

## Radico Khaitan

### Performance Highlights

#### Quarterly Data

(₹ cr)	4QFY16	4QFY15	% yoy	3QFY16	% qoq
Revenue	378	343	10.0	401	(5.8)
EBITDA	39	33	17.0	58	33.6
Margin (%)	10.3	9.7	61bp	14.6	(430bp)
Adj. PAT	15	15	(0.8)	25	(41.8)

Source: Company, Angel Research

For 4QFY2016, Radico Khaitan (RKL) outperformed our estimates on the top-line front although the bottom-line came in flat yoy. The company's top-line grew by ~10% to ₹378cr on back of higher sales of premium products while the bottom-line came in flat on a yoy basis at ₹15cr due to higher interest costs and taxes. During the quarter the Karnataka government gave a price increase (₹35/case) to the company which would be effective from July 1, 2016 and would contribute towards margin improvement. Further, the government of Uttar Pradesh has reduced the excise duty on Indian made foreign liquor (IMFL) by 20-25% with effect from April 1, 2016, which is expected to result in an increase in IMFL sales volume in the state going forward. These policy actions should significantly benefit the company as the two states account for ~20% of its volumes.

We believe that the company has the potential to perform better on the bottom-line front on back of (a) improvement in volume growth (b) higher sales of premium products (c) anticipation of better price hikes and (d) gradual reduction in debt which should lead to significant savings in interest costs. **Hence, we recommend a Buy rating on the stock with a target price of ₹125.**

**Top-line grew ~10% on back of higher sales in premium products:** Despite of overall volumes declining by 4.5% during the quarter, the company's top-line was able to report a ~10% yoy growth to ₹378cr (our estimate was of ₹351cr), mainly due to the company's shift in focus towards prestige & above products over higher volume mass market products. During the quarter, prestige & above brands' volume grew ~7% yoy while their contribution to total IMFL volumes increased from 19.5% in 4QFY2015 to 22% in 4QFY2016.

**OPM improved but PAT was flat yoy:** On the operating front, the company's margin improved by 61bp yoy to 10.3%, primarily on account of lower selling & distribution expenses and other expenditure. However, raw material cost as a percentage of sales increased by 331bp yoy. The company reported a net profit of ₹14.8cr, which is flat yoy, on account of higher interest costs and taxes.

#### Key financials

Y/E March (₹ cr)	FY2015	FY2016	FY2017E	FY2018E
Net sales	1,488	1,543	1,659	1,802
% chg	2.5	3.7	7.5	8.6
Net profit	68	77	84	98
% chg	(5.1)	13.7	9.6	16.4
EBITDA margin (%)	11.4	12.6	13.0	13.2
EPS (₹)	5.1	5.8	6.3	7.4
P/E (x)	18.1	15.9	14.5	12.5
P/BV (x)	1.5	1.4	1.3	1.2
RoE (%)	8.1	8.5	8.6	9.3
RoCE (%)	7.8	8.8	9.6	10.4
EV/Sales (x)	1.3	1.3	1.2	1.1
EV/EBITDA (x)	11.5	10.1	9.0	8.1

Source: Company, Angel Research, Note: CMP as of May 11, 2016

## BUY

CMP	₹92
Target Price	₹125

Investment Period	12 months
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#### Stock Info

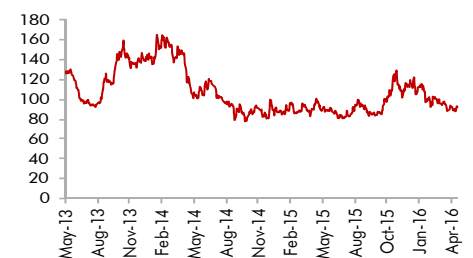
Sector	Breweries & Distilleries
Market Cap (₹ cr)	1,221
Net Debt (₹ cr)	742
Beta	0.8
52 Week High / Low	131 / 78
Avg. Daily Volume	71,845
Face Value (₹)	2
BSE Sensex	25,597
Nifty	7,849
Reuters Code	RADC.BO
Bloomberg Code	RDCK@IN

#### Shareholding Pattern (%)

Promoters	40.5
MF / Banks / Indian Fls	13.3
FII / NRIs / OCBs	21.1
Indian Public / Others	25.1

Abs. (%)	3m	1yr	3yr
Sensex	11.4	(4.8)	30.0
RKL	(4.9)	3.8	(21.6)

#### 3-year price chart



Source: Company, Angel Research

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**Exhibit 1: Quarterly performance**

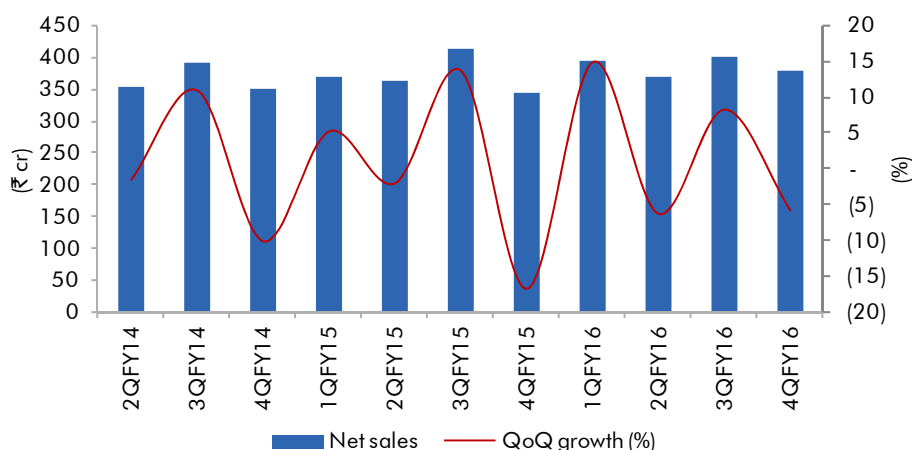
Y/E March (₹ cr)	4QFY16	4QFY15	% yoy	3QFY16	% qoq	FY2016	FY2015	% chg
<b>Net Sales</b>	<b>378</b>	<b>343</b>	<b>10.0</b>	<b>401</b>	<b>(5.8)</b>	<b>1,543</b>	<b>1,488</b>	<b>3.7</b>
Consumption of RM	183	155	18.0	179	2.5	721	720	0.1
(% of Sales)	48.5	45.2		44.6		46.7	48.3	
Staff Costs	34	28	21.9	29	16.3	131	120	9.6
(% of Sales)	8.9	8.1		7.2		8.5	8.0	
Selling & Administrative Exps.	65	67	(3.4)	71.4	(9.2)	273	284	(3.8)
(% of Sales)	17.2	19.5		17.8		17.7	19.1	
Operating Expense	57	60	(5.2)	63	(9.8)	224	195	14.7
(% of Sales)	15.1	17.6		15.8		14.5	13.1	
<b>Total Expenditure</b>	<b>339</b>	<b>310</b>	<b>9.2</b>	<b>342</b>	<b>(1.0)</b>	<b>1,348</b>	<b>1,318</b>	<b>2.3</b>
<b>Operating Profit</b>	<b>39</b>	<b>33</b>	<b>17.0</b>	<b>58</b>	<b>(33.6)</b>	<b>195</b>	<b>170</b>	<b>14.2</b>
OPM (%)	10.3	9.7		14.6		12.6	11.4	
Interest	23	22	6.0	20	16.8	85	90	(5.8)
Depreciation	10	8	24.3	10	3.4	40	38	5.3
Other Income	14.8	14.9	(1.1)	6.8	116.5	38	45	(15.2)
<b>PBT</b>	<b>20</b>	<b>18</b>	<b>11.8</b>	<b>36</b>	<b>(43.1)</b>	<b>108</b>	<b>87</b>	<b>23.6</b>
(% of Sales)	5.4	5.3		8.9		7.0	5.9	
Provision for Taxation	6	3	70.1	10	(46.2)	31	19	58.1
(% of PBT)	27.2	17.9		28.8		28.6	22.4	
Minority Interest	-	-	-	-	-	-	-	-
<b>Reported PAT</b>	<b>15</b>	<b>15</b>	<b>(0.8)</b>	<b>25</b>	<b>(41.8)</b>	<b>77</b>	<b>68</b>	<b>13.7</b>
PATM	3.9	4.3		6.3		5.0	4.5	

Source: Company, Angel Research

### Top-line grew ~10% on back of higher sales in premium products

Despite of overall volumes declining by 4.5% during the quarter, the company's top-line was able to report a ~10% yoy growth to ₹378cr (our estimate was of ₹351cr), mainly due to the company's shift in focus towards prestige & above products over higher volume mass market products. During the quarter, prestige & above brands' volume grew ~7% yoy while their contribution to total IMFL volumes increased from 19.5% in 4QFY2015 to 22% in 4QFY2016.

#### Exhibit 2: Top-line growth trend

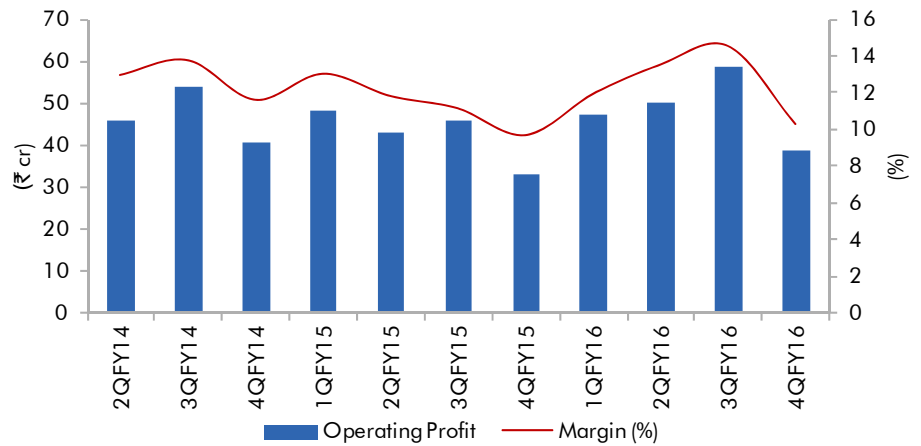


Source: Company, Angel Research

### Operating margin expansion due to lower selling & distribution and other expenses

On the operating front, the company's margin improved by 61bp yoy to 10.3%, primarily on account of lower selling & distribution expenses and other expenditure. However, raw material cost as a percentage of sales increased by 331bp yoy.

**Exhibit 3: Operating profit and margin trend**

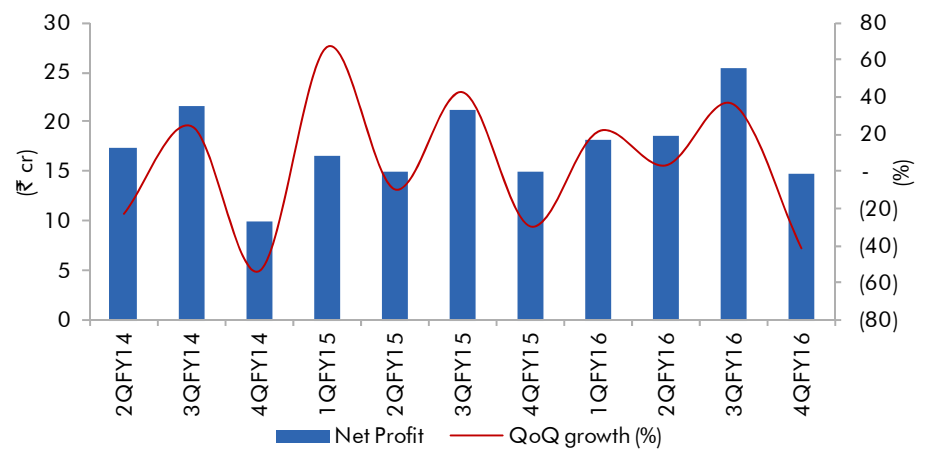


Source: Company, Angel Research

**PAT was flat yoy**

The company reported a net profit of ₹14.8cr (flat yoy) on account of higher interest costs and taxes.

**Exhibit 4: Net Profit and growth trend**



Source: Company, Angel Research

## **Investment rationale**

### **Pricing environment expected to be favorable for IMFL industry**

Our interaction with liquor companies suggests that prices have now bottomed out. We expect the industry's pricing environment to likely get better going ahead mainly because there has not been any significant price hike in products in recent times due to delay in approval by various state governments. Hence, the industry is now expecting a significant price hike in the coming financial year. Also, the industry leader United Spirits has been facing pressure at the operating level and the company has a huge debt on its balance sheet. Hence we believe that the company's new Management would shift focus on profitability over volume growth, which in turn, would lead to increased scope for other liquor companies to hike prices.

### **Higher proportion of premium products in volume mix to drive profitability**

In the IMFL segment, more than 20% of the company's volumes come from prestige and above products, which is a high margin business, and the balance volumes come from regular and others brands. Since the last eight years, the company's prestige and above brands' volume has reported a CAGR of ~23% and their share in the product mix has increased from 7.9% in FY2009 to 24% in FY2016. We expect volume contribution of prestige and above products in the IMFL segment to increase further on back of higher ad spend. The company has roped in celebrity Hrithik Roshan as its brand ambassador. Also, the company's presence in the prestige Vodka segment is under penetrated which leaves scope for growth. Thus, this would improve the overall margin for the company and result in higher profitability.

### **Wide distribution network with strong brands**

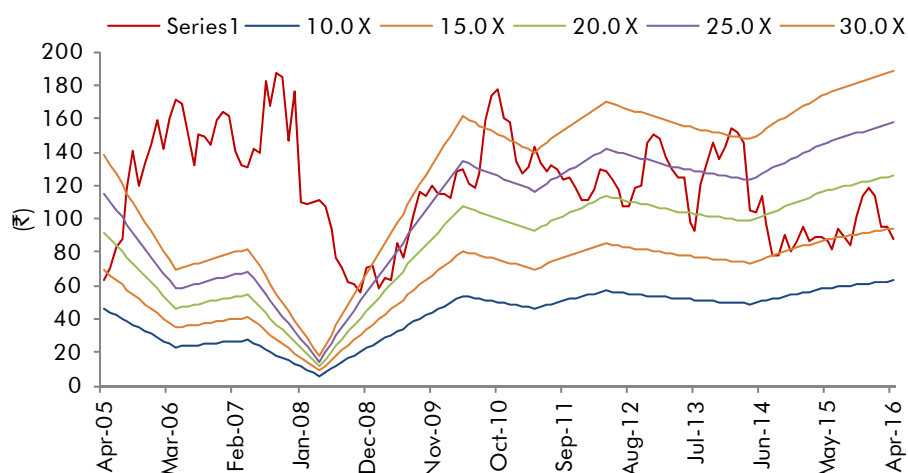
RKL has a strong sales and distribution network with a presence in retail and off-trade outlets in the relevant segments in different parts of India. Currently, the company is selling its products through over 45,000 retail outlets and over 5,000 on-premise outlets. Apart from wholesalers, a total of around 300 employees divided into four zones, each headed by regional profit centre head, ensure an adequate on-the-ground sales and distribution presence across the country.

The company has strong brands likes Magic Moments Vodka, Morpheus Brandy, Verve Vodka, Florence Brandy, After Dark Whisky etc.

## Outlook and valuation

The company has not performed well in the last two years due to increasing raw material costs (ENA is a key raw material) and with it not receiving significant price hikes from various states. We expect the company to perform well going forward in anticipation of better price hikes and healthy sales growth in premium products. This would result in an overall improvement in the operating margin of the company. We expect the company to report strong earnings CAGR of ~13% to ~₹98cr over FY2016-18E. **Hence, we recommend a Buy rating on the stock with a target price of ₹125.**

### Exhibit 5: One-year forward P/E band



Source: Company, Angel Research

## Company Background

Radico Khaitan Ltd is an India-based spirits company engaged in the manufacture of liquor. The company has three distilleries and one JV with total capacity of 150mn litres and 33 bottling units spread across the country. The company is one of the largest providers of branded IMFL to the Canteen Stores Department (CSD), which has significant entry barriers. RKL's brands include After Dark Whisky, Magic Moments Vodka, Morpheus Brandy, Contessa Rum, Old Admiral Brandy and 8 PM. Its liquor business also includes rectified spirit and country liquor. Its alcohol products include rectified spirit, silent spirit, cane juice spirit, malt spirit, grain spirit and ethanol. The company's PET division produces a range of PET bottles and jars for industries such as pharmaceutical, cosmetics, home and personal care, edible oil and confectionery.

**Profit & Loss Statement**

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
<b>Total operating income</b>	<b>1,258</b>	<b>1,452</b>	<b>1,488</b>	<b>1,543</b>	<b>1,659</b>	<b>1,802</b>
% chg	10.0	15.4	2.5	3.7	7.5	8.6
<b>Total Expenditure</b>	<b>1,074</b>	<b>1,258</b>	<b>1,318</b>	<b>1,348</b>	<b>1,443</b>	<b>1,564</b>
Raw Material Cost	585	653	717	721	771	834
Personnel Expenses	79	93	107	131	129	141
Selling & Administrative Exp.	235	286	284	273	290	315
Others Expenses	176	226	210	224	252	274
<b>EBITDA</b>	<b>184</b>	<b>193</b>	<b>170</b>	<b>195</b>	<b>216</b>	<b>238</b>
% chg	17.7	5.0	(11.9)	14.2	11.0	10.3
(% of Net Sales)	14.6	13.3	11.4	12.6	13.0	13.2
Depreciation & Amortisation	35	39	38	40	43	45
<b>EBIT</b>	<b>149</b>	<b>155</b>	<b>132</b>	<b>154</b>	<b>173</b>	<b>194</b>
% chg	20.4	3.9	(14.6)	16.8	12.3	11.7
(% of Net Sales)	11.8	10.7	8.9	10.0	10.4	10.7
Interest & other Charges	70	85	90	85	89	89
Other Income	30	36	45	38	40	40
(% of PBT)	27.8	34.3	51.6	35.4	32.3	27.7
Share in profit of Associates	-	-	-	-	-	-
<b>Recurring PBT</b>	<b>109</b>	<b>106</b>	<b>87</b>	<b>108</b>	<b>124</b>	<b>144</b>
% chg	25.7	(2.6)	(18.1)	23.6	15.1	16.4
Prior Period & Extra. Exp./ (Inc.)	-	-	-	-	-	-
<b>PBT (reported)</b>	<b>109</b>	<b>106</b>	<b>87</b>	<b>108</b>	<b>124</b>	<b>144</b>
Tax	32	35	19	31	40	46
(% of PBT)	29.3	33.0	22.4	28.6	32.0	32.0
<b>PAT (reported)</b>	<b>77</b>	<b>71</b>	<b>68</b>	<b>77</b>	<b>84</b>	<b>98</b>
% chg	21.4	(7.8)	(5.1)	13.7	9.6	16.4
(% of Net Sales)	6.1	4.9	4.5	5.0	5.1	5.4
<b>Basic EPS (₹)</b>	<b>5.8</b>	<b>5.4</b>	<b>5.1</b>	<b>5.8</b>	<b>6.3</b>	<b>7.4</b>
<b>Fully Diluted EPS (₹)</b>	<b>5.8</b>	<b>5.4</b>	<b>5.1</b>	<b>5.8</b>	<b>6.3</b>	<b>7.4</b>
% chg	21.2	(7.9)	(5.1)	13.7	9.6	16.4

**Balance Sheet**

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
<b>SOURCES OF FUNDS</b>						
Equity Share Capital	27	27	27	27	27	27
Reserves & Surplus	702	754	812	877	949	1,032
<b>Shareholders Funds</b>	<b>728</b>	<b>781</b>	<b>839</b>	<b>904</b>	<b>976</b>	<b>1,059</b>
Total Loans	768	904	849	851	830	810
Deferred Tax Liability	70	85	85	85	85	85
<b>Total Liabilities</b>	<b>1,566</b>	<b>1,770</b>	<b>1,773</b>	<b>1,840</b>	<b>1,890</b>	<b>1,954</b>
<b>APPLICATION OF FUNDS</b>						
Gross Block	744	821	831	851	871	891
Less: Acc. Depreciation	214	250	288	329	371	416
<b>Net Block</b>	<b>529</b>	<b>571</b>	<b>542</b>	<b>522</b>	<b>499</b>	<b>475</b>
Capital Work-in-Progress	5	8	8	8	8	8
<b>Investments</b>	<b>109</b>	<b>108</b>	<b>98</b>	<b>98</b>	<b>98</b>	<b>98</b>
Current Assets	1,161	1,330	1,379	1,471	1,560	1,684
Inventories	186	211	212	220	232	252
Sundry Debtors	435	523	538	562	604	657
Cash	16	15	10	11	14	15
Loans & Advances	314	441	470	492	518	562
Other Assets	209	139	149	185	192	198
Current liabilities	249	262	270	274	290	326
<b>Net Current Assets</b>	<b>912</b>	<b>1,067</b>	<b>1,109</b>	<b>1,197</b>	<b>1,270</b>	<b>1,358</b>
<b>Deferred Tax Asset</b>	<b>11</b>	<b>15</b>	<b>15</b>	<b>15</b>	<b>15</b>	<b>15</b>
Mis. Exp. not written off	-	-	-	-	-	-
<b>Total Assets</b>	<b>1,566</b>	<b>1,770</b>	<b>1,773</b>	<b>1,840</b>	<b>1,890</b>	<b>1,954</b>



**Cashflow Statement**

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Profit before tax	109	106	87	108	124	144
Depreciation	35	39	38	40	43	45
Change in Working Capital	(242)	(53)	(47)	(87)	(70)	(87)
Interest / Dividend (Net)	42	50	90	85	89	89
Direct taxes paid	(23)	(26)	(19)	(31)	(40)	(46)
Others	13	22	-	-	-	-
<b>Cash Flow from Operations</b>	<b>(66)</b>	<b>137</b>	<b>149</b>	<b>115</b>	<b>146</b>	<b>145</b>
(Inc.)/ Dec. in Fixed Assets	48	(141)	11	(20)	(20)	(20)
(Inc.)/ Dec. in Investments	(3)	(0)	(10)	-	-	-
<b>Cash Flow from Investing</b>	<b>46</b>	<b>(141)</b>	<b>0.2</b>	<b>(20)</b>	<b>(20)</b>	<b>(20)</b>
Issue of Equity	1	1	-	-	-	-
Inc./(Dec.) in loans	97	99	(55)	2	(21)	(20)
Dividend Paid (Incl. Tax)	(12)	(12)	(10)	(12)	(13)	(15)
Interest / Dividend (Net)	(71)	(84)	(90)	(85)	(89)	(89)
<b>Cash Flow from Financing</b>	<b>15</b>	<b>3</b>	<b>(154)</b>	<b>(94)</b>	<b>(123)</b>	<b>(124)</b>
Inc./(Dec.) in Cash	(5)	(1)	(5)	1	2	1
<b>Opening Cash balances</b>	<b>21</b>	<b>16</b>	<b>15</b>	<b>10</b>	<b>11</b>	<b>14</b>
<b>Closing Cash balances</b>	<b>16</b>	<b>15</b>	<b>10</b>	<b>11</b>	<b>14</b>	<b>15</b>

**Key Ratios**

Y/E March	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
<b>Valuation Ratio (x)</b>						
P/E (on FDEPS)	15.8	17.2	18.1	15.9	14.5	12.5
P/CEPS	10.9	11.1	11.6	10.4	9.6	8.6
P/BV	1.7	1.6	1.5	1.4	1.3	1.2
Dividend yield (%)	0.9	0.9	0.8	0.9	1.0	1.2
EV/Sales	1.5	1.4	1.3	1.3	1.2	1.1
EV/EBITDA	10.1	10.4	11.5	10.1	9.0	8.1
EV / Total Assets	1.0	1.0	1.0	0.9	0.9	0.8
<b>Per Share Data (₹)</b>						
EPS (Basic)	5.8	5.4	5.1	5.8	6.3	7.4
EPS (fully diluted)	5.8	5.4	5.1	5.8	6.3	7.4
Cash EPS	8.5	8.3	8.0	8.8	9.5	10.7
DPS	0.8	0.8	0.8	0.9	1.0	1.1
Book Value	54.8	58.7	63.0	67.9	73.3	79.6
<b>Returns (%)</b>						
ROCE	10.0	9.2	7.8	8.8	9.6	10.4
Angel ROIC (Pre-tax)	10.9	9.9	8.4	9.4	10.2	11.0
ROE	10.6	9.1	8.1	8.5	8.6	9.3
<b>Turnover ratios (x)</b>						
Asset Turnover (Gross Block)	2.4	2.5	2.7	3.0	3.3	3.8
Inventory / Sales (days)	54	53	52	52	51	51
Receivables (days)	126	132	132	133	133	133
Payables (days)	36	33	33	32	31	31
WC cycle (ex-cash) (days)	144	152	151	153	153	153

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Disclosure of Interest Statement	Radico Khaitan
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

*Note: We have not considered any Exposure below ₹ 1 lakh for Angel, its Group companies and Directors*

<b>Ratings (Based on expected returns over 12 months investment period):</b>	Buy (> 15%)	Accumulate (5% to 15%) Reduce (-5% to -15%)	Neutral (-5 to 5%) Sell (< -15%)
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