

CMP: ₹ 1417

Target: ₹ 1470 (4%)

Target Period: 12 months

HOLD

May 3, 2023

Splendid volume growth continues...

About the stock Varun Beverage (VBL) is one of the largest franchisees of PepsiCo in the world. The company produces & distributes carbonated drinks, juices & packaged drinking water in six countries including India. Some of the PepsiCo brands produced by VBL include Pepsi, Diet Pepsi, Seven-Up, Mirinda, Mountain Dew, Nimbooz, String, Slice, Tropicana, Aquafina among others.

- The company has operations in India (except Andhra Pradesh, J&K & Ladakh), Sri Lanka, Nepal, Morocco, Zambia and Zimbabwe

Q1CY23 Results: Varun Beverages witnessed strong volume growth of 24.7%.

- Sales were up 37.7% YoY led by 24.7% volume & 10.4% realisation growth
- EBITDA was at ₹ 798 crore, up 50.3% YoY, with margins at 20.5%
- Consequently, PAT was at ₹ 438.6 crore, up 61.8%

What should investors do? Varun Beverage's share price has given 6.6x return (from ₹ 214 in April 2018 to ₹ 1417 in April 2023).

- We estimate 11% volume CAGR and sustainable operating margins above 21%. This would lead to earning CAGR of 16.4% in CY22-24E
- We maintain our **HOLD** recommendation on the stock

Target Price and Valuation: We value the stock at ₹ 1470, valuing the business at 45x CY24 PE.

Key triggers for future price performance:

- VBL has seen 15% organic volume growth in the last three years led by distribution expansion in underpenetrated territories and new launches (Sting, Milk based beverages, etc). It is continuing the growth momentum with 25% volume growth in Q1CY23
- It has commissioned greenfield capacity in Kota, Rajasthan and is expected to commission another plant in Jabalpur, MP soon. This, along with brownfield expansion in six other plants have improved capacity by 20-25%
- The growth in newer brands like 'Sting' & milk-based beverages growing at faster pace, supporting overall volume growth. VBL would undertake capex with two new facilities in Maharashtra & UP for energy & milk beverages

Alternate Stock Idea: We like Tata Consumer Products in our FMCG coverage.

- Strong innovation & premiumisation strategy in salt, tea, Sampann & Soulful in the India market are expected to drive sales and margins
- We value the stock at ₹ 980 on ascribing 52x FY25 earnings multiple

Key Financial Summary

	CY20	CY21	CY22	5 Year CAGR (CY17- CY22)	CY23E	CY24E	CAGR (CY22-24E)
Net Sales	6450.1	8823.2	13173.1	26.9	15181.0	16957.2	13.5%
EBITDA	1201.9	1654.6	2788.1	27.2	3258.1	3662.8	14.6%
EBITDA Margin %	18.6	18.8	21.2		21.5	21.6	
Net Profit	362.1	746.1	1550.1	48.6	1788.2	2100.4	16.4%
Diluted EPS (₹)	5.57	11.49	23.86	15.3	27.53	32.34	16.4%
P/E	254.2	123.4	59.4		51.5	43.8	
RoNW %	10.3	18.3	30.4		27.8	26.9	
RoCE (%)	10.9	17.1	23.8		28.7	32.2	

Source: Company, ICICI Direct Research



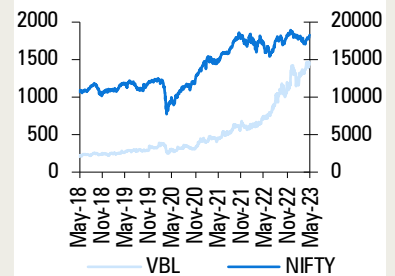
Particulars

Particulars (₹ crore)	Amount
Market Capitalization	92,041.0
Total Debt (CY22)	3,718.4
Cash & Investments (CY22)	371.7
EV	95,387.6
52 week H/L (₹)	1480 / 675
Equity capital	288.7
Face value	10.0

Shareholding pattern

(in %)	Jun-22	Sep-22	Dec-22	Mar-23
Promoter	63.9	63.9	63.9	63.9
FII	23.9	25.0	26.5	26.0
DII	5.3	4.5	3.4	3.7
Others	6.9	6.6	6.2	6.4

Price Chart



Recent event & key risks

- VBL has expanded its capacity by 20-25% after completing ₹1500 crore capex
- Key Risk:** (i) Possibility of softer summer product demand given high base of 2022 (ii) Any sharp increase in RM cost like PET or sugar may impact gross margins adversely

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Key takeaways of recent quarter

Q1CY23 Results: Margin expansion propelled by operating leverage

- Revenue witnessed growth of 37.7% to ₹ 3893 crore led by 24.7% & 10.4% growth in net realisation, respectively, in Q1CY23. Consolidated sales volume grew 24.7% to 224.1 million cases & average realisations increased 10.4% to ₹ 173.7 / case during the quarter. Domestic volume grew 28%
- Carbonated soft drinks (CSD), juices & water account for 71.2%, 7.4% & 21.4%, respectively, of total volumes. The strong growth was led by stupendous growth in energy drink brand 'Sting'
- CSD volumes have grown by 27% to 160 million cases whereas juices & water volumes have grown at 23.1% & 17.1% to 16 million cases & 48 million cases, respectively
- Rural growth has recovered and now both rural & urban regions are growing at a similar rate
- Gross margins expanded 89 bps on account of a softening of major raw material prices & increasing contribution of high margins products. Employee spends (percentage to sales) were down 102 bps while overhead spends (percentage to sales) were up 19 bps during the quarter
- Operating profit grew 50.3% to ₹ 798 crore with operating profit margin expansion of 172 bps to 20.5% on the back of operating leverage benefit. Net profit grew 61.8% to ₹ 438.6 crore
- The company has commissioned its greenfield facility at Kota, Rajasthan. Further, it has expanded its capacity at six existing locations. Another greenfield plant in Jabalpur, MP would get commissioned soon. The company incurred ₹ 1500 crore capex for this capacity addition
- Energy drink 'Sting' continues to grow at a faster pace in Q1 with double digit volume growth. Energy drink growth has been aided by distribution expansion & addition of Visi-Coolers
- The growth in juices & milk-beverages was constrained by lack of capacity. VBL would be commissioning two plants in Maharashtra and UP by the end of the year. The company is concentrating on juices, sports drinks & milk-beverages to drive the next level of growth
- Margins in sports drinks, juices & milk-beverages are similar to the existing carbonated soft drinks. GST + cess for soft drinks is 40% whereas it is only 12% for other beverages. Given the company is in value added milk products rather than plain milk, margins in the category are strong
- Major raw materials like PET & sugar prices have remained stable. A small increase in prices in future would not adversely impact margins in the medium term
- International business margins were lower mainly due to adverse currency movement in Zambia
- Direct distribution reach for the company has increased by 10% from 3 million retail outlets to 3.3 million retail outlets with total number of distributors at 2400. VBL would continue to focus on increasing distribution
- Sports drink Gatorade, which was only available in 500 ml SKU is now available in 200 ml SKU as well. With the capacity expansion, smaller SKUs & higher distribution reach, sports drink brand can grow at a faster pace, going forward
- The current net debt for the company is at ₹ 4000 crore and debt to EBITDA was at 1.3x. With the increase in asset turnover, return ratios can improve from 30% to 35% in the next three to five years

Varun Beverages - ESG Disclosure Score*

ESG Disclosure Score			
Score	CY19	CY20	CY21
Environmental	5.8	10.1	10.1
Social	17.4	17.4	22.6
Governance	73.6	76.1	76.1
Overall ESG Score	32.3	34.6	36.3

- The Board recommended stock split of existing equity shares of the company from one equity share having face value of ₹ 10 each into two equity shares having face value of ₹ 5 each

Exhibit 1: Peer Comparison

Sector / Company	CMP (₹)	TP (₹)	Rating	M Cap (₹ Cr)	Sales growth (%)				EBITDA Margins (%)				P/E(x)				RoE (%)				RoCE (%)			
					FY22	FY23E	FY24E	FY25E	FY22	FY23E	FY24E	FY25E	FY22	FY23E	FY24E	FY25E	FY22	FY23E	FY24E	FY25E	FY22	FY23E	FY24E	FY25E
Nestle (NESIND)	21750	23000	Hold	199195	10.2	14.9	12.8	10.5	24.5	22.1	23.0	24.7	97.8	87.7	72.5	61.7	104.1	87.0	84.5	86.5	57.3	54.4	57.0	61.6
Dabur India (DABIND)	536	700	Buy	97880	13.9	5.9	10.6	10.9	20.7	19.6	20.7	20.9	54.4	52.3	44.6	39.9	20.8	20.5	22.2	22.7	24.9	23.9	26.1	27.2
Varun Beverage (VARBEV)	1415	1470	Hold	92041	36.8	49.3	15.2	11.7	18.8	21.2	21.5	21.6	82.1	59.3	51.4	43.8	18.3	30.4	27.8	26.9	17.1	23.8	28.7	32.2
Zydus Wellness (ZYDWEL)	1511	2000	Buy	8979	23.1	14.3	21.6	12.1	17.2	17.3	18.8	19.7	31.1	27.5	22.4	20.0	6.4	7.1	8.3	9.0	6.1	6.8	8.1	9.2

Source: Company, ICICI Direct Research

VBL has maintained growth momentum in Q1 with strong growth across categories. With the distribution expansion & strong growth in energy drink ‘Sting’, the company has been able to grow at faster pace in last one year. The company is focusing on sports drink ‘Gatorade’, juices & milk based beverages to maintain current growth momentum. Further, softening of raw material prices have expanded margins above 21% level. We believe raw material prices would remain benign in the medium term, which would help the company to sustain high margins. The company is expanding capacity in markets with high growth potential like Madhya Pradesh, Rajasthan, Uttar Pradesh and Bihar. It is important to see if the company would be able to maintain the growth momentum on the very high base of last year. We remain positive on the company from a long-term perspective. We maintain our HOLD rating with a revised target price of ₹1470 (earlier: ₹ 1340).

Exhibit 2: Variance Analysis

Particulars (₹ crore)	Q1CY23	Q1CY22	YoY (%)	Q4CY22	QoQ (%)	Comments
Net Sales	3,893.0	2,827.5	37.7	2,214.2	75.8	Net sales witnessed a growth of 37.7% led by 24.7% volume & 10.4% realisation growth
Raw Material Expenses	1,851.7	1,370.2	35.1	967.8	91.3	Gross margin expanded by 89 bps on account of softening of key raw material prices like PER resins
Employee Expenses	339.1	275.1	23.3	319.9	6.0	Employee spends contracted by 102 bps
Other operating Expenses	904.1	651.2	38.8	619.0	46.1	Ovehead spends were up by 19 bps
EBITDA	798.0	531.0	50.3	307.5	159.5	Operating profit grew by 50.3% led by strong sales growth, higher gross margins & operating leverage benefits
EBITDA Margin (%)	20.5	18.8	172 bps	13.9	661 bps	
Depreciation	172.2	131.3	31.1	179.7	-4.2	
Interest	62.6	47.0	33.3	47.5	31.8	
Other Income	10.1	8.5	19.1	9.2	9.6	
PBT	573.4	361.2	58.7	89.6	539.9	
Exceptional Items	0.0	0.0		0.0		
Tax Outgo	134.8	90.1	49.6	8.1	1,568.8	
PAT	438.6	271.1	61.8	81.5	438.0	Net profit grew by 61.8% driven by strong operating profit growth
Adj. PAT	438.6	271.1	61.8	81.5	438.0	

Source: Company, ICICI Direct Research

Exhibit 3: Change in estimates

(₹ Crore)	CY23E			CY24E			Comments
	Old	New	% Change	Old	New	% Change	
Net Sales	14,558.6	15,181.0	4.3	16,263.8	16,957.2	4.3	We raise our volume growth estimate based given beverage category is growing at faster pace
EBITDA	3,105.3	3,258.1	4.9	3,478.2	3,662.8	5.3	
EBITDA Margin(%)	21.3	21.5	13 bps	21.4	21.6	21 bps	
PAT	1,692.2	1,788.2	5.7	1,946.5	2,100.4	7.9	
EPS (₹)	26.1	27.5	5.7	30.0	32.3	7.9	

Source: ICICI Direct Research

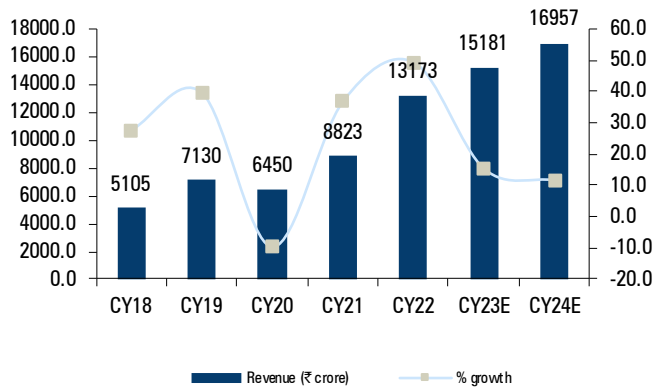
Exhibit 4: Assumptions

Particulars (in million cases)	Current					Earlier			Comments
	CY19	CY20	CY21	CY22	CY23E	CY24E	CY23E	CY24E	
Carbonated Products	347.0	309.0	399.8	562.0	629.4	686.1	618.2	673.8	
Non Carbonated drinks	33.0	26.0	36.1	57.0	63.8	71.5	63.8	71.5	We change our estimate factoring in strong growth in Carbonated soft drinks
Water	111.0	90.0	132.3	182.0	203.8	224.2	205.7	226.2	

Source: ICICI Direct Research

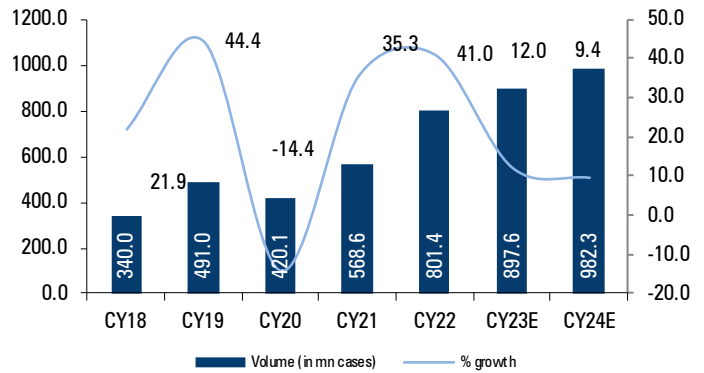
Key Metrics

Exhibit 5: Revenue growth trend (₹ crore)



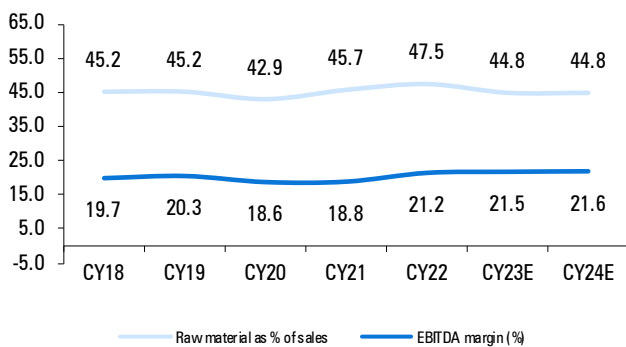
Source: Company, ICICI Direct Research

Exhibit 6: Volume recovery to drive growth



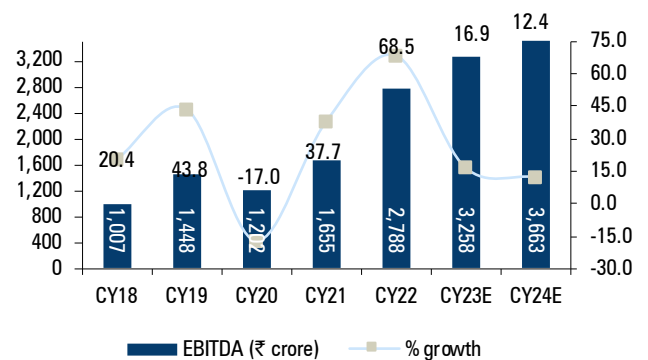
Source: Company, ICICI Direct Research

Exhibit 7: Raw material to sales & EBITDA margins (%)



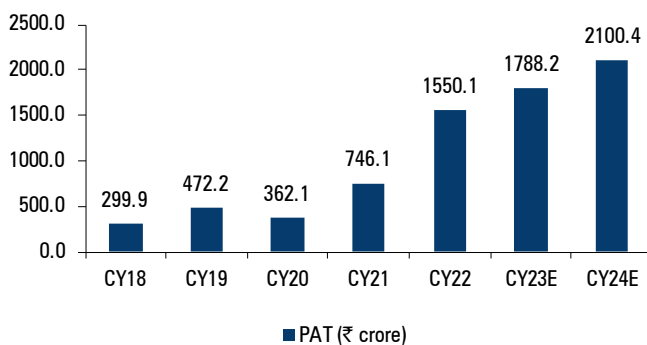
Source: Company, ICICI Direct Research

Exhibit 8: EBITDA (₹ crore) & EBITDA growth (%) trend



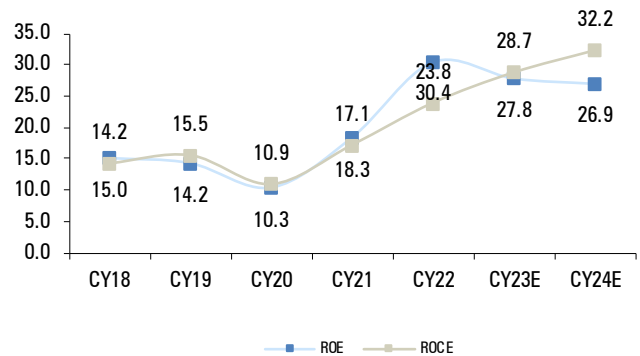
Source: Company, ICICI Direct Research

Exhibit 9: Robust earnings growth in last five years (₹ crore)



Source: Company, ICICI Direct Research

Exhibit 10: Return ratio trend (%)



Source: Company, ICICI Direct Research

Exhibit 11: Valuation

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
CY21	8823.2	36.8	17.2	106.1	82.2	57.0	18.3	17.1
CY22	13173.1	49.3	23.9	38.5	59.4	34.3	30.4	23.8
CY23E	15181.0	15.2	27.5	15.4	51.5	28.8	27.8	28.7
CY24E	16957.2	11.7	32.3	17.5	43.8	25.2	26.9	32.2

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 12: Profit and loss statement				
	₹ crore			
	CY21	CY22	CY23E	CY24E
Total operating income	8823.2	13173.1	15181.0	16957.2
Growth (%)	36.8	49.3	15.2	11.7
Raw Material Expenses	4034.7	6261.2	6805.6	7600.6
Employee Expenses	1007.7	1216.6	1411.8	1610.9
Marketing Expenses	0.0	0.0	279.0	311.5
Other expenses	2126.2	2907.2	3426.5	3771.3
Total Operating Expenditure	7168.6	10385.0	11922.9	13294.4
EBITDA	1,654.6	2,788.1	3,258.1	3,662.8
Growth (%)	37.7	68.5	16.9	12.4
Depreciation	531.3	617.2	774.0	811.4
Interest	184.7	186.1	204.5	201.8
Other Income	67.9	38.8	42.7	43.2
PBT	1006.6	2023.6	2322.3	2692.8
Total Tax	260.6	473.5	534.1	592.4
Minority interest	0.0	0.0	0.0	0.0
Profit from Associates	0.0	0.0	0.0	0.0
PAT	746.1	1,550.1	1,788.2	2,100.4
Growth (%)	106.1	107.8	15.4	17.5
EPS (₹)	17.2	23.9	27.5	32.3

Source: Company, ICICI Direct Research

Exhibit 13: Cash flow statement				
	₹ crore			
(Year-end March)	CY21	CY22	CY23E	CY24E
Profit After Tax	1,067.4	1,835.8	1,992.7	2,302.2
Add: Depreciation	531.3	583.1	774.0	811.4
(Inc)/dec in Current Assets	-596.8	-1,005.9	-613.2	-625.1
Inc/(dec) in CL and Provisions	328.1	420.7	1,564.8	650.0
CF from operating activities	1,231.4	1,790.0	3,718.3	3,138.5
(Inc)/dec in Investments	0.0	0.0	0.0	0.0
(Inc)/dec in LT loans & advances	0.0	0.0	0.0	1.0
(Inc)/dec in Fixed Assets	-815.4	-1,749.9	-1,028.9	-878.9
Others	-87.7	45.3	0.0	0.0
CF from investing activities	-1,010.6	-1,704.6	-1,028.9	-878.9
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	109.7	339.6	-1,700.0	-1,200.0
Dividend paid & dividend tax	-108.3	-162.4	-447.0	-735.1
Others	-179.1	-171.7	-204.5	-201.8
CF from financing activities	-177.7	-17.9	-2,603.0	-2,108.5
Net Cash flow	43.1	67.5	86.4	151.0
Opening Cash	104.6	150.8	154.3	240.8
Other Bank balance	185.9	185.9	185.9	185.9
Closing Cash	150.8	154.3	240.8	391.8

Source: Company, ICICI Direct Research

Exhibit 14: Balance Sheet				
	₹ crore			
(Year-end March)	CY21	CY22	CY23E	CY24E
Liabilities				
Equity Capital	433.0	649.5	649.5	649.5
Reserve and Surplus	3646.9	4452.8	5794.0	7159.2
Total Shareholders funds	4079.9	5102.4	6443.5	7808.8
LT Borrowings & Provisions	1813.3	1727.0	1227.0	577.0
Deferred Tax Liability	311.1	336.8	353.7	371.4
Total Liabilities	6561.6	7649.5	8239.2	8982.8
Assets				
Gross Block	8,974.6	10,220.9	11,727.5	12,677.5
Less: Acc Depreciation	3,246.6	3,863.8	4,637.8	5,449.2
Net Block	5,728.0	6,357.1	7,089.7	7,228.3
Capital WIP	496.6	606.6	150.0	50.0
Net Intangible Assets	558.6	550.9	578.5	607.4
Non-current Investments	0.8	0.0	0.0	0.0
Goodwill	24.2	24.2	24.2	24.2
Current Assets				
Inventory	1,448.1	1,993.9	2,403.7	2,826.2
Debtors	221.2	299.3	379.5	471.0
Loans and Advances	9.5	0.0	21.1	23.6
Other Current Assets	301.9	427.8	548.2	612.3
Cash	150.8	154.3	240.8	391.8
Deferred Tax Assets	2.4	0.0	0.0	0.0
Current Liabilities				
Creditors	711.8	824.3	927.7	1,036.3
Provisions	49.7	29.2	84.3	94.2
Short term debt & other CL	2,244.8	3,039.7	3,321.5	3,303.1
Application of Funds	6,561.6	7,649.5	8,239.2	8,982.8

Source: Company, ICICI Direct Research

Exhibit 15: Key ratios				
(Year-end March)	CY21	CY22	CY23E	CY24E
Per share data (₹)				
EPS	17.2	23.9	27.5	32.3
Cash EPS	29.5	33.4	39.4	44.8
BV	94.2	78.6	99.2	120.2
DPS	2.5	6.0	6.9	11.3
Cash Per Share	75.0	59.5	71.4	83.9
Operating Ratios (%)				
EBITDA Margin	18.8	21.2	21.5	21.6
PBT / Total Operating income	11.4	15.4	15.3	15.9
PAT Margin	8.5	11.8	11.8	12.4
Inventory days	59.9	55.2	57.8	60.8
Debtor days	9.2	8.3	9.1	10.1
Creditor days	29.4	22.8	22.3	22.3
Return Ratios (%)				
RoE	18.3	30.4	27.8	26.9
RoCE	17.1	23.8	28.7	32.2
Valuation Ratios (x)				
P/E	82.2	59.4	51.5	43.8
EV / EBITDA	57.0	34.3	28.8	25.2
EV / Net Sales	10.7	7.3	6.2	5.5
Market Cap / Sales	10.4	7.0	6.1	5.4
Price to Book Value	15.0	18.0	14.3	11.8
Solvency Ratios				
Debt/EBITDA	1.5	1.3	0.6	0.2
Debt / Equity	0.6	0.7	0.3	0.1
Current Ratio	0.7	1.2	0.8	0.8
Quick Ratio	0.1	0.2	0.1	0.1

Source: Company, ICICI Direct Research

Exhibit 16: ICICI Direct coverage universe (FMCG)

	CMP	TP	M Cap	EPS (₹)				P/E (x)				Price/Sales (x)				RoCE (%)			RoE (%)					
	(₹)	(₹) Rating		(₹ Cr)	FY22	FY23E	FY24E	FY25E	FY22	FY23E	FY24E	FY25E	FY22	FY23E	FY24E	FY25E	FY22	FY23E	FY24E	FY25E				
Colgate (COLPAL)	1,572	1,440	Hold	39,473	39.6	37.7	40.3	41.7	39.7	41.6	39.0	37.7	7.8	7.6	7.1	6.7	77.8	81.9	92.8	99.9	62.2	62.4	70.9	76.5
Dabur India (DABIND)	536	700	Buy	97,880	9.9	10.3	12.0	13.4	54.4	52.3	44.6	39.9	9.0	8.5	7.7	6.9	24.9	23.9	26.1	27.2	20.8	20.5	22.2	22.7
Hindustan Unilever (HINLEV)	2,452	2,780	Hold	5,79,879	37.5	42.4	45.4	51.1	65.3	57.8	54.0	48.0	11.5	10.0	9.2	8.4	20.2	22.0	23.7	25.9	18.1	19.9	20.6	22.5
ITC Limited (ITC)	424	450	Buy	4,67,841	12.4	14.7	16.0	17.4	34.2	28.9	26.5	24.4	7.9	6.8	6.2	5.7	31.4	36.0	37.5	39.1	24.5	27.7	28.7	29.9
Jyothy Lab (JYOLAB)	192	215	Hold	7,485	4.3	6.7	7.8	8.5	45.2	28.9	24.7	22.7	3.5	3.1	2.8	2.6	18.7	27.5	31.4	32.6	16.6	24.2	27.0	27.9
Marico (MARLIM)	500	555	Hold	63,710	9.7	10.3	11.1	12.4	51.4	48.5	44.9	40.3	6.7	6.5	6.0	5.6	41.2	44.0	46.2	49.9	37.5	38.5	40.6	43.8
Nestle (NESIND)	21,750	23,000	Hold	1,99,195	222.4	247.9	299.9	352.7	97.8	87.7	72.5	61.7	13.6	11.9	10.5	9.5	57.3	54.4	57.0	61.6	104.1	87.0	84.5	86.5
Patanjali Foods (RUCSOY)	936	1,750	Buy	50,721	27.3	30.9	43.5	52.7	34.3	30.3	21.5	17.7	2.1	1.7	1.5	1.4	13.2	15.6	17.3	19.0	13.1	11.3	14.2	15.3
Tata Consumer Products (TAT)	780	980	Buy	68,740	11.0	14.2	16.4	19.0	70.8	54.9	47.7	41.0	5.5	5.0	4.5	4.1	8.4	8.7	10.5	11.6	7.0	7.4	9.0	10.1
Varun Beverage (VARBEV)	1,415	1,470	Hold	92,041	17.2	23.9	27.5	32.3	82.1	59.3	51.4	43.8	10.4	7.0	6.1	5.4	17.1	23.8	28.7	32.2	18.3	30.4	27.8	26.9
VST Industries (VSTIND)	3,285	3,300	Hold	5,059	207.4	211.8	210.0	245.5	15.8	15.5	15.6	13.4	4.3	3.9	3.7	3.4	39.0	35.7	39.0	50.9	29.8	27.7	29.3	38.2
Zydus Wellness (ZYDWEL)	1,511	2,000	Buy	8,979	48.5	55.0	67.4	75.6	31.1	27.5	22.4	20.0	4.5	4.0	3.6	3.2	6.1	6.8	8.1	9.2	6.4	7.1	8.3	9.0

Source: Bloomberg, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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