Stock Idea

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TASTY BITE EATABLES LTD.

14th April 2015

Rs 640

Content

Tasty Bite Eatables – Snapshot

Suggested Allocation: 3-4% | **Industry:** Consumer Food
Market Cap: INR 165 Cr. | **Shares Outstanding:** 0.26 Cr.
Bloomberg Code: TSTY IN | **Reuters Code:** TABE.BO
Listed on BSE | **BSE Code:** 519091

Particulars	9mFY15	FY14	FY13	FY12
Sales (INR Cr.)	123.5	145.4	111.5	82.4
Operating Margins (%) (Exc. OI)	13.4	8.1	11.7	6.9
PAT Margins (%)	5.8	2.9	5.6	2.0
Cash Flow From Operations (INR Cr.)		23.4	-2.3	11.3
RoE (%)		13.5	23.5	7.1
RoCE (%)		10.4	17.3	8.2
LT Debt (INR Cr.)		23.8	29.1	10.5
Cash & Equivalents (INR Cr.)		4.4	9.3	6.1

Source: Ace Equity

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The Synopsis

- **Business:** An indirect play on the rapidly rising QSR industry in India, which is growing at 20+%. It supplies frozen foods and sauces to the likes of Domino's and Mc Donald's. Its essentially a volume game and not so much about margins. TBE also happens to be market leading player of ready-to-eat foods in USA with 65% market share.

- **Management:** Run by an ethical and competent team with decades of experience in top management of global brands like Pepsi and HUL.

- **Valuation:** At CMP of Rs 640 and market cap of Rs 165 Cr., it is trading at P/E and EV/EBITDA multiple of 18 and nine respectively. A reasonable valuation restrict the downside whereas rapidly rising earnings and absence of institutional investors makes re-rating imminent offering good upside potential.

The History

- **1986**: Tasty Bite Eatables(TBE) was founded by the Ghai Family, who also used to own franchise of Kwality Ice Cream in Western India.
- The company was barely able to survive and hence got referred to BIFR. The company was later sold to HLL (now Hindustan Unilever - HUL)
- **1995**: 'Tasty Bite' ready-to-eat brand was launched in the USA.
- However, it remained very small and hence a non-core asset for the FMCG giant HUL.
- In a drastic move, Tasty Bite went through a management buy-out where Mr. Ashok Vasudevan & Mr. Ravi Nigam convinced HUL to sell the company to the duo.

The History…

- Surely it wouldn't have been an easy decision as the company had a small scale of operations and had never made any money in its 13 years of existence.

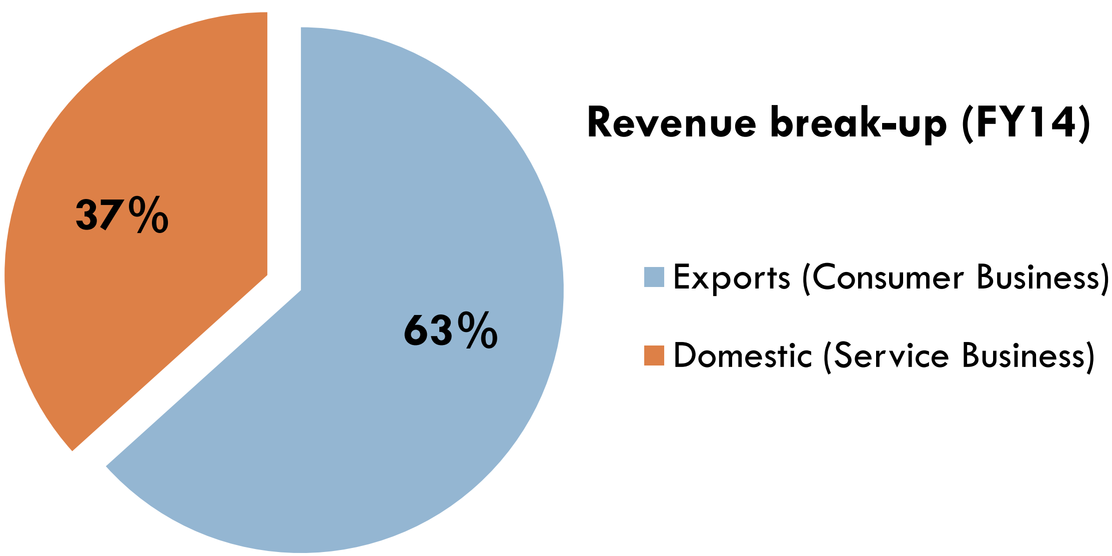
- However the duo were successful in turning around the company and put it on an aggressive growth path.

- **1999:** It was another important year for the company as it crossed revenues of 5 Cr. And turned profitable for the first time since inception.

TBE's Current Avatar

The company now has two business units –

- Consumer Business where it sells ready-to-eat food in the USA, Australia, Canada, New Zealand and the UK.
- Service Business where is supplies frozen foods and sauces to Indian QSR chains.



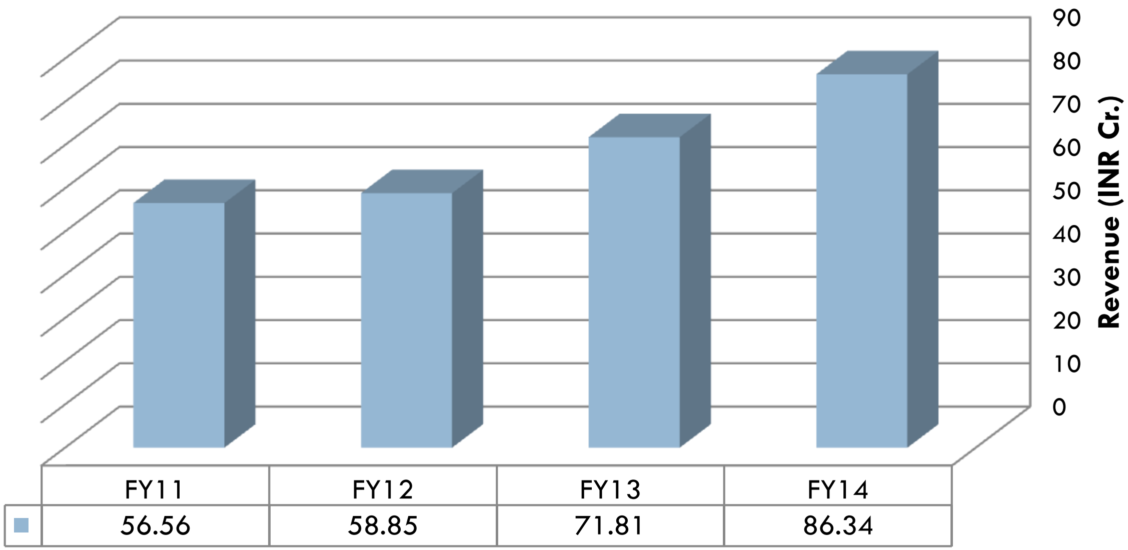
Business Unit I – Consumer Business

- *Tasty Bite* is a brand of ready to eat, all-natural Indian and pan-Asian cuisine. Tasty Bite offers over 42 products across 4 categories: entrées, rice, noodles and meal inspirations.
- The flavours range from classic Indian restaurant favourites such as a Channa Masala to unique fusion items such as the Tofu Corn Masala.
- The products require no cooking, have no preservatives, require no refrigeration, and can be used as a main dish or a side dish.
- With the use of a uniquely designed multi-layer retort pouch, Tasty Bite products remain fresh for 18 months.

Market Leader

- The company which first launched its products in USA, now has presence in Canada, Australia, New Zealand, and the UK.
- In North America, it is the largest brand of Indian shelf stable prepared foods and commands a whooping 65% market share in natural channel and 28% in conventional grocery and ranks amongst the top 3 brands among all Indian and Asian brands combined.

Revenue (INR Cr.) - Consumer Business/Exports



Distribution

- The Company manufactures its products in India, however marketing and distribution is taken care by its parent company, Preferred Brands International (PBI) based out of US.
- PBI has a wide distribution channel that covers the majority of supermarket chains in North America and other international markets.
- Products are either sold directly by PBI to retail chains or through a distributor that services several retailers and independent grocery stores.
- The mainstream retail chains include the likes of Safeway, Whole Foods, Costco, Krogers, HEB, Walmart, Coles, Woolworths amongst numerous others in the US and Australia.

Ready-to-eat Industry

- The grocery segment pertaining to the Company's products, namely the international/ethnic foods category is approximately $2.5 billion in size and growing at a rate of 15-20%.
- Ethnic food mainly consists of Mexican/Hispanic foods, Asian and Indian Foods. This is one of the fastest growing segments of supermarkets and driven by an increasingly diverse population, a growing interest in international foods driven by travel and cooking shows and the growing number of ethnic restaurants.
- At 29%, Asian foods holds the second-largest share of the ethnic foods market and continues a steady growth trend. Asian foods are a much larger industry, having sales of $700 million, compared to Indian foods which is a $41 million category.

Trends in the RTE industry

The three major global food trends driving the growth of the company's revenues in its international markets are:

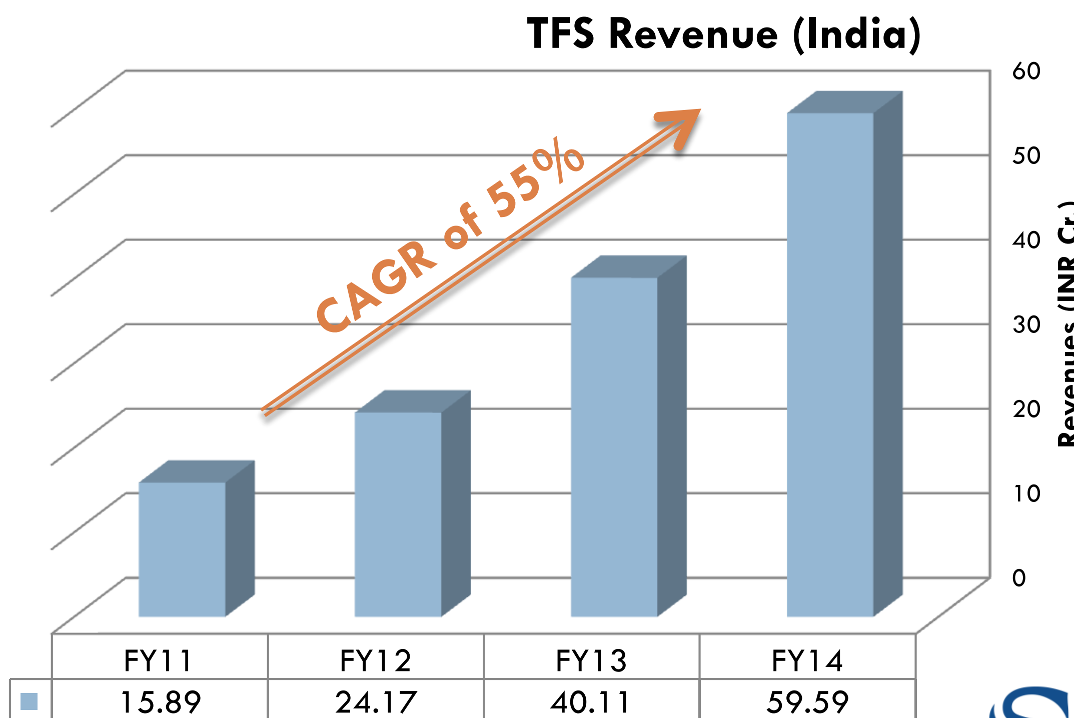
1. Increased focus on illnesses (like diabetes, heart disease, and obesity) has resulted in consumers taking health into consideration when making food choices and purchasing packaged foods.
2. Consumers are increasingly eating at home and are seeking products that are convenient to prepare and integrate into their meals while adding new flavours and cuisines.
3. Growth of international cuisines also called specialty foods. Cuisines such as Indian and Asian are growing in demand.

Business Unit II - TFS

- Tasty Bite Food Service business (TFS) was launched in India in 2006.
- TFS business is built around providing unique food solutions for leaders in the food service industry in India - in the area of Formed Frozen Products (FFP) and Culinary Sauces.
- The Company manufactures specialty products like Patties, Sauces & Appetizers for international and domestic Quick Service Restaurants (QSRs) as well as companies that focus on HORECA (hotels, restaurants and catering) sector.

TFS Business Performance

- The growth rates in this business unit have been phenomenal at as high as 55% CAGR over the last 4 years (albeit on a low base)
- Two-third of the business comes from frozen foods and rest from sauces.



TFS Unit recently started supplying *makhani* sauce to Hindustan Unilever for its *Kissan* Brand.

This unit has turned out to be the key growth driver for TBE.

Manufacturing Capabilities

- Tasty Bite manufactures its products in a world-class, versatile manufacturing facility encompassing manufacture of products in multiple formats (shelf-stable, frozen), multiple packaging (pouches, trays), multiple cuisines and multiple pack sizes.

- This facility is spread over 33-acre about 50 km from Pune on the Pune-Solapur Road and is ISO-9001-2000, HACCP (Hazard Analysis and Critical Control Points), ISO14001 (Environmental Management), ISO 22000 (Integrated Food Safety) ,OHSAS 18001 (Occupational Health and Safety Management) and FDA audited. The company is also certified for CT-PAT (Customs-Trade Partnership Against Terrorism).

Manufacturing Capabilities…

- 80% of the energy used in the Tasty Bite factory comes from renewable sources such as sugarcane by-products, and food and crop waste.

- The Company prides itself on its quality and has endeavoured to set industry standards of quality assurance.

- Company has been on a capex spree over last 3 years having spent around Rs ~45 Cr. The company now has manufacturing capacity to prepare over 100,000 meals per day in addition to manufacturing prepared frozen formed products.

Organic Farm

- TBE uses 75 vegetables, 75 spices and condiments, 42 grains and 10 dry fruits. It has an in-house organic farm which acts both as a source of some of their produce, and as a demonstration farm where they interact with their large community of farmers and exchange information and learnings on modern organic farming techniques and sustainable practices.

- They have a cold storage facility at the factory which is a good enabler in being able to store vegetables at the time of commodity harvest in order to manage costs.

Research Centre

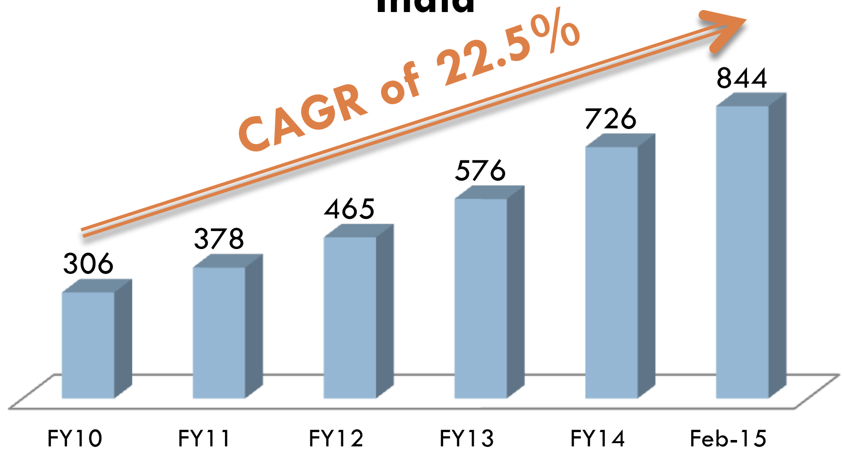
- The company has setup state-of-the-art Research Centre comprising of a strong team of highly skilled culinary professionals and food technologists who work towards development of improving existing SKUs, adding new SKUs to existing product categories as well as focusing on developing new product categories.

An impressive list of Clients

Domino's Growth Plans

Source: JF's Annual Report FY14

Number of Domino's Pizza Stores in India



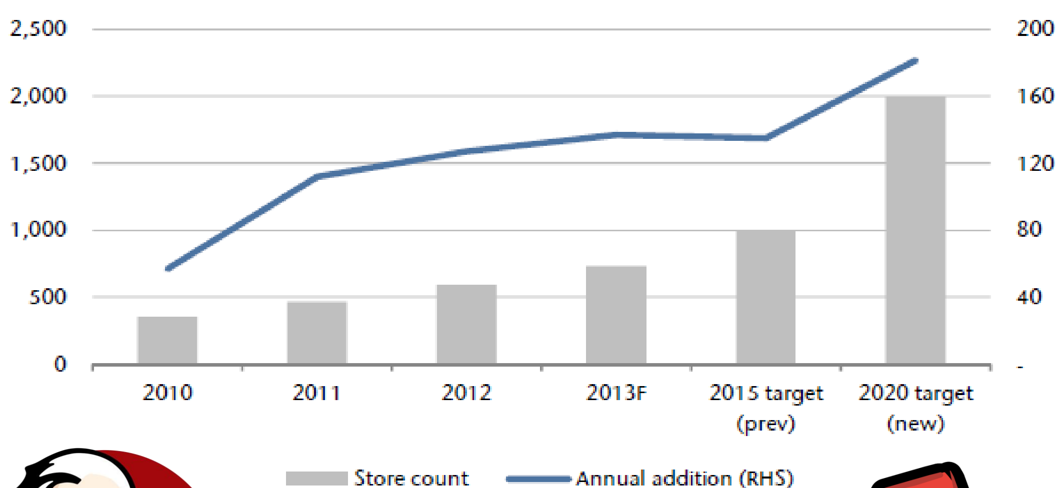
Jubilant Foodworks' owned Domino's Pizza franchise in India has seen an unprecedented pace in number of store additions over the last 5 years. It now operates 844 stores and is present in over 150 Indian cities.

Jubilant Foodworks also operates 50 Dunkin Donuts stores in India

"Jubilant Foodworks plans to add 150 new Domino's stores & 25 new Dunkin Donuts stores per annum over next three years"

Yum! India’s Growth Plans

Yum! India’s Store Count and Target Addition over next five years



Yum! India, that operates KFC, Pizza Hut and Taco Bell stores in India has also seen store additions being trebled in last three years. From 155 stores in 2011 compared to 240 of McDonald’s, KFC alone has reduced the gap in two years and now operates 305 KFC stores vis-à-vis ~350 of McDonald’s.

As per Yum, eating out market in India is highly underpenetrated and is currently less than 10% China’s. While China has 4 restaurants per million, India has less than 1 restaurant per million.

“Yum! India aspires to have 2,000 stores in India by 2020; three times its current number of stores”

Quick-service-restaurant (QSR) Industry

- As per Euromonitor data published in FY2014, the QSR segment in India is projected to grow at a CAGR of 20.5% to Rs 33,050 Crore in FY2018 from Rs 13,010 Crore in FY2013. The QSR segment is the fastest growing segment in the food service industry (FSI).

- Another recent study indicates that an urban Indian eats out over 6 times a month (a 300% growth compared to a decade back), many a time at such restaurants. This change in eating habits has grown and will continue to grow given the young demographics of the country, rising disposable incomes and the emergence of dual income nuclear families.

Source of competitive advantages

- We feel the service business despite being a B2B business enjoys moat as the customers (think Domino's or McD) are extremely quality conscious. Ideally they would never compromise on quality to save few pennies. Imagine if we found a cockroach in Mc Donald's burger, wouldn't it do some serious damage to the brand franchise? Further, in this social media era Mc Donald's will be unable to undo any of it. This risk of loosing brand value makes buyers extremely quality conscious. This is similar to the advantage Kitex Garments enjoy, as despite being a B2B business it caters to highly quality conscious customers.
- It would take significant time for any new entrant to qualify as a 'vendor' for QSR players. It would also imply a significant capital investment as one would have to commit a certain minimum quantity. This makes the process lengthy and expensive. Tasty Bite due to its learning curve and focus on Quality now qualifies as a **'Preferred'** supplier to the largest QSR chains of India giving it some sort of a moat. This isn't a very Deep moat but surely a wide moat.

Board & Leadership Team

Mr. Ashok Vasudevan

Mrs. Meera Vasudevan

Board Of Directors	
Mr. Ashok Vasudevan	Chairman
Mr. Ravi Nigam	Managing Director
Mrs. Meera Vasudevan	Director
Mr. K. P. Balasubramaniam	Independent Director
Dr. V. S. Arunachalam	Independent Director
Mr. Kavas Patel	Independent Director
Mr. Sohel Shikari	Alternate Director & CFO

Mr. Ravi Nigam

Mr. Sohel Shikari

Highly experienced management

Mr. Ashok Vasudevan, Chairman

- His 30-year career has been spent almost equally between being an entrepreneur and a corporate executive. Prior to Tasty Bite, Ashok headed the India desk of Pepsi World Trade in Somers, New York. He received Pepsi's prestigious MVP award in 1991.
- Before joining Pepsi, Ashok spent 10 years with Unilever in various functions that included Management Development, Sales & Marketing and International Business.
- Ashok Vasudevan graduated in Agricultural Sciences from Bangalore and received his business education at the Bajaj Institute of Management in Bombay and the Harvard Business School.

Mr. Ravi Nigam, Managing Director

- Most of his 32-year corporate and entrepreneurial career has been in the area of Agri & Food business. Prior to joining TBEL in 1997, he held senior positions in International Business at Pepsi, Ballarpur Industries and Britannia Industries. In an earlier entrepreneurial stint, Ravi founded 'Action management Group' (AMG); a consulting firm specializing in setting up exports led agri businesses. His clients included large firms such as L&T, Pepsi, Tata Exports and BILT.
- He has been on the national committee on Food processing at CII for the last 3 years. Ravi has a BS in Chemistry and an MBA from The Institute of Rural Management, Anand, India (IRMA) and an OPM from the Harvard Business School.

Guidance

- Management has hinted at a potential asset turnover of 3.5-4 times. This implies the recent capacity expansion of Rs ~25 Cr. could yield incremental revenues to the tune of Rs 80-100 Cr.
- In terms of margins, management has indicated that sustainable gross margins are in the vicinity of 35% whereas operating margins could be in the range of 13-15%. This is owing to the fact that company is staying away from commoditized products and only focusing on specialty products for service business.
- TBE's story primarily seems to be a volume led growth story which will be dependent upon growth plans and same-store-sales growth (SSSG) of its QSR customers.
- We feel QSR service business could continue on high growth trajectory of 30-40% CAGR for next few years, whereas consumer business (exports) can clock 15-20% growth making blended growth rates to be at least 20%+.

Balance Sheet

- TBE has a tiny equity capital of Rs 2.6 Cr. And Rs 60 lacs non-convertible preference shares. Networth (as on Sep14) of the company stands at Rs 40 Cr.
- It carries long term debt to the tune of Rs. 23 Cr. Total debt-equity ratio is above one, however interest coverage ratio of five is comforting. Recently, ICRA upgraded its debt rating from BBB to BBB+ (Link to ICRA's report)
- In last three years, gross block has trebled to 82 Cr. owing to capex incurred to increase capacity of service business.
- In FY14, receivable days stood at 40, inventory days at 30 and payable days at 50, implying net working capital cycle of 20 days.

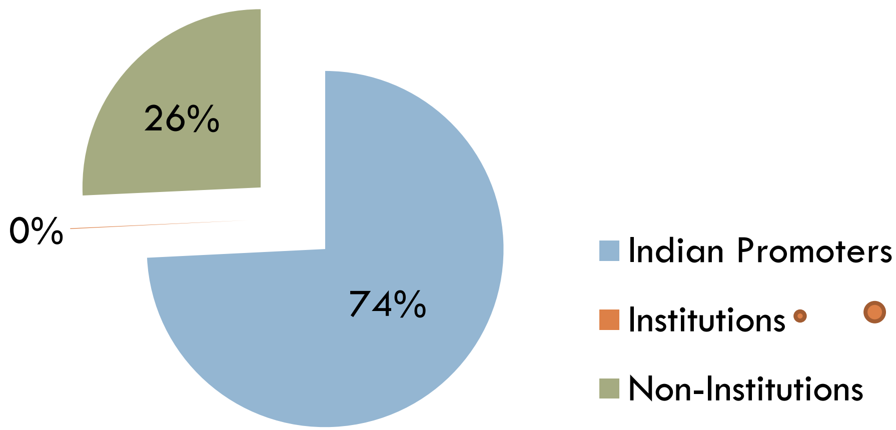
Valuation

- At current price of Rs640 and market cap of Rs ~165 Cr., the stock discounts its trailing twelve months' earnings (P/e) at less than 18 times. In terms of forward earnings, it is available at less than 15 times.

- Re-rating seems imminent, given the growth potential in the business, likely margin expansion and entry of institutional investors once the company achieves bigger scale and liquidity in stock improves.

- A strong earnings growth coupled with re-rating could make this stock a multi-bagger in 3-4 years time-frame with limited downside risks.

Shareholding* (%)



Promoters hold 74.2% in the company through their holding company Preferred Brands Foods India Pvt. Ltd.

Institutions hold a negligible 0.06%

Shareholders with more than 1% Holding*

1.	K Swapna	6.15
2.	Tanvi J Mehta	1.22
3.	Rahul Kayan	1.09

We have been tracking this story from a long time, however 100% pledging of promoter holding (for raising ECB/Debt), deterred us from getting into this.

As per filing to exchange dated 14^{th} April 2015 (today), the holding company has got the entire pledge released.

**As on March 31, 2015*
Source: Ace Equity

Triggers & Upside

- An indirect play on the fast growing QSR industry in India
- Market leading brand in fast growing RTE meals category in the USA
- Negligible presence of institutional investors
- Ethical and competent management with impeccable execution capabilities
- Attractive valuations presenting decent scope for re-rating given the size of the opportunity

Risks & Concerns

- **Low free float:** The biggest concern while investing in TBE is low traded volumes. Out of the total of 26 lacs shares, promoters own 19.5 lac, whereas ~2.5 lac is in the hands of big investors (as indicated by shareholding pattern). This leaves only four lac shares as real free float in the markets. Anyone looking to accumulate bigger chunk would have to keep patience and do it slowly. One can keep accumulating till levels of ~Rs900 (40% higher than CMP).
- **Distribution by Parent Co.:** First impression of this arrangement, where holding company distributes the products abroad, could be negative due to transfer pricing concerns. However, there seems enough indicators pointing out to the contrary; promoters have diluted stake in holding company and hence its not 100% owned, promoter holding in TBE at 74.2% is close to maximum allowed by SEBI and looking at the track record of the promoters, chance of any adverse move against minority shareholders looks remote.

Risks & Concerns

- **Volatility in Raw Material Cost:** Vegetable prices move sharply based on supply in each season. A bad monsoon or unseasonal rains disrupts the supply leading to short term spike in prices. TBE has annual fixed price contract with its parent whereas pricing for TFS business is revised quarterly. This makes it susceptible to raw material price variation and hence could impact margins. However, the process to buy in bulk in peak season (of harvesting) and having a cold storage mitigates this risk to some extent. Further, there will be times when prices shoot up and there will also be times when prices correct which should ideally even out in the long run.
- **Volatility in Forex:** Any adverse move in exchange rate could affect margins as over half the revenues come from exports.

Some interesting Links

1. Corporate Film on Tasty Bite
   - https://www.youtube.com/watch?v=Nmqb5gSkrNk

2. A conversation with Tasty Bite's CEO
   - https://www.youtube.com/watch?v=xSB_zMflqSw

Indian Entrees

Asian Noodles

Rices


TASTY BITE
organic
Long-Grain Rice


TASTY BITE
Jasmine
Rice


TASTY BITE
organic
Brown Rice


TASTY BITE
Basil
Chili Rice


TASTY BITE
Tandoori
Rice
organic


TASTY BITE
Stir Fried
Brown Rice


TASTY BITE
Thai
Fried Rice


TASTY BITE
Ginger Lentil
Rice


TASTY BITE
Garlic
Brown Rice
organic


TASTY BITE
Thai
Lime Rice
organic


TASTY BITE
Asian
Vegetable Rice


TASTY BITE
organic
Basmati Rice

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Please read 'Frequently asked questions' to understand our thought process better.

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