

Sector: Consumer Goods  
Company Update

	Change
Reco: Buy	↑
CMP: Rs. 1,500	
Price Target: Rs. 1,780	↑

↑ Upgrade ↔ No change ↓ Downgrade

## Company details

Market cap:	Rs. 8,650 cr
52-week high/low:	Rs. 1830/1085
NSE volume: (No of shares)	14,462
BSE code:	531335
NSE code:	ZYDUSWELL
Sharekhan code:	ZYDUSWELL
Free float: (No of shares)	1.9 cr

## Shareholding (%)

Promoters	67.6
FII	4.7
DII	19.2
Others	8.5

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	2.8	5.1	7.0	-5.3
Relative to Sensex	8.0	9.0	1.0	-6.3

Sharekhan Research, Bloomberg

Zydus Wellness Limited's (ZWL's) Q1FY2020 results are not comparable y-o-y due to consolidation of the acquired Heinz portfolio. ZWL's base portfolio grew by 10% while the Heinz portfolio grew by 20% in Q1FY2020. OPM stood strong at about 20%. The management has indicated at a sustained double-digit growth on a comparable basis and a 200 bps improvement in OPM in the next two years. We have increased our earnings estimates to factor in higher than estimated growth for the Heinz portfolio. In view of improved earning visibility, we upgrade the stock to Buy with a revised price target (PT) of Rs.1,780.

## Key positives

- Key brands such as Sugarfree, Everyuth Scrub, Everyuth Peeloff, Nycil and Glucon D maintained leadership positioning in their respective categories.
- The Heinz Portfolio grew by 20% due to seasonality factor (Q1 contributes 30% to overall sales).
- Heinz portfolio gained market share (Glucon D - 51 bps, Nycil – 105 bps).
- OPM jumped significantly to 19.7% in Q1FY2020 as against 8.1% in Q1FY2019.

## Key negatives

- Sugarfree grew by just 3.8%; ZWL has ~94% market share
- Consolidated gross margins declined to 59.2% in Q1FY2020 from ~68% in Q1FY2019 on account of lower gross margins of 55% in the Heinz portfolio.

## Our Call

**Valuation:** The Heinz portfolio performed extremely well in Q1FY2020 (30% of overall Heinz sales) with strong traction in the Nycil and Glucon D brands. The company is focusing on improving growth prospects for Complian in the next six months through adequate investments on brands and re-aligning the distribution system. If acquired brands continue to perform well and OPM improves by 80-100 bps in the coming years, the Heinz acquisition will be earnings accretive by FY2021. In view of improved earning visibility, we upgrade the stock from Hold to Buy with a revised price target of Rs. 1,780 (valuing stock at 32x its FY2021E earnings).

## Key Risks

- As ZWL's operates in niche, discretionary categories, any macroeconomic slowdown will affect growth of these categories.
- Slow growth in the Heinz's portfolio will prolong the time for the acquisition to become earnings positive.

## Valuation (consolidated)

Particulars	FY17	FY18	FY19	FY20E*	FY21E*
Revenue	463	503	843	1,993	2,318
OPM (%)	21.4	24.9	20.7	20.0	20.7
Adjusted PAT	111	137	171	241	320
% YoY growth	5.7	22.7	25.4	40.8	32.9
Adjusted EPS (Rs.)	28.5	34.9	29.7	41.8	55.6
P/E (x)	52.7	42.9	50.5	35.9	27.0
P/B (x)	10.5	8.5	2.6	2.4	2.2
EV/EBIDTA (x)	58.6	45.4	49.3	21.4	17.6
RoNW (%)	21.5	21.9	8.4	6.9	8.6
RoCE (%)	23.0	22.9	7.1	7.6	8.7

Source: Company, Sharekhan Estimartes

\* Estimates are including the Heinz consolidation

**Q1FY2020 numbers not comparable with Q1FY2019 on Heinz acquisition**

**Revenue stood at Rs. 620 crore; OPM at 19.7%:** Q1FY2020 revenue stood at Rs. 620.3 crore as against Rs. 131.6 crore in Q1FY2019. The ZWL base portfolio grew by 10% (entirely volume led) for the quarter whereas the Heinz portfolio registered a healthy 20% growth (volume led growth of 12-13% and 7-8% price led growth). The strong growth in the Heinz portfolio was mainly on account of robust performance of the summer products such as Glucon-D and Nycil which registered double-digit growth during the quarter. All key brands including Sugar Free, Everyuth scrub, Everyuth Peel-off and Glucon-D maintained their leadership positions. Gross margin stood at 59.2% (Gross margin of Heinz portfolio stood at 55%+). OPM stood at 19.7% in Q1FY2020, while the Q1FY2019 number was 8.1%. Operating profit stood at Rs. 122 crore. Adjusted PAT stood at Rs. 80.4 crore as against Rs. 15.9 crore in Q1FY2019.

**Key brands performed well:** In terms of brands, Sugar Free grew by 3.8% YTD and maintained its leadership position with a market share of 94.3% backed by media campaigns, television commercials and sampling. Sugar Free Green and Sugar Free Lite gained good traction during the quarter. Everyuth Scrub and Peel-off Mask registered 16.6% and 18% YTD growth, respectively, led by good growth in e-commerce channels and were category leaders with a market share of 32.7% and 84%, respectively. Nycil was re-launched during the quarter with a new formula and new packaging and its market share improved by 105 BPS to 33.4%. Glucon-D's market share improved by 51 BPS to 59.8% and the category grew by 17.9% YTD. Nutralite had a soft quarter registering a volume-led single-digit growth. The MFD category growth stood at 9% backed by consumer offers and Complian's market share declined marginally to 5.9%.

**Results (Consolidated)**

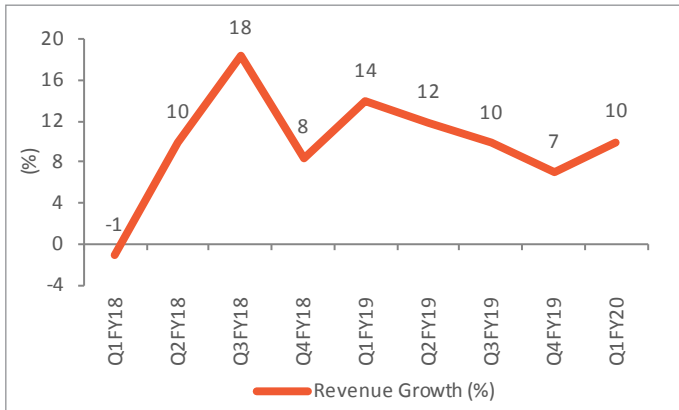
Particulars	Rs cr				
	Q1FY20	Q1FY19	YoY %	Q4FY19	QoQ %
Net Revenue	607.4	131.6	-	416.2	45.9
Total expenditure	498.2	121.0	-	340.1	46.5
Operating profit	109.1	10.6	-	76.0	43.5
Interest Expense	34.9	0.4	-	28.8	21.2
Depreciation	10.4	2.0	-	6.3	64.8
Tax	-1.9	4.0	-	-12.8	-85.6
PAT before M.I.	68.8	15.9	-	62.3	10.4
Minority Interest	0.0	0.6	-	0.0	-
PAT after M.I.	68.8	15.3	-	62.3	10.4
Exceptional item	11.6	8.5	-	0.0	-
Reported PAT	80.4	23.8	-	62.3	29.0
Reported EPS (Rs.)	20.6	6.1	-	15.9	29.0
					<b>BPS</b>
GPM (%)	58.4	68.5	-	59.8	-141
OPM(%)	18.0	8.1	-	18.3	-30

Source: Company; Sharekhan Research

\*Q1FY2019 numbers does not include the acquired portfolio and are thus, not comparable

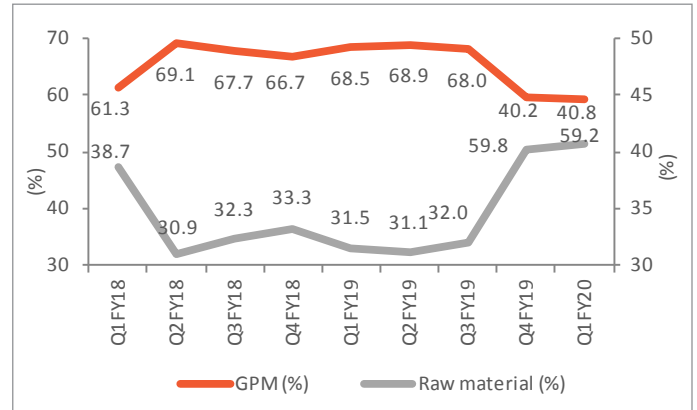
**Financials in charts**

**Comparable revenue growth stood at 10%**



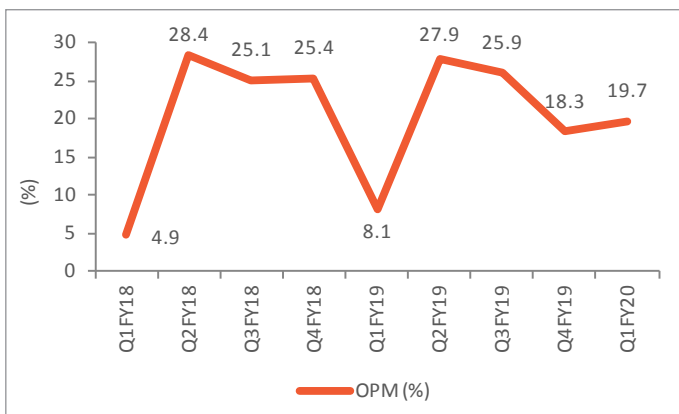
Source: Company, Sharekhan Research

**Gross margins improved**



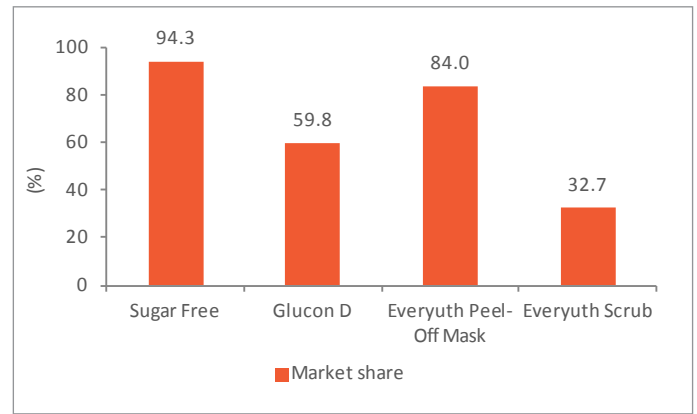
Source: Company, Sharekhan Research

**OPM stood at 19.7%**



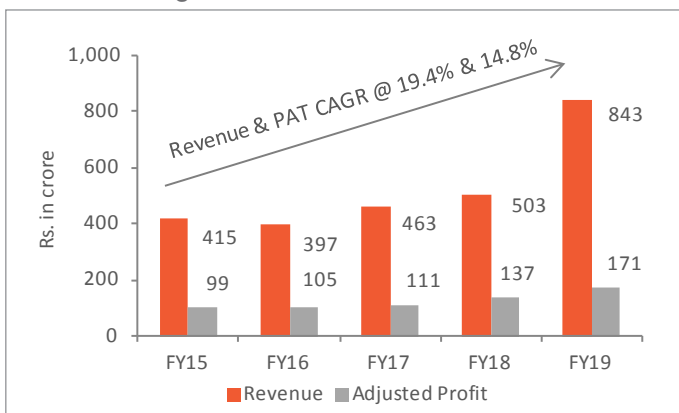
Source: Company, Sharekhan Research

**Key brands maintain leadership position**



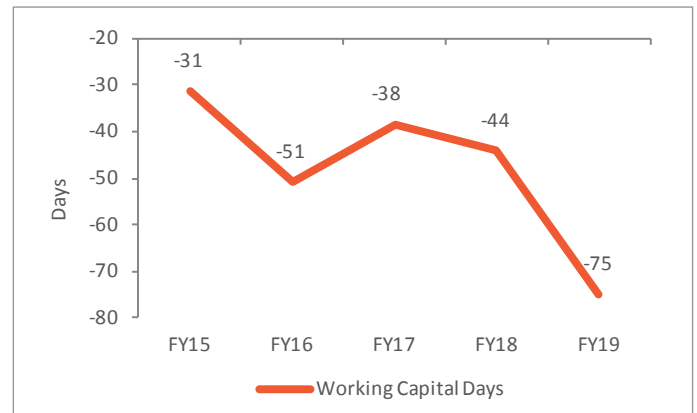
Source: Company, Sharekhan Research

**Revenue & PAT grew @ CAGR of 19.4% and 14.8%**



Source: Company, Sharekhan Research

**Working capital remains negative**



Source: Company, Sharekhan Research

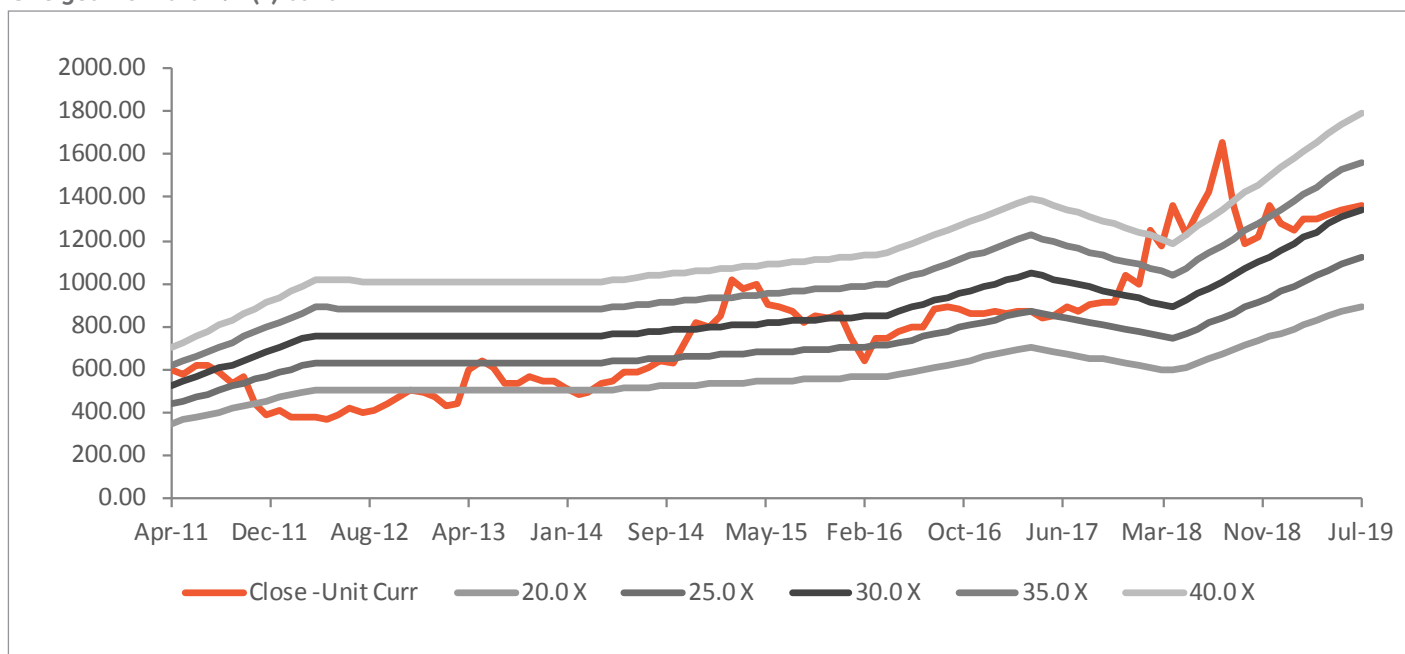
## Outlook

ZWL clocked a strong set of numbers in Q1FY2020 led by strong double-digit growth in the Heinz portfolio. The company's base product portfolio is expected to grow by 10-12% with Sugarfree expected to see a sequential improvement in growth. The Heinz portfolio will continue to do well in the coming quarters as the company will be invest on brands, re-align distribution networks and bring required SKUs into the market. The company aims to increase direct distribution reach to 5 lakh outlets from 2.5 lakh outlets currently. Also, the synergy benefits of Heinz acquisition would start flowing in from the coming quarters and OPM is expected to improve by 200 bps in the next two years (we have factored in 70 bps improvement in OPM for FY2021).

## Valuation

The Heinz portfolio performed extremely well in Q1FY2020 (30% of overall Heinz sales) with strong traction in the Nycil and Glucon D brands. The company is focusing on improving growth prospects for Complian in the next six months through adequate investments on brands and re-aligning the distribution system. If acquired brands continue to perform well and OPM improves by 80-100 bps in the coming years, the Heinz acquisition will be earnings accretive by FY2021. In view of improved earning visibility, we upgrade the stock from Hold to Buy with a revised price target of Rs. 1,780 (valuing stock at 32x its FY2021E earnings).

### One year forward P/E (x) band



Source: Sharekhan Research

### Peer valuation

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
Hindustan Unilever	60.1	50.6	43.4	42.4	36.8	32.1	113.2	109.0	96.8
Marico	49.8	41.1	35.2	36.4	29.3	25.1	40.9	44.1	44.4
Zydus Wellness	50.5	41.5	32.3	49.3	22.0	18.6	7.1	7.4	8.4

Source: Company, Sharekhan Estimates

## About company

ZyduS Wellness Limited (ZWL) is the listed entity of the ZyduS group and one of the leading companies in the fast-growing Indian consumer wellness market. The company's growth over the years has been led by pioneering brands such as Sugar Free, EverYuth and Nutralite and innovations offering new benefits to consumers. The company is the market leader in most of its product categories. The company has recently acquired Heinz India, subsidiary of Kraft Heinz. With this, ZWL's product portfolio widened to include health food drinks and energy drinks. The Heinz acquisition has also boosted ZWL's revenue trajectory to ~Rs. 2,000 crore from Rs. 600 crore earlier.

## Investment theme

ZWL has portfolio of strong brands that lead their categories. The Sugarfree brand has a 94% market share in the artificial sweeteners category, while Everyuth Peel-off mask has an 84% market share. The acquisition of Heinz enhanced the company's product portfolio and distribution reach. However, the same is earnings dilutive in the initial years as the acquisition was funded through a mix of debt and equity. The acquisition will start adding to the bottom-line in another 3-4 years, in the backdrop of a stable consumption environment.

## Key Risks

- ◆ **Macroeconomic slowdown:** ZWL is largely present in niche categories, which are discretionary in nature. Any slowdown in the macro environment will affect growth of these categories.
- ◆ **Slow growth in acquired brands:** Slow growth in acquired brands (Heinz's portfolio) will prolong the time for the acquisition to become earnings positive.
- ◆ **Increase in competition:** ZWL is facing stiff competition in skin care products such as face wash and scrubs from multinationals, which has affected the revenue growth of these categories.

## Additional Data

### Key management personnel

Sharvil P Patel	Chairman
Tarun Arora	Whole Time Director and CEO
Dhanraj P Dagar	Company Secretary

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Cadila Healthcare Ltd	63.6
2	Threpsi LLP	12.5
3	ZyduS Family Trust	4.1
4	Matthews International Capital Management	3.2
5	Life Insurance Corp Of India	2.2
6	Reliance Capital Trustee Co Ltd	1.7
7	Prazim Trading & Inv Company	1.4
8	PPFAS Asset Management	0.7
9	Dimensional Fund Advisors LP	0.4
10	Aditya Birla Sun Life Asset Management	0.2

Source: Bloomberg

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by BNP PARIBAS

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