

Varun Beverages Limited

3rd August 2023

Growth momentum to continue

In Q2 CY23, Varun Beverages Limited (VBL) reported a stable topline growth of ~13% and volume growth of ~5% on a YoY basis. The Company has improved its Gross margins and EBITDA margins by 196 bps & 169 bps on a YoY basis on the back of softening of PET chip prices and operational efficiencies. For the next leg of growth, VBL will focus on value-added dairy products, energy drinks and juices. The Company has commissioned greenfield plants and brownfield manufacturing lines to ramp up its operational capacity. Given the growth outlook and guidance, we maintain our stance on VBL with a BUY rating and a target price of Rs. 962, valuing it at 55x CY24 earnings.

Stable volume growth with a reducing raw material prices led to margin improvement

In Q2 CY23, VBL achieved a YoY volume growth of ~5%, accompanied by an increase in realization per case by ~8%. The Company's gross margin improved due to a decrease in PET chip prices. Furthermore, VBL's EBITDA per case improved by ~15% from ~42 to ~48 on a YoY basis due to operational efficiencies.

Expansion for next leg of growth

The Company has successfully set up greenfield plants and brownfield manufacturing lines in Bundi, Rajasthan, and Jabalpur, Madhya Pradesh, while also augmenting the capacity at six existing locations. In addition to this, the Company is actively engaged in establishing greenfield facilities in Uttar Pradesh, Maharashtra, and Odisha, in addition to one international plant in the Democratic Republic of the Congo (DRC). These strategic initiatives align with their previously communicated plans to address the growing demand for juices and dairy products.

View & Valuation

Based on the increase in operating capacity and change in product mix, we believe that in CY23 & CY24, VBL would be able to grow in volume by ~12% & ~10% respectively and realization by ~9% and ~5% respectively. Based on our revised estimates, we maintain a BUY rating on Varun Beverages with a target of Rs. 962 (55x CY24 earnings).

BUY

CMP Rs. 824
TARGET Rs. 962 (+17%)

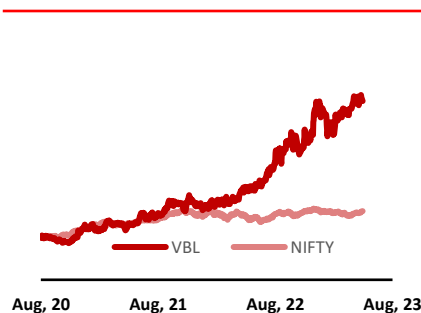
Company Data

Bloomberg Code	VBL IN
MCAP (Rs. Mn)	10,705,448
O/S Shares (Mn)	1299
52w High/Low	874/452
Face Value (in Rs.)	5
Liquidity (3M) (Rs. Mn)	1,915

Shareholding Pattern %

	Jun 23	Mar 23	Dec 22
Promoters	63.6	63.9	63.9
FII's	26.7	26	26.5
DII's	3.2	3.7	3.4
Non-Institutional	6.5	6.4	6.2

VBL vs Nifty



Source: Keynote Capitals Ltd.

Key Financial Data

(Rs Bn)	CY22	CY23E	CY24E
Revenue	131.7	160.9	180.5
EBITDA	27.9	35	38.4
Net Profit	15.0	19.5	21.6
Total Assets	116.1	136.7	154.1
ROCE (%)	23%	24%	24%
ROE (%)	33%	32%	28%

Source: Company, Keynote Capitals Ltd.

Devin Joshi, Research Analyst
Devin@keynoteindia.net

Varun Beverages Limited | Quarterly Update

Q2 CY23 Result Update

Result Highlights (Rs. Mn)

Particulars	Q2 CY23	Q2 CY22	Change % (Y-o-Y)	Q1 CY23	Change % (Q-o-Q)	H1 CY23	H1 CY22	Change % (Y-o-Y)	CY22
Revenue from Operation	56,114	49,548	13%	38,930	44%	95,044	77,823	22%	1,31,731
Gross Profit	29,448	25,030	18%	20,413	44%	49,861	39,603	26%	69,120
Gross Profit %	52.5%	50.5%	196 Bps	52.4%	4 Bps	52.5%	50.9%	157 Bps	52.5%
Employee Cost	3,646	3,104	17%	3,391	8%	7,037	5,855	20%	12,166
Other Expenses	10,692	9,419	14%	9,041	18%	19,733	15,932	24%	29,072
EBITDA	15,110	12,506	21%	7,981	89%	23,091	17,816	30%	27,881
EBITDA %	26.9%	25.2%	169 Bps	20.5%	643 Bps	24.3%	22.9%	140 Bps	21.2%
Depreciation	1,719	1,531	12%	1,722	0%	3,441	2,844	21%	6,172
EBIT	13,391	10,975	22%	6,259	114%	19,649	14,972	31%	21,709
EBIT %	23.9%	22.2%	171 Bps	16.1%	779 Bps	20.7%	19.2%	144 Bps	16.5%
Finance Cost	694	464	50%	626	11%	1,319	934	41%	1,861
Other Income	416	105	297%	101	312%	517	190	173%	388
PBT	13,113	10,616	24%	5,734	129%	18,847	14,229	32%	20,236
Tax Expenses	3,057	2,596	18%	1,348	127%	4,405	3,497	26%	4,735
Profit from Associates	-2	0		0		-3	0		0
Minority Interest	116	146	-20%	95	22%	211	315	-33%	527
PAT attributable to shareholders	9,938	7,874	26%	4,291	132%	14,229	10,416	37%	14,974
EPS	7.65	6.06		3.30		10.95	8.02		11.53

Source: Company, Keynote Capitals Ltd.

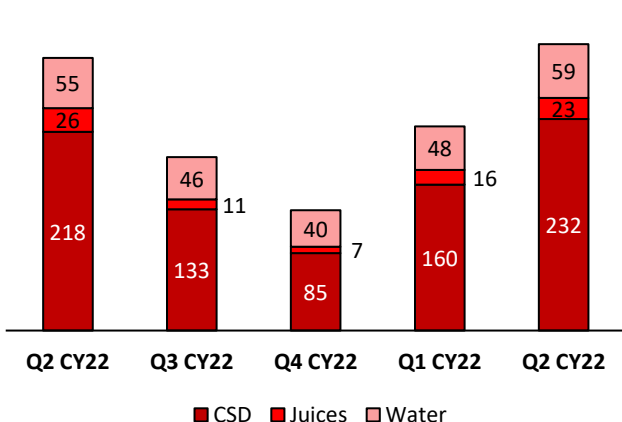
Unit Economics (Rs/Case)

Particulars	Q2 CY23	Q2 CY22	Change % (Y-o-Y)	Q1 CY23	Change % (Q-o-Q)	H1 CY23	H1 CY22	Change % (Y-o-Y)	CY22
Volume Sold (Mn Cases)	314	300	5%	224	40%	538	480	12%	802
Revenue from Operation	178.7	165.2	8%	173.8	3%	176.7	162.1	9%	164.3
Gross Profit	93.8	83.4	12%	91.1	3%	92.7	82.5	12%	86.2
Employee Cost	11.6	10.3	12%	15.1	-23%	13.1	12.2	7%	15.2
Other Expenses	34.1	31.4	8%	40.4	-16%	36.7	33.2	11%	36.2
EBITDA	48.1	41.7	15%	35.6	35%	42.9	37.1	16%	34.8
EBIT	42.6	36.6	17%	27.9	53%	36.5	31.2	17%	27.1
PBT	41.8	35.4	18%	25.6	63%	35.0	29.6	18%	25.2
Tax Expenses	9.7	8.7	12%	6.0	62%	8.2	7.3	12%	5.9
PAT attributable to shareholders	31.7	26.2	21%	19.2	65%	26.4	21.7	22%	18.7

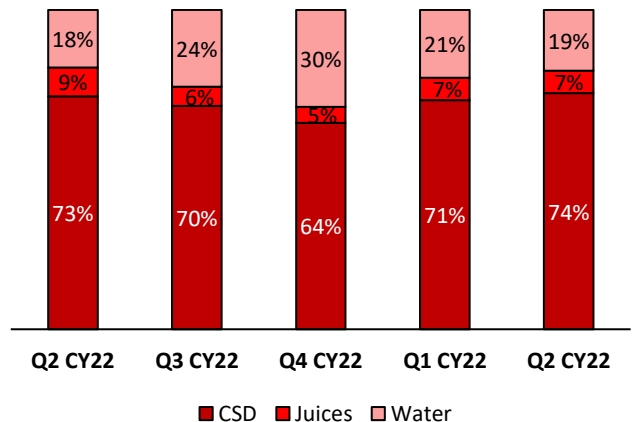
Source: Company, Keynote Capitals Ltd.

Quarterly Business Progression

Volume Sold (in Mn cases) [Product-wise]



Volume Mix% [Product-wise]



Source: Company, Keynote Capitals Ltd.

Q2 CY23 Conference Call Highlights

General Highlights

- Recently, the Company has introduced 100% recycled PET bottles for Pepsi Black in specific sub-territories.
- VBL has incorporated a wholly owned subsidiary in Johannesburg (South Africa) to explore the business of manufacturing and distribution of beverages.
- During Q2 CY23, gross margins experienced a notable improvement, rising by 196 basis points to 52.5% from 50.5% on a YoY basis, primarily attributed to the decline in PET chips prices.
- EBITDA margins demonstrated significant progress, increasing by 169 basis points from 25.2% to 26.9% in Q2 CY23 on a YoY basis, driven by enhanced gross margins and operational efficiencies.
- In Q2 CY23, depreciation increased by 12.3%, and finance costs rose by 49.5% on a YoY basis due to the capitalization of assets and the establishment of new production facilities.
- As of June 30, 2023, the net debt stood at ~Rs 32 Bn, compared to Rs 34 Bn as of December 31, 2022.
- The continued enhancement in the proportion of smaller SKUs (250ml) as compared to Q2 CY22 contributed to an ~8% increase in realization.

Management Guidance

- The Company experienced a deceleration in demand, which was attributed solely to sales in the northern regions of India, caused by unseasonal rains.
- Within the international market, larger territories such as Zimbabwe and Morocco exhibited faster growth compared to other regions.
- Dairy products achieved a realization that is 15-20% higher than Carbonated Soft Drinks (CSD).
- The management stated that it is premature to make any comments regarding the potential competition posed by Campa Cola.

CAPEX

- The Company has commissioned greenfield plants and brownfield manufacturing lines to ramp up its operational capacity.
- At present, the Company is actively engaged in establishing greenfield facilities in Uttar Pradesh, Maharashtra, and Odisha, in addition to one international plant in the Democratic Republic of the Congo (DRC). These upcoming facilities are anticipated to be operational before the next season, effectively alleviating capacity constraints for Juices and Dairy products.

Varun Beverages Limited | Quarterly Update

Financial Statement Analysis

Income Statement						Cash Flow					
Y/E Mar, Rs. Mn	CY21	CY22	CY23E	CY24E	CY25E	Y/E Mar, Rs. Mn	CY21	CY22	CY23E	CY24E	CY25E
Net Sales	88,232	1,31,731	1,60,863	1,84,027	2,08,503	Pre-tax profit	10,066	20,236	26,738	31,074	35,966
Growth %		49%	22%	14%	13%	Adjustments	6,178	7,249	8,883	9,625	10,098
Raw Material Expenses	40,347	62,612	75,927	86,861	98,413	Change in Working Capital	-2,687	-5,852	-2,675	-3,140	-2,777
Employee Expenses	10,077	12,166	14,478	16,562	18,765	Total Tax Paid	-1,242	-3,733	-6,685	-7,768	-8,991
Other Expenses	21,040	28,893	35,390	40,486	45,871	Cash flow from operating Activities	12,314	17,900	26,262	29,790	34,295
EBITDA	16,769	28,061	35,068	40,118	45,454	Net Capital Expenditure	-8,154	-17,499	-19,000	-10,000	-10,000
Growth %		67%	25%	14%	13%	Change in investments	1	4	0	0	0
Margin%	19%	21%	22%	22%	22%	Other investing activities	-1,953	449	400	400	400
Depreciation	5,313	6,172	6,835	7,705	8,305	Cash flow from investing activities	-10,106	-17,046	-18,600	-9,600	-9,600
EBIT	11,457	21,889	28,233	32,413	37,149	Equity raised / (repaid)	0	0	0	0	0
Growth %		91%	29%	15%	15%	Debt raised / (repaid)	1,286	3,396	-3,000	-3,000	-3,000
Margin%	13%	17%	18%	18%	18%	Dividend (incl. tax)	-1,083	-1,624	-2,925	-3,409	-3,955
Interest Paid	2,073	2,041	1,895	1,739	1,583	Other financing activities	-1,980	-1,951	-1,895	-1,739	-1,583
Other Income & exceptional	683	388	400	400	400	Cash flow from financing activities	-1,777	-179	-7,820	-8,148	-8,538
PBT	10,066	20,236	26,738	31,074	35,966	Net Change in cash	431	675	-159	12,042	16,157
Tax	2,606	4,735	6,685	7,768	8,991	Valuation Ratios					
PAT	7,461	15,501	20,054	23,305	26,974		CY21	CY22	CY23E	CY24E	CY25E
Others (Minorities, Associates)	-520	-527	-553	-581	-610	Per Share Data					
Net Profit	6,941	14,974	19,500	22,725	26,364	EPS	11	23	15	17	20
Growth %		116%	30%	17%	16%	Growth %		116%	-35%	17%	16%
Shares (Mn)	433.0	649.6	1299.2	1299.2	1299.2	Book Value Per Share	94	79	54	70	88
EPS	10.69	23.05	15.01	17.49	20.29	Return Ratios					
						Return on Assets (%)	8%	14%	15%	16%	16%
						Return on Equity (%)	18%	33%	32%	28%	26%
						Return on Capital Employed (%)	15%	23%	24%	24%	23%
						Turnover Ratios					
						Asset Turnover (x)	1.0	1.2	1.3	1.3	1.2
						Sales / Gross Block (x)	1.0	1.3	1.4	1.4	1.5
						Working Capital / Sales (%)	-6%	-4%	-3%	2%	10%
						Receivable Days	10	7	9	10	10
						Inventory Days	108	100	112	120	120
						Payable Days	49	41	49	59	58
						Working Capital Days	68	66	71	71	72
						Liquidity Ratios					
						Current Ratio (x)	0.8	0.9	0.9	1.2	1.6
						Interest Coverage Ratio (x)	5.9	10.9	15.1	18.9	23.7
						Total Debt to Equity	0.8	0.7	0.3	0.2	0.1
						Net Debt to Equity	0.7	0.7	0.3	0.0	-0.1
						Valuation					
						PE (x)	58.7	27.2	92.4	79.3	68.3
						Earnings Yield (%)	2%	4%	1%	1%	1%
						Price to Sales (x)	4.6	3.1	5.6	4.9	4.3
						Price to Book (x)	10.0	17.7	13.2	10.2	8.1
						EV/EBITDA (x)	26.1	33.3	26.7	23.3	20.6
						EV/Sales (x)	5.0	7.1	5.8	5.1	4.5

Source: Company, Keynote Capitals Ltd.

KEYNOTE Rating History

Date	Rating	Market Price at Recommendation	Upside/Downside
4 th December 2022	BUY	659	+16.8%
7 th February 2022	BUY	653	+11.8%
2 nd May 2023	BUY	708	+14.7%
3 rd August 2023	BUY	824	+17%

Rating Methodology

Rating	Criteria
BUY	Expected positive return of > 10% over 1-year horizon
NEUTRAL	Expected positive return of > 0% to < 10% over 1-year horizon
REDUCE	Expected return of < 0% to -10% over 1-year horizon
SELL	Expected to fall by >10% over 1-year horizon
NOT RATED (NR)/UNDER REVIEW (UR)/COVERAGE SUSPENDED (CS)	Not covered by Keynote Capitals Ltd/Rating & Fair value under Review/Keynote Capitals Ltd has suspended coverage

Disclosures and Disclaimers

The following Disclosures are being made in compliance with the SEBI Research Analyst Regulations 2014 (herein after referred to as the Regulations).

Keynote Capitals Ltd. (KCL) is a SEBI Registered Research Analyst having registration no. INH000007997. KCL, the Research Entity (RE) as defined in the Regulations, is engaged in the business of providing Stock broking services, Depository participant services & distribution of various financial products. Details of associate entities of Keynote Capitals Limited are available on the website at <https://www.keynotecapitals.com/associate-entities/>

KCL and its associate company(ies), their directors and Research Analyst and their relatives may; (a) from time to time, have a long or short position in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.; however the same shall have no bearing whatsoever on the specific recommendations made by the analyst(s), as the recommendations made by the analyst(s) are completely independent of the views of the associates of KCL even though there might exist an inherent conflict of interest in some of the stocks mentioned in the research report.

KCL and / or its affiliates do and seek to do business including investment banking with companies covered in its research reports. As a result, the recipients of this report should be aware that KCL may have a potential conflict of interest that may affect the objectivity of this report. Compensation of Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

Details of pending Enquiry Proceedings of KCL are available on the website at <https://www.keynotecapitals.com/pending-enquiry-proceedings/>

A graph of daily closing prices of securities is available at www.nseindia.com, www.bseindia.com. Research Analyst views on Subject Company may vary based on Fundamental research and Technical Research. Proprietary trading desk of KCL or its associates maintains arm's length distance with Research Team as all the activities are segregated from KCL research activity and therefore it can have an independent view with regards to Subject Company for which Research Team have expressed their views.

Regional Disclosures (outside India)

This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject KCL & its group companies to registration or licensing requirements within such jurisdictions. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

Specific Disclosure of Interest statement for subjected Scrip in this document:

Financial Interest of Research Entity [KCL] and its associates; Research Analyst and its Relatives	NO
Any other material conflict of interest at the time of publishing the research report by Research Entity [KCL] and its associates; Research Analyst and its Relatives	NO
Receipt of compensation by KCL or its Associate Companies from the subject company covered for in the last twelve months; Managing/co-managing public offering of securities in the last twelve months; Receipt of compensation towards Investment banking/merchant banking/brokerage services in the last twelve months; Products or services other than those above in connection with research report in the last twelve months; Compensation or other benefits from the subject company or third party in connection with the research report in the last twelve months.	NO
Whether covering analyst has served as an officer, director or employee of the subject company covered	NO
Whether the KCL and its associates has been engaged in market making activity of the Subject Company	NO
Whether the Research Entity [KCL] and its associates; Research Analyst and its Relatives, have actual/beneficial ownership of 1% or more securities of the subject company, at the end of the month immediately preceding the date of publication of the research report or date of the public appearance.	NO

The associates of KCL may have:

- financial interest in the subject company
- actual/beneficial ownership of 1% or more securities in the subject company
- received compensation/other benefits from the subject company in the past 12 months
- other potential conflict of interests with respect to any recommendation and other related information and opinions.; however, the same shall have no bearing whatsoever on the specific recommendations made by the analyst(s), as the recommendations made by the analyst(s) are completely independent of the views of the associates of KCL even though there might exist an inherent conflict of interest in some of the stocks mentioned in the research report.
- acted as a manager or co-manager of public offering of securities of the subject company in past 12 months
- be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies)
- received compensation from the subject company in the past 12 months for investment banking / merchant banking / brokerage services or from other than said services.

The associates of KCL has not received any compensation or other benefits from third party in connection with the research report.

Above disclosures includes beneficial holdings lying in demat account of KCL which are opened for proprietary investments only. While calculating beneficial holdings, it does not consider demat accounts which are opened in name of KCL for other purposes (i.e. holding client securities, collaterals, error trades etc.). KCL also earns DP income from clients which are not considered in above disclosures.

Analyst Certification

The views expressed in this research report accurately reflect the personal views of the analyst(s) about the subject securities or issues, and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations and views expressed by research analyst(s) in this report.

Terms & Conditions:

This report has been prepared by KCL and is meant for sole use by the recipient and not for circulation. The report and information contained herein is strictly confidential and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of KCL. The report is based on the facts, figures and information that are believed to be true, correct, reliable and accurate. The intent of this report is not recommendatory in nature. The information is obtained from publicly available media or other sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. The report is prepared solely for informational purpose and does not constitute an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments for the clients. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. KCL will not treat recipients as customers by virtue of their receiving this report

Disclaimer:

The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent. This report and information herein is solely for informational purpose and may not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. Certain transactions -including those involving futures, options, another derivative product as well as non-investment grade securities - involve substantial risk and are not suitable for all investors. No representation or warranty, express or implied, is made as to the accuracy, completeness or fairness of the information and opinions contained in this document. The Disclosures of Interest Statement incorporated in this document is provided solely to enhance the transparency and should not be treated as endorsement of the views expressed in the report. This information is subject to change without any prior notice. The Company reserves the right to make modifications and alternations to this statement as may be required from time to time without any prior approval. KCL, its associates, their directors and the employees may from time to time, effect or have affected an own account transaction in, or deal as principal or agent in or for the securities mentioned in this document. KCL, its associates, their directors and the employees may from time to time invest in any discretionary PMS/AIF Fund and those respective PMS/AIF Funds may affect or have effected any transaction in for the securities mentioned in this document. They may perform or seek to perform investment banking or other services for, or solicit investment banking or other business from, any company referred to in this report. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting the document. This report has been prepared on the basis of information that is already available in publicly accessible media or developed through analysis of KCL. The views expressed are those of the analyst, and the Company may or may not subscribe to all the views expressed therein. This document is being supplied to you solely for your information and may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, copied, in whole or in part, for any purpose. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject KCL to any registration or licensing requirement within such jurisdiction.

The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction. Neither the Firm, not its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information. The person accessing this information specifically agrees to exempt KCL or any of its affiliates or employees from, any and all responsibility/liability arising from such misuse and agrees not to hold KCL or any of its affiliates or employees responsible for any such misuse and further agrees to hold KCL or any of its affiliates or employees free and harmless from all losses, costs, damages, expenses that may be suffered by the person accessing this information due to any errors and delays.

Keynote Capitals Limited (CIN: U67120MH1995PLC088172)

Compliance Officer: Mr. Jairaj Nair; Tel: 022-68266000; email id: jairaj@keynoteindia.net

Registered Office: 9th Floor, The Ruby, Senapati Bapat Marg, Dadar West, Mumbai – 400028, Maharashtra. Tel: 022 – 68266000.

SEBI Regn. Nos.: BSE / NSE (CASH / F&O / CD): INZ000241530; DP: CDSL- IN-DP-238-2016; Research Analyst: INH000007997

For any complaints email at kcl@keynoteindia.net

General Disclaimer: Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on www.keynotecapitals.com; Investment in securities market are subject to market risks, read all the related documents carefully before investing.