



SUBLIME FINANCIAL ADVISORY
NO COMPROMISE IN EXCELLENCE

Varun Beverages Ltd

-Strong brands & relationship to drive growth

Turnaround Report

Recommendation	:	Buy
CMP	:	Rs 515
Target	:	NA
% Allocation	:	5%

Sector	:	Consumption
Sensex	:	32075
NSE code	:	VBL
BSE Code	:	540180

AT A GLANCE

52 Week High Low	:	:569.40/340.00
Mkt. Cap (Rs. in Crs)	:	:9320
Major Shareholders		
Promoters (%)	:	:73.66%
Free Float (%)	:	:26.34%

Background: VBL, is PepsiCo’s second largest CSD/NCB franchisee outside US and operates in several Indian and international markets. VBL is a key player in the soft drinks industry operating in six countries with end-to-end execution capabilities and presence across a large part of the beverage value chain. PepsiCo owns the brands, provides concentrate for beverages, undertakes investment in R&D (both product and packaging innovations) and is responsible for consumer-level marketing/advertising support.

Strong relationship with pepsiCo

VBL’s strong relations with PepsiCo has benefitted it in multiple ways which includes access to modern technology, marketing leverage, operational know-how, industry best practices, access to raw materials and equipment at competitive prices as well as access to experienced personnel. VBL has developed a strategic and operational alignment with PepsiCo across its functions and organizational levels.

Increasing pepsiCo share - Growth driver

VBL has acquired licenses for additional territories and sub-territories from PepsiCo continuously. This was possible as VBL demonstrated ability to grow PepsiCo product sales in its territories. These were either earlier operated by PepsiCo directly or other franchises. VBL’s share in PepsiCo soft drinks India volumes increased to 45% in CY16 from 27% in CY11.

Wide distribution network

VBL has 537 primary distributors in India apart from 57 depots, 1,421 delivery vehicles and more than 1,300 sales and distribution personnel. VBL has also developed an extensive distribution network in international markets which included 14 depots, 603 delivery vehicles and 649 distributors at the end of 2016.

Outlook & Valuation

We Initiate coverage of VBL with a **BUY** rating. Given the Increasing demand ,Increasing capacity expansion, strong relationship with pepsiCo, wide distribution network and improving product mix are key positives for the stock. We expect VBL to report an EPS growth of 25% for the next 3 years. At the CMP of INR 515, the stock trades at 25.12x EPS of FY19E. **Key Risks** to our recommendation include seasonality and growing competition in the non-carbonates category.

Investment Arguments

Company Profile: VBL, is PepsiCo's second largest CSD/NCB franchisee outside US and operates in several Indian and international markets. VBL is a key player in the soft drinks industry operating in six countries with end-to-end execution capabilities and presence across a large part of the beverage value chain.

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VBL undertakes all other activities including manufacturing and distribution, supply chain management, in-market execution, local-level promotions, merchandising, in-store activations and driving market share gains. It has also made investments in setting up backward integration facilities for production of preforms, crowns, corrugated boxes and pads, plastic crates and shrink-wrap films to ensure operational efficiencies.

Activity	Infrastructure/ VBL's role
Manufacturing	PepsiCo provides concentrate for beverages
	Other RMs are procured by VBL
	VBL operates 21 manufacturing/bottling facilities (16 in India)
Distribution & Warehousing	71 depots, 2,024 owned vehicles and 1,186 primary distributors
Customer management	PepsiCo undertakes brand development and consumer-level marketing/advertising
	VBL does local-level promotions, in-store activations and merchandising
	VBL has installed 458,000 visi-coolers across markets
In-market execution	VBL is responsible for category value/volume growth
	Experienced region-specific sales team (1,300+ sales/distribution staff)
	GPRS enabled handheld devices and system (SAMNA)
Cost efficiencies	VBL has invested in backward integration

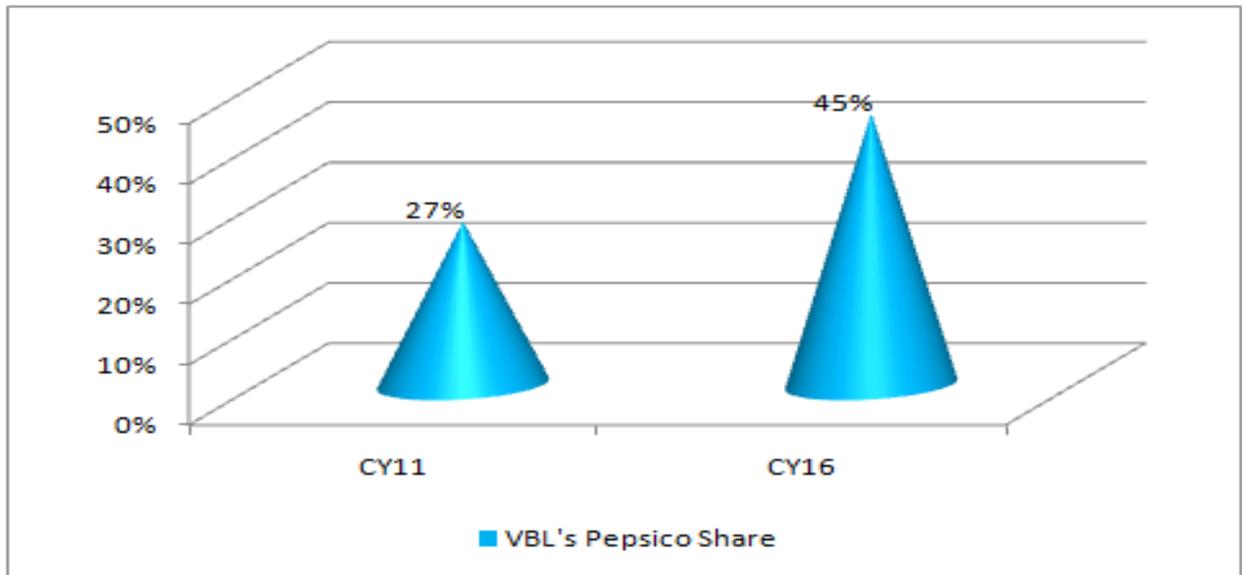
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VBL has developed strong sales teams that work closely with PepsiCo to develop and implement local advertising and marketing strategies. While PepsiCo controls the global marketing of its brands, VBL, as a franchisee, primarily focuses on customer-level marketing including managing distributor and retailer relationships, special occasion-based marketing at points of sale, and implementing promotional activities to strengthen a strong distribution network. It also works with PepsiCo's active product development team to strategize new product launches in India.

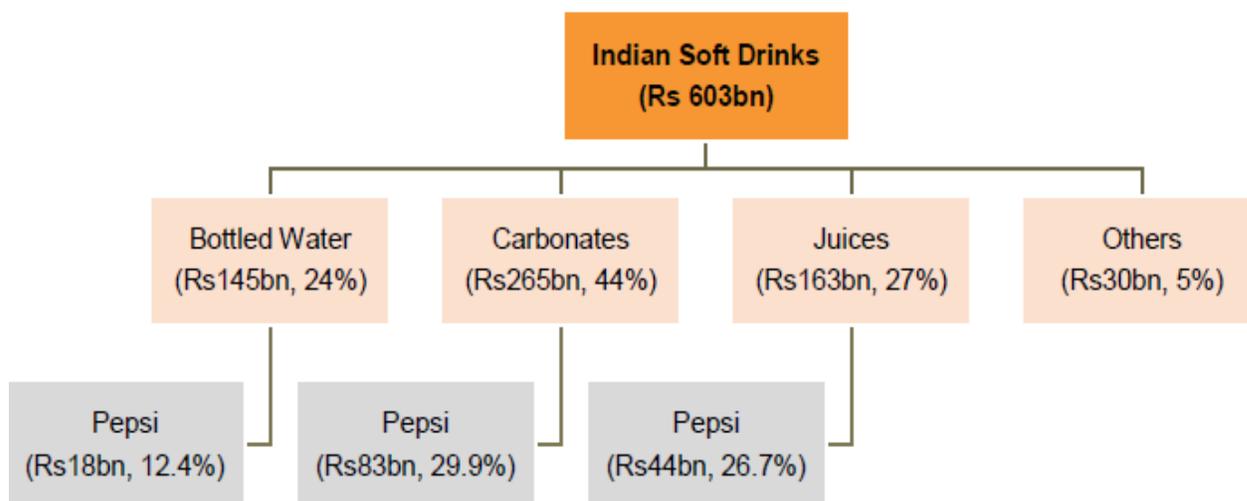
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Strong product portfolio

VBL scales 95% of soft drinks market through its presence in carbonates (44%, Rs265bn), juices (27%, Rs163bn) and bottled water (24%, Rs145bn). The total addressable market size is Rs570bn.(excluding others)



Non carbonates focus

PepsiCo plans to capitalize on the changing consumer sentiment from regular cola-carbonates to non-cola carbonates by focusing on products like 7UP Nimbooz Masala Soda. VBL is working closely with PepsiCo to launch new products and diversify its product portfolio. It has introduced a number of non-carbonates' brands in India like Tropicana Slice, Tropicana Frutz (Lychee, Apple and Mango) and 7UP Nimbooz. VBL is also actively evaluating growth opportunities in new product segments.

PepsiCo is investing to reduce sugars in global beverages in line with its 'portfolio with purpose 2025' goal. They are looking forward to bringing more variants of existing products in zero calories or no-sugar category. They plan to keep rolling out products every 2-3 months.

PepsiCo brand portfolio in India (non-cola carbonated soft drinks)



Juices & Water - Fast growing Category

Over the past five years, packaged water has seen a 22% CAGR in volume. The key growth drivers include increasing consumer awareness and growing consciousness about water borne diseases. The trend is likely to continue led by continued rise in awareness over health concerns along with drinking water shortages especially in urban areas, making consumers opting for bulk packaged drinking water.

PepsiCo brand portfolio in India (Juices and Water)

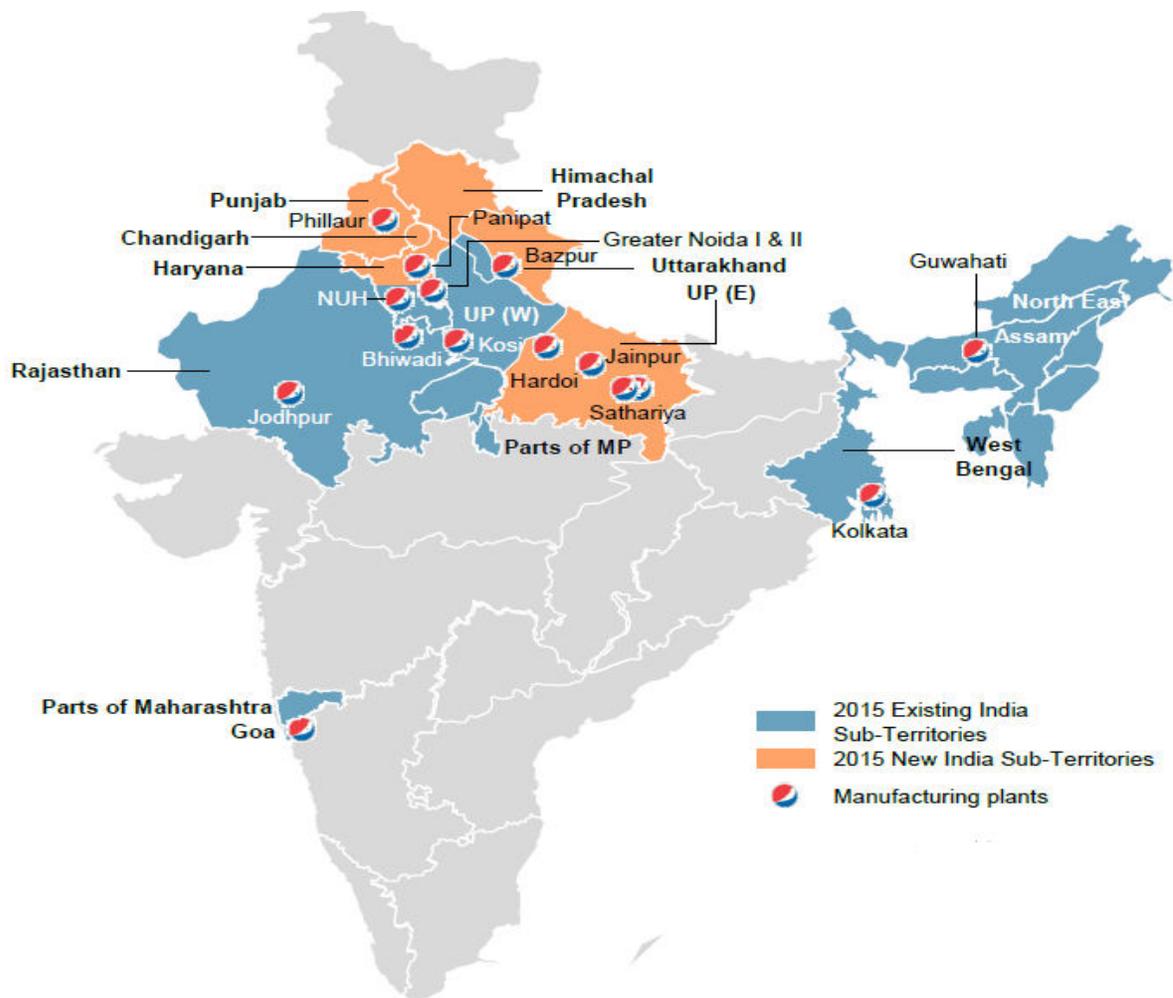


The juice market in India is estimated at Rs160bn in CY16 which has seen a 20% volume CAGR over CY11-16. The market is divided into three categories: 1) Juice drinks: Contains up to 24% juice which has seen a 21% CAGR and forms 83% of total juice market in volumes; 2) Nectars: The Juice content is between 25-99% and growing at 16% CAGR; 3) 100% juice: This is the fastest growing segment with a 23% CAGR growth.

Pepsi and Coca Cola will also dominate the non-carbonates market as they have been dominating the carbonates space. The distribution and reach are far superior to new home grown local players like Manpasand, Parle Agro, Hectar Beverages etc. Once the overall volume picks up for the category, large players including PepsiCo will capture market share. VBL will be a direct beneficiary of such growth as PepsiCo will require a credible and large franchises to manufacture and distribute its products.

Distribution Network

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Financials

P&L

Consolidated Profit & Loss account(Rs.Cr)	Dec '15	Dec '16
Income		
Sales Turnover	3,905.89	4,522.29
Excise Duty	511.75	670.28
Net Sales	3,394.14	3,852.01
Other Income	14.28	34.78
Stock Adjustments	28.99	31.59
Total Income	3,437.41	3,918.38
Expenditure		
Raw Materials	1,777.89	1,809.29
Power & Fuel Cost	131.15	156.39
Employee Cost	323.75	426.36
Other Manufacturing Expenses	0	0
Selling and Admin Expenses	0	0
Miscellaneous Expenses	553.26	696.35
Preoperative Exp Capitalised	0	0
Total Expenses	2,786.05	3,088.39
Operating Profit	637.08	795.21
PBDIT	651.36	829.99
Interest	168.79	214.79
PBDT	482.57	615.2
Depreciation	317.41	372.36
Other Written Off	0	0
Profit Before Tax	165.16	242.84
Extra-ordinary items	25.45	0
PBT (Post Extra-ord Items)	190.61	242.84
Tax	78.86	82.85
Reported Net Profit	111.75	159.99
EPS	8.35	8.78

Balance Sheet

Consolidated Balance Sheet(Rs.Cr)	Dec '15	Dec '16
Sources Of Funds		
Total Share Capital	583.77	182.31
Equity Share Capital	133.77	182.31
Share Application Money	0	0
Preference Share Capital	450	0
Init. Contribution Settler	0	0
Preference Share Application Money	0	0
Employee Stock Opiton	0	0
Reserves	90.51	1,711.55
Networth	674.28	1,893.86
Secured Loans	986.21	1,214.46
Unsecured Loans	845.73	154.39
Total Debt	1,831.94	1,368.85
Minority Interest	0	0.06
Policy Holders Funds	0	0
Group Share in Joint Venture	0	0
Total Liabilities	2,506.22	3,262.77
Application Of Funds		
Gross Block	4,529.35	5,302.31
Less: Revaluation Reserves	0	0
Less: Accum. Depreciation	1,033.79	1,338.97
Net Block	3,495.56	3,963.34
Capital Work in Progress	37.91	95.58
Investments	3.27	5.62
Inventories	424.66	489.93
Sundry Debtors	97.91	130.32
Cash and Bank Balance	58.07	65.7
Total Current Assets	580.64	685.95
Loans and Advances	319.15	478.63
Fixed Deposits	0	0
Total CA, Loans & Advances	899.79	1,164.58
Deferred Credit	0	0
Current Liabilities	1,848.81	1,861.00
Provisions	81.52	105.35
Total CL & Provisions	1,930.33	1,966.35
Net Current Assets	-1,030.54	-801.77
Minority Interest	0	0
Group Share in Joint Venture	0	0
Miscellaneous Expenses	0	0
Total Assets	2,506.20	3,262.77

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