

PRABHAT DAIRY

Stable sales; milk procurement volumes to pick up

India Equity Research | Dairy



Prabhat Dairy (Prabhat) reported sales growth of 9% YoY to INR2.9bn, driven by growth in SMP (40%), ghee (60%) and curd (22%). However, EBITDA fell 8% YoY with margins dipping to 8.5% (10% in Q1FY16) due to gross margins contracting 125bps YoY to 19.2%, as milk procurement prices increased on droughts conditions in Maharashtra. Driven by fall in interest cost and lower tax, PAT surged 64% YoY. Given expected 20% EBITDA CAGR (led by increase in value-added sales), strong 72% earnings CAGR, and 387bps jump in adjusted pre-tax RoCE to 15.1% (17.1% including incentives) over FY16-18E, we maintain 'BUY' with an unchanged target price of INR144.

Revenue growth driven by SMP, curd and ghee; cheese picking up

Prabhat reported revenue of INR2.9bn, up 9% YoY (versus 2% growth reported by Parag and 5% growth in dairy sales reported by Heritage Foods). This was driven by strong growth in SMP (surged 40% YoY) and ghee & butter (soared 60% YoY), led by pick up in Maharashtra and northern parts of India. Similarly, curd also posted 22% YoY growth this quarter. Distribution for curd also ramped up significantly. Earlier available through 7-8,000 outlets, distribution has expanded to >10,000 outlets. The company also launched the Prabhat 'Ghar jaisa dahi' campaign during the quarter. It made good progress in cheese. *Prabhat received orders from Yum Brands and also began exporting cheese to the Middle East. Current utilisation in cheese stands at ~15% and the company plans to take this to 35-40% in FY18 and ~65-70% in FY19.*

Margins fall; procurement to pick up, targets 17% CAGR (FY16-18)

The average milk procurement prices increased from INR21/litre last quarter to INR25/litre (Q1FY16: INR18/litre). Further, procurement also fell to 0.76mn litres/day compared to 0.93mn litres/day in Q1FY16. As a result, gross margins corrected by 125bps YoY to 19.2%. However, management expects procurement to scale back to 1mn litres in coming quarters, and to 1.4mn litres over the next 2-3 years.

Outlook and valuations: Story intact; maintain 'BUY'

We estimate Prabhat to clock revenue/PAT CAGR of 17%/72% over FY16-18, with adjusted pre-tax RoCE of 15.1% (17.1% including incentives) in FY18. In light of robust earnings visibility and strong growth in the organised dairy space, we continue to value the stock at 18x FY18E EPS with an unchanged target price of INR144.

Financials (Consolidated)						(INR mn)		
Year to March	Q1FY17	Q1FY16	% change	Q4FY16	% change	FY16	FY17E	FY18E
Net rev.	2,931	2,689	9.0	3,083	(4.9)	11,705	13,174	16,009
EBITDA	248	270	(8.1)	278	(10.9)	1,192	1,224	1,712
Adj. PAT	60	37	64.4	82	(26.5)	245	375	724
Adj. Dil. EPS (INR)	0.6	0.5	20.2	0.8	(26.5)	2.5	3.8	7.4
Diluted P/E (x)						36.1	23.6	12.2
EV/EBITDA (x)						8.7	8.7	5.9
ROAE (%)*						5.6	6.2	11.1

*Adjusted for revaluation reserves, not including sales tax incentives

EDELWEISS RATINGS			
Absolute Rating		BUY	
Investment Characteristics		Growth	
MARKET DATA (R: , B: PRABHAT IN)			
CMP	: INR 91		
Target Price	: INR 144		
52-week range (INR)	: 169 / 71		
Share in issue (mn)	: 97.7		
M cap (INR bn/USD mn)	: 9 / 132		
Avg. Daily Vol. BSE/NSE ('000)	: 283.6		
SHARE HOLDING PATTERN (%)			
	Current	Q4FY15	Q3FY15
Promoters *	44.2	44.2	43.8
MF's, FI's & BKs	3.5	3.4	5.6
FII's	28.1	27.6	26.1
Others	24.2	24.7	24.5
* Promoters pledged shares (% of share in issue)		:	NIL
RELATIVE PERFORMANCE (%)			
	Sensex	Stock	Stock over Sensex
1 month	0.7	14.7	14.0
3 months	7.4	(11.3)	(18.7)
12 months	9.7	(21.7)	(31.4)

Shradha Sheth
+91 22 6623 3308
shradha.sheth@edelweissfin.com

Nihal Mahesh Jham
+91 22 6623 3352
nihal.jham@edelweissfin.com

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Q1FY17 highlights

- The quarter was lean due to lower availability of milk and severe draught in Maharashtra in past 2 years.
- Last 2 consecutive years of drought had severely affected milk availability and prices.
- Achieved revenue growth through judicious mix and focus on value-added products.
- Confident of increasing procurement this year.
- Launched Prabhat 'Ghar jaisa dahi' campaign.
- The company is looking to increase modern trade presence beyond Maharashtra and Gujarat this year.
- Share of value-added has increased from 76% to 82% (as per Prabhat's definition).
- Other expenses have fallen as conversion charges were lower due to lower milk procurement.
- Inventory up 20-25% from Q4 mainly due to cheese and milk powder.

Milk prices

- Ghee and butter revenues grew 60% YoY.
- Gross margins fell due to higher milk prices and milk procurement efforts.
- Procurement:
 - Q1FY16: 0.93mn litres
 - Q1FY17: 0.76mn litres
 - Can expect this to be back to 1mn litres in coming quarters
- Used SMP from own stocks and purchased butter and fat from outside
- Average price paid for milk was INR25/litre. Q4FY16 price was INR21/litre
- Wants to take procurement to 1.4mn litres in next 3 years

Products

- Liquid milk sales this quarter: 13mn litres
- SMP and specialty powder revenues grew by 40%
- Ghee and butter revenues grew 60% YoY
- Ghee has picked up in Maharashtra and northern parts of India. It is available at ~55,000 outlets.
- Cheese:
 - Received orders from Yum Brands for cheese and exports of cheese and SCM to the Middle East
 - Already procured orders from major QSR chains in India
 - In Q1, the company has seen a good establishment in a lot of QSR.
 - In Q1, the company established a good distribution network across the country
 - Mix is 50:50 between large QSR's and HORECA

- Overall capacity utilisation is below 15% currently
- Next year it will be 35-40%. Post that, it will be 65-70%.
- Prabhat is clocking Volumes: 2-3MT/day of cheese this year and expects to ramp this up to 8MT/day by next year
- Closely working with large-scale QSR's since past 2 years
- Not making significant margins on cheese right now
- Cheese competition:
 - Indian market is growing at 25% plus. Institutional market constitutes 70% on which Prabhat is focusing on
 - Main players are Amul, Parag, Dynamix and Prabhat
 - The time has come where this business has started growing exponentially driven by:
 - Modern trade, home delivery, restaurants
 - Cheese consumption is not only increasing in larger towns, but also in smaller towns
 - There are very limited players in cheese given the requirement of high-quality milk
 - The company's cheese prices are at par with competition as quality is very high
 - Every buyer has minimum 2-3 players it procures from
- Ingredients business:
 - Major part of ingredients business comes from condensed milk
 - In SMP, for majority of its clients Prabhat works on cost plus model. The company was EBITDA positive
 - SMP realisations are down, but fat realisation has gone up. So, net it was the same
 - SCM (condensed milk) in the Middle East also started since we are a large player in SCM exports holds huge potential
- Curd:
 - Via the 'Ghar Jaisa Dahi' campaign, Prabhat opened a lot of new outlets and customers
 - Increased distribution. Earlier, it was only available in New Mumbai but now it has reached Western and Central Mumbai too
 - As revenues/distribution of dahi increases, it gives a leg to distribution for other products
 - Earlier, was available at 7-8,000 outlets, now it is available at more than 10,000 outlets
 - Has been doing 200tonnes/month and by year end it will be higher. Envisages 25-30% growth

Others:

- Prabhat is present in more than 11 states in operations
- The company is focusing on Below the line (BTL) advertising rather than Above the line (ATL) market. Focus is not on wresting market share from competitors, but to achieve a shift from unorganised segment to organised market.
- **VAT refund:**
 - Prabhat has already received the eligibility certificate. The company expects the payout this year only.
 - First VAT refund will be ~INR150mn which is expected to accrue this year
- The company is looking at increasing yield and higher cattle per farmer and more farmers per village. It is increasing penetration, which is just 30-40% at present.

Guidance:

- Prabhat will be in the full tax bracket this year
- Net debt:
 - Q4FY16: INR1.5bn
 - Q1FY17: ~INR1.7bn
- Major expansion of gross margins will come from consumer business. It is in the 26-34% margin range whereas ingredient is 16-18%
- In last few years, clocked 60% CAGR in B2C. Looking at increasing B2C mix from 30% of sales to 50% of sales by 2020
- Brand building and logistics cost will increase, expects EBITDA margins to improve on higher B2C share

Financial snapshot

(INR mn)

Year to March	Q1FY17	Q1FY16	% change	Q4FY16	% change	FY16	FY17E	FY18E
Net revenues	2,931	2,689	9.0	3,083	(4.9)	11,705	13,174	16,009
Raw material	2,369	2,139	10.7	2,420	(2.1)	9,097	10,310	12,315
Staff costs	82	67	22.2	78	5.8	282	329	380
Other expenses	232	212	9.3	307	(24.3)	1,134	1,311	1,601
Total expenditure	2,683	2,419	10.9	2,804	(4.3)	10,513	11,950	14,297
EBITDA	248	270	(8.1)	278	(10.9)	1,192	1,224	1,712
Depreciation	104	82	27.5	104	(0.2)	399	453	471
EBIT	144	188	(23.5)	174	(17.4)	793	771	1,241
Other income	2	5	(56.4)	2	(13.1)	15	9	12
Interest	71	132	(46.1)	72	(1.5)	427	221	172
Profit before tax	75	61	23.0	104	(28.3)	381	559	1,081
Provision for taxes	14	24	(40.6)	22	(35.0)	136	185	357
Minority interest								
Associate profit share								
Reported net profit	60	37	64.4	82	(26.5)	245	375	724
Adjusted Profit	60	37	64.4	82	(26.5)	245	375	724
Diluted shares (mn)	98	71		98		98	98	98
Adjusted Diluted EPS	0.6	0.5	20.2	0.8	(26.5)	2.5	3.8	7.4
Diluted P/E (x)	-	-		-		36.1	23.6	12.2
EV/EBITDA (x)	-	-		-		8.7	8.7	5.9
ROAE (%)*	-	-		-		5.6	6.2	11.1
As a % of net revenues								
Raw material	80.8	79.6		78.5		77.7	78.3	76.9
Employee cost	2.8	2.5		2.5		2.4	2.5	2.4
Other expenses	7.9	7.9		9.9		9.7	9.9	10.0
EBITDA	8.5	10.0		9.0		10.2	9.3	10.7
Reported net profit	2.1	1.4		2.7		2.1	2.8	4.5

*Adjusted for revaluation reserves, not including sales tax incentives

Company description

Prabhat, incorporated in 1998, is an integrated milk and dairy products player in India with aggregate milk processing capacity of 1.5mn litres per day. Over the years, the company has diversified into pasteurised milk, flavoured milk, sweetened condensed milk, ultra-pasteurised or ultra-high temperature (UHT) milk, yoghurt, dairy whitener, clarified butter (ghee), milk powder, ingredients for baby foods, lassi and chaas. It sells these products under retail consumer brands as well as ingredient products or as co-manufactured products to a number of institutional and multinational companies. Prabhat commenced commercial production of cheese, paneer and shrikhand in FY16.

Investment theme

Coursing ahead to be a value-added player

Leveraging its strong track record as a specialty ingredients supplier to large global dairy players, Prabhat catapulted its gross block in value-added products >40% in FY16, to be the third largest cheese player in India. On the anvil is a 2-pronged strategy to scale up its value-added sales in HORECA and B2C segments via tier II/III cities with targeted ad spends at 1.3% of sales (0.8% in FY16). Consequently, share of value-added products is expected to jump from 4% to 17% and B2C sales from 27% to 37% over FY16-18E. Management has set a target of B2C mix at ~50% of sales by FY20.

Superior mix and utilisation: Margin and return ratio boosters

Prabhat's gross and EBITDA margins are likely to surge 79bps and 56bps over FY16-18E, respectively, led by: a) rising share of B2C & value-added products; and b) increasing utilisation. Ergo, we estimate adjusted pre-tax RoCE to catapult 386bps over the period to 15.0%.

Key risk:

Availability and price volatility of raw milk

Prabhat's business depends on its ability to procure sufficient good quality raw milk at commercially viable prices. Though the company has longstanding relationships with milk farmers and other suppliers, it has not entered into any formal supply agreements.

Overdependence on few institutional customers

In FY12, FY13, FY14, FY15, FY16 sales contribution from top-5 customers represented 44%, 41%, 41%, 36% and 38%, respectively, while sales to largest customers represented 33%, 27%, 21%, 18% and 16.5% of total revenues, respectively.

Trademark and brand infringement

Although Prabhat sells retail consumer products under its own trademarks and brands such as *Prabhat*, *Flava* and *Milk Magic*, these trademarks and brands have not yet been registered.

Financial Statements

Key assumptions

Year to March	FY15	FY16	FY17E	FY18E
Macro				
GVA(Y-o-Y %)	7.2	7.4	7.9	8.3
Inflation (Avg)	5.9	4.8	5.0	5.2
Repo rate (exit rate)	7.5	6.8	6.0	6.0
Sector assumptions				
Milk purchase prices (INR/litre)	20.0	21.5	22.6	23.5
Sales growth				
Processed and Pouch Milk (%)	21	2	7	10
SMP / WMP / DW (%)	31	4	40	13
Condensed milk added sugar (SCM) (%)	1	(7)	(44)	15
Ghee (%)	46	113	17	13
Flavoured Milk (%)	(70)	36	21	71
Butter (%)	109	(100)	NA	NA
Ice Cream (%)	142	24	34	41
Curd (%)	253	13	120	59
Long shelf Milk (UHT Milk) (%)	1,465	34	51	108
Cheese (%)	0	0	2,059	127
Paneer (%)	0	0	3,188	165
Shrikhand (%)	0	0	3,172	165
% of sales				
Processed and Pouch Milk (%)	24	21	20	18
SMP / WMP / DW (%)	32	28	35	33
Condensed milk added sugar (SCM) (%)	29	23	11	11
Ghee (%)	12	21	22	20
Butter (%)	0	0	0	0
Others	0	3	2	2
Total other products (%)	96	96	90	83
Flavoured Milk (%)	0	0	0	0
Ice Cream (%)	1	1	1	1
Curd (%)	2	2	3	4
Long shelf Milk (UHT Milk) (%)	1	1	1	2
Cheese (%)	0	0	4	7
Paneer (%)	0	0	1	1
Shrikhand (%)	0	0	1	1
Total value added products (%)	3	4	10	17
Capacity utilisation (%)				
Cheese (%)	NA	1	19	40
Channel mix				
B2B (%)	76	73	66	63
B2C (%)	24	27	34	37
Financial Assumptions				
Depreciation (% of gross block)	8.1	7.9	7.4	7.4
Interest rate (%)	10.0	12.8	12.0	9.5
Tax rate (%)	10	36	33	33
Capex (INR mn)	536	322	305	100

Income statement

(INR mn)

Year to March	FY15	FY16	FY17E	FY18E
Net revenue	10,034	11,705	13,174	16,009
Materials costs	7,762	9,097	10,310	12,315
Gross profit	2,272	2,608	2,864	3,693
Employee costs	256	282	329	380
Other Expenses	981	1,134	1,311	1,601
Operating expenses	1,237	1,416	1,640	1,982
Total operating expenses	8,999	10,513	11,950	14,297
EBITDA	1,035	1,192	1,224	1,712
Depreciation	344	399	453	471
EBIT	691	793	771	1,241
Add: Other income	10	15	9	12
Less: Interest Expense	412	427	221	172
Profit Before Tax	289	381	559	1,081
Less: Provision for Tax	29	136	185	357
Reported Profit	260	245	375	724
Adjusted Profit	260	245	375	724
Shares o/s (mn)	71	98	98	98
Adjusted Basic EPS	3.6	2.5	3.8	7.4
Diluted shares o/s (mn)	71	98	98	98
Adjusted Diluted EPS	3.6	2.5	3.8	7.4
Adjusted Cash EPS	8.4	6.0	8.5	12.2
Dividend per share (DPS)	0.1	0.4	0.5	1.0
Dividend Payout Ratio(%)	2.2	19.2	15.6	15.6

Common size metrics

Year to March	FY15	FY16	FY17E	FY18E
Gross margin	22.6	22.3	21.7	23.1
Interest Expense	4.1	3.6	1.7	1.1
EBITDA margins	10.3	10.2	9.3	10.7
EBIT margins	6.9	6.8	5.9	7.8
Net Profit margins	2.6	2.1	2.8	4.5

Growth ratios (%)

Year to March	FY15	FY16	FY17E	FY18E
Revenues	17.3	16.7	12.5	21.5
EBITDA	16.3	15.2	2.6	39.9
PBT	22.4	31.9	46.8	93.2
Adjusted Profit	49.9	(5.6)	52.8	93.2
EPS	(37.0)	(31.0)	52.8	93.2

Balance sheet		(INR mn)			
As on 31st March	FY15	FY16	FY17E	FY18E	
Share capital	714	977	977	977	
Reserves & Surplus	2,802	5,572	5,888	6,499	
Shareholders' funds	3,516	6,549	6,865	7,476	
Short term borrowings	1,958	1,197	1,704	1,204	
Long term borrowings	2,159	388	388	323	
Total Borrowings	4,118	1,586	2,093	1,528	
Long Term Liabilities	11	14	14	14	
Def. Tax Liability (net)	178	236	236	236	
Sources of funds	7,822	8,385	9,208	9,254	
Gross Block	4,259	5,891	6,341	6,391	
Net Block	3,049	4,288	4,285	3,864	
Capital work in progress	1,591	245	100	150	
Intangible Assets	9	10	10	10	
Total net fixed assets	4,649	4,542	4,395	4,024	
Non current investments	1	1	1	1	
Cash and Equivalents	215	120	279	282	
Inventories	634	879	1,143	1,302	
Sundry Debtors	2,084	2,265	2,953	3,038	
Loans & Advances	965	1,274	1,052	1,250	
Other Current Assets	87	18	18	18	
Current Assets (ex cash)	3,770	4,437	5,166	5,608	
Trade payable	622	521	421	397	
Other Current Liab	191	193	211	263	
Total Current Liab	813	714	632	660	
Net Curr Assets-ex cash	2,957	3,722	4,534	4,948	
Uses of funds	7,822	8,385	9,208	9,254	
BVPS (INR)	49.2	67.0	70.3	76.5	

Free cash flow		(INR mn)			
Year to March	FY15	FY16	FY17E	FY18E	
Reported Profit	260	245	375	724	
Add: Depreciation	344	399	453	471	
Interest (Net of Tax)	276	286	148	115	
Others	94	122	64	45	
Less: Changes in WC	959	765	812	414	
Operating cash flow	14	287	227	942	
Less: Capex	536	322	305	100	
Free Cash Flow	(521)	(35)	(78)	842	

Cash flow metrics		FY15	FY16	FY17E	FY18E
Year to March					
Operating cash flow	14	287	227	942	
Investing cash flow	(533)	(243)	(305)	(100)	
Financing cash flow	691	(130)	237	(838)	
Net cash Flow	173	(86)	159	3	
Capex	(536)	(322)	(305)	(100)	
Dividend paid	(6)	-	(59)	(113)	

Profitability and efficiency ratios		FY15	FY16	FY17E	FY18E
Year to March					
ROAE (%)*	9.5	5.6	6.2	11.1	
ROACE (%)*	11.2	11.2	9.9	15.1	
ROA	3.7	3.0	4.3	7.8	
Inventory Days	25	30	36	36	
Debtors Days	66	68	72	68	
Payable Days	25	23	17	12	
Cash Conversion Cycle	67	75	91	92	
Current Ratio	4.9	6.4	8.6	8.9	
Debt/EBITDA (x)	4.0	1.3	1.7	0.9	
Debt/Equity (x)	1.2	0.2	0.3	0.2	
Adjusted Debt/Equity	1.2	0.3	0.3	0.2	
Interest Coverage Ratio	1.7	1.9	3.5	7.2	
LT debt /Cap empl. (%)	52.6	18.9	22.7	16.5	
Debt / Cap employed (%)	65.3	30.2	32.2	26.2	

*Adjusted for revaluation reserves, not including sales tax incentives

Operating ratios		FY15	FY16	FY17E	FY18E
Year to March					
Total Asset Turnover	1.4	1.4	1.5	1.7	
Fixed Asset Turnover	3.1	3.2	3.1	3.9	
Equity Turnover	3.0	2.3	2.0	2.2	

Valuation parameters		FY15	FY16	FY17E	FY18E
Year to March					
Adj. Diluted EPS (INR)	3.6	2.5	3.8	7.4	
Y-o-Y growth (%)	(37.0)	(31.0)	52.8	93.2	
Adjusted Cash EPS (INR)	8.4	6.0	8.5	12.2	
Diluted P/E (x)	24.9	36.1	23.7	12.2	
P/B (x)	1.8	1.4	1.3	1.2	
EV / Sales (x)	1.0	0.9	0.8	0.6	
EV / EBITDA (x)	10.0	8.7	8.7	5.9	
Dividend Yield (%)	0.1	0.4	0.5	1.1	

Additional Data

Directors Data

Sarangdhar R Nirmal	Chairman and MD	Vivek S Nirmal	Jt Managing Director
Ashok Sinha	Independent Director	Seemantinee Khot	Independent Director
Rajesh Srivastava	Additional Non- Executive Director	Raphael Gabriel Roger Plihon	Additional Non- Executive Director
Soundararajan Bangaruswamy	Independent Director	Omprakash V. Bundellu	Independent Director

Auditors - BSR & Co.

**as per last annual report*

Holding Top -10

	Perc. Holding		Perc. Holding
Indian Agribusiness Fund	14.37	Societe Prom & Part Econom	8.68
IL&FS Trust Co Ltd	7.57	Wasatch Advisors	6.34
Reliance Capital	2.81	Styrax Commodities	2.49
Ecap Equities	1.75	Genesis Emerge Sm Com Port	1.45
HDFC Asset Management	1.34	Birla Sun Life Asset Mgmt	1.08

**as per last available data*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
28 Dec 2015	Reliance Capital Ltd	Buy	2744000	150.04
28 Dec 2015	Payone Enterprises Pvt Ltd	Sell	2894323	150.26
05 Oct 2015	Reliance Mutual Fund	Buy	2087000	117.00
22 Sep 2015	Abhilasha Money Operations Pvt Ltd	Sell	552984	117.69

**as per last available data*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
24 Aug 2016	Sarangdhar R.Nirmal - Trustee of Nirmal Family Trust	Buy	126000.00
03 Mar 2016	Sarangdhar R.Nirmal - Trustee of Nirmal Family Trust	Buy	200000.00
02 Mar 2016	Sarangdhar R.Nirmal - Trustee of Nirmal Family Trust	Buy	186800.00

**as per last available data*

Edelweiss Securities Limited, Edelweiss House, off C.S.T. Road, Kalina, Mumbai – 400 098.

Board: (91-22) 4009 4400, Email: research@edelweissfin.com

Manoj Bahety

Deputy Head Research

manoj.bahety@edelweissfin.com

Coverage group(s) of stocks by primary analyst(s): Dairy

Prabhat Dairy Ltd

Recent Research

Date	Company	Title	Price (INR)	Recos
22-Aug-16	Prabhat Dairy	Discovering greener pastures; Initiating Coverage	79	Buy

Distribution of Ratings / Market Cap

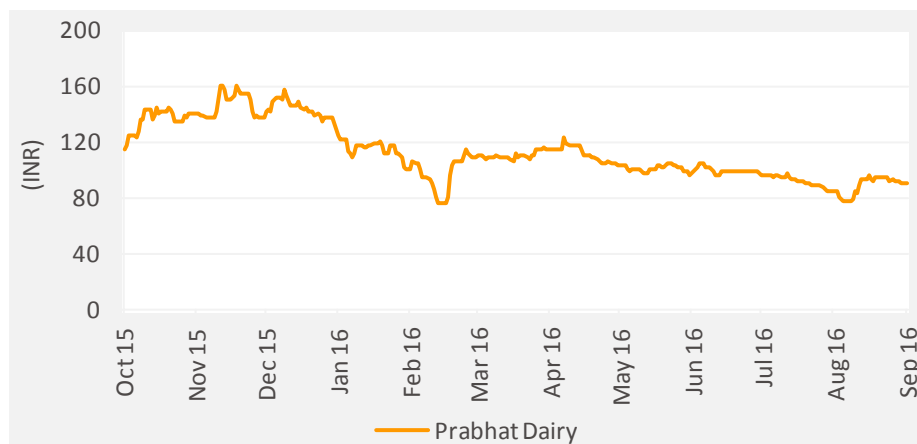
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	158	59	12	229
* - stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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