

## Superlative performance in challenging environment

VST Industries reported resilient sales despite manufacturing, supply chain as well as retails selling points remaining closed for ~40 days. Gross sales declined merely 4.4% but net of excise, sales were down 19.4%. Cigarette sales de-grew 4% to ₹ 274.7 crore while tobacco sales fell 7% to ₹ 40 crore. Cigarette volumes were down 39% (similar to ITC's decline of ~40%). The company took a blended price hike of 11% after the excise increase in Budget in February 2020. The new price points for 'Edition', 'Total' are ₹ 11, ₹ 7, respectively. More, importantly it curtailed trade promotions & schemes (18-20% of MRP) in Q1 as biggest focal point stayed improving supply by expanding manufacturing & distribution in second half of Q1. July continues to remain disrupted with many localised lockdowns. VST is gradually increasing promotions with competitive intensity rising in Q2. Operating profit was down 13.2% to ₹ 99.3 crore. Operating margins expanded 264 bps to 40.4% with gross margin expansion of 612 bps (due to withdrawal of promotions) & 343 bps (percentage to sales) rise in employee spends. Net profit saw flat growth at ₹ 75.7 crore with reduction in corporate tax rate.

## Improving realisation with focus on high priced cigarettes

In the last two year, VST introduced two new brands 'Edition' & 'Total' at higher price points, resulting in an increase in volume contribution of high priced brands (₹ 6 to ₹11) to more than 50%. We believe the company would continue to grow with consistent realisation growth as volume contribution is gradually shifting from ₹ 4-5 to ₹ 6-7 per stick cigarettes. Moreover, in a stable taxation year, volume growth (FY18-20 volumes rose 9-10% with no increase in GST & excise) could also aid revenues. We expect 9% volume decline in FY21E (with H1 staying disrupted due to lockdowns) and 10% volume growth (recovery) in FY22E. Further, with withdrawal of trade promotions & 11% blended price increase, we expect realisation growth of 34% & 5% in FY21E & FY22E, respectively.

## Strong free cash flows; high dividend payout

With consistent earnings growth of 26.1% CAGR in the last three years and no capex requirement, VST is generating more than ₹ 250 crore free cash flows every year. Further, it had a consistent dividend payout of 60-70% in 2009-19. Though the company has reduced its payout to 52% in FY20 with extreme uncertainty due to business disruption during lockdown, we believe dividend payout would increase above 60%, going forward, with sustainable earnings and strong free cash flows generation.

## Valuation & Outlook

VST has a wide presence at lower price point cigarettes. With continuous increase in taxes & duties, the consumer market now has been largely concentrated at 64 & 69 mm cigarettes. Moreover, gap between ITC & VST's (at lower end) prices led to market share gains for the latter. The possibility of curbs on illicit cigarettes due to supply disruptions could also help drive volume growth for the company. We retain our positive stance valuing it at 20x FY22 PE with target price of ₹ 4,450/share and **BUY** recommendation.



VST Industries Ltd.

### Particulars

Particulars (₹ crore)	Amount
Market Capitalization	5,000.1
Total Debt (FY19)	0.0
Cash and Investments (FY20)	788.6
EV	4,211.4
52 week H/L (₹)	4856 / 2550
Equity capital	₹ 15.4
Face value (₹)	10.0

### Key Highlights

- Gross revenue was down merely 4.4% despite 39% drop in cigarette volumes as the company withdrew trade promotion during the quarter
- Operating margins expanded 264 bps mainly due to ~11% price hike after budget & curtailment of trade promotions
- Maintain BUY rating on stock with revised target price of ₹ 4,450

### Research Analyst

Sanjay Manyal  
sanjay.manyal@icicisecurities.com

### Key Financial Summary

Key Financials	FY18	FY19	FY20	FY21E	FY22E	CAGR (FY20-22E)
Net Sales	946.0	1097.6	1238.1	1204.5	1404.6	6.5%
EBITDA	293.6	353.1	414.7	416.2	457.8	5.1%
EBITDA Margin %	31.0	32.2	33.5	34.6	32.6	
Net Profit	181.5	226.8	304.1	312.0	343.7	6.3%
EPS (₹)	117.52	146.90	196.95	202.05	222.59	
P/E	27.6	22.0	16.4	16.0	14.5	
RoNW %	31.2	34.2	38.6	34.2	33.0	
RoCE (%)	46.8	51.4	52.1	46.3	44.8	

Source: Company, ICICI Direct Research

**Exhibit 1: Variance Analysis**

	Q1FY21	Q1FY21E	Q1FY20	YoY (%)	Q4FY20	QoQ (%)	Comments
Total Operating Income	245.6	152.3	304.7	-19.4	291.5	-15.7	Sales (net of excise) declined only 19.4% despite ~40 days loss of sales during lockdown. Though volume de-grew 39%, realisation growth would have been much higher given 11% price hike & complete withdrawal of trade promotions
Other Operating Income	0.2	0.4	0.2	4.3	0.2	26.3	
Raw Material Expenses	93.1	70.1	134.1	-30.6	139.9	-33.5	
Employee Expense	29.3	25.9	25.9	13.2	21.3	37.7	
Excise Duty	69.3	29.1	24.6	182.1	58.2	19.1	
Other operating Expenses	24.0	24.0	29.6	-19.0	35.7	-32.8	
EBITDA	99.3	32.3	115.1	-13.7	94.7	4.9	Operating profit declined 13.7% on the back of 39% dip in volume growth but operating margins expanded with withdrawal of almost all promotional offers
EBITDA Margin (%)	40.4	21.2	37.8	264 bps	32.5	795 bps	
Depreciation	8.9	10.3	9.4	-4.8	12.9	-30.7	
Interest	0.0	0.0	0.0	NA	0.0	NA	
Other Income	11.6	12.0	11.8	-1.3	12.3	-5.5	
PBT	102.0	33.9	117.5	-13.2	94.1	8.4	
Tax Outgo	26.3	9.1	41.9	-37.1	23.5	11.9	
PAT	75.7	24.7	75.7	0.0	70.6	7.2	Net profit flat aided by reduction in corporate tax rate last year
<b>Key Metrics</b>							
Cigarette Sales (₹ crore)	274.7	157.3	286.0	-4.0	285.5	-3.8	Gross sales declined merely 4% with 39% dip in volumes & sharp increase in cigarette realisation given the company withdrew almost all promotional offers
Tobacco Sales (₹ crore)	40.0	23.7	43.0	-7.0	64.0	-37.5	

Source: Company, ICICI Direct Research

**Exhibit 2: Change in estimates**

(₹ Crore)	FY21E			FY22E			Comments
	Old	New	% change	Old	New	% change	
Net sales	1093.0	1204.5	10.2	1,402.2	1,404.6	0.2	We change our realisation estimate with the company significantly curtailing promotional offers & trade schemes during lockdown & only gradually increasing it currently
EBITDA	255.8	416.2	62.7	448.4	457.8	2.1	
EBITDA Margin (%)	23.4	34.6	1115 bps	32.0	32.6	61 bps	
PAT	192.7	312.0	61.9	333.9	343.7	2.9	Withdrawal of trade promotions would directly percolate down to operating profit
EPS (₹)	124.8	202.05	61.9	216.3	222.59	2.9	

Source: Company, ICICI Direct Research

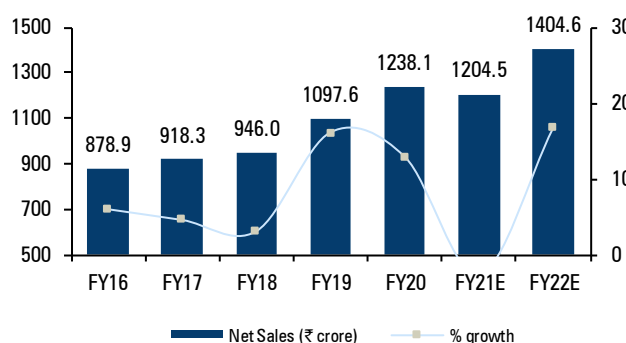
**Exhibit 3: Assumptions**

	Current				Earlier		Comments
	FY18	FY19	FY20	FY21E	FY22E	FY20E	
Cig. Vol. (mn sticks)	7,370.0	8,031.1	8,753.9	7,966.1	8,762.7	8,053.6	9,342.2
Cig. Vol. Growth (%)	1.2	9.0	9.0	-9.0	10.0	-8.0	16.0
Realization/cig (₹)	2.9	1.2	1.3	1.7	1.8	1.5	1.7
Tobacco Sales(₹ crore)	250.0	238.9	264.7	251.5	282.1	251.5	282.1
% of <64mm in sales	50.0	40.0	40.0	40.0	40.0	40.0	40.0
% of >64mm in sales	50.0	60.0	60.0	60.0	60.0	60.0	60.0

Source: Company, ICICI Direct Research

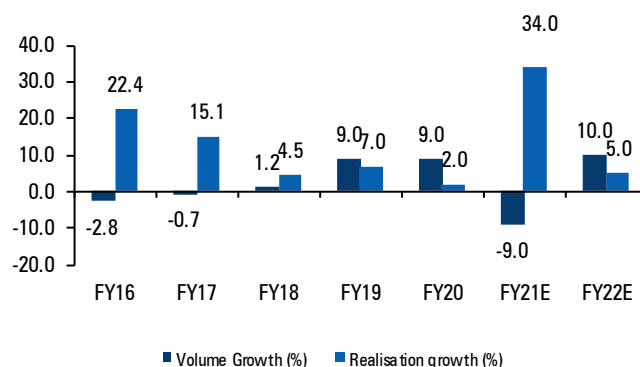
## Key Metrics

**Exhibit 4: Net revenue to grow at 6.5% CAGR over FY20-22E**



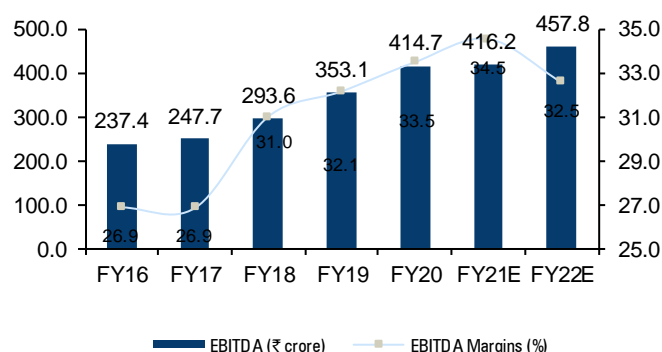
Source: ICICI Direct Research, Company

**Exhibit 5: Volume growth to stabilise in FY22**



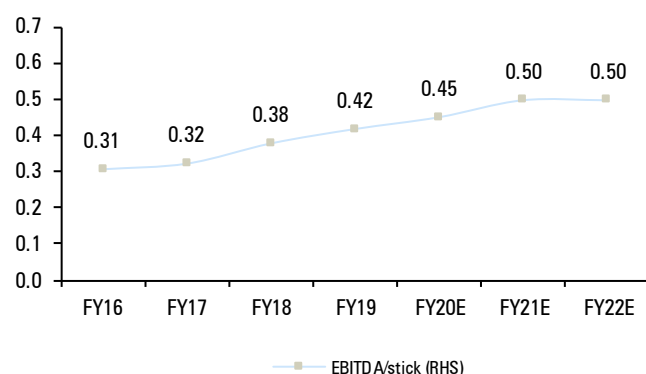
Source: ICICI Direct Research, Company

**Exhibit 6: Improved product mix to aid EBITDA margins**



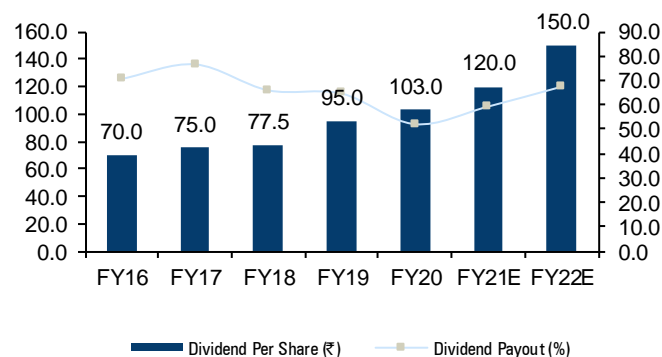
Source: Company, ICICI Direct Research

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



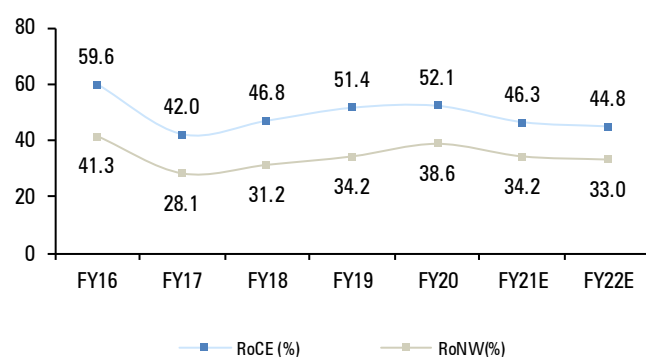
Source: Company, ICICI Direct Research

**Exhibit 8: High dividend payout to continue**



Source: Company, ICICI Direct Research

**Exhibit 9: Attractive return ratios % (except bump in FY21)**

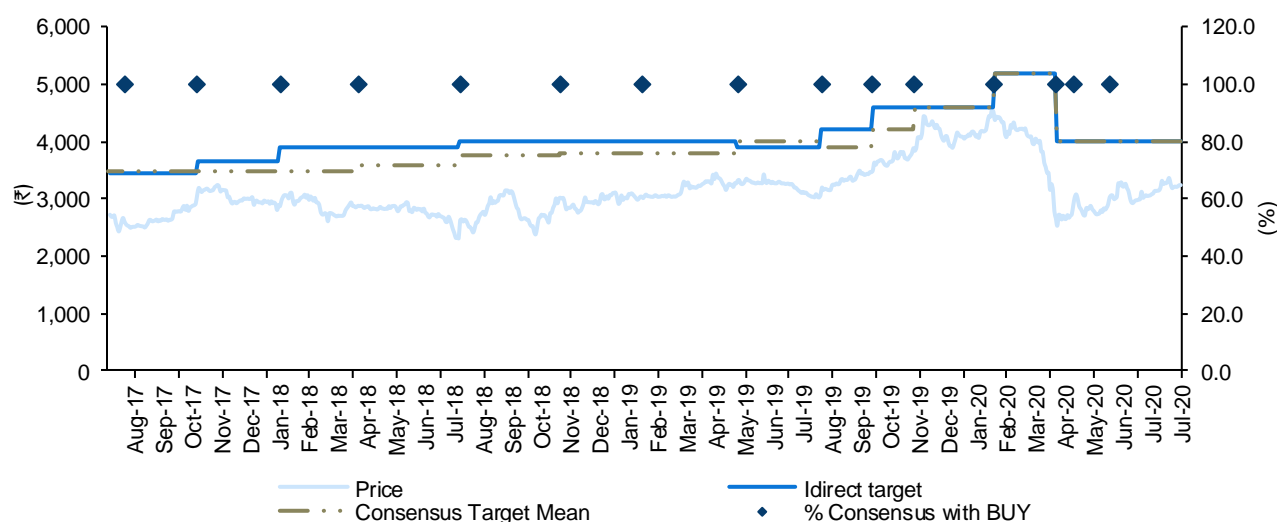


Source: Company, ICICI Direct Research

**Exhibit 10: Valuation**

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY19	1097.6	16.0	146.9	25.0	22.0	14.0	34.2	51.4
FY20	1238.1	12.8	196.9	34.1	16.4	11.9	38.6	52.1
FY21E	1204.5	-2.7	202.1	2.6	16.0	11.6	34.2	46.3
FY22E	1404.6	16.6	222.6	10.2	14.5	10.6	33.0	44.8

Source: Company, ICICI Direct Research

**Exhibit 11: Recommendation History vs. Consensus**


Source: Bloomberg, Company, ICICI Direct Research

**Exhibit 12: Top 10 Shareholders**

Rank	Investor Name	Filing Date	% O/S	Position (m)	Change (m)
1	Bright Star Investme	31-Mar-20	26.0	4.0	0.0
2	Raleigh Investment C	31-Mar-20	23.5	3.6	0.0
3	British American Tob	31-Mar-20	8.7	1.3	0.0
4	Hdfc Asset Managemen	31-Mar-20	7.1	1.1	0.0
5	Matthews Intl Capita	31-Mar-20	5.6	0.9	-0.2
6	Damani S Radhakrishna	31-Mar-20	5.0	0.8	0.8
7	L&T Mutual Fund	31-Mar-20	2.7	0.4	-0.1
8	New India Assurance	30-Jun-19	1.5	0.2	0.0
9	Dsp Blackrock Invest	31-Mar-20	1.4	0.2	0.0
10	Axis Asset Managemen	31-Mar-20	0.9	0.1	0.0

Source: Reuters, ICICI Direct Research

**Exhibit 13: Shareholding Pattern**

(in %)	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20
Promoter	32.2	32.2	32.2	32.2	32.2
FII	8.8	7.8	6.8	5.5	4.6
DII	18.3	18.5	16.7	15.5	15.6
Others	40.8	41.5	44.4	46.8	47.6

Source: Company, ICICI Direct Research

## Financial summary

Exhibit 14: Profit and loss statement ₹ crore				
(Year-end March)	FY19	FY20	FY21E	FY22E
<b>Total Operating Income</b>	<b>1099.0</b>	<b>1239.4</b>	<b>1206.1</b>	<b>1406.5</b>
Growth (%)	16.0	12.8	-2.7	16.6
Raw Material Expenses	550.2	598.6	555.6	694.4
Employee Expenses	92.3	102.4	112.6	120.8
Excise Duty	85.1	131.1	394.5	434.0
Administrative Expenses	13.7	0.0	0.0	0.0
Other expenses	82.4	123.7	121.7	133.4
Total Operating Expenditure	745.9	824.7	789.9	948.7
<b>EBITDA</b>	<b>353.1</b>	<b>414.7</b>	<b>416.2</b>	<b>457.8</b>
Growth (%)	20.3	17.4	0.4	10.0
Depreciation	41.3	41.8	39.6	39.0
Interest	0.0	0.0	0.0	0.0
Other Income	0.0	0.0	0.0	0.0
PBT	350.7	420.3	424.5	467.6
Others	38.9	47.4	47.8	48.8
Total Tax	123.8	116.2	112.5	123.9
<b>PAT</b>	<b>226.8</b>	<b>304.1</b>	<b>312.0</b>	<b>343.7</b>
Growth (%)	25.0	34.1	2.6	10.2
EPS (₹)	146.9	196.9	202.1	222.6

Source: Company, ICICI Direct Research

Exhibit 15: Cash flow statement ₹ crore				
(Year-end March)	FY19	FY20	FY21E	FY22E
Profit after Tax	222.0	314.8	312.0	343.7
Add: Depreciation	41.3	41.8	39.6	39.0
(Inc)/dec in Current Assets	4.5	-29.0	57.9	-267.3
Inc/(dec) in CL and Provisions	58.6	49.6	-48.9	82.2
<b>CF from operating activities</b>	<b>290.2</b>	<b>331.4</b>	<b>360.6</b>	<b>197.6</b>
(Inc)/dec in Investments	-122.3	-133.3	0.1	-0.3
(Inc)/dec in Fixed Assets	-25.8	-21.9	-40.0	-35.0
(Inc)/dec in LT Loans & Adv.	0.0	0.0	0.0	0.0
Others	0.0	0.5	-16.2	0.6
<b>CF from investing activities</b>	<b>-148.0</b>	<b>-154.8</b>	<b>-56.1</b>	<b>-34.7</b>
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	-144.3	-176.9	-186.1	-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
<b>CF from financing activities</b>	<b>-144.3</b>	<b>-176.9</b>	<b>-186.1</b>	<b>-216.8</b>
Net Cash flow	-2.1	-0.2	118.4	-53.9
Opening Cash	28.5	26.4	26.2	144.6
<b>Closing Cash</b>	<b>36.9</b>	<b>37.4</b>	<b>155.9</b>	<b>102.0</b>

Source: Company, ICICI Direct Research

Exhibit 16: Balance sheet ₹ crore				
(Year-end March)	FY19	FY20	FY21E	FY22E
<b>Liabilities</b>				
Equity Capital	15.4	15.4	15.4	15.4
Reserve and Surplus	648.6	771.7	897.6	1,024.5
Total Shareholders funds	664.0	787.1	913.0	1,039.9
Total Debt	0.0	0.0	0.0	0.0
Long Term Provisions	18.5	19.9	3.6	4.2
<b>Total Liabilities</b>	<b>682.5</b>	<b>806.9</b>	<b>916.6</b>	<b>1044.1</b>
<b>Assets</b>				
Gross Block	329.5	345.0	375.0	405.0
Less: Acc Depreciation	116.2	157.9	197.5	236.5
Net Block	213.3	187.1	177.5	168.5
Capital WIP	0.3	12.7	22.7	27.7
Deferred Tax Asset	31.0	26.4	26.4	26.4
Non Current Investments	2.3	1.8	1.7	1.9
LT Loans & Advances/Others	1.3	5.4	5.4	5.4
<b>Current Assets</b>				
Inventory	281.9	297.7	287.1	338.7
Debtors	14.3	15.4	14.9	19.2
Cash	36.9	37.4	155.9	102.0
Loans & Advances	0.0	0.0	8.3	9.6
Current Investments	573.1	751.2	691.2	896.2
Other CA	50.6	62.0	67.0	72.0
<b>Current Liabilities</b>				
Creditors	83.0	142.8	145.2	161.6
Provisions	0.0	0.0	0.0	0.0
Other CL	439.4	447.3	396.0	461.8
Net Current Assets	434.3	573.6	683.1	814.3
<b>Total Assets</b>	<b>682.5</b>	<b>806.9</b>	<b>916.6</b>	<b>1044.1</b>

Source: Company, ICICI Direct Research

Exhibit 17: Key ratios ₹ crore				
(Year-end March)	FY19	FY20	FY21E	FY22E
<b>Per share data (₹)</b>				
EPS	146.9	196.9	202.1	222.6
Cash EPS	173.7	224.0	227.7	247.8
BV	430.0	509.8	591.3	673.5
DPS	95.0	103.0	120.0	150.0
Cash Per Share	23.9	24.3	101.0	66.1
<b>Operating Ratios (%)</b>				
EBITDA Margin	32.1	33.5	34.5	32.5
PBT / Net Sales	31.9	33.9	35.2	33.3
PAT Margin	20.7	24.6	25.9	24.5
Inventory days	93.7	87.8	87.0	88.0
Debtor days	4.8	4.5	4.5	5.0
Creditor days	27.6	42.1	44.0	42.0
<b>Return Ratios (%)</b>				
RoE	34.2	38.6	34.2	33.0
RoCE	51.4	52.1	46.3	44.8
RoIC	26.3	25.3	27.0	23.6
<b>Valuation Ratios (x)</b>				
P/E	22.0	16.4	16.0	14.5
EV / EBITDA	14.0	11.9	11.6	10.6
EV / Net Sales	4.5	4.0	4.0	3.5
Market Cap / Sales	4.6	4.0	4.2	3.6
Price to Book Value	7.5	6.4	5.5	4.8
<b>Solvency Ratios</b>				
Debt/EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	1.8	1.9	2.0	2.1
Quick Ratio	1.2	1.4	1.4	1.6

Source: Company, ICICI Direct Research

**Exhibit 18: ICICI Direct coverage universe (FMCG)**

Sector / Company	CMP	TP	Rating	M Cap	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)		(₹ Cr)	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY21E	FY20	FY21E	FY22E	FY20	FY21E	FY22E
Colgate (COLPAL)	1,411	1,540	Hold	39,377	30.0	31.0	34.3	47.0	45.6	41.2	8.8	8.6	7.8	60.7	68.0	76.0	51.2	52.1	58.3
Dabur India (DABIND)	510	565	Buy	87,118	8.2	8.8	10.3	62.3	57.9	49.8	10.0	9.9	8.6	26.1	24.0	24.7	21.9	20.9	21.4
Hindustan Unilever (HINLEV)	2,205	2,410	Hold	519,159	31.2	32.4	40.1	70.7	68.1	54.9	13.6	12.2	0.0	89.5	26.7	33.0	85.7	20.3	25.4
ITC Limited (ITC)	193	250	Buy	245,475	12.5	11.7	13.0	15.5	16.4	14.8	5.3	5.2	4.6	29.4	28.3	36.1	23.8	21.7	27.7
Jyothy Lab (JYOLAB)	125	115	Hold	4,535	4.3	4.1	5.7	29.1	30.3	21.7	2.7	2.9	2.4	24.3	23.3	28.8	21.7	18.8	23.8
Marico (MARLIM)	363	380	Hold	45,286	8.1	8.5	9.6	44.9	42.7	37.9	6.2	6.1	5.5	41.0	42.3	46.2	34.5	35.6	39.5
Nestle (NESIND)	16,525	18,000	Hold	164,869	204.3	230.3	268.9	80.9	71.8	61.5	13.4	12.4	10.9	56.9	59.3	65.9	101.9	114.2	123.6
Tata Consumer Products (TATGLC)	434	440	Buy	37,667	5.0	8.7	10.9	87.0	50.0	39.9	3.9	3.7	3.4	6.9	7.9	8.8	4.6	5.9	7.1
VST Industries (VSTIND)	3,236	4,450	Buy	5,000	196.9	202.1	222.6	16.4	16.0	14.5	4.0	4.2	3.6	52.1	46.3	44.8	38.6	34.2	33.0
Varun Beverage (VARBEV)	684	580	Reduce	20,122	16.4	9.7	17.8	41.8	70.2	38.4	2.8	3.3	2.7	15.5	11.3	16.3	14.2	8.8	14.2
Zydus Wellness (ZYDWEL)	1,723	1,925	Buy	9,266	24.6	39.0	55.0	70.1	44.2	31.3	5.2	5.1	4.5	5.9	6.5	7.8	5.4	6.2	8.1

Source: Company, ICICI Direct Research

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ICICI Direct endeavours to provide objective opinions and recommendations. ICICI Direct assigns ratings to its stocks according to their notional target price vs. current market price and then categorizes them as Buy, Hold, Reduce and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock

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

## ANALYST CERTIFICATION

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