# Stock Idea

**Sector: Consumer Goods** October 06, 2021

## Radico Khaitan Ltd


**Add some magic to your portfolio**

Sharekhan
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Stock Idea

# Radico Khaitan Ltd

## Add some magic to your portfolio

| Consumer Goods | Sharekhan code: RADICO | Initiating Coverage |
|---|---|---|

| 3R MATRIX | + | = | - |
|---|---|---|---|
| Right Sector (RS) | ✓ | | |
| Right Quality (RQ) | ✓ | | |
| Right Valuation (RV) | ✓ | | |

\+ Positive = Neutral - Negative

| Reco/View | |
|---|---|
| Reco: | **Buy** |
| CMP: | **Rs. 905** |
| Price Target: | **Rs. 1,250** |

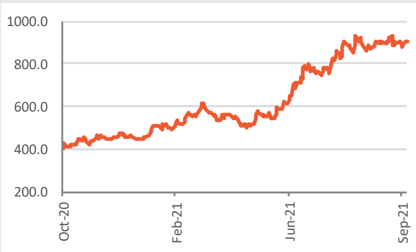
### Company details

| | |
|---|---|
| Market cap: | Rs. 12,090 cr |
| 52-week high/low: | Rs. 964/391 |
| NSE volume: (No of shares) | 6.3 lakh |
| BSE code: | 532497 |
| NSE code: | RADICO |
| Free float: (No of shares) | 8.0 cr |

### Shareholding (%)

| | |
|---|---|
| Promoters | 40.3 |
| FII | 20.6 |
| DII | 18.2 |
| Others | 20.93 |

### Price chart




### Price performance

| (%) | 1m | 3m | 6m | 12m |
|---|---|---|---|---|
| Absolute | 0.1 | 19.2 | 65.1 | 122.5 |
| Relative to Sensex | -2.4 | 6.3 | 43.8 | 69.6 |

*Sharekhan Research, Bloomberg*


### Summary

- We initiate coverage on Radico Khaitan Limited (RKL) with a Buy and PT of Rs. 1,250; Stock trades at 30.9x/24.7x its FY2023/24E EPS, at a 50% discount to USL's valuations. Better earnings growth, higher FCF and strong return profile will reduce valuation gap.
- RKL has emerged as a branded IMFL player by launching premium liquor brands; Premiumisation strategies have helped RKL become the volume growth leader with IMFL volumes outpacing industry growth in the past 3-4 years.
- Improving demographics, favourable state policies and rising preference for premium brands would help RKL's IMFL sales volumes post a CAGR of ~13% over FY2021-24, outpacing the industry. OPM to improve to 19% by FY2024.
- RKL aims to turn net cash positive by FY2023 led by better working capital management and profitability. In absence of major capex, higher cash generated will be used for potential higher dividend payouts to shareholders.


**Radico Khaitan (RKL) has transformed itself into a leading Indian Made Foreign Liquor (IMFL) brand player from being just a distillery player with premiumisation at the core of its growth strategy. Volumes of Prestige & Above (P&A) brands clocked a CAGR of 16% over FY2017-21 contributing 30% to total IMFL sales volumes (that were 50% of sales value). This helped OPM improve by 430BPS to 17% in FY2021. The premiumisation strategy aided RKL to become volume growth leader with IMFL volume growth beat industry growth in the past 3-4 years. Efficient working capital management and improved profitability would help, the company to generate high free cash flows (FCF) in the coming years. With no major capex on books, the higher cash generated will be utilised for developing more premium brands and potential higher payouts to shareholders. We expect RKL's RoE/RoCE to improve to 17.6%/22.9% in FY2024 from 15.1%/17.4% in FY2021.**

- **Sustained focus on gaining market share:** RKL has developed a strong portfolio of premium brands, bridging the gap in the domestic liquor industry, which has helped it to improve market share over the years. Its holds 7% market share. Two of its leading brands, Magic Moment Vodka and the Morpheus brand hold a 60% and 56% market shares respectively, in the premium category. It is focusing on improving its share in largest domestic liquor category - whiskey by investing behind new launches and launching 2-3 premium products in the coming years.
- **Premiumisation core of growth strategy; OPM to expand by 200 bps by FY2024:** Premiumisation is at the core of RKL's growth strategy. Prestige & Above (P&A) brands' contribution improved to 30% in volume terms (and 50% in value terms) in FY2021 from 26% in FY2017. OPM expanded by 430 bps to 16.9% over the same period. With P&A brands' (OPM of 22-25%) sales volumes expected to clock a CAGR of 18% over FY2021-24, OPM is expected to further improve by 200BPS to 19% by FY2024 (with P&A brands' contribution expected to further improve to 34% in FY2024).
- **Net cash positive with improved return ratios by FY2023:** With an efficient working capital cycle (reduced to 34 days from 61 days from FY2017) and an improvement in the profitability, the net debt reduced by Rs. 750 crore over FY16-21 to Rs. 150 crore. RKL is expected to be net cash positive by FY2023. The company does not have any major capital expenditure plans going ahead and a large part of cash generation will be utilised for improving growth prospects of core brands, developing new premium brands and potential higher dividend payouts. We expect RKL's RoE/RoCE to improve to 17.6%/22.9% in FY2024 from 15.1%/17.4% in FY2021.

### Our Call

**View: Initiate coverage with Buy assigning Price Target of Rs. 1,250:** RKL will be one of the key beneficiaries of improving Indian demographics, consumer preference to premium brands and reviving liquor policies in various states. This along with deleverage balance sheet, the company is well-poised to achieve strong revenue and earnings CAGR of 17% and 22% over FY2021-24. The stock is trading at 30.9x/24.7x its FY2023/24E EPS, which is at ~50% discount to United Spirits Ltd (USL) valuations. Improved quality of earnings, higher free cash generation and a strong return profile will reduce valuation gap in the coming years. We initiate coverage on the stock with a Buy recommendation assigning price target of Rs. 1250 (valuing at 34x its FY2024E EPS).

### Key risk

Any change in the liquor policies in key states/sustained increase in the excise rate on liquor would act the sales volume and earnings growth of the company in the near to medium term.

**Valuation (Consolidated)** Rs cr

| Particulars | FY21 | FY22E | FY23E | FY24E |
|---|---|---|---|---|
| Revenue | 2,418 | 2,883 | 3,348 | 3,875 |
| OPM (%) | 16.9 | 17.1 | 18.0 | 18.9 |
| Adjusted PAT | 271 | 311 | 391 | 490 |
| Adjusted EPS (Rs.) | 20.8 | 23.3 | 29.3 | 36.7 |
| P/E (x) | 43.6 | 38.9 | 30.9 | 24.7 |
| P/B (x) | 6.7 | 5.9 | 5.1 | 4.4 |
| EV/EBIDTA (x) | 29.7 | 24.2 | 19.8 | 16.0 |
| RoNW (%) | 15.1 | 15.1 | 16.4 | 17.6 |
| RoCE (%) | 17.4 | 18.5 | 20.7 | 22.9 |

*Source: Company, Sharekhan estimates*

# Executive Summary

## 3R Research Positioning Summary

- **Right Sector:**
  Improving demographics, shift to premium brands and favourable liquor policies would help IMFL segment grow in double digits in the coming years.
- **Right Quality:**
  RKL has transformed itself into a leading IMFL manufacturing company with premiumisation at the core of its growth strategy.
- **Right Valuation:**
  The stock trades at 30.9x/24.7x its FY23/24E EPS, which is at 50% discount to USL valuation.

## Valuation and return potential

- **Discounted valuation :** The stock trades at 30.9x/24.7x its FY23/24E EPS, which is at 50% discount to USL's valuation.
- **Valuation gap to reduce:** Improved earnings growth potential, high FCF generation and a strong return profile will reduce valuation gap in future.

## Catalysts

**Long-term triggers**

- P&A brands' sales volume currently stands at 6-7 million cases, which is just 18% of USL's domestic P&A sales volumes.
- RKL will expand its portfolio with sustained new product addition in the premium segment.
- RKL has a 6% market share in the whiskey category, which provides ample opportunity to grow in the domestic market.

**Medium Term Triggers**

- P&A brands' sales volumes are expected to grow by 18% over FY21-24; contribution is expected to go up 34% by FY24.
- Premiumisation would help margins to further expand by 200 bps to 19% in FY24.
- Strong operating performance and reduction in interest cost will help earnings to grow at 22% over FY21-24.

**Key Risks:** A sustained increase in the excise rate on liquor would affect RKL's sales volumes and earnings growth in the near to medium term.

## Earnings and Balance sheet highlights

- **Strong financial track record:** Premiumisation strategy aided the company to post industry leading volume growth of 12% over FY17-21. Revenues and PAT grew at CAGR of 10% and 36%, respectively over FY17-21 with OPM expanding by 430 bps to 17% over the same period.
- **Efficient working capital management:** RKL's working capital cycle decreased to 34 days in FY2021 from 61 days in FY17; cumulative FCF stood at Rs. 1,370 crore over the same period. With strong cash flows, net debt declined by Rs. 750 crore.
- **Return profile to improve:** With strong earnings growth prospects and efficient working capital management, the cash flows on books further expected to improve. RoE and RoCE is expected to improve to 17.6% and 22.9% in FY2024E from 15.1% and 17.4% in FY2021.

| Table of Contents | Pages |
|---|---|
| **Right Sector - why we like liquor industry** | **1** |
| ◆ Premium liquor product sales to beat industry growth | 1 |
| ◆ Growth drivers for Indian liquor industry | 2 |
| ◆ Regulated structure | 4 |
| **Right Quality - why we like RKL** | **7** |
| ◆ Strong product portfolio with premium touch | 7 |
| ◆ Volume growth leader for past 3-4 years | 8 |
| ◆ Focus on gaining market share | 8 |
| ◆ Privilege & above brands contribution improved to 30% of sales volume | 9 |
| ◆ Focus on increasing global footprint | 10 |
| ◆ Revenues to grow at CAGR of 17% over FY2021-24 | 10 |
| ◆ Inflation in the ENA prices would be mitigated by backward integration and premiumisation | 10 |
| ◆ Increasing efficiencies through supply chain management | 11 |
| ◆ Premiumisation & efficient supply chain would help in margin improvement | 11 |
| ◆ Better profitability and lower interest cost would aid strong growth in the bottom-line | 11 |
| ◆ Better working capital management and higher cash flows led to debt reduction | 12 |
| ◆ Limited capex will pave way for higher investment behind brands and better dividend payout | 12 |
| **Financials in charts** | **13** |
| **Company overview** | **14** |
| **Valuation - Discounted valuation and strong growth prospects with improving cash flows makes it a good pick** | **19** |
| ◆ Sector Outlook – Liberal state policies and changing consumer preference to drive growth | 19 |
| ◆ Company Outlook – Premiumisation would lead to strong earnings growth | 19 |
| ◆ Valuation – Initiate coverage with Buy assigning a price target of Rs. 1,250 | 19 |
| ◆ Peer comparison | 20 |
| **Key financials** | **21** |
| ◆ P/L account | 21 |
| ◆ Balance Sheet | 22 |
| ◆ Cash Flow Statement | 22 |
| ◆ Key Ratios | 23 |
| **RKL snapshot** | **24** |
| ◆ About company | 24 |
| ◆ Investment argument | 24 |
| ◆ Key risks | 24 |
| ◆ Key management personnel | 24 |
| ◆ Top 10 shareholders | 24 |
| **3R Philosophy definitions** | 25 |

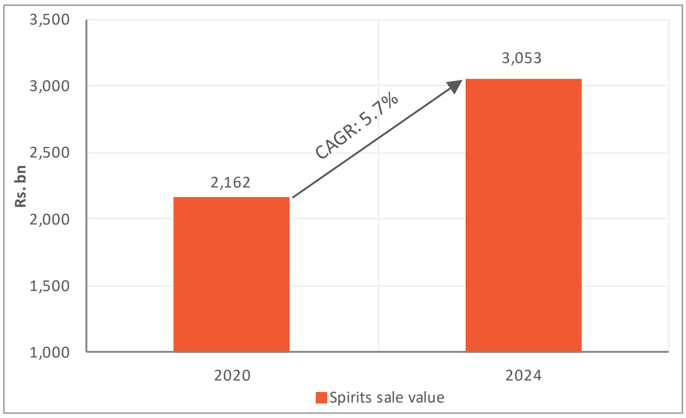
## Why we like liquor industry

***Improving demographics, lower per capita consumption, shift to premium brands and favourable change in liquor policies in some of the key states, provides huge scope for Indian Made Foreign Liquor (IMFL) players to grow strongly in the coming years. Though the IMFL segment is expected to grow at ~6% over CY2020-2024, the liquor companies with a portfolio of strong premium brands will outpace the industry in the medium to long term due to increase in preference for premium brands.***

### Premium liquor product sales to beat industry growth

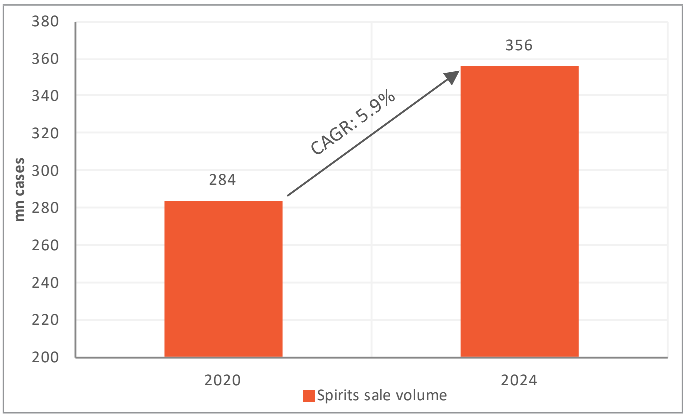
The Indian spirits industry has been clocking an over 12% CAGR since 2001 making it one of the fastest growing markets in the world. A slowdown of economy in 2019 followed by COVID-19 virus outbreak in 2020 hit liquor consumption in India. However, demand for premium brands was relatively less impacted by the industry slowdown. Consumers are having more disposable incomes which they can use to have a quality experience at home. Therefore, premium brands are likely to show much more resilience and grow in the near future. India has an incredibly large young demography, which presents many opportunities to firms in the industry. Revenues from IMFL sales are expected to post a CAGR of 5.7%, while sales volumes are likely to clock a 5.9% CAGR during CY2020-24. The vodka segment is expected to perform better during the same period with volume growth of 5.6% and value growth of 11.0%.

**CY2020-24 – Trend in revenues...**




*Source: Industry, Sharekhan Research*

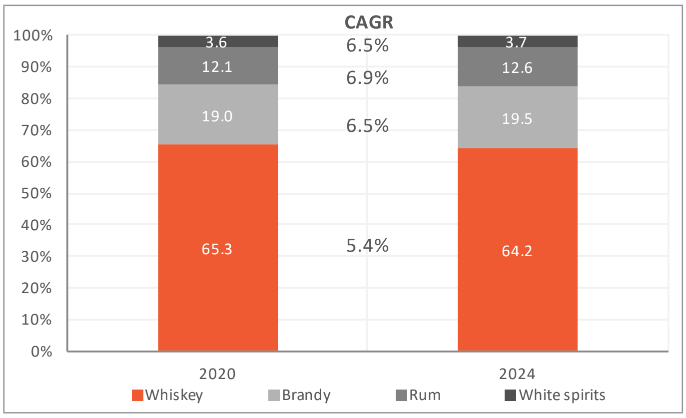
**...in line with that of sales volumes**




*Source: Industry, Sharekhan Research*

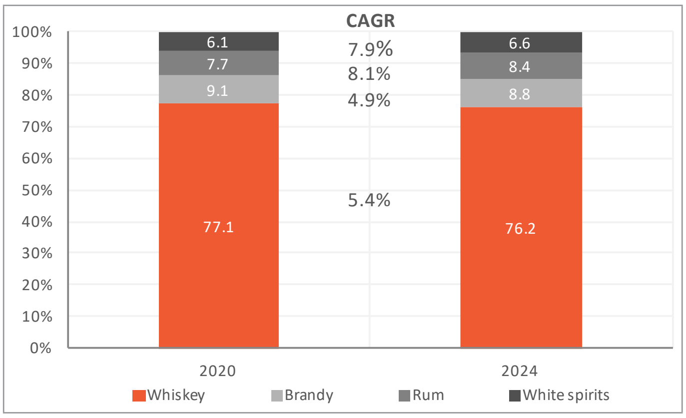
The Indian spirits industry is segmented into IMFL (Indian Made Foreign Liquor), IMIL (Indian Made Indian Liquor), wine, beer and imported alcohol. Whiskey dominates the industry by a very wide margin. The IMFL segment accounts for more than 70% of the market. Traditionally, brown spirits which include Whiskey, Brandy and Dark Rum have been the major contributors towards overall IMFL sales volume together comprising of 96.4% of the total IMFL volumes and 93.4% of revenues in CY2020, while white spirits such as Vodka and Gin account for 3.6% of the total IMFL volumes and 6.6% of the value in the same year. Each of these categories are expected to grow at 5-8% CAGR during CY2020-24.

**Category-wise volume growth...**




*Source: Industry, Sharekhan Research*

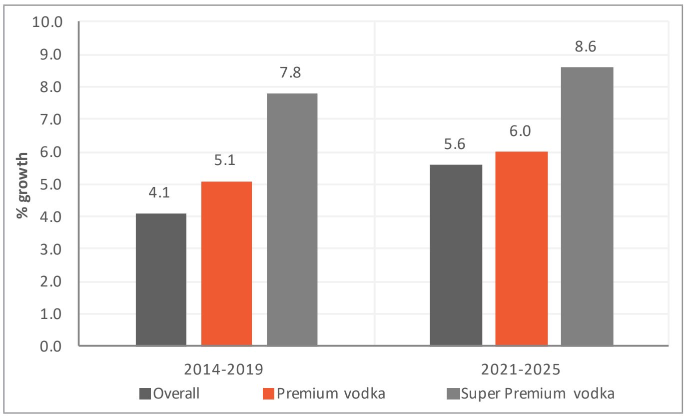
**...and revenue growth**




*Source: Industry, Sharekhan Research*

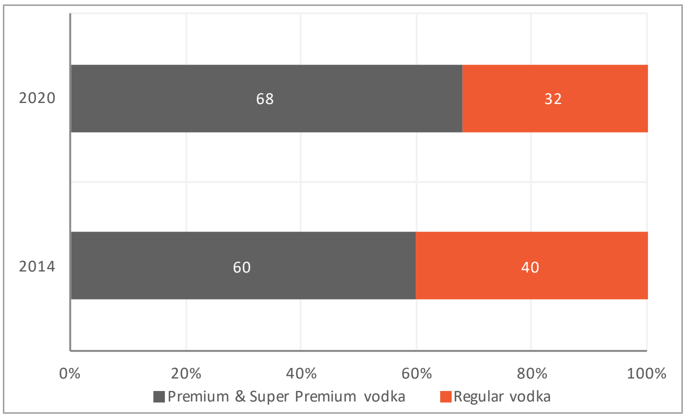
Among white spirits, the vodka segment's growth indicates a strong premiumisation trend with volume growth of Super Premium and Premium Vodka higher that the overall volume growth coupled with an increase in market share. This trend is expected to continue and the share of premium category vodka is anticipated to increase further.

**Premiumisation trend in vodka category**




*Source: Industry, Sharekhan Research*

**Increased market share of Super-Premium and Premium Vodka**

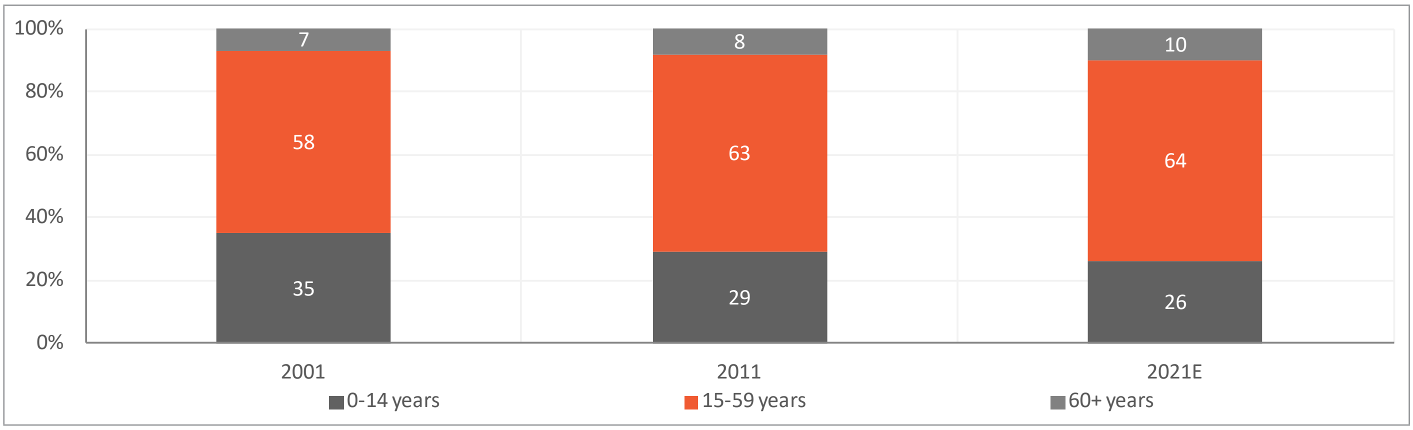



*Source: Industry, Sharekhan Research*

## Growth drivers for Indian liquor industry

**Favourable demographics:** India has a young demographic profile and over 15 million people are expected to enter the drinking age every year, which represents significant growth opportunities for the industry. Total household consumption is expected to reach a size of Rs. 300 trillion by 2030. Further, with proportion of high-income households getting widely distributed, the contribution from tier-2, -3 and -4 cities to the consumption is likely to increase.

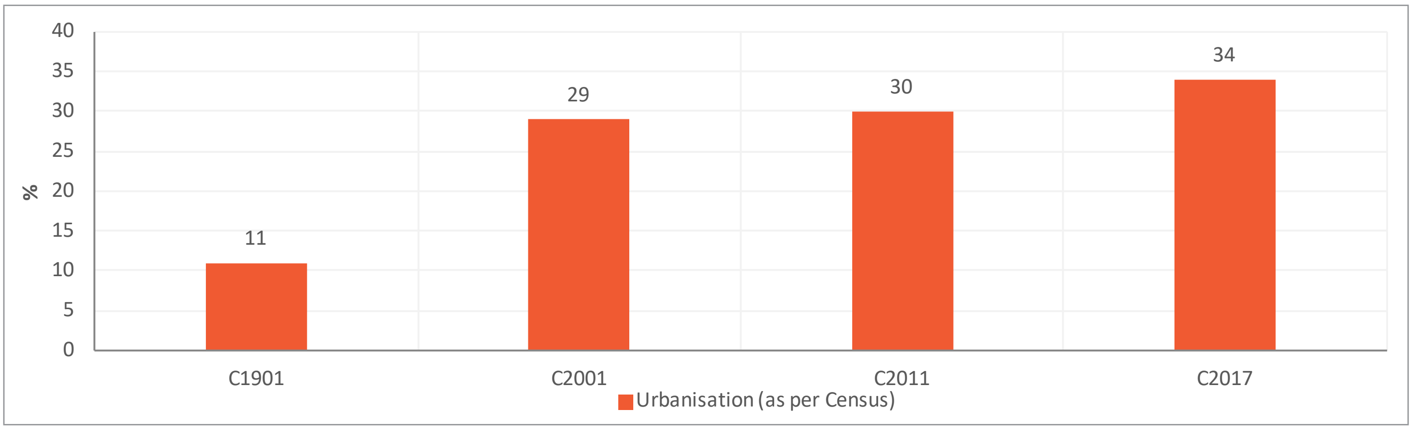
**A wider drinking age population**




*Source: Industry, Sharekhan Research*

**Urbanisation:** India's huge population is migrating towards bigger cities, where they are exposed to a wider variety of alcoholic beverage products, including IMFL and thus they significantly contribute to market growth. Rapid urbanisation is expected to enhance disposable income, which is favourable for the industry's growth.

**Rising Urbanisation**

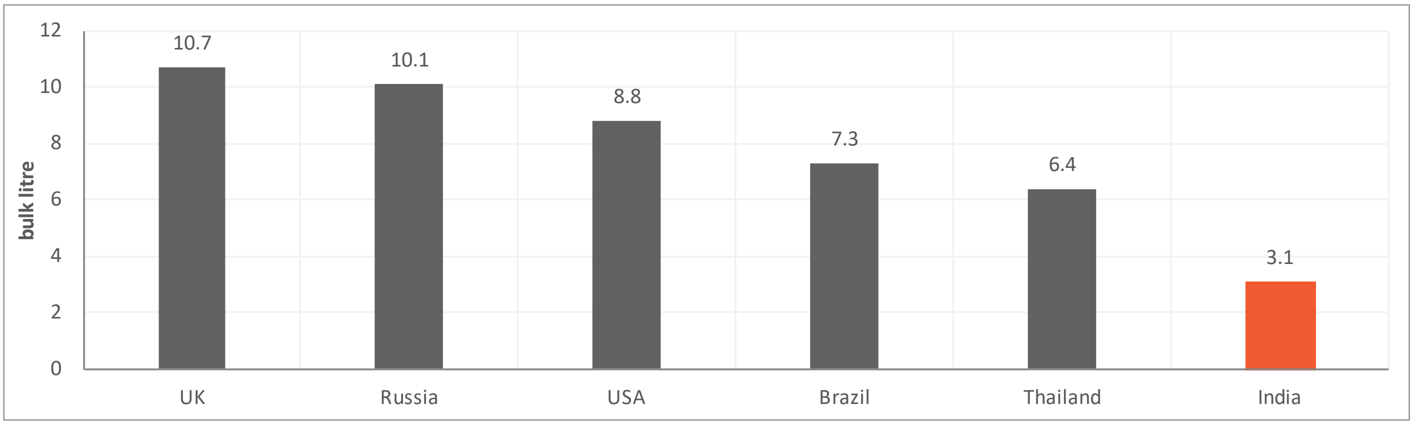



*Source: Industry, Sharekhan Research*

**Growth in rural consumption:** Rural consumption is expected to grow faster with growing incomes and greater internet penetration. Even during COVID-19, the rural economy has shown more resilience over the last year due to a better crop season and ongoing policy support.

**Low per capita consumption:** India remains one of the most under-penetrated markets, indicating ample scope to grow further. It is expected that per capita consumption will increase with changes in lifestyle and aspirations of the population.

**Per capita (15+ years) alcohol consumption (2014)**



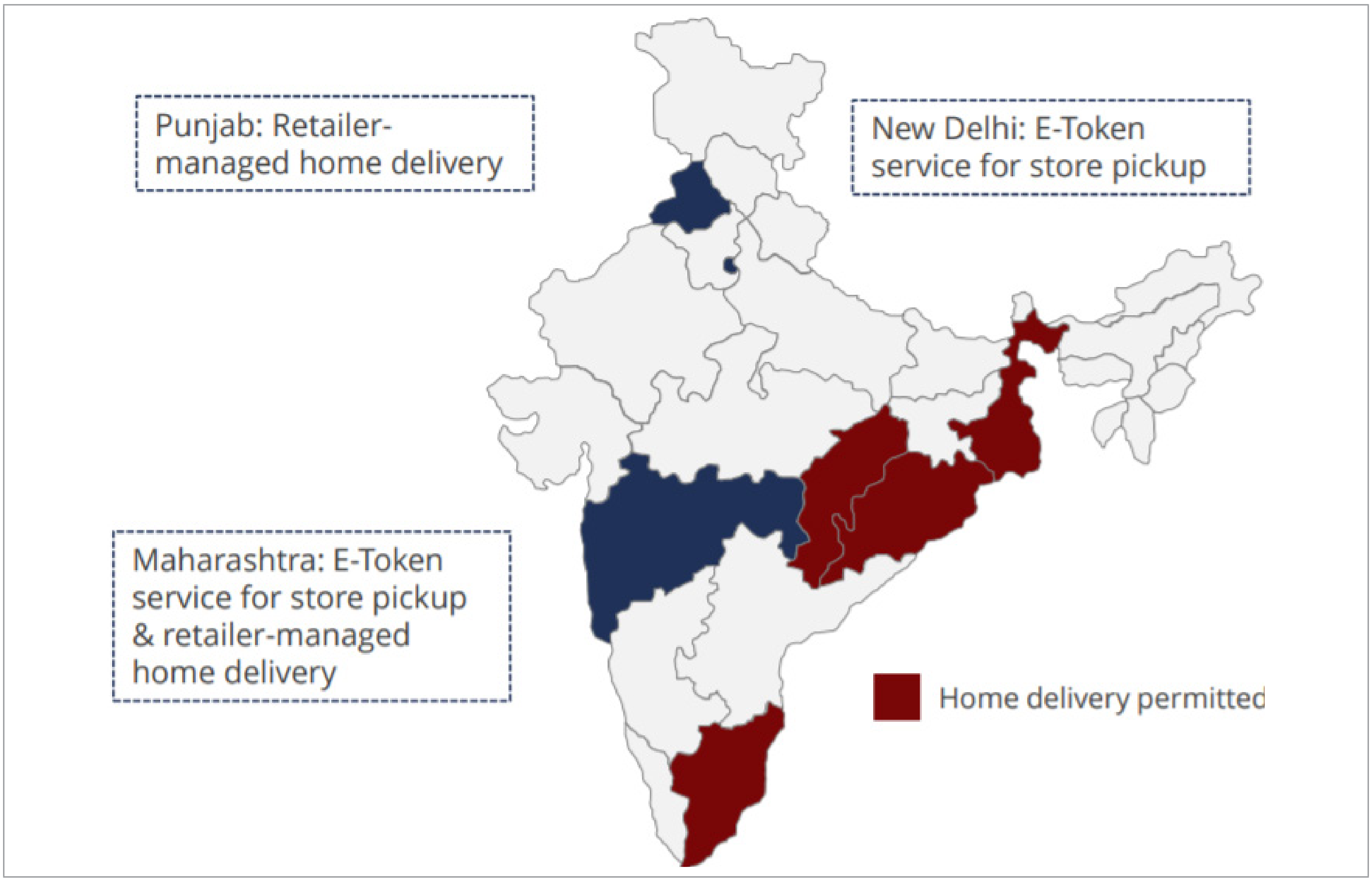

*Source: Industry, Sharekhan Research*

**Changing consumer preferences towards premiumisation:** Rising affluence is the biggest driver of increasing consumption. With more Indians traveling abroad, rising aspirations, favourable environment for imported liquor and higher disposable income, consumers are upgrading towards premium liquor segments. Additionally, consumer behaviour and spending patterns are shifting as disposable incomes rise and Indian society evolves with a preference for lifestyle and aspirational brands. The rise in premiumisation is evident in the higher focus of the big players on semi-premium and premium categories with an increase in product launches and marketing of these categories.

**Increased Alcohol Accessibility and Availability:** Over the past few years, there has been a huge change in attitudes and lifestyle, making consumption of alcohol more socially acceptable. This acceptability of alcohol extends to drinking in family environments, at social events and by females/youngsters. There has been an increase in the variety of alcoholic beverages and brands with most of them easily available at government-licensed outlets, government shops, private licensed retail chains, restaurants, pubs and bars.

**New avenues of online orders and home delivery:** Amid the COVID-19 pandemic and to make-up for the loss of sales with consumers refraining from going for liquor purchases, many state governments have now allowed home delivery of liquor. Retailers directly deliver liquor to homes and also through agencies like food aggregators and standard technology platforms. In long run, this may help increase industry revenues as many consumers, particularly women, are not comfortable going out to buy liquor from shops.

**Online liquor sales in India**




*Source: Company*

**Improved operating environment:** The importance of the liquor industry to the state's exchequer cannot be understated. A significantly improved operating environment led by state-wide price hikes and favourable policy changes resulted in this robust industry performance. Most of the excise policy changes last year have focused on enhancing state revenues without increasing taxes which bodes well for the organic growth in the industry.

### Regulatory structure

Both central and state governments have certain restrictions on production, movement and sale of spirits in the country. Licenses are required to produce, bottle, store, distribute or retail all alcoholic beverage products. Prohibitively high inter-state duties compel national alcoholic beverage players to set-up owned or contract manufacturing setups in every state. Distribution is also highly controlled, both at wholesale and retail levels. In addition, direct advertising of alcoholic beverage products is not permitted in India.

**State wise structure and regulations**

| Market structure | Overview | Pricing control | States |
|---|---|---|---|
| Free / Open market | A business may apply for a license for a fee defined by the state government subject to license availability | Company has reasonable independence over price hikes | Arunachal Pradesh, Assam, Goa, Maharashtra, Meghalaya, Tripura, Uttar Pradesh |
| Auction market | The license for sale of liquor is auctioned by the Government to the highest bidder on an annual basis based on an auction process | Company has to negotiate price increases with state appointed distributors | Chandigarh, Haryana, Punjab |
| State owned/ Government corporations | The government is the wholesaler and/or distributor who purchases directly from a company. Some states also have retail shops run by the government | Strict control on pricing by the state government | Andhra Pradesh, Chhattisgarh, Delhi, Jharkhand, Karnataka, Kerala, Madhya Pradesh, Rajasthan, Tamil Nadu, Telangana, West Bengal |
| Prohibition | States where sales of liquor is prohibited | Not applicable | Bihar, Gujarat |

*Source: Company; Sharekhan Research*

## Additional taxes/levies due to COVID-19

During FY2021, post the COVID-19 outbreak, most of the states experienced lockdown which created stress in the economy. As a result, there were additional taxes/levies in some states leading to a price increase for consumers.

**Actions taken by states**

| State | Rate hike during COVID-19 |
|---|---|
| Rajasthan | 10% increase in excise duty on IMFL |
| Delhi | 70% COVID-19 cess on MRP |
| Karnataka | 11% increase in excise duty |
| Andhra Pradesh | 75% increase in excise duty |
| Telangana | 15% COVID-19 cess on MRP |
| West Bengal | 30% additional sales tax |
| Odisha | 30% COVID-19 cess on MRP |
| Punjab | Additional excise of Rs. 10 per bottle |
| Tamil Nadu | 15% increase in excise duty |
| Kerala | 35% COVID-19 cess on IMFL |
| Assam & Meghalaya | 25% increase in excise duty |
| Uttar Pradesh | Hike of Rs. 5 to Rs. 400 depending upon type and size |
| Jammu & Kashmir | 50% increase in excise duty |
| Goa | 20% increase in excise duty |

*Source: Industry; Sharekhan Research*

## Progressive liquor policy in Uttar Pradesh

In 2018, the Uttar Pradesh state government came out with a new policy for sale of liquor in the state. The policy aimed at hitting the liquor cartels operating in Uttar Pradesh, especially in western UP and curb rampant liquor smuggling from neighbouring states. Liquor smuggling was quite rampant in western UP due to a higher excise duty in the state compared to neighbouring states. A new online bidding process for liquor retail shops was introduced and traders would individually bid for each retail outlet. To encourage digital payments, liquor retailers would provide facilities for electronic payments through debit/credit cards, e-wallets, etc. The policy further sought to curb rampant illegal liquor trade and smuggling, which resulted in excise revenue loss to exchequer.

According to the 2021-22 policy, UP has made it mandatory to obtain licence to purchase, transport and store liquor more than prescribed limit of 1.5 litres of each country made foreign liquor and IMFL. The sale of foreign liquor in 90 ml bottles under the regular category would be permitted. Low-alcohol beverages (LBA) would now be available at retail shops of foreign-made liquor, model shops, and premium retail vend besides the beer shops. Renewal of country liquor, foreign liquor, beer, bhang retail shops, and model shops has been permitted for 2021-22. To promote ease of doing business, brand registration, label approval, bar and micro-brewery licences will have the option to be renewed up to three years instead of requiring approvals every year. The new policy also encompasses the total digitalisation of the excise department in 2021-22. Efforts would be made to computerise all processes and procedures of the excise department under the Integrated Excise Supply Chain Management System (IESCMS). The provision that no liquor shop shall be opened within 5 kilometres of the border of another district, without the consent of the collectors of both the districts, will be removed. All these majors will be positive for branded players to increase their sales volumes in the coming years. With such favourable reforms, UP government is targeting excise revenues of Rs. 50,000 crore from Rs. 32,000 crore in the short span.

**Delhi liquor policy, 2021 – following footsteps of UP**

The new liquor policy will be implemented from November 17, 2021 and will mark the exit of the Delhi government from the retail business of liquor. By appointing new retail licensees, the Delhi government is trying to pave the way for a range of sweeping reforms to boost the city's revenue, to crack down on the liquor mafia and improve user experience under the new state excise policy. Under the Delhi Excise Policy, 2021, the city has been divided into 32 zones and allotment of licenses is now being done on a zonal basis. Those who have won a zone or two have been given L-7Z or L-7V licences which are meant for retail sale of Indian and foreign liquor (except country liquor) in Delhi. With the new policy, liquor shops in the capital, will also be able to offer discounts, enabling festive season offers that are usually seen around Diwali on vehicles, electronics, and gift items. It also allows home delivery of liquor in the capital through websites and apps.

**Rajasthan liquor policy 2021 – transforming from conservative to liberal liquor policy**

Rajasthan government has allowed bars to operate microbreweries. The state has also allowed an additional 2,100 urban vendors to sell both IMFL and country liquor, raising the total number of vendors selling both IMFL and country liquor from 5,600 to 7,700. The new policy also does away with the lottery system for allotment of liquor shops. In its place, an e-auction system has been introduced.

## Why we like Radico Khaitan

***Radico Khaitan Limited (RKL) has transformed itself into a leading Indian Made Foreign Liquor (IMFL) brand player from just a distillery player with premiumisation at core of its growth strategy. The company has leadership positioning in categories such as vodka and premium brandy and focusing on improving its positioning in the whiskey segment through new launches. Premiumisation strategy helped it to become volume growth leader with IMFL volume growth outpacing industry growth in the past 3-4 years. The contribution of Prestige & Above (P&A) brands to IMFL sales volumes improved to 30% (50% in value terms). This along with operating efficiencies aided in OPM improving by 430 bps to 17% in FY2021 and is further expected to enhance by 200 bps to 19% by FY2024. With no major capex plan going ahead, we expect enhanced cash flows will be utilised for potential higher dividend payout to shareholders, adding more premium brands to the portfolio and improving growth prospects of core brands.***

### Strong product portfolio with premium touch

RKL started its journey of branded products from 1998. Product innovation, catering to consumer aspirations and identifying gap in the market has been key to RKL's success over the years. The company has continuously tracked changing industry dynamics, consumption patterns and consumer preferences to drive its product innovation. It has launched multiple brands including 8PM Whisky, Old Admiral Brandy, Contessa Rum, etc, with a focus on improving its presence in key spirits categories in India. The company started its premiumisation journey in 2006 by launching multiple brands (including Magic Moment Vodka), which helped the company to achieve sustainable revenue growth and consistent improvement in OPM. Further, the company has improved its brand image in the international market with the launch of super-premium brands such as Rampur Indian Single Malt Whisky and Jaisalmer Indian Craft Gin. Its strong premium product portfolio, resilient business model and presence across key markets has aided it to consistently outperform the industry (during pandemic as well). Customer-centric new product launches, supporting the brands with higher media spends (7-8% of IMFL sales) and improving distribution would help the company to remain ahead of industry over the next few years.

**RKL: Journey to Premiumisation**

| Before 1998: Bulk supplier & bottler | 1998-2006: Volume creation | 2006 onwards: Premiumisation |
|---|---|---|
| During this phase, the company's operations were concentrated on supplying bulk spirits and as a bottler to other spirit manufacturers. By 1996, RKL had created large capabilities and gained expertise to manufacture high quality spirit for branded players and armed forces/CSD. | This phase saw RKL move steadily in the branded, premium market with the launch of multiple brands including 8PM Whisky, Old Admiral Brandy, Contessa Rum, etc. It concentrated on building a strong manufacturing platform, establishing a robust pan India distribution network and achieved sales volume of over 10 million cases. | Premiumisation started with the launch of Magic Moments vodka, which became the largest selling vodka in India and one of the largest globally. During this period, RKL achieved premium sales volume of over 7 Million cases. The Company has launched twelve new brands over the last decade of which eleven have been from the premium category. |

*Source: Company; Sharekhan Research*

**Built strong portfolio of premium brands in last 10 years**


*Source: Company; Sharekhan Research*

**Broad choice for consumers with Premium pricing** **(Price per 750ml)**

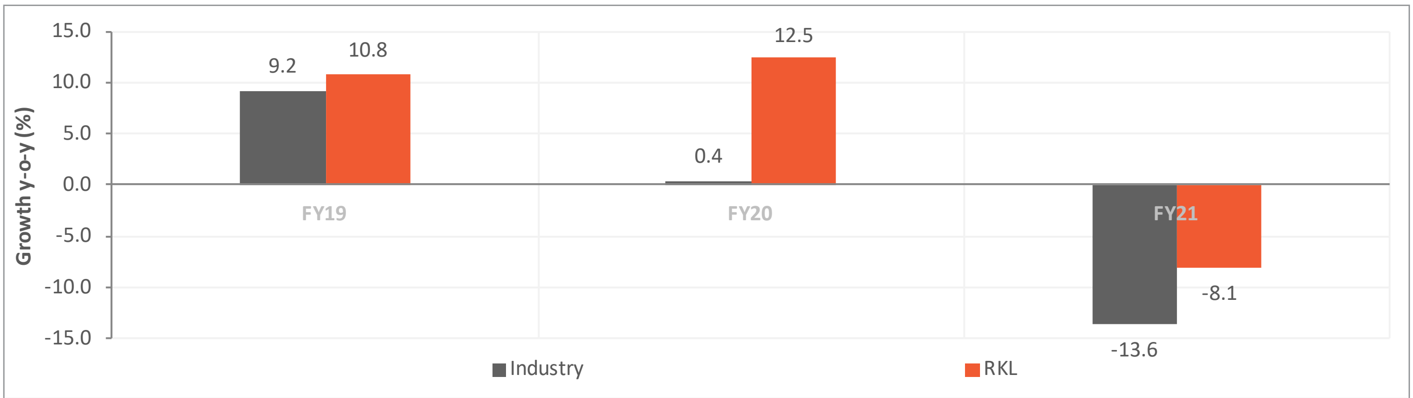
| Company | Whiskey | Premium Whiskey | Vodka | Premium Vodka | Brandy | Rum |
|---|---|---|---|---|---|---|
| Radico | 8pm - 460; 8PM Black - Rs600-700 | Rampur - ~Rs4000 | Magic Moments - 800 | Magic Moments Verve - 900 | Morpheus - 1390 | Contessa - 550 |
| | After dark - 1400 | | | | Whytehall - Rs400-500 | RKL 1965 - 550 |
| United Spirits | McDowells No.1 - 640 | Black Dog Centenary - 2500 | Romanov - 670 | Smirnoff - 1560 | McDowells No. 1 - 540 | McDowells No. 1 Rum - 540 |
| | Royal Challenge - 800 | Black Dog Triple Gold - 3060 | White Mischief - 730 | Ketel One - 3500 | Honey Bee - 580 | |
| | Imperial Blue - 670 | Black & White Blenders Scotch - 2650 | | | | |
| Pernod | Royal Stag - 720 | Ballantines - 3075 | Fuel - 850 | Absolut - 3100 | | |
| | Imperial Blue Superior - 600 | Chivas Regal - 5600 | | | | |
| | Blenders Pride - 1350 | 100 Pipers Premium Scotch - 3650 | | | | |

*Source: Sharekhan Research*

## Volume growth leader for past 3-4 years

With more than 60% of India's market dominated by whiskey category, RKL has taken non-conventional route of building presence in smaller categories such as rum, vodka and gin by launching premium products in each category. With higher demand for premium brands, RKL premium portfolio registered faster growth in the domestic market. The company's IMFL volume growth stood ahead of industry growth for the past four years (even during the pandemic year).

**Consistently outperforming the industry over the past three years**




*Source: Company, Sharekhan Research*

## Focus on gaining market share

RKL has dominant market positioning in few of its product categories. In the vodka and super premium brandy categories, the company has leadership positioning with over 60% market share each. In rum category the company has 30% market share. Magic Moment Vodka Verve has a 20% market share in the premium vodka category. In whiskey (constituting more than 60% of domestic liquor market), the company has 6% market share. Overall RKL has 7% market share in the domestic liquor industry. The company has two formidable brands in whiskey segment - 8PM Whisky and 8PM Premium Black Whisky. The company will be focusing on enhancing its market share in the whiskey segment by launching 2-3 new products in the coming years. The company would be focusing on launching these products in the premium (contribution rate is $20 million a case), which is around 10% of the overall whiskey market. It is also planning to launch one new brand in the vodka category and a premium brand in the Gin category. With premiumisation at core of strategy and sustained new product launches the management is confident of achieving 100-150 bps expansion in the market share over the next two to three years. Further, RKL is aggressively investing behind brands to improve its visibility amongst the consumer.

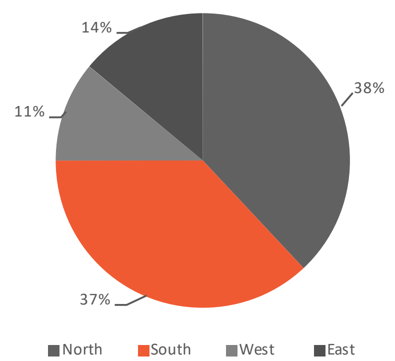
**Market share in key categories**

| Brands | Category | Market share (%) |
|---|---|---|
| Magic Moment | Vodka | 60% |
| Morpheus Super Premium; Whytehall | Brandy | 60% |
| Contessa | Rum | 30% |
| Magic Moment Verve | Premium Vodka | 20% |

*Source: Company*

Uttar Pradesh (UP), Karnataka, Andhra Pradesh, Telangana and Tamil Nadu constitute 65% of liquor market in India. With premium product portfolio, RKL has strong presence across key markets. In UP, the company has 30% market share. Lesser per capita consumption, progressive liquor policy and introduction of modern shops/premium shops in the state will help, RKL's market share to further expand in the state of UP. Delhi has followed the UP model with some restrictions. Similarly, Punjab and Haryana are also considering transferring their model in-line with the UP model. This will help RKL to gain market share in some of this states. Further, the company has strong market share in states such as Maharashtra, Karnataka, Telangana, Andhra Pradesh and Uttarakhand. In southern states, the company has gained market share by 150-200 bps in last two years.

**Region wise revenue split**

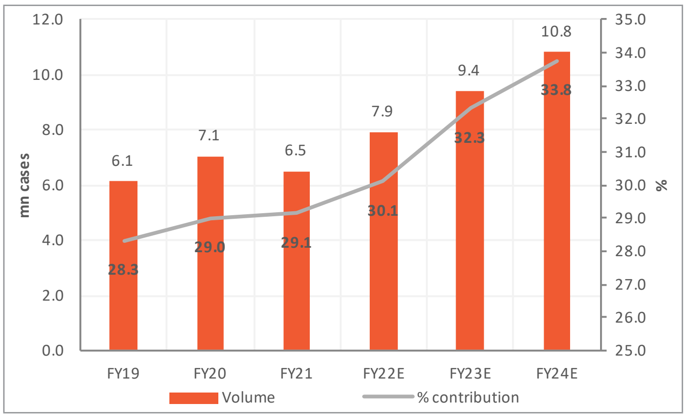



*Source: Company, Sharekhan Research*

### Prestige & above brands contribution improved to 30% of sales volume

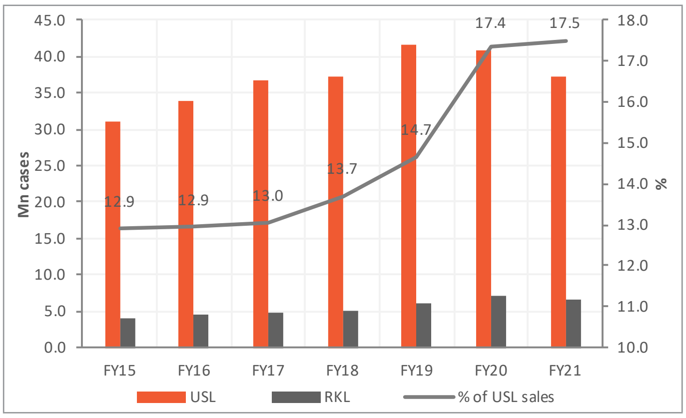
Prestige & Above (P&A) brands' contribution improved to 30% of sales volume (50% of sales value in FY2021) from 26% in FY2017 (18% in FY2014). Due to improving demographics and changing consumer preferences to premium products, the demand for premium products has grown consistently in key markets. This along with higher media spends helped RKL post consistent improvement in P&A sales volume in past few years. RKL's P&A sales volume clocked an 11.7% CAGR over FY2015-20 aiding IMFL sales volume to grow at CAGR of 4.5% over the same period. RKL's P&A sales volumes to United Spirits sales of P&A brands is just 17%, which provides huge opportunity for RKL to improve its sales in the coming years. With new product launches in the key categories, P&A sales volume is expected to further improve to 34-35% by FY2024. P&A brands are expected to post a CAGR of 18% over FY2021-24.

**P&A contribution to sales volume improve**




Source: Company, Sharekhan Research

**RKL's P&A sales are 17% of USL P&A sales volume**




Source: Company, Sharekhan Research

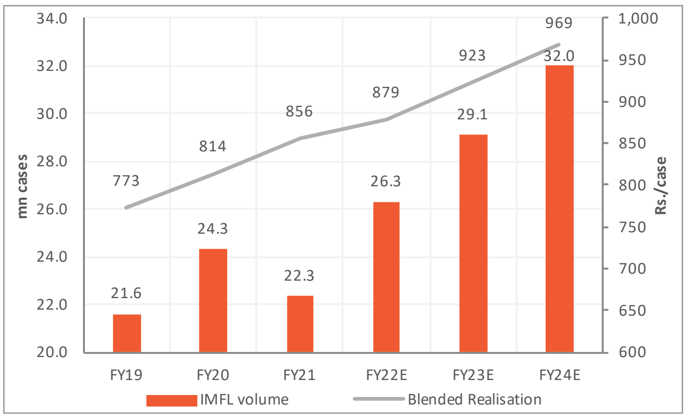
## Focus on increasing global footprint

The sustained focus on creating strong brand portfolio over the past few years is now paying rich dividends in the international markets. RKL's brands are available in more than 85 countries. Despite the pandemic and frequent lockdowns, RKL's exports registered strong growth during FY2021 and contributed over 7% of the total net revenue from operations. Due to strong brand equity, RKL's brands were the preferred ones for home consumption. Online sales for its luxury portfolio were able to offset non-availability of Global Travel Retail Channel. RKL successfully launched a new expression of its Indian Single Malt – Rampur Asava in London. The brand has received encouraging response from global whiskey experts, consumers as well as traders. Within a short span, Jaisalmer Indian Craft Gin has a global footprint in more than 25 countries.

## Revenues to grow at CAGR of 17% over FY2021-24

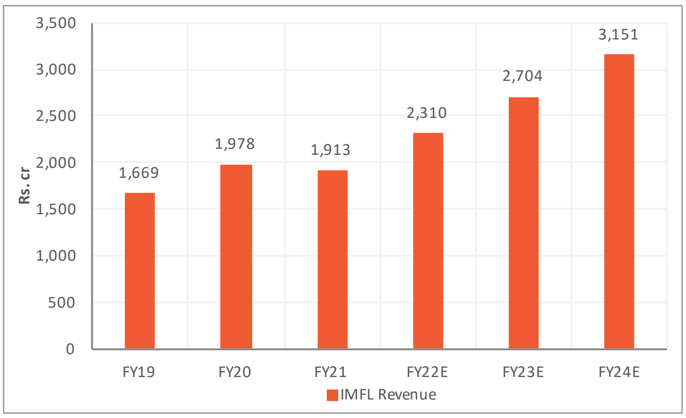
RKL's net revenues clocked a 10% CAGR over FY2017-21 affected by roadblocks such as implementation of GST and pandemic. However, with consumers shifting to premium IMFL brands, RKL's focus on improving presence of each brand in key markets and emergence of favourable liquor policies in key states would help in faster growth of branded liquor products in the near to medium term. Thus we expect RKL's revenues to grow at CAGR of 17% over FY2021-24 to Rs. 3,875 crore. The growth will be largely driven by ~13% volume growth in the IMFL brands over the same period (led by 18% volume growth in P&A brands). Better revenue mix would lead to blended realisation to grow at CAGR of 4% over the same period.

**Increase in sales volume of IMFL brand and blended realisation**




Source: Company, Sharekhan Research

**Trend in IMFL brand revenues**




Source: Company, Sharekhan Research

## Inflation in ENA prices would be mitigated by backward integration and premiumisation

Raw material prices remained been benign sequentially in Q1 FY2022. Towards the end of last fiscal, some inflationary pressure was seen in dry goods such as packing material, but it has remained stable around those levels in Q1 FY2022. ENA prices remained stable in Q1 FY2022. Given the Centre's ethanol blending policy, the company might see some headwinds in the ENA prices, but that should not be significant. Around 65% of the company's alcohol is manufactured through grain based ENA while 35% is manufactured through molasses based ENA. Inflation in grain prices not expected to be significant as it consumed by common man. Hence inflation in the ENA prices for RKL is expected to be moderate. Moreover, with the backward integration into captive ENA production, the company is protected from any significant fluctuations in ENA prices. Further as the company moves to premiumisation ladder the margins are less susceptible to raw material inflation. Overall, gross margins are gradually expected to improve in the medium to long term.

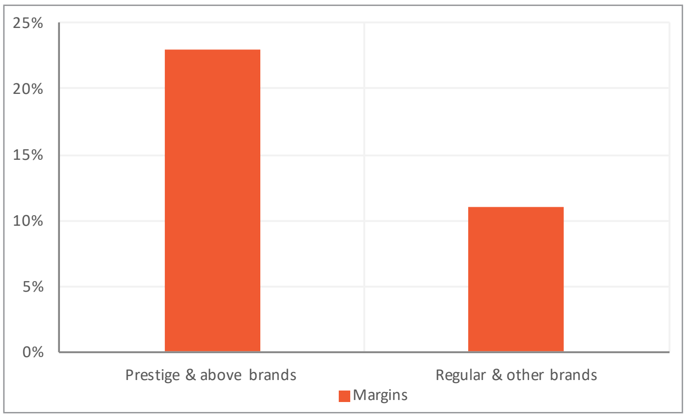
### Increasing efficiencies through supply chain management

To mitigate supply chain risks emerging from the pandemic, RKL is minimising import from China and other countries. The company is developing its sourcing base in India to maximise the supply chain efficiency. RKL has done reverse auction in past in logistics and is currently exploring the possibility in packaging and other materials to control costs. To enable more efficiency in procurement process, RKL is utilising IT based tools for full-fledged material requisition planning starting from sales forecast to ordering, inventory management to cost control and to service market fast. The company is also identifying the key business partners to create collaborative approach to improve the supply chain in the medium to long term.

### Premiumisation & efficient supply chain would help in margin improvement

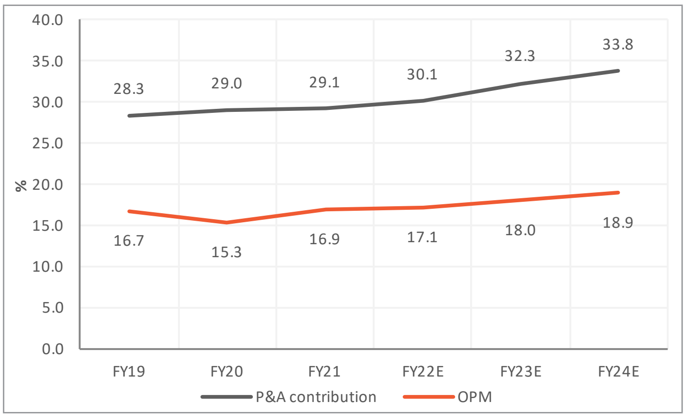
Premiumisation strategy and operating efficiencies helped OPM to expand by 430 bps to ~17% in FY2021 (contribution of P&A brands to IMFL sales volume improved by 310 bps over the same period). With contribution of P&A expected to go up to 34% by FY2024 (IMFL brand sales to reach 32 million cases), the OPM is expected to further improve to 19% by FY2024.

**Prestige & above brands have higher margins than regular brands**




*Source: Company, Sharekhan Research*

**Trend in increase in contribution of P&A brands and OPM**

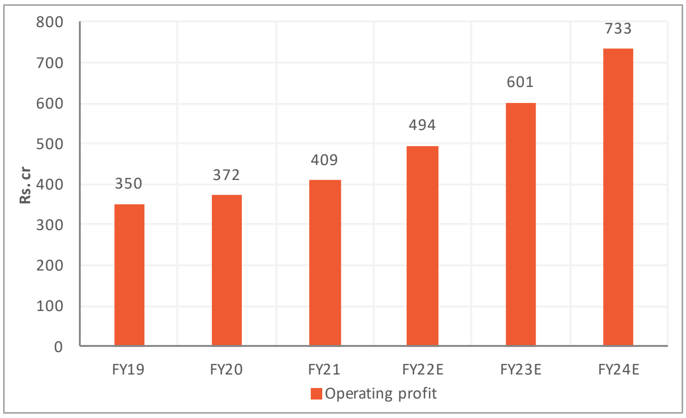



*Source: Company, Sharekhan Research*

### Better profitability and lower interest cost would aid strong growth in the bottom-line

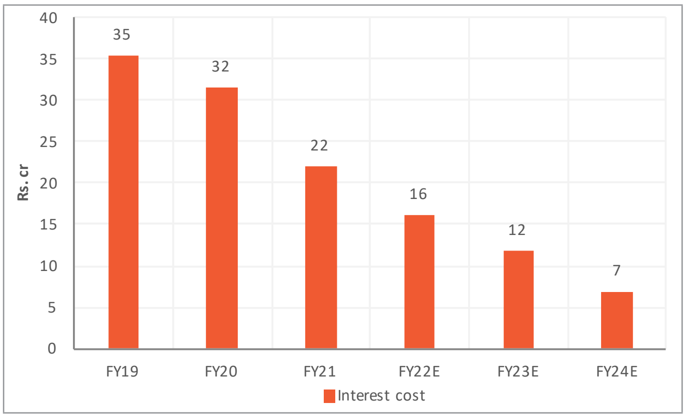
RKL's operating profit is expected to clock a CAGR of 21% over FY2021-24. This will be driven by strong revenue growth and expansion in the margins in the same period. Further the reduction in the debt would lead to sustained decline in the interest cost by 60-70% by FY2024. Overall PAT is expected to grow at CAGR of 21% over FY2021-24.

**Steady rise in operating profit**




*Source: Company, Sharekhan Research*

**Reduction in the interest cost**

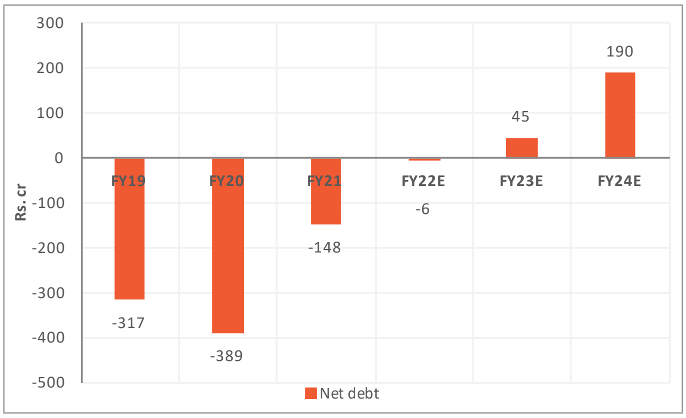



*Source: Company, Sharekhan Research*

### Better working capital management and higher cash flows led to debt reduction

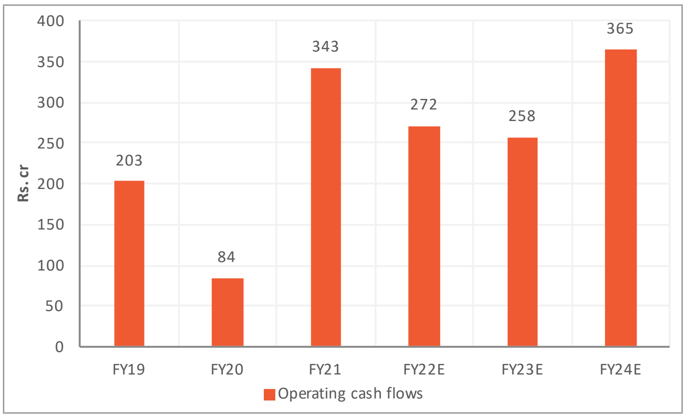
Scaling down of volumes in certain states were company was making lower margins and tight on credit norms coupled with efficient inventory management helped RKL to reduce working capital days from 61 days in FY2016 to 34 days in FY2021. This aided the company to generate cumulative free cash flow of Rs. 1,144 crore over FY2017-21. The large chunk of FCF generated was utilised to reduce debt by Rs. 400 crore over the same period. With higher cash generation, the company is expected to be net cash positive by FY2023.

**Company to be net cash positive in FY2023**




*Source: Company, Sharekhan Research*

**Improvement in operating cash flows**

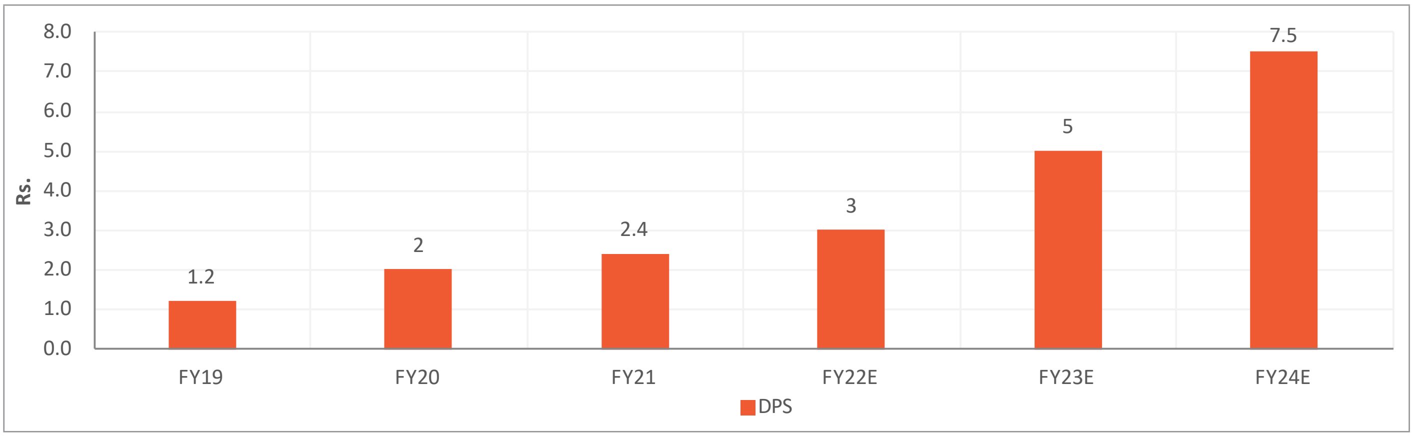



*Source: Company, Sharekhan Research*

### Limited capex will pave way for higher investment behind brands and potential higher pay-out

With no major capex plan going ahead, the company is planning to invest large part of cash generated in creating high margin products, which will help it to improve return ratios at faster pace. We expect RKL's return ratios – RoE and RoCE are expected to improve to 17.4% and 22.6% in FY2024 from 15.1% and 17.4% in FY2021. This brands will be created organically as there are no inorganic opportunities visible in the domestic market. Further after investing behind brands, the company has decided remaining cash in creating value for shareholders in the form of potential higher dividend pay-outs or buybacks.

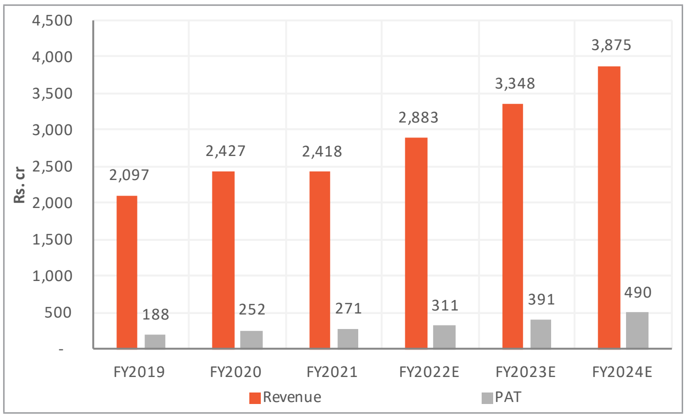
**Trend in Dividend per share**




*Source: Company, Sharekhan Research*

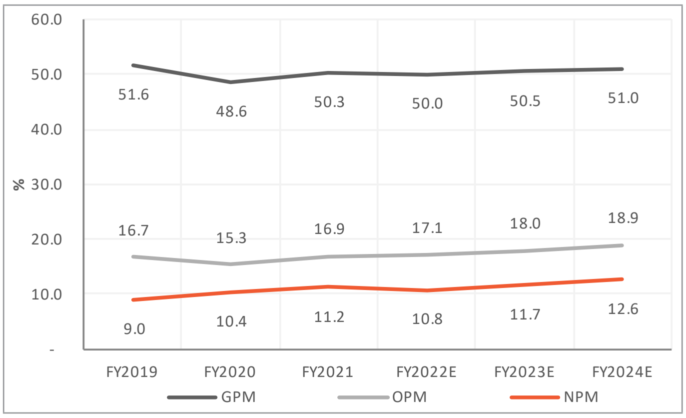
## Financials in charts

### Consistent growth in revenue and PAT



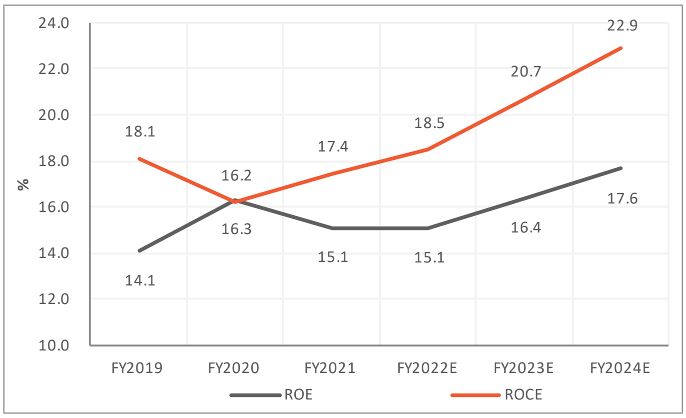

Source: Company, Sharekhan Research

### Margins to expand from current level



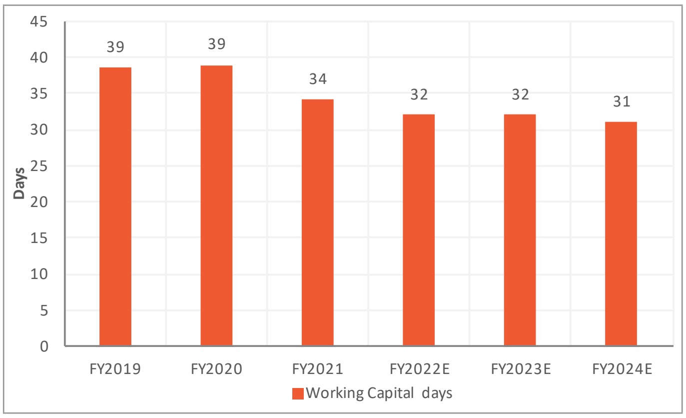

Source: Company, Sharekhan Research

### Return ratios to improve



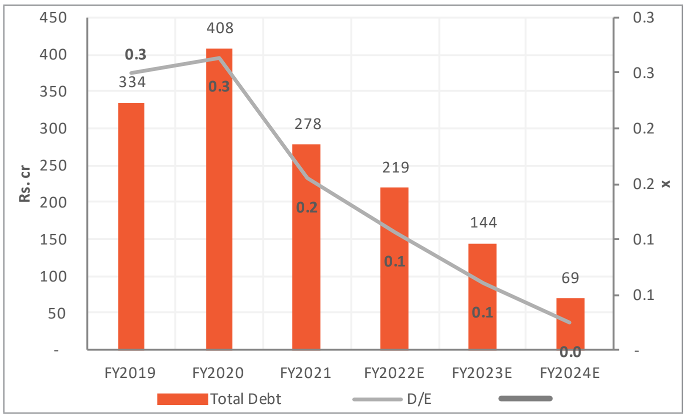

Source: Company, Sharekhan Research

### Consistent working capital cycle



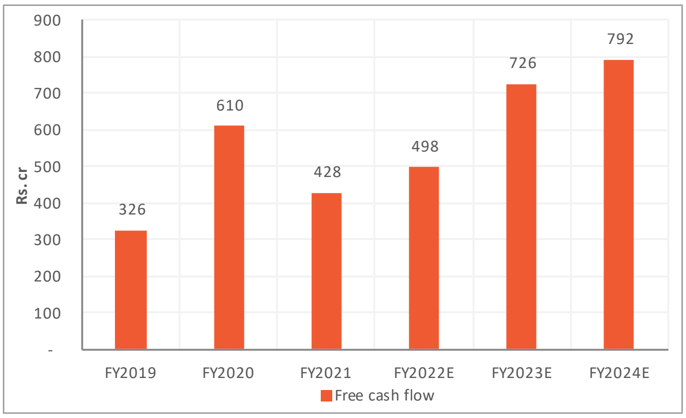

Source: Company, Sharekhan Research

### Debt position to improve




Source: Company, Sharekhan Research

### Significant free cash flow generation

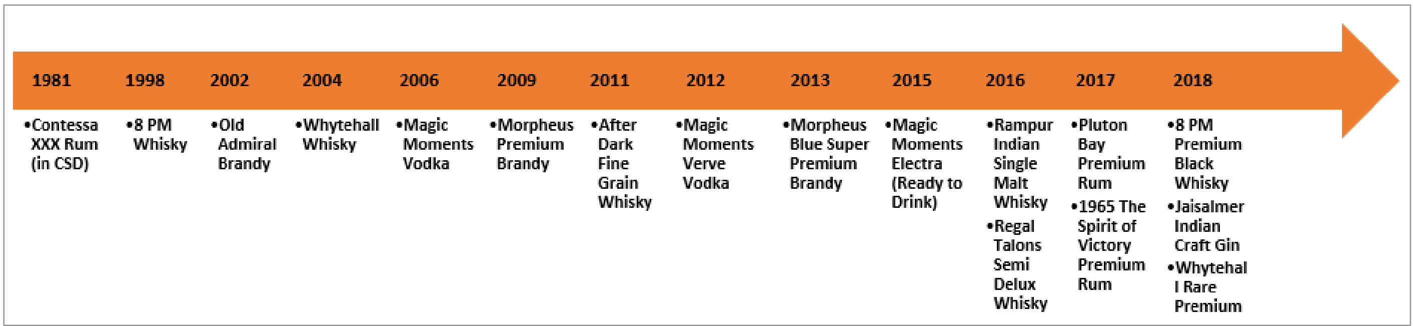



Source: Company, Sharekhan Research

## Company overview

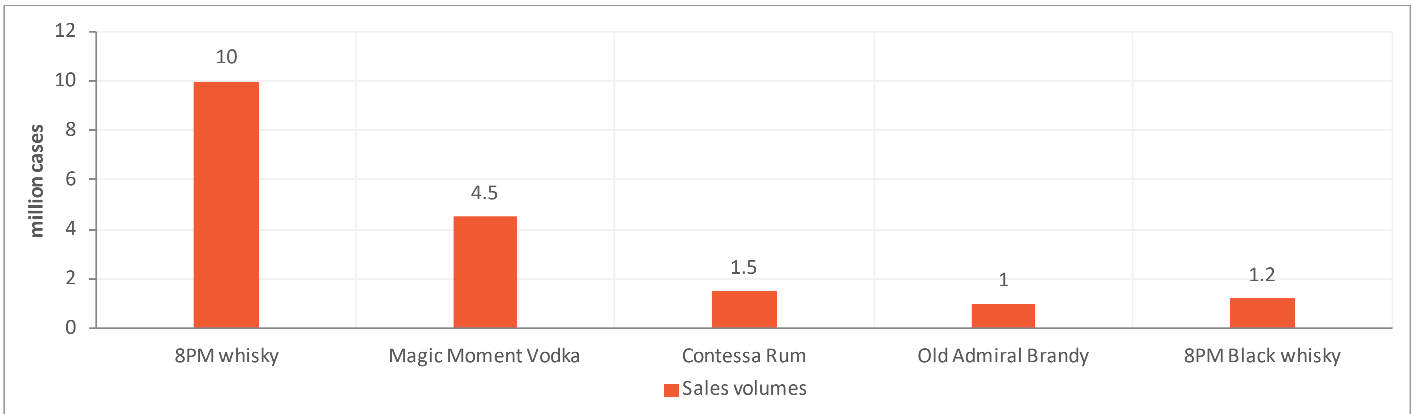
Radico Khaitan Limited (RKL), formerly known as Rampur Distillery, is one of the oldest and the largest manufacturers of IMFL in India. RKL commenced its operations in 1943 and over the years has evolved from being just a distiller of spirits for others to a leading IMFL company. In 1998, the company started its own label - after supplying bulk spirits and bottling services to other spirit manufacturers for over five decades - with the introduction of *8PM Whisky*. Over the years, RKL's focus on innovation, R&D strength and understanding of customer preferences has helped the company to develop its entire brand portfolio organically, with in-house capabilities. At present, the company's brand portfolio across the IMFL categories of Whiskey, Brandy, Rum and white spirits includes *Rampur Indian Single Malt Whisky, Magic Moments and Magic Moments Verve Vodka, Morpheus Premium and Morpheus Blue Brandy, 8 PM and 8 PM Premium Black Whisky, Contessa Rum, Old Admiral Brandy*, etc. Currently, the company has five millionaire brands, which are *8 PM Whisky, 8PM Premium Black Whisky, Contessa Rum, Old Admiral Brandy and Magic Moments Vodka*.

**Product launch timelines**




*Source: Company; Sharekhan research*

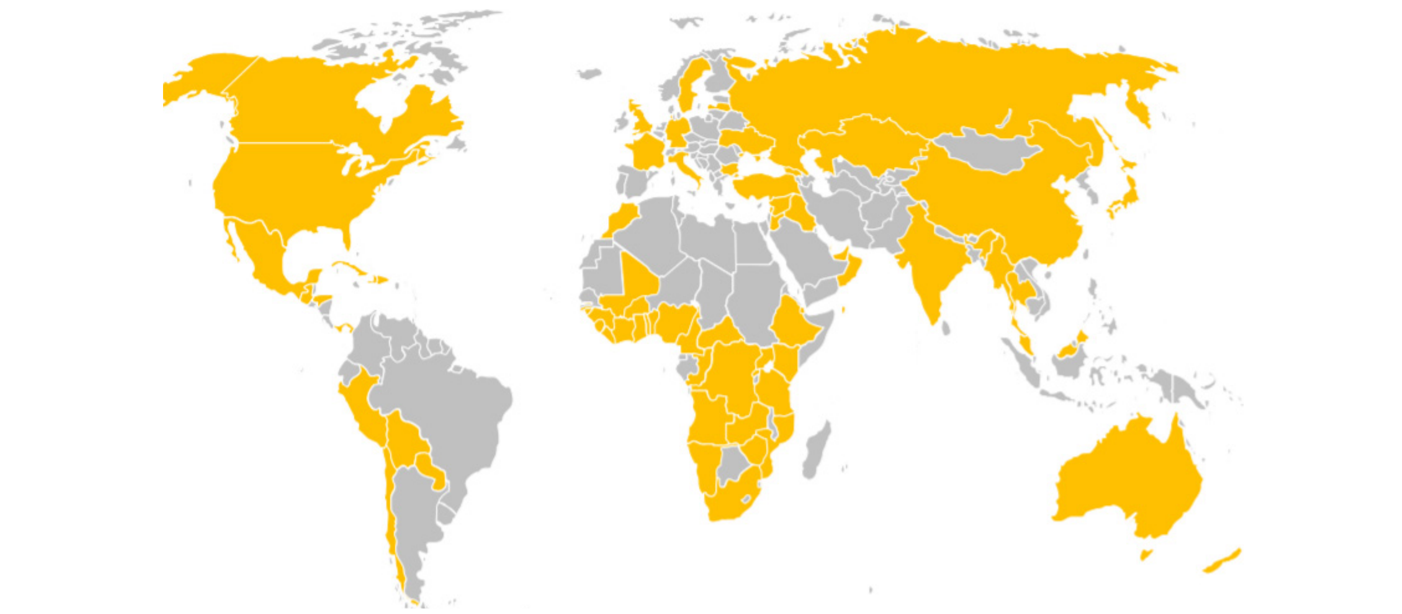
**5 brands entered Milloinare club**




*Source: Company; Sharekhan research*

RKL is also one of the largest providers of branded IMFL to the Canteen Stores Department (CSD). There are stringent conditions for entering into CSD segment leading to high entry barriers for new players. The company has been successfully building its brand equity in international markets and currently exports its products to more than 85 countries. The company has been able to establish a niche position for itself in the global spirits market. RKL's exports registered strong growth during FY2021 and contributed over 7% of the total net revenue from operations.

**Global presence**

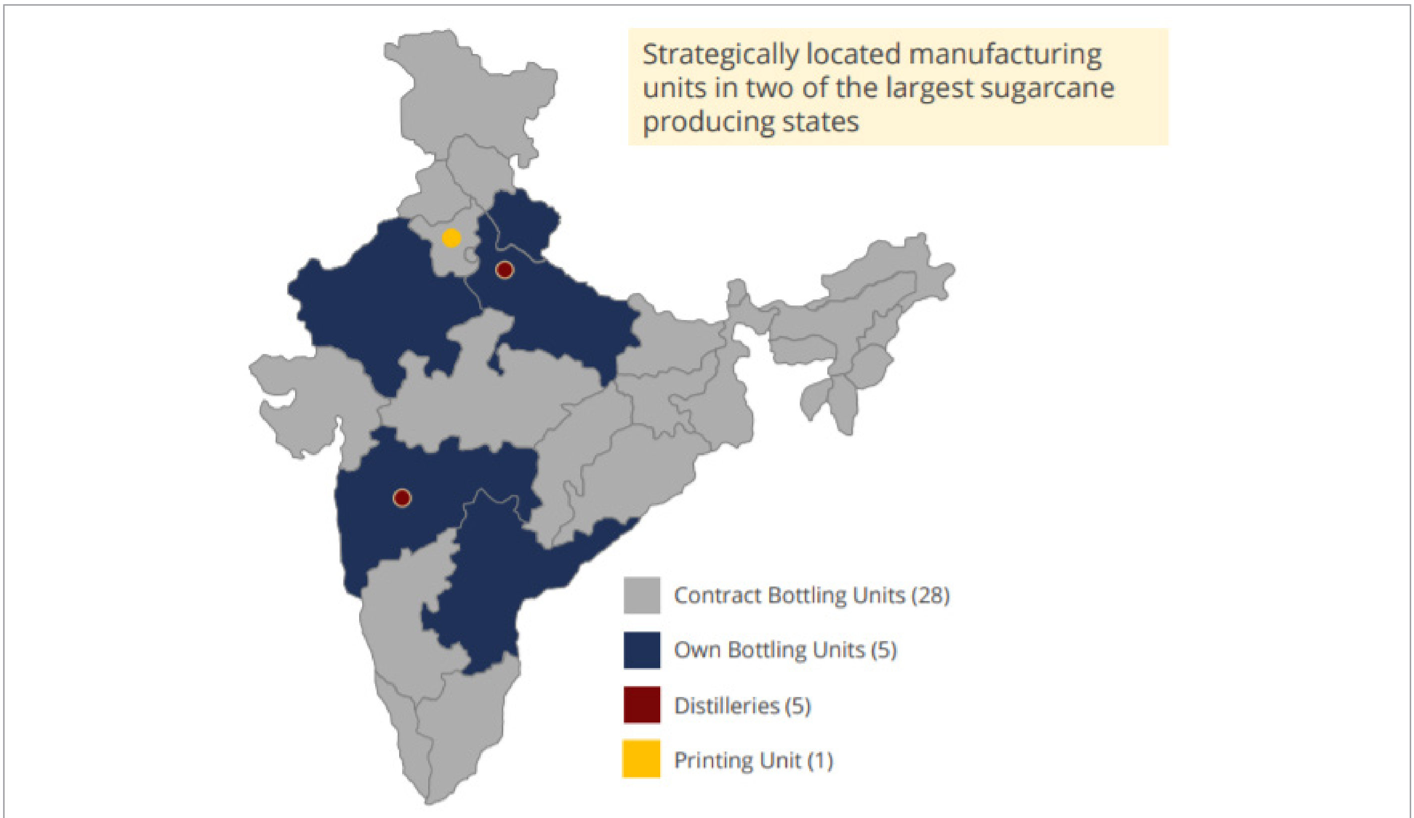


*Source: Company;*

### Pan India Manufacturing units and Significant Distillation Capacity

RKL has three distilleries in Rampur (Uttar Pradesh) and two in joint venture RNV in Aurangabad (Maharashtra) in which RKL owns a 36% equity. The company operates five owned and 28 contract bottling units spread across the country with a combined capacity of 160 million litres. Its strategically located manufacturing facilities and distribution centres at various locations provide easy access to key markets. Apart from a nationwide presence, strategic location also helps to avoid the high taxes levied on interstate movement of finished and in-process liquor.

**Distribution of manufacturing units**




*Source: Company;*

**Distilleries and their capacities**

| Location | Number of distilleries | Capacity (million litres) | | | |
|---|---|---|---|---|---|
| | | Molasses | Grain | Malt | Total |
| Rampur, UP | 3 | 75.0 | 27.0 | 7.5 | 109.5 |
| Aurangabad, Maharashtra | 2 | 40.0 | 15.0 | - | 55.0 |
| **Total** | **5** | **115.0** | **42.0** | **7.5** | **164.5** |

*Source: Company; Sharekhan Research*

## Strong distribution network

RKL has a strong sales and distribution network with a presence in retail and on-trade through more than 75,000 retail and 8,000 on-premise outlets in different parts of India. Apart from wholesalers, a total of ~300 employees divided into four zones, each headed by a regional profit centre head, ensure an adequate on-the-ground sales and distribution network across the country. The robust distribution system enables the company to ensure availability of products across channels and geographies.

**Senior management having thorough industry knowledge**

| Key executive | Position | Background |
|---|---|---|
| Dr. Lalit Khaitan | MD & Chairman | • Has over 50 years of industry experience<br>• He has been instrumental in improving quality standards and enhancing customer satisfaction<br>• He has been associated with a number of developmental projects, has represented India with several international delegations, and is involved in social & educational activities across India. |
| Abhishek Khaitan | MD | • Has over 25 years of industry experience<br>• He holds a Bachelor degree of Engineering from BMS college of Engineering, Bangalore and has completed a Managerial Finance & Accounting course from Harvard, USA.<br>• Started IMFL division and has played an instrumental role in the brand creation journey of the company |
| Amar Sinha | COO | • Has over 33 years of experience of heading reputable Indian and multinational FMCG companies and in the field of sales & marketing<br>• Prior to joining the company in April 2017, he was the Executive Director at Wave Industries |
| Dilip K Banthiya | CFO | • Has over 35 years of in corporate finance, treasury, international finance and corporate mergers and acquisitions<br>• Has been associated with various professional bodies and committees |
| K P Singh | Director – Production | • Has over 45 years of industry experience and has been with the company for over three decades |
| Sanjeev Banga | President – International business | • Has over 30 years of industry experience<br>• Joined the company in 2008, previously worked with Seagram India, Nestle India, Kohinoor Foods, Mason and Summers Alcobev, and Godfrey Phillips India |

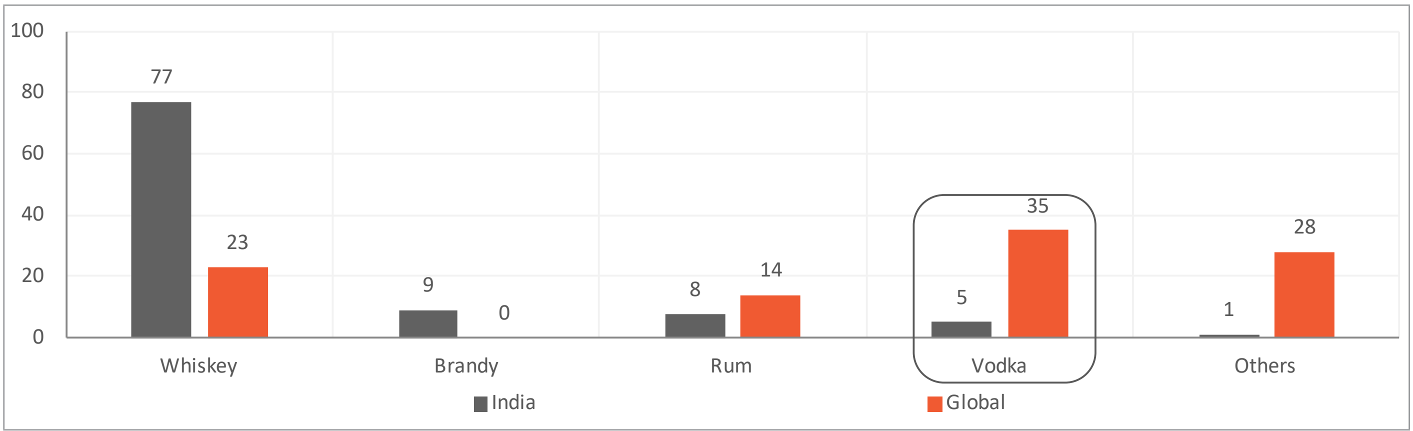
*Source: Company; Sharekhan Research*

**Leading through innovation & brand building**

**Vodka**

Market share for vodka in value terms in India is much lower than the global industry. This provides huge opportunity for growth in the vodka category.

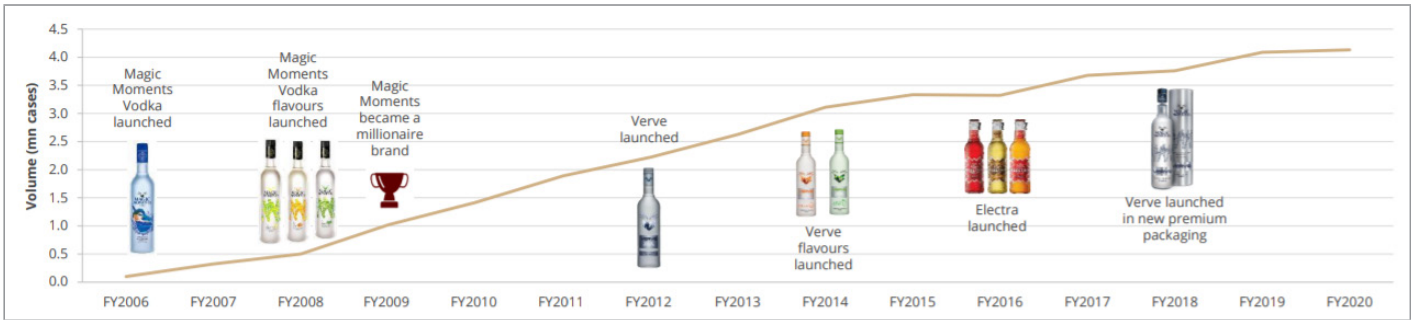
**Market share of various categories**




*Source: Company, Sharekhan Research*

RKL's Magic Moments family of vodka leads the Indian vodka industry with over 60% market share. Changing consumption patterns and consumer preference represent significant growth opportunity for already a market leader.

**Journey of building the Vodka portfolio**

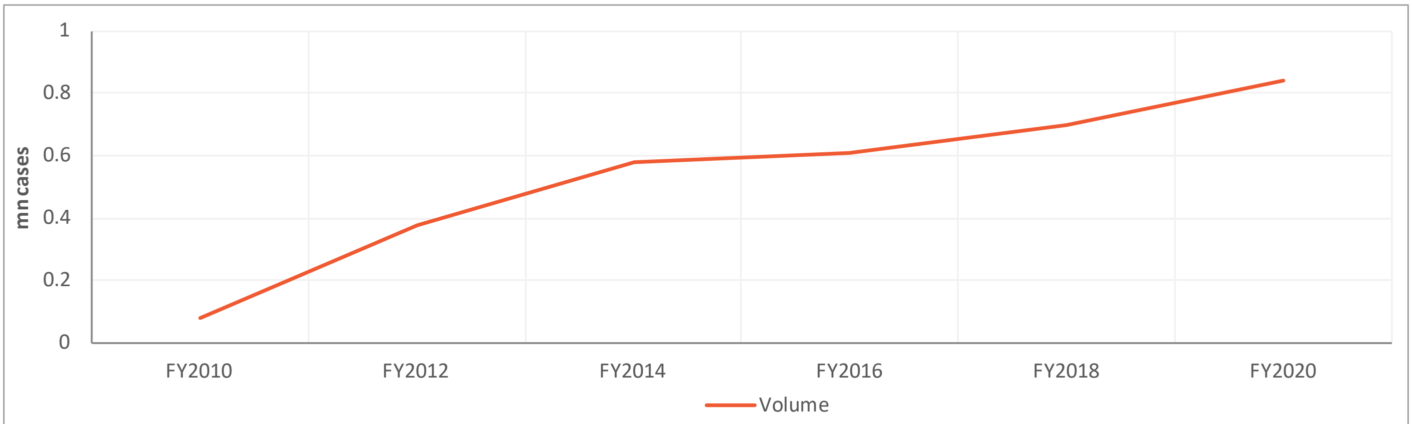



*Source: Company; Sharekhan Research*

**Brandy**

*Morpheus* is India's largest selling premium brandy and leads the super-premium brandy segment with 56% market share in India. Its goblet packaging and brand positioning have helped create a niche. After the success of *Morpheus*, the company launched *Morpheus Super Premium Brandy* in 2018.

**Growth in Morpheus volume**

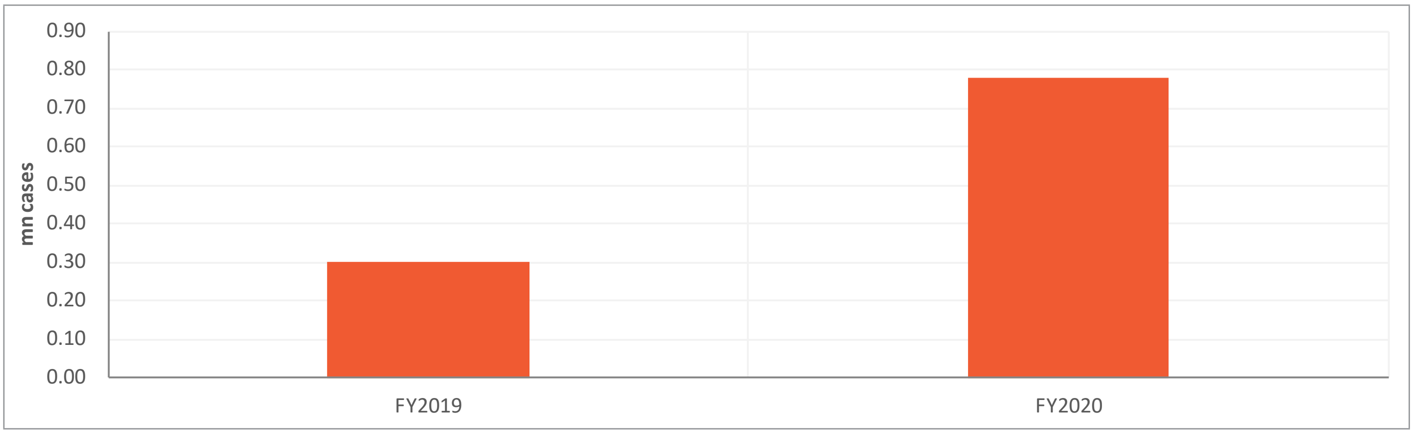



*Source: Company, Sharekhan Research*

### Whiskey

*8 PM Premium Black Whisky* has established its mark within a short span after its launch. Derived from the ancient Indian knowledge of herbs; retaining the classic gin flavour of juniper berries, a refreshing twist has been added with hand-picked Indian botanicals. Of the 11 botanicals used in the distillation, 7 have been sourced from all four corners of India.

**Volume growth of 8PM Premium Black Whisky**




*Source: Company, Sharekhan Research*

**Rewards & recognitions achieved**

| | | | | |
|---|---|---|---|---|
| The Millionaires' Club | 9th Largest whisky globally by volume | 11th Largest vodka globally by volume | 9th Largest rum globally by volume | 2nd Largest brandy globally by volume |
| The Spirits Business Brand Champions | 5th Best-selling Indian Whisky<br>Fastest growing Indian Whisky | 13th Best-selling vodka globally | 11th Best-selling rum globally | 1st Best-selling brandy globally |

*Source: Company; Sharekhan Research*

**ESG corner - steps towards sustainable future**

| Use of recycled glass bottles | Energy Consumption |
|---|---|
| Glass bottles are used on a large scale in RKL. The company's continuous efforts to increase consumption of recycled glass bottles has led to improvement in recycled glass bottle usage from 4.5% in FY2019 to 14.1% in FY2021 | In FY2021, out of the total power consumption at the Rampur plant, RKL generated 71% through captive power plants using renewable energy/ bio fuels. A significant portion of the power generation comes from biogas generated through waste produced during the alcohol manufacturing process – significantly reducing carbon footprint |
| **Water Consumption** | **Water recharging** |
| RKL has been continuously working to bring down the water consumption through technology upgrade throughout the manufacturing process. As a result, RKL's water consumption is one of the lowest in the Alcobev industry. Today both, the molasses and grain distilleries, use about 6.2-6.3 litres of water per bulk litres of alcohol production. This has come down by 48% in case of Molasses based distillery and 40% in case of Grain based distillery. | RKL has taken various steps for rainwater harvesting and ground level recharging. Currently, RKL is able to recharge ~300% of total water it draws from the ground, giving back more to the ecosystem. This has been achieved by installing 129 recharging structures across 38 villages in Chamraua Block of District Rampur. Consequently, the ground water level in Chamraua Block has improved by about 1 meter and reached a stable level. |
| **Tree Plantation** | |
| In FY2021, RKL undertook plantation of 10,000 trees at various locations in the Rampur district. | |

*Source: Company; Sharekhan Research*

## Valuation - Discounted valuation and strong growth prospects with improving cash flows makes it a good pick

***RKL currently trades at 30.9x/24.7x its FY2023/24 EPS, which is at ~50% discount to USL valuation. Improved quality of earnings, higher free cash generation and strong return profile will reduce valuation gap in the coming years.***

### ■ Sector outlook – Liberal state policies and changing consumer preference to drive growth

IMFL sales volumes in India witnessed a significant dip of 18% to 274 million cases due to COVID-19 induced lockdowns during the early part of the year. By Q4FY2021, eight out of eleven top liquor consuming states had returned to above pre-COVID levels. Demand for premium brands is relatively less impacted by the industry slowdown due to COVID-19. Consumers are having more disposable incomes which they can use to have quality experience at home. Therefore, premium brands are likely to show much more resilience and grow in the near future. India has an incredibly large young demography which presents many opportunities to firms in the industry. As the youth approach the legal drinking age and become more affluent, they are likely to drive much of the expected and projected future demand. Further, some of the key states are coming out with more liberal policies to drive its respective excise revenue, which will help brand players to scale up its revenues in those states.

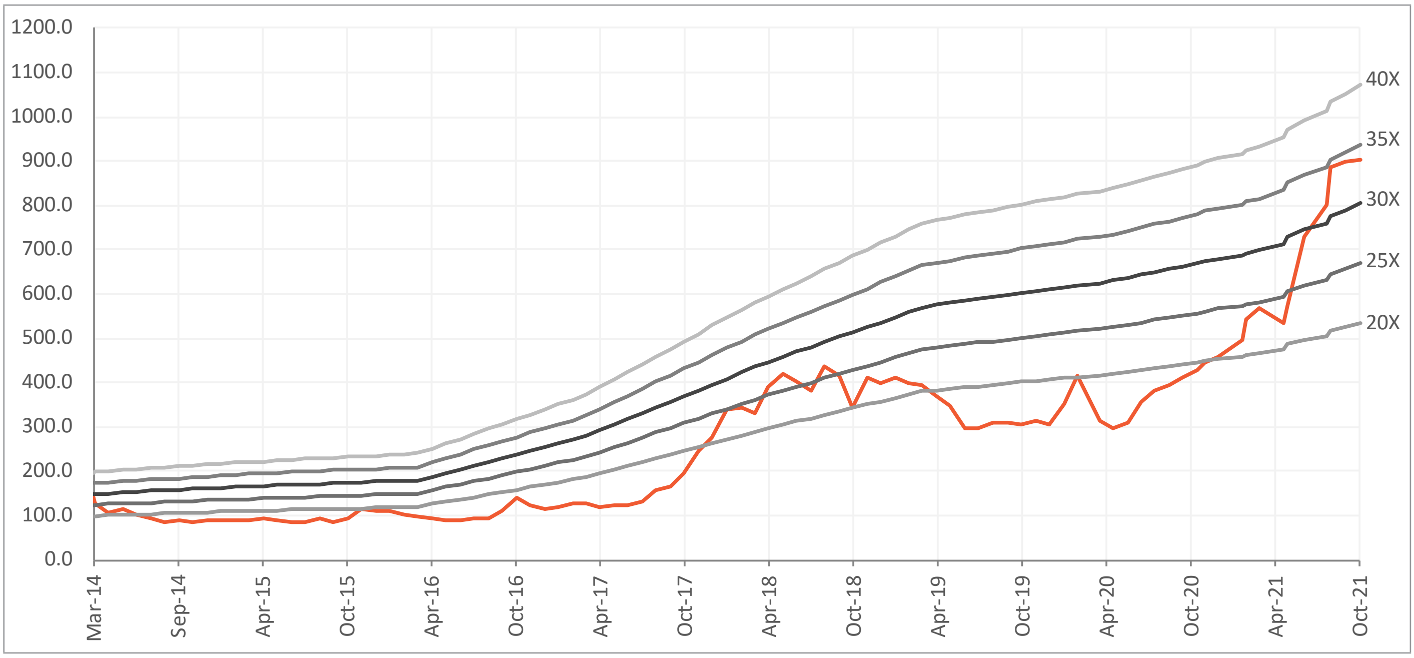
### ■ Company outlook – Premiumisation would lead to strong earnings growth

With consumers shifting to premium IMFL brands, RKL's focus on improving presence of each brand in key markets and emergence of favourable liquor policies in key states would help in faster growth branded liquor products in the near to medium term. Thus, we expect RKL's revenues to grow at CAGR of 17% over FY2021-24 to Rs. 3,875 crore. With contribution of P&A brands expected to go up to 34% by FY2024 (IMFL brand sales to reach 32mn cases), the OPM is expected to further improve to 19% by FY2024. RKL's operating profit is expected to grow at CAGR of 22% over FY2021-24.

### ■ Valuation – Initiate coverage with Buy assigning a price target of Rs. 1,250

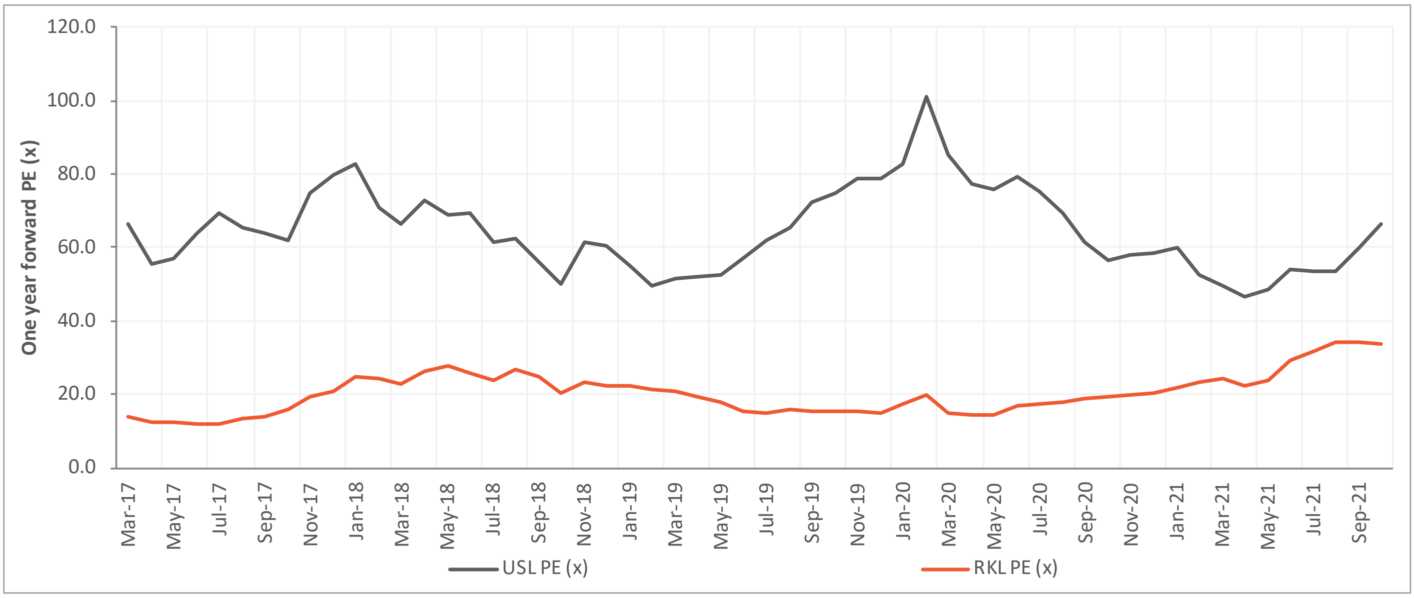
RKL will be one of the key beneficiaries of improving Indian demographics, consumer preference to premium brands and reviving liquor policies in various states. This along with deleverage balance sheet, the company is well-poised to achieve strong revenue and earnings CAGR of 17% and 22% over FY2021-24. The stock is trading at 30.9x/24.7x its FY2023/24E EPS, which is at ~50% discount to United Spirits Ltd (USL) valuations. Improved quality of earnings, higher free cash generation and a strong return profile will reduce valuation gap in the coming years. We initiate coverage on the stock with a Buy recommendation assigning price target of Rs. 1250 (valuing at 34x its FY2024E EPS).

**One-year forward P/E (x) band**



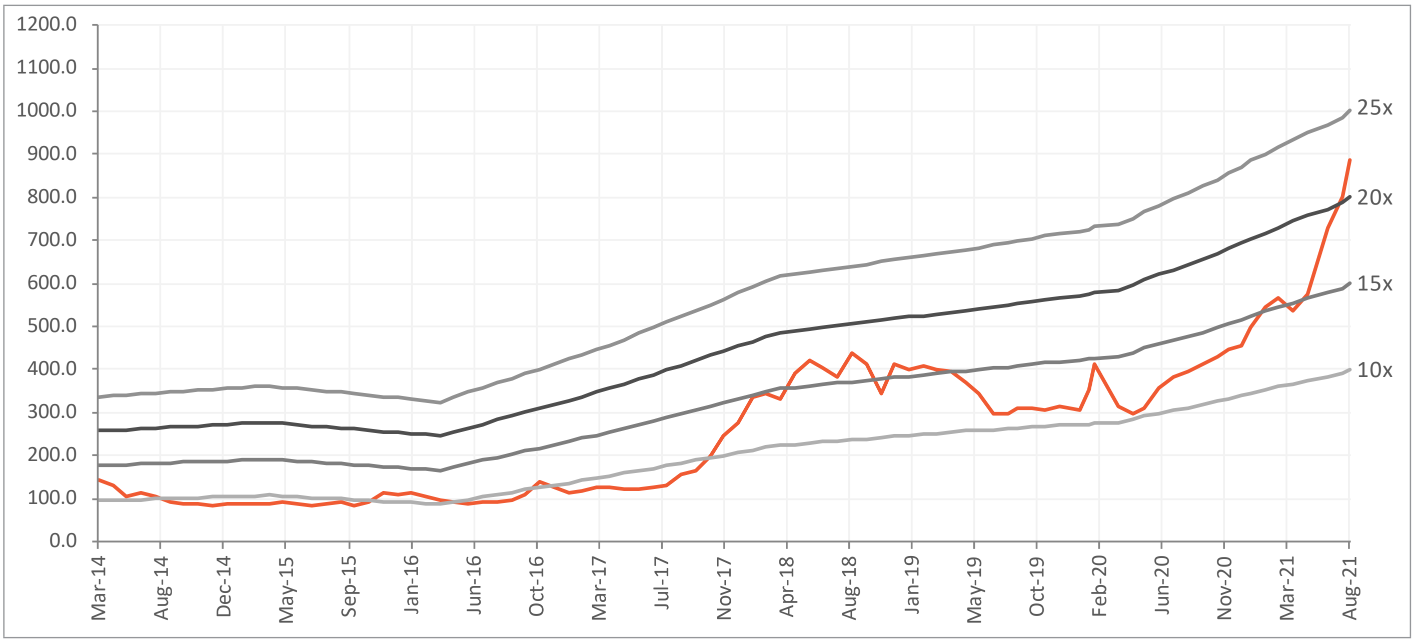

*Source: Sharekhan Research*

**Valuation GAP between USL and RKL to reduce**




*Source: Sharekhan Research*

**One-year forward EV/EBIDTA (x) band**




*Source: Sharekhan Research*

**Peer Comparison**

| Particulars | P/E (x) | | | EV/EBIDTA (x) | | | RoCE (%) | | |
|---|---|---|---|---|---|---|---|---|---|
| | FY21 | FY22E | FY23E | FY21 | FY22E | FY23E | FY21 | FY22E | FY23E |
| United Spirits | 137.9 | 79.5 | 60.4 | 65.5 | 48.0 | 38.4 | 16.8 | 22.1 | 24.8 |
| Globus Spirits | 29.3 | 20.3 | 15.2 | 16.5 | 12.1 | 9.3 | 26.8 | 31.6 | 32.9 |
| Radico Khaitan | 43.6 | 38.9 | 30.9 | 29.7 | 24.2 | 19.8 | 17.4 | 18.5 | 20.7 |

*Source: Consensus estimates; Sharekhan estimates*

## Financials (Consolidated)

**Statement of Profit and Loss** Rs cr

| Particulars | FY2020 | FY2021 | FY2022E | FY2023E | FY2024E |
|---|---|---|---|---|---|
| **Gross Sales** | **9,417.9** | **10,367.4** | **12,533.4** | **15,217.0** | **18,453.6** |
| Excise Duty | 6,990.9 | 7,949.2 | 9,650.7 | 11,869.2 | 14,578.4 |
| **Net Sales** | **2,427.0** | **2,418.1** | **2,882.7** | **3,347.7** | **3,875.3** |
| *y-o-y %* | *15.7* | *-0.4* | *19.2* | *16.1* | *15.8* |
| Raw Material Cost | 1,248.2 | 1,202.4 | 1,441.3 | 1,657.1 | 1,898.9 |
| Employee Cost | 186.1 | 176.3 | 197.5 | 227.1 | 261.2 |
| Other Expenses | 621.0 | 630.4 | 749.5 | 862.0 | 982.4 |
| **Total Operating Cost** | **2,055.2** | **2,009.2** | **2,388.3** | **2,746.3** | **3,142.4** |
| ***Operating Profit*** | ***371.8*** | ***408.9*** | ***494.3*** | ***601.4*** | ***732.8*** |
| *y-o-y %* | *6.1* | *10.0* | *20.9* | *21.7* | *21.8* |
| OPM % | 15.3 | 16.9 | 17.1 | 18.0 | 18.9 |
| Interest & Other Financial Cost | 31.6 | 22.0 | 16.2 | 11.8 | 6.9 |
| Depreciation | 52.5 | 53.9 | 57.9 | 60.7 | 63.4 |
| **Profit Before Tax** | **296.9** | **353.1** | **420.3** | **528.9** | **662.4** |
| *y-o-y %* | *3.9* | *18.9* | *19.0* | *25.9* | *25.2* |
| Tax Expense | 45.2 | 82.5 | 109.3 | 137.5 | 172.2 |
| **Adjusted PAT** | **251.7** | **270.6** | **311.0** | **391.4** | **490.2** |
| *y-o-y %* | *33.8* | *7.5* | *14.9* | *25.9* | *25.2* |
| NPM % | 10.4 | 11.2 | 10.8 | 11.7 | 12.6 |
| Minority Interest | 1.6 | 6.6 | 0.0 | 0.0 | 0.0 |
| Exceptional Items | -24.2 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Reported PAT** | **229.1** | **277.2** | **311.0** | **391.4** | **490.2** |
| *y-o-y %* | *18.0* | *21.0* | *12.2* | *25.9* | *25.2* |

*Source: Company; Sharekhan estimates*

**Balance Sheet** Rs cr

| Particulars | FY2020 | FY2021 | FY2022E | FY2023E | FY2024E |
|---|---|---|---|---|---|
| **Sources of Funds** | | | | | |
| Equity Capital | 26.7 | 26.7 | 26.7 | 26.7 | 26.7 |
| Reserves & Surplus | 1,516.2 | 1,766.2 | 2,037.1 | 2,361.8 | 2,751.8 |
| **Net Worth** | **1,542.9** | **1,792.9** | **2,063.8** | **2,388.5** | **2,778.5** |
| | | | | | |
| **Other liabilities** | | | | | |
| Deferred Tax Liabilities (Net) | 78.5 | 80.2 | 80.2 | 80.2 | 80.2 |
| Total Borrowings | 407.7 | 278.0 | 219.2 | 144.2 | 69.2 |
| **Capital Employed** | **2,029.1** | **2,151.2** | **2,363.3** | **2,612.9** | **2,928.0** |
| | | | | | |
| **Application of Funds** | | | | | |
| Net Block | 729.5 | 778.4 | 770.5 | 759.8 | 746.3 |
| Capital WIP | 18.1 | 37.8 | 20.0 | 50.0 | 50.0 |
| Goodwill on consolidation | 13.9 | 11.5 | 11.5 | 11.5 | 11.5 |
| Investment | 299.2 | 262.0 | 319.6 | 383.5 | 454.5 |
| | | | | | |
| **Current Assets** | **1,422.1** | **1,624.7** | **1,947.1** | **2,262.6** | **2,700.6** |
| Inventories | 374.2 | 489.1 | 533.3 | 646.2 | 784.1 |
| Sundry Debtors | 823.1 | 697.5 | 815.6 | 988.4 | 1,153.1 |
| Cash and Bank Balance | 10.1 | 121.1 | 202.9 | 173.0 | 238.9 |
| Fixed Deposits with Bank | 8.1 | 8.9 | 10.0 | 12.0 | 15.0 |
| Loans & Advances | 61.2 | 74.7 | 93.4 | 107.4 | 123.5 |
| Other Current Assets | 145.3 | 233.5 | 291.9 | 335.7 | 386.0 |
| | | | | | |
| **Less: Current Liab. & Provisions** | **453.7** | **563.2** | **705.3** | **854.5** | **1,035.0** |
| Trade Payables | 264.2 | 261.9 | 345.1 | 418.2 | 507.4 |
| Other Current Liabilities & Provisions | 189.5 | 301.3 | 360.3 | 436.3 | 527.6 |
| **Net Current Assets** | **968.4** | **1,061.5** | **1,241.7** | **1,408.1** | **1,665.6** |
| | | | | | |
| **Net Assets** | **2,029.1** | **2,151.2** | **2,363.3** | **2,612.9** | **2,928.0** |

*Source: Company; Sharekhan estimates*

**Cash Flow Statement** Rs cr

| Particulars | FY2020 | FY2021 | FY2022E | FY2023E | FY2024E |
|---|---|---|---|---|---|
| Cash flow from operating activities | 84.5 | 343.0 | 271.6 | 257.8 | 365.1 |
| Cash flow from investing activities | -86.0 | -83.5 | -91.0 | -145.9 | -124.0 |
| Cash flow from financing activities | 3.4 | -148.5 | -98.9 | -141.8 | -175.2 |
| **Net change in cash and cash equivalents** | **1.9** | **111.0** | **81.8** | **-29.9** | **65.9** |
| Opening cash balance | 8.3 | 10.1 | 121.1 | 202.9 | 173.0 |
| **Closing cash balance** | **10.1** | **121.1** | **202.9** | **173.0** | **238.9** |
| **Free cash flows** | **610.1** | **428.4** | **498.4** | **726.4** | **792.2** |

*Source: Company; Sharekhan estimates*

**Key Ratios**

| Particulars | FY2020 | FY2021 | FY2022E | FY2023E | FY2024E |
|---|---|---|---|---|---|
| **Margins & tax rates (%)** | | | | | |
| GPM | 48.6 | 50.3 | 50.0 | 50.5 | 51.0 |
| OPM | 15.3 | 16.9 | 17.1 | 18.0 | 18.9 |
| NPM | 10.4 | 11.2 | 10.8 | 11.7 | 12.6 |
| Tax rate | 15.2 | 23.4 | 26.0 | 26.0 | 26.0 |
| | | | | | |
| **Cost matrix (% of revenues)** | | | | | |
| Raw material cost | 51.4 | 49.7 | 50.0 | 49.5 | 49.0 |
| Employee Cost | 7.7 | 7.3 | 6.9 | 6.8 | 6.7 |
| Other Expenses | 25.6 | 26.1 | 26.0 | 25.8 | 25.4 |
| Total Operating Cost | 84.7 | 83.1 | 82.9 | 82.0 | 81.1 |
| | | | | | |
| **Growth ratios (y-o-y %)** | | | | | |
| Revenue | 15.7 | -0.4 | 19.2 | 16.1 | 15.8 |
| Operating profit | 6.1 | 10.0 | 20.9 | 21.7 | 21.8 |
| PBT | 3.9 | 18.9 | 19.0 | 25.9 | 25.2 |
| Adjusted PAT | 33.8 | 7.5 | 14.9 | 25.9 | 25.2 |
| Reported PAT | 18.0 | 21.0 | 12.2 | 25.9 | 25.2 |
| | | | | | |
| **Per share (Rs.)** | | | | | |
| CMP | 905.0 | 905.0 | 905.0 | 905.0 | 905.0 |
| Adjusted EPS | 19.0 | 20.8 | 23.3 | 29.3 | 36.7 |
| Cash EPS | 22.8 | 24.3 | 27.6 | 33.8 | 41.5 |
| Book value (BVPS) | 115.5 | 134.2 | 154.5 | 178.8 | 208.0 |
| DPS | 2.0 | 2.4 | 3.0 | 5.0 | 7.5 |
| | | | | | |
| **Valuation ratios (x)** | | | | | |
| P/E | 47.7 | 43.6 | 38.9 | 30.9 | 24.7 |
| Price / Book value (BV) | 7.8 | 6.7 | 5.9 | 5.1 | 4.4 |
| EV / EBIDTA | 33.2 | 29.7 | 24.3 | 19.8 | 16.1 |
| EV / Sales | 5.1 | 5.0 | 4.2 | 3.6 | 3.0 |
| Market cap / Sales | 5.0 | 5.0 | 4.2 | 3.6 | 3.1 |
| | | | | | |
| **Working capital (Days)** | | | | | |
| Inventory | 15.6 | 18.0 | 17.0 | 17.0 | 17.0 |
| Debtors | 34.4 | 25.7 | 26.0 | 26.0 | 25.0 |
| Creditors | 11.0 | 9.7 | 11.0 | 11.0 | 11.0 |
| Operating cash cycle | 39.0 | 34.1 | 32.0 | 32.0 | 31.0 |
| | | | | | |
| **Financial ratios** | | | | | |
| Fixed asset turnover ratio (x) | 3.3 | 3.0 | 3.5 | 4.1 | 4.8 |
| Total asset turnover ratio (x) | 1.0 | 0.9 | 1.0 | 1.0 | 1.0 |
| Operating cash flow/EBIDTA (%) | 22.7 | 83.9 | 54.9 | 42.9 | 49.8 |
| Dividend Payout Ratio (%) | 12.7 | 11.6 | 12.9 | 17.1 | 20.4 |
| Debt / Equity (x) | 0.3 | 0.2 | 0.1 | 0.1 | 0.0 |
| RoE (%) | 16.3 | 15.1 | 15.1 | 16.4 | 17.6 |
| RoCE (%) | 16.2 | 17.4 | 18.5 | 20.7 | 22.9 |

*Source: Company; Sharekhan estimates*

## About company

Radico Khaitan Limited (RKL), formerly known as Rampur Distillery, commenced its operations in 1943 and over the years has evolved from being just a distiller of spirits for others to a leading IMFL company. The company's brand portfolio spans Whiskey, Brandy, Rum and white spirits include *Rampur Indian Single Malt Whisky, Magic Moments and Magic Moments Verve Vodka, Morpheus Premium and Morpheus Blue Brandy, 8 PM and 8 PM Premium Black Whisky, Contessa Rum, Old Admiral Brandy*, among others. Currently, the company has five millionaire brands which are 8 PM Whisky, 8PM Premium Black Whisky, Contessa Rum, Old Admiral Brandy and Magic Moments Vodka. RKL has three distilleries in Rampur (Uttar Pradesh) and two in joint venture RNV in Aurangabad (Maharashtra) in which RKL owns 36% equity. The company operates 5 own and 28 contract bottling units spread across the country with a combined capacity of 160 million litres. RKL is one of the largest providers of branded IMFL to the Canteen Stores Department (CSD) and also exports its products to more than 85 countries.

## Investment Argument

RKL has transformed itself into a leading IMFL brand player from just a distillery player with premiumisation at core of its growth strategy. Its prestige and above brands grew at CAGR of 16% over FY2017-21 contributing to 30% to sales volume IMFL (50% to sales value) helping operating margins to improve by 430 bps to 17% in FY2021. Increased preference for premium products aided, the company to post double digit volume ahead of industry growth over FY2017-20. Efficient working capital management and improved profitability would help, the company to generate high free cash flows in the coming years. With no major capex on books higher cash generated will be utilised for developing more premium brands and higher pay-outs to shareholders. We expect RoE/RoCE of the company to improve to 17.4%/22.6% from 15.1%/17.4% in FY2021.

## Key Risks

- **Decline in demand for the company's products:** The slowdown in global economic growth and other declines or disruptions in the Indian economy in general may result in a reduction in disposable income of consumers and slowdown in the IMFL industry. This could adversely affect the company's business and financial performance.
- **Risk due to stringent regulation norms:** The Indian spirit industry is highly regulated and complex as each state has its own regulations governing the manufacture and sale of spirits. Any change in rules and regulations by the respective state governments and noncompliance with laws and regulations could adversely impact the business.
- **Increase in raw material prices:** ENA and packaging materials are the two key components of the raw materials. Any price volatility in the price of these components may have a bearing on the company's profitability.

## Additional Data

**Key management personnel**

| | |
|---|---|
| Dr. Lalit Khaitan | MD & Chairman |
| Abhishek Khaitan | MD |
| Amar Sinha | COO |
| Dilip K Banthiya | CFO |
| Dinesh Kumar Gupta | Company Secretary |

*Source: Company Website*

**Top 10 shareholders**

| Sr. No. | Holder Name | Holding (%) |
|---|---|---|
| 1 | TIMF Holdings | 5.82 |
| 2 | HDFC Asset Management Co Ltd | 3.26 |
| 3 | Nippon Life India Asset Management Ltd | 3.23 |
| 4 | Aditya Birla Sun Life Asset Management Co Ltd | 2.90 |
| 5 | Tata Asset Management Ltd | 2.83 |
| 6 | DSP Investment Managers Pvt Ltd | 1.90 |
| 7 | Vanguard Group Inc | 1.86 |
| 8 | Massachusetts Institute of Technology | 1.70 |
| 9 | IDFC Sterling Pvt | 1.59 |
| 10 | IDFC Mutual Fund | 1.58 |

*Source: Bloomberg*

## Understanding the Sharekhan 3R Matrix

| | |
|---|---|
| **Right Sector** | |
| Positive | Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies |
| Neutral | Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies |
| Negative | Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability. |
| **Right Quality** | |
| Positive | Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance. |
| Neutral | Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable |
| Negative | Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet |
| **Right Valuation** | |
| Positive | Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment. |
| Neutral | Trading at par to historical valuations and having limited scope of expansion in valuation multiples. |
| Negative | Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple. |

*Source: Sharekhan Research*

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