a recovery in demand for textiles.

Overall EBIDTA margin for KLRF is expected to rise from an estimated 9.2% in FY10 to 9.9% in FY11 and 9.5% in FY12.

PAT margin to turn positive in FY10, to rise thereafter



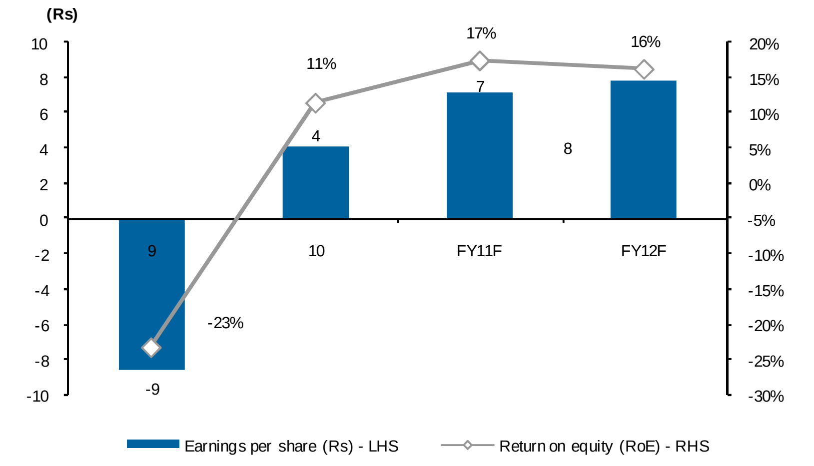
Source: Company, CRISIL Equities estimate

EPS to register a two-year CAGR of 39% to be Rs 17.9 in FY12

EPS to rise in line with revenues and PAT

We expect KLRF to earn Rs 7.9 per share in FY12 from an estimated Rs 4.0 in FY10, registering a two-year CAGR of 39%. During the same time, we expect the company's RoE to increase from an estimated 11.4% in FY10 to 16.1% in FY12.

EPS and ROE to be higher



Source: Company, CRISIL Equities estimate

Management Overview

CRISIL's fundamental grading methodology includes a broad assessment of management quality, apart from other key factors such as industry and business prospects, and financial performance.

Established, family-driven business

Mr V. Jagannathan (71 years old) started the company in 1961 with the setting up of a flour milling unit in the Tirunelveli district of Tamil Nadu. A textile engineer by qualification, he was an employee of Laxmi Mills Company (LMC), a vertically integrated textile manufacturing company. The unit commenced operations while he was still employed. He later discontinued active service to grow the business. His son, Mr Suresh Jagannathan (52) has been involved in the business since the early 80s**.** He is currently the Managing Director and chief decision maker. Mrs Chandrakanthi, Mr V.Jagannathan's wife, is also actively involved in the administration of the food and textiles divisions.

Management has domain expertise in flour milling and textiles

The management team for the food and textiles divisions comprises qualified personnel who have been associated with KLRF for a long period of time. For the castings business, the company has recruited experienced industry professionals. The systems and processes are adequate for the current level of the company's operations.

Unrelated diversification = low synergies

Unrelated diversification makes little business sense

Since inception, KLRF has diversified into low value-adding businesses. The management identified the castings business in order to reduce its dependence on commoditized businesses. However, it may face significant challenges in achieving the desired scale of operations since it has no experience in the business and power is expected to continue to constrain operations. Further, the ability to graduate to the more value-accretive machined castings will require investments in designing and equipment; the inability to do so, may cause margins to remain low. Also, the management has diversified the business into unrelated segments, offering low synergies.

Corporate Governance

CRISIL's fundamental grading methodology includes a broad assessment of corporate governance and management quality, apart from other key factors such as industry and business prospects, and financial performance. CRISIL Equities also analysed the company's shareholding structure, board composition, typical board processes, disclosure standards and related-party transactions. Any qualifications by regulators or auditors also serve as useful inputs while assessing corporate governance.

Board composition and processes meet minimum standards

KLRF adheres to minimum corporate governance standards

KLRF's board comprises seven directors, four of whom are independent. In addition to Mr Suresh Jagannathan (MD) and his mother Mrs J. Chandrakanthi (Vice Chairman), the rest of the board comprises qualified professionals who have also been associated with the company for a long time.

The minimum corporate governance standards are reflected in the board's constitution and by the presence of audit and other committees, which support the board processes. Based on balance sheet disclosures, attendance record of independent directors and their level of engagement in company affairs, it appears that corporate governance meets the minimum standards.

Group company in flour milling business creates conflict of interest

Cape Flour Mills Pvt Ltd is a 100% promoter-owned company in Nagercoil, Kanyakumari engaged in flour milling. Its revenues are approximately half of that of KLRF's flour milling division. Cape is currently utilising the "Kuthuvillaku" trademark under licence from KLRF for wheat flour and operates in different geography.

Valuation Grading Grade:3/5

We have valued KLRF's business using the discounted free cash flow to firm method (DCF). Based on the DCF method, we believe the fair value of KLRF's businesses to be Rs 35 per share. We initiate our coverage on KLRF with a valuation grade of **3/5.** This grade indicates that the current market price of KLRF is aligned with the fair value of Rs.35.

The following are the key factors in our valuation:

- We have considered discounted free cash flows from FY10 to FY16.
- We have assumed a target debt-equity ratio of 0.35.
- We have assumed terminal growth rate of 3%, equity risk premium of 6% and risk-free rate of return of 7%.
- Due to low trading volumes, a higher cost of equity of 18.4% has been assigned.
- We have assumed beta of 1.9.

Below is the sensitivity table of fundamental value to assumptions of WACC and terminal growth rate:

WACC	Terminal growth rate				
	1.0%	2.0%	3.0%	4.0%	5.0%
12.3%	43	53	66	81	100
13.3%	31	39	49	61	75
14.3%	21	27	35	44	56
15.3%	12	18	24	32	40
16.3%	5	10	15	21	28

Company overview

KLRF is a diversified player with presence in three business segments – wheat flour milling, textiles and engineering (which includes sheet metal fabrication and castings). KLRF commenced operations with a flour milling unit in the Tirunelveli district of Tamil Nadu in 1964. It markets its flour under the brand "Kuthuvilakku" which is fairly well known in Tamil Nadu.

The company established an engineering division in 1978 for the manufacturing of sheet metal products to cater to the requirements of textile machinery and other capital goods manufacturers. The sheet metal unit was started as a sub-contracting plant for Laxmi Machine Works (LMW). It still derives most of its revenues from LMW. Its share in the overall revenues is negligible.

Building on Mr V. Jagannathan's experience in textiles, the company forayed into textiles in 1982 with a cotton textile spinning unit located next to the flour mill. It started with a capacity of 12,000 spindles which was subsequently expanded to 29,520 spindles. In 1988, a second textile mill was commissioned in the Virudunagar district of Tamil Nadu. It was an open-end spinning unit with 672 rotors. Subsequently, the capacity was expanded to 2,760 rotors.

To increase revenues from the engineering division, KLRF acquired Eltex Super Castings Ltd, a foundry belonging to the promoter's brother and located next to the Sheet Metal division. The company was referred to the BIFR following management issues. It had the requisite licences and environmental clearances, which made it a good takeover target for KLRF.

Year	Milestone
1964	Commencement of commercial production from flour milling unit
1978	Commencement of operations of the Sheet Metal division
1982	Public listing of the company on BSE
1982	Start of commercial production of Textile unit I
1988	Start of commercial production of Textile unit II
1995	Start of windmill division
2007	Substantial acquisition in Eltex Super Castings
2007	Follow on Public Offer for dilution of 32% stake

Source: Company reports

The company has been listed on the BSE since 1982. It undertook a follow-on public offer in 2007 for dilution of 31.7% of the promoter's holding, for revamping the foundry.

Business overview

KLRF's main business is to manufacture and distribute wheat flour, cotton yarn and grey iron castings.

Flour milling - Wheat flour (mainly maida), produced from roller flour mills, is used in the preparation of parottas (a South Indian bread), and in bread and biscuits. The main customers of KLRF are bakeries and parotta makers. The products are sold through dealers and agents in Tamil Nadu and Kerala. A small portion of retail sales are made to the local markets in South Tamil Nadu and South Kerala. It does not intend to enter the retail segment in a big way since it faces competition from MNCs and other established domestic brands in this segment.

Textiles - The textile division at Gangaikondan has a capacity of 29,520 ring spindles. The company has the facility to manufacture ring spun yarn from 30s to 100s counts. The superfine counts ranging from 92s to 100s are used to manufacture high quality fabrics. The yarn is sold through depots and agents who have been associated with the company since the inception of the textile mill in 1982. The cotton yarn manufactured in unit II ranges from 6s to 20s and is mostly used to manufacture home furnishing fabrics.

The entire plant and machinery for the unit has been supplied by LMW. The unit also manufactures hosiery yarn, which is used for knitted garments. The company supplies to various knitting fabric manufacturers in Tirupur.

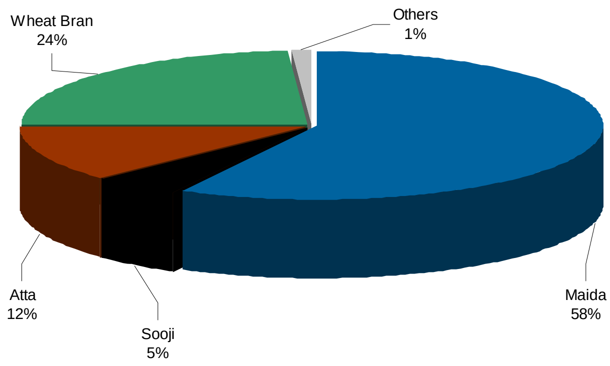
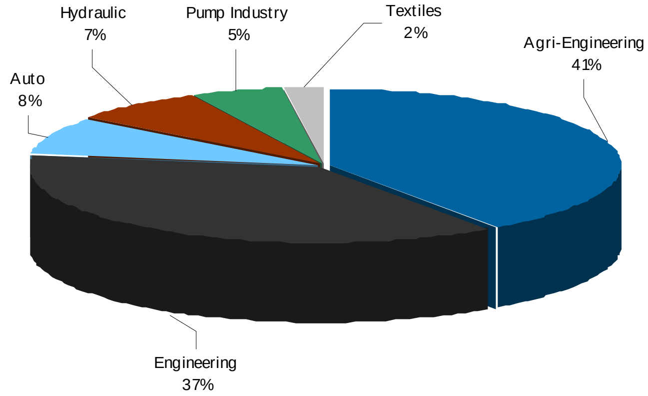
Engineering

Sheet metal fabrication – This unit is involved in the manufacturing of sheet metal fabrication, involving simple engineering processes of cutting, notching, welding and surface treatment of cold rolled steel sheets.

Grey iron castings – This new line of business was identified due to:

1. Proximity of foundry to pumps and valves, and auto industry players in Tamil Nadu.
2. Capacity enhancements by general engineering units like pump and valve manufacturers.
3. Developing export potential due to closure of foundry units in the European Union and America due to environmental issues.
4. Entry of new units in this sector is limited due to considerable delay in getting pollution control approvals.

The foundry has an installed capacity of 7,200 tpa and it operated at a utilisation rate of 58% in FY10. Currently, the top three clients account for around 50% of the company's revenues from castings.

Wheat flour – Break-up of revenues	Castings – Break-up of revenues
	
Source: Company data, CRISIL Equities estimate	Source: Company data, CRISIL Equities estimate

Windmills – KLRF has set up windmills in the Kanyakumari and Tirunelveli districts of Tamil Nadu to cater to its captive requirements of power. The total installed capacity of the windmills is 6.25 MW.

Annexure: Financials

Income Statement

(Rs Mn)	FY08	FY09	FY10F	FY11F	FY12F
Net sales	1,401	1,420	1,550	1,690	1,799
Operating Income	**1,403**	**1,423**	**1,553**	**1,694**	**1,802**
EBITDA	**124**	**70**	**144**	**167**	**171**
Depreciation	42	53	50	52	53
Interest	54	70	66	65	62
Other Income	5	3	3	3	3
PBT	**33**	**(50)**	**30**	**54**	**59**
PAT	**30**	**(43)**	**20**	**36**	**40**
No. of shares	5	5	5	5	5
Earnings per share (EPS)	**5.9**	**(8.7)**	**4.0**	**7.2**	**7.9**

Balance Sheet

(Rs Mn)	FY08	FY09	FY10F	FY11F	FY12F
Equity (Including reserves)	205	169	189	225	265
Debt	684	657	657	637	607
Current Liabilities and Provisions	108	78	81	88	99
Deferred Tax Liability/(Asset)	(2)	(10)	(10)	(10)	(10)
Capital Employed	**995**	**894**	**917**	**940**	**960**
Net Fixed Assets	394	390	365	338	310
Capital WIP	8	17	17	17	17
Loans and advances	76	98	107	117	124
Inventory	376	243	265	289	308
Receivables	134	137	150	163	174
Cash & Bank Balance	6	8	13	16	28
Applications of Funds	**995**	**894**	**917**	**940**	**960**

Cash Flow

(Rs Mn)	FY08	FY09	FY10F	FY11F	FY12F
Pre-tax profit	33	(50)	30	54	59
Total tax paid	(2)	(1)	(10)	(18)	(19)
Depreciation	42	53	50	52	53
Change in working capital	(197)	78	(40)	(40)	(26)
Cash flow from operating activities	**(124)**	**80**	**31**	**48**	**67**
Capital expenditure	(142)	(59)	(25)	(25)	(25)
Cash flow from investing activities	**(142)**	**(59)**	**(25)**	**(25)**	**(25)**
Equity raised/(repaid)	-	-	-	-	-
Debt raised/(repaid)	256	(27)	-	(20)	(30)
Dividend (incl. tax)	(12)	-	-	-	-
Cash flow from financing activities	**244**	**(27)**	**-**	**(20)**	**(30)**
Change in cash posiiton	**(23)**	**(6)**	**6**	**3**	**12**
Opening Cash	19	6	8	13	16
Closing Cash	(4)	0	13	16	28

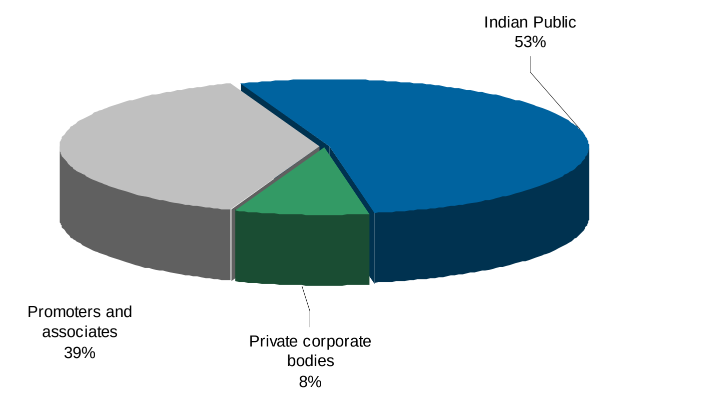
Ratios

	FY08	FY09	FY10F	FY11F	FY12F
Growth ratios					
Sales growth (%)	18.2	1.5	9.1	9.1	6.4
EBITDA growth (%)	14.0	(43.4)	104.4	16.4	2.4
EPS growth (%)	78.6	(246.7)	47.7	76.7	10.0
Profitability Ratios					
EBITDA Margin (%)	8.8	4.9	9.2	9.9	9.5
PAT Margin (%)	2.1	(3.1)	1.3	2.1	2.2
Return on Capital Employed (RoCE) (%)	11.0	2.0	11.1	13.5	13.6
Return on equity (RoE) (%)	15.6	(23.3)	11.4	17.3	16.1
Dividend and Earnings					
Dividend per share (Rs)	2.3	0.0	0.0	0.0	0.0
Dividend payout ratio (%)	39.6	0.0	0.0	0.0	0.0
Dividend yield (%)	8.2	-	-	-	-
Earnings Per Share (Rs)	5.9	-8.7	4.0	7.2	7.9
Efficiency ratios					
Asset Turnover (Sales/GFA)	1.8x	1.6x	1.7x	1.8x	1.9x
Asset Turnover (Sales/NFA)	4.0x	3.6x	4.1x	4.8x	5.6x
Sales/Working Capital	3.7x	3.2x	3.7x	3.7x	3.7x
Financial stability					
Net Debt-equity	3.3	3.8	3.4	2.8	2.2
Interest Coverage	1.5	0.2	1.4	1.8	1.9
Current Ratio	5.5	6.3	6.6	6.6	6.4
Valuation Multiples					
Price-earnings	4.8x	-1.5x	7.9x	4.5x	4.1x
Price-book	0.7x	0.4x	0.8x	0.7x	0.6x
EV/EBITDA	6.6x	10.2x	5.6x	4.7x	4.3x

Source: Company, CRISIL Estimates

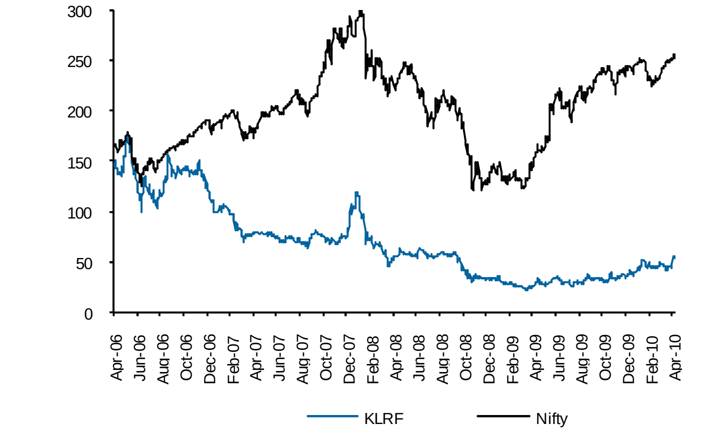
Focus Charts

Shareholding pattern



Source: BSE

Share Price movement



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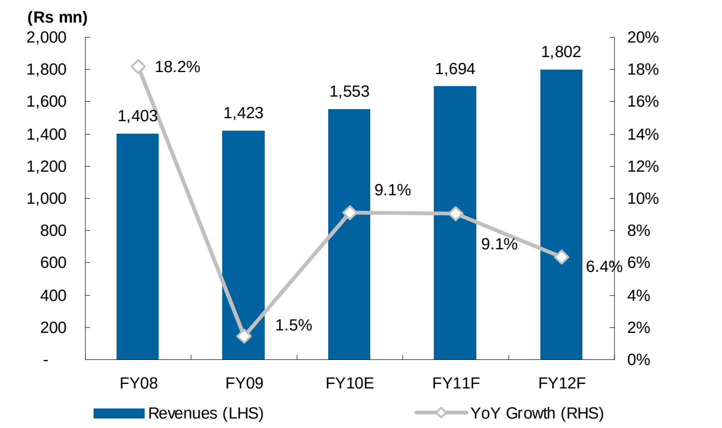
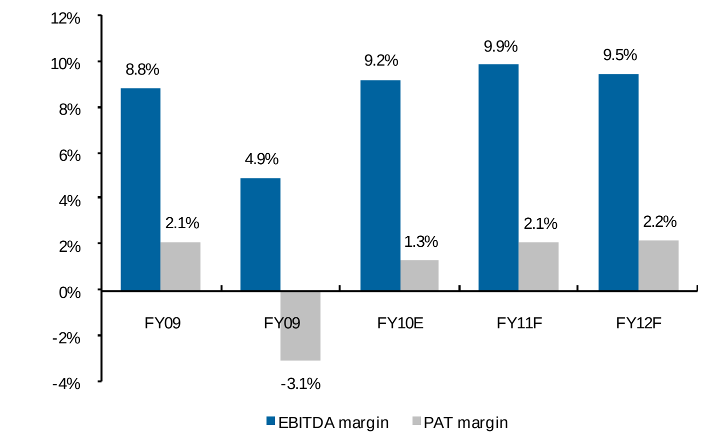
Top line growth to be fuelled by castings business



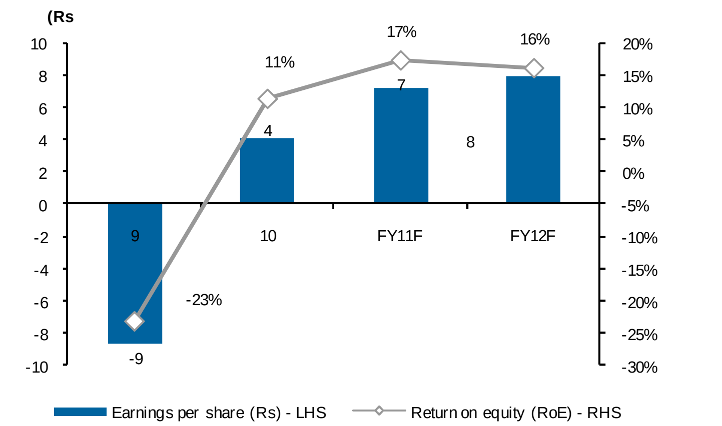
Source: Company, CRISIL Equities estimate

PAT margin to turn positive in FY10, to rise thereafter



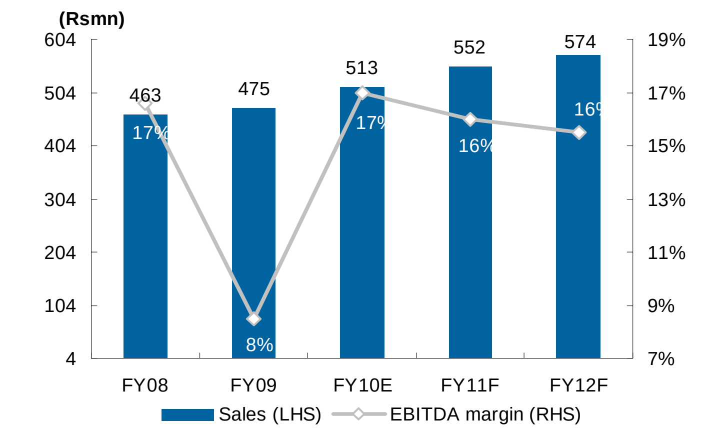
Source: Company, CRISIL Equities estimate

EPS and ROE to be higher



Source: Company, CRISIL Equities estimate

Yarn segment to clock higher sales; EBIDTA margin for yarn to be constrained



Source: CRISIL Equities

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