

Splendid volume growth boosts earnings...

Revenue (net of GST) for the quarter increased 25.3% YoY to ₹ 304.7 crore, above our estimate of ₹ 269 crore. Cigarette sales increased 26% to ₹ 245 crore led by 20% YoY volume growth along with blended price hike of 1-2% and change in product mix. There is significant shift towards the contribution of ₹5-6/stick price point which now contributes ~60% of volumes from ~20% three years back. Aided by higher EBITDA, net profit for the quarter surged 23.6% YoY to ₹ 75.7 crore.

Dealer stocking before Union Budget leads to increased sales

With 20% volume growth during the quarter, the company posted one of the strongest quarters in the last five years. However, strong volumes have been led by dealer stocking of a week of additional inventories before the Budget in anticipation of introduction of excise duty. We believe Q2FY20 would witness moderation in volume growth with correction in inventory at the dealer level. In the last two years, the company has changed its product mix in favour of ₹ 5-6 price point, which now accounts of 60% of the portfolio. Moreover, 'Edition' brand at ₹ 10 /stick accounts for 4-5% of volumes. We change our volume growth estimates to 8% (earlier 4%) for FY20E as volumes for the company have been growing much above industry average of 4%. This results in ~6% increase in our PAT estimates for both FY20E & FY21E. We estimate earnings CAGR of 13.8% in FY19-21E.

Change in sales mix to aid EBITDA/stick, margins

With a favourable product mix, EBITDA/stick has improved from ₹ 0.24 in FY14 to ₹ 0.43 in FY19. Given higher sales mix of high price cigarettes (20%+) and volume recovery, we estimate a further improvement in EBITDA/stick to ₹ 0.46 in FY20E and ₹ 0.47 in FY21E. At CMP, dividend yield is ~3% and dividend payout is 65%. VST is generating strong cash flows from its cigarettes business. Also, given low capex requirement, maximum cash flows are distributed as dividend. With high dividend payout, the business enjoys healthy return ratios (FY19: RoCE – 53.2%, RoNW – 34.6%).

Valuation & Outlook

With over 85 years of presence, VST Industries has positioned itself as the lowest cost filter cigarette provider with market presence in south, south central, UP and north-east states. The company's fundamentals are driven by a strong capital structure, steady cash flow and adequate liquidity. VST has a healthy portfolio of investments (mainly in debt mutual funds) and cash of ₹ 610 crore as on FY19, supporting liquidity. The company has a robust margin profile with its operating margin at 32.3% for FY19. With robust volume growth this quarter and strong volume growth guidance of 8% for FY20E, we upgrade the stock to **BUY** recommendation with a revised target price of ₹ 4,200/share.



VST Industries Ltd.

Particulars

Particulars (₹ crore)	Amount
Market Capitalization	5,250.2
Total Debt (FY19)	0.0
Cash and Investments (FY19)	609.9
EV	4,640.3
52 week H/L (₹)	3838 / 2482
Equity capital	₹ 15.4
Face value (₹)	10.0

Key Highlights

- The sales volume contribution of 64 mm category was 45% and the balance 55% was contributed by 69 mm and above categories
- The company has 'Edition' brand in King Size category, which contributed 4-5% to volumes. The ₹ 5-6 price point contributed 60% of volumes for the quarter
- Upgrade the stock from HOLD to BUY recommendation with a revised target price of ₹ 4,200 per share

Research Analyst

Sanjay Manyal
sanjay.manyal@icicisecurities.com

Kapil Jagasia, CFA
kapil.jagasia@icicisecurities.com

Key Financial Summary

Key Financials	FY17	FY18	FY19	FY20E	FY21E	CAGR (FY19-21E)
Net Sales	918.3	946.4	1097.6	1259.6	1362.5	11.4%
EBITDA	247.7	294.8	353.6	417.6	450.1	12.8%
EBITDA Margin %	27.0	31.2	32.2	33.2	33.0	
Net Profit	151.5	181.9	226.8	270.0	293.6	13.8%
EPS (₹)	98.13	117.80	146.90	174.87	190.17	
P/E	34.6	28.9	23.1	19.4	17.9	
RoNW %	28.1	31.3	34.2	35.8	35.4	
RoCE (%)	42.0	46.9	51.4	53.2	52.5	

Source: Company, ICICI Direct Research

Exhibit 1: Variance Analysis

	Q1FY20	Q1FY20E	Q1FY19	YoY (%)	Q4FY19	QoQ (%)	Comments
Total Operating Income	304.7	268.6	243.2	25.3	272.6	11.8	Led by strong volume growth of 20%, net sales increased 25.3% during the quarter
Other Operating Income	0.2	0.4	0.4	-46.5	0.3	-17.9	
Raw Material Expenses	134.1	115.7	100.5	33.4	146.2	-8.3	
Employee Expense	25.9	24.7	23.4	10.5	21.2	22.2	
Excise Duty	24.6	21.2	19.9	23.5	21.6	13.7	
Other operating Expenses	29.6	25.6	23.3	26.9	24.1	22.6	
EBITDA	115.1	102.7	95.9	20.1	81.1	41.9	Operating profit increased 20.1% during the quarter
EBITDA Margin (%)	37.8	38.2	39.4	-165 bps	29.8	802 bps	Operating margins contracted 165 bps mainly due to 266 bps contraction in gross margins, partly mitigated by 114 bps saving in employee costs to sales
Depreciation	9.4	11.3	9.3	0.4	11.2	-16.1	
Interest	0.0	0.0	0.0	NA	0.0	NA	
Other Income	11.8	8.2	8.4	40.6	10.8	9.0	
PBT	117.5	99.5	95.0	23.8	80.8	45.5	
Tax Outgo	41.9	33.8	33.7	24.2	27.8	50.8	
PAT	75.7	65.8	61.2	23.6	53.0	42.7	Net profit increased 23.6% led by higher operating and other income
Key Metrics							
Cigarette Sales (₹ crore)	286.0	249.0	227.6	25.7			Cigarettes volumes grew a strong 20% during the quarter
Tobacco Sales (₹ crore)	43.0	40.5	35.0	22.9			Tobacco sales witnessed growth of 23% during the quarter with 12% margins

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY20E			FY21E			Comments
	Old	New	% change	Old	New	% change	
Net sales	1222.3	1259.6	3.1	1,321.8	1,362.5	3.1	On the back of robust volume growth this quarter and strong volume growth guidance for FY20E, we change our revenue and earnings estimates
EBITDA	393.6	417.6	6.1	423.9	450.1	6.2	
EBITDA Margin (%)	32.2	33.2	95 bps	32.1	33.0	97 bps	
PAT	253.9	270.0	6.3	276.0	293.6	6.4	
EPS (₹)	164.44	174.87	6.3	178.78	190.17	6.4	

Source: Company, ICICI Direct Research

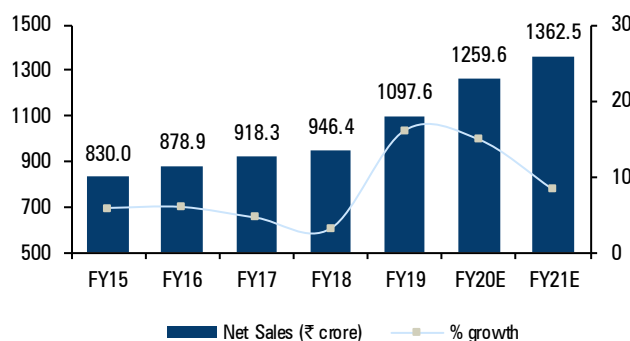
Exhibit 3: Assumptions

	Current				Earlier			Comments
	FY17	FY18	FY19	FY20E	FY21E	FY20E	FY21E	
Cig. Vol. (mn sticks)	7,280.0	7,370.0	7,886.4	8,517.3	8,858.0	8,201.9	8,529.9	We increase our volume estimates for FY20E
Cig. Vol. Growth (%)	-1.0	0.6	8.0	8.0	4.0	4.0	4.0	
Realization/cig (₹)	2.8	2.9	1.2	1.3	1.3	1.3	1.3	
Tobacco Sales(₹ crore)	275.0	250.0	259.5	270.0	280.9	270.0	280.9	
% of <64mm in sales	55.0	50.0	40.0	40.0	40.0	40.0	40.0	
% of >64mm in sales	45.0	50.0	60.0	60.0	60.0	60.0	60.0	

Source: Company, ICICI Direct Research

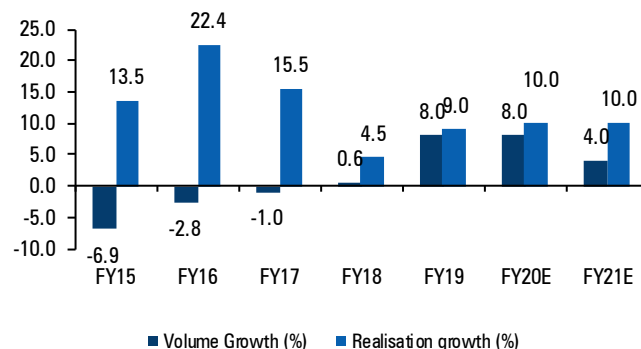
Key Metrics

Exhibit 4: Net revenue to grow at 11% CAGR over FY19-21E



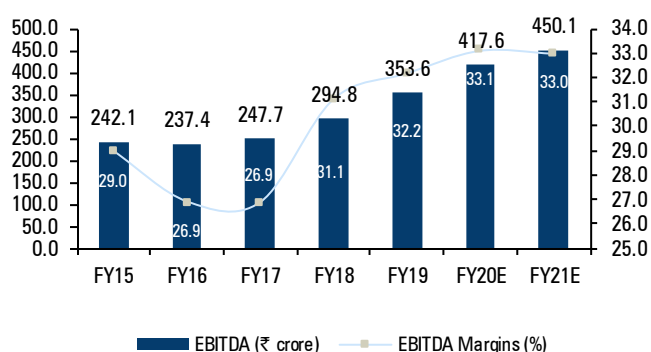
Source: ICICI Direct Research, Company

Exhibit 5: Volume growth to stabilise, going forward



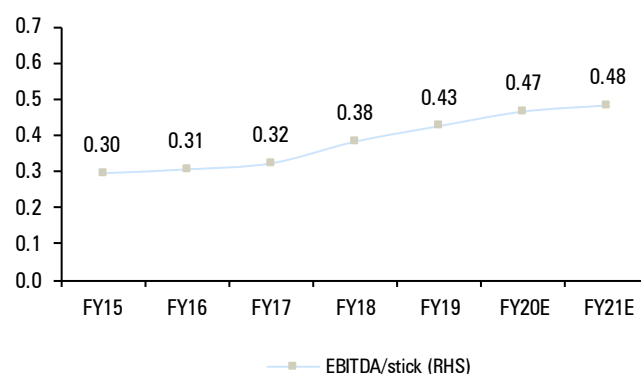
Source: ICICI Direct Research, Company

Exhibit 6: Improved product mix to aid EBITDA margins



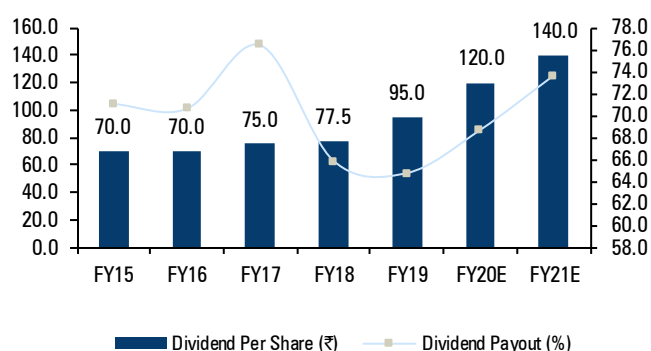
Source: Company, ICICI Direct Research

Exhibit 7: Healthy growth in EBITDA/stick (₹)



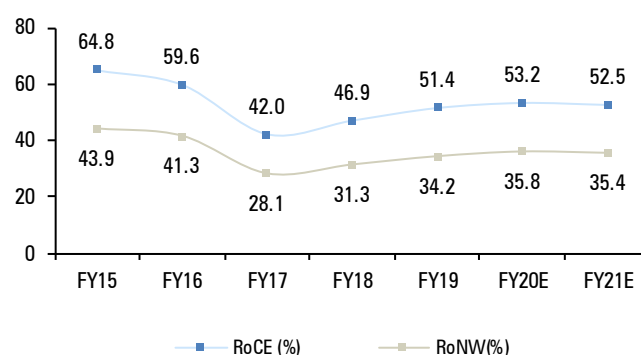
Source: Company, ICICI Direct Research

Exhibit 8: High dividend payout to continue



Source: Company, ICICI Direct Research

Exhibit 9: Return ratios to improve

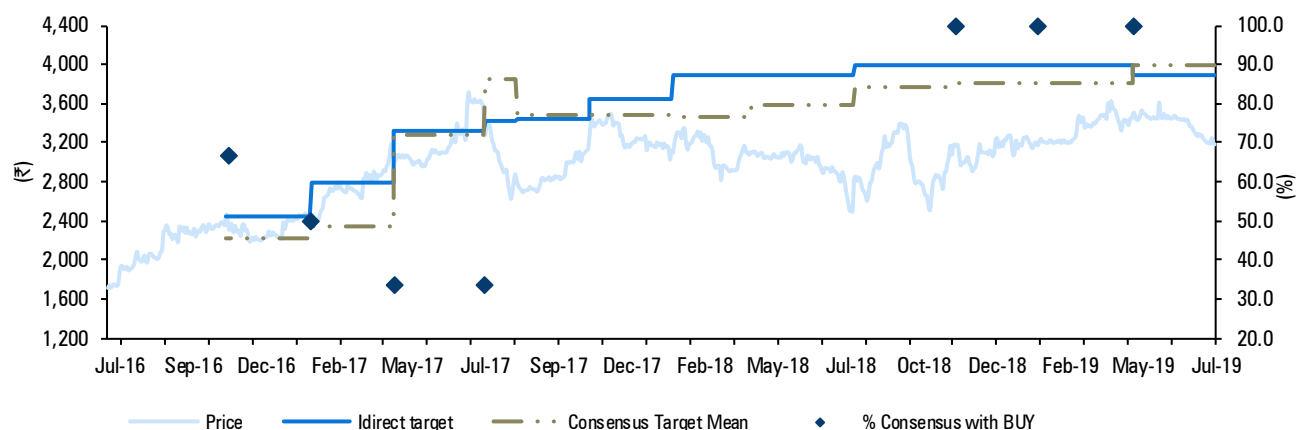


Source: Company, ICICI Direct Research

Exhibit 10: Valuation

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY18	946.4	2.4	117.8	13.6	28.9	17.6	31.3	46.9
FY19	1097.6	16.0	146.9	24.7	23.1	14.7	34.2	51.4
FY20E	1259.6	14.8	174.9	19.0	19.4	12.3	35.8	53.2
FY21E	1362.5	8.2	190.2	8.7	17.9	11.5	35.4	52.5

Source: Company, ICICI Direct Research

Exhibit 11: Recommendation History vs. Consensus


Source: Bloomberg, Company, ICICI Direct Research

Exhibit 12: Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	British American Tobacco PLC	30-Jun-19	31.73	4.9	0.0
2	Bright Star Investments Pvt. Ltd.	30-Jun-19	25.95	4.0	0.0
3	HDFC Asset Management Co., Ltd.	30-Jun-19	8.89	1.4	0.0
4	Matthews International Capital Management, L.L.C.	31-Mar-19	7.89	1.2	0.0
5	DSP Investment Managers Pvt. Ltd.	30-Jun-19	3.76	0.6	0.0
6	The New India Assurance Co. Ltd.	30-Jun-19	1.53	0.2	0.0
7	L&T Investment Management Limited	30-Jun-19	1.35	0.2	0.0
8	Tata Asset Management Limited	30-Jun-19	1.10	0.2	0.0
9	IDBI Asset Management Limited	30-Jun-19	0.69	0.1	0.0
10	ICICI Prudential Asset Management Co. Ltd.	30-Jun-19	0.46	0.1	0.0

Source: Reuters, ICICI Direct Research

Exhibit 13: Recent Activity

Buys			Sells		
Investor name	Value	Shares	Investor name	Value	Shares
Tata Asset Management Limited	0.50m	0.01m	Fidelity Management & Research (Hong Kong) Limited	-0.60m	-0.01m
L&T Investment Management Limited	0.32m	0.01m	DSP Investment Managers Pvt. Ltd.	-0.51m	-0.01m
			SEI Investments Canada	-0.03m	0.00m
			Acadian Asset Management LLC	-0.02m	0.00m
			State Street Global Advisors (US)	-0.02m	0.00m

Source: Reuters, ICICI Direct Research

Exhibit 14: Shareholding Pattern

(in %)	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19
Promoter	32.2	32.2	32.2	32.2	32.2
FII	9.5	9.8	9.2	8.9	8.8
DII	15.5	16.2	17.0	17.9	18.3
Others	42.8	41.9	41.6	41.1	40.8

Source: Company, ICICI Direct Research

Financial summary

Exhibit 15: Profit and loss statement ₹ crore				
(Year-end March)	FY18	FY19	FY20E	FY21E
Gross Revenue	947.6	1099.0	1261.3	1364.5
Growth (%)	2.7	16.0	14.8	8.2
Raw Material Expenses	470.3	550.2	583.9	633.7
Employee Expenses	89.2	92.3	121.1	130.8
Excise Duty	411.1	85.1	87.6	94.7
Administrative Expenses	12.1	0.0	0.0	0.0
Other expenses	67.9	103.0	138.7	149.9
Total Operating Expenditure	652.8	745.4	843.7	914.4
EBITDA	294.8	353.6	417.6	450.1
Growth (%)	19.0	19.9	18.1	7.8
Depreciation	39.2	41.4	47.3	41.3
Interest	0.0	0.0	0.0	0.0
Other Income	0.0	0.0	0.0	0.0
PBT	279.5	350.7	403.0	438.2
Others	23.8	38.5	32.6	29.4
Total Tax	97.6	123.8	133.0	144.6
PAT	181.9	226.8	270.0	293.6
Growth (%)	20.1	24.7	19.0	8.7
EPS (₹)	117.8	146.9	174.9	190.2

Source: Company, ICICI Direct Research

Exhibit 16: Cash flow statement ₹ crore				
(Year-end March)	FY18	FY19	FY20E	FY21E
Profit after Tax	178.4	226.8	270.0	293.6
Add: Depreciation	39.2	41.4	47.3	41.3
(Inc)/dec in Current Assets	5.0	-154.5	274.7	-52.8
Inc/(dec) in CL and Provisions	221.1	56.4	-369.0	8.9
CF from operating activities	420.1	165.6	222.9	291.0
(Inc)/dec in Investments	-220.9	-0.2	0.5	-0.1
(Inc)/dec in Fixed Assets	-43.2	-25.7	-0.4	-80.0
(Inc)/dec in LT Loans & Adv.	0.0	0.0	0.0	0.0
Others	0.0	0.0	-14.7	0.3
CF from investing activities	-264.1	-26.0	-14.6	-79.8
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	0.0	0.0	0.0	0.0
Dividend paid & dividend tax	-139.4	-140.0	-171.6	-216.8
Inc/(dec) in Reval. Reserve	0.0	0.0	0.0	0.0
Inc/(dec) in Exch. Fluc. Res.	0.0	0.0	0.0	0.0
CF from financing activities	-139.4	-140.0	-171.6	-216.8
Net Cash flow	16.6	-0.3	36.7	-5.6
Opening Cash	11.9	28.5	28.2	64.9
Closing Cash	28.5	28.2	64.9	59.3

Source: Company, ICICI Direct Research

Exhibit 17: Balance sheet ₹ crore				
(Year-end March)	FY18	FY19	FY20E	FY21E
Liabilities				
Equity Capital	15.4	15.4	15.4	15.4
Reserve and Surplus	566.7	648.6	738.3	815.1
Total Shareholders funds	582.1	664.0	753.7	830.6
Total Debt	0.0	0.0	0.0	0.0
Long Term Provisions	14.2	18.5	3.8	4.1
Total Liabilities	596.2	682.5	757.5	834.7
Assets				
Gross Block	270.0	300.0	330.0	390.0
Less: Acc Depreciation	75.0	116.3	163.6	204.8
Net Block	195.1	213.3	166.5	185.2
Capital WIP	34.2	0.3	0.3	20.3
Deferred Tax Asset	24.8	31.0	31.0	31.0
Non Current Investments	2.0	2.3	1.7	1.9
LT Loans & Advances/Others	3.2	1.3	1.3	1.3
Current Assets				
Inventory	252.9	281.9	345.1	373.3
Debtors	27.3	14.3	17.3	18.7
Cash	37.6	36.9	64.9	59.3
Loans & Advances	0.0	0.0	8.6	9.3
Current Investments	414.1	573.1	276.1	298.6
Other CA	73.0	52.5	0.0	0.0
Current Liabilities				
Creditors	58.1	83.0	44.9	44.8
Provisions	0.0	0.0	0.0	0.0
Other CL	409.8	441.3	110.4	119.5
Net Current Assets	337.0	434.3	556.7	594.9
Total Assets	596.2	682.5	757.5	834.7

Source: Company, ICICI Direct Research

Exhibit 18: Key ratios ₹ crore				
(Year-end March)	FY18	FY19	FY20E	FY21E
Per share data (₹)				
EPS	117.8	146.9	174.9	190.2
Cash EPS	143.2	173.7	205.5	216.9
BV	377.0	430.0	488.2	537.9
DPS	77.5	95.0	120.0	140.0
Cash Per Share	24.3	23.9	42.0	38.4
Operating Ratios (%)				
EBITDA Margin	31.1	32.2	33.1	33.0
PBT / Net Sales	29.5	31.9	32.0	32.2
PAT Margin	19.2	20.7	21.4	21.6
Inventory days	97.5	93.7	100.0	100.0
Debtor days	10.5	4.8	5.0	5.0
Creditor days	22.4	27.6	13.0	12.0
Return Ratios (%)				
RoE	31.3	34.2	35.8	35.4
RoCE	46.9	51.4	53.2	52.5
RoIC	51.7	53.7	56.3	56.7
Valuation Ratios (x)				
P/E	28.9	23.1	19.4	17.9
EV / EBITDA	17.6	14.7	12.3	11.5
EV / Net Sales	5.5	4.7	4.1	3.8
Market Cap / Sales	5.5	4.8	4.2	3.9
Price to Book Value	9.0	7.9	7.0	6.3
Solvency Ratios				
Debt/EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	1.6	1.8	4.2	4.3
Quick Ratio	1.1	1.2	1.9	2.0

Source: Company, ICICI Direct Research

Exhibit 19: ICICI Direct coverage universe (FMCG)

Sector / Company	CMP	TP	M Cap	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)			
	(₹)	(₹) Rating		(₹ Cr)	FY19E	FY20E	FY21E	Y19E	FY20E	Y21E	Y19E	FY20E	FY21E	Y19E	FY20E	FY21E	FY19E	FY20E	FY21E
Colgate (COLPAL)	1,160	1,250	Hold	32,502	28.5	30.9	33.8	40.7	37.6	34.3	7.3	6.7	6.2	70.7	71.6	71.0	52.2	50.7	50.1
Dabur India (DABIND)	425	500	Buy	74,651	8.2	9.0	9.9	51.9	47.4	42.8	8.7	7.9	7.1	29.6	27.6	28.1	25.7	23.6	24.0
GSK CH (GLACON)	7,300	8,340	Buy	30,028	166.5	233.7	244.1	43.9	31.2	29.9	6.9	6.3	5.8	29.8	36.1	33.4	20.1	24.0	22.8
Hindustan Unilever (HINLEV)	1,700	1,900	Hold	378,000	28.5	32.9	37.9	59.6	51.7	44.9	9.9	8.7	7.6	100.8	123.7	162.3	87.2	106.9	141.3
ITC Limited (ITC)	270	340	Buy	352,275	10.3	11.3	12.6	26.3	24.0	21.4	7.9	7.2	6.6	30.8	32.7	33.3	21.5	22.2	22.6
Jyothy Lab (JYOLAB)	155	180	Hold	5,817	5.3	5.9	6.4	29.2	26.4	24.1	3.3	3.1	2.8	28.6	29.3	30.7	22.6	22.3	23.3
Marico (MARLIM)	365	425	Buy	46,963	8.8	8.7	9.8	41.5	42.1	37.4	6.4	5.5	4.9	38.0	42.6	41.7	31.6	35.8	34.6
Nestle (NESIND)	11,500	12,000	Buy	100,277	166.7	199.7	238.9	69.0	57.6	48.1	8.9	8.0	7.0	42.9	44.5	47.6	45.6	45.9	47.0
Tata Global Bev (TATGLO)	255	250	Buy	12,622	7.2	7.9	8.7	35.2	32.3	29.2	1.7	1.7	1.6	8.4	9.1	9.5	6.5	7.2	7.6
VST Industries (VSTIND)	3,400	4,200	Buy	5,250	146.9	174.9	190.2	23.1	19.4	17.9	4.8	4.2	3.9	51.4	53.2	52.5	34.2	35.8	35.4
Varun Beverage (VARBEV)	665	693	Hold	17,890	11.7	16.4	12.6	56.7	40.5	52.7	4.5	3.5	2.5	12.7	14.2	13.1	12.1	15.0	10.7

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com

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