

Expect margins to normalise in medium term...

About the stock: United Spirits (USL) is India's leading alcoholic beverage company and subsidiary of global leader Diageo plc. It manufactures, sells premium liquor brands such as Johnnie Walker, Black Dog, Black & White, Vat 69, Antiquity, Signature, Royal Challenge, McDowell's No 1, Smirnoff and Captain Morgan.

- Prestige and above segment comprises 71% of its revenues
- It aims to grow its revenues in double digits and expects its operating margin to remain in mid to high-teen levels in the medium term

Q1FY23 Results: Margins impacted by inflationary pressure on input materials

- Net revenues were up 34% YoY to ₹ 2169 crore amid 17% rise in volumes
- EBITDA grew 63% to ₹ 274 crore with margins at 12.6% (10.4% in Q1FY22)
- However, PAT grew 3x to ₹ 210 crore, in spite of a one-off exceptional loss of ₹ 38 crore, due to higher other income and deferred tax asset recognition

What should investors do? USL is undergoing a complete revamp of its product mix (with premiumisation expected to accelerate over 90% of revenue mix, post-slump sale of its several popular brands by H1FY23 end). Thus, it will strengthen its already existing moat around the business (duopoly with Pernod Richard) and further improve its return ratios in the longer term

- We remain positive on the long term growth prospects of the stock and maintain our **BUY** recommendation

Target Price and Valuation: We value USL at ₹ 920 i.e. 61x P/E on FY24E EPS.

Key triggers for future price performance:

- Newer launches and brand extensions in the upper prestige and introduction of international brands from the Diageo stable
- Favourable regulatory environment (lower customs duty, higher distribution, composite shops, etc) in several states
- Debt free status, double-digit return ratios & strong cash generation

Alternate Stock Idea: Apart from USL, we remain positive on Radico.

- It has been reporting volume growth, well ahead of the industry and is strategising on entering premium whisky category
- It has been continuously reducing its overall net-debt from peak of ~₹ 950 crore to ~₹ 198 crore in FY21 and generated ~₹ 380 crore of CFO in FY21

Key Financial Summary

₹ crore	FY20	FY21	FY22	5 years CAGR (%)	FY23E	FY24E	2 years CAGR (%)
Net Sales	9325.4	8131.3	9712.4	2.0	10170.9	10833.5	5.6
EBITDA	1572.3	1052.7	1608.1	5.3	1373.1	1668.4	1.9
EBITDA margin (%)	16.9	12.9	16.6		13.5	15.4	
PAT	658.9	383.6	828.6	15.6	1494.5	1093.3	14.9
P/E (x)	91.3	158.0	70.8		38.4	52.5	
Market cap to Sales (x)	6.2	7.1	5.9		5.6	5.3	
RoCE (%)	23.8	15.6	24.4		28.8	18.7	
RoE (%)	16.9	8.8	16.4		23.2	14.5	

Source: Company, ICICI Direct Research



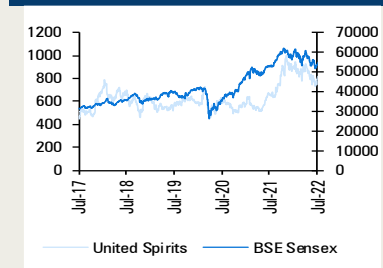
Stock data

Particular	Amount
Market Capitalization (₹ cr)	57,393.5
Total Debt (FY22) (₹ cr)	341.7
Cash (FY22) (₹ cr)	60.3
EV (₹ cr)	57,393.5
52 week H/L	1020/629
Equity Capital (₹ cr)	145.3
Face Value (₹)	2.0

Shareholding pattern

(in %)	Sep-21	Dec-21	Mar-22	Jun-22
Promoter	56.7	56.7	56.7	56.7
FII	19.1	17.9	17.7	16.8
DII	6.7	7.5	7.7	8.0
Others	17.5	17.8	17.9	18.5

Price Chart



Recent event & key risks

- Strategic sale transaction to be completed in Q2FY23 end
- **Key Risk:** (i) Raw material inflation, (ii) local shutdown of on-trade channels

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Key takeaways

Q1FY23 Results: One-offs impact quarter

- During the quarter, Premium and Luxury portfolio grew faster than the Prestige portfolio. Within Scotch portfolio, Johnnie Walker, Black and White and Black Dog delivered very strong growth
- The reported PAT was higher than I-direct estimates due to higher other income and a tax credit on account of recognition of deferred tax asset. The company has also recorded an exceptional expense of ₹ 38 crore, due to an ongoing business restructuring expense

Q1FY23 Earnings Conference Call highlights

- The management expects ENA and glass price to remain elevated in the near term (growth at double digit)
- The management remains positive on combatting the inflation with change in portfolio mix (higher mix of mid to high renovated brands, strategic sale of popular portfolio) and price hike in various states
- During the quarter, USL has received price hikes in Madhya Pradesh, Rajasthan and Haryana
- The management expects Advertisement expenses to remain intact, inspite of pressure on margins, as they prepare for building long term brand equity. Also, digital marketing now constitutes 50% of the overall A&P expense
- The management expects to complete the slump sale by September end (FY23). Post the slump sale, expect revision in the current guidance of double digit revenue growth (upward revision)
- EBITDA margins are expected to remain range-bound in the near to medium term

Exhibit 1: Variance Analysis

Standalone	Q1FY23	Q1FY23E	Q1FY22	YoY (%)	Q4FY22	QoQ (%)	Comments
Revenue	2,169.0	2,351.4	1,615.0	34.3	2,435.1	-10.9	Lower than estimates due to weaker than expected P&A volume growth
Consumption of RM	1,281.1	1,363.8	894.6	43.2	1,418.5	-9.7	Gross margins (40.9%) was below I-direct estimates (42%), due to high ENA, glass, PET inflation
Employee Expenses	166.5	152.8	187.4	-11.2	135.7	22.7	Employee costs include a bonus for staff
A&P Expenses	140.3	188.1	83.8	67.4	131.2	6.9	Lower advertisement in Q1 (6.5%), supported EBITDA margins to an extent
Other Expense	307.2	305.7	281.6	9.1	323.0	-4.9	
Total Expense	1,895.1	2,010.5	1,447.4	30.9	2,008.4	-5.6	
EBITDA	273.9	341.0	167.6	63.4	426.7	-35.8	EBITDA lower than estimates mainly due to lower gross margins, higher employee and other expenses
EBITDA Margin (%)	12.6	14.5	10.4	225 bps	17.5	-489 bps	
Depreciation	65.3	68.4	55.4	17.9	67.1	-2.7	
Interest	16.6	23.5	19.8	-16.2	12.7	30.7	
Other Income	25.1	2.6	10.6	136.8	25.8	-2.7	
Exceptional Gain/Loss	-38.4	0.0	-36.4	NA	-173.2	NA	Includes Voluntary Separation Scheme (VSS) covering permanent employees at 4 factories
PBT	178.7	251.6	66.6	168.3	199.5	-10.4	
Total Tax	-31.3	63.3	-2.4	1,204.2	63.3	-149.4	Deferred tax asset recognition due to certainty in utilisation of carried forward losses
PAT	210.0	188.2	69.0	204.3	136.2	54.2	
Key Metrics	Q1FY23	Q1FY23E	Q1FY22	YoY (%)	Q4FY22	QoQ (%)	
P & above vol (Mn cases)	10.0	11.2	8.0	24.4	10.9	-8.9	Constraints in scotch supplies in select markets on account of price deliberations with the Government
Regular	8.6	8.4	7.8	10.2	9.8	-12.4	Largely in-line performance
Total volume (mn cases)	18.5	19.6	15.8	17.4	20.7	-10.5	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY23E				FY24E				Comments
	FY22	Old	New	% Change	Old	New	% Change		
Revenue	9,712.4	10,389.0	10,170.9	-2.1	10,943.4	10,833.5	-1.0	Revenues reduced marginally	
EBITDA	1,608.1	1,589.5	1,373.1	-13.6	1,794.7	1,668.4	-7.0		
EBITDA Margin (%)	16.6	15.3	13.5	-180 bps	16.4	15.4	-100 bps	Margins reduced due to higher inflationary impact on raw material prices	
PAT	810.6	1,607.9	1,494.5	-7.1	1,172.0	1,093.3	-6.7		
EPS (₹)	11.2	22.1	20.6	-6.9	16.1	15.0	-6.5		

Source: ICICI Direct Research

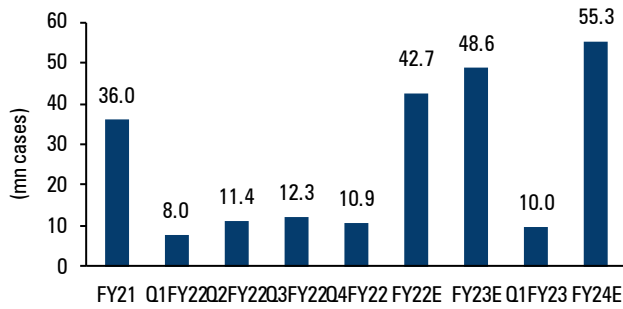
Exhibit 3: Assumptions

	Current				Earlier		Comments
	FY21	FY22	FY23E	FY24E	FY23E	FY24E	
Volume (Standalone) Cr Cases	6.9	7.9	7.6	7.2	7.9	7.5	Volumes reduced marginally due to continued weakness in P&A volumes
Volume Growth (%)	-15.2	14.4	-4.1	-4.9	-0.3	-5.1	
Net Realisation (standalone)	1,088	1,169	1,282	1,448	1,259	1,415	
Realisation Growth (%)	-1.4	7.5	9.7	12.9	7.7	12.4	

Source: ICICI Direct Research

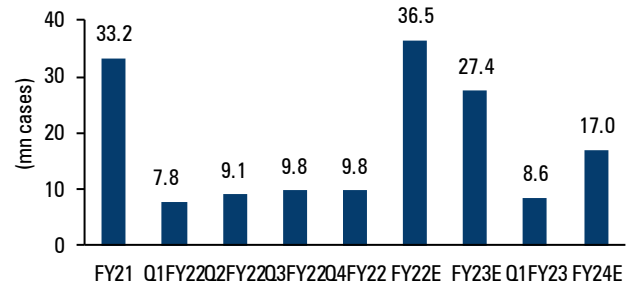
Key Metrics

Exhibit 4: P&A expected to grow at 14% CAGR (FY22-24)



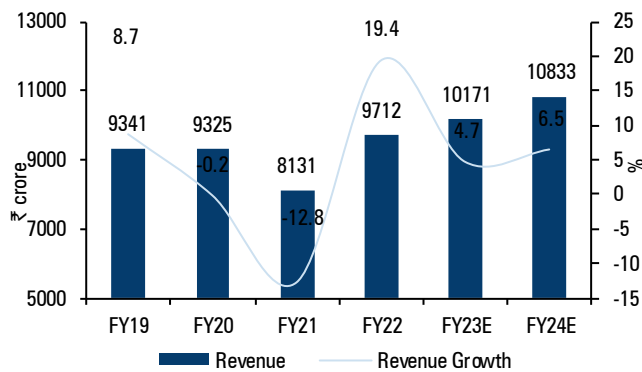
Source: ICICI Direct Research, Company

Exhibit 5: Popular to likely de-grow 32% CAGR (FY22-24)



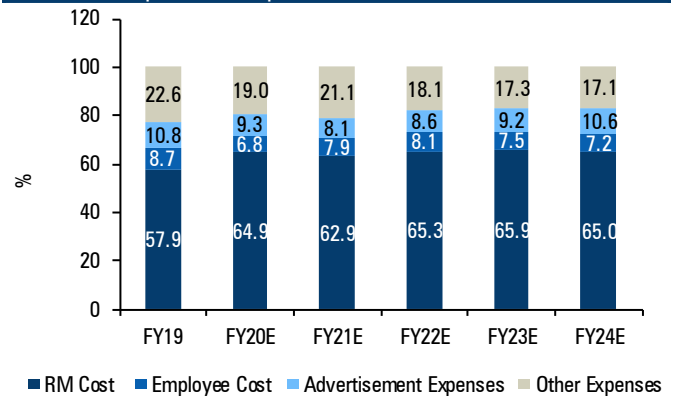
Source: ICICI Direct Research, Company

Exhibit 6: Revenues to grow at 6% CAGR over FY22-24E



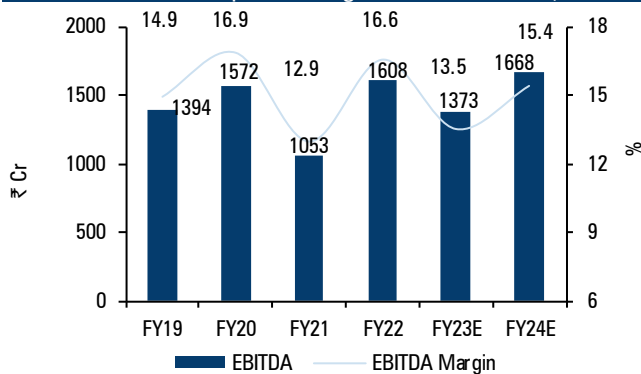
Source: ICICI Direct Research, Company

Exhibit 7: Expense composition



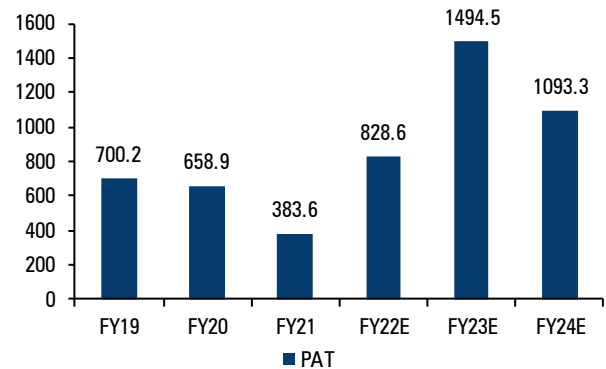
Source: ICICI Direct Research, Company

Exhibit 8: EBITDA expected to grow at 2% CAGR (FY22-24)



Source: Company, ICICI Direct Research

Exhibit 9: PAT expected to grow at 15% CAGR in FY22-24



Source: Company, ICICI Direct Research

Exhibit 10: Valuation ratios

	Sales (₹ cr)	Sales Growth (%)	EPS (₹)	EPS Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY20	9325.4	-0.2	8.7	-9.0	91.3	27.8	17.7	23.8
FY21	8131.3	-12.8	5.0	-42.2	158.0	40.8	9.3	15.6
FY22	9712.4	19.4	11.2	123.1	70.8	26.4	16.7	24.4
FY23E	10170.9	4.7	20.6	84.4	38.4	30.4	23.2	28.8
FY24E	10833.5	6.5	15.0	-26.8	52.5	24.9	14.5	18.7

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 11: Profit and loss statement ₹ crore

(Year-end March)	FY21	FY22	FY23E	FY24E
Total operating Income	8,131.3	9,712.4	10,170.9	10,833.5
Growth (%)	-12.8	19.4	4.7	6.5
Cost of materials consumr	4,455.6	5,291.5	5,797.4	5,958.4
Employee benefit expens	556.4	653.1	661.1	660.8
Advertisement&Promo	574.7	694.9	813.7	975.0
Other Expenses	1,491.9	1,464.8	1,525.6	1,570.9
EBITDA	1,052.7	1,608.1	1,373.1	1,668.4
Growth (%)	-33.0	52.8	-14.6	21.5
Depreciation	299.1	303.8	228.0	246.0
EBIT	753.6	1,304.3	1,145.0	1,422.3
Interest	187.6	88.0	31.4	18.4
Other Income	39.6	35.5	841.5	57.2
Exceptional Item	-64.3	-165.2	-38.4	0.0
PBT	541.3	1,086.6	1,916.8	1,461.1
Tax	177.9	276.0	422.2	367.8
Reported PAT	363.4	810.6	1,494.5	1,093.3
Adjustments	20.2	18.0	0.0	0.0
Adjusted PAT	383.6	828.6	1,494.5	1,093.3
EPS	5.0	11.2	20.6	15.0

Source: Company, ICICI Direct Research

Exhibit 12: Cash flow statement ₹ crore

(Year-end March)	FY21	FY22	FY23E	FY24E
Profit after Tax	383.6	828.6	1,494.5	1,093.3
Add: Depreciation	299.1	303.8	228.0	246.0
Add: Interest paid	187.6	88.0	31.4	18.4
Cash Profit	682.7	1,132.4	1,722.5	1,339.4
Increase/(Decrease) in CL	94.8	-51.2	-334.6	1.6
(Increase)/Decrease in CA	77.7	-384.0	-85.0	-317.9
Others	774.9	103.3	0	0
CF from Operating Activitie	1,817.7	888.5	1,334.3	1,041.4
Purchase of Fixed Assets	-128.9	-77.8	345.2	-155.0
(Inc)/Dec in Investments	70.4	-155.4	-1,213.1	-666.2
Others	77.7	-55.9	211.4	65.1
CF from Investing Activitie	19.2	-289.1	-656.4	-756.1
Inc/(Dec) in Loan Funds	-744.0	-535.0	-100.0	-100.0
Inc/(Dec) in Sh. Cap. & Re	0.0	0.0	0.0	0.0
Less: Interest paid	-187.6	-88.0	-31.4	-18.4
Others	-894.9	0.0	0.0	0.0
CF from financing activitie	-1,826.5	-623.0	-131.4	-118.4
Op. Cash and cash Eq.	73.5	83.9	60.3	606.8
Adjustments	0	0	0	0
Cl. Cash and cash Eq.	83.9	60.3	606.8	773.7

Source: Company, ICICI Direct Research

Exhibit 13: Balance Sheet ₹ crore

(Year-end March)	FY21	FY22	FY23E	FY24E
Source of Funds				
Equity Capital	145.3	145.3	145.3	145.3
Reserves & Surplus	3,974.5	4,808.4	6,302.9	7,396.3
Shareholder's Fund	4,119.8	4,953.7	6,448.2	7,541.6
Minority Interest	-60.9	-78.9	-78.9	-78.9
Loan Funds	876.7	341.7	241.7	141.7
Provisions	9.6	48.3	53.1	58.4
Other Liabilities	157.8	263.7	290.1	319.1
Total Current Liabilities	3,434.0	3,382.8	3,048.2	3,049.8
Source of Funds	8,537.0	8,911.3	10,002.4	11,031.7
Application of Funds				
Gross Block	2,246.9	2,250.2	1,900.2	2,050.2
Less: Acc. Depreciation	922.2	1,035.0	1,263.0	1,509.0
Net Block	1,324.7	1,215.2	637.2	541.2
Intangible Assets	375.5	358.0	358.0	358.0
Capital WIP	96.7	95.7	100.5	105.5
Goodwill	21.0	21.0	21.0	21.0
Non-Current Investments	23.7	0.0	1,150.0	1,750.0
Deferred Tax Assets (net)	171.1	147.8	0.0	0.0
Long term loans & advan	1,082.3	1,261.4	1,324.5	1,390.7
Other Non current assets	639.0	648.8	616.4	585.5
Current Investments	0.0	222.1	222.1	222.1
Inventories	2,051.9	2,156.7	2,089.9	2,226.1
Debtor	2,187.2	2,373.6	2,507.9	2,671.3
Cash	83.9	60.3	606.8	773.7
Loan & Advance, Other C	480.0	350.7	368.2	386.6
Total Current assets	4,803.0	5,163.4	5,794.9	6,279.8
Application of Funds	8,537.0	8,911.3	10,002.4	11,031.7

Source: Company, ICICI Direct Research

Exhibit 14: Key ratios

(Year-end March)	FY21	FY22	FY23E	FY24E
Per share data (₹)				
Book Value	56.7	68.2	88.7	103.8
Cash per share	1.2	0.8	8.4	10.6
EPS	5.0	11.2	20.6	15.0
Cash EPS	9.4	15.6	23.7	18.4
DPS	0.0	0.0	0.0	0.0
Profitability & Operating Ratios				
EBITDA Margin (%)	12.9	16.6	13.5	15.4
PAT Margin (%)	4.7	8.5	14.7	10.1
Fixed Asset Turnover (x)	3.6	4.3	5.4	5.3
Inventory Turnover (Days)	92.1	81.1	75.0	75.0
Debtor (Days)	98.2	89.2	90.0	90.0
Creditors (Days)	63.6	59.5	48.0	48.0
Return Ratios (%)				
RoE	8.8	16.4	23.2	14.5
RoCE	15.6	24.4	28.8	18.7
RoIC	15.4	24.9	23.2	27.6
Valuation Ratios (x)				
P/E	158.0	70.8	38.4	52.5
Price to Book Value	10.2	8.5	6.5	5.6
EV/EBITDA	40.8	26.4	30.4	24.9
EV/Sales	5.3	4.4	4.1	3.8
Leverage & Solvency Ratios				
Debt to equity (x)	0.2	0.1	0.0	0.0
Interest Coverage (x)	4.0	14.8	36.4	77.2
Debt to EBITDA (x)	1.5	0.5	0.2	0.1
Current Ratio	1.4	1.5	1.9	2.1

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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