

## BRITANNIA INDUSTRIES

FMCG

# BUY

Target Price: Rs 5,300

### Category growth revives; steps up launches

Britannia will launch 50 products by FY19 and step up intensity in adjacent categories to become a total food company. We continue to like the snacking space given its higher growth, but more importantly we are comfortable with the way the management is steering Britannia. While margin tailwinds from benign raw material cost remain, intensity of competition remains the key. We upgrade to **BUY** with TP of Rs 5,300 based on forward P/E of 42x. We justify a higher-than-usual target P/E given the 20% EPS CAGR over FY17-20E.

**Q3FY18 in line:** Consolidated net sales, EBITDA and adjusted PAT grew 13%, 27% and 20% (vs. consensus estimates of 13%, 27% and 22%). Domestic sales grew 15% YoY on 13% volume growth. Gross margin improved 111 bps YoY at 38.5% on benign input cost. EBITDA margin was up 175 bps YoY at 15.5%.

CMP : Rs 4,759  
Potential Upside : 11%

#### MARKET DATA

No. of Shares : 120 mn  
Free Float : 49%  
Market Cap : Rs 571 bn  
52-week High / Low : Rs 4,964 / Rs 3,052  
Avg. Daily vol. (6mth) : 175,135 shares  
Bloomberg Code : BRIT IB Equity  
Promoters Holding : 51%  
FII / DII : 18% / 12%

### Management commentary

- ◆ **Segment performance:** Standalone sales grew 15% YoY in Q3. Domestic volume growth stood at 13%. Bread sales grew in double digits (aided by low base) with improved profitability. International business remained muted with deteriorating geopolitical situation and currency fluctuations. Dairy segment continued to be impacted by strategic call to reduce mix of low-margin offerings
- ◆ **Biscuits category growth likely to accelerate:** Management attributed volume growth recovery in Q3FY18 to revival in category growth. It hopes category growth be back to 9-10% in coming quarters
- ◆ **To step up product launch intensity:** As part of its efforts to be a total food company, Britannia aims to launch 50 new products under its existing as well as new categories by end FY19. It does not expect stepped-up launch intensity to impact margin materially
- ◆ **Input cost inflation was flat in Q3:** However, inflation is expected to be ~3-3.5% for FY19. For next three months, Britannia does not envisage any price action

### Financial summary (Consolidated)

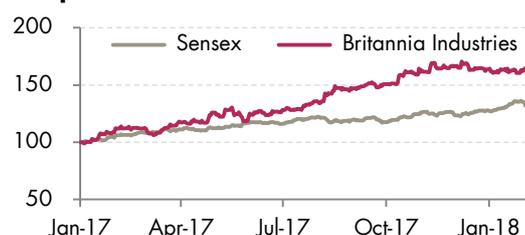
Y/E March	FY17	FY18E	FY19E	FY20E
Sales (Rs mn)	89,623	98,688	112,537	128,169
Adj PAT (Rs mn)	8,845	10,201	12,560	15,236
Con. EPS* (Rs)	-	84.4	102.2	123.3
EPS (Rs)	73.7	84.8	104.2	126.2
Change YOY (%)	7.3	15.1	22.9	21.1
P/E (x)	64.6	56.1	45.7	37.7
RoE (%)	36.9	33.5	32.7	31.6
RoCE (%)	52.7	49.1	47.1	45.3
EV/E (x)	44.3	37.0	31.5	26.1
DPS (Rs)	22.0	26.0	30.0	34.0

Source: \*Consensus broker estimates, Company, Axis Capital, CMP as on 14 FEB 2018

### Key drivers

(%)	FY18E	FY19E	FY20E
Standalone revenue growth	10.7	14.0	13.8
Standalone OPM	15.3	15.7	16.4
Subsidiaries revenue growth	-0.1	14.4	14.3
Subsidiaries OPM	13.4	13.5	13.5

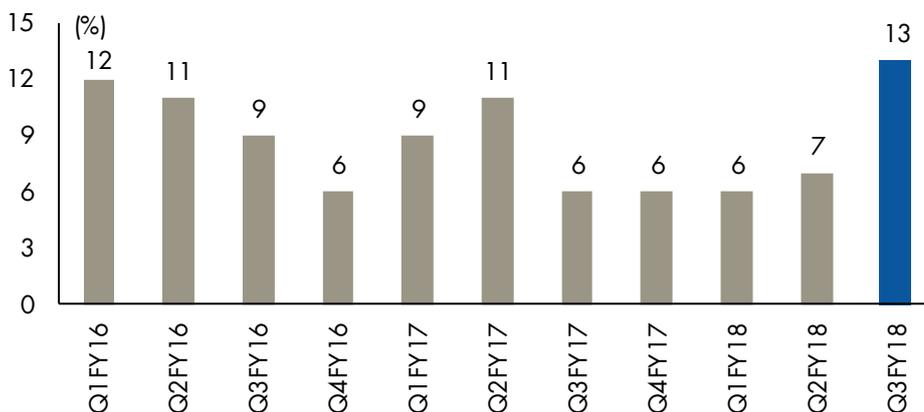
### Price performance



## Conference call highlights

- ◆ **Biscuits category growth likely to accelerate:** Management attributed volume growth recovery in Q3FY18 (volume growth stood at 13% for Britannia) to revival in category growth. It hopes category growth to be back to 9-10% in coming quarters. Premium segment, where share of organized is high, has posted good growth. However, in value segment, the growth remains muted as some players are not playing by rules. While industry mix is 55% in premium and 45% in value, Britannia's mix is 75% in premium and 25% in value. Management highlighted as the value segment does play material role in its portfolio, it is not looking to expand its share in it

### Exhibit 1: Quarterly volume growth



Source: Company, Axis Capital

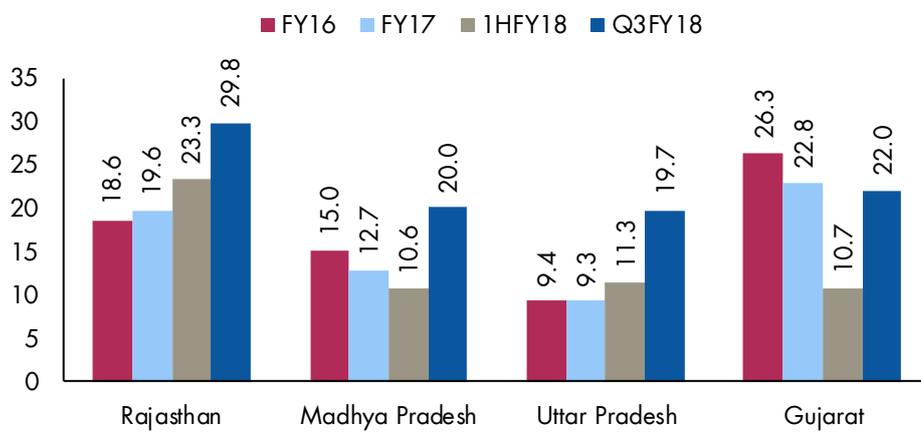
- ◆ **Focus area:** Company continues to aim at profitable growth on
  - a) Premiumization and innovation – in Q3, *Pure Magic Deuce Choco* and *vanilla* launched and revamped *Good Day Chocolate*
  - b) Distribution expansion – Direct reach expanded 2.5x since FY14 to 1.75 mn outlets, rural continue to grow in double digits and growth in weak states accelerated in Q3
  - c) Cost leadership – Total savings of Rs 2.3 bn from reduction in distance travelled, new and larger factories for efficiency, reduction in wastage and value engineering in FY18
  - d) Leveraging fixed costs
- ◆ **To step up product launch intensity:** As a part of efforts to be a total food company, Britannia aims to launch 50 products under its existing as well as new categories by end FY19. Of this, ~15 products are already in the market. Management does not see any material margin impact on stepped-up launch intensity, as most of the offerings are under existing segments. Croissants launch is likely by Oct-18. Dairy pilot going in Maharashtra near Ranjangaon, where with right scale and output it will take call to move forward. In macro snacking area, the company will look into new and differentiated offerings
- ◆ **Looking for apt partner to expand franchise in dairy segment:** Real intent is to have complete control of the entire process – from collection of fresh milk to processing to introduction of value-added products (such as cheese deserts, cheese rolls and lollypops). The company is hopeful of some confirmation in next three to four months to this end. Management is clear in its strategy to be present only in the premium end (closed market for International players give

“Almost 50 new products would be there by the end of next financial year,”  
- Varun Berry, MD, Britannia

high import duty rates). The company aims four-fold rise in revenue from Rs 4 bn now to ~ Rs15 bn in next five years. Given high gestation period for the business, product launches likely in FY20. Its bulk of dairy business is from liquid milk, which it is defocusing area given the limited margin. Given limited knowhow in the space, it will look to partner with international players who can help bring new offerings in the premium end

- ◆ **Weak state agenda working well.** Uttar Pradesh growth is now in line with management's expectation (growing at 20%, vs. earlier growth below management expectation). Growth momentum in other states continues; Rajasthan growth accelerates to 30%, Madhya Pradesh to 20% and Gujarat to 22%

### Exhibit 2: Weak state growth



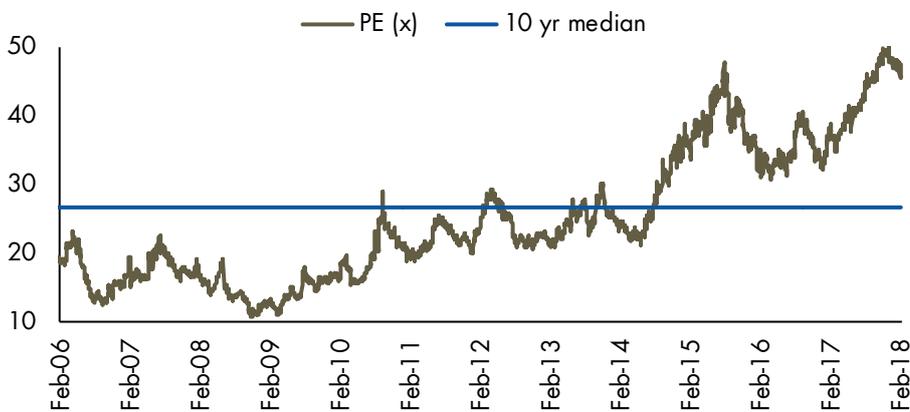
Source: Company, Axis Capital

- ◆ **Higher effective tax rate (up 280 bps YoY to 33.7%)** lowered PAT growth to 20% in Q3. Management highlighted that lower investment allowances (15% on investment in plant and machinery and 200% of R&D was available till FY17) pushed tax rate up
- ◆ **Treat likely to move to be a power brand.** In media interactions, management highlighted that the premium portfolio drove the domestic volume growth. With integration of cream biscuits under *Treat*, the company views *Treat* to be one of the power brand along with *Good Day*, *Marie Gold*, *Tiger*, *50:50* and *NutriChoice*

**Exhibit 3: Results update (Consolidated)**

(Rs. mn)	Quarter ended				
	Dec-17	Dec-16	% Chg	Sep-17	% Chg
<b>Net sales</b>	<b>25,583</b>	<b>22,648</b>	<b>13.0</b>	<b>25,365</b>	<b>0.9</b>
Other operating income	92	172	(46.6)	88	4.8
<b>Total revenues</b>	<b>25,675</b>	<b>22,820</b>	<b>12.5</b>	<b>25,453</b>	<b>0.9</b>
Raw material cost	15,745	14,190	11.0	15,840	(0.6)
(% of net sales)	61.5	62.7	-111 bps	62.2	-69 bps
Staff expenditure	936	882	6.1	900	4.0
(% of net sales)	3.6	3.9	-22 bps	3.5	11 bps
Other expenses	5,010	4,605	8.8	4,766	5.1
(% of net sales)	19.5	20.2	-67 bps	18.7	79 bps
<b>EBITDA</b>	<b>3,984</b>	<b>3,142</b>	<b>26.8</b>	<b>3,947</b>	<b>0.9</b>
EBITDA margin (%)	15.5	13.8	175 bps	15.5	1 bps
Other income	359	372	(3.4)	508	(29.3)
<b>PBITD</b>	<b>4,343</b>	<b>3,514</b>	<b>23.6</b>	<b>4,455</b>	<b>(2.5)</b>
Depreciation	329	303	8.7	336	(2.2)
Interest	26	11	131.8	14	82.1
<b>PBT</b>	<b>3,989</b>	<b>3,201</b>	<b>24.6</b>	<b>4,104</b>	<b>(2.8)</b>
Tax	1,354	997	35.8	1,326	2.1
Minority interest	(1)	(1)	-	(2)	-
<b>Adjusted PAT</b>	<b>2,636</b>	<b>2,205</b>	<b>19.6</b>	<b>2,781</b>	<b>(5.2)</b>
Extraordinary items	0	0	-	(170)	-
<b>Reported PAT</b>	<b>2,636</b>	<b>2,205</b>	<b>19.6</b>	<b>2,611</b>	<b>1.0</b>

Source: Company, Axis Capital

**Exhibit 4: 1-year forward PE (on consensus EPS)**


Source: Bloomberg, Axis Capital

## Financial summary (Consolidated)

### Profit & loss (Rs mn)

Y/E March	FY17	FY18E	FY19E	FY20E
<b>Net sales</b>	<b>89,623</b>	<b>98,688</b>	<b>112,537</b>	<b>128,169</b>
Other operating income	918	825	903	983
<b>Total operating income</b>	<b>90,541</b>	<b>99,513</b>	<b>113,440</b>	<b>129,152</b>
Cost of goods sold	(55,887)	(61,095)	(69,205)	(78,531)
Gross profit	34,654	38,419	44,235	50,621
<i>Gross margin (%)</i>	<i>38.7</i>	<i>38.9</i>	<i>39.3</i>	<i>39.5</i>
Total operating expenses	(21,872)	(23,269)	(26,626)	(29,649)
<b>EBITDA</b>	<b>12,782</b>	<b>15,150</b>	<b>17,609</b>	<b>20,971</b>
<i>EBITDA margin (%)</i>	<i>14.3</i>	<i>15.4</i>	<i>15.6</i>	<i>16.4</i>
Depreciation	(1,193)	(1,329)	(1,335)	(1,583)
<b>EBIT</b>	<b>11,589</b>	<b>13,821</b>	<b>16,274</b>	<b>19,388</b>
Net interest	(55)	(55)	(60)	(65)
Other income	1,505	1,614	2,268	2,901
<b>Profit before tax</b>	<b>13,040</b>	<b>15,381</b>	<b>18,482</b>	<b>22,223</b>
Total taxation	(4,197)	(5,180)	(5,922)	(6,987)
<i>Tax rate (%)</i>	<i>32.2</i>	<i>33.7</i>	<i>32.0</i>	<i>31.4</i>
Profit after tax	8,843	10,201	12,560	15,236
Minorities	(1)	-	-	-
Profit/ Loss associate co(s)	3	-	-	-
<b>Adjusted net profit</b>	<b>8,845</b>	<b>10,201</b>	<b>12,560</b>	<b>15,236</b>
<i>Adj. PAT margin (%)</i>	<i>9.9</i>	<i>10.3</i>	<i>11.2</i>	<i>11.9</i>
Net non-recurring items	-	-	-	-
<b>Reported net profit</b>	<b>8,845</b>	<b>10,201</b>	<b>12,560</b>	<b>15,236</b>

### Balance sheet (Rs mn)

Y/E March	FY17	FY18E	FY19E	FY20E
Paid-up capital	240	241	241	242
Reserves & surplus	26,724	33,748	42,556	53,454
Net worth	26,964	33,988	42,797	53,696
Borrowing	1,157	1,153	1,153	1,153
Other non-current liabilities	(231)	(231)	(231)	(231)
<b>Total liabilities</b>	<b>27,916</b>	<b>34,940</b>	<b>43,753</b>	<b>54,657</b>
Gross fixed assets	13,275	16,325	19,625	23,175
Less: Depreciation	(1,675)	(3,004)	(4,339)	(5,923)
Net fixed assets	11,600	13,321	15,286	17,252
Add: Capital WIP	301	103	103	103
Total fixed assets	11,901	13,424	15,389	17,355
Total Investment	4,869	2,411	2,391	2,358
Inventory	6,615	6,418	7,175	8,017
Debtors	1,792	1,918	2,136	2,506
Cash & bank	1,208	9,866	15,445	22,807
Loans & advances	8,750	9,824	11,027	12,376
Current liabilities	12,941	15,440	17,242	19,245
Net current assets	11,147	19,104	25,973	34,944
Other non-current assets	-	-	-	-
<b>Total assets</b>	<b>27,916</b>	<b>34,940</b>	<b>43,753</b>	<b>54,657</b>

Source: Company, Axis Capital

### Cash flow (Rs mn)

Y/E March	FY17	FY18E	FY19E	FY20E
Profit before tax	13,040	15,381	18,482	22,223
Depreciation & Amortisation	1,193	1,329	1,335	1,583
<i>Chg in working capital</i>	<i>(4,514)</i>	<i>127</i>	<i>(1,876)</i>	<i>(2,198)</i>
<b>Cash flow from operations</b>	<b>4,286</b>	<b>10,042</b>	<b>9,751</b>	<b>11,722</b>
<i>Capital expenditure</i>	<i>(3,518)</i>	<i>(2,852)</i>	<i>(3,300)</i>	<i>(3,550)</i>
<b>Cash flow from investing</b>	<b>(1,499)</b>	<b>1,219</b>	<b>(1,012)</b>	<b>(616)</b>
<i>Equity raised/ (repaid)</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Debt raised/ (repaid)</i>	<i>(70)</i>	<i>(4)</i>	<i>-</i>	<i>-</i>
<i>Dividend paid</i>	<i>(2,884)</i>	<i>(3,178)</i>	<i>(3,752)</i>	<i>(4,338)</i>
<b>Cash flow from financing</b>	<b>(2,951)</b>	<b>(2,603)</b>	<b>(3,161)</b>	<b>(3,744)</b>
Net chg in cash	(163)	8,658	5,579	7,362

### Key ratios

Y/E March	FY17	FY18E	FY19E	FY20E
<b>OPERATIONAL</b>				
FDEPS (Rs)	73.7	84.8	104.2	126.2
CEPS (Rs)	83.6	95.9	115.3	139.3
DPS (Rs)	22.0	26.0	30.0	34.0
Dividend payout ratio (%)	29.8	30.6	28.8	26.9
<b>GROWTH</b>				
Net sales (%)	7.6	10.1	14.0	13.9
EBITDA (%)	5.3	18.5	16.2	19.1
Adj net profit (%)	7.3	15.3	23.1	21.3
FDEPS (%)	7.3	15.1	22.9	21.1
<b>PERFORMANCE</b>				
RoE (%)	36.9	33.5	32.7	31.6
RoCE (%)	52.7	49.1	47.1	45.3
<b>EFFICIENCY</b>				
Asset turnover (x)	5.0	4.4	4.6	4.6
Sales/ total assets (x)	2.4	2.2	2.0	1.9
Working capital/ sales (x)	0.1	0.1	0.1	0.1
Receivable days	7.3	7.1	6.9	7.1
Inventory days	31.0	27.8	27.3	27.1
Payable days	35.5	38.4	38.0	37.9
<b>FINANCIAL STABILITY</b>				
Total debt/ equity (x)	-	-	-	-
Net debt/ equity (x)	(0.2)	(0.4)	(0.4)	(0.5)
Current ratio (x)	1.9	2.2	2.5	2.8
Interest cover (x)	212.6	251.3	271.2	298.3
<b>VALUATION</b>				
PE (x)	64.6	56.1	45.7	37.7
EV/ EBITDA (x)	44.3	37.0	31.5	26.1
EV/ Net sales (x)	6.3	5.7	4.9	4.3
PB (x)	21.2	16.8	13.4	10.7
Dividend yield (%)	0.5	0.5	0.6	0.7
Free cash flow yield (%)	-	-	-	-

Source: Company, Axis Capital

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