VENKY’S INDIA LTD

PRICE: Rs.4575
TARGET PRICE: Rs.3700
RECOMMENDATION: SELL
FY20E PE: 24.6x

Venky’s stock has now run up 216% since we initiated coverage (July, 2017) on the stock. In the last three months, the stock has appreciated 85%, as strong earnings performance in recent quarters has led to better perception among investors, aiding a re-rating. In our last update (March, 2018), we had noted signs of weakening poultry prices. Over the last month, decline in poultry prices has been sharper (more than 20% decline y/y), which is likely to affect near-term performance of the stock negatively. Moreover, industry sources indicate that there may be an excess supply in the poultry market (supply has risen faster than anticipated demand growth), which could affect medium-term earnings. We lower our (poultry) pricing assumptions, leading to a cut in gross margins/earnings. With FY19E/20E earnings estimates 15%/16% lower, we cut our price target to Rs 3700 (Rs 4600 earlier). Downgrade to SELL as we think there is a high likelihood of significantly lower entry points in the stock (for longer-term play).

Broiler/ chick prices under pressure, signs of oversupply

We had noted in our earlier report (March, 2018), that poultry prices growth had turned negative. While the navratri in the period has had an impact on prices, we also gather from industry sources that the supply of chicken may be rising faster than demand, indicating that it may be general oversupply that has begun to impact prices negatively. Venky’s revenues/earnings have benefited in the past few quarters, due to a re-adjustment in poultry supply that was affected in the weaker years of the industry (FY14-FY15). Recent price trends, as well as industry sources indicate that the industry has not been able to contain supply at low levels. This could have implications for medium/long-term; in the immediate term, 4QFY18/1QFY19 results are likely to be less exciting than what investors have seen over the past few quarters. We expect 7.5% EBITDA growth in 4QFY18 (PAT growth is likely to be strong, helped by lower interest expenses/ lower effective tax rate).

Forecast of normal monsoon a positive, reduce uncertainty related with raw material prices

While data on broiler prices over the past one month has been incrementally negative, news on monsoon is a positive. Venky’s has been enjoying the benefits of relatively low raw material prices over the past year, and a weak monsoon could have an impact on soya/ corn prices, which are primary raw materials for the company. Forecast by Skyment indicates that India is likely to witness a normal monsoon in 2018. Therefore, raw material prices should be expected to register only moderate growth over the coming quarters.

Cut estimates on lower pricing growth expectations, cut price target to Rs 3700, downgrade to SELL

Given that data/industry sources indicate that there may be a case of at least a temporary oversupply (implying that y/y prices growth is negative) in the industry, our prior pricing assumptions may be high; we reduce our pricing growth expectation by 3%. We note that if there is indeed a case of significant oversupply, our 5% pricing growth assumption may prove too high – while we wait for confirmation and persistence of this trend, we find it prudent to cut pricing growth expectation from 8% to 5%. Our FY19/FY20 earnings estimates are cut by 15%/16% as a result. We also cut our target multiple to 20X (21X FY20 earlier), on lower growth expectations and higher uncertainty on
earnings. Given the weakness in poultry prices over the past six weeks, the run-up in the stock over the past month has likely been excessive, and takes for granted a significant rise in poultry prices. We believe there is a high likelihood of a significant decline in Venky’s stock over the next year. We downgrade the stock to **SELL**, with a price target of Rs 3700.

**Risks to our investment view/earnings estimates**

(1) Venky’s earnings estimates are significantly dependent on broiler/day-old chick prices, and our assumption of lower pricing growth may be incorrect. There may be upside/downside risks to our earnings estimates/investment view on Venky’s. We would be watching poultry prices carefully. (2) the company is likely to benefit, over the longer term, from a shift to frozen chicken – how early the market shall begin to discount the same determines the re-rating that Venky’s stock may see. There may be downside risks to our investment view from such developments.

We recommend SELL on Venky’s India Ltd with a price target of Rs.3700
**RATING SCALE**

**Definitions of ratings**

BUY – We expect the stock to deliver more than 12% returns over the next 12 months

ACCUMULATE – We expect the stock to deliver 5% - 12% returns over the next 12 months

REDUCE – We expect the stock to deliver 0% - 5% returns over the next 12 months

SELL – We expect the stock to deliver negative returns over the next 12 months

NR – Not Rated. Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.

RS – Rating Suspended. Kotak Securities has suspended the investment rating and price target for this stock, either because there is not a sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.

NA – Not Available or Not Applicable. The information is not available for display or is not applicable

NM – Not Meaningful. The information is not meaningful and is therefore excluded.

NOTE – Our target prices are with a 9-month perspective. Returns stated in the rating scale are our internal benchmark.

---

**FUNDAMENTAL RESEARCH TEAM**

Sanjeev Zarbade  
Capital Goods, Engineering  
sanjeev.zarbade@kotak.com  
+91 22 6218 6424

Ruchir Khare  
Capital Goods, Engineering  
ruchir.khare@kotak.com  
+91 22 6218 6431

Amit Agarwal  
Logistics, Paints, Transportation  
agarwal.amit@kotak.com  
+91 22 6218 6439

Nipun Gupta  
Information Technology  
nipun.gupta@kotak.com  
+91 22 6218 6433

Teena Virmani  
Construction, Cement, Building Mat  
teea.virmani@kotak.com  
+91 22 6218 6432

Ritwik Rai  
FMCG, Media  
ritwik.rai@kotak.com  
+91 22 6218 6426

Jatin Damania  
Metals & Mining  
jatin.damania@kotak.com  
+91 22 6218 6440

Jayesh Kumar  
Economy  
kumar.jayesh@kotak.com  
+91 22 6218 5373

Arun Agarwal  
Auto & Auto Ancillary  
arun.agarwal@kotak.com  
+91 22 6218 6443

Sumit Pokharna  
Oil and Gas  
sumit.pokharna@kotak.com  
+91 22 6218 6438

Pankaj Kumar  
Midcap  
pankaj.kumar@kotak.com  
+91 22 6218 6434

K. Kathirvelu  
Production  
k.kathirvelu@kotak.com  
+91 22 6218 6427

---

**TECHNICAL RESEARCH TEAM**

Shrikant Chouhan  
91 22 6218 5408

Amol Athawale  
amol.athawale@kotak.com  
+91 20 6620 3350

---

**DERIVATIVES RESEARCH TEAM**

Sahaj Agrawal  
sahaj.agrawal@kotak.com  
+91 79 6607 2231

Malay Gandhi  
malay.gandhi@kotak.com  
+91 22 6218 6420

Prashanth Lalu  
prashanth.lalu@kotak.com  
+91 22 6218 5497

Prasenjit Biswas, CMT, CFte  
prasenjit.biswas@kotak.com  
+91 33 6625 9810
Disclosure/Disclaimer
Kotak Securities Limited established in 1994, is a subsidiary of Kotak Mahindra Bank Limited. Kotak Securities is one of India’s largest brokerage and distribution houses. Kotak Securities Limited is a corporate trading and clearing member of Bombay Stock Exchange Limited (BSE), National Stock Exchange of India Limited (NSE), Metropolitan Stock Exchange of India Limited (MSE). Our businesses include stock broking, services rendered in connection with distribution of primary market issues and financial products like mutual funds, AMC, PMS, Portfolio Managements.
Kotak Securities Limited is also a depository participant with National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited (CDSL). Kotak Securities Limited is also registered with Insurance Regulatory and Development Authority as Corporate Agent for Kotak Mahindra Old Mutual Life Insurance Limited and is also a Mutual Fund Advisor registered with Association of Mutual Funds in India (AMFI). We are registered as a Research Analyst under SEBI (Research Analyst) Regulations, 2014.
We hereby declare that our activities were neither suspended nor we have defaulted with any stock exchange authority with whom we are registered in last five years. However SEBI, Exchanges and Depositories have conducted the routine inspection and based on their observations have advised/warned/deficiency letters or levied minor penalty on KSL for certain operational deviations. We have not been debarred from doing business by any Stock Exchange / SEBI or any other authorities, nor has our certificate of registration been canceled by SEBI at any point of time.
We offer our research services to clients as well as our prospects. This document is not for public distribution and has been furnished to you solely for your information and must not be reproduced or redistributed to any other person. Persons into whose possession this document may come are required to observe these restrictions.
This material is for the personal information of the authorized recipient, and we are not directing any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. It is for the general information of clients of Kotak Securities Ltd. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients.
We have reviewed the report, and in so far as it includes current or historical information, it is believed to be reliable though its accuracy or completeness cannot be guaranteed. Neither Kotak Securities Limited, nor any person connected with it, accepts any liability arising from the use of this document. The recipients of this material should rely on their own investigations and take their own professional advice. Price and value of the investments referred to in this material may go up or down. Past performance is not a guide for future performance. Certain transactions - including those involving futures, options and other derivatives as well as non-investment grade securities - involve substantial risk and are not suitable for all investors. Reports based on technical analysis centers on studying charts of a stock’s price movement and trading volume, as opposed to focusing on a company’s fundamentals and as such, may not match with a report on a company’s fundamentals.
Opinions expressed are our current opinions as of the date appearing on this material only. We make no endeavor to update on a reasonable basis the information discussed in this material, or to comply with any obligations that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.
Kotak Securities Limited has two independent equity research groups: Institutional Equities and Private Client Group. This report has been prepared by the Private Client Group.
The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, target price of the Institutional Equities Research Group of Kotak Securities Limited.
We and our affiliates/associates, officers, directors, and employees, Research Analysts(including relatives) worldwide may: (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the subject company/company (ies) discussed herein or act as advisor or lender / borrower to such company (ies) or have other potential/material conflict of interest with respect to any recommendation and related information and opinions at the time of publication of Research Report or at the time of public appearance. Kotak Securities Limited (KSL) may have proprietary long/short position in the above mentioned scrips or other raison d'etre and therefore may be considered as interested. The views provided herein are general in nature and does not consider risk appetite or investment objective of particular investor; readers are requested to take independent professional advice before investing. This should not be construed as invitation or solicitation to do business with KSL. Kotak Securities Limited is also a Portfolio Manager. Portfolio Management Team (PMS) takes its investment decisions independent of the PCG research and accordingly PMS may have positions contrary to the PCG research recommendation. Kotak Securities Limited does not provide any promise or assurance of favourable view for a particular industry or sector or business group in any manner. The investor is requested to take into consideration all the risk factors including their financial condition, suitability to risk return profile and take professional advice before investing.
This report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report.
Details of Associates are available on our website ie www.kotak.com Research Analyst has served as an officer, director or employee of subject company(ies): No
We or our associates may have received compensation from the subject company(ies) in the past 12 months. No
We or our associates have managed or co-managed public offering of securities for the subject company(ies) in the past 12 months: No
We or our associates may have received compensation for investment banking or merchant banking or brokerage services from the subject company(ies) in the past 12 months: No
We or our associates may have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company(ies) in the past 12 months: No
We or our associates may have positions contrary to the PCG research and accordingly PMS may have positions contrary to the PCG research recommendation. Kotak Securities Limited does not provide any promise or assurance of favourable view for a particular industry or sector or business group in any manner.
If you still have not received a satisfactory response at Level 2 within 3 working days, you may contact our Compliance Officer (Mr. Manoj Agarwal ) at ks.compliance@kotak.com.
In case you require any clarification or have any concerns, kindly write to us at below email ids:
- Level 1: For Trading related queries, contact our customer service at 'service@kotak.com' and for demat related account queries contact us at ks.demat@kotak.com or 022-24285830
- Level 2: If you do not receive a satisfactory response at Level 1 within 3 working days, you may write to us at ksescalation@kotak.com or call us on 022-24285845 and if you feel you are still unheard, write to our customer service HOD at ks.servicehead@kotak.com or call us on 022-24285828
- Level 3: If you still have not received a satisfactory response at Level 2 within 3 working days, you may contact our Compliance Officer (Mr. Manoj Agarwal ) at ks.compliance@kotak.com or call us on 91- (022) 2428 8300.
- Level 4: If you have not received a satisfactory response at Level 3 within 7 working days, you may also approach CEO (Mr. Kamlesh Rao) at ceo@kotak.com or call us on 91- (022) 2428 8300.