

**₹ 3114**

## VST Industries (VSTIND)

### Premium brands to aid profitability...

- VST Industries reported strong revenue growth of 26.5% to ₹ 279.1 crore on a comparable basis with cigarettes and tobacco segments contributing ₹ 209.6 crore and ₹ 90 crore to revenues, respectively. Cigarette volumes were flat during the quarter and for FY18. The contribution of 64 mm and 69 mm category cigarettes to the topline was in the ratio of 50:50. Premium brands *Total* and *Edition* contributed 20% to overall volumes
- With the increasing contribution of premium brands, operating profit witnessed a considerable jump of 25.6% for the quarter YoY to ₹ 79.6 crore (I-direct estimate: ₹ 71.2 crore). EBITDA margin came in at 28.5%, similar to the corresponding quarter, as employee and other expenses were curtailed vs. the run rate of previous quarters. Net profit for the quarter, thus, jumped 35.9% YoY to ₹ 48.3 crore (I-direct estimate: ₹ 41.8 crore)

### Realisation to lead growth, going ahead; volume growth to recover

In FY18, cigarette volumes remained flat on account of a steep rise in tax incidence. The company took a price hike to the tune of 10% in the year largely passing on the increase in the indirect tax incidence post GST implementation. We estimate 9.0% and 10.0% realisation increase for FY19E and FY20E, respectively. Given the steep price hike in the current year resulting in flat volumes for FY18, we expect a volume recovery in 3% and 2% growth in FY19E and FY20E, respectively, largely on the back of a favourable product mix towards high priced cigarettes in the regular & king size category. Thus, we estimate net revenue CAGR of 11.4% in FY18-20E to ₹ 1176 crore.

### EBITDA/stick to improve with favourable product mix

VST Industries, with 7.5% volume market share, is a prominent player in the low priced cigarette (₹ 3.0-5.0/stick) segment in India (brands: *Charms*, *Charminar*, *Kingston*, *Moments*, premium: *Total* & *Edition*). Over time, VST has shifted its product mix towards lower length cigarettes, which attracted lower tax (aiding volume) and also launched premium cigarettes – *Total*, under 69 mm at price point of ₹ 6 (contributing ~15% to the total mix) and *Edition*, under King's size at price point of ₹ 10 (~5% contribution to total mix). Currently, Charms remain the largest brand for VST contributing more than 20% of sales. With a favourable product mix and price hikes, we estimate the EBITDA/stick will increase from ₹ 0.38 in FY18 to ₹ 0.41 in FY19E and ₹ 0.47 in FY20E.

### Dividend payout to remain encouraging

VST's dividend payouts increased from 52.9% in FY08 to 65.8% in FY18 on account of robust profitability and free cash flows over the same period. The company's profitability has increased at 12.1% CAGR in FY08-18 while FCF has grown at 10.9% CAGR in FY08-18. Going ahead, with no major capex requirement, we expect the payout to remain elevated at 64.7% and 68.5% for FY19E and FY20E, respectively.

### Favourable mix of premium cigarettes to drive profitability; maintain BUY

Increased tax incidence and, thus, the muted consumption environment is expected to restrict any significant volume growth. However, with the improving product mix towards high margin products (contributing ~20% currently to total volumes), EBITDA/stick is estimated to increase to ₹ 0.47 per stick. We reiterate **BUY** recommendation on the stock with a target price of ₹ 3900/share, valuing it at 24.3x FY20E earnings.

Rating matrix		
Rating	:	Buy
Target	:	₹ 3900
Target Period	:	12-15 months
Potential Upside	:	25%

What's changed?		
Target		Unchanged
EPS FY19E	Changed from ₹ 144.5 to ₹ 139.1	
EPS FY20E	Changed from ₹ 163.5 to ₹ 160.4	
Rating		Unchanged

Quarterly performance					
	Q4FY18	Q4FY17	YoY (%)	Q3FY18	QoQ (%)
Sales	278.8	220.4	26.5	238.7	16.8
EBITDA	79.6	63.4	25.6	79.9	-0.4
EBITDA (%)	28.5	28.7	-23 bps	33.4	-491 bps
PAT	48.3	35.6	35.9	49.8	-2.9

Key financials				
₹ Crore	FY17	FY18	FY19E	FY20E
Gross Sales	918.3	946.4	1,070.4	1,174.6
EBITDA	247.8	294.8	328.1	375.6
Net Profit	151.5	181.9	214.9	247.8
EPS (₹)	98.1	117.8	139.1	160.5

Valuation summary				
	FY17	FY18	FY19E	FY20E
P/E	31.8	26.5	22.4	19.4
Target P/E	39.7	33.1	28.0	24.3
Div. Yield	2.4	2.5	2.9	3.5
Mcap/Sales	5.2	5.1	4.5	4.1
RoNW (%)	28.1	31.3	33.4	34.0
RoCE (%)	42.0	46.9	47.5	48.4

Stock data	
	Amount
Market Capitalization (₹ Crore)	4,814.8
Total Debt (FY18) (₹ Crore)	0.0
Cash and Investments (FY18) (₹ Crore)	451.7
EV (₹ Crore)	4,363.1
52 week H/L	3774 / 2092
Equity capital	₹ 15.4 crore
Face value	₹ 10

Price performance				
% change	1M	3M	6M	12M
VST Industries	5.7	-1.7	3.8	4.3
ITC	-3.0	-2.1	-1.9	-7.0
Godfrey Phillips	6.7	-15.3	-13.4	-20.6

### Research Analyst

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**Variance analysis**

	Q4FY18	Q4FY18E	Q4FY17	YoY (%)	Q3FY18	QoQ (%)	Comments
Net Revenue	278.8	262.6	220.4	26.5	238.7	16.8	Net sales witnessed growth of 26.5% to ₹ 279.1 crore led by cigarette business contributing ₹ 209 crore to sales
Other Operating Income	0.3	3.5	0.6	-45.8	0.3	14.3	
Raw Material Expenses	153.5	136.9	105.0	46.2	116.6	31.6	
Employee Expense	25.2	25.0	24.0	4.9	21.2	19.0	
Excise Duty	20.8	0.0	347.3	-94.0	18.0	15.5	
Other operating Expenses	20.8	29.5	28.1	-25.8	21.3	-2.2	
EBITDA	79.6	71.2	63.4	25.6	79.9	-0.4	Operating profit increased 25.6% to ₹ 79.6 crore considering premium brands <i>Total &amp; Edition</i> contributed ~20% to sales
EBITDA Margin (%)	28.5	27.1	28.7	-23 bps	33.4	-491 bps	
Depreciation	11.1	9.9	10.5	5.0	9.4	18.3	
Interest	0.0	0.0	0.0	NA	0.0	NA	
Other Income	7.8	1.0	4.2	84.4	5.5	43.2	
PBT	76.4	62.3	57.1	33.8	76.0	0.5	
Tax Outgo	28.0	20.4	21.5	30.4	26.2	6.9	
PAT	48.3	41.8	35.6	35.9	49.8	-2.9	Led by higher EBITDA, net profit witnessed growth of 36% to ₹ 48.3 crore

**Key Metrics**

Cigarette Sales (₹ crore)	209.6	175.7	168.9	24.1	196.7	6.6	Cigarettes volume growth was flat during the quarter.
Tobacco Sales (₹ crore)	90.0	63.0	65.0	38.5	60.0	50.0	

Source: Company, ICICIdirect.com Research

**Change in estimates**

(₹ Crore)	FY19E			FY20E			Comments
	Old	New	% change	Old	New	% change	
Net sales	1,087.7	1,070.4	-1.6	1188.6	1174.6	-1.2	We marginally tweak our FY19E & FY20E estimates
EBITDA	342.0	328.1	-4.1	385.7	375.6	-2.6	
EBITDA Margin (%)	31.4	30.6	-83 bps	32.5	32.0	-48 bps	
PAT	223.2	214.9	-3.7	252.4	247.8	-1.8	
EPS (₹)	144.5	139.1	-3.7	163.5	160.5	-1.8	

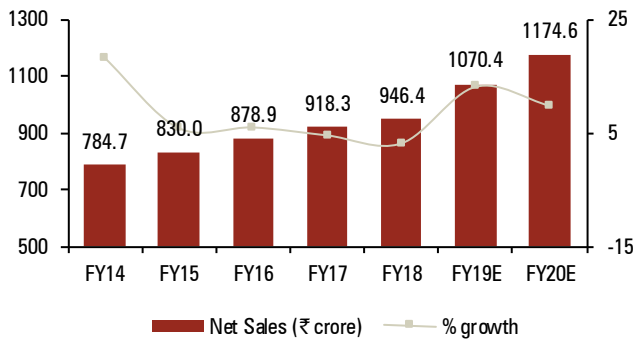
Source: Company, ICICIdirect.com Research

**Assumptions**

	Current				Earlier		Comments
	FY17	FY18	FY19E	FY20E	FY19E	FY20E	
Cig. Vol. (mn sticks)	7,258.7	7,302.2	7,521.3	7,671.7	7,476.4	7,626.0	We expect 3% & 2% volume growth in FY19E & FY20E
Cig. Vol. Growth (%)	-1.0	0.6	3.0	10.0	3.0	2.0	
Realization/cig (₹)	2.8	2.9	3.2	3.5	9.0	10.0	
Tobacco Sales(₹ crore)	275.0	250.0	262.6	273.3	262.6	273.3	
% of <64mm in sales	55.0	50.0	50.0	50.0	50.0	50.0	
% of >64mm in sales	45.0	50.0	50.0	50.0	50.0	50.0	

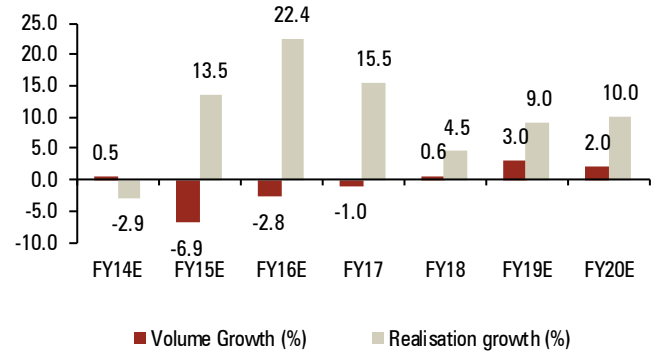
Source: Company, ICICIdirect.com Research

**Exhibit 1: Net revenue to grow at CAGR of 11.4 % over FY18-20E...**



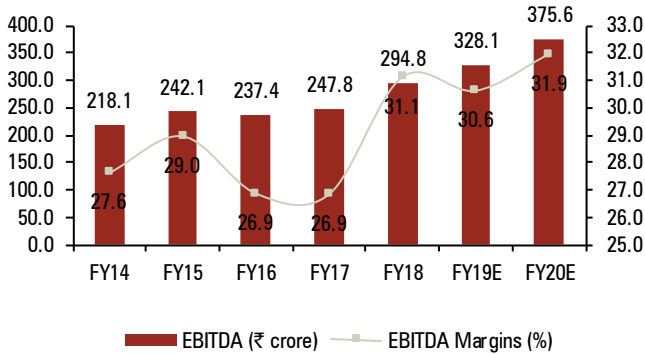
Source: Company, ICICIdirect.com Research

**Exhibit 2: ...led by realisation growth; volume growth to remain muted**



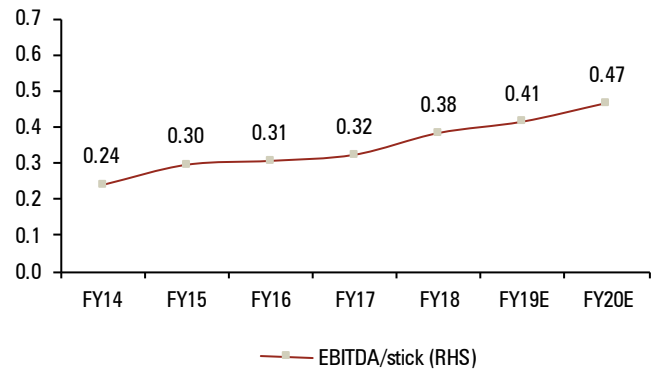
Source: Company, ICICIdirect.com Research

**Exhibit 3: Improved product mix to aid EBITDA margin expansion**



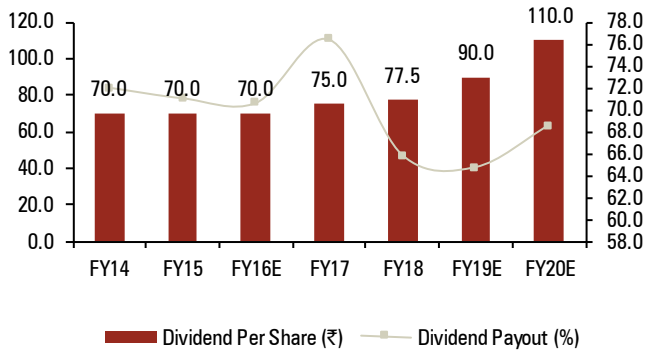
Source: Company, ICICIdirect.com Research

**Exhibit 4: Healthy growth in EBITDA/stick (₹)**



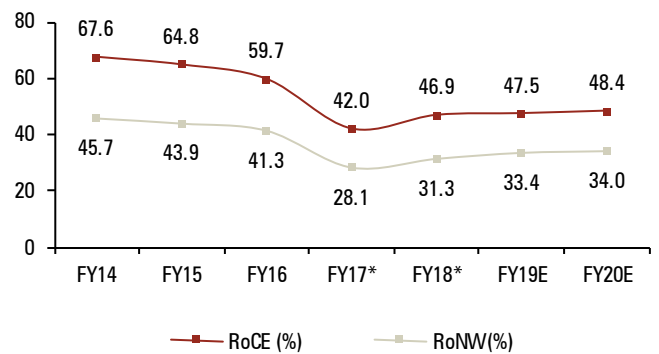
Source: Company, ICICIdirect.com Research

**Exhibit 5: High dividend payout to continue**



Source: Company, ICICIdirect.com Research

**Exhibit 6: Return ratios to improve**



Source: Company, ICICIdirect.com Research; \* Not comparable to previous years due to change in accounting standard

## Outlook & valuation

We expect VST to clock net revenue CAGR of 11.4% in FY18-20E, primarily led by 12.2% growth in cigarettes sales on account of realisation CAGR of 9.5% over the same period. We expect volumes to recover in FY19E & FY20E from flat growth for FY18 to 3% & 2% growth for FY19E and FY20E. EBITDA for the company is expected to grow at a CAGR of 12.9% in FY18-20E with EBITDA margin of 31.9% in FY20E. Thus, with increase in tax incidence and similar price hike undertaken coupled with an improved revenue mix, the EBITDA/stick is estimated to grow at a CAGR of 11.2% in FY18-20E. Thus, PAT is estimated to grow at 16.7% CAGR in FY18-20E.

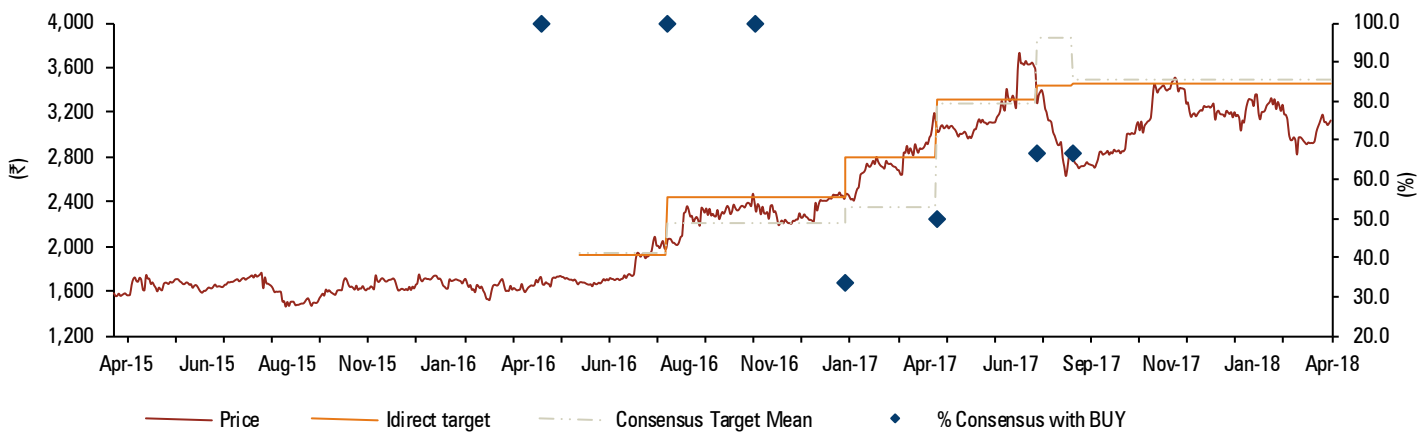
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### Exhibit 7: Valuations

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY17	924.7	5.2	103.7	4.6	30.1	19.2	29.8	43.6
FY18	946.4	2.4	117.8	13.6	26.5	16.1	31.3	46.9
FY19E	1070.4	13.1	139.1	18.1	22.4	13.8	33.4	47.5
FY20E	1174.6	9.7	160.5	15.4	19.4	11.9	34.0	48.4

Source: Company, ICICIdirect.com Research

### Recommendation history vs. Consensus



Source: Bloomberg, Company, ICICIdirect.com Research

### Key events

Date	Event
Apr-09	Final dividend of ₹ 30/share on closing share price of ₹ 213 yielding a dividend of 14.1%
Apr-10	Final dividend of ₹ 30/share; margins decline significantly to 17.6%
Apr-11	Final dividend of ₹ 45/share; margins improve by robust 1050 bps YoY to 28.1%
Jan-12	Profits decline ~10% YoY with volume growth in cigarettes declining ~9% YoY
Feb-12	Gol increases excise duty on cigarettes above 65 mm by ~21% in FY13 Budget
Apr-12	Final dividend of ₹ 65/share
Sep-12	Profitability declines ~17% YoY led by muted sales growth of ~6% and decline in margins by ~690 bps YoY to 24.6%
Apr-13	Volume growth in cigarettes or FY13 comes in ~13% lower with a margin decline of ~600 bps to 27%. Profits also remain lower by ~11% for the year
Jul-14	Government increases excise duty on <65 mm segment cigarettes by ~72% and other lengths by 11-21%
Feb-15	Excise duty on below 65 mm category increased by 25% with above 65 mm category increased by 15% in Union Budget FY16
Feb-16	Excise hike of 10% on cigarettes in Budget 2016
Feb-17	Government announces a 6% hike in excise duty across categories of cigarette
Jul-17	Ad valorem VAT replaced by GST rate of 28% and excise duty replaced by GST compensation cess of 5% plus specific duty as per the cigarette size
Jul-17	GST Council raises specific cess on cigarettes in all categories below 75 mm

Source: Company, ICICIdirect.com Research

### Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	British American Tobacco PLC	31-Dec-17	31.73	4.9	0.0
2	Bright Star Investments Pvt. Ltd.	31-Dec-17	25.95	4.0	0.0
3	HDFC Asset Management Co., Ltd.	31-Dec-17	8.88	1.4	0.0
4	Matthews International Capital Management, L.L.C.	31-Dec-17	8.54	1.3	0.0
5	DSP BlackRock Investment Managers Pvt. Ltd.	31-Dec-17	2.41	0.4	0.0
6	ICICI Lombard General Insurance Company Ltd.	31-Dec-17	2.11	0.3	0.0
7	The New India Assurance Co. Ltd.	31-Dec-17	1.53	0.2	0.0
8	IDBI Asset Management Limited	31-Mar-18	0.75	0.1	0.0
9	Fidelity Management & Research (Hong Kong) Limited	28-Feb-18	0.47	0.1	0.0
10	Rothmans International Enterprises, Ltd.	31-Dec-17	0.43	0.1	0.0

Source: Reuters, ICICIdirect.com Research

### Shareholding Pattern

(in %)	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17
Promoter	32.2	32.2	32.2	32.2	32.2
FII	10.4	10.3	10.1	9.5	9.5
DII	14.3	14.4	14.7	14.6	14.6
Others	43.2	43.2	43.1	43.7	43.7

### Recent Activity

Buys			Sells		
Investor name	Value	Shares	Investor name	Value	Shares
DSP BlackRock Investment Managers Pvt. Ltd.	0.41m	0.01m	Fidelity Management & Research Company	-0.48m	-0.01m
State Street Global Advisors (US)	0.07m	0m	ICICI Lombard General Insurance Company Ltd.	-0.24m	-0.00m
			Kotak Mahindra Asset Management Company Ltd.	-0.23m	0m
			Tata Asset Management Limited	-0.18m	0m
			Axis Asset Management Company Limited	-0.16m	0m

Source: Reuters, ICICIdirect.com Research

## Financial summary

Profit and loss statement		₹ Crore			
(Year-end March)	FY17	FY18	FY19E	FY20E	
Gross Revenue	922.4	947.6	1071.6	1176.0	
Growth (%)	4.5	2.7	13.1	9.7	
Raw Material Expenses	468.4	470.3	499.5	532.6	
Employee Expenses	89.7	89.2	103.8	113.9	
Excise Duty	1,338.9	411.1	1,566.0	1,762.0	
Administrative Expenses	0.0	0.0	0.0	0.0	
Other expenses	116.6	93.3	140.2	153.9	
Total Operating Expenditure	674.6	652.8	743.5	800.4	
EBITDA	247.8	294.8	328.1	375.6	
Growth (%)	4.4	19.0	11.3	14.5	
Depreciation	36.9	39.2	40.0	42.1	
Interest	0.0	0.0	0.0	0.0	
Other Income	0.0	0.0	0.0	0.0	
PBT	230.9	279.5	306.9	354.1	
Others	20.1	23.8	18.9	20.6	
Total Tax	79.4	97.6	92.1	106.2	
PAT	151.5	181.9	214.9	247.8	
Growth (%)	-1.0	20.0	18.1	15.3	
EPS (₹)	98.1	117.8	139.1	160.5	

Source: Company, ICICIdirect.com Research

Cash flow statement		₹ Crore			
(Year-end March)	FY17E	FY18	FY19E	FY20E	
Profit after Tax	151.5	181.9	214.9	247.8	
Add: Depreciation	36.9	39.2	40.0	42.1	
(Inc)/dec in Current Assets	35.1	-239.3	516.5	-24.4	
Inc/(dec) in CL and Provisions	-199.6	220.1	-347.7	11.7	
CF from operating activities	23.9	201.9	423.8	277.3	
(Inc)/dec in Investments	0.5	-0.3	0.6	-0.1	
(Inc)/dec in Fixed Assets	-43.1	-47.6	-45.8	-30.0	
(Inc)/dec in LT Loans & Adv.	5.0	0.0	0.0	0.0	
Others	-4.6	2.4	-10.9	0.3	
CF from investing activities	-42.2	-45.4	-56.2	-29.8	
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0	
Inc/(dec) in loan funds	0.0	0.0	0.0	0.0	
Dividend paid & dividend tax	0.0	-135.5	-140.0	-162.6	
Inc/(dec) in Reval. Reserve	0.0	0.0	0.0	0.0	
Inc/(dec) in Exch. Fluc. Res.	0.0	0.0	0.0	0.0	
CF from financing activities	0.0	-135.5	-140.0	-162.6	
Net Cash flow	-18.3	20.9	227.6	84.8	
Opening Cash	21.2	3.0	23.9	251.5	
Closing Cash	3.0	23.9	251.5	336.3	

Source: Company, ICICIdirect.com Research

Balance sheet		₹ Crore			
(Year-end March)	FY17	FY18	FY19E	FY20E	
<b>Liabilities</b>					
Equity Capital	15.4	15.4	15.4	15.4	
Reserve and Surplus	523.5	566.7	627.8	713.0	
Total Shareholders funds	539.0	582.1	643.2	728.4	
Total Debt	0.0	0.0	0.0	0.0	
Long Term Provisions	10.9	14.2	3.2	3.5	
Total Liabilities	549.9	596.2	646.4	732.0	
<b>Assets</b>					
Gross Block	526.9	556.9	586.9	616.9	
Less: Acc Depreciation	306.9	346.1	386.1	428.3	
Net Block	220.0	195.1	200.8	188.7	
Capital WIP	0.8	34.2	34.2	34.2	
Deferred Tax Asset	23.0	24.8	24.8	24.8	
Non Current Investments	1.8	2.0	1.5	1.6	
LT Loans & Advances/Others	4.2	3.2	3.2	3.2	
<b>Current Assets</b>					
Inventory	329.3	252.9	155.4	170.6	
Debtors	12.0	27.3	5.9	6.4	
Cash	19.9	37.6	251.5	336.3	
Loans & Advances	0.0	0.0	7.3	8.0	
Current Investments	171.8	414.1	82.1	90.1	
Other CA	14.8	73.0	0.0	0.0	
<b>Current Liabilities</b>					
Creditors	56.0	58.1	26.4	29.0	
Provisions	0.0	0.0	0.0	0.0	
Other CL	191.8	409.8	93.8	103.0	
Net Current Assets	300.1	337.0	381.9	479.5	
Total Assets	549.9	596.2	646.4	732.0	

Source: Company, ICICIdirect.com Research

Key ratios					
(Year-end March)	FY17	FY18	FY19E	FY20E	
<b>Per share data (₹)</b>					
EPS	98.1	117.8	139.1	160.5	
Cash EPS	122.0	143.2	165.1	187.8	
BV	349.0	377.0	416.5	471.8	
DPS	75.0	77.5	90.0	110.0	
Cash Per Share	12.9	24.3	162.8	217.8	
<b>Operating Ratios (%)</b>					
EBITDA Margin	26.9	31.1	30.6	31.9	
PBT / Net Sales	25.1	29.5	28.7	30.1	
PAT Margin	16.5	19.2	20.1	21.1	
Inventory days	130.9	97.5	53.0	53.0	
Debtor days	4.8	10.5	2.0	2.0	
Creditor days	22.3	22.4	9.0	9.0	
<b>Return Ratios (%)</b>					
RoE	28.1	31.3	33.4	34.0	
RoCE	42.0	46.9	47.5	48.4	
RoIC	42.2	50.1	86.9	100.5	
<b>Valuation Ratios (x)</b>					
P/E	31.8	26.5	22.4	19.4	
EV / EBITDA	19.3	16.1	13.8	11.9	
EV / Net Sales	5.2	5.0	4.2	3.8	
Market Cap / Sales	5.2	5.1	4.5	4.1	
Price to Book Value	8.9	8.3	7.5	6.6	
<b>Solvency Ratios</b>					
Debt/EBITDA	0.0	0.0	0.0	0.0	
Debt / Equity	0.0	0.0	0.0	0.0	
Current Ratio	2.1	1.6	2.1	2.1	
Quick Ratio	0.8	1.1	0.8	0.8	

Source: Company, ICICIdirect.com Research

## ICICIdirect.com coverage universe (FMCG)

Sector / Company	CMP			M Cap (₹ Cr)	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)	Rating		FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E
Colgate (COLPAL)	1,100	1,120	Hold	29,918	21.2	22.9	24.1	51.8	48.1	46.4	6.7	6.8	6.1	64.1	64.0	62.6	45.3	46.1	45.1
Dabur India (DABIND)	344	390	Buy	62,180	7.2	7.6	8.5	47.5	45.5	45.9	8.1	7.7	6.9	28.0	26.2	26.9	26.4	24.0	24.2
GSK CH (GLACON)	5,982	6,740	Buy	25,111	156.1	166.7	192.8	38.3	35.9	35.0	5.7	5.7	5.1	30.8	29.6	30.7	21.0	20.2	21.3
Hindustan Unilever (HINLEV)	1,403	1,360	Hold	295,704	20.8	23.4	27.2	67.5	59.9	50.0	8.7	8.6	7.6	74.9	88.1	105.8	66.6	74.7	89.0
ITC Limited (ITC)	261	320	Buy	327,190	8.4	8.7	9.9	31.1	29.9	32.5	8.3	8.4	7.3	32.9	29.9	34.3	22.5	21.0	23.8
Jyothy Lab (JYOLAB)	372	420	Buy	6,788	11.1	7.5	9.3	33.5	49.6	45.0	4.0	4.1	3.6	28.1	25.5	28.6	30.9	20.6	24.1
Marico (MARLIM)	317	362	Hold	40,674	6.3	6.7	7.9	50.4	47.2	45.9	6.9	6.1	5.2	44.6	42.2	44.4	34.9	33.4	35.4
Nestle (NESIND)	8,700	8,600	Buy	72,797	103.9	127.1	154.9	83.8	68.5	55.5	7.7	7.2	6.2	34.9	37.3	44.7	36.2	36.8	41.7
Prabhat Dairy (PRADAI)	179	215	Buy	1,797	4.8	5.7	8.6	38.3	32.5	21.5	1.3	1.1	1.0	8.0	9.1	12.5	5.1	6.1	9.4
VST Industries (VSTIND)	3,114	3,900	Buy	4,815	98.1	117.8	139.1	31.7	26.4	28.0	5.2	5.1	4.5	42.0	46.9	47.5	28.1	31.3	33.4
Varun Beverage (VARBEV)	664	590	Buy	11,942	11.7	15.4	22.3	55.8	42.6	29.4	3.0	2.4	2.2	12.8	14.9	18.9	10.5	12.7	16.8

Source: Company, ICICIdirect.com Research

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