

Rating matrix		
Rating	:	Buy
Target	:	₹ 4130
Target Period	:	12-15 months
Potential Upside	:	10%

What's changed?	
Target	Changed from ₹ 3320 to ₹ 4130
EPS FY18E	Changed from ₹ 127.1 to ₹ 134.6
EPS FY19E	Changed from ₹ 150.8 to ₹ 164.6
Rating	Changed from Hold to Buy

Key financials				
₹ Crore	FY16	FY17	FY18E	FY19E
Net Sales	878.9	944.1	1,100.5	1,238.3
EBITDA	237.4	246.2	321.8	386.1
Net Profit	153.1	167.2	207.8	254.1
EPS (₹)	99.2	108.3	134.6	164.6

\*From FY16 onwards, financials are reported as per Ind AS

Valuation summary				
	FY16	FY17	FY18E	FY19E
P/E	37.8	34.6	27.9	22.8
Target P/E	41.7	38.1	30.7	25.1
Div. Yield	1.9	2.0	2.4	2.9
Mcap/Sales	6.6	6.1	5.3	4.7
RoNW (%)	41.3	31.1	34.1	36.2
RoCE (%)	59.7	45.0	49.0	51.5

\*From FY16 onwards, financials are reported as per Ind AS

Stock data		Amount
Market Capitalization (₹ Crore)		5,790.7
Total Debt (FY17) (₹ Crore)		0.0
Cash and Investments (FY17) (₹ Crore)		189.9
EV (₹ Crore)		5,600.8
52 week H/L		3664 / 1690
Equity capital		₹ 15.4 crore
Face value		₹ 10

Price performance				
	1M	3M	6M	12M
VST Industries	19.7	29.8	54.0	118.3
ITC	10.6	21.4	42.4	39.9
Godfrey Phillips	6.2	12.4	26.3	48.0

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## VST Industries (VSTIND)

₹ 3750

### Cigarette volumes to revive...

VST industries would be the bigger beneficiary of the change in the indirect tax structure. With the abolition of excise duty and additional excise duty, net tax incidence for VST industries would come down by 8.3% and to comply with the anti profiteering clause, the company would require taking price cut by 6.0%. State VAT has been replaced by GST and cess would replace specific excise duty. Though, the absolute tax rate on cigarettes has remained same but with the elimination of 'Tax on Tax' has reduced the tax liabilities for cigarettes companies. We have increased our volume growth estimate from 2.5% to 6% for FY18E and from 3% to 5% in FY19E. This would translate in to EPS increase by 5.9% to ₹134.6 in FY18E and 9.1% to ₹ 164.6 in FY19E. We remain positive on the stock and upgrade our recommendation to Buy with the target price of ₹ 4130/share.

#### Exhibit 1: Lower tax incidence under GST

(₹ Per stick)	Earlier	Under GST	Difference
Net Realisation	0.96	0.96	
Excise Duty/NCCD	1.81	0.12	
Gross realisation	2.77	1.08	
VAT @ 25% / GST @ (28%+5%)	0.69	0.36	
Cess	0.00	1.82	
<b>Total tax incidence</b>	<b>2.50</b>	<b>2.29</b>	<b>-8.3%</b>
Dealers Margin @ 15%	0.52	0.49	
<b>MRP</b>	<b>3.98</b>	<b>3.74</b>	<b>-6.0%</b>

Source: Company, ICICIdirect.com Research

#### Upgrading volume estimates on lower tax incidence

With lower tax incidence under GST, we expect the cigarette volumes to report higher growth; hence we have revised our volume estimates upwards from 2.5% to 6.0% for FY18E and from 3.0% to 5.0% for FY19E. On account of higher volumes, our revenue estimates are getting upgraded by 2.5% and 4.1% for FY18E and FY19E, respectively. We expect the EBITDA margin at 29.2% and 31.1% for FY18E and FY19E, respectively.

#### Exhibit 2: Change in estimates

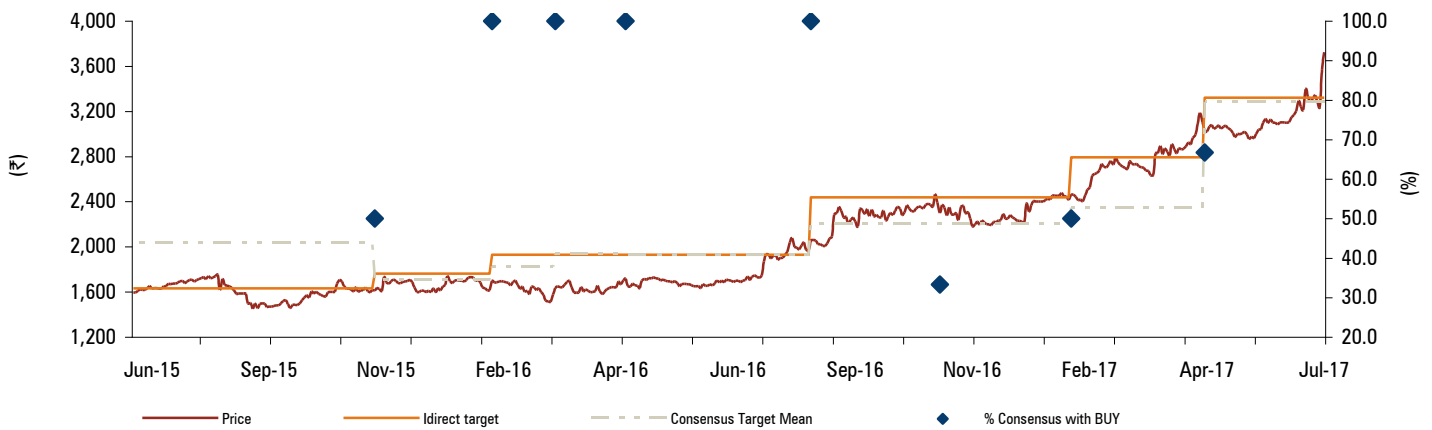
(₹ Crore)	FY18E			FY19E		
	Old	New	% change	Old	New	% change
Revenue	1073.6	1100.5	2.5	1,189.9	1,238.3	4.1
EBITDA	305.2	321.8	5.4	355.7	386.1	8.5
EBITDA Margin (%)	28.4	29.2	84 bps	29.8	31.1	126 bps
PAT	196.3	207.8	5.8	232.8	254.1	9.2
EPS (₹)	127.1	134.6	5.9	150.8	164.6	9.1

Source: Company, ICICIdirect.com Research

#### Volume growth to come after five years of decline, upgrade to Buy

With the clarity on reduction in indirect tax liability, we remain positive on volume growth prospects for the company. We expect VST to clock revenue CAGR of 14.5% FY17-19E led by volume CAGR of 5.5% after witnessing volume decline for five consecutive years. Led by healthy revenue growth and EBITDA margin expansion of 510 bps, profit for the company is estimated to grow at a CAGR of 23.3% over the same period. Hence, we are upgrading our recommendation on the stock to Buy with a revised target price of ₹ 4130/share valuing it at 25x on its FY19E EPS of ₹ 164.6.

### Recommendation history vs. Consensus



Source: Bloomberg, Company, ICICIdirect.com Research

### Key events

Date	Event
Apr-09	Final dividend of ₹ 30/share on closing share price of ₹ 213 yielding a dividend of 14.1%
Apr-10	Final dividend of ₹ 30/share; margins decline significantly to 17.6%
Apr-11	Final dividend of ₹ 45/share; margins improve by robust 1050 bps YoY to 28.1%
Jan-12	Profits decline ~10% YoY with volume growth in cigarettes declining ~9% YoY
Feb-12	Gol increases excise duty on cigarettes above 65 mm by ~21% in FY13 Budget
Apr-12	Final dividend of ₹ 65/share
Sep-12	Profitability declines ~17% YoY led by muted sales growth of ~6% and decline in margins by ~690 bps YoY to 24.6%
Apr-13	Volume growth in cigarettes or FY13 comes in ~13% lower with a margin decline of ~600 bps to 27%. Profits also remain lower by ~11% for the year
Jul-14	Government increases excise duty on <65 mm segment cigarettes by ~72% and other lengths by 11-21%
Feb-15	Excise duty on below 65 mm category increased by 25% with above 65 mm category increased by 15% in Union Budget FY16
Feb-16	Excise hike of 10% on cigarettes in Budget 2016
Feb-17	Government announces a 6% hike in excise duty across categories of cigarette

Source: Company, ICICIdirect.com Research

### Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	British American Tobacco PLC	31-Mar-17	31.73	4.9	0.0
2	Bright Star Investments Pvt. Ltd.	31-Mar-17	25.95	4.0	0.0
3	HDFC Asset Management Co., Ltd.	31-Mar-17	8.89	1.4	0.0
4	Matthews International Capital Management, L.L.C.	31-Mar-17	7.68	1.2	-0.1
5	ICICI Lombard General Insurance Company Ltd.	31-Mar-17	2.14	0.3	0.0
6	The New India Assurance Co. Ltd.	31-Mar-17	1.71	0.3	0.0
7	DSP BlackRock Investment Managers Pvt. Ltd.	31-Mar-17	1.63	0.3	0.0
8	IDBI Asset Management Limited	30-Apr-17	0.78	0.1	0.0
9	Rothmans International Enterprises, Ltd.	31-Mar-17	0.43	0.1	0.0
10	Axis Asset Management Company Limited	31-May-17	0.40	0.1	0.0

Source: Reuters, ICICIdirect.com Research

### Shareholding Pattern

(in %)	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17
Promoter	32.2	32.2	32.2	32.2	32.2
FII	10.6	10.6	10.4	10.4	10.3
DII	14.2	14.4	14.3	14.3	14.4
Others	43.1	42.9	43.2	43.2	43.2

### Recent Activity

Buys			Sells		
Investor name	Value	Shares	Investor name	Value	Shares
IDBI Asset Management Limited	0.06m	0m	Fidelity Management & Research Company	-0.16m	0m
State Street Global Advisors (US)	0.01m	0m	HDFC Asset Management Co., Ltd.	-0.06m	0m
Dimensional Fund Advisors, Ltd.	0m	0m		0	0m

Source: Reuters, ICICIdirect.com Research

## Financial summary

Profit and loss statement		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Total Operating Income	883.1	948.2	1104.9	1243.0	
Growth (%)	5.6	7.4	16.5	12.5	
Raw Material Expenses	435.3	468.4	529.1	577.3	
Employee Expenses	80.4	91.3	104.5	117.6	
Marketing Expenses	47.5	0.0	50.4	56.7	
Administrative Expenses	43.2	0.0	55.0	59.4	
Other expenses	39.4	142.4	44.0	45.8	
Total Operating Expenditure	645.7	702.0	783.1	856.9	
EBITDA	237.4	246.2	321.8	386.1	
Growth (%)	-2.0	3.7	30.7	20.0	
Depreciation	31.0	36.9	38.0	40.1	
Interest	0.0	0.0	0.0	0.0	
Other Income	0.0	0.0	0.0	0.0	
PBT	226.6	246.8	300.8	363.0	
Others	20.2	37.6	17.0	17.0	
Total Tax	73.5	79.6	93.0	108.9	
PAT	153.1	167.2	207.8	254.1	
Growth (%)	0.6	9.2	24.3	22.3	
EPS (₹)	99.2	108.3	134.6	164.6	

Source: Company, ICICIdirect.com Research

\*From FY16 onwards, financials are reported as per Ind AS

Balance sheet		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
<b>Liabilities</b>					
Equity Capital	15.4	15.4	15.4	15.4	
Reserve and Surplus	355.0	521.6	594.5	686.0	
Total Shareholders funds	370.4	537.1	609.9	701.4	
Total Debt	0.0	0.0	0.0	0.0	
Long Term Provisions	9.3	10.9	3.3	3.7	
Total Liabilities	379.7	548.0	613.2	705.1	
<b>Assets</b>					
Gross Block	484.7	527.8	557.8	587.8	
Less: Acc Depreciation	270.0	306.9	344.9	385.0	
Net Block	214.7	220.8	212.8	202.7	
Capital WIP	0.0	0.0	0.0	0.0	
Deferred Tax Asset	20.8	21.9	21.9	21.9	
Non Current Investments	2.3	2.3	52.8	59.4	
LT Loans & Advances/Others	5.2	4.2	4.2	4.2	
<b>Current Assets</b>					
Inventory	377.0	329.3	437.2	491.9	
Debtors	12.4	12.0	18.1	20.4	
Cash	21.2	19.9	28.2	86.9	
Loans & Advances	12.9	15.0	33.2	37.3	
Current Investments	160.0	170.0	286.4	322.3	
Other CA	0.7	0.3	6.9	7.8	
<b>Current Liabilities</b>					
Creditors	64.6	56.0	81.4	91.6	
Provisions	131.5	0.0	0.0	0.0	
Other CL	251.4	191.8	407.0	458.0	
Net Current Assets	136.8	298.8	321.6	417.0	
Total Assets	379.7	548.0	613.2	705.1	

Source: Company, ICICIdirect.com Research

Cash flow statement		₹ Crore			
(Year-end March)	FY16	FY17E	FY18E	FY19E	
Profit after Tax	153.1	167.2	207.8	254.1	
Add: Depreciation	31.0	36.9	38.0	40.1	
(Inc)/dec in Current Assets	5.9	36.3	-255.1	-97.9	
Inc/(dec) in CL and Provisions	-25.8	-199.6	240.7	61.2	
CF from operating activities	164.2	40.8	231.3	257.5	
(Inc)/dec in Investments	0.0	0.0	-50.5	-6.6	
(Inc)/dec in Fixed Assets	-47.9	-43.1	-30.0	-30.0	
(Inc)/dec in LT Loans & Adv.	-4.1	1.0	0.0	0.0	
Others	-3.6	0.5	-7.6	0.4	
CF from investing activities	-55.7	-41.6	-88.1	-36.2	
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0	
Inc/(dec) in loan funds	0.0	0.0	0.0	0.0	
Dividend paid & dividend tax	-129.5	0.0	-135.5	-162.6	
Inc/(dec) in Reval. Reserve	0.0	0.0	0.0	0.0	
Inc/(dec) in Exch. Fluc. Res.	0.0	0.0	0.0	0.0	
CF from financing activities	-129.4	0.0	-135.5	-162.6	
Net Cash flow	-20.8	-0.7	7.7	58.7	
Opening Cash	42.1	21.2	20.5	28.2	
Closing Cash	21.2	20.5	28.2	86.9	

Source: Company, ICICIdirect.com Research

Key ratios					
(Year-end March)	FY16	FY17	FY18E	FY19E	
<b>Per share data (₹)</b>					
EPS	99.2	108.3	134.6	164.6	
Cash EPS	119.2	132.2	159.2	190.5	
BV	239.9	347.8	395.0	454.2	
DPS	70.0	75.0	90.0	110.0	
Cash Per Share	13.7	12.9	18.3	56.3	
<b>Operating Ratios (%)</b>					
EBITDA Margin	26.9	26.0	29.1	31.1	
PBT / Net Sales	25.8	26.1	27.3	29.3	
PAT Margin	17.4	17.7	18.9	20.5	
Inventory days	156.6	127.3	145.0	145.0	
Debtor days	5.1	4.7	6.0	6.0	
Creditor days	26.8	21.6	27.0	27.0	
<b>Return Ratios (%)</b>					
RoE	41.3	31.1	34.1	36.2	
RoCE	59.7	45.0	49.0	51.5	
RoIC	62.5	41.9	56.1	64.9	
<b>Valuation Ratios (x)</b>					
P/E	37.8	34.6	27.9	22.8	
EV / EBITDA	24.2	23.3	17.7	14.6	
EV / Net Sales	6.5	6.1	5.2	4.5	
Market Cap / Sales	6.6	6.1	5.3	4.7	
Price to Book Value	15.6	10.8	9.5	8.3	
<b>Solvency Ratios</b>					
Debt/EBITDA	0.0	0.0	0.0	0.0	
Debt / Equity	0.0	0.0	0.0	0.0	
Current Ratio	1.3	2.1	1.6	1.6	
Quick Ratio	0.4	0.8	0.7	0.7	

Source: Company, ICICIdirect.com Research

## ICICIdirect.com coverage universe (FMCG)

Sector / Company	CMP		Rating	M Cap (₹ Cr)	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)			FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E
Colgate (COLPAL)	1,111	990	Hold	27,904	21.2	23.6	26.0	52.3	47.2	38.0	6.2	5.7	5.2	64.1	71.4	70.4	45.3	50.2	49.3
Dabur India (DABIND)	292	305	Hold	49,990	7.2	7.5	8.0	40.3	39.0	38.0	6.5	6.0	5.5	28.0	25.6	25.5	26.4	23.4	22.6
GSK CH (GLACON)	5,354	6,074	Buy	22,775	156.1	176.3	199.2	34.3	30.4	30.5	5.2	4.5	4.0	30.8	30.3	31.3	21.0	21.2	21.7
Hindustan Unilever (HINLEV)	1,080	1,120	Hold	234,662	20.8	22.8	26.7	51.9	47.4	41.9	6.9	6.4	5.8	74.9	82.2	85.6	66.6	66.7	69.0
ITC Limited (ITC)	342	407	Buy	393,394	8.4	10.3	11.6	40.7	33.2	35.0	7.2	6.6	5.8	32.9	38.1	40.2	22.5	26.5	27.9
Jyothy Lab (JYOLAB)	356	397	Hold	6,625	11.1	10.7	12.7	32.0	33.1	31.3	3.9	3.5	3.2	28.1	29.0	30.5	30.9	27.1	28.0
Marico (MARLIM)	314	341	Hold	41,532	6.3	6.9	8.4	49.9	45.5	40.4	7.0	6.0	5.1	44.6	45.1	49.4	34.9	34.6	37.7
Nestle (NESIND)	6,737	7,420	Buy	64,106	103.9	133.4	154.5	64.9	50.5	48.0	6.8	6.0	5.3	34.9	36.7	44.3	36.2	40.0	44.1
Tata Global Bev (TATGLO)	151	147	Hold	9,773	7.2	7.7	8.2	20.9	19.6	18.0	1.4	1.4	1.3	8.8	9.1	9.3	7.2	7.7	7.8
VST Industries (VSTIND)	3,750	4,130	Buy	5,791	108.3	134.6	164.6	34.6	27.9	25.1	6.1	5.3	4.7	45.0	49.0	51.5	31.1	34.1	36.2
Prabhat Dairy (PRADAI)	131	140	Buy	1,160	4.8	6.4	9.5	24.7	18.5	12.5	0.8	0.7	0.6	8.0	9.7	12.2	5.1	6.8	9.7
McLeod Russel (MCLRUS)	174	183	Hold	1,855	7.8	5.6	9.2	NA	31.0	20.0	23.5	16.8	15.1	6.2	5.8	6.5	3.3	2.3	3.6

Source: Company, ICICIdirect.com Research

## **RATING RATIONALE**

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Strong Buy: > 15%/20% for large caps/midcaps, respectively, with high conviction;

Buy: > 10%/15% for large caps/midcaps, respectively;

Hold: Up to +/-10%;

Sell: -10% or more;



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