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Q4FY20 result review and
earnings revision

Dairy

Target price: Rs360

Earnings revision

(%)	FY21E	FY22E
Sales	↓ 4.6	↓ 6.4
EBITDA	↓ 17.7	↓ 10.4
EPS	↓ 21.6	↓ 12.1

Target price revision

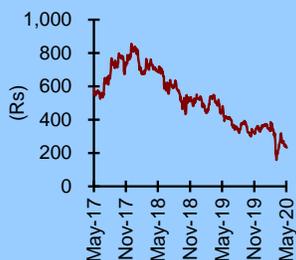
Rs360 from Rs404

Shareholding pattern

	Sep '19	Dec '19	Mar '20
Promoters	39.9	39.9	39.9
Institutional investors			
MFs and other	19.0	18.7	19.4
Banks / FI's	12.8	13.4	14.2
FII's	0.0	0.0	0.0
FII's	6.2	5.3	5.2
Others	41.1	41.4	40.7

Source: BSE

Price chart



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INDIA

Heritage Foods

BUY

Maintained

Expect margin improvement Q1FY21 onwards

Rs236

Heritage reported revenue growth of 2.8% and PAT decline of 65.6% YoY. EBITDA margin declined 350bps, YoY. We expect it to report revenue CAGR of 8.2% over FY20-22 with (1) volume CAGR of 3% and (2) price hikes of 5%. We also model value-added products (except curd) to report revenue decline in FY21-22. Post lockdown, the milk procurement prices have corrected and we expect EBITDA margins to be above 6% in FY21 due to (1) price hikes of ~10% in FY20, (2) lower sales of ghee and SMP which have lower margins and (3) correction in milk procurement prices. We model Heritage to report PAT CAGR 38.3% over FY20-FY22 with improvement in core return ratios. Maintain BUY with a target price of Rs360 (15x FY22E; Earlier TP-Rs404).

- **Price-driven growth:** Heritage reported revenue growth of 2.8%, YoY. The liquid milk volume declined 1.9%, while the value-added products revenues grew 6.3%, YoY. Curd revenues were up 26.8% YoY which indicates that other value added products (ghee, ice cream, buttermilk etc) reported revenue decline of 62% YoY. The company had raised prices of its products by ~10% in FY20.
- **EBITDA margin declined due to higher RM prices:** EBITDA margin declined 350bps, YoY, due to higher raw material prices. Milk procurement prices have increased by Rs5.6/ltr to Rs 38.5/ltr in Q4FY20 from Rs32.8/ltr in Q4FY19. In spite of lower income taxes, adjusted net profit declined 66%, YoY.
- **Correction in input prices post lockdown:** Milk procurement prices have corrected by Rs5-6/ltr post lockdown with lower demand of milk. Lower off-take by HoReCa and lower sales of value added products has impacted milk demand. The correction in milk procurement price will lead to better margins Q1FY21 onwards.
- **Decline in value added products to continue:** While revenues of curd continue to grow well, we note other value added products may continue to suffer in FY21 and expect revenue decline for other value added products in FY21. The company's yoghurt plant near Mumbai is almost ready to commence production but we believe the demand outlook for premium products is not yet encouraging.
- **Recovery in H2FY21 is essential:** Consensus expects there is shift of some consumption from H1FY21 to H2FY21 with postponement of marriages and other events. Also off-take by HoReCa will commence in H2FY21. We believe improvement in demand outlook is necessary to sustain high single digit revenue growth for Heritage.
- **Retain BUY:** We expect Heritage to report revenue and PAT CAGRs of 11.9% and 16.1%, respectively, over FY19-FY22. Core return ratios are expected to improve over the same timeframe. We reiterate our **BUY** rating on the stock with a SoTP-based target price of Rs521. We have valued the stock as per DCF methodology at Rs360 (Implied PE 15x FY22E).

Market Cap	Rs10.9bn/US\$145mn	Year to March	FY19	FY20P	FY21E	FY22E
Reuters/Bloomberg	HEFI.BO / HTFL IN	Revenue (Rs mn)	25,148	27,259	29,191	31,901
Shares Outstanding (mn)	46.4	Adj. Net Profit (Rs mn)	853	582	812	1,114
52-week Range (Rs)	455/158	Dil. Rec. EPS (Rs)	18.4	12.5	17.5	24.0
Free Float (%)	61.1	% Chg YoY	55.8	(31.8)	39.4	37.2
FII (%)	5.2	P/E (x)	12.8	18.8	13.5	9.8
Daily Volume (US\$'000)	177	CEPS (Rs)	28.0	23.4	30.2	39.0
Absolute Return 3m (%)	(37.2)	EV/EBITDA (x)	6.9	10.1	7.2	5.7
Absolute Return 12m (%)	(47.8)	Dividend Yield (%)	0.8	1.1	1.1	1.2
Sensex Return 3m (%)	(20.3)	RoCE (%)	13.1	8.5	16.3	21.9
Sensex Return 12m (%)	(19.5)	RoE (%)	10.5	8.9	15.7	18.6

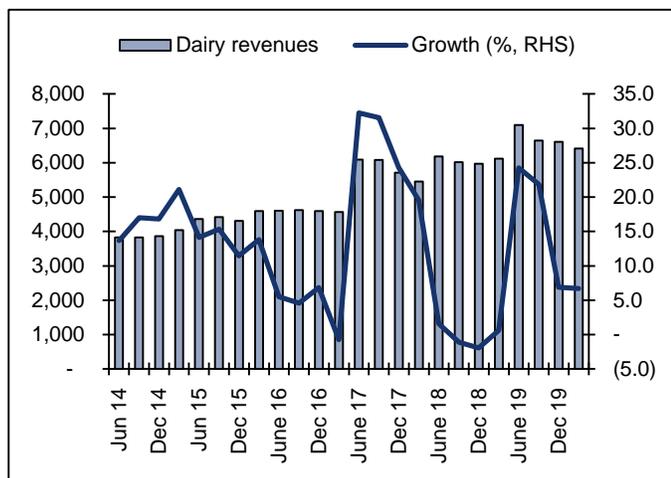
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Table 1: Q4FY20 financial performance*(Rs mn, year ending March 31)*

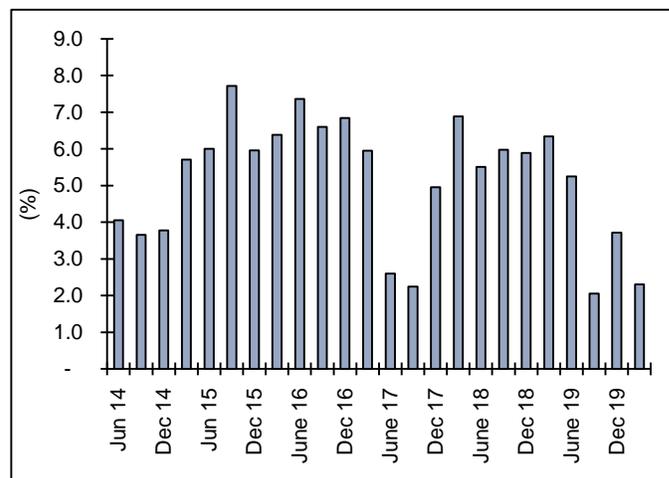
Y/e March	Q4FY20	Q4FY19	YoY gr.	Q3FY20	QoQ gr.
Revenue	6,526	6,350	2.8	6,724	(2.9)
Expenditure					
Raw materials	5,363	4,960	8.1	5,465	(1.9)
% of revenue	82.2	78.1		81.3	
Employee cost	362	330	9.9	399	(9.3)
% of revenue	5.6	5.2		5.9	
Other expenditure	526	570	(7.6)	526	(0.0)
% of revenue	8.1	9.0		7.8	
Total expenditure	6,252	5,859	6.7	6,391	(2.2)
EBITDA					
EBITDA	275	491	(44.1)	334	(17.7)
EBITDA margin	4.2	7.7		5.0	
Other income	19	32	(38.5)	13	48.6
PBDIT	294	522	(43.7)	347	(15.2)
Depreciation	118	113	4.0	128	(8.3)
PBIT	176	409	(56.9)	218	(19.3)
Interest	65	63	2.4	54	19.7
PBT	112	346	(67.7)	164	(32.1)
Prov for tax	30	108	(72.5)	45	(33.8)
% of PBT	26.6	31.2		27.3	
Adjusted PAT	82	238	(65.6)	119	(31.4)
Extra ordinary items	(3,351)	(267)	1,153.9	(184)	1,722.8
Reported PAT	(3,270)	(29)	11,041.5	(64)	4,975.3

Source: Company data, I-Sec research

Key performance highlights

Chart 1: Revenues and revenue growth

Source: Company data, I-Sec research

Chart 2: EBIT margin of dairy segment

Source: Company data, I-Sec research

Table 2: Key financial details

Particulars	Mar 18	Jun 18	Sept 18	Dec 18	Mar 19	Jun 19	Sept 19	Dec 19	Mar 20
Liquid milk sales (llpd)	10.4	10.8	11.4	11.1	11.2	11.6	12.1	11.3	10.9
Milk price realization (Rs/ltr)	39.0	38.9	38.8	38.9	38.9	39.8	41.0	42.5	44.3
Mil procurement (llpd)	13.2	13.5	13.4	14.5	14.0	15.0	13.9	13.6	12.7
Milk procurement price (Rs/ltr)	33.4	32.4	31.7	32.5	32.8	33.4	35.1	36.5	38.5
Packaged curd as % Value added products	74.0	78.0	76.0	78.0	77.0	77.0	89.3	91.1	91.9

Source: Company data, I-Sec research

Valuation and risks

We expect Heritage to report revenue and PAT CAGRs of 8.2% and 38.3%, respectively, over FY20-FY22 and core RoE to expand from 19% in FY20 to 25.8% in FY22. We value the stock at a target price of Rs360 as per DCF methodology. At the DCF price, the implied P/E works out to 15x on FY22E EPS. Maintain **BUY**.

Table 3: DCF valuation

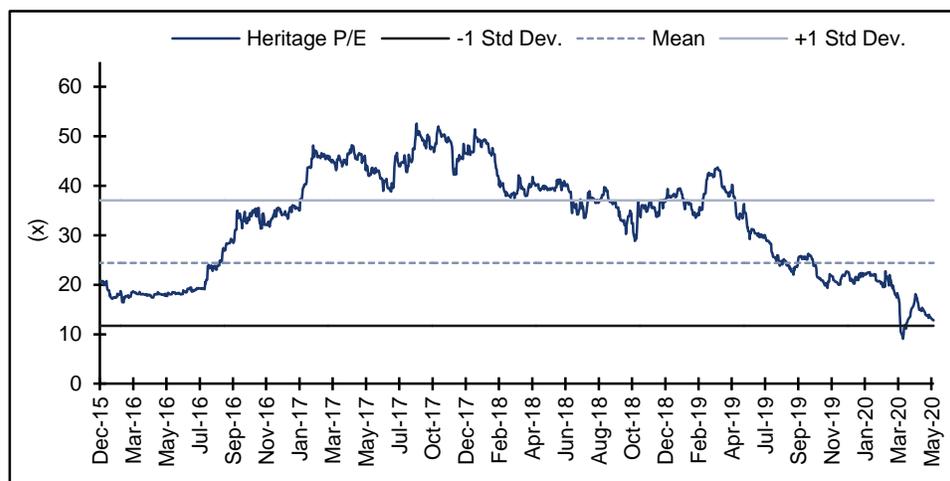
Particulars	Amt (Rs)
Cost of Equity	13.5%
Terminal growth rate	3.0%
Discounted interim cash flows	8,706
Discounted terminal value	8,016
Total equity value	16,722
Value per share (Rs)	360

Source: Company data, I-Sec research

Mean P/E and standard valuation

The stock has traded at an average P/E of 28x over the past eight years. The stock is trading near its Mean PE- 1 SD now.

Chart 3: Mean P/E and standard deviation



Source: Company data, I-Sec research

Risks

Sharp increase in input prices and/or competitive pressures

Any major increase in commodity prices and/or competitive pressures will result in downside to our estimates.

Financial summary

Table 4: Profit & loss statement

(Rs mn, year ending March 31)

	FY19	FY20P	FY21E	FY22E
Net Sales	25,148	27,259	29,191	31,901
Operating Expenses	23,261	25,966	27,395	29,619
EBITDA	1,887	1,293	1,797	2,282
% margins	7.5	4.7	6.2	7.2
Depreciation & Amortisation	447	501	590	696
Gross Interest	215	226	176	100
Other Income	90	89	81	31
Recurring PBT	1,316	654	1,111	1,517
Less: Taxes	447	153	283	387
Less: Minority Interest	16	(82)	16	16
Net Income (Reported)	853	582	812	1,114
Extraordinaries (Net)	(493)	(3,897)	-	-
Recurring Net Income	361	(3,315)	812	1,114

Source: Company data, I-Sec research

Table 5: Balance sheet

(Rs mn, year ending March 31)

	FY19	FY20P	FY21E	FY22E
Assets				
Total Current Assets	2,749	2,461	2,079	2,224
of which cash & cash eqv.	747	582	86	65
Total Current Liabilities & Provisions	2,310	2,308	2,510	2,744
Net Current Assets	439	152	(431)	(520)
Investments	5,514	1,892	1,892	1,892
Net Fixed Assets	4,719	4,752	5,735	5,939
Capital Work-in-Progress	418	773	-	-
Total Assets	11,090	7,570	7,196	7,311
Liabilities				
Borrowings	2,684	2,729	1,679	829
Deferred Tax Liability	263	224	224	224
Minority Interest	117	22	22	22
Equity Share Capital	232	232	232	232
Face Value per share (Rs)	10	10	10	10
Reserves & Surplus*	7,794	4,364	5,040	6,005
Less: Misc. Exp. n.w.o.	-	-	-	-
Net Worth	8,026	4,596	5,272	6,237
Total Liabilities	11,090	7,570	7,196	7,311

Source: Company data, I-Sec research

Table 6: Quarterly trend

(Rs mn, year ending March 31)

	June 19	Sept 19	Dec 19	Mar 20
Net sales	7,212	6,796	6,724	6,526
% growth (YoY)	12.4	9.7	8.7	2.8
EBITDA	463	222	334	275
Margin (%)	6.4	3.3	5.0	4.2
Other income	25	31	13	19
Extraordinaries (Net)	110	(471)	(184)	(3,351)
Adjusted Net profit	317	(328)	(38)	(3,266)

Source: Company data, I-Sec research

Table 7: Cashflow statement

(Rs mn, year ending March 31)

	FY19	FY20P	FY21E	FY22E
Operating Cashflow	1,391	(2,909)	1,402	1,811
Working Capital Changes	(82)	122	87	68
Capital Commitments	(1,242)	(890)	(800)	(900)
Free Cashflow	67	(3,678)	689	978
Cashflow from Investing Activities	(113)	3,623	-	-
Issue of Share Capital	-	-	-	-
Inc (Dec) in Borrowings	284	45	(1,050)	(850)
Dividend paid	(112)	(155)	(136)	(149)
Change in Deferred Tax Liability	-	-	-	-
Chg. in Cash & Bank balance	115	(165)	(497)	(21)

Source: Company data, I-Sec research

Table 8: Key ratios

(Year ending March 31)

	FY19	FY20P	FY21E	FY22E
Per Share Data (Rs)				
EPS	18.4	12.5	17.5	24.0
Cash EPS	28.0	23.4	30.2	39.0
Dividend per share (DPS)	2.0	2.5	2.5	2.8
Book Value per share (BV)	178.7	103.9	118.4	139.2
Growth (%)				
Net Sales	6.0	8.4	7.1	9.3
EBITDA	44.7	(31.5)	39.0	27.0
PAT	55.8	(31.8)	39.4	37.2
Cash EPS	40.4	(16.6)	29.4	29.1
Valuation Ratios (x)				
P/E	12.8	18.8	13.5	9.8
P/CEPS	8.4	10.1	7.8	6.0
P/BV	1.3	2.3	2.0	1.7
EV / EBITDA	6.9	10.1	7.2	5.7
EV / Sales	0.5	0.5	0.4	0.4
Operating Ratios				
Raw Material / Sales (%)	78.5	81.6	80.1	79.1
Employee cost / Sales (%)	5.6	5.7	5.7	5.7
SG&A / Sales (%)	0.8	0.8	0.8	0.8
Other Income / PBT (%)	6.9	13.6	7.3	2.1
Effective Tax Rate (%)	34.0	23.5	25.5	25.5
Working Capital (days)	(1.2)	(1.6)	(1.8)	(1.8)
Inventory Turnover (days)	20.1	19.4	19.3	19.3
Receivables (days)	6.1	2.9	2.9	2.9
Payables (days)	32.3	29.4	29.9	29.9
Net D/E (x)	0.2	0.4	0.3	0.1
Profitability Ratios (%)				
Net Income Margins	3.5	1.8	2.8	3.5
RoACE	13.1	8.5	16.3	21.9
RoAE	10.5	8.9	15.7	18.6
Dividend Payout	10.9	19.9	14.3	11.5
Dividend Yield	0.8	1.1	1.1	1.2
EBITDA Margins	7.5	4.7	6.2	7.2

Source: Company data, I-Sec research

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