

Sector: Consumer Goods
Result Update

	Change
Reco: Buy	↔
CMP: Rs. 3,195	
Price Target: Rs. 3,625	↑

↑ Upgrade ↔ No change ↓ Downgrade

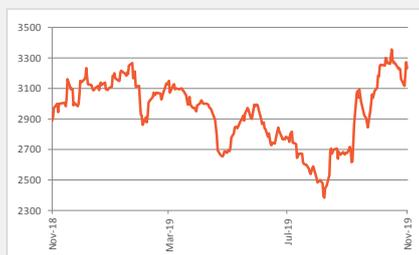
Company details

Market cap:	Rs. 76,782 cr
52-week high/low:	Rs. 3444/2302
NSE volume: (No of shares)	5.1 lakh
BSE code:	500825
NSE code:	BRITANNIA
Sharekhan code:	BRITANNIA
Free float: (No of shares)	11.9 cr

Shareholding (%)

Promoters	50.7
FII	16.6
DII	13.6
Others	19.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	3.9	30.3	20.5	12.6
Relative to Sensex	-1.6	20.5	10.6	-2.9

Sharekhan Research, Bloomberg

Britannia Industries

Steady performance in tough environment

Britannia Industries registered steady performance in the backdrop of tough demand, with revenue growing by 6.2% (driven by volume growth of 3%) and a 31 bps rise in OPM to 16.1% (better than our expectation of 14.5%). New products (3% of overall sales) are performing well and gaining good acceptance in the domestic market. Most of the new products launched in recent times are gross margin accretive. The revenue mix between biscuit and non-biscuit products will reduce to 70:30 from 75:25 earlier over the next 2-3 years. Middle East and Africa continue to remain challenging affecting the performance of the subsidiaries. The management believes that recovery will take another two quarters. Raw material cost inflation is expected to stay at around 4.5% in H2FY2020. Britannia has maintained its target of cost saving of ~Rs. 250 crore through various cost saving initiatives in FY2020.

Key positives

- ◆ Britannia continues to gain market share despite slowdown in the industry growth; gained market share from second best player and other small players.
- ◆ New launches (contribute ~3% to overall revenue) performed well, finding strong acceptance in most markets.
- ◆ Despite a rise in milk prices, gross margins stayed at 40.2% and OPM improved by 31 bps, led by efficiencies.

Key negatives

- ◆ Subsidiaries (including international regions) witnessed a significant drop in profitability.

Our Call

Valuation: We have reduced our earnings estimates by 2-3% for FY2020 and FY2021 to factor in a little lower than earlier expected revenue growth (introduced FY2022 estimates in this note). Recovery in the biscuit category's growth and a scale-up in performances of new products and adjacencies (including dairy and bakery businesses) would help Britannia record better earnings in the near to medium term. We expect Britannia's revenue and PAT to grow at a CAGR of 9.6% and 18.7% over FY2019-22. The stock currently trades at 45.4x and 39.7x its FY2021E and FY2022E earnings. We retain our Buy recommendation on the stock with a revised PT of Rs. 3,625 (rolling over our price target to average of FY2021/22 earnings).

Key Risks

Dismal performance by some of the new ventures would affect the company's overall performance in the near to medium term.

Valuation (Consolidated)

Particulars	Rs cr				
	FY18	FY19	FY20E	FY21E	FY22E
Revenue	9,914	11,054.7	11,814.6	13,152.2	14,572.0
OPM (%)	15.1	15.7	16.0	16.4	16.8
Adjusted PAT	1,004	1,156.4	1,441.9	1,692.2	1,934.5
% YoY growth	13.6	15.2	24.7	17.4	14.3
Adjusted EPS (Rs.)	41.8	48.2	60.1	70.5	80.6
P/E (x)	76.4	66.4	53.2	45.4	39.7
P/B (x)	22.5	18.0	14.5	11.7	9.5
EV/EBIDTA (x)	51.1	44.4	40.2	35.0	30.5
RoNW (%)	32.9	30.2	30.3	28.6	26.5
RoCE (%)	47.4	42.8	37.6	36.4	34.0

Source: Company; Sharekhan estimates

Volume growth came in at just 3%; OPM declined by ~70 bps: For Q2FY2020, Consolidated revenue grew by 6.2% y-o-y (in-line with our expectation) to Rs. 3,048.8 crore in Q2FY2020 from Rs. 2,869.6 crore in Q2FY2019 driven by premiumisation and innovation. We believe volume growth would be in the range of 3-4%. In spite of moderate inflation in key raw material prices including increase in milk prices, cost efficiencies resulted in GPM to remain flat at 40.2%. Lower other expenditure (down by 40 bps as a percentage of sales) resulted in OPM to expand by 31 bps to 16.1% (ahead of our expectation of 14.5%). This resulted in operating profit to grow by 8.3% y-o-y to Rs. 492.2 crore. Despite higher other income, a rise in finance costs and depreciation resulted in profit before tax (PBT) to grow in line with operating profit at 8.8% y-o-y. Reported PAT grew by 33% y-o-y to Rs. 403.5 crore (ahead of our expectation of Rs. 377.6 crore) largely due to lower incidence of tax as a result of reduction of corporate tax rate.

Domestic business grew in single-digits; Adjacencies affected by one-offs: Domestic business grew by 6.8% y-o-y. For Britannia rural growth was better than urban growth as the company is enhancing its distribution reach in the rural market. The company continues its investment momentum in key brands in the form of innovative product launches, consumer promotions and digital activations. Britannia launched Treat cream biscuits and Little Hearts – Strawberry and various re-launches during the quarter. Treat Cream Wafers has gained a more than 10% market share the baked salted snacks (Timepass) are gaining good momentum. Winkin Cow Milk Shakes have achieved the second position within a year of launch. Revenues of the subsidiary declined by ~7.4% y-o-y. The revenue decline is mainly on account of lower sales of commodities dairy business and muted sales in the Middle East. The dairy business reported low single-digit growth affected by rise in milk prices, however, profitability of the dairy business improved sequentially. With respect to the bread business, the company is expecting to tap newer markets. In terms of international business, America posted double-digit growth, but a slowdown was seen in Middle East and Africa. Nepal is performing well and reported strong market share gains. Operating profit of subsidiaries stood at Rs. 21.9 crore as against Rs. 29.6 crore in Q2FY2019.

Other conference call highlights:

- ♦ Milk Bikis (which was largely sold in South India) has been taken to rest of India under the Rs. 5 price point. The company has launched limited edition of Cream Treat – Tiramisu and Red Velvet. The company will continue with its strategy to create more attraction for the respective brands. The company has test launched Croissant in the state of West Bengal and Tamil Nadu. The wheat flour procurement issue has been resolved and focus is on increasing efficiencies. The company has introduced one more production line of Croissant at its Ranjangaon facility in Maharashtra. The product is expected to get launched in west India soon based on the response in the states where it was launched. Timepass Snacks has been launched in western India with addition of one more line in Ranjangaon facility.
- ♦ Raw material cost inflation stood at ~3% in Q2FY2020. The company has an inventory of low cost raw material for another three to four months. It does not expect raw material cost inflation to cross 4.5% in the coming quarters. However, if it increases significantly in the coming quarters, the company might opt for selective price hikes in some brands.
- ♦ Inter-corporate loans currently amount to Rs. 450 crore and are expected to reduce by end of the current fiscal.
- ♦ Britannia's direct distribution reach increased by 2.9x from March 2014 to 21.3 lakh outlets to date (number of preferred rural dealers stood at 20,000). However the same has sustained on a quarter-on-quarter basis. The management has decided to slow down the distribution expansion in view of the current slowdown in the domestic market. It will focus on selling more products/SKUs of existing products through its current distributor network.
- ♦ ~60% of total production happens in-house and 40% is out-sourced. The company has done capex of Rs. 170-180 crore in H1FY2020 and does not expect significant capex in the coming quarters.

Results (Consolidated)

Particulars	Rs cr				
	Q2FY20	Q2FY19	Y-o-Y (%)	Q1FY20	Q-o-Q (%)
Net Sales	3022.9	2854.8	5.9	2677.3	12.9
Other operating income	25.9	14.8	75.4	23.0	12.6
Net revenue	3048.8	2869.6	6.2	2700.4	12.9
Raw materials	1824.1	1720.5	6.0	1609.2	13.4
Employee costs	123.6	108.0	14.4	120.6	2.5
Other expenditure	608.9	586.7	3.8	576.0	5.7
Total expenditure	2556.6	2415.3	5.9	2305.7	10.9
Operating profit	492.2	454.3	8.3	394.7	24.7
Other income	68.2	44.0	55.0	67.5	1.0
Interest expenses	16.1	2.4	-	10.1	59.8
Depreciation	44.9	36.9	21.5	44.8	0.2
Profit Before Tax	499.4	458.9	8.8	407.2	22.6
Tax	95.9	155.9	-38.5	148.2	-35.3
Adjusted PAT	403.5	303.0	33.1	259.1	55.7
Share of profit from associates	0.0	-0.1	-	0.0	-50.0
Adjusted PAT after MI	403.5	303.0	33.2	259.1	55.7
Extra-ordinary items	0.8	0.0	-	10.5	-
Reported PAT	402.7	303.0	32.9	248.6	62.0
Adjusted EPS (Rs)	16.8	12.6	33.1	10.8	55.7
			BPS		BPS
GPM (%)	40.2	40.0	13	40.4	-24
OPM (%)	16.1	15.8	31	14.6	153

Source: Company; Sharekhan Research

Results (Standalone)

Particulars	Rs cr				
	Q2FY20	Q2FY19	Y-o-Y (%)	Q1FY20	Q-o-Q (%)
Net revenue	2896.1	2704.6	7.1	2579.5	12.3
Operating profit	470.4	424.7	10.8	388.2	21.2
Adjusted PAT	469.1	283.6	65.4	260.9	79.8
Extra-ordinary items	-23.5	0.0	-	10.7	-
Reported PAT	492.6	283.6	73.7	250.2	96.9
Adjusted EPS (Rs)	19.5	11.8	65.4	10.9	79.8
			BPS		BPS
GPM (%)	39.4	39.2	21	40.0	-55
OPM (%)	16.2	15.7	54	15.0	119

Source: Company; Sharekhan Research

Results (Subsidiaries-extracts)

Particulars	Rs cr		
	Q2FY20	Q2FY19	Y-o-Y (%)
Net revenue	152.8	165.0	-7.4
Operating profit	21.9	29.6	-26.3
Adjusted PAT	-65.7	19.5	-
Extra-ordinary items	-24.2	0.0	-
Reported PAT	-89.9	19.5	-
			BPS
GPM (%)	54.7	54.0	69
OPM (%)	14.3	18.0	-367

Source: Company; Sharekhan Research

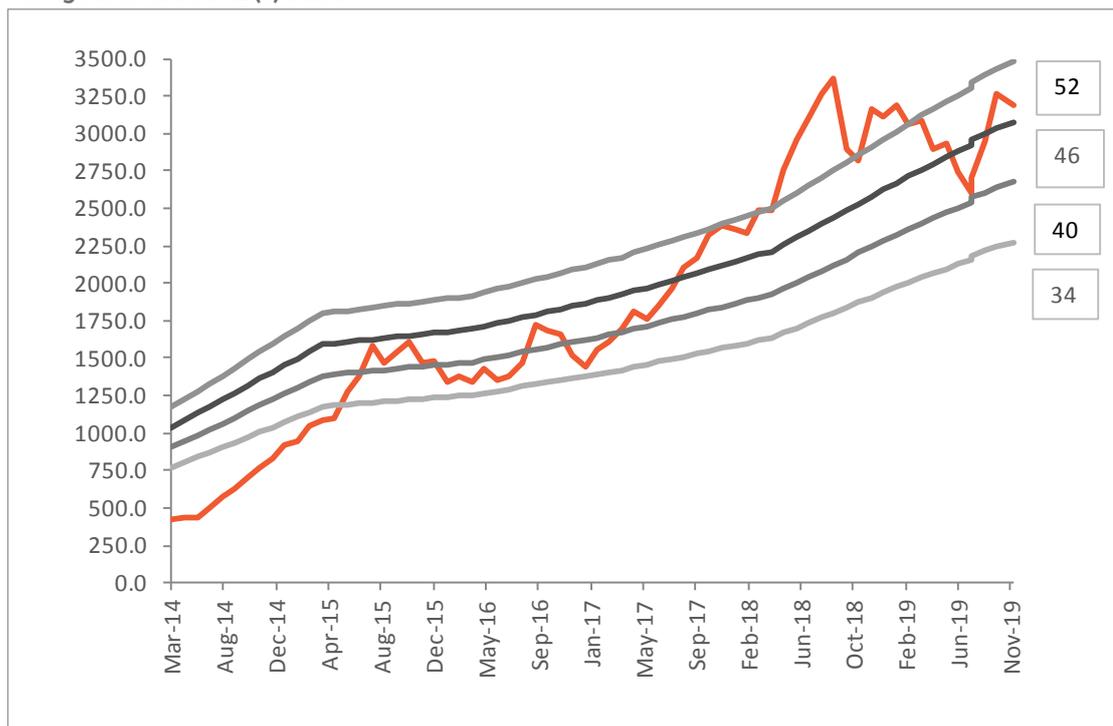
Outlook

H2FY2020 will be modest; Recovery expected in FY2021: Volume growth stood at 3% in H1FY2020 on account of a slowdown in the biscuit category's growth, led by a slowdown in the rural market. Liquidity concerns will take a toll on rural demand. Hence, volume growth will take another two quarters to recover (expected to be at 4-5% in the near term). Raw material cost inflation is expected to stay at around 4.5% in H2FY2020. Britannia has maintained its target of cost saving of ~Rs. 250 crore through various cost-saving initiatives in FY2020. Overall, we expect Britannia's revenue to grow by 7% and OPM to expand by 30-40 bps to 16.4% in FY2020. However, with a recovery in demand, revenue growth will improve to double-digits in FY2021.

Valuation

We have reduced our earnings estimates by 2-3% for FY2020 and FY2021 to factor in a little lower than earlier expected revenue growth (introduced FY2022 estimates in this note). Recovery in the biscuit category's growth and a scale-up in performances of new products and adjacencies (including dairy and bakery businesses) would help Britannia record better earnings in the near to medium term. We expect Britannia's revenue and PAT to grow at a CAGR of 9.6% and 18.7% over FY2019-22. The stock currently trades at 45.4x and 39.7x its FY2021E and FY2022E earnings. We retain our Buy recommendation on the stock with a revised PT of Rs. 3,625 (rolling over our price target to average of FY2021/22 earnings).

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
Nestle	83.6	70.5	57.3	51.0	48.1	40.1	70.3	67.1	67.9
Hindustan Unilever	71.7	58.4	49.1	50.7	42.1	36.3	113.2	108.7	95.9
Britannia	66.4	53.2	45.4	44.4	40.2	35.0	42.8	37.6	36.4

Source: Company, Sharekhan estimates

About company

Britannia is one of India's leading packaged food companies with a 100-year legacy and annual revenue in excess of Rs. 10,000 crore. The company is among the most trusted food brands and manufactures well-known brands such as Good Day, Tiger, NutriChoice, Milk Bikis and Marie Gold, which are household names in India. Britannia's product portfolio includes biscuits, bread, cakes, rusk and dairy products, including cheese, beverages, milk and yoghurt. The company is the market leader in the biscuit category, with close to 34% market share in the domestic market. The dairy business contributes 5% of overall revenue.

Investment theme

Britannia is a strong brand with market leadership in the domestic biscuit market. Sustained new launches and entry into healthier and premium variants helped it gain market share and beat category growth. The company is also focusing on growing its adjacent categories such as dairy and bakery. Steady improvement in volume growth, improved product mix and operating efficiencies helped Britannia post a sustained improvement in operating margin to 15.7% in the past nine years. Though rural slowdown will keep a toll on near-term performance, new product launches, entry into new categories and scale-up in the adjacent categories will drive long-term performance.

Key Risks

- ◆ Dismal performance by some of the new ventures would affect the company's overall performance in the near to medium term.

Additional Data

Key management personnel

Nusli N Wadia	Chairman
Varun Berry	Managing Director
N Venkataraman	Chief Financial Officer
T V Thulsidass	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Associated Biscuits International	67.3
2	Life Insurance Corp of India	6.6
3	Nacupa Enterprises Pte Ltd	1.7
4	Dowbiggin Enterprises Pte Ltd	1.7
5	Valletort Enterprises Pte Ltd	1.7
6	Spargo Enterprises Pte Ltd	1.7
7	Bannatyne Enterprises Pte Ltd	1.7
8	Arisaig Partners Asia Pte Ltd	1.5
9	Arisaig India Fund Limited	1.5
10	BlackRock Inc	1.2

Source: Bloomberg

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