

Rating matrix	
Rating	: Hold
Target	: ₹ 160
Target Period	: 12-15 months
Potential Upside	: -9%

What's changed?	
Target	Changed from ₹ 168 to ₹ 160
EPS FY18E	Changed from ₹ 5.1 to ₹ 9.0
EPS FY19E	Changed from ₹ 8.4 to ₹ 8.8
Rating	Unchanged

Quarterly performance					
	Q1FY18	Q1FY17	YoY (%)	Q4FY17	QoQ (%)
Sales	193.4	178.9	8.1	376.9	-48.7
EBITDA	10.3	-14.8	-169.7	-217.9	NA
EBITDA (%)	5.3	NA	NA	NA	NA
PAT	-1.7	-17.3	NA	-107.8	NA

Key financials				
₹ Crore	FY16	FY17	FY18E	FY19E
Net Sales	1,900.1	1,776.4	2,038.2	2,167.5
EBITDA	168.9	110.4	174.0	153.1
Net Profit	27.7	64.5	74.3	72.4
EPS (₹)	3.4	7.8	9.0	8.8

Valuation summary				
	FY16	FY17	FY18E	FY19E
P/E (Adj.)	51.9	22.4	19.4	19.9
Target P/E	47.5	20.4	17.7	18.2
Div. Yield	1.7	0.1	-	-
Mcap/Sales	1.0	1.1	0.9	0.9
EV/EBITDA	15.0	24.1	14.4	16.0
RoNW (%)	1.4	3.3	3.6	3.4
RoCE (%)	5.3	6.2	7.1	6.6

Stock data	
Particular	Amount
Market Capitalization (₹ Crore)	1,914.9
Total Debt (FY17) (₹ Crore)	841.1
Cash (FY17) (₹ Crore)	50.7
EV (₹ Crore)	2,705.4
52 week H/L	198 / 137
Equity capital	₹ 41.2 Crore
Face value	₹ 5

Price performance				
	1M	3M	6M	12M
McLeod Russel	-1.7	-6.3	4.7	-8.9
Jayshree Tea	-6.8	-9.1	-11.3	-9.4
Goodricke Tea	-3.1	-10.7	-8.3	41.9

Research Analyst	
Sanjay Manyal	sanjay.manyal@icicisecurities.com
Tejashwini Kumari	tejashwini.kumari@icicisecurities.com

McLeod Russel (MCLRUS)

₹ 175

Weak operational performance to continue...

- McLeod Russel was able to restrict its losses for the quarter on account of higher production and sales volume. Revenue for the quarter grew 8.1% YoY to ₹ 193.4 crore (I-direct estimate ₹ 167.7 crore) primarily on account of 11% growth in volumes to 11.1 lakh kg
- However, the blended price continued to remain under pressure and declined 1.6% YoY to ₹ 168.4/kg. Domestic prices continued to remain under pressure and were largely flat YoY. Conversely, prices at Mombassa auctions jumped ~20% YoY to US\$2.8/kg as production in Kenya declined (down by 50 mn kg YTD)
- Production at 241 lakh kg was up 9.5% YoY (primarily due to growth in own leaf production). Employee cost continued to increase for the quarter on account of wage revision and was up 13.9% YoY. Led by higher production, EBITDA came in at ₹ 10.3 crore against EBITDA loss of ₹ 14.8 crore in the same quarter last year against our estimate of EBITDA loss of ₹ 15.9 crore
- Revenue growth & positive EBITDA helped the company curb the loss at ₹ 1.7 crore for quarter against loss of ₹ 17.3 crore in Q1FY17

Lower domestic realisation & increasing employee cost to restrict growth

So far in the current fiscal, domestic tea prices are under pressure and have remained lower YoY. However, domestic production is estimated to be higher by 19 mkg to ~1220-1230 mkg in CY17 primarily led by higher production in southern India. We are factoring in a marginal improvement of 3.5% and 6.3% in domestic realisation for FY18E and FY19E at ₹ 160/kg and ₹ 170/kg, respectively. We believe that with better export environment, MRL would focus on improving exports. Hence, we consider 4.4% decline in domestic sales volume for FY18E & marginal growth of 1.1% for FY19E. Thus, we estimate domestic revenue will see muted CAGR of 3.0% in FY17-19E. Additionally, increasing employee cost due to wage revision (expected at start of CY19E) would continue to put pressure on the company's performance (employee cost to increase 9.7% and 9.6% YoY in FY18E & FY19E, respectively). Thus, EBITDA margin is expected at 8.5% and 7.1% for FY18E and FY19E, respectively.

Export revenue to improve on low base, improving international price

Globally, CY16 witnessed record tea production led by increased production in both Kenya and India. However, since the start of CY17, weather conditions are getting adverse. Hence, Kenya's tea production is already down by 50 mkg in H1CY17. This decline in production has positively impacted the Mombassa auction prices, which have increased ~20% YoY (in Q1FY17) to US\$2.8/kg. With a favourable production scenario, we estimate exports for the company would grow significantly on a low base. We estimate export realisation at ₹ 230/kg and ₹ 235/kg for FY18E and FY19E, respectively. Thus, export revenue is expected to clock 30.0% CAGR in FY17-19E.

Employee cost to restrict profitability; maintain HOLD

We estimate revenue for the company will grow at a CAGR of 10.2% in FY17-19E on a low base formed in FY17. However, increasing employee cost would restrict significant improvement in operating margin and expect it at 7.1% for FY19E. We maintain our cautious view on the stock in the absence of any operational improvement. We reiterate our **HOLD** recommendation on the stock with a revised target price of ₹ 160.

Variance analysis

	Q1FY18	Q1FY18E	Q1FY17	YoY (%)	Q4FY17	QoQ (%)	Comments
Net Sales	193.4	167.7	178.9	8.1	376.9	-48.7	Net sales grew on account of volume growth of ~11% but price remained under pressure and declined 1.6% YoY
Raw Material Expenses	-165.0	-126.4	-117.2	NA	328.2	-150.3	Due to higher production of 9.5% YoY to 241 lakh kgs
Employee Expenses	213.7	187.9	187.7	13.9	183.2	16.6	On account of wage revision, the employee cost was up by 13.9%
Other operating Expenses	134.4	122.1	123.3	9.0	83.5	61.0	
EBITDA	10.3	-15.9	-14.8	-169.7	-217.9	NA	EBITDA remained flat on account of higher raw material cost
EBITDA Margin (%)	5.3	NA	NA	NA	NA	NA	
Depreciation	20.6	25.1	20.1	2.2	20.8	-1.0	
Interest	30.1	28.9	23.6	27.8	39.4	-23.6	
Other Income	38.1	33.1	33.4	14.0	108.8	-65.0	
PBT	-2.2	-36.8	-25.0	-91.1	-169.2	NA	
Tax Outgo	-0.6	0.0	-7.7	NA	-61.4	NA	
PAT	-1.7	-36.8	-17.3	NA	-107.8	NA	Sales and EBITDA decline resulted in profit decline for the quarter
Key Metrics (%)							
Tea sales volumes growth (%)	11.0		2.0		5.0		
Tea realisation increase (%)	-1.6		0.6		6.6		

Source: Company, ICICIdirect.com Research

Change in estimates

₹ Crore)	FY18E			FY19E			Comments
	Old	New	% Change	Old	New	% Change	
Sales	1,976.9	2038.2	3.1	2151.8	2167.5	0.7	Revised export estimates upwards, leading to revenue growth
EBITDA	133.5	174.0	30.4	149.2	153.1	2.6	EBITDA for FY18E getting revised significantly upwards due to higher exports and improved realisation estimates
EBITDA Margin (%)	6.8	8.5	179 bps	6.9	7.1	13 bps	
PAT	41.9	74.3	77.5	69.3	72.4	4.5	
EPS (₹)	5.1	9.0	77.5	8.4	8.8	4.5	Led by higher EBITDA estimates

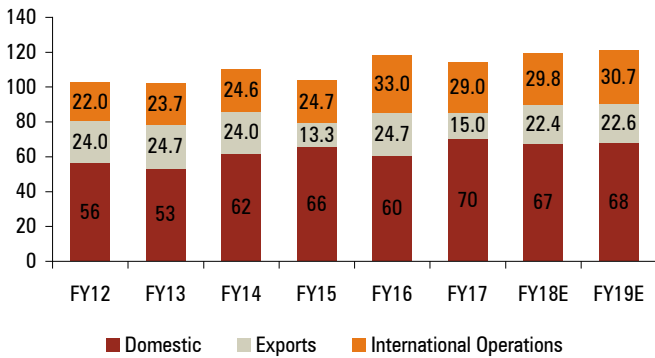
Source: Company, ICICIdirect.com Research

Assumptions

	Current				Earlier		
	FY16	FY17E	FY18E	FY19E	FY18E	FY19E	
Sales volume (in mkg)	85.2	85.2	89.5	90.4	89.5	93.9	Tweaked the volume estimate for FY19E
Domestic	60.5	70.2	67.1	67.8	69.8	70.4	
Exports	24.7	15.0	22.4	22.6	19.7	23.5	Revised export estimates upwards on favorable export environment
Africa + Vietnam (in mkg)	33.0	29.0	29.8	30.7	29.8	30.7	
Overall Realization (₹/kg)	174.1	163.5	177.5	186.3	174.3	181.3	
Domestic	160.6	154.5	160.0	170.0	160.0	165.0	
Exports	198.5	210.0	230.0	235.0	225.0	230.0	Revised export realisation upwards as Kenya tea production declines
Bought leaf Prod (mkg)	27.5	30.0	30.0	30.0	30.0	30.0	
Employee cost (₹ per kg)	63.5	73.6	77.2	83.4	77.2	80.3	

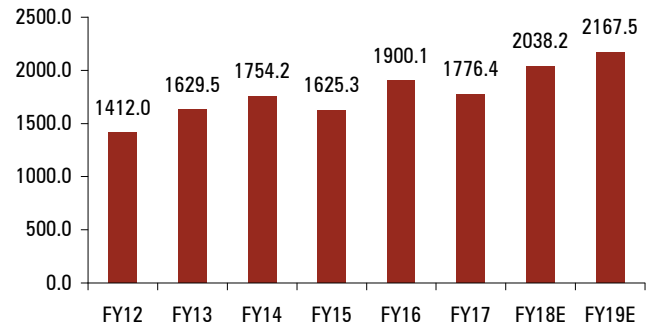
Source: Company, ICICIdirect.com Research

Exhibit 1: MRL's sales volume (million kg)



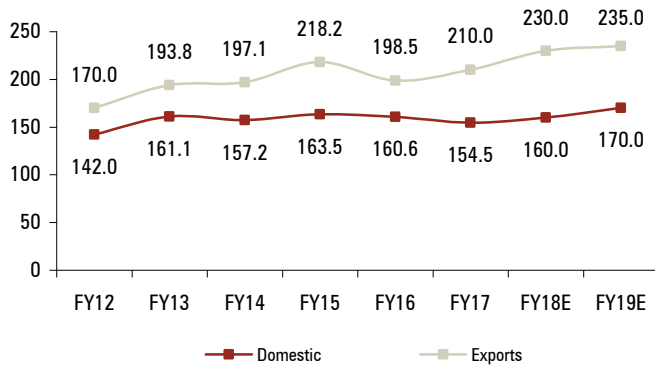
Source: Company, ICICIdirect.com, Research

Exhibit 2: Revenue to be driven by volumes (₹ crore)



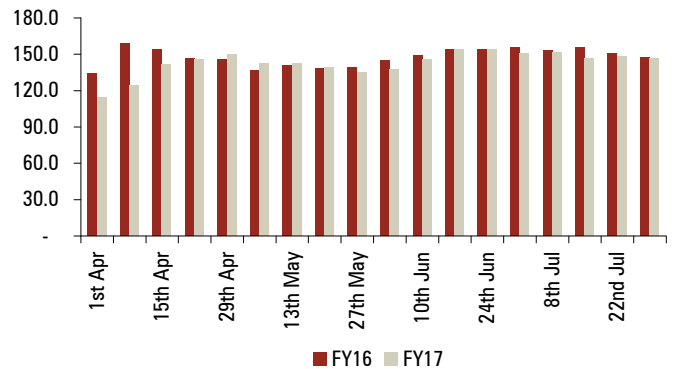
Source: Company, ICICIdirect.com, Research

Exhibit 3: Company realisation to witness marginal improvement (₹/kg)



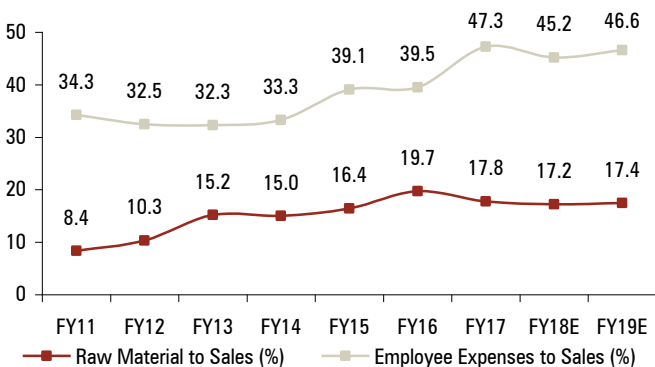
Source: Company, ICICIdirect.com, Research

Exhibit 4: Domestic tea prices remain under pressure (₹/kg)



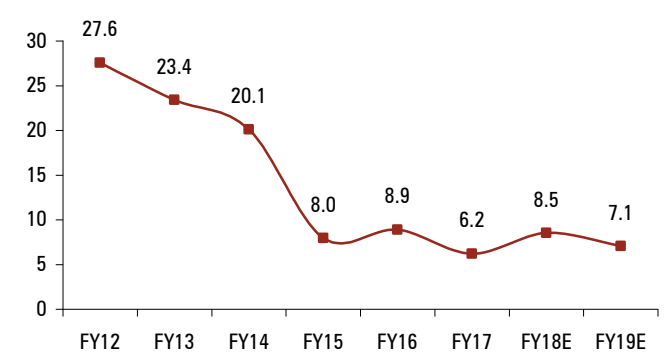
Source: Tea board of India, ICICIdirect.com, Research

Exhibit 5: Employee cost to remain elevated



Source: Company, ICICIdirect.com, Research

Exhibit 6: EBITDA margin to remain capped (%)



Source: Company, ICICIdirect.com, Research

Outlook & Valuation

McLeod Russel is the country's largest tea producer with domestic production of ~85 million kg (FY17) and production from Vietnam & Africa at ~29 million kg (FY17). Due to unavailability of further land to increase crop production, the only way to increase sales volume in tea industry is through acquisitions, re-plantation and processing of bought green leaves. MRL is actively undertaking all the above measures to increase its sales volume and has, thereby, increased it from ~75 mkg in FY08 to ~85 mkg in FY17. The increase in sales volume has been led by both domestic and international acquisitions (Africa & Vietnam). As per BSE filing, the company is also looking at an opportunity to form a JV with Eveready for developing 'packet tea business' through a separate entity. This JV, if finalised, will give MRL an entry into a ₹ 10,000 crore packet tea market.

Given the crop loss of 6.3 million kg in FY15, lower export volumes & subdued performance of African business, earnings saw a fall from ₹ 257.2 crore in FY14 to ₹ 31.2 crore in FY15. The performance in FY16 & FY17 worsened for MRL as failure in tea volumes' recovery, high employee wages & high interest cost resulted in EBIT loss of ₹ 42.4 crore and ₹ 129.0 crore, respectively. Kenyan tea production had recovered significantly in CY16 on account of improved weather conditions to ~473 mkg (up 73 mkg YoY) putting pressure on the Mombassa auction prices. However, at the start of CY17, weather conditions are getting adverse. Production is expected to decline to 417 mkg for the year. On the other hand, overall domestic production is estimated to higher by 19mkg to ~1220-1230 mkg in CY17.

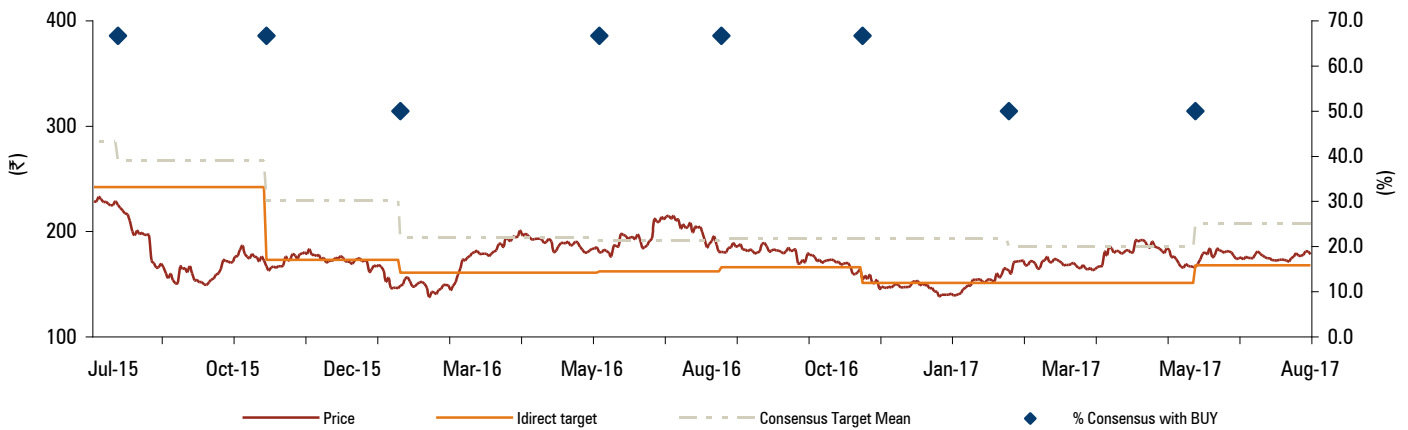
On a low base of FY17 and recovery in exports on account of favourable dynamics, we estimate the revenue for the company will grow at a CAGR of 10.2% in FY17-19E on a low base formed in FY17. However, increasing employee cost (increase of 9.7% YoY in FY18E and 9.6% YoY in FY19E) would restrict any significant improvement in operating margin, and expect it at 7.1% for FY19E. We estimate profit of ₹ 74.3 crore and ₹ 72.4 crore for, FY18E & FY19E, respectively. We maintain our cautious view on the stock in the absence of any operational improvement. We reiterate our **HOLD** recommendation on the stock with a revised target price of ₹ 160 valuing the stock at 18x FY19E EPS of ₹ 8.8.

Exhibit 7: Valuations

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY16	1900.1	16.9	3.4	18.3	51.9	15.0	1.4	5.3
FY17	1776.4	-6.5	7.8	132.3	22.4	24.1	3.3	6.2
FY18E	2038.2	14.7	9.0	15.3	19.4	14.4	3.6	7.1
FY19E	2167.5	6.3	8.8	-2.6	19.9	16.0	3.4	6.6

Source: Company, ICICIdirect.com Research

Recommendation history vs. Consensus



Source: Bloomberg, Company, ICICIdirect.com Research

Key events

Date	Event
Aug-09	Government of Rwanda approves sale of 60% shares of Gisovu Tea Co to Borelli Tea Holdings, UK, a wholly owned subsidiary of MRIL
Dec-09	Borelli Tea Holdings Ltd, UK, wholly-owned subsidiary of MRIL signs a share purchase agreement with James Finlay Ltd and James Finlay International Holdings Ltd (both of UK) for acquisition of 100% of share capital of Rwenzori Tea Investments Ltd, Uganda for a provisional consideration of \$25 million (James Finlay has six tea estates with annual production around 15 mkg of black tea)
Feb-11	India's tea production drops 1.3% to the lowest in five years on account of damaged crops due to pest attacks in Assam and West Bengal
Jan-12	Tea production in India climbs 2.3% and exports fall 3% resulting in stable domestic tea prices and moderate increase in MRIL's realisation
Apr-13	Export realisation of McLeod Russel witnesses a steep increase by 14% mainly due to sharp currency depreciation in FY13
May-13	MRIL sets up a company in Kenya called McLeod Russel Africa Ltd to engage in tea trading activities in Africa
Dec-13	Kenya reports highest production in 10 years resulting in a drop in global prices and limiting the increase in Indian tea prices, thereby limiting MRIL's realisations
Mar-14	Purchases a tea processing factory in Vietnam with annual production capacity of 6 lakh kg of green tea for a consideration of \$820,000
Jul-14	Acquires a tea processing factory in Vietnam with an annual production capacity of 1.2 mkg for \$2.09 million (~₹ 13 crore)
Nov-14	Acquires Pfunda Tea Co. Ltd., Rwanda's biggest private tea plantation for \$19.5 million making McLeod Russel account for 25% of Rwanda's tea production

Source: Company, ICICIdirect.com Research

Top 10 Shareholders

Rank	Shareholder	Holdings (m)	%	Change (m)
9	M & G Investment Management Ltd. [Activist]	42825	0.0195	2.133437
10	Baheti (Kamal)	31-Mar-17	24.73	27.1
11	Williamson Magor Group	31-Mar-17	16.04	17.6
12	Edgbaston Investment Partners LLP	31-Mar-17	6.16	6.7
13	ICICI Prudential Asset Management Co. Ltd.	30-Jun-17	5.68	6.2
14	IDFC Asset Management Company Private Limited	31-Mar-17	4.59	5.0
15	Woodside Parks, Ltd.	31-Mar-17	4.12	4.5
16	Bishnauth Investments, Ltd.	31-Mar-17	3.63	4.0
17	M & G Investment Management Ltd. [Activist]	31-Mar-17	1.95	2.1
18	Dimensional Fund Advisors, L.P.	30-Jun-17	1.80	2.0
19	Kotak Mahindra Asset Management Company Ltd.	31-Mar-17	1.28	1.4

Source: Reuters, ICICIdirect.com Research

Shareholding Pattern

(in %)	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17
Promoter	49.9	49.9	49.9	49.9	49.9
FII	19.6	18.9	19.5	18.3	17.4
DII	16.9	18.0	16.0	14.5	16.9
Others	13.6	13.3	14.6	17.3	15.9

Recent Activity

Top Investors (As of Latest Filing)			Top Investors (As of Latest Filing)			
Investor Rank	Investor Name	Filing Date	Position	Change	Turnover	
1	Sundaram Asset Management Company Limited	3.8m	1.47m	APG Asset Management	-5.49m	-2.14m
2	Lakshmi Capital Investment Ltd.	3.55m	1.39m	L&T Investment Management Limited	-0.89m	-0.38m
3	Kotak Mahindra Asset Management Company Ltd.	2.16m	0.84m	Reliance Nippon Life Asset Management Limited	-0.33m	-0.13m
4	M & G Investment Management Ltd.	0.36m	0.14m	JM Financial Asset Management Pvt. Ltd.	-0.09m	-0.04m
5	IDFC Asset Management Company Private Limited	0.36m	0.14m	Principal PNB Asset Management Company Ltd.	-0.05m	-0.02m

Source: Reuters, ICICIdirect.com Research

Financial summary

Profit and loss statement		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Total operating Income	1926.3	1870.8	2137.3	2271.6	
Growth (%)	17.0	-2.9	14.2	6.3	
Raw Material Expenses	374.7	315.6	351.0	378.0	
Power & Fuel Expenses	216.1	208.0	234.4	249.3	
Employee Expenses	750.6	839.8	921.4	1,010.0	
Marketing Expenses	102.1	94.7	106.0	114.9	
Other expenses	314.0	302.4	350.6	366.3	
Total Operating Expenditure	1,757.4	1,760.4	1,963.3	2,118.5	
EBITDA	168.9	110.4	174.0	153.1	
Growth (%)	16.1	-34.6	57.6	-12.0	
Depreciation	102.2	103.5	100.5	101.0	
Interest	109.1	135.9	121.0	106.3	
Other Income	91.4	183.5	140.4	144.6	
PBT	49.0	54.5	92.9	90.5	
Others	0.0	0.0	0.0	0.0	
Total Tax	14.0	-9.9	18.6	18.1	
PAT	35.0	64.5	74.3	72.4	
Growth (%)	2.9	83.9	15.3	-2.6	
EPS (₹)	3.4	7.8	9.0	8.8	

Source: Company, ICICIdirect.com Research

Balance sheet		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Equity Capital	41.2	41.2	41.2	41.2	
Reserve and Surplus	1908.8	1917.6	2015.0	2087.3	
Minority Share	18.2	22.2	22.2	22.2	
Non-Current Liability					
Long Term Borrowings	325.4	226.4	236.4	246.4	
Deferred Tax Liabilities (Net)	219.9	185.1	185.1	185.1	
Long term Provisions	30.7	53.1	53.1	53.1	
Current Liabilities					
Short term Borrowings	424.3	614.8	464.8	364.8	
Trade Payable	136.0	116.6	139.6	142.5	
Other current Liabilities	273.8	271.5	307.1	296.9	
Short term provisions	11.4	3.5	119.1	119.1	
Total Liabilities	3,389.5	3,451.9	3,583.5	3,558.6	
Fixed Assets	2260.6	2228.5	2238.5	2248.5	
Tangible Assets	1820.3	1820.3	1830.3	1840.3	
Intangible Assets	343.9	317.0	317.0	317.0	
Capital WIP	96.4	91.2	91.2	91.2	
Intangible assets UD	0.0	0.0	0.0	0.0	
Non current assets	78.1	72.3	72.3	72.3	
Long term Loans and Advances	0.1	0.1	0.2	0.2	
Other non-currents assets	83.2	47.6	47.6	47.6	
Current Assets	967.5	1103.5	1225.1	1190.1	
Inventory	250.1	237.2	273.6	267.2	
Trade Receivable	127.3	108.9	111.7	118.8	
Cash & Bank	46.1	50.7	58.0	32.1	
Short-term Loans & Liability	323.7	419.8	474.7	475.1	
Other current assets	220.4	286.9	307.1	296.9	
Application of Funds	3,389.5	3,451.9	3,583.5	3,558.6	

Source: Company, ICICIdirect.com Research

Cash flow statement		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Profit before Tax	49.0	54.5	92.9	90.5	
Add: Depreciation	82.2	103.5	100.5	101.0	
(Inc)/dec in Current Assets	-1.7	-131.4	-114.3	9.1	
Inc/(dec) in CL and Provisions	43.7	160.9	24.3	-107.3	
Others	-0.2	-20.8	-18.6	-18.1	
CF from operating activities	173.1	166.8	84.8	75.1	
(Inc)/dec in Investments	0.0	0.0	0.0	0.0	
(Inc)/dec in Fixed Assets	-127.2	79.4	-10.0	-10.0	
Others	-146.1	-103.5	-100.5	-101.0	
CF from investing activities	-273.3	-24.2	-110.5	-111.0	
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0	
Inc/(dec) in loan funds	227.6	-99.0	10.0	10.0	
Dividend paid & dividend tax	-32.7	-2.4	0.0	0.0	
Inc/(dec) in Sec. premium	-105.7	0.0	0.0	0.0	
Others	0.0	0.0	0.0	0.0	
CF from financing activities	89.2	-101.4	10.0	10.0	
Net Cash flow	-10.9	41.2	-15.7	-25.9	
Opening Cash	43.4	32.5	73.7	58.0	
Closing Cash	46.1	50.7	58.0	32.1	

Source: Company, ICICIdirect.com Research

Key ratios					
(Year-end March)	FY16	FY17	FY18E	FY19E	
Per share data (₹)					
EPS	3.4	7.8	9.0	8.8	
Cash EPS	15.8	20.4	21.2	21.0	
BV	236.7	237.8	249.6	258.4	
DPS	3.1	0.3	0.0	0.0	
Cash Per Share	5.6	6.1	7.0	3.9	
Operating Ratios (%)					
EBITDA Margin	8.9	6.2	8.5	7.1	
PBT / Total Operating income	2.6	3.1	4.6	4.2	
PAT Margin	1.8	3.6	3.6	3.3	
Inventory days	48.0	48.7	49.0	45.0	
Debtor days	24.5	22.4	20.0	20.0	
Creditor days	26.1	24.0	25.0	24.0	
Return Ratios (%)					
RoE	1.4	3.3	3.6	3.4	
RoCE	5.3	6.2	7.1	6.6	
RoIC	2.4	0.2	2.6	1.8	
Valuation Ratios (x)					
P/E	51.9	22.4	19.4	19.9	
EV / EBITDA	15.0	24.1	14.4	16.0	
EV / Net Sales	1.3	1.5	1.2	1.1	
Market Cap / Sales	1.0	1.1	0.9	0.9	
Price to Book Value	0.7	0.7	0.7	0.7	
Solvency Ratios					
Debt/EBITDA	4.4	7.6	4.0	4.0	
Debt / Equity	0.4	0.4	0.3	0.3	
Current Ratio	2.2	2.7	2.1	2.1	
Quick Ratio	1.6	2.1	1.6	1.6	

Source: Company, ICICIdirect.com Research

RATING RATIONALE

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

Strong Buy: > 15%/20% for large caps/midcaps, respectively, with high conviction;

Buy: > 10%/15% for large caps/midcaps, respectively;

Hold: Up to +/-10%;

Sell: -10% or more;



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

**ICICIdirect.com Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com**

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