Zydus Wellness (ZYDWEL)

CMP: ₹ 1918 | Target: ₹ 2500 (30%) | Target Period: 12 months | BUY

February 3, 2021

Healthy growth across product portfolio

Zydus wellness (ZWL) posted strong Q3FY21 results with 15.6% growth in net sales led by double digit growth in Sugarfree & healthy growth across segments (except Nutralite). With the increased health awareness, Sugarfree has been witnessing strong growth in the last three quarters. The company is trying to leverage this trend by introducing newer variants and is also aggressively spending towards brand building through digital campaigns. Further, it maintained its leadership position in Glucon D, EverYuth Scrub & Nycil with market share of 58.3%, 34.8% & 35.7%, respectively. Gross margins expanded 262 bps on account of significant decline in milk prices. The continuous exercise of cost cutting measures resulted in overhead savings of 362 bps & integration of acquired business results in lower employee cost 113 bps. The company aggressively increased its marketing spends by 560 bps towards media & digital campaigns. Despite high advertisement spend, operating profit increased 32.7% to ₹ 49.5 crore & operating margins expanded 176 bps to 13%. The company pre-paid ₹ 1500 crore non-convertible debenture (NCD) which resulted in one-time expense of ₹ 132.1 crore, of which ₹ 34.2 was incurred in Q3. Adjusting for one-time expense, PAT grew from ₹ 8.9 crore to ₹ 35.9 crore.

Focus on new product launches; foraying in new markets

The company has launched nine new products or variants in 2020, which includes Sugarfree D'lite dark chocolate, Aloevera Gel under EverYuth & Glucon-C ImmunoFizz, Nycil sanitisers wipes in Q3. It also introduced Nutralite Choco Spreads & smaller sachets in Complan earlier. In January 2021, it launched Ghee & Probiotic butter spread under Nutralite DoodhShakti brand. ZWL is looking to enter new markets & build scale in Saarc, Middle East & South East Asia countries. We believe aggressive new launches & foraying in international geographies would drive growth in the medium term. We estimate 9.5% revenue growth in FY20-23.

Lower milk prices, synergy benefits to aid margins

Milk prices saw a sharp decline in March-April due to significant reduction in consumption post coivd however, it has started inching up in last one month. The company generally procures skimmed milk powder (SMP) for extended period to safeguard against any abrupt price movement. We believe benefit of lower milk prices would continue in next few quarters. However, the sharp increase in palm oil could pull back some gains. The eliminating common costs after Heinz integration should also aid margins. We estimate 300 bps operating margin expansion to 21.2% in FY23.

Valuation & Outlook

The company has benefited from strong growth in Sugarfree, Complan, Glucon-D & Nycil mainly led by tailwinds from heightened health awareness, aggressive new launches & improving direct reach. We believe ZWL would be able to grow its brands by leveraging chemist channel & doctor's advisory. We value the stock 35x FY23 earnings and maintain our **BUY** recommendation with a revised target price of ₹ 2500/share (earlier ₹ 2300).

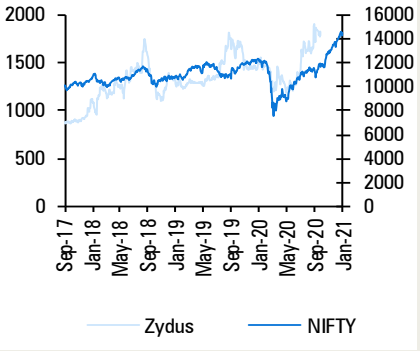
Particulars

Particulars (₹ crore)	Amount
Market Capitalization	12,484.9
Total Debt (FY20)	1,519.1
Cash and Investments (FY20)	192.8
EV	13,811.1
52 week H/L (₹)	2218 / 1100
Equity capital	57.7
Face value (₹)	10.0

Key Risk

- Disallowing goodwill amortisation in Budget 2021 may impact earnings & cash flows
- Any significant increase in milk prices & palm oil prices could negatively impact gross margins

Price Chart



Research Analyst

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Key Financial Summary

₹ Crore	FY18	FY19	FY20	FY21E	FY22E	FY23E	CAGR FY20-23E
Net Sales	512.6	842.8	1,766.8	1,877.4	2,117.3	2,321.2	9.5
EBITDA	125.3	174.4	321.1	348.9	435.0	491.9	15.3
EBITDA Margin %	24.4	20.7	18.2	18.6	20.5	21.2	
Adjusted Net Profit	133.9	169.1	185.9	254.2	388.1	459.2	35.2
Adjusted EPS (₹)	17.1	29.3	32.2	39.5	60.3	71.3	
Adjusted P/E (x)	113.2	66.1	60.2	49.1	32.2	27.2	
RoCE (%)	15.9	3.2	5.9	6.2	7.8	9.0	
RoE (%)	19.4	5.0	5.4	5.5	8.0	9.3	

Source: Company, ICICI Direct Research

Result Update
ICICI Securities – Retail Equity Research

Exhibit 1: Variance Analysis

	Q3FY21	Q3FY21E	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	Comments
Net Sales	376.4	356.0	325.7	15.6	537.4	-30.0	Net sales witnessed growth of 15.6% led by double digit growth in Sugar Free & strong traction in Complan, Nycil, Glucon-D. Nutralite continued to post muted sales mainly due to partial opening up of HORECA
Raw Material Expenses	173.1	170.6	159.6	8.4	109.5	58.1	Gross margins expanded 262 bps on account of lower milk prices. However, palm oil prices were up during the quarter
Employee Expenses	38.4	39.8	37.2	3.1	52.7	-27.2	
SG&A Expenses	56.8	35.17	30.9	84.0	49.1	15.6	The company increased the marketing spends to sales by 560 bps to support new variant launches
Other operating Expenses	63.8	65.7	67.7	-5.7	74.9	-14.8	In a continuous expercise of cost cutting, it was able to save 362 bps to sales in Q3FY21
EBITDA	49.5	44.8	37.3	32.7	122.4	-59.5	
EBITDA Margin (%)	13.0	12.6	11.2	176 bps	22.8	-979 bps	Operating margins increased 176 bps on account of higher gross margins, saving in overhead spends, lower employee
Depreciation	6.3	5.3	5.3	17.2	6.4	-2.5	
Interest	9.9	4.1	35.3	-72.0	34.6	-71.5	
Other Income	2.5	3.4	2.4	3.7	1.8	38.5	
PBT	35.9	38.7	-0.8	-4,376.2	83.2	-56.8	
Exceptional Items	-34.2	0.0	-4.6	NA	0.0	NA	The company incurred total one time expense of ₹ 132 crore as a premium towards pre-payment of NCDs. Out of this ₹ 34.2 crore was paid during Q3FY21
Tax Outgo	0.0	0.0	-9.7	NA	-6.1		
PAT	1.7	34.1	4.2	-59.0	89.2	-98.0	
Adjusted PAT	35.9	34.1	8.9	NC	89.2	-59.7	Adjusting for one-time expense, profits were at ₹ 35.9 crore against ₹ 8.9 crore in the corresponding quarter

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

	FY21E			FY22E			FY23E			
(₹ Crore)	Old	New	% change	Old	New	% change	Old	New	% change	Comments
Sales	1,855.1	1,877.4	1.2	2,093.0	2,117.3	1.2	2,294.2	2,321.2	1.2	We tweak our revenue estimate slightly
EBITDA	363.9	348.9	-4.1	442.2	435.0	-1.6	482.5	491.9	1.9	
EBITDA Margin (%)	19.6	18.6	-103 bps	21.1	20.5	-58 bps	21.0	21.2	16 bps	On sharp increase in palm oil prices & expected reversal of downward milk prices, we change our operating margin estimate
Adjusted PAT	276.7	254.2	-8.1	423.0	388.1	-8.2	461.2	459.2	-0.4	
EPS (₹)	43.0	39.5	-8.1	65.7	60.3	-8.2	71.7	71.3	-0.5	

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

	Currect				Earlier			Comments
	FY20E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	
Sugarfree (₹ crore)	344.7	386.0	433.6	477.6	379.1	425.8	469.1	We change our estimate marginally after the strong Q3FY21 results
Everyuth (₹ crore)	178.3	169.9	208.0	237.6	164.1	200.9	229.5	
Glucon D (₹ crore)	472.0	505.3	561.4	612.7	500.6	556.1	606.9	
Complan (₹ crore)	378.0	404.5	449.4	490.4	400.7	445.2	485.8	
RM / Sales (%)	42.7	44.1	39.6	40.2	44.2	40.1	40.7	

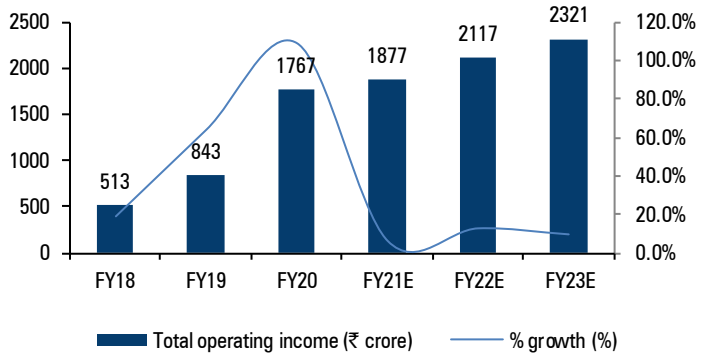
Source: Company, ICICI Direct Research

Conference call highlight

- Revenue increased 14.7% to ₹ 381.6 crore (net sales growth of 15.6%) led by strong double digit growth in Sugarfree and sustain growth in other brands. The company maintained its leadership position Glucon-D, Sugar Free, EverYuth Scrub, Peel off Face Mask and Nycil
- Nycil gained market share by 213 bps to 35.7% in Prickly heat powder category. EverYuth Scrub maintained its market share at 34.8% & Glucon-D market share was 58.3%. In the Malted Food Drink category, Complan has a market share of 5.5%
- Nutralite continue to de-grow due to its higher concentration of HORECA. However, business improved sequentially including institutional business. Mayo portfolio saw healthy performance because of increased demand for the category. Nutralite Choco Spread, continued to deliver steady business on E-Commerce and Modern Trade channels
- The company launched nine new products & variants in 2020. It introduced Sugarfree D'lite dark chocolate, Aloevera Gel under EverYuth, Glucon-D ImmunoVolt, Glucon-C ImmunoFizz, Nycil sanitisers, Nycil Sanitisers wipes, Nutralite Choco Spreads & smaller sachets in Complan earlier. Further, In January 2021, it launched Ghee & Probiotic butter spread under Nutralite DoodhShakti brand
- The company is focusing on increasing its direct distribution reach from current 0.35 million outlets to 0.5 million outlets by March 2021. On overall basis, its distribution reach is 2.0 million retail outlets. It would like to maintain a ratio of 1:4 for direct to indirect reach. E-commerce channel sales increased by 240% in Q3
- The company increased its advertisement spends by 83% to ₹ 56.8 crore (560 bps higher). It is effectively using media, print & digital channels to market Sugarfree, EverYuth & Complan
- ZWL has benefited from lower milk prices. However, the management indicated a sharp rise in palm oil remains a concern. The company procures refined palm oil in India only
- The company has not taken any price hikes during the quarter but is looking to increase prices next quarter
- The company repaid ₹ 1500 crore NCDs during the quarter and incurred one-time expense of ₹ 132 crore, of which ₹ 34 crore was incurred in Q3FY21. The company has taken debt of ₹ 565 crore at 5% interest rate, which would be repaid over the next 30 months
- The change in income tax provision in Budget related to dis-allowing goodwill amortisation could impact tax liability for the company. However, it is yet to assess the exact impact of these provisions

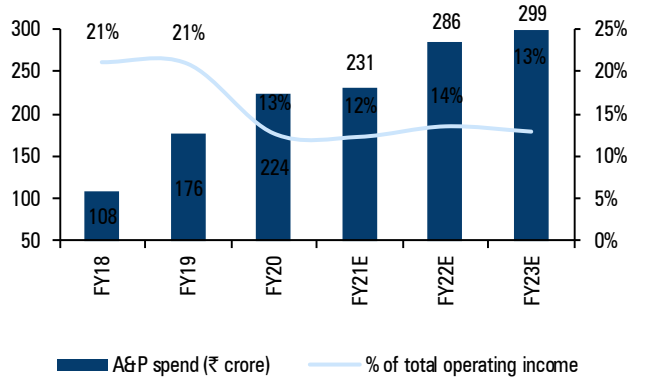
Key Metrics

Exhibit 4: Revenue & revenue growth trend



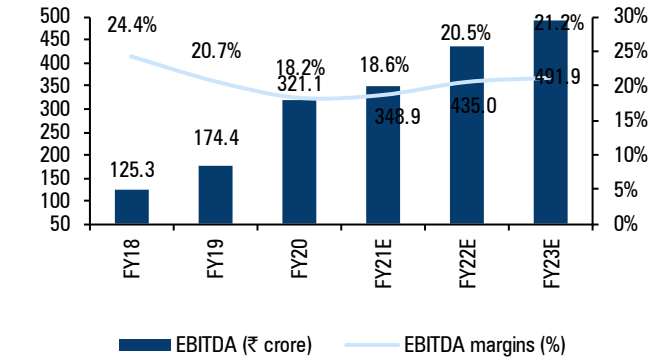
Source: ICICI Direct Research, Company

Exhibit 5: Marketing spend trend



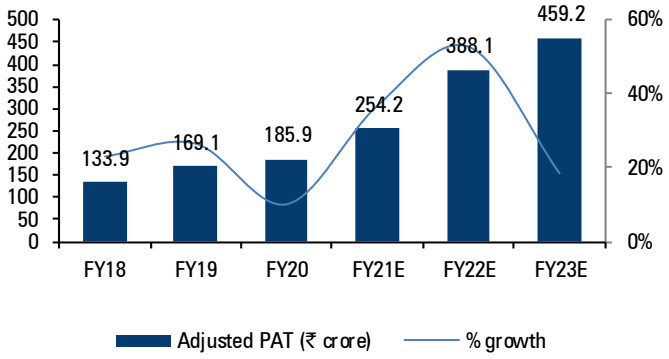
Source: ICICI Direct Research, Company

Exhibit 6: Operating margins trend (%)



Source: Company, ICICI Direct Research

Exhibit 7: Adjusted PAT growth to recover in FY22E



Source: Company, ICICI Direct Research

Exhibit 8: Brand wise revenues (I-direct Estimate)

₹ crore	FY20 Revenues
Sugar Free	344.7
Everyuth	178.3
Complan	378.0
Glucon D	472.0
Nycil	297.5
Nutralite	40.7
Others	58.8

Source: ICICI Direct Research

Exhibit 9: Valuation

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY20	1766.8	109.6	32.2	9.9	78.9	43.4	5.4	5.9
FY21E	1877.4	6.3	39.5	22.5	102.2	36.4	5.5	6.2
FY22E	2117.3	12.8	60.3	52.7	32.2	28.9	8.0	7.8
FY23E	2321.2	9.6	71.3	18.3	27.2	25.5	9.3	9.0

Source: Company, ICICI Direct Research

Financial summary

Exhibit 10: Profit and loss statement ₹ crore

	FY20	FY21E	FY22E	FY23E
Total operating Income	**1,766.8**	**1,877.4**	**2,117.3**	**2,321.2**
Growth (%)	109.6	6.3	12.8	9.6
Raw Material Expenses	778.8	834.3	940.2	1,044.7
Employee Expenses	156.0	186.4	215.8	241.4
Marketing Expenses	224.3	230.6	286.3	299.3
Administrative Expenses	0.0	87.9	90.3	94.1
Other expenses	286.7	189.4	149.7	149.7
Total Operating Expenditure	1,445.8	1,528.5	1,682.3	1,829.3
EBITDA	**321.1**	**348.9**	**435.0**	**491.9**
Growth (%)	84.1	8.7	24.7	13.1
Depreciation	26.4	26.7	29.4	32.1
Interest	139.9	82.6	29.3	13.0
Other Income	10.7	8.6	11.8	12.4
PBT	165.5	248.2	388.1	459.2
Total Tax	-20.5	-6.1	0.0	0.0
Exceptional Item	44.2	132.1	0.0	0.0
PAT	141.7	122.1	388.1	459.2
Adjusted PAT	**141.7**	**254.2**	**388.1**	**459.2**
Growth (%)	-16.2	79.4	52.7	18.3
Adjusted EPS (₹)	32.24	39.51	60.31	71.35

Source: Company, ICICI Direct Research

Exhibit 11: Cash flow statement ₹ crore

(Year-end March)	FY20	FY21E	FY22E	FY23E
Profit After Tax	119.7	122.1	388.1	459.2
Add: Depreciation	26.4	26.7	29.4	32.1
(Inc)/dec in Current Assets	16.0	42.3	-99.3	-89.1
Inc/(dec) in CL and Provisions	97.1	133.1	68.3	75.5
CF from operating activities	**259.2**	**324.2**	**386.6**	**477.7**
(Inc)/dec in Investments	0.0	0.0	0.0	0.0
(Inc)/dec in LT loans & advances	-64.0	-10.0	-10.0	-10.0
(Inc)/dec in Fixed Assets	-5.1	-50.0	-50.0	-50.0
Others	-14.1	-5.0	-5.0	-5.0
CF from investing activities	**-83.2**	**-65.0**	**-65.0**	**-65.0**
Issue/(Buy back) of Equity	0.0	1,100.0	0.0	0.0
Inc/(dec) in loan funds	-50.2	-990.0	-170.0	-200.0
Dividend paid & dividend tax	-69.4	-64.4	-160.9	-386.1
Interest Paid	-140.1	-82.6	-29.3	-13.0
Others	0.0	0.0	0.0	0.0
CF from financing activities	**-259.7**	**-36.9**	**-360.2**	**-599.1**
Net Cash flow	-83.7	222.3	-38.6	-186.4
Opening Cash	138.2	82.4	304.6	266.0
Cash with Bank	27.9	0.0	0.0	0.0
Closing Cash	**82.4**	**304.6**	**266.0**	**79.6**

Source: Company, ICICI Direct Research

Exhibit 12: Balance sheet ₹ crore

(Year-end March)	FY20	FY21E	FY22E	FY23E
Liabilities				
Equity Capital	57.7	64.4	64.4	64.4
Reserve and Surplus	3,403.0	4,554.1	4,781.3	4,854.3
Total Shareholders funds	3,460.7	4,618.4	4,845.7	4,918.7
LT Borrowings & Provisions	1500.0	510.0	340.0	140.0
Deferred Tax Liability	19.1	19.1	19.1	19.1
Others Non-current Liabilities	27.2	27.2	27.2	27.2
Total Liabilities	**5,006.9**	**5,174.7**	**5,231.9**	**5,104.9**
Assets				
Gross Block	372.7	412.7	452.7	492.7
Less: Acc Depreciation	168.1	194.8	224.2	256.3
Net Block	204.7	218.0	228.5	236.4
Capital WIP	3.5	13.5	23.5	33.5
Goodwill	3,920.0	3,920.0	3,920.0	3,920.0
Non-current Investments	1.6	1.6	1.6	1.6
LT loans & advances	4.7	14.7	24.7	34.7
Deferred Tax Assets	120.8	120.8	120.8	120.8
Other Non-Current Assets	558.6	563.6	568.6	573.6
Current Assets				
Inventory	292.3	257.2	319.0	368.8
Debtors	118.2	123.4	145.0	159.0
Loans and Advances	0.0	6.2	7.0	7.7
Other Current Assets	172.4	346.8	391.1	428.8
Cash	82.4	304.6	266.0	79.6
Investments	110.4	0.0	0.0	0.0
Current Liabilities				
Creditors	491.1	540.1	585.9	642.3
Provisions	0.0	5.1	5.8	6.3
Short term debt & other CL	91.7	170.7	192.5	211.0
Application of Funds	**5,006.9**	**5,174.6**	**5,231.9**	**5,104.9**

Source: Company, ICICI Direct Research

Exhibit 13: Key ratios ₹ crore

(Year-end March)	FY20	FY21E	FY22E	FY23E
Per share data (₹)				
EPS	32.2	39.5	60.3	71.3
Cash EPS	29.2	23.1	64.9	76.3
BV	600.2	717.6	753.0	764.3
DPS	10.0	10.0	25.0	60.0
Cash Per Share	14.3	47.3	41.3	12.4
Operating Ratios (%)				
EBITDA Margin	18.2	18.6	20.5	21.2
PBT / Total Operating income	9.4	13.2	18.3	19.8
PAT Margin	8.0	6.5	18.3	19.8
Inventory days	60.4	50.0	55.0	58.0
Debtor days	24.4	24.0	25.0	25.0
Creditor days	101.5	105.0	101.0	101.0
Return Ratios (%)				
RoE	5.4	5.5	8.0	9.3
RoCE	5.9	6.2	7.8	9.0
Valuation Ratios (x)				
P/E	78.9	102.2	32.2	27.2
EV / EBITDA	43.4	36.4	28.9	25.5
EV / Net Sales	7.9	6.8	5.9	5.4
Market Cap / Sales	7.1	6.7	5.9	5.4
Price to Book Value	3.2	2.7	2.6	2.5
Solvency Ratios				
Debt/EBITDA	4.7	1.5	0.8	0.3
Debt / Equity	0.4	0.1	0.1	0.0
Current Ratio	1.0	1.0	1.1	1.1
Quick Ratio	0.5	0.7	0.7	0.7

Source: Company, ICICI Direct Research

Exhibit 14: ICICI Direct coverage universe (FMCG)

	CMP	TP		M Cap	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)	Rating	(₹ Cr)	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Colgate (COLPAL)	1,618	1,860	Buy	43,654	35.0	37.8	40.5	46.2	42.8	40.0	9.3	8.5	8.0	76.7	80.2	83.7	58.7	61.5	64.3
Dabur India (DABIND)	526	620	Buy	91,067	9.9	11.0	12.3	53.1	47.8	42.9	9.4	8.5	7.7	26.5	27.0	27.4	22.9	23.0	23.3
Hindustan Unilever (HINLEV)	2,230	2,600	Hold	561,507	33.6	40.5	45.0	66.3	55.1	49.6	12.4	10.8	10.0	25.3	29.4	31.7	19.1	22.5	24.3
ITC Limited (ITC)	218	225	Buy	213,884	11.2	12.0	13.4	19.5	18.1	16.3	4.7	4.2	3.8	27.2	30.5	35.7	20.9	23.4	27.5
Jyothy Lab (JYOLAB)	160	175	Hold	5,728	5.9	6.4	7.1	27.4	25.1	22.5	3.1	2.8	2.6	30.6	31.1	31.6	26.0	25.9	26.3
Marico (MARLIM)	424	490	Buy	53,156	9.1	9.8	10.9	46.6	43.4	38.8	6.8	6.1	5.5	42.9	45.4	48.2	37.1	38.6	40.9
Nestle (NESIND)	17,190	18,000	Hold	152,970	223.4	253.4	284.2	76.9	67.8	60.5	11.5	10.4	9.5	59.9	66.6	73.7	119.1	139.2	160.6
Tata Consumer Products (TATGLO	575	605	Buy	52,158	12.0	13.5	15.1	47.9	42.5	38.0	4.8	4.4	4.1	9.8	10.5	11.1	7.8	8.6	9.3
VST Industries (VSTIND)	3,621	4,200	Hold	5,809	202.4	218.7	235.2	17.9	16.6	15.4	5.1	4.7	4.3	44.7	47.4	52.8	33.2	35.2	39.0
Varun Beverage (VARBEV)	870	730	Hold	19,429	11.3	21.7	26.6	76.9	40.0	32.7	3.0	2.5	2.3	12.3	18.6	20.7	10.1	16.7	17.6
Zydus Wellness (ZYDWEL)	1,918	2,500	Buy	12,343	19.0	60.3	71.3	101.1	31.8	26.9	6.6	5.8	5.3	6.2	7.8	9.0	5.5	8.0	9.3

Source: Company, ICICI Direct Research

RATING RATIONALE

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%

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