

BRITANNIA INDUSTRIES LTD

FMCG

18 NOV 2019

Quarterly Update

HOLD

Target Price : Rs 3,235

CMP : Rs 3,195
 Potential Upside : 1%
 Relative to Sector : Positive

MARKET DATA

No. of Shares : 24.03Cr
 FV (Rs) : 2
 Market Cap (Rs Cr.) : 37,812
 52-week High / Low : Rs 3,444 / Rs 1,151
 Avg. Daily vol. (6mth) : 228,593 share
 Bloomberg Code : BRITIB
 Reuters Code : BRIT. NS
 BSE Code : 500825
 NSE Code : BRITANNIA

Q2FY20: Modest performance but category headwinds remain

Britannia delivered a modest quarter with in-line revenue versus our estimates for quarter 7% YoY growth amid slowdown challenges. Volumes reported a 3% growth (in-line with estimates) on the back of high base and weak demand conditions. However, operating leverage and marginal GM gains (input cost inflation modest at 3%) aided EBITDA Margin expansion of 31bps YoY at 16.1% during Q2FY20. Commodity led inflation could be contained due to strategic covers for key RMs and focus on cost savings initiatives which may support margin sustenance.

With, topline continuing to remain under pressure given slowdown concerns, management has cut down on NPDs, capex and direct reach expansion in-line with revised growth expectations and market conditions. Earnings undergo a revision on account of lower corporate tax rates but remain muted owing to growth concerns. **Owing to these factors our target price gets revised to Rs. 3,235 (48x FY21E EPS) with our HOLD rating.**

Key Highlights

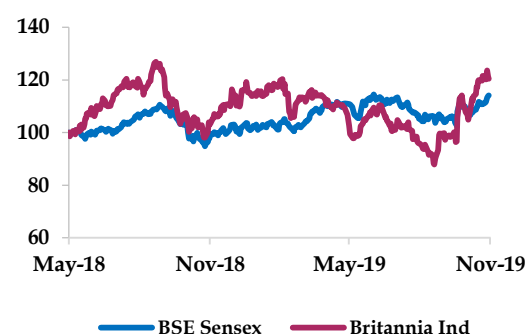
- **Q2FY20 performance –mixed performance aided by operating leverage:** Britannia reported modest growth in the quarter (in-line with our estimates) amid slowdown challenges. BRIT’s consolidated Revenue, EBITDA and PAT growth was just 6%/8% and 33% respectively with PAT growth aided by corporate tax rate reduction. Key performance metrics were 1-9% above our estimates with volume growth of 3% and a 3.2% price/mix led growth (in-line with our estimates). EBITDA Margin at 16.1% was higher by 31bps YoY (12bps GM improvement and 19bps reduction in SG&A expenses; A&SP maintained at 6% in-line with topline growth). Further owing to operating leverage the EBITDA Margin at 16.1% beat our estimates by 134bps. Recurring PAT growth was substantially up 33% YoY aided by 7x jump in other income and corporate tax rate cut announcement. Biscuits / Non-Biscuits revenue share stands at 75:25% as of Q2FY20. Non-biscuits share to rise going ahead backed by growth in adjacent businesses – Cake, Salty Snacks, Croissants and Dairy.
- **Subsidiary revenues (Consol minus Subsidiary, International + Dairy)** performance witnessed a decline of 8% YoY in revenues with EBITDA/PAT declining sharply on a YoY basis. Management highlighted that commoditized dairy business contributed to the drop in revenues alongside rise in other expenses (increased sourcing from India to Oman factory). Nepal commenced operations and is doing well with market share gains as per management.

FINANCIAL SUMMARY (Consolidated)

Y/E	Sales (Rs Cr)	EBITDA (Rs Cr)	PAT (Rs Cr)	EPS (Rs)	Change (YoY %)	P/E (x)	RoE (%)	RoCE (%)	EV/EBITDA (x)	DPS (Rs)
March										
FY19	11,054	1,733	1,159	48.2	15.3	64.0	30.2	35.7	42.4	15.0
FY20E	11,981	1,889	1,350	57.4	18.9	55.7	29.0	32.9	40.7	19.6
FY21E	13,509	2,206	1,581	67.4	17.4	47.4	29.1	33.3	34.8	23.6

Source: Company, Axis Securities; CMP as of 18th Nov 2019

PRICE PERFORMANCE



Suvarna Joshi
suvarna.joshi@axissecurities.in

Key Concall takeaways:

- Modest topline growth with beat on EBITDA against our estimates:** During Q2FY20, Net Revenue increased by a modest 7% YoY to Rs. 3,023 crore. During the quarter volume/price led growth was 3%/4% respectively. Given modest 3% inflation in its RM basket, Gross Margin expanded by 12bps YoY to 40.2%. Although, employee expenses witnessed a rise (29bps) and 47bps YoY decline in other expenses aided 31bps EBITDA Margin expansion. EBITDA Margin stood at 16.1% vs 15.8% in Q2FY29. EBITDA rose 8% YoY to Rs. 492 crore. Interest expenses surged 7x YoY to Rs. 16cr on account sharp jump its Gross Debt to Rs. 1,355 cr in the nature of working capital loan Rs. 581 cr for strategic cover of commodities upto Feb 2020 and Rs. 720 crore towards bonus debentures. Recurring PAT grew 34% YoY at Rs.404 cr aided by
- Market share gain continues amid market slowdown:** In Q2FY20, BRIT gained market share from its largest competitor, Parle and the gap has widened every year since FY13. While, distribution led gains have aided BRIT to grow faster in the Hindi belt, it highlighted that rural growth was growing faster for the company than the Industry and also as compared to the urban market. Management's commentary was guarded on near term demand recovery and highlighted that it could take another 9-12 months for the demand momentum to come back, largely due to deceleration in rural demand.
- New categories:** Company entered 4 new categories in recent past - **Wafers** (No. 3 brand with a 10% market share in less than a year of launch and widely distributed today), **Milkshakes** (no. 2 brand in the category in less than a year of launch with 20% market share), **Baked Salty Snacks** (Q2FY20 launched in West (value based snack market) owing to commercialization of Ranjangaon facility; currently in South; to become a pan-India product in a phased manner) and **Croissants** (initial issues with imported flour; now sorted; did focused launch in West Bengal & Tamil Nadu - taking product pan-India in a phased manner). While GMs are accretive on new products, further investment is required to grow them profitably. The 4 new products account for only ~3% of topline. BRIT expects its 'Treat' brand to clock revenues of Rs. 50-100cr in the next 1 year from launch.
- Premiumization:** Management highlighted that premium products continue to do well for the company. However, slowdown in value categories of the business is noted. Management is trying to innovate in the biscuit category by creating premium niches - in Q2FY20 it launched limited edition Treat Tiramisu and Treat Velvete which could help BRIT differentiate versus peers in the industry. Share of premium products is 65% of total portfolio.
- RM inflation and price hikes:** Even though BRIT noted 37% inflation in milk and 14% inflation in flour partially offset by 13% deflation in palm oil and just 1% inflation in sugar. This resulted in an overall Q2FY20 food inflation at a moderate rate of 3% as per management. Flour (14%) and Milk (37%) saw inflation, RPO prices were down 13%, while sugar inflation was 1% respectively during Q2FY20. RM

inflation is expected to be moderate going forward. Further, to combat the higher prices in some of its RMs management took a calibrated call of having forward RM covers (sufficient upto mid Q4FY20).

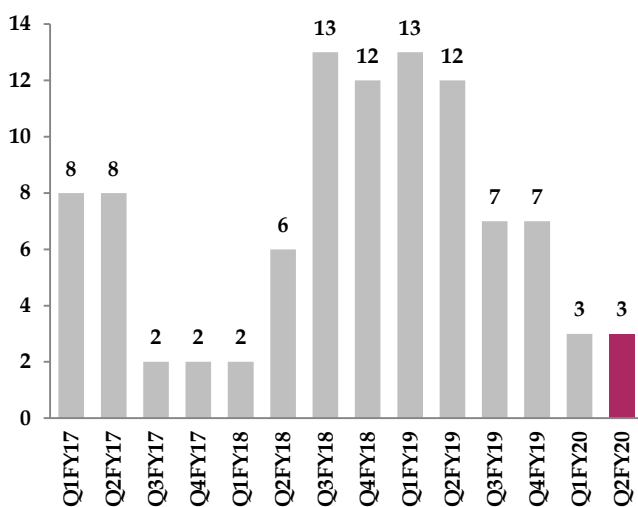
- **Other takeaways:**

- **On industry growth:** Management highlighted domestic market conditions remain tepid. Growth for the industry in value segment is less than 5% and expects the value segment growth to improve going forward. BRIT's growth in Hindi belt has particularly got impacted. Rural growth has underperformed Urban markets for the industry. However, for BRIT Rural has still grown ahead of Urban given its persistent growth in reaching into the hinterland. While the biscuit market is growing at a very slow pace (down to ~1-2%), Britannia's market share continues to expand in the space - at the expense of the its competitor (no. 2 player) and also from small players. Management expects a wait of 9-12 months for growth to return to normal levels.
- **Revenue Mix:** Biscuits and Non-biscuits share in Q2FY20 was 75:25% which is expected to be ~70%:30% over the next couple years. Further, focus is on improving profitability in breads and in reducing share of commoditized product sales in dairy business.
- **Channel Mix:** For BRIT, wholesale channel contributes to ~33% of sales which continues to be under pressure owing to tight liquidity.
- **ICDs to group companies:** About Rs. 690cr that was put in ICDs of group companies in Q4FY19 has been brought down to about Rs. 450cr bearing an interest rate of 10% on these ICDs. Management plans to bring this down by another Rs. 150 cr by fiscal year end.
- **Others:**
 - *Distribution:* 21.3 lakh direct outlets are currently reached out by BRIT same as Q1FY20. Rural preferred dealers are at 20,000 dealers (expanded by 2,000 dealers). However, given the aggressive slowdown in the market the management has taken a conscious call to go slow on pace of distribution expansion.
 - *Cost efficiencies:* Current target is 2% of revenues at ~Rs. 250cr which is incremental cost savings (cost saving target in FY19 - Rs.230cr)
 - *New categories contribution:* Of the new businesses - Milk Shakes and Wafer are GM accretive. Management highlighted that new categories constituted ~3% of sales.
 - *Share of outsourced manufacturing:* Management highlighted that as share of in-house manufacturing which stands at 60% as of Q2FY20 increases the outsourced (40%) component shall reduce gradually.
 - *Capex:* H1FY20 capex stood at Rs. 170-180cr and for FY20 management guided for Rs. 340-360cr capex. Given the slowdown in market BRIT has scaled down its investment plans and projects.

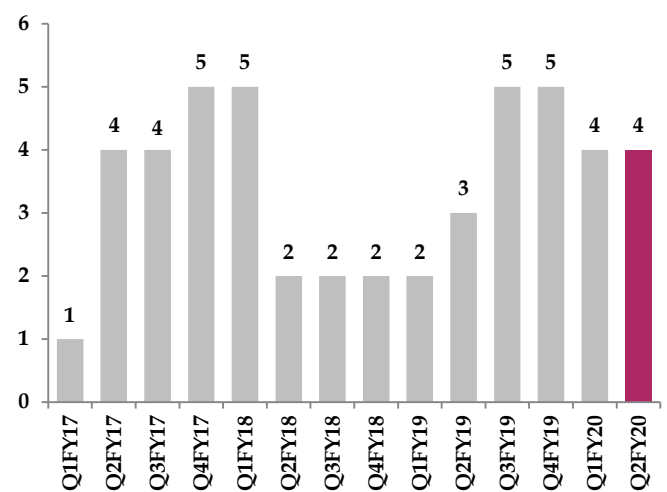
- **Outlook:** Britannia has continually reported healthy market share gain which is only seen to accelerate going forward. However, the slowdown in biscuits (core category) which forms 75% of its revenues is likely to impact its growth rates going forward (recovery unlikely soon). Traction in new categories is

good news for medium term sales growth and is also likely to be gross margin accretive and eventually EBITDA Margin accretive. While, the near term is expected to be challenging given slowdown concerns, for the long haul at lower price levels BRIT is expected to continue to deliver on earnings momentum driven by new category launches, premiumization (65% of portfolio is premium biscuits) etc to drive growth over the long term. However, despite corporate tax rate cut BRIT trades at 47x FY21E EPS which is at a premium given the reset in growth expectation and market dynamics. **We maintain HOLD but revise our TP to Rs. 3,235 (48x FY21E EPS).**

Volume growth (%)

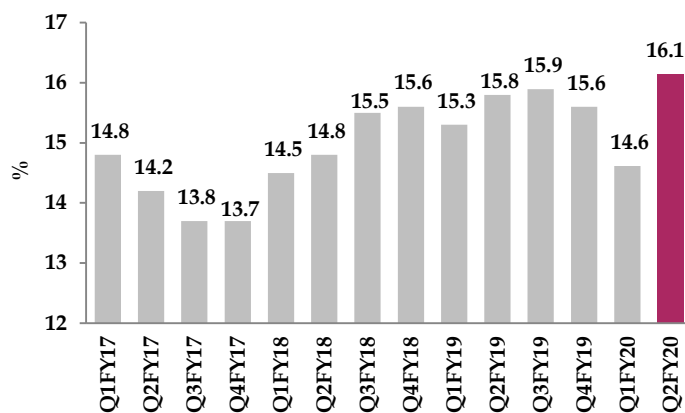


Price/Mix growth (%)

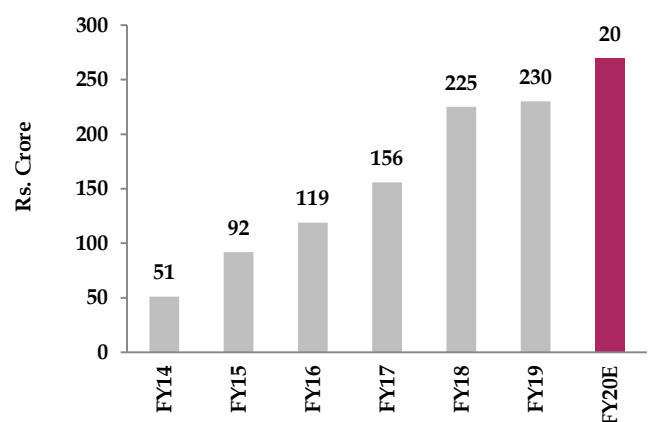


Source: Company, Axis Securities

EBITDA Margin improved aided by op. leverage and mix

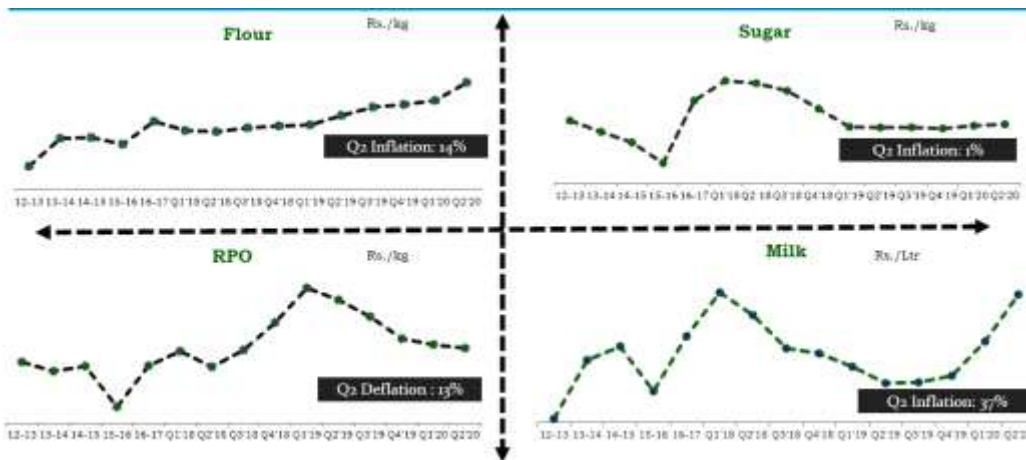


Cost Saving initiative to improve EBITDA Margin



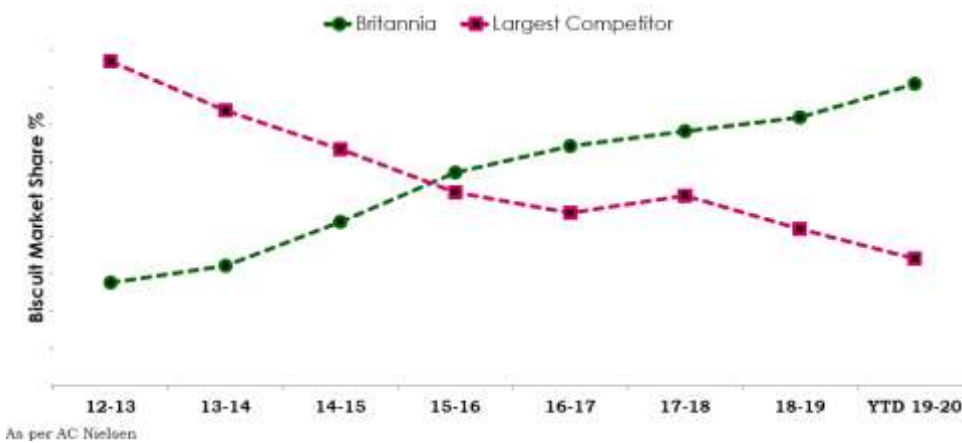
Source: Company, Axis Securities

Overall commodity inflation moderate at 3% in Q2FY20



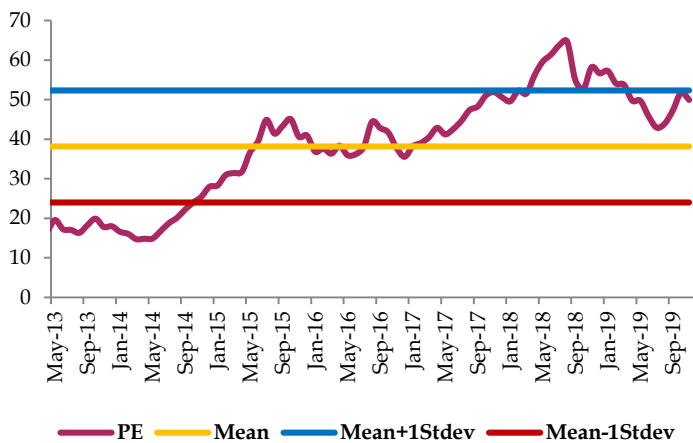
Source: Company, Axis Securities

Acceleration in market share gains continued even in Q2FY20

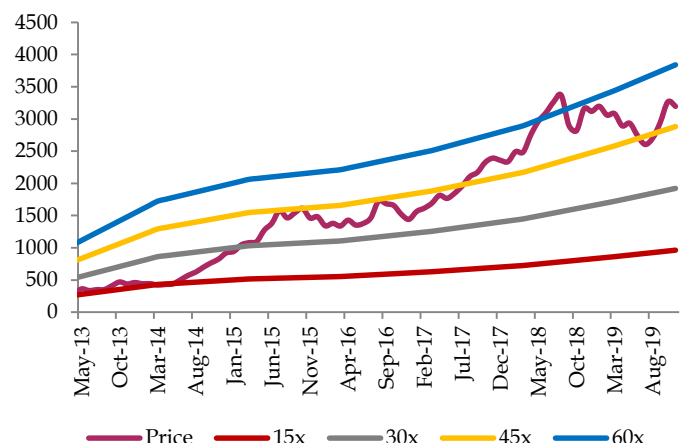


Source: Company, Axis Securities

P/E Band



12 month Forward P/E (x)



Source: Company, Axis Securities

Results Update

(Rs.Cr.)	Quarterly Performance				
	Q2FY20	Q2FY19	% Change (YoY)	Q1FY20	% Change (QoQ)
Net Sales	3,023	2,855	5.9	2,677	12.9
Other Op. Inc	26	15		23	
Total Revenue	3,049	2,870	6.2	2,700	12.9
GM	40.2	40.0		40.4	
Expenditure					
Net Raw Material	1,824	1,720	6.0	1,609	13.4
Employee expenses	124	108	14.4	121	2.5
Other Exp	609	587	3.8	576	5.7
Total Expenditure	2,557	2,415	5.9	2,306	10.9
EBIDTA	492	454	8.3	395	24.7
EBITDA Margin (%)	16.1%	15.8%		14.6%	
Oth. Inc.	68	44	55.0	67	1.0
Interest	16	2	567	10	59.8
Depreciation	45	37	22	45	0.2
Exceptional Item	0	0		0	
PBT	499	459	8.8	407	22.6
Tax	96	156	(38.7)	143	
PAT	404	303	33.2	264	52.8
EPS (Rs.)	16.8	12.6	33.2	11.0	52.8
Key Ratios					
Gross Margin (%)	40.2	40.0	+12bps	41.2	-24bps
EBITDA Margin (%)	16.1	15.8	+31bps	15.6	+153bps
PAT Margin (%)	13.2	10.6	+265bps	10.5	+345bps
Cost Analysis					
RM Costs (%)	59.8	60.0	-12bps	59.6	+24bps
Employee Cost (%)	4.1	3.8	+29bps	4.5	-41bps
Other Expenses (%)	20.0	20.4	-47bps	21.3	-136bps

Source: Company, Axis Securities

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