Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Tata Consumer Products Ltd

Reorganisation to simplify operational structure

Consumer Goods	Sharekhan code: TATACONSUM

Reco/View: Buy	↔	CMP: **Rs. 766**	Price Target: **Rs. 960**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

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

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↓	
RQ		↔	
RV		↑	

ESG Disclosure Score NEW

ESG RISK RATING 30.27

Updated Jan 08, 2022

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

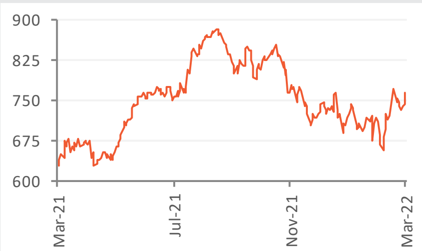
Company details

Market cap:	Rs. 70,586 cr
52-week high/low:	Rs. 889 / 614
NSE volume: (No of shares)	21.5 lakh
BSE code:	500800
NSE code:	TATACONSUM
Free float: (No of shares)	60.2 cr

Shareholding (%)

Promoters	34.7
FII	26.8
DII	13.4
Others	25.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	6.6	5.2	-7.0	21.8
Relative to Sensex	2.3	3.7	-5.8	4.7

Sharekhan Research, Bloomberg

Summary

- Tata Consumer Products Limited's (TCPL's) board proposed reorganisation of its India and overseas business to simplify, align, and synergise the business.
- TCPL proposed to consolidate Tata Coffee Limited's (TCL) business into TCPL and its wholly owned subsidiary at a share swap ratio of 3 TCL shares for 10 TCPL shares; and purchase 10.15% stake in TCP UK through preferential allotment.
- Proposed reorganisation is expected to result in revenue and operational efficiences, which will lead to 5-10% PAT accretion in the next 12-18 months.
- The stock is currently trading at 54.4x/45.3x its FY2023E/FY2024E EPS. We maintain Buy with an unchanged PT of Rs. 960.

Tata Consumer Products Limited's (TCPL) board in its meeting held on March 29, 2022, proposed to consolidate Tata Coffee Limited's (TCL) business into TCPL and its wholly own subsidiary – Tata Consumer Products Beverages & Foods Limited (TBFL) and purchase minority stake of 10.15% in Tata Consumer Products (TCP) UK to make it a wholly owned subsidiary of TCPL. The proposed restructure would result in equity dilution of 3.4% for TCPL with post diluted equity at 95.3 crore shares. The proposed reorganisation is expected to result in revenue and operational efficiences, which will lead to 5-10% PAT accretion in the next 12-18 months. The proposed reorganisation is in-line with the group's strategy to simplify the organisation structure to reap operational, adminsitrative and supply chain benefits in the medium to long run.

- **Event - TCPL proposed reorganisation to simplify structure:** TCPL announced a reorganisation plan in line with its strategic priority of unlocking synergies and efficiencies. This includes demerger of the plantation business of TCL into TBFL, a wholly owned subsidiary of TCPL, and merger of the remaining business of TCL, consisting of its extraction and branded coffee business with TCPL. Post the regulatory approvals, shareholders of TCL will get 3 shares of TCPL for every 10 shares held in TCL. Additionally, TCPL proposes to purchase the minority interest of 10.15% in its UK subsidiary, TCP UK, by making a preferential allotment of 74.6 lakh shares at a price of Rs. 765.15 per share. The proposed reorganisation will lead to equity dilution of 3.4% to 95.3 crore shares.
- **Deal will drive in synergies and efficiencies in the long run:** Consolidation of minority entities will drive efficiencies through aligning of corporate structure with management and administrative structures, significant reduction in entities (from current 45 entities to 22-23 entities over the next 18 months), faster decision making and execution under one roof, increasing focus on separated businesses such as branded tea and foods, plantation and extraction business, and revenue and cost synergies expected in the medium term.
- **PAT accretive by 5-10%:** Management expects proposed restructure to be PAT accretive by 5-10% with larger savings anticipated at tax levels due to simplification of structure, dividend withhold tax, efficiencies at administrative cost, and building of revenue synergies (especially in the plantation business); considering the equity dilution, the deal will be EPS accretive by 3-5%.

Our Call

View – Retain Buy with an unchanged PT of Rs. 960: We believe the proposed re-structuring process under TCPL is in line with the group's overall strategy to simplify the structure of each entity to improve operating efficiencies in the long run. The proposed scheme of arrangement will not only be earnings accretive for TCPL but will enable better leverage in supply chain, increased focus under different business verticals with specialised management team, and accelerate decision making in the coming years. With strategies in place, TCPL is well poised to achieve double-digit revenue and PAT CAGR of 13% and 17%, respectively, over FY2021-FY2024 (excluding the benefits of proposed re-organisation). The stock is trading at 54.4x and 45.3x its FY2023E and FY2024E earnings, respectively. We maintain our Buy rating on the stock with an unchanged price target (PT) of Rs. 960.

Key Risks

Any slowdown in demand in the domestic or international market or any significant increase in raw tea and coffee prices would act as a risk to our earnings estimates in the near term.

Valuation (Consolidated) Rs cr

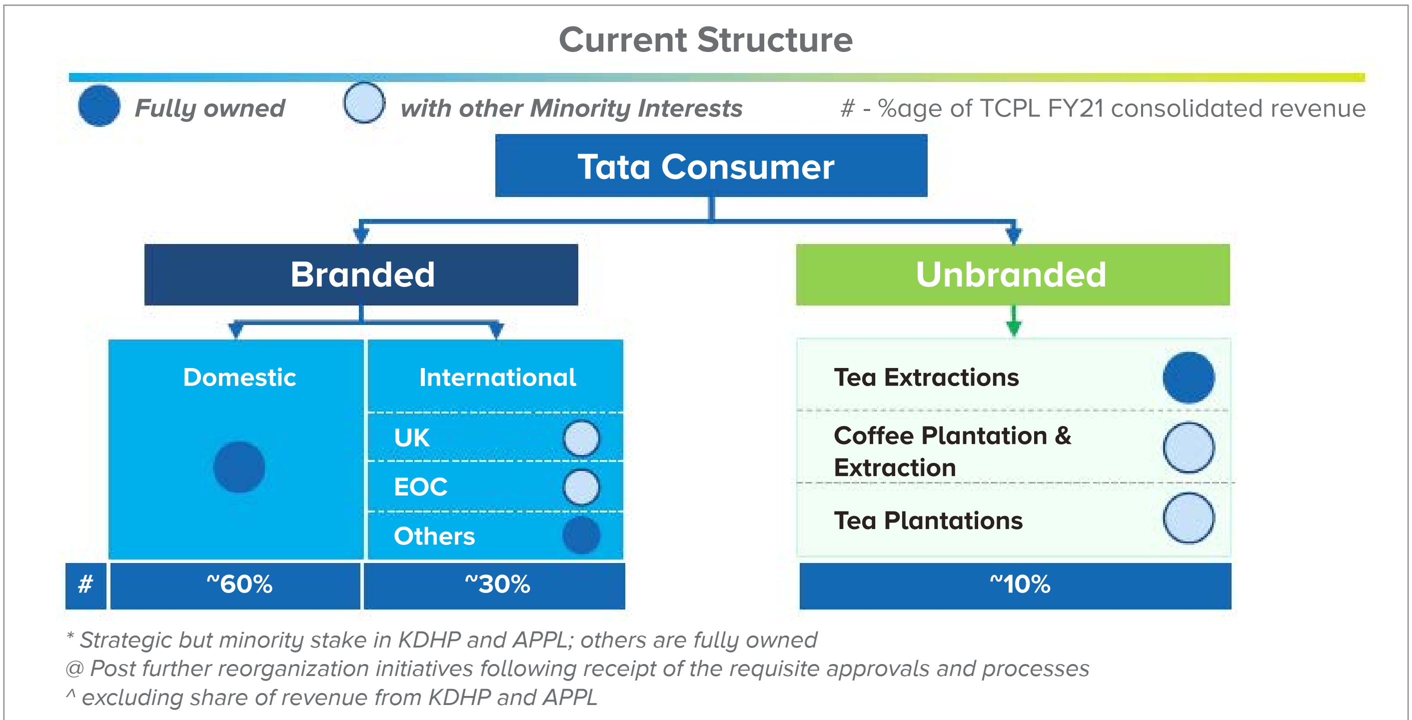
Particulars	FY21	FY22E	FY23E	FY24E
Revenue	11,602	12,356	14,320	16,522
OPM (%)	13.3	14.1	14.8	15.5
Adjusted PAT	953	1,033	1,299	1,560
% Y-o-Y growth	*44.2*	*8.4*	*25.7*	*20.1*
Adjusted EPS (Rs.)	10.3	11.2	14.1	16.9
P/E (x)	74.1	68.3	54.4	45.3
P/B (x)	4.9	4.7	4.4	4.1
EV/EBIDTA (x)	44.5	39.6	32.3	26.4
RoNW (%)	7.2	7.3	8.7	9.9
RoCE (%)	8.1	8.6	10.3	11.8

Source: Company; Sharekhan estimates

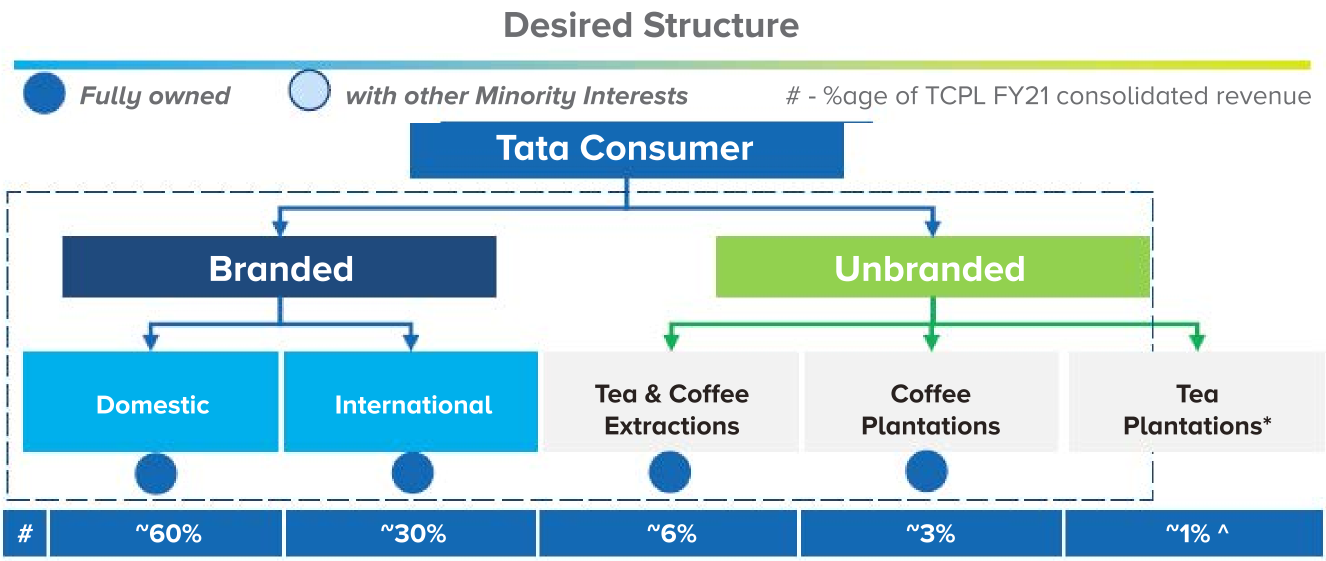
Overview of TCPL's reorganisation to simply operational and cost struture

- **Proposed scheme of arrangement for re-organisation:**
  1. TCPL holds 57.48% stake in TCL. Post the proposed scheme of demerger and merger, TCL's consumer business will be consolidated in TCPL, while TCL's plantation business will be demerged into a new subsidiary of TBFL. Share swap ratio is 3 shares of TCPL for every 10 shares held in TCL.
  2. TCPL will be acquiring 10.15% shares in its foreign subsidiary (TCPL currently holds 89.85%) by issuing 74,59,935 shares at Rs. 765.2 per share.
- **Equity dilution:** Post restructuring, the diluted equity of TCPL will stand at 95.3 crore shares (existing is 92.2 crore shares; pre-issue equity dilution of 3.4%).
- **Unlock synergises and efficiencies:**
  - Alignment of legal and management structure while converge minority interests of subsidiaries in TCPL
  - Significant reduction in entities (from current 45 entities to 22-23 entities over the next 18 months).
  - Consolidation paves way to enhance value through operational and structural benefits.
  - Unification of extraction business to increase geographical reach with wider variety of product offerings.
  - Provides room to better leverage supply chain for efficient materials.
- **PAT accretive by 5-10%:** Management expects the proposed restructure to be PAT accretive by 5-10% with larger savings anticipated at tax levels due to simplification of structure, dividend withhold tax, efficiencies at administrative cost, and building of revenue synergies (especially in the plantation business). Considering the equity dilution, the deal will be EPS accretive by 3-5%.
- **Deal timeline:** Implementation of the scheme is expected to take around 12-14 months subject to the receipt of regulatory approval.

Efficiencies from consolidation of legal structure



Source: Company presentation



** Strategic but minority stake in KDHP and APPL; others are fully owned*
@ Post further reorganization initiatives following receipt of the requisite approvals and processes
^ excluding share of revenue from KDHP and APPL

Source: Company presentation

Increased equity due to proposed re-organisation

Particulars	No. of shares (cr)	
TCPL no. of equity shares (existing)		**92.2**
Add: Share swap deal: 3 shares of TCPL for every 10 shares held in TCL	5.6	
Less: Cancelation of TCPL holding in TCL	3.2	
Net addition		**2.4**
Acquisition of minority stake of 10.15% in TCPL UK		0.7
TCPL no. of equity shares (post dilution)		**95.3**

Equity dilution (%) on pre-issue equity 3.4%

Source: Company; Sharekhan Research

Details of both - consolidation of TCL's merger and minority stake buy

1. **TCPL and TCL composite scheme of demerger and merger**

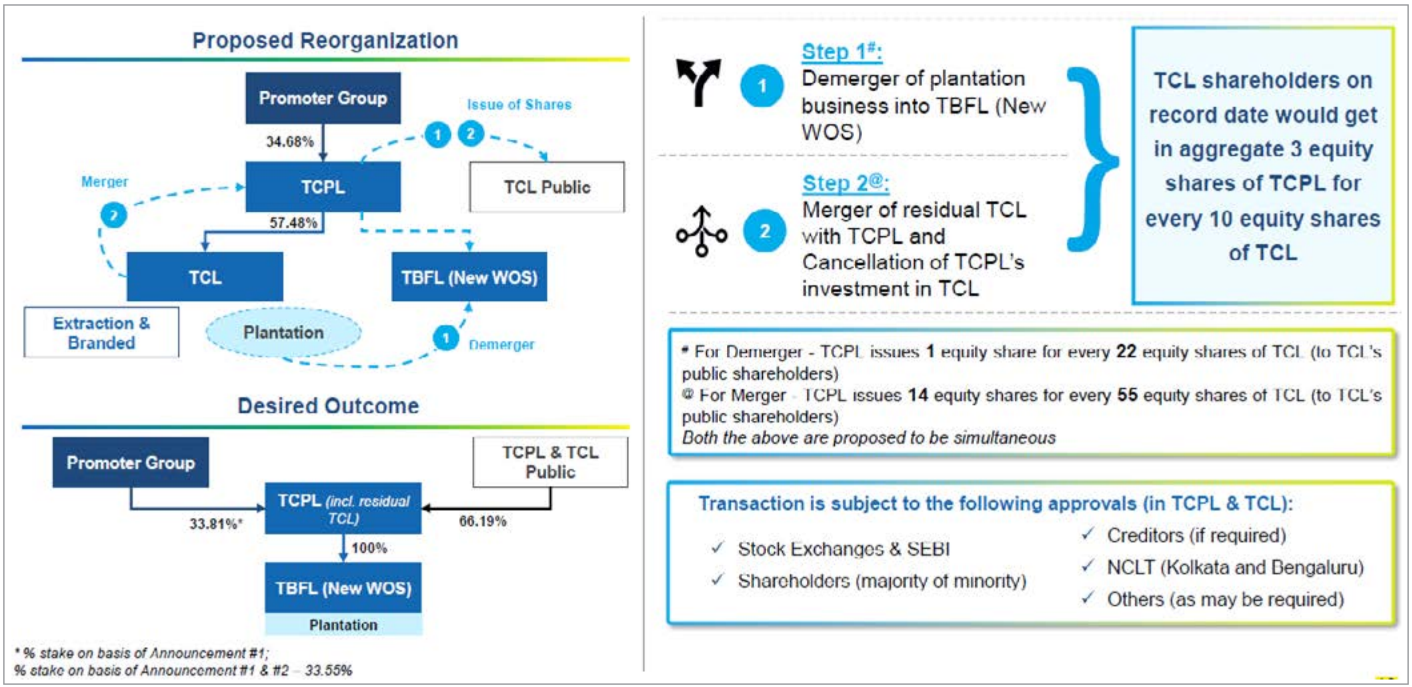
   a. **Deal structure:** i) Demerger of the plantation business into newly, wholly owned subsidiary, TBFL, and ii) Merger of residual TCL's business (largely consumer business) with TCPL and cancellation of TCPL's investment in TCL.

   b. **Swap ratio:** TCL's shareholders would get aggregate 3 equity shares of TCPL for every 10 equity shares of TCL. Based on swap ratio, TCL is valued at Rs. 223 per share, which is at a premium of 13.6% to TCL's CMP of Rs. 196.2 per share. Swap ratio is favourable for Tata Coffee shareholders.

   c. **Deal valuation:** Total enterprise value of TCL as per the swap ratio stands at Rs. 4,555.5 crore. The deal is valued at EV/sales of 2.0x (its FY2021 consolidated sales of Rs. 2,255 crore) and 11.3x its FY2021 EV/EBIDTA.

   d. **Synergistic benefits:** Revenue synergies would emerge for the plantation business with larger offerings to clients under one entity, dedicated and specialised management focus for respective businesses, recurring and one-time operational, and administrative and financial benefits.

TCPL – TCL's Composite Scheme of Demerger and Merger



Source: Company presentation

Beneficial for shareholders of both TCPL and TCL

For Tata Coffee Shareholders

- Broder play
- Multiple growth engines
- Larger market cap

For Tata Consumer Shareholders

- Synergies
- Efficiencies
- Focus

Source: Company, Sharekhan Research

Deal structure of TCL's merger with TCPL

Particulars	No. of shares (cr)
TCPL outstanding shares (cr.)	92.2
TCL outstanding shares (cr.)	18.7
TCPL's stake in TCL (%)	57.5
No of shares (cr.)	10.7
Minority shareholding (%)	42.5
No of shares (cr.)	7.9
Swap ratio: 3 shares of TCL for every 10 shares of TCPL	
Total number of TCPL shares to be issue to TCL's minority shareholders (cr.)	2.4
Implied value of TCL as per the swap ratio (Rs.)	223
TCL CMP (Rs.)	196.3
Premium (%)	13.6
Deal valuation	
Implied market capital at Rs. 223.0 per share (Rs. Cr)	4164.5
Add: Debt (Rs. Cr)	675.2
Less: Cash (Rs. Cr)	284.2
Enterprise value (Rs. Cr)	**4555.5**
Consolidated revenues (Rs. Cr)	2255
Consolidated EBIDTA (Rs. Cr)	402.6
EV/Sales (x)	2
Market cap/sales (x)	1.8
EV/EBIDTA (x)	11.3

Source: Company, Sharekhan Research

2. **Purchase minority interest (10.15% stake) in TCP UK from Tata Enterprises Overseas (TEO)**

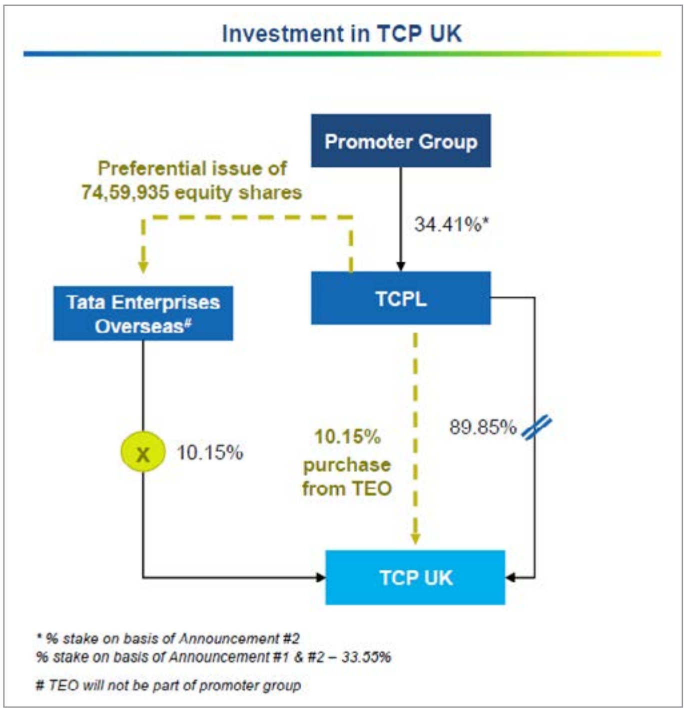
   a. **Deal structure:** Purchase 10.15% stake in TCP UK from Tata Enterprises Overseas (TEO) resulting in 100% ownership in TCP UK, which includes branded international tea business based in UK, Canada, parts of Europe and coffee business in the US. TCPL currently holds 89.85% stake in the subsidiary.

   b. **Consideration:** As part of the deal, TCPL will issue 74,59,935 equity shares at Rs. 765.15 per share i.e. 0.8% of post diluted equity.

   c. **Deal valuation:** Total enterprise value of TCP UK stands at Rs. 3,788 crore (based on implied value of Rs. 5,624 crore). The minority stake is valued at EV/sales of 1.7x (valuing at FY2021 revenue of GBP 227.7 million or Rs. 2,252.9 crore) and EV/EBIDTA of 23.4x.

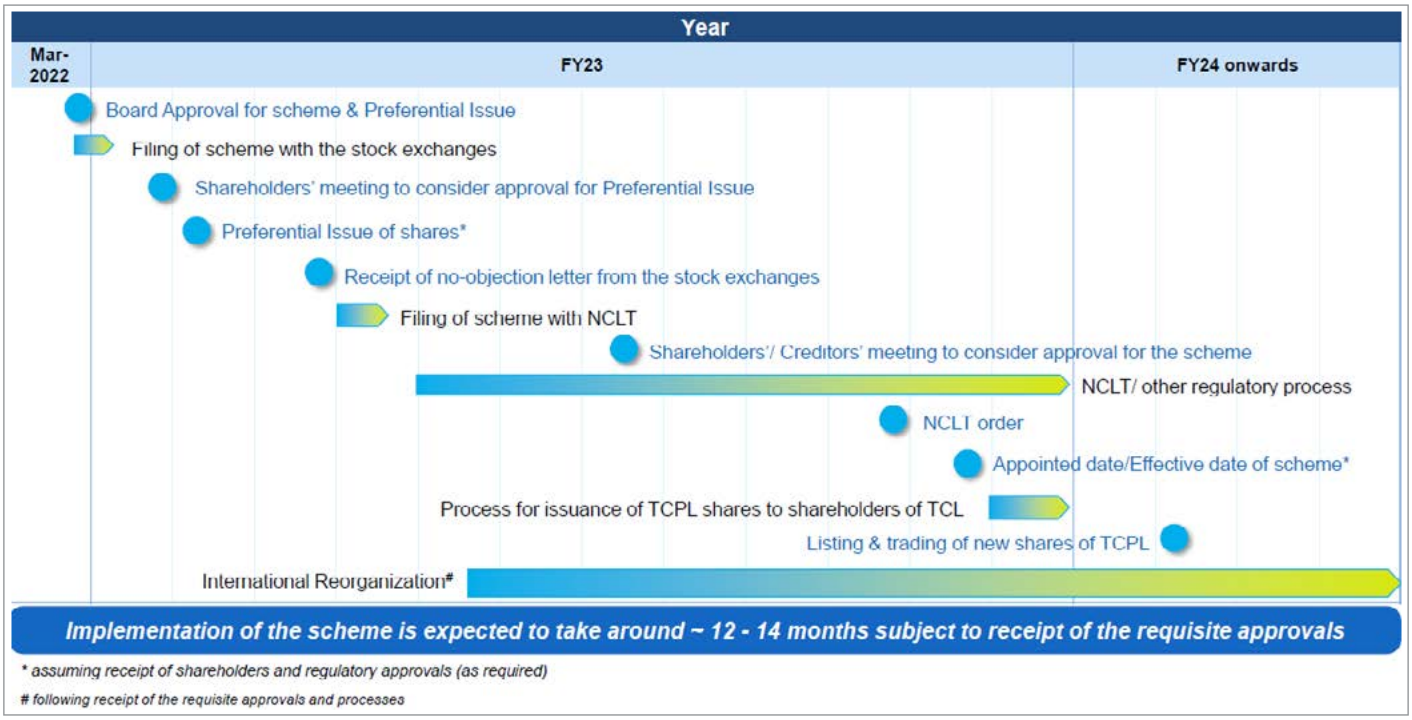
   d. **Acquisition benefits:** 100% ownership of all core businesses of the company (30% of international operations) and enable efficient re-organisation of international business with larger focus on gaining shares in key markets in the coming years.

Purchase of Minority Interest in TCP UK from TEO



Source: Company presentation

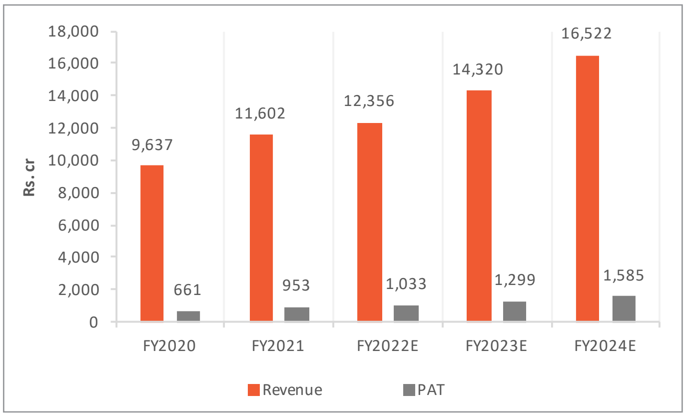
Plan of action and timelines



Source: Company presentation

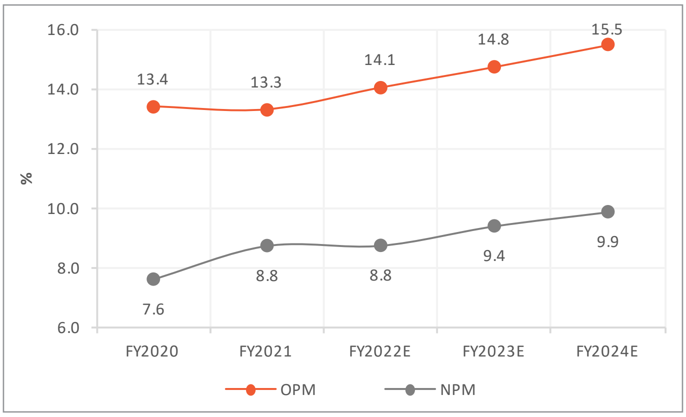
Financials in charts

Steady growth in revenue and profit



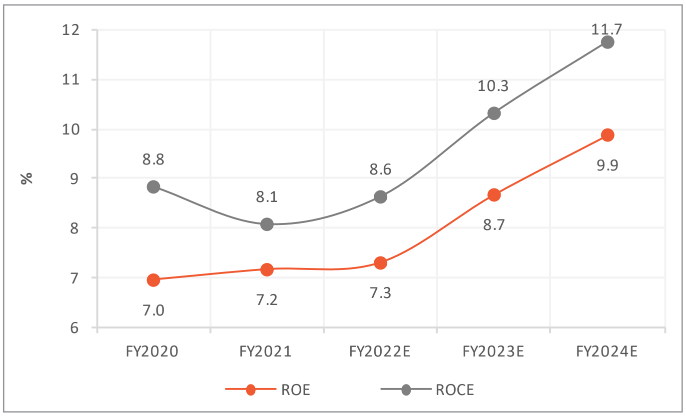
Source: Company, Sharekhan Research

Margins to improve from current levels



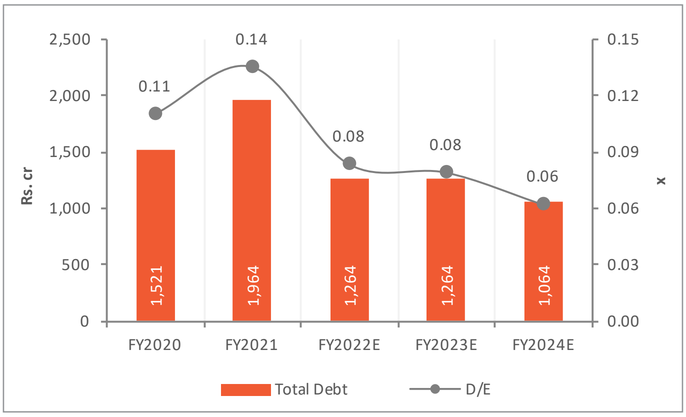
Source: Company, Sharekhan Research

Return ratios expected to improve significantly



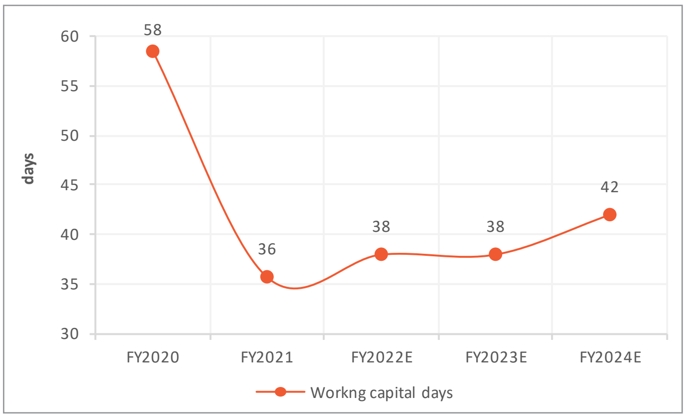
Source: Company, Sharekhan Research

Debt reduction to improve balance sheet position



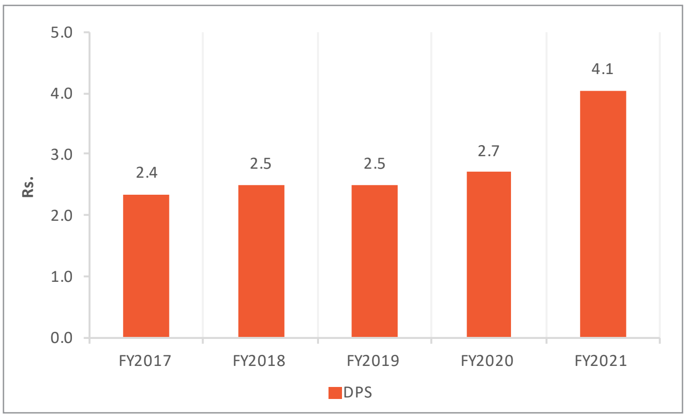
Source: Company, Sharekhan Research

Trend in working capital days



Source: Company, Sharekhan Research

Consistent dividend payout



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Near-term weakness; Long-term growth prospects intact

Slowdown in rural demand, consumer inflation, and weakness in consumer sentiments will hamper overall consumption in the coming quarters. Further, easing of the third COVID-19 wave would affect recovery in out-of-home consumption. On the other hand, companies expect that raw-material inflation will take another two to three quarters to ease and would continue to put pressure on margins. Though near-term headwinds will take a toll on the performance of consumer goods companies, long-term growth prospects are intact. Low penetration levels in key categories (especially in rural India), lower per capita consumption compared to other countries, large shift to branded products, and emergence of new channels such as e-commerce/D2C provide a number of opportunities for consumer goods companies to achieve sustainable growth in the medium to long run.

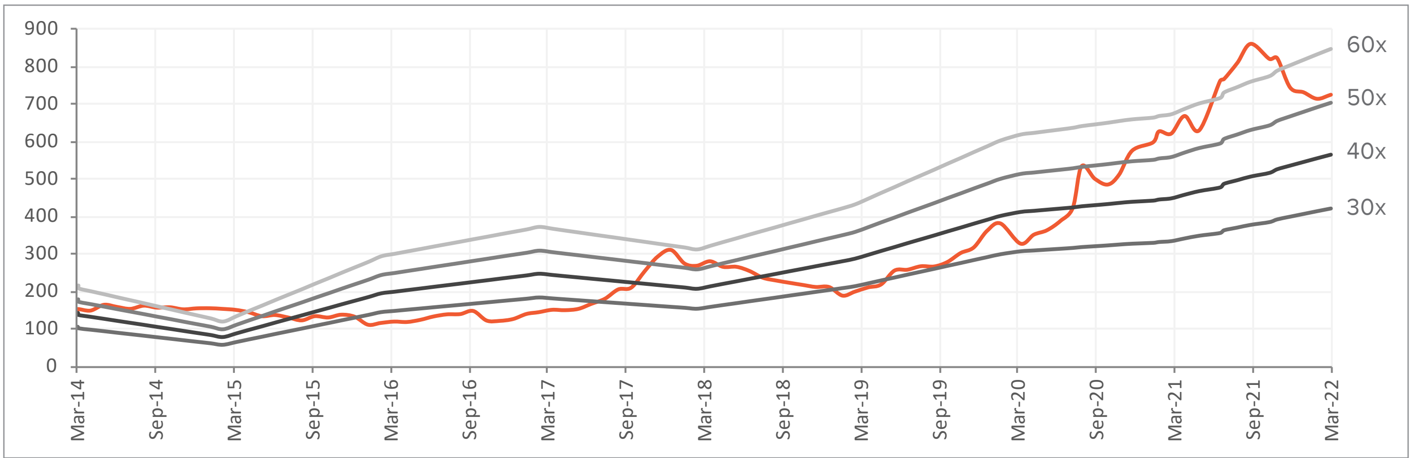
■ Company Outlook – Correcting tea prices augur well for margins

Distribution expansion and sustained share gains would help sales volume of the domestic tea business to improve to mid-to-high single digit in the medium to long term. Foods business growth will be driven by sustained new product launches, shift to branded products, and distribution expansion. Base of the international business has normalised and, with demand trend improving in most markets, business revenue growth trajectory will improve in the quarters ahead. Raw tea prices have corrected from their high and will ease out gross margin pressure despite higher fuel and packaging cost. The company is banking on operating efficiencies and mix to post better margins in the quarters ahead.

■ Valuation – Retain Buy with an unchanged price target of Rs. 960

We believe the proposed re-structuring process under TCPL is in line with the group's overall strategy to simplify the structure of each entity to improve operating efficiencies in the long run. The proposed scheme of arrangement will not only be earnings accretive for TCPL but will enable better leverage in supply chain, increased focus under different business verticals with specialised management team, and accelerate decision making in the coming years. With strategies in place, TCPL is well poised to achieve double-digit revenue and PAT CAGR of 13% and 17%, respectively, over FY2021-FY2024 (excluding the benefits of proposed re-organisation). The stock is trading at 54.4x and 45.3x its FY2023E and FY2024E earnings, respectively. We maintain our Buy rating on the stock with an unchanged price target (PT) of Rs. 960.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Hindustan Unilever	58.2	52.3	43.8	41.4	36.8	31.5	36.5	24.9	30.0
Nestle India*	80.1	71.9	60.5	51.6	46.3	40.7	136.4	138.3	134.9
Tata Consumer Products	74.1	68.3	54.4	44.5	39.6	32.3	8.1	8.6	10.3

Source: Company, Sharekhan estimates **Values for Nestle India are for CY20, CY21 and CY22E*

About company

TCPL is the world's second largest branded tea player in the world with a strong brand portfolio such as *Tata Tea, Tetley, Eight O' Clock Coffee*, and *Himalayan* (mineral water brand). Recently, the company has announced the merger of TCL's consumer business with TCPL to expand its India business, the contribution of which will increase to ~61% from 48% currently. TCPL has a very vast presence in international geographies such as UK, US, Canada, South Asia, and Africa through various subsidiaries. NourishCo markets and distributes branded non-carbonate beverage products such as *Tata Gluco Plus (TGP), Tata Water Plus, and Himalayan*. TCPL has a 50:50 joint venture with Starbucks Corporation named Tata Starbucks Private Limited, which is performing well.

Investment theme

After the integration of TCL's consumer business with TGBL, India business is expected to become a key revenue driver for the company. Rising per capita income, increasing brand awareness, increased in-house consumption, and consumption through modern channels such as large retail stores/e-commerce would act as key revenue drivers for branded pulses and spices businesses in India in addition to the consistently growing tea business. Along with margin expansion, innovation, and diversification, the merger will help TCPL to expand its distribution network. An enhanced product portfolio and expanded distribution reach would help India business revenue to grow in double digits in the next two-three years as against a 5% CAGR over FY2016-FY2020.

Key Risks

- Sustained slowdown in domestic consumption; heightened competition from new players; and spike in key input prices would act as key risks to our earnings estimates in the near term.

Additional Data

Key management personnel

N. Chandrasekaran	Chairman
Sunil D'Souza	Managing Director and CEO
L. Krishna Kumar	Executive Director and group CFO
John Jacob	Chief Finance Officer
Neelabja Chakrabarty	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	First State Investments ICVC	4.71
2	Life Insurance Corp of India	3.44
3	Blackrock Inc	2.28
4	Vanguard Group Inc	2.13
5	Norges Bank	2.11
6	GOVERNMENT PENSION FUND	2.10
7	Goldman Sachs Group Inc	1.60
8	SBI Funds Management Ltd	1.17
9	Baron Capital Inc	0.77
10	Dimensional Fund Advisors LP	0.68

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

Sharekhan

by BNP PARIBAS

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