India Midcaps

RESULT UPDATE

VIP INDUSTRIES

Robust volumes spur revenue; margin zooms

India Equity Research| Miscellaneous

Edelweiss
Ideas create, values protect

VIP Industries' (VIP) Q4FY17 revenue at INR3.1bn (up 12% YoY) and EBITDA at INR307mn (up 41% YoY) surpassed estimates 3% and 15%, respectively. Domestic revenue jumped 16% (6.5% in FY17) led entirely by volume growth. While gross margin rose to 48.3% (highest in 3 plus years), EBITDA margin expanded 208bps YoY to 10.0% fuelled by lower advertising & other expenses. Management is concerned about the impact of 28% GST rate (current tax burden: ~18-19%). Despite limited upside at current level, we maintain 'BUY' with target price of INR204 due to: (1) VIP's market leadership (50% plus share); (2) strong revenue visibility; (3) sustained margin expansion; (4) anticipated shift of trade from unorganised to organised segment; and (5) potentially higher dividend payout. We estimate VIP to post robust 25% PAT CAGR and RoCE to expand 460bps to 37% over FY17-19E.

Volume-led revenue spurt; outlook positive

Domestic revenue growth of 16% in Q4FY17 (6.5% for FY17) was entirely volume led. However, international revenue declined due to distribution issue, which has been resolved. Overall FY17 revenue grew 5% (12% adjusting for Haj order), this was on account of poor marriage season in Q1, one-off Haj order in FY16 and demonetisation. Skybags continued to outperform and has become as big as VIP with similar margin. Further, VIP has become the market leader in backpacks from negligible presence in the segment. Management guided this growth rate to be sustainable.

Strong margin expansion to sustain; GST a concern

VIP's EBITDA margin expanded 208bps YoY on cost control and advancing of advertisement expenses to Q3FY17. For FY17, it jumped ~150bps led by gross margin expansion riding improved product mix, cost control, better negotiation with suppliers and muted inflation. We envisage the appreciation of INR to further boost margin, impact of which will reflect Q1FY18 onwards. However, management perceives the higher tax rate of 28% under GST as a concern from margin perspective.

Outlook and valuations: Long-term benefits; maintain 'BUY'

Over the long term, VIP is well positioned as mix improves in favour of high-margin products and rising penetration of branded luggage. We estimate it to post 25% PAT CAGR and RoCE to expand 460bps to 37% over FY17-19. We maintain **'BUY'** with TP of INR204 (22x FY19E EPS). At CMP, the stock trades at 20.8x FY19E EPS.

Financials (Consolidated) (INR mn)

Year to March	Q4FY17	Q4FY16	*Y-o-Y %*	Q3FY17	*Q-o-Q %*	FY17	FY18E	FY19E
Revenues	3,072	2,753	*11.6*	3,074	*(0.1)*	12,752	14,282	16,578
EBITDA	307	218	*41.0*	260	*18.4*	1,318	1,612	1,987
Adj PAT	189	129	*46.4*	155	*21.8*	839	1,048	1,310
Dil. EPS (INR)	1.3	0.9	*46.4*	1.1	*21.8*	5.9	7.4	9.3
Dil. P/E (x)						32.5	26.0	20.8
EV/EBITDA (x)						20.1	16.1	12.8
ROAE (%)						22.4	23.8	25.5

EDELWEISS RATINGS	
Absolute Rating	**BUY**
Investment Characteristics	Growth

MARKET DATA *(R: VIPI.BO, B: VIP IN)*	
CMP	: INR 193
Target Price	: INR 204
52-week range (INR)	: 217 / 103
Share in issue (mn)	: 141.3
M cap (INR bn/USD mn)	: 27 / 422
Avg. Daily Vol. BSE/NSE ('000)	: 544.0

SHARE HOLDING PATTERN (%)

	Current	Q2FY17	Q1FY17
Promoters *	52.5	52.5	52.5
MF's, FI's & BKs	16.8	17.9	16.4
FII's	4.2	3.3	3.6
Others	26.5	26.3	27.5
** Promoters pledged shares (% of share in issue)*	:		*NIL*

PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	(0.1)	(3.3)	(3.1)
3 months	7.1	31.3	24.2
12 months	31.2	68.2	37.0

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Q4FY17: Key highlights

- **Revenue:** Top line grew 12% YoY in Q4FY17 and 5% in FY17. While domestic revenue grew ~16%, international business continued to decline. However, one issue that was there in international business has been solved. Sales spurt was driven entirely by volume growth and not price. For FY17, while domestic business grew ~6.5%, international business declined due to issue with a distributor. Q1FY17 saw lower growth which is generally the best quarter, but poor marriage season led to poor demand in May. Lower growth in FY17 was also due to one-time Haj order in 2016, which contributed 5% to revenue. Excluding this, domestic growth was around 12%. Demonetisation also impacted FY17 sales growth.

- **Margin:** Gross margin improved slightly over an already high base by 15bps YoY and 45bps QoQ to 48.26%, the highest in more than 3 years. EBITDA margin expanded 208bps YoY and 156bps QoQ. This strong expansion was driven by lower advertisement expenses during the quarter as they were incurred in Q3FY17 as well as lower other expenses. FY17 EBITDA margin jumped ~150bps led by gross margin expansion. This was on account of improved product mix, cost control measures, better negotiation and muted inflationary environment. Appreciation of INR also contributed to the improvement; however, the effect will be felt more Q1FY18 onwards due to some lag. However, the impact of GST on margin is a concern. Management is targeting 14-15% margin in the long run. Prices were increased ~3% in April, as usual.

- **Brand-wise:** *Skybags* continued to be the best performing brand, logging the fastest growth. It has become as big as VIP and clocked similar margin. Aristocrat, the value brand, has also done well after sharpened focus and marketing with celebrity cricketers. Caprese too continued to grow rapidly with good margin.

- **Channels:** Modern trade continued to grow well while e-commmerce has also picked up pace. VIP has around 3,000 direct dealers and 250 company run stores. It is looking for distribution expansion FY18 onwards. Management wants to continue to remain in all channels as it aids market share gains, brand reach, etc.

- **GST:** The applicable GST rate for VIP is 28%, which is significantly higher than the existing blended tax rate of 18-19%. This higher rate will impair the shift from unorganised to organised players as the incentive for evasion is even higher. This rate may also impact margin going forward, though management is unsure of quantum of impact.

- **Competition:** Competitive intensity remains high, though VIP's market share remains above 50%. Increasing it further will be expensive. Over the past few years, VIP has wrested share from Samsonite across segments, though it has lost share to Safari, primarily in the value segment. VIP gained large market share in backpacks and has become the market leader from NIL presence a few years ago. None of the competitors have cut prices.

- **International business:** International business has lagged this year. The decline was due to lower brand strength in foreign markets as well as an issue with a distributor. However, the agreement has been terminated. Going forward, the strategy is to improve distribution and reach as well as brand strength.

- **Bangladesh subsidiary:** Profit before tax was around INR35mn for Q4FY17 and ~INR90mn in FY17. It was a good year for the Bangladesh subsidiary with steady growth and good margins. Capacity utilisation stands at 90% and management is open to the idea of further expansion, though nothing is planned currently.

- **Management:** VIP is comfortable with the top management team operating the day to day business while Ms. Radhika Piramal, Executive Director, is in London. Mr. Dilip Piramal has come back as MD and practically the roles will largely remain the same. This will also aid international business expansion.

Q3FY17: Key highlights

- **Revenue:** Top line grew 6% YoY, despite the impact of demonetisation. Good growth in October was stunted by decline in November, before stabilizing somewhat in December. Domestic luggage grew 10%, which was entirely volume driven, while international luggage declined by nearly 30% due to distribution partner related issues in Dubai. Product mix did not improve this quarter.

- **Margin:** Gross margin jumped 378bps YoY and 152bps QoQ to 47.8%. This strong expansion was driven by better negotiation with the suppliers, relatively stable INR exchange rate and containment of plastic price from second half of 2016. Better negotiation was possible due to overcapacity and no cost pressures for suppliers. However, it will be tough to improve margins from these levels. EBITDA margin expanded 216bps YoY due to the gross margin expansion, though it fell 74bps QoQ. The reason for the QoQ dip was higher ad spends this quarter, as VIP ran its pre-Diwali marketing campaign. Overall, going ahead, management expects gross margin to sustain at this level, subject to INR/USD remaining below 68.

- **Channels:** Modern trade continues to grow rapidly, though traditional channel still remains their largest. Dealer channel was strongly impacted by demonetisation. CSD, which contributes ~20% of revenues, works like a modern trade partner. Pricing and products are decided centrally, though orders are done by individual canteens.

- **Industry:** Expected see shift from unorganised to organised, due to various factors such as demonetisation and GST. As customers upgrade from unorganised to organised, they will choose value products rather than premium products. This provides good growth potential to VIP's entry level brands, *Alfa* and *Aristocrat*.

- **Brand-wise:** *Skybags* continued to be the best performing brand, growing above the company average. *Alfa*, *Aristocrat* and *Carlton* grew at similar level to the average, while *VIP* grew at a more subdued rate. *VIP* brand is having trouble growing due pre-existing perception with customers, which the company is hoping to change. Management continued to stress they want to maintain the number of brands, as each brand has its own strengths. *Alfa* and *Aristocrat* may have lost market share to *Safari* in the value segment, considering *Safari's* high growth rate. Handbags and backpacks continued to post strongest growth.

- **Competition:** Competitive intensity remains high. Management believes they would have gained market share from Samsonite, though lost market share somewhat from Safari in 2016.

- **Demonetisation:** Management explained that due to relatively smaller size and lower penetration of the branded luggage industry, demonetisation didn't affect the industry as much as other sectors.

- **Bangladesh subsidiary:** The unit in Bangladesh has capacity of 90,000 units and it is running at 75-80% utilisation. It was a good quarter for the subsidiary, running on stable processes and margins. VIP buys from the subsidiary, like any other vendor, and the products are sold at standard MRPs.

Chart 1: Movement of USD/INR

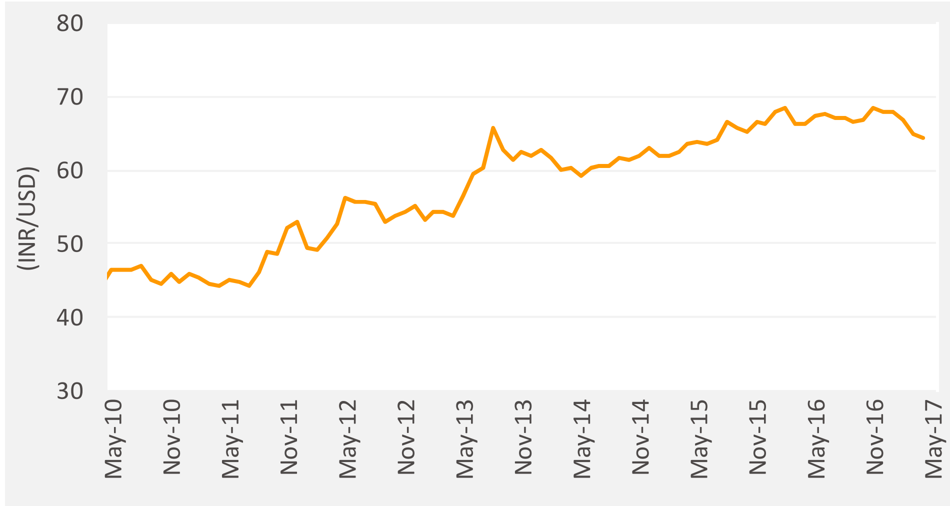
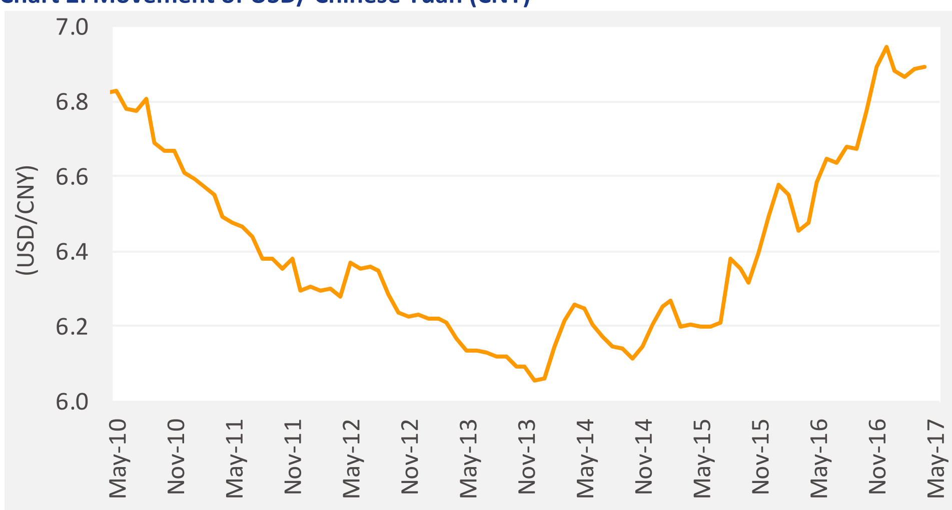
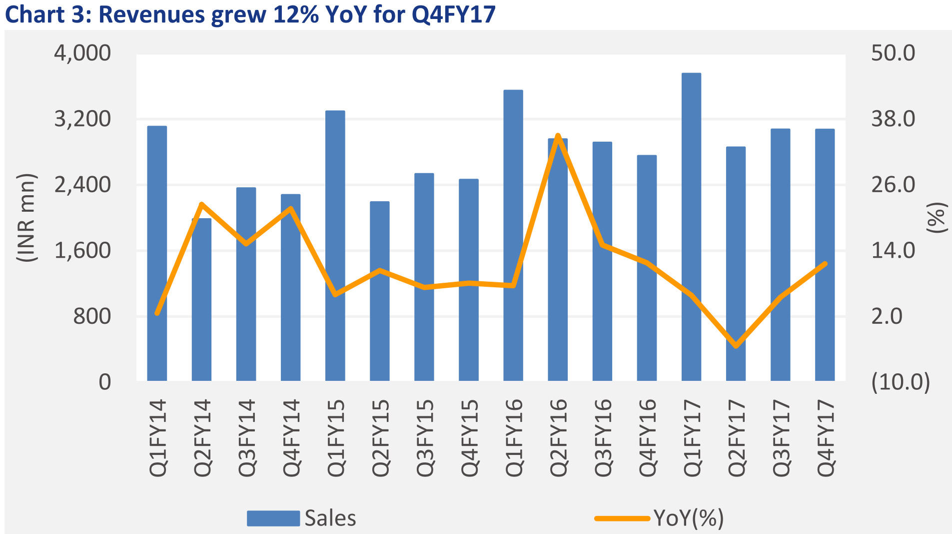


Chart 2: Movement of USD/ Chinese Yuan (CNY)



Source: Bloomberg, Edelweiss research

Chart 3: Revenues grew 12% YoY for Q4FY17



Source: Edelweiss research

Financial snapshot **(INR mn)**

Year to March	Q4FY17	Q4FY16	*% change*	Q3FY17	*% change*	FY17	FY18E	FY19E
Net revenues	3,072	2,753	*11.6*	3,074	*(0.1)*	12,752	14,282	16,578
Raw material	1,590	1,429	*11.3*	1,604	*(0.9)*	6,760	7,557	8,773
Staff costs	357	312	*14.6*	352	*1.6*	1,415	1,500	1,658
Other expenses	818	795	*3.0*	859	*(4.7)*	3,259	3,613	4,161
Total expenditure	2,765	2,535	*9.1*	2,814	*(1.8)*	11,434	12,670	14,592
EBITDA	307	218	*41.0*	260	*18.4*	1,318	1,612	1,987
Depreciation	33	34	*(3.3)*	33	*(0.9)*	136	137	141
EBIT	275	184	*49.1*	227	*21.2*	1,182	1,475	1,846
Other income	8	9	*(10.0)*	5	*58.8*	59	69	84
Interest	4	1	*191.7*	1	*337.5*	6	2	4
Add: Prior period items								
Add: Exceptional items								
Profit before tax	279	192	*45.4*	231	*20.9*	1,235	1,542	1,926
Provision for taxes	90	63	*43.3*	76	*19.0*	397	493	616
Minority interest								
Associate profit share								
Reported net profit	189	129	*46.4*	155	*21.8*	839	1,048	1,310
Adjusted Profit	189	129	*46.4*	155	*21.8*	839	1,048	1,310
Equity capital(FV INR10)	283	283		283		283	283	283
Diluted shares (mn)	141	141		141		141	141	141
Adjusted Diluted EPS	1.3	0.9	*46.4*	1.1	*21.8*	5.9	7.4	9.3
Diluted P/E (x)	-	-		-		32.5	26.0	20.8
EV/EBITDA (x)	-	-		-		20.1	16.1	12.8
ROAE (%)	-	-		-		22.4	23.8	25.5
Market cap / rev. (x)	-	-		-		2.1	1.9	1.6
As % of net revenues	-	-		-		2	2	2
Raw material	51.7	51.9		52.2		53.0	52.9	52.9
Employee cost	11.6	11.3		11.4		11.1	10.5	10.0
Other expenses	26.6	28.9		27.9		25.6	25.3	25.1
EBITDA	10.0	7.9		8.4		10.3	11.3	12.0
Reported net profit	6.2	4.7		5.1		6.6	7.3	7.9

Change in Estimates

	FY18E			FY19E			
	New	**Old**	***% change***	**New**	**Old**	***% change***	**Comments**
Net Revenue	14,282	14,133	*1.1*	16,578	16,383	*1.2*	
EBITDA	1,612	1,461	*10.3*	1,987	1,776	*11.9*	On account of margin expansion due to appreciation of INR
EBITDA Margin	*11.3*	*10.3*		*12.0*	*10.8*		
Adjusted Profit After Tax	1,048	929	*12.8*	1,310	1,148	*14.1*	
Net Profit Margin	*7.3*	*6.6*		*7.9*	*7.0*		
Capex	134	100	*34.1*	80	80	*0.0*	

Company Description

VIP, the flagship company of DG Piramal Group, was established in 1968. It began manufacturing suitcases in 1971. The company operates in luggage and moulded furniture segments. The company manufactures a range of hard-sided and soft-sided luggage including trolleys, suitcases, duffels and overnight travel solutions, executive cases, backpacks and school bags. Key brands are VIP, Skybags, Alfa, Aristocrat, Carlton, Caprese. The company's manufacturing facilities are located at Nashik and in Haridwar (Uttarakhand).

Investment Theme

VIP, which began as a moulding furniture company in 1970, is now the second largest player in the world and largest in Asia commanding ~50% market share in luggage market in India, followed by Samsonite and Safari. The company derives ~45% of its sales from the VIP brand, 27% plus from Skybags brand, 20% from Aristocrat and Alfa combined, and ~8% combined from premium Carlton and Caprese brands.

Key Risks

Stiff competition from organised sector

Increase in competition from the organised sector can affect VIP's sales and profitability growth as players like Samsonite post having grown strong in market share are now focused on profitability, while players like Safari are strongly focused on gaining market share.

Increase in raw material prices

The company currently derives ~30% of its revenues from hard luggage that is manufactured in-house. Major raw materials consumed in manufacture of hard luggage are polypropylene and aluminum. Any substantial rise in their prices will adversely impact the company's margins and, hence, profitability.

Fluctuation in exchange rates, particularly appreciation of Yuan

Any appreciation in Yuan could hit VIP's realizations as the company imports its entire soft luggage (70% of sales) from China. Also, the impact of currency depreciation, is passed with a lag. In this context, appreciation of the Yuan is particularly harmful for earnings.

Working capital increase from growing modern trade

Working capital of the company can deteriorate if the modern trade channel grows aggressively.

Financial Statements

Key Assumptions

Year to March	FY16	FY17	FY18E	FY19E
Macro				
GDP(Y-o-Y %)	7.2	6.5	7.1	7.7
Inflation (Avg)	4.9	4.8	5.0	5.2
Repo rate (exit rate)	6.8	6.3	6.3	6.3
USD/INR (Avg)	65.0	67.5	67.0	67.0
Company				
Domestic growth	16.3	8.5	13.0	17.0
Exports	15.0	4.0	2.0	6.0
Raw Material (% net rev)	54.5	53.0	52.9	52.9
Employee cost (% of rev)	10.3	11.1	10.5	10.0
Selling exp.(% Net Rev)	26.3	25.6	25.3	25.1
Avg. Interest rate (%)	5.2	8.0	8.0	8.0
Depreciation rate (%)	5.1	4.8	4.7	4.7
Tax rate (%)	30.1	32.1	32.0	32.0
Soft luggage %	79.0	79.0	84.0	84.0
Hard luggage %	21.0	21.0	16.0	16.0
Net borrowings (INR mn)	143	-	50	50
Capex (INR mn)	21	70	100	100
Debtor days	39	39	35	36
Inventory days	142	154	146	144
Payable days	77	83	75	74
Cash conversion cycle	104	110	106	106

Income statement (INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Net revenue	12,165	12,752	14,282	16,578
Materials costs	6,627	6,760	7,557	8,773
Gross profit	5,537	5,992	6,725	7,806
Employee costs	1,259	1,415	1,500	1,658
Other Expenses	3,200	3,259	3,613	4,161
Total operating expenses	11,086	11,434	12,670	14,592
EBITDA	1,079	1,318	1,612	1,987
Depreciation	142	136	137	141
EBIT	937	1,182	1,475	1,846
Add: Other income	25.7	59.1	68.66	84.24
Less: Interest Expense	12	6	2	4
Profit Before Tax	951	1,235	1,542	1,926
Less: Provision for Tax	287	397	493	616
Reported Profit	665	839	1,048	1,310
Adjusted Profit	665	839	1,048	1,310
Shares o /s (mn)	141	141	141	141
Adjusted Basic EPS	4.7	5.9	7.4	9.3
Diluted shares o/s (mn)	141	141	141	141
Adjusted Diluted EPS	4.7	5.9	7.4	9.3
Adjusted Cash EPS	5.6	6.9	8.6	10.5
Dividend per share (DPS)	2.0	1.6	2.4	3.0
Dividend Payout Ratio(%)	51.2	31.5	37.8	37.9

Common size metrics

Year to March	FY16	FY17	FY18E	FY19E
Operating expenses	36.7	36.7	35.8	35.1
Cost of goods sold	54.5	53.0	52.9	52.9
Depreciation	1.2	1.1	1.0	0.9
Interest Expense	0.1	-	-	-
EBITDA margins	8.9	10.3	11.3	12.0
Net Profit margins	5.5	6.6	7.3	7.9

Growth ratios (%)

Year to March	FY16	FY17	FY18E	FY19E
Revenues	16.1	4.8	12.0	16.1
EBITDA	39.3	22.2	22.3	23.3
PBT	45.2	29.9	24.8	24.9
Adjusted Profit	52.5	26.2	25.0	24.9
EPS	52.5	26.2	25.0	24.9

Miscellaneous

Balance sheet (INR mn)

As on 31st March	FY16	FY17	FY18E	FY19E
Share capital	283	283	283	283
Reserves & Surplus	3,111	3,801	4,452	5,266
Shareholders' funds	3,393	4,084	4,735	5,549
Long term borrowings	143	-	50	50
Total Borrowings	143	-	50	50
Long Term Liabilities	69	97	106	115
Def. Tax Liability (net)	(41)	(51)	(51)	(51)
Sources of funds	**3,564**	**4,129**	**4,839**	**5,662**
Gross Block	2,787	2,857	2,957	3,057
Net Block	656	600	563	522
Capital work in progress	11	6	40	20
Intangible Assets	10	11	11	11
Total Fixed Assets	677	616	614	553
Non current investments	-	-	-	-
Cash and Equivalents	80	785	1,366	1,854
Inventories	2,874	2,826	3,209	3,725
Sundry Debtors	1,493	1,210	1,526	1,771
Loans & Advances	630	558	596	638
Other Current Assets	53	45	50	55
Current Assets (ex cash)	5,051	4,639	5,381	6,189
Trade payable	1,608	1,457	1,656	1,923
Other Current Liab	636	454	865	1,011
Total Current Liab	2,244	1,912	2,521	2,933
Net Curr Assets-ex cash	2,807	2,728	2,860	3,256
Uses of funds	**3,564**	**4,129**	**4,839**	**5,662**
BVPS (INR)	24.0	28.9	33.5	39.3

Free cash flow (INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Reported Profit	665	839	1,048	1,310
Add: Depreciation	142	136	137	141
Interest (Net of Tax)	8	4	1	3
Others	(398)	186	(291)	(828)
Less: Changes in WC	200	(108)	124	387
Operating cash flow	617	1,057	1,019	1,012
Less: Capex	21	65	134	80
Free Cash Flow	**596**	**992**	**885**	**932**

Cash flow metrics

Year to March	FY16	FY17	FY18E	FY19E
Operating cash flow	617	1,057	1,019	1,012
Investing cash flow	(20)	(36)	(90)	(24)
Financing cash flow	(522)	(413)	(349)	(500)
Net cash Flow	75	609	580	488
Capex	(21)	(65)	(134)	(80)
Dividend paid	(340)	(265)	(397)	(496)

Profitability and efficiency ratios

Year to March	FY16	FY17	FY18E	FY19E
ROAE (%)	20.6	22.4	23.8	25.5
ROACE (%)	27.9	32.6	34.8	37.2
ROA	19.1	21.8	23.4	24.9
Debt/EBITDA (x)	0.1	-	-	-
Debt/Equity (x)	-	-	-	-
Interest Coverage Ratio	79.4	207.4	737.5	461.4
Debt / Cap employed (%)	65.8	45.1	52.1	51.8

Operating ratios

Year to March	FY16	FY17	FY18E	FY19E
Total Asset Turnover	3.5	3.3	3.2	3.2
Fixed Asset Turnover	17.6	20.0	24.1	30.0
Equity Turnover	3.8	3.4	3.2	3.2

Valuation parameters

Year to March	FY16	FY17	FY18E	FY19E
Adj. Diluted EPS (INR)	4.7	5.9	7.4	9.3
Y-o-Y growth (%)	*52.5*	*26.2*	*25.0*	*24.9*
Adjusted Cash EPS (INR)	5.6	6.9	8.6	10.5
Diluted P/E (x)	41.0	32.5	26.0	20.8
P/B (x)	8.0	6.7	5.8	4.9
EV / Sales (x)	2.2	2.1	1.8	1.5
EV / EBITDA (x)	25.3	20.1	16.1	12.8
Dividend Yield (%)	1.0	0.8	1.2	1.6

Additional Data

Directors Data

Dilip G Piramal	Chairman & Non Executive Director	Radhika Piramal	Managing Director
Ashish K Saha	Director Works	DK Poddar	Independent - Non-Executive Director
Vijay Kalantri	Independent - Non-Executive Director	G.L. Mirchandani	Independent - Non-Executive Director
Nabankur Gupta	Independent - Non-Executive Director	Rajeev Gupta	Independent - Non-Executive Director
Amit Jatia	Independent - Non-Executive Director		

Auditors - Price Waterhouse Chartered Accountants LLP

Holding Top -10

	Perc. Holding		Perc. Holding
SBI Funds	4.45	Religare India AMC	1.40
Reliance Capital	3.03	Dimensional Fund Advisors	1.22
Templeton Asset Management	2.35	ICICI Pru AMC	1.06
Birla Sun Life AMC	1.86	Van Eck Associates	0.29
HDFC Asset Management	1.74	LIC Nomura Mutual Fund	0.17

*as per last available data

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

*as per last available data

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
13 Jun 2016	Mr. Dilip G. Piramal and Mrs. Shalini Piramal	Sell	288640.00

*as per last available data

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Coverage group(s) of stocks by primary analyst(s): Miscellaneous

AIA Engineering, Apar Industries Ltd, Aarti Industries, Agro Tech Foods, Balkrishna Industries, CCL Products India, Essel Propack, Orient Refactories, Supreme Industries, Solar Industries, SRF, Vesuvius India, VIP Industries

Recent Research

Date	Company	Title	Price (INR)	Recos
28-Feb-17	**Vesuvius India**	Decent quarter; margin dip on one off; *Result Update*	1,215	Buy
23-Feb-17	**Orient Refractories**	Decent show despite challenges; *Result Update*	137	Buy
15-Feb-17	**VIP Industries**	Growth stable; margins catapult; *Result Update*	148	Buy

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution* * 1stocks under review	161	67	11	240

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	156	62	11

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart

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