

Volume continues to remain sluggish

VST Industries reported dismal set of numbers with ~13% decline in cigarette volumes given demand conditions still remained weak due to continue work from home culture. Moreover, the company faced stiff competitive pressure with peers increasing trade discounts & schemes. Gross revenues witnessed a growth of 3.3% led by 18% increase in cigarettes sales. The increase in sales was largely on account of price increase taken last year after the excise duty increase in budget & change in product mix. High priced cigarettes brands 'Total' (₹ 7/stick) & 'Edition' (₹11/stick) contributes 45% to volumes. Tobacco sales was down to ₹ 60 crore from ₹ 100 crore in corresponding quarter due to sluggish demand of Indian tobacco in export market. The company paid ₹ 93.5 crore excise duty as against ₹ 24.7 crore in corresponding quarter. Gross margins were higher by 674 bps mainly due to increase in cigarettes prices & change in product mix towards the high priced cigarettes. Operating profit dipped by 7.8% to ₹ 100 crore. Net profit witnessed de-growth of 9.5% to ₹ 73.7 crore.

Stability in taxation is key to growth

Cigarette Industry faced stiff challenges of excise duty increase & pandemic induced lockdown in FY21. This resulted in significant declined in cigarettes volumes for the Industry. In similar lines, VST also witnessed 22% cigarette volume decline in 9MFY21. Work from home culture & still some restrictions on large celebratory gatherings has been one of the major reasons for continued volume de-growth. We believe stable taxation is key for recouping lost volumes in next two years. We have seen two years of stable taxation between FY18-20 resulted in double digit growth in cigarettes volumes. We expect 2.6% revenue CAGR during FY20-23 with 6% & 3% volume growth in FY22E & FY23E. Considering continuous increasing contribution of premium priced cigarettes, we expect operating margin improvement & subsequent earnings CAGR of 6.1% in FY20-23E.

Strong free cash flows; high dividend pay-out

VST is generating ~₹ 300 crore (on an average) free cash flow every year from FY18 onwards. Despite, severe impact on volumes, it has been able to maintain similar profitability & continuation of strong free cash flows in FY21E. Moreover, it has consistently paid ~65% dividend in last five years (except 52% in current year due to uncertainty over pandemic). We believe pay-out would increase to 70% given company is holding more than ₹700 crore of cash & equivalent & doesn't have any capex requirement in future. Despite, expected subdued earning, we expect RoCE & RoE to improve to 52.8% & 39% respectively by FY23E

Valuation & Outlook

The company has maintained its profitability despite severe volume challenges shows its ability to manoeuvre pricing & promotion to its advantage. However, we believe stable taxation is necessary for volume growth in future, which would determine revenue & earnings trajectory for the next few years. We will wait for cues in 2021 budget and maintain our **Hold** with revised target price of ₹ 4200/share (18x FY23E PE)

Key Financial Summary

Key Financials	FY19	FY20	FY21E	FY22E	FY23E	CAGR (FY20-23E)
Net Sales	1097.6	1238.1	1150.1	1237.8	1336.3	2.6%
EBITDA	353.1	414.7	414.1	446.5	486.4	5.5%
EBITDA Margin %	32.2	33.5	36.0	36.1	36.4	
Net Profit	226.8	304.1	312.5	337.7	363.2	6.1%
EPS (₹)	146.90	196.95	202.40	218.70	235.24	
P/E	25.6	19.1	18.6	17.2	16.0	
RoNW %	34.2	38.6	33.2	35.2	39.0	
RoCE (%)	51.4	52.1	44.7	47.4	52.8	

Source: Company, ICICI Direct Research

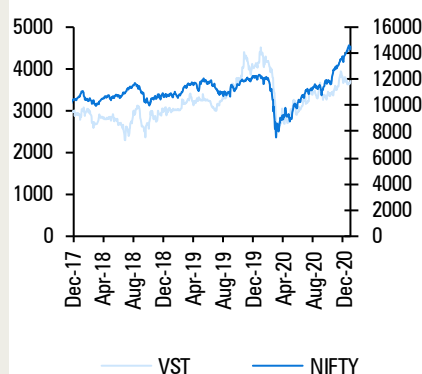


VST Industries Ltd.

Particulars

Particulars (₹ crore)	Amount
Market Capitalization	5,809.2
Total Debt (FY19)	0.0
Cash and Investments (FY20)	788.6
EV	5,020.6
52 week H/L (₹)	4856 / 3010
Equity capital	₹ 15.4
Face value (₹)	10.0

Price Chart



Key Risk to our call

- Downside Risk :** Any significant change in taxation in 2021 Budget or any of the GST council meeting
- Upside Risk :** Volume recovery in FY22E could be much faster than our estimate of 6%

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Exhibit 1: Variance Analysis

	Q3FY21	Q3FY21E	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	Comments
Total Operating Income	286.9	306.3	343.8	-16.5	300.3	-4.5	Gross revenue increased by 3.3% however, net of excise sales saw 16.5% decline in sales largely on account of 40% dip in tobacco sales & 13% decline in cigarettes volumes
Other Operating Income	0.3	0.5	0.6	-46.9	0.3	3.0	
Raw Material Expenses	129.4	131.1	178.2	-27.4	135.0	-4.2	Gross margins improved significantly due to price hikes taken last year after budget & chane in product mix
Employee Expense	29.4	28.0	30.5	-3.6	28.1	4.6	
Excise Duty	93.5	100.2	24.7	278.5	94.6	-1.1	
Other operating Expenses	28.2	31.5	26.7	5.4	24.1	16.8	
EBITDA	100.0	115.7	108.4	-7.8	113.1	-11.6	
EBITDA Margin (%)	34.8	37.8	31.5	332 bps	37.6	-280 bps	Operating margins improved on the back of expansion in gross margins partially off-set of higher fixed cost due to negative operating leverage
Depreciation	9.4	10.9	10.3	-8.4	8.9	5.4	
Interest	0.0	0.0	0.0	NA	0.0	NA	
Other Income	9.2	10.8	11.1	-17.0	14.7	-37.5	
PBT	99.7	115.6	109.2	-8.6	118.8	-16.1	
Tax Outgo	26.0	27.6	27.7	-6.0	30.3	-14.1	
PAT	73.7	88.0	81.5	-9.5	88.5	-16.7	Net profit saw 9.5% de-growth during the quarter
Key Metrics							
Cigarette Sales (₹ crore)	320.1	316.0	267.8	19.5	333.6	-4.0	Cigarette sales was higher despite significant dip in volumes mainly due to increase in cigarette prices last year & change in product mix
Tobacco Sales (₹ crore)	60.0	90.0	100.0	-40.0	61.0	-1.6	Tobacco sales was lower mainly on account of lower export demand for Indian tobacco

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

₹ Crore	FY21E			FY22E			FY23E			Comments
	Old	New	% change	Old	New	% change	Old	New	% change	
Net sales	1169.1	1150.1	-1.6	1,258.2	1,237.8	-1.6	1,358.1	1,336.3	-1.6	We marginally change our estimate of realisation growth given trade discounts are back of pre-covid
EBITDA	421.6	414.1	-1.8	432.4	446.5	3.3	462.6	486.4	5.1	
EBITDA Margin (%)	36.1	36.0	-6 bps	34.4	36.1	171 bps	34.1	36.3	228 bps	We changed our gross margin estimate for FY22 & FY23 with company pushing for higher proportion premium priced cigarettes
PAT	318.1	312.5	-1.8	327.2	337.7	3.2	345.7	363.2	5.1	
EPS (₹)	206.0	202.40	-1.8	211.9	218.70	3.2	223.9	235.2	5.1	

Source: Company, ICICI Direct Research

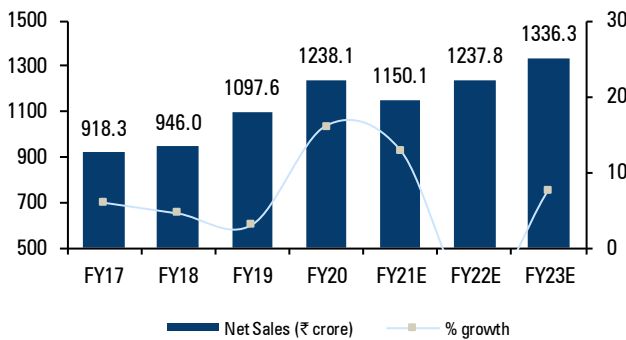
Exhibit 3: Assumptions

	FY19	FY20	FY21E	FY22E	FY23E	Earlier			Comments
						FY21E	FY22E	FY23E	
Cig. Vol. (mn sticks)	8,031.1	8,753.9	7,353.3	7,794.5	8,028.3	7,353.3	7,794.5	8,028.3	No major change in estimates
Cig. Vol. Growth (%)	9.0	9.0	-16.0	6.0	3.0	-16.0	6.0	3.0	
Realization/cig (₹)	1.2	1.3	1.7	1.7	1.8	1.7	1.8	1.8	Small change in realisation growth estimate as trade promotions are back to pre-covid levels
Tobacco Sales(₹ crore)	238.9	264.7	251.5	271.9	285.6	251.5	271.9	285.6	
% of <64mm in sales	40.0	40.0	40.0	40.0	40.0	40.0	40.0	40.0	
% of >64mm in sales	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	

Source: Company, ICICI Direct Research

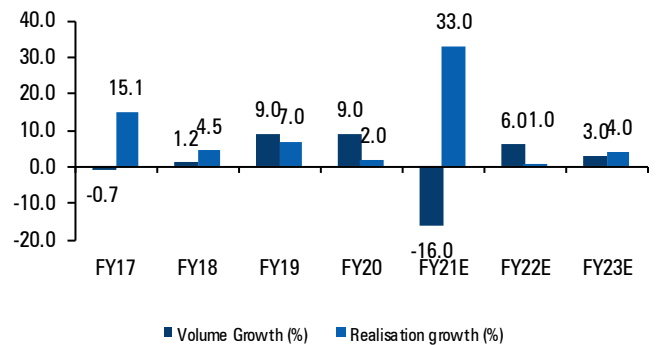
Key Metrics

Exhibit 4: Net revenue to grow at 2.6% CAGR over FY20-23E



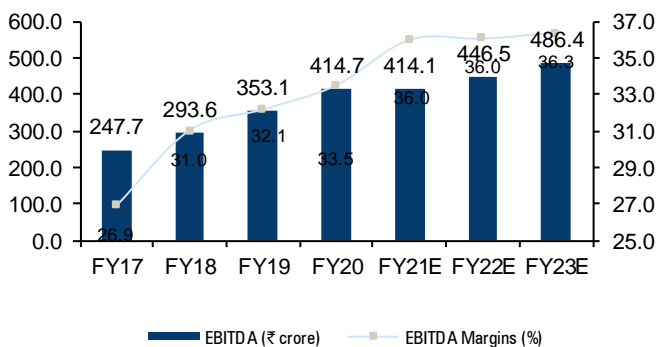
Source: ICICI Direct Research, Company

Exhibit 5: Steeper than expected volume decline in FY23E



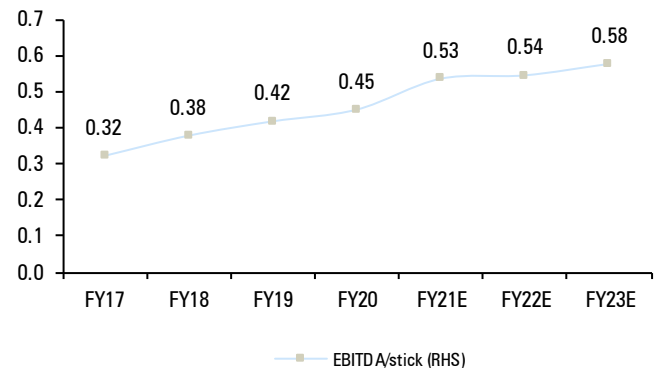
Source: ICICI Direct Research, Company

Exhibit 6: Improved product mix to aid EBITDA margins



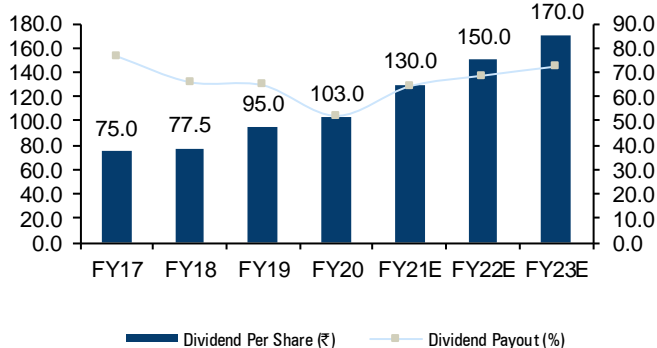
Source: Company, ICICI Direct Research

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



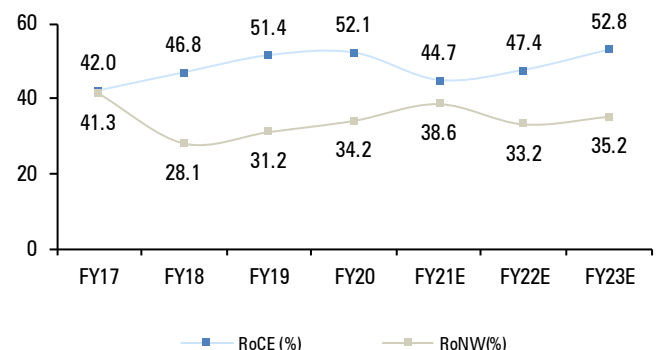
Source: Company, ICICI Direct Research

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 (%)
FY20	1238.1	12.8	196.9	34.1	19.1	13.9	38.6	52.1
FY21E	1150.1	-7.1	202.4	2.8	18.6	13.5	33.2	44.7
FY22E	1237.8	7.6	218.7	8.1	17.2	12.8	35.2	47.4
FY23E	1336.3	8.0	235.2	7.6	16.0	11.8	39.0	52.8

Source: Company, ICICI Direct Research

Financial summary

Exhibit 11: Profit and loss statement				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Total Operating Income	1239.4	1151.7	1239.7	1338.5
Growth (%)	12.8	-7.1	7.6	8.0
Raw Material Expenses	598.6	513.3	560.4	594.2
Employee Expenses	102.4	115.0	117.6	131.0
Excise Duty	131.1	364.2	386.0	397.6
Administrative Expenses	0.0	0.0	0.0	0.0
Other expenses	123.7	109.3	115.1	126.9
Total Operating Expenditure	824.7	737.6	793.1	852.1
EBITDA	414.7	414.1	446.5	486.4
Growth (%)	17.4	-0.1	7.8	8.9
Depreciation	41.8	39.6	39.0	42.0
Interest	0.0	0.0	0.0	0.0
Other Income	0.0	0.0	0.0	0.0
PBT	420.3	422.3	456.3	494.2
Others	47.4	47.8	48.8	49.8
Total Tax	116.2	109.8	118.6	131.0
PAT	304.1	312.5	337.7	363.2
Growth (%)	34.1	2.8	8.1	7.6
EPS (₹)	196.9	202.4	218.7	235.2

Source: Company, ICICI Direct Research

Exhibit 12: Cash flow statement				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Profit after Tax	314.8	312.5	337.7	363.2
Add: Depreciation	41.8	39.6	39.0	42.0
(Inc)/dec in Current Assets	-29.0	71.9	-152.7	-60.8
Inc/(dec) in CL and Provisions	49.6	-73.3	32.6	43.7
CF from operating activities	331.4	350.7	256.6	388.1
(Inc)/dec in Investments	-133.3	0.2	-0.1	-0.1
(Inc)/dec in Fixed Assets	-21.9	-40.0	-35.0	-35.0
(Inc)/dec in LT Loans & Adv.	0.0	0.0	0.0	0.0
Others	0.5	-16.4	0.3	0.3
CF from investing activities	-154.8	-56.2	-34.9	-34.8
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	-176.9	-159.0	-319.7	-390.4
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	-176.9	-159.0	-319.7	-390.4
Net Cash flow	-0.2	135.5	-97.9	-37.1
Opening Cash	26.4	26.2	161.7	63.7
Closing Cash	37.4	172.9	75.0	37.8

Source: Company, ICICI Direct Research

Exhibit 13: Balance sheet				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Liabilities				
Equity Capital	15.4	15.4	15.4	15.4
Reserve and Surplus	771.7	925.1	943.1	915.9
Total Shareholders funds	787.1	940.6	958.5	931.3
Total Debt	0.0	0.0	0.0	0.0
Long Term Provisions	19.9	3.5	3.7	4.0
Total Liabilities	806.9	944.0	962.2	935.3
Assets				
Gross Block	345.0	375.0	405.0	435.0
Less: Acc Depreciation	157.9	197.5	236.5	278.5
Net Block	187.1	177.5	168.5	156.5
Capital WIP	12.7	22.7	27.7	32.7
Deferred Tax Asset	26.4	26.4	26.4	26.4
Non Current Investments	1.8	1.6	1.7	1.8
LT Loans & Advances/Others	5.4	5.4	5.4	5.4
Current Assets				
Inventory	297.7	274.1	298.4	322.2
Debtors	15.4	14.2	17.0	18.3
Cash	37.4	172.9	75.0	37.8
Loans & Advances	0.0	7.9	8.5	9.2
Current Investments	751.2	691.2	811.2	841.2
Other CA	62.0	67.0	72.0	77.0
Current Liabilities				
Creditors	142.8	138.6	142.4	153.8
Provisions	0.0	0.0	0.0	0.0
Other CL	447.3	378.1	407.0	439.3
Net Current Assets	573.6	710.5	732.6	712.6
Total Assets	806.9	944.0	962.2	935.3

Source: Company, ICICI Direct Research

Exhibit 14: Key ratios				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Per share data (₹)				
EPS	196.9	202.4	218.7	235.2
Cash EPS	224.0	228.0	244.0	262.4
BV	509.8	609.2	620.8	603.2
DPS	103.0	130.0	150.0	170.0
Cash Per Share	24.3	112.0	48.6	24.5
Operating Ratios (%)				
EBITDA Margin	33.5	36.0	36.0	36.3
PBT / Net Sales	33.9	36.7	36.9	37.0
PAT Margin	24.6	27.2	27.3	27.2
Inventory days	87.8	87.0	88.0	88.0
Debtor days	4.5	4.5	5.0	5.0
Creditor days	42.1	44.0	42.0	42.0
Return Ratios (%)				
RoE	38.6	33.2	35.2	39.0
RoCE	52.1	44.7	47.4	52.8
RoC	25.3	26.6	24.9	26.6
Valuation Ratios (x)				
P/E	19.1	18.6	17.2	16.0
EV / EBITDA	13.9	13.5	12.8	11.8
EV / Net Sales	4.6	4.9	4.6	4.3
Market Cap / Sales	4.7	5.1	4.7	4.3
Price to Book Value	7.4	6.2	6.1	6.2
Solvency Ratios				
Debt/EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	1.9	2.0	2.2	2.1
Quick Ratio	1.4	1.5	1.7	1.6

Source: Company, ICICI Direct Research

Exhibit 15: ICICI Direct coverage universe (FMCG)

	CMP	TP	M Cap	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)			
	(₹)	(₹)		Rating	(₹ Cr)	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E
Colgate (COLPAL)	1,544	1,700	Buy	38,812	33.4	35.4	37.8	46.2	43.6	40.8	8.4	7.7	7.2	83.5	100.8	123.9	64.2	78.0	96.5
Dabur India (DABIND)	538	595	Buy	90,864	9.6	10.7	11.8	56.2	50.2	45.7	9.5	8.6	7.8	25.9	26.7	27.1	22.3	22.7	22.9
Hindustan Unilever (HINLEV)	2,356	2,500	Buy	510,548	32.4	38.8	43.2	72.7	60.7	54.5	12.0	10.4	9.7	24.5	28.5	31.2	18.6	21.9	23.9
ITC Limited (ITC)	218	225	Buy	213,884	11.2	12.0	13.4	19.4	18.1	16.3	4.7	4.2	3.8	27.2	30.5	35.7	20.9	23.4	27.5
Jyothy Lab (JYOLAB)	156	150	Hold	4,957	5.8	6.1	6.7	27.1	25.6	23.2	2.7	2.5	2.3	31.1	30.9	31.5	25.7	25.1	25.6
Marico (MARLIM)	417	440	Buy	46,834	8.8	9.5	9.9	47.4	43.8	42.2	6.2	5.6	5.4	42.3	45.1	46.0	36.3	38.5	39.3
Nestle (NESIND)	17,681	18,000	Hold	152,970	223.4	253.4	284.2	79.1	69.8	62.2	11.5	10.4	9.5	59.9	66.6	73.7	119.1	139.2	160.6
Tata Consumer Products (TATGLO)	597	605	Buy	52,158	12.0	13.5	15.1	49.7	44.1	39.4	4.8	4.4	4.1	9.8	10.5	11.1	7.8	8.6	9.3
VST Industries (VSTIND)	3,762	4,200	Hold	5,809	202.4	218.7	235.2	18.6	17.2	16.0	5.1	4.7	4.3	44.7	47.4	52.8	33.2	35.2	39.0
Varun Beverage (VARBEV)	917	730	Hold	19,429	11.3	21.7	26.6	81.1	42.2	34.5	3.0	2.5	2.3	12.3	18.6	20.7	10.1	16.7	17.6
Zydus Wellness (ZYDWEL)	1,987	2,300	Buy	11,359	27.8	65.7	71.7	71.5	30.2	27.7	6.1	5.4	5.0	6.9	8.3	8.9	5.9	8.6	9.2

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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