Future Consumer Ltd.

TP: INR 41 - ACCUMULATE

30 March 2017

FMCG

Initiating Coverage

Key Statistics

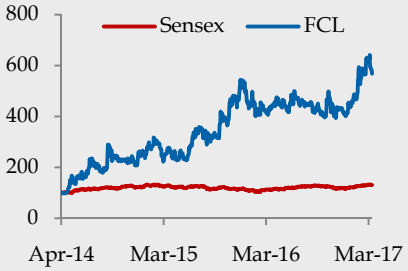
CMP (INR)	29.0
Upside/downside (%)	41.4
Market Cap (INR/USD m)	48,213/743
Shares outstanding (mn)	1,662.5
3 months avg volume (mn)	5.2
Dividend Yield (FY16, %)	0
52 Wk high/low	31.3/18.1
Sensex/Nifty	29,647/9,174
Bloomberg Code	FCON IN

Performance (%)*	1M	3M	12M
Absolute (%)	(0.9)	42.0	40.6
Rel. to Sensex (%)	(3.6)	30.0	22.0

Sh. Pattern, % (as Dec-2016)

Promoter	43.4
FII	18.7
DII	0.9
Other	37.0
Total	**100.0**

Stock Price Performance*



* Rebased to 100 | Based on daily closing prices

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Multiple growth drivers in place

Future Consumer Ltd. (FCL) is the food and FMCG arm of the Future Group. Post the group level restructuring, FCL has been largely focusing its energies on the food space. Food and beverages formed about 94% of the brands business with the balance coming in from its home & personal care stable. FCL's key brands include Golden Harvest, Premium Harvest, Kosh, Nilgiris, Tasty Treat, and Fresh & Pure. Growth is expected to be exponential as it would be driven by 1) Expansion of product portfolio; 2) Incremental penetration of existing products within Future Retail Ltd (FRL) stores; 3) Expansion of distribution network both at FRL level as well as other tie-ups. We expect FCL to grow its sales at a CAGR of ~40% over FY16 to FY19E. Increased penetration and contribution of higher margin brands will help improve profitability as well. We expect gross margins to expand by 292 bps over the same period. Focused distribution strategy, strength in sourcing & manufacturing as well as reduction in interest costs through paring of debt are expected to help the company turn PAT positive by FY19. We initiate coverage on FCL with ACCUMULATE and a TP of INR 41.

- ✓ **Growth to remain strong over next few years:** FCL is expected to grow at a strong pace led by multiple drivers - (i) expansion of FRL's store count; (ii) increased penetration to such stores; (iii) increased focus on non-Future Group retail outlet; (iv) higher proportion of value added products to existing stores. The company is also looking to leverage on the distribution network of its acquisition of Grasim's personal and baby care products portfolio. Through such efforts (including acquisitions of retail chains), FCL now reaches out to ~29,000 outlets. Further, the company has tied up with Nissin Foods (owner of 'Cup Noodles' and 'Top Ramen' brands) to reach out to *kirana* stores.
- ✓ **Improving profitability:** FCL's profit margins are slated to improve as the share of higher margin products increases. Currently staples account for ~60% of top line and these have lower margins in high single digit to low double digits. The company is looking to push its higher value and higher margin products which typically enjoy margins in the range of 25% to 30%. This would help improve gross margins. In addition to this lower interest costs by paring debt and divestment of its loss making subsidiary, Amar Chitra Katha (ACK), would help improve profitability at the net level as well.
- ✓ **Initiate with ACCUMULATE rating and TP of INR 41:** Considering that FCL is going through a transformation and is still in the investment phase, we believe that the best way to value the company would be on a price to sales basis. At current levels, the stock is trading at 1.6x/1.1x our FY18E/FY19E sales estimates which is at a significant discount to its closest listed competitor. FCL is still in an investment phase and will take time to see returns on its investments. However given its scope of growth and improvement in profitability, we believe it deserves a multiple of at least 0.5x that of its closest competitor. We initiate coverage on FCL with ACCUMULATE rating and a TP of INR 41 based on a multiple of 1.6x FY19E sales.

Year End (31 Mar)	FY15	FY16	FY17E	FY18E	FY19E
Revenues (INR mn)	13,123	17,578	21,196	33,468	47,724
Growth (%)	59.6	34.0	20.6	57.9	42.6
EBITDA (INR mn)	(515)	(197)	199	855	1,683
EBITDA Margin (%)	(3.9)	(1.1)	0.9	2.6	3.5
Adjt. PAT (INR mn)	(892)	(1,128)	(870)	(256)	381
Adjt. PAT Margin (%)	(6.8)	(6.4)	(4.1)	(0.8)	0.8
Diluted adjt. EPS (INR)	(0.5)	(0.6)	(0.5)	(0.1)	0.2
Growth (%)	NM	NM	NM	NM	NM
ROE (%)	(11.3)	(15.6)	(9.8)	(2.4)	3.5
P/E (x)	NM	NM	NM	NM	142.7
EV/EBITDA (x)	NM	NM	252.3	62.3	32.5
P/BV (x)	7.1	8.0	5.0	5.1	4.9

Source: Company, YSL estimates; Note: Valuations as on 30th March 2017

A host of factors to improve FCL's profitability

✓ **Growth to remain robust:** FCL has been able to grow its revenues by 2.1x from FY14 to FY16. This growth was a combined function of acquisitions, launch of new products and variants, strategic tie-ups (includes JVs) and expanding distribution network and reach. The company continues to work on many aspects that will keep its growth momentum intact.

1) **Leveraging the retail store network of the Future Group:** Around 93% of FCL's topline is its branded business which is predominantly being pushed through FRL's store network that includes hypermarket and convenience stores through brands/ formats such as Big Bazaar and Easyday which together contributed ~68% of total FCL's brand revenues. As on date, FRL has a distribution network of ~ 900 stores including Heritage, Nilgiris and Aadhar which together account for a little over 80% of FCL's brand revenues.

   FRL's management has an aggressive growth plan for adding stores, both at Big Bazaar and Easyday levels. It plans to take the store count for the two to 360 and 3000 respectively by 2021 (Currently ~230 and ~380 respectively). That includes having ~ 3,000 Easyday stores by 2021 (currently ~ 380 stores). This means that FRL would need to add at least 750 Easyday convenience stores per annum. On a conservative basis even if the company is able to add half of this, the store count increase for Easyday would still be ~370 stores per annum.

   Apart from the increase in store count, what will also drive growth is the increase in share of FCL's products in each of FRL's stores. FRL is looking to increase its food sourcing from group brands (essentially FCL's product portfolio). The Group has a target to source as much as 70% of the food sales from in house brands by 2021 (current contribution ~20%). This further increases the scope of business opportunity for FCL as it is the group's branded products FMCG arm.

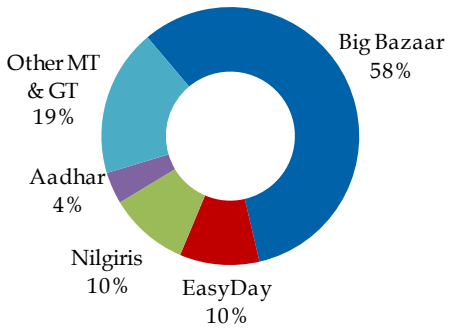
2) **Incremental penetration of product variants/brands:** FCL is also looking at increasing the sales of its relatively high value added (and higher margin) food products and categories to FRL's stores in times to come. As per our interaction with the company, currently the staples brands (Golden Harvest and Premium Harvest; as well as fruits and vegetables) and Tasty Treat products are available across its retail chain. But when it comes to the other categories and brands, there's still a huge scope to increase penetration further.

3) **Expanding reach to other general and modern trade outlets:** In addition to increasing sales contribution to the group, FCL is also looking to expand its reach in other general and modern trade outlets. It has entered into tie-ups and JVs for pushing their brands through other retail channels. For instance, the company has tied up with Nissin Foods to push some of its products under the Tasty Treats brand to reach out to 0.2 to 0.3 mn touch points by 2021.

4) **Aggressive spending on promotional and advertising efforts:** Launch of new products/variants as well as pushing the same through new sales channels will require the company to create and back the brands by the requisite promotional

and advertising efforts. In FY16, the company spent about INR 140 mn towards A&P expenses. In FY17, the company will be increasing this to INR 700 mn. For FY18, the estimate is INR 1 bn.

Exhibit 1: Non-Future Group business to drive growth and margins?



Format	Count**
Future Group stores	900
Rajasthan FPS	5,300
Other modern trade	81
General trade	17,000
Kirana stores*	200,000

*Access through Nissin
**Approximate numbers

Source: Company

✓ **Huge potential for some large brands coming out from the existing portfolio:**

FCL is an integrated play on the food space involved in every stage of the chain – sourcing, manufacturing, marketing, distributing and selling. Given the shift in consumer preference moving towards premium and branded food items, the company is looking to capitalize on the same by having a plethora of brands across categories by concentrating on 4 main strategies:

1) Creating brands in the commodities/ staples space.
2) Entering categories where there are very few branded players.
3) Creating new categories altogether.
4) Price play in the home and personal care space.

FCL's current portfolio stable has around 30 brands across various categories.

Exhibit 2: FCL's brand stable

Source: Company

FCL has entered into several tie-ups to boost its product portfolio and/or to expand their distribution reach. This route of entering into tie-ups/JVs allows for faster product launches (including new categories) as well as lets the company focus on marketing and distribution. We believe some of the new initiatives have the potential to be big categories/ brands because of their differentiating factors.

Exhibit 3: Recent tie-ups/developments of FCL

Company	Product (category)	Type
Sunkist Growers, Inc.	Sunkist (beverages)	License agreement
Mibelle AG	Swiss Tempelle (personal care products)	JV
Nilgiris	Nilgiris (dairy and bakery)	Acquisition
Hain Celestial	Terra (chips), baby food, non-dairy milk	JV
SVA India	Kosh (oats)	JV

Source: Company

- **Kosh (Oats brand)**: Kosh is being marketed and positioned as the third grain in India (after rice and wheat). The aim is to push oats to the centre of the plate. FCL is looking to spend ~ INR 500 - 600 mn on the Kosh brand over a 3 year period starting mid FY17. It has initiated trade launch in over 8,500 stores and is also in the process of setting up a distributor network to accelerate the sales.

- **Hain Celestial:** In early 2017, FCL tied up with the Hain Celestial Group, a move that will mark FCL's entry into the organic food space. The plan is to locally manufacture brands and products that belong to Hain Celestial. To start with, this unit will focus on non-dairy milks (rice, oats, almond, soy), baby foods and healthy chips. It is expected that overtime, other Hain Celestial brands such as Garden of Eatin, Sensible Portions, Dream and Earth's Best could be launched here.

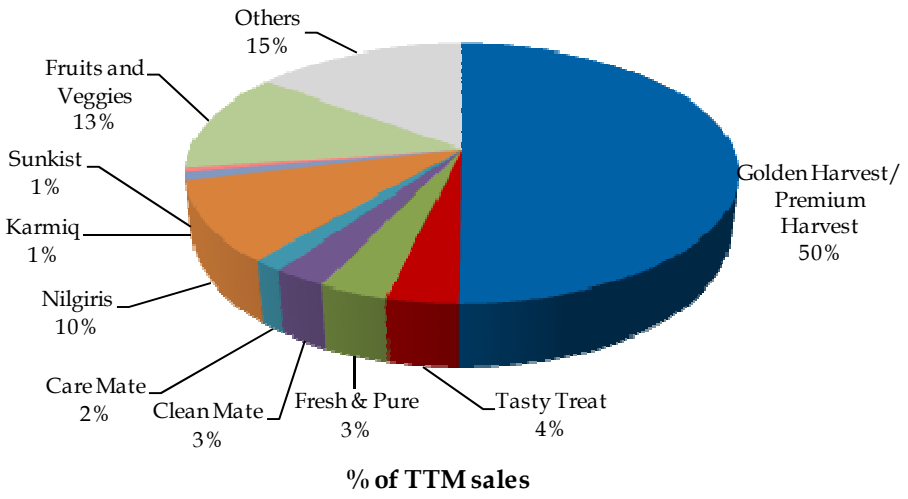
- **Tasty Treat:** This umbrella brand has many product categories in its stable that include chips, wafers, Indian savories, juices, cookies, baked snacks, ketchups, noodles, pasta, jams, frozen foods, amongst others. Currently this brand of products is available across FRL's stores. To push this further, FCL has tied up with Nissin Foods to reach out to an additional 200,000 – 300,000 touch points by 2021. FCL is also looking to push the brand through other General Trade (GT) and Modern Trade (MT) outlets that will give this brand a strong fillip in the future.

- **Nilgiris**: FCL acquired the retail chain and manufacturing setup of Nilgiris in 2014. It is now investing towards revamping its product portfolio (bakery and dairy) and pushing FCL's products into Nilgiris stores. FCL is also looking to push the longer shelf life products of Nilgiris to other parts of the country and is also setting up manufacturing units closer to markets to sell products that have shorter shelf lives.

We believe the full year impact of the new launches and new developments/ tie-ups - opening up of select brands to general trade, reach to new outlets, as well as expansion of FRL's stores - will drive growth by over FY18 and FY19. Over FY16 to FY19, we expect the company to clock a CAGR of ~ 40% in the top line.

- ✓ **Change in product mix to lead to improved margins:** FCL's staples and fruits and vegetables combined form a little over 60% of the FCL's top line at present.

Exhibit 4 : FCL: At present, staples form a significant portion of sales



Source: Company

Gross margins in this segment range in high single digits to low double digit region. The company is working on increasing contribution from its value added products, some of which include those developed in-house as well as through collaborations (including JVs). All of this is expected to improve FCL's margin profile as gross margins in other categories are relatively higher. For instance, products from FCL's Tasty Treat and Kosh portfolio earn gross margins in the range of 20%-30%, while products from the Kara and Sangi's Kitchen stable earn margins of around 60%.

- ✓ **Focused distribution strategy:** As of January 2017, FCL currently has an overall distribution footprint of ~29,000 stores and has an access to ~900+ store network of FRL. It has extended itself to access the modern trade network at Lulu and Haiko. As compared to the traditional distribution strategy of having a multi-layered distribution network across the country, FCL looks to directly sell to the modern trade outlets (including FRL's outlets), or go through cash and carry stores (Metro, Booker) – which in turn sell to the General Trade (GT) outlets. Its latest strategic tie-up with Nissin will allow it to further penetrate the GT space. FCL also has access to the end to end GT network (through which is currently largely selling Kara and Kosh products) that comes through the acquisition of Grasim's personal care product portfolio.

  - **Distribution for F&B (94% of branded sales):** FCL has ready access to the outlets of FRL. As for its modern trade F&B distribution strategy, Tasty Treat as a brand is available in over 40 MT outlets. Kosh products are currently available in over 80 MT outlets. While there is a scope to increase penetration within the group given that Easyday and Heritage are getting integrated into the system, there would also be a sizeable opportunity to launch other F&B brands into the market through the modern trade system. FCL will be selective in pushing certain brands (focused on those that are being pushed

outside of FRL's network) and would be focusing on in-store promotional activities to promote the other brands (relatively low cost affair with a higher conversion ratio). For instance, the roll out in modern trade has begun for Desi Atta. Further, Karmiq is available in 15 MT outlets. The staples and fruits & vegetables portfolio has access to FRL's network including the Aadhaar and Annapurna Bhandar route.

- **Distribution for Home & Personal Care (HPC):** Within its HPC portfolio, the strategy remains the same. Apart from ready access to FRL's network, Kara is a brand that is available in over 150 Modern Trade outlets and has access to ~17,000 stores. This provides the company the opportunity to cross sell other products. Further, the proposed tie up with Booker will expand its reach in the GT space. The company expects this to offer a huge piggybacking opportunity for the remainder of the HPC portfolio.

- **Nilgiris:** Nilgiris as a standalone unit also has good potential considering it contributes to nearly 10% of the company's revenues. The aim here is to launch the rebranded products of Nilgiris across FRL's other chains. Within the GT space, the brand enjoys strong presence in southern India, through 40 institutions which further sell to GT outlets.

✓ **Other efforts to add to growth:** In mid 2015, FCL partnered with the Rajasthan government to manage the overall public distribution system to sell multi-brand consumer goods through the ration shops - Annapurna Bhandars. So far, the company has revamped more than 5,000 fair price shops. The Rajasthan government has given its nod for a facelift of another 2,500 shops. This development provides FCL access to sell its products to a wider range of audience. A year ago, out of ~214 products that were being sold through the PDS network, ~ 20% SKUs were those of FCL. While this effort is expected to provide a boost to sales, the margins on the revenues that come through this initiative will be on the lower side due to a higher proportion of sales of staples brands.

In addition, with FCL looking to reduce dependence on the group's distribution chain to boost its reach, the company has opened up its products to general trade, as well as other modern retail outlets. However, the strategy will be largely limited to the brands and products that it plans to back with the requisite marketing and sales efforts. The acquisition of Kara and other brands from Grasim Industries gives it access to ~17,000 outlets, which can be utilized to push products overtime as well. FCL also tied up with wholesaler Booker Group's retail arm (50% stake in the JV). The company is investing INR 500 mn for this stake, which will allow it to make further inroads into Maharashtra and Gujarat. Through this, the company is targeting to reach 0.2 to 0.3 mn outlets over a five-year period.

✓ **Efforts to pare expenses and improve margins:** Apart from the aim to shift the focus towards more value added (higher margin) products as well as the benefits that will accrue from larger operations and economies of scale, FCL is looking to work towards improving the health of its balance sheet (this is in addition to paring debt on books). One major step it took is to franchise all of its then loss making and more working capital intensive retail operations to FRL (apart from

Nilgiris which was operating a franchise model prior to acquisition). This includes KB's Fair Price and Big Apple. This led it to free up capital which was locked up in the form of inventory. As per the agreement, FCL now earns ~1.25% of sales as royalty from FRL.

What has also been a drag on FCL's books has been the financial performance of its subsidiary (~74% stake) Amar Chitra Katha (ACK), a legacy investment. ACK is in the business of education and entertainment, and publishes various children's magazines and books, such as Tinkle and Amar Chitra Katha – both of which are well-known comics in India. In FY16, the revenues of this business stood at INR 500 mn, while EBITDA stood at a negative INR 62 mn (-12.4% operating margin). PBT loss on a TTM basis has been over INR 200 mn. With ACK being a non-core business segment, FCL has been on the lookout to divest this stake. We believe this could improve performance at the PBT level considerably.

- ✓ **Capital infusion has strengthened balance sheet:** In FY16, the company issued compulsory convertible debentures (CCDs) to Black River Food 2 Pte Limited (Cargill's PE arm) on a preferential allotment basis. Further, the company also raised nearly INR 168 mn (25% of total consideration for warrants) from the promoter group in FY16 by issuing warrants which may be exercised within 18 months of issuance. In addition, the International Finance Corporation (IFC) invested about US$ 20 mn or INR 1.34 bn) in the company in mid 2016 in the form of CCDs which would be convertible into equity shares within 18 months of issuance. The conversion price for the CCDs is INR 22.73 per share.

All of these developments have brought in about US$ 75 mn into FCL. The company plans to pare down its debt levels considerably through this. As per the company, the gross debt on the books stands at INR 4.4 bn currently as compared to ~INR 6.1 bn as of FY16. The company has utilized funds to repay debt. Interest costs in the quarter ended December 2016 stood at INR 121 mn as compared to INR 159 mn in the corresponding period a year before.

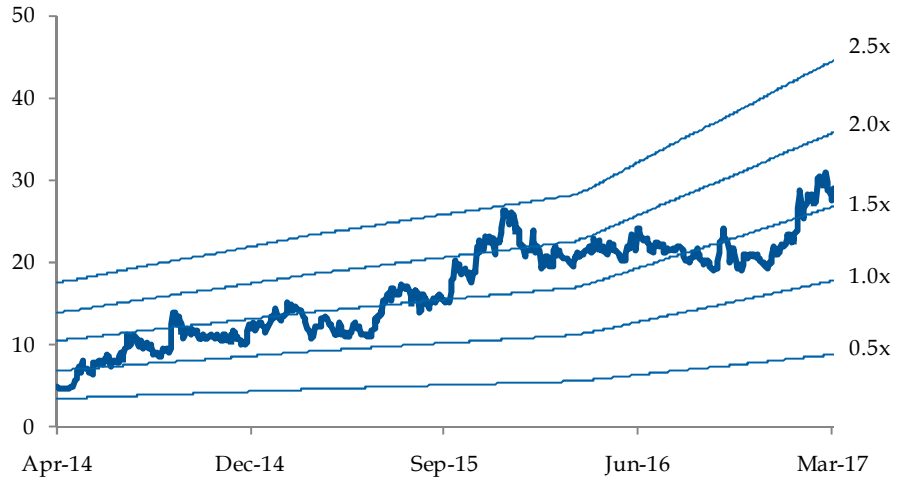
FCL is also been keeping an eye on its working capital requirements. The non-cash working capital to sales ratio has declined to 8% in FY16 from 11% in FY11.

Valuation

- ✓ **Initiate with target price of INR 41; ACCUMULATE rating**

Since FCL is going through a transformation and is still in the investment phase, we believe the best way to value the company would be on a price to sales basis. At current levels, the stock is trading at 1.6x/1.1x our FY18E/FY19E sales estimates. This is at a significant discount to other players in the industry which trade at an average forward multiple of ~5x/4x their FY18E/FY19E sales. FCL's closest listed competitor which is trading at 3.8x/3.3x its FY18E/FY19E sales (Bloomberg estimates). Given that FCL is still in an investment phase and will take time to see returns on its investments, but given its scope of growth and improvement in profitability, we believe it deserves a multiple of at least 0.5x that of its closest competitor. **We initiate coverage on FCL with ACCUMULATE rating and a TP of INR 41 based on a multiple of 1.6x FY19E sales.**

Exhibit 5: FCL- 1 year forward P/S band chart



Source: YSL

Exhibit 6: Peer Comparison

Company Name	Ticker	Market Cap (INR mn)	CMP (INR)	Price to Sales (x)		Gross Margins		Return on Equity	
				FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Britannia Industries Ltd.	BRIT IN	407,421	3,395	3.79	3.31	40.2%	40.7%	40.5%	38.4%
Dabur India Ltd.	DABUR IN	482,921	274	5.24	4.68	52.4%	52.6%	27.8%	27.3%
Future Consumer Ltd.*	**FCON IN**	**48,212**	**29**	**1.63**	**1.14**	**18.0%**	**18.9%**	**-2.4%**	**3.5%**
Hindustan Unilever Ltd.	HUVR IN	1,989,428	919	5.38	4.81	51.2%	51.7%	108.4%	117.9%
ITC Ltd.	ITC IN	3,432,589	283	7.27	6.58	55.0%	55.0%	30.1%	30.7%
Nestle India Ltd.	NEST IN	636,845	6,605	5.31	4.83	57.7%	50.4%	NA	NA

Source: Bloomberg, *YSL estimates
Valuations based on closing price as on 30th March 2017.

✓ Risks to our thesis

i. **Fund requirements may lead to further dilution:** Further investments could necessitate to go in for capital raising, which may lead to further dilution.

ii. **Failure of brands to take off as expected:** With FCL getting aggressive in product launches and looking to hit the GT trade with select brands, it will require the requisite investment and resources to support the same. Inability to do so may result in underachieving desired results.

iii. **No meaningful change in product mix will lead margins to remain under pressure:** While FCL is targeting aggressive growth, what remains essential is how the product mix changes in favor of the non-staples products. If the proportion of the value added products does not increase meaningfully, it could lead to margins being lower than expectations.

iv. **ACK divestment takes longer than expected:** Given that ACK is negatively impacting the consolidated financials, any delay in its stake sale will lead to extended period of losses to that proportion.

v. **Upside risks:** New launches/variants within existing brands or new brands which have not been factored into our estimates.

Company background

FCL is the FMCG arm of the Future Group, which has presence across businesses but is renowned for its dominance in the organized retail space (both for food and fashion). FCL broadly categorizes its segments into two – branded products (~93% of revenues) and others (~7% of revenues; this includes franchise royalties, food park and Aadhar revenues). The former includes two segments - F&B and HPC. F&B contributes to ~94% of branded goods business, while the balance is contributed by the HPC portfolio.

Key brands and their description:

- Golden Harvest - Packaged staples such as wheat flour, maida, besan, spices, rice, daliya, sooji, pulses, sugar
- Premium Harvest – premium packaged staples, pulses, spices, cereals, basmati rice, sugar, sprouts
- Tasty Treat - processed foods, snacking items such as bhujia, ketchup, pasta
- Nilgiris - dairy and bakery products
- Sunkist - beverages including fruit juices, sparkling beverages
- Swiss Tempelle - personal care products such as body wash, body lotions,
- Kara- beauty-on-the-go with various types of wipes
- Clean Mate – household cleaning products such as toilet & floor cleaners, utensil cleaners, detergent powder
- Care Mate – personal hygiene products such as tissues & foil, liquid hand soap, sanitary pads and diapers
- Sangi's Kitchen – Sauces, chutneys and dips
- Karmiq - dry fruit range, various oils including olive, canola and rice bran
- Kosh – oats: instant, broken, flours. The oats are available in 4 varieties - broken oats, oats atta, instant oats and wheat & oats atta. This is being positioned to not just focus on eating healthy breakfasts and snacks – in the form of oat based meals/ instant oats - but also to bring in the healthy aspect in every meal. Through Kosh's positioning and promotional activity, the company's communication is for consumers to use/ mix oats in their daily food dishes .
- Veg Affaire – frozen vegetables
- Fresh & Pure - Ghee, edible oils, packaged honey, amongst others
- Desi Atta Company – multiple variants of flour
- Soo Fresh & Go Bananas - packed fruits and vegetables

Prior to FY14, FCL was known as Future Ventures Limited. The business model then was that of it being a holding company, investing in businesses including fashion and food brands. ACK is a legacy investment that remains on FCL's books today. FCL has been operating in its current avatar since FY14, post the restructuring that happened at the group level.

As of December 2016, the promoter group held around 43.4% stake. Institutions held around 19.55% stake, with domestic mutual funds having an exposure of less than 1%. Balance was held by foreign portfolio and institutional investors; some prominent names include Verlinvest SA (8.45%) and Arisaig Partners (9.15%).

At the helm is Mr. Kishore Biyani who is FCL's Vice-Chairman. He is the founder and Group CEO of Future Group. Has over 25 years experience and is considered as the

pioneer of modern retail industry in India. Mr. Devendra Chawla is the CEO of FCL. He has over two decades of industry experience. He has been associated with the Future Group for over 8 years leading the food retailing and FMCG business in various capacities. Previously, he was associated with Reliance Fresh and Coca-Cola.

FCL has a number of subsidiaries and associate companies. Details of some of them are below:

- **Nilgiris (100% stake)**: FCL has a presence in the neighbourhood convenience stores in south India through Nilgiris, which is one of the oldest retail, dairy and bakery brand in the region. These stores are run through a network of franchisees. Nilgiris has also brought with it its FMCG brand (which has been around for over a century) and manufacturing facilities for dairy, bakery and confectionery products.

- **Aadhaar (100% stake):** Rural distribution is led through Aadhaar that operates through cash-and-carry model in Gujarat and Punjab and another 38 smaller format retail stores that are either operated by the company or through franchisees.

- **Sublime Foods (51% stake):** Sublime Foods makes convenient food products (sold under the Sangi's Kitchen brand) such as sauces, condiments and dressings. The unit (set up at India Food Park) produces oriental and western sauces such sweet & chilli, chilli garlic, sriracha, schezwan, mayonnaise, Indian ginger garlic paste & imli chutney and Italian classic arrabiatta & alfredo.

- **MNS Foods (50.01% stake)**: MNS Foods is set up to manufacture, brand, sell & distribute various kinds and flavors of wafers biscuits.

- **India Food Park (IFP; ~74% stake):** Located at Tumkur (Karnataka), IFP is an 114 acre integrated multi food manufacturing facility set-up in partnership with the Ministry of Food Processing Industries, Government of India. This park facilitates end to end food processing along the value chain (grading, sorting, pulping, packaging & distribution) from the farm to the market. The park is a home for several food processing firms where IFP enables them to work through a single window system.

- **Aussee Oats Milling (50%+1 share):** Aussee Oats operates a state-of-the-art oats based breakfast cereals manufacturing facility (EOU - Export Oriented Unit) in Sri Lanka through a JV initiative with SVA India Limited. Aussee Oats focuses on manufacturing and selling of a range of breakfast cereals such as mueslis, oats, cornflakes, wheat flakes, etc. The finished products are targeted to be sold by Aussee Oats in various countries such as India, Sri Lanka, Pakistan, Nepal, Bangladesh, Bhutan, etc.

- **Aussie Oats India (50% stake+1 share):** Aussee Oats India is engaged in the business of selling, importing, exporting and processing of all types of food products, primarily focusing on oats and oats based products in India.

- **Mibelle Future Consumer Products AG (50% stake)**: FCL entered into JV with Mibelle AG (Switzerland) for marketing and distribution of imported personal care products under the brand name "Swiss Tempelle" in India.

- **JV with Booker Group (50% stake):** In November 2016, FCL announced the signing of a non-binding termsheet to form an equal joint venture with United Kingdom's largest wholesaler, Booker Group to expand and develop Booker India. FCL and Booker Group will jointly invest in scaling up the network, with the aim to service the merchandizing requirements of neighbourhood retailers across the country.

- **JV with Tilda Hain India (50% stake):** In January 2017, FCL entered into a JV agreement with Tilda Hain India Private Limited, a part of Hain Celestial Group, Inc., New York, USA for undertaking the business of manufacturing, marketing, trading, selling and distributing various food products in the health and wellness category such as chips, non-dairy beverages, straws and infant / toddler foods.

- **Amar Chitra Katha (ACK; ~74% stake):** ACK owns the flagship brands 'Amar Chitra Katha', 'Tinkle' and 'Brainwave', and also has a strategic investment in a children's audio book brand 'Karadi Tales'. It has basket of 400+ titles and over 100 proprietary characters. It is an established leader in the under 15 age group with diverse product offerings in various formats that are compatible to new media platforms. ACK also operates India Book House (IBH), the largest distributor of books and magazines in India. It has also entered into a licensing arrangement with National Geographic Society, USA for publishing 'National Geographic Magazine' and 'National Geographic Traveller' in India.

Exhibit 7: A showcase of some of FCL's brands and products

Source: Company website, presentation; YSL

PEER COMPARISION

When it comes to product pricing, here's a list of some of FCL's non staples brands and how they are priced against similar products in the market:

Exhibit 8: Price point comparison

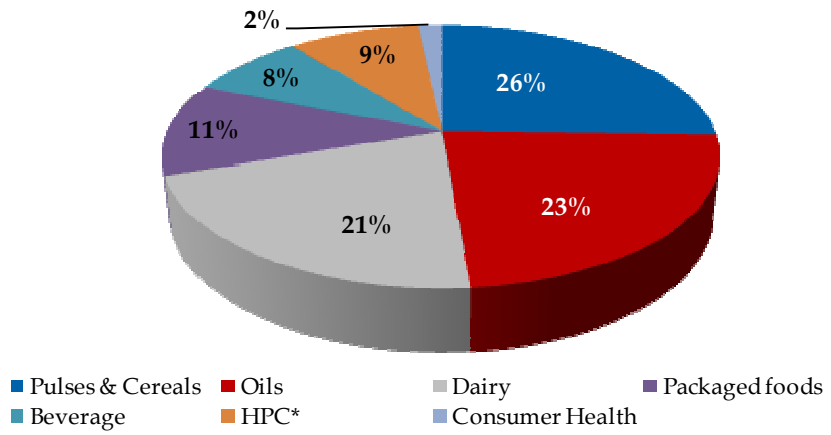
Category	FCL*	Others*
Bhujiya	Tasty Treat (INR 45, wasabi/ barbeque, 150 gms); (INR 209 Namkeen Aloo Bhujia, 1 kg)	Garden (INR 35, Alu Bhujiya 150 gms); Haldiram's (INR 35, Nagpur Bhujia Sev, 150g; Haldiram (INR 190; Aloo bhujia, 1 kg)
Body wash	Swiss Tempelle (body wash, INR 175/185, 300 ml)	Lifebuoy (INR 175, Lemon Fresh Body Wash, 300ml); Nivea (INR 175, Bath Care Shower Cream Soft, 250 ml); Dove (INR 160, Gentle Exfoliating Body Wash, 190 ml)
Flavoured milk	Nilgiris (INR 35, 180 ml)	Amul Kool (INR 20, 200 ml); Sofit (INR 25, Kesar Pista, 200ml); Danone (INR 25, Smoothie - Choco, 180 ml); Hersheys (INR 35, Milkshake cookies & creme, 200 ml)
Flour	Kosh oats + wheat (INR 270, 5 kg)	Bagrry's (INR 99, Oats for Atta, 500g); Pillsbury (INR 215, Chakki Fresh Atta, 5kg); Aashirvaad (INR 220, Superior MP Atta, 5kg); Patanjali (INR 160, Whole Wheat Atta, 5kg)
Arrabbiata pasta sauce	Sangis Kitchen (INR 120, 400 gms)	K's Kitchen (INR 115, Arrabiata Pasta Sauce, 270g); Chef's Basket (INR 149, Chunky Arrabbiata Pasta and Pizza Sauce, 300g)
Tomato ketchup	Tasty Treat (INR 120, pouch 1 Kg)	Kissan Fresh (INR 125, Tomato Ketchup pouch, 1kg); Delmonte (INR 125, Tomato Ketchup Original Blend, 1kg); Maggi (INR 140, Rich Tomato Ketchup bottle, 1kg)

Source: Big Bazaar, Amazon, bigbasket, Zopnow; *only MRPs considered

FOOD – AN INDUSTRY PERSPECTIVE

India's FMCG industry was estimated to be USD 185 bn at the end of December 2015, growing at a CAGR of 12% over 2005 to 2015 *(Source: CII National FMCG Summit-2015, Boston Consulting Group)*. Food constitutes a significant portion of the total industry.

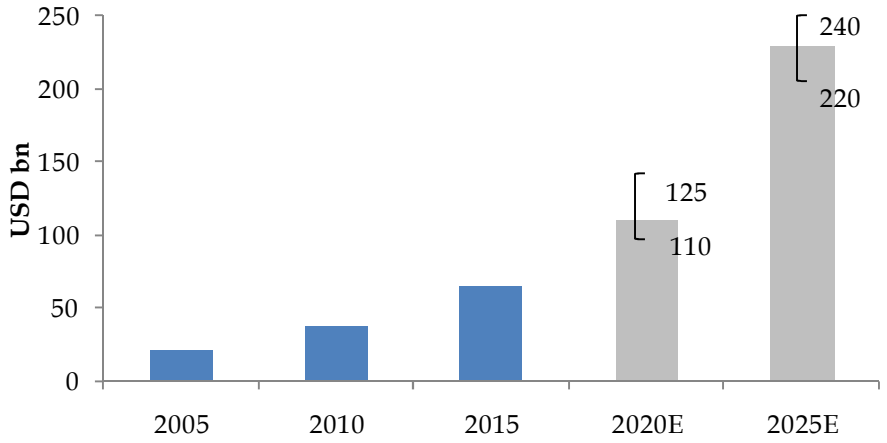
Exhibit 9 : Breakup of India's FMCG market (as at the end of December 2015)



Source: CII National FMCG Summit-2015, Boston Consulting Group (BCG)
*HPC – Home & Personal Care

Of the total industry, the branded portion constitute 34% or USD 65 bn. As per BCG, this portion is expected to grow at a CAGR of ~ 14% over 2015 to 2025 to USD ~220-240 bn.

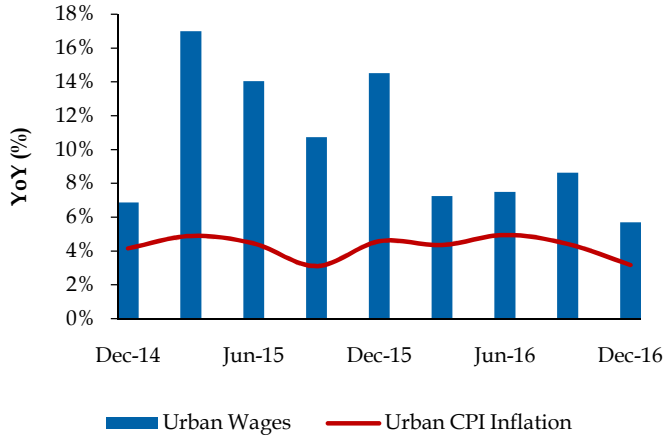
Exhibit 10 : Growth of branded segment in FMCG to accelerate over 2015-2025



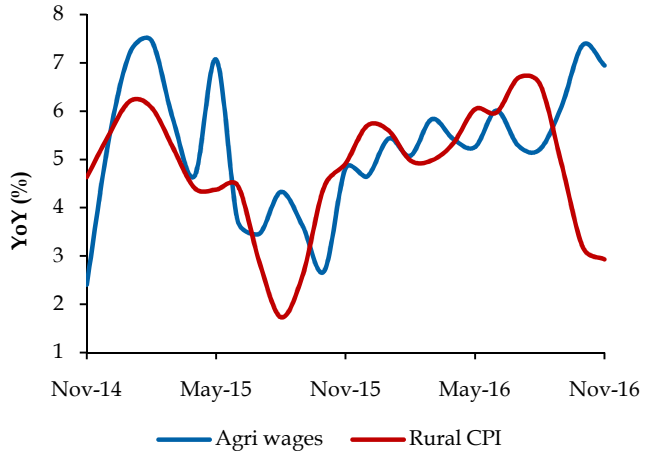
Source: CII National FMCG Summit-2015, Boston Consulting Group (BCG)

This growth would be driven by 1) **Increasing consumer income:** Real average household incomes have been rising. On the urban side, real urban disposable income has remained stable particularly as inflation has ebbed away. On the rural side too, easing inflation plus better farm output has led to an improvement in real wages.

Exhibit 11: Urban disposable income has maintained…..



… rural income too has shown signs of improvement



Source: YES Bank

2) Urbanization: Increasing urbanization has resulted in an increase in a preference for branded products. BCG expects ~ 35% of Indian population to be urbanized by 2020 as compared to 32% in 2015. **3) Growing work force**.

- ✓ **Premiumization gaining prominence:** Urbanization and increasing disposable incomes have led to a rise in number of consumers seeking "premium" products. According to IMRB's Kantar World Panel report, published in 2013, nearly 50% of the total number of new launches in the personal care category have been in the premium segment. Even in the food segment, most companies have been concentrating on innovation to launch premium variants for expanding their product portfolios. Competition is rapidly moving towards premiumization rather than pure pricing.

- **Growth in organized trade as food companies seek to curtail costs while pushing complex product portfolios:** As companies focus on premiumization and pushing these complex product portfolios, they have to also concentrate on improving margins which is done through increasing reliance on larger and/or mega distributors and cutting down on smaller distributors. This in turn has led to an increased shift towards modern retail in the country. FICCI expects this shift to modern trade to continue and sales to grow at the rate of 20% per annum; twice as fast as that of traditional trade.

- **Modern Retail distribution network and private labels:** Private labels are finding their footing and favor with consumers looking for value. According to a Nielsen report, 5% of all modern trade sales in India in 2014 were contributed by private labels, which are increasingly entering categories such as confectionary and dairy with shoppers trusting the quality of store brands. Categories such as food and house-cleaning products are especially generating strong sales of private labels in modern formats.

INCOME STATEMENT

(INR Millions)

Year ending March	FY15	FY16	FY17E	FY18E	FY19E
Total operating revenues	13,123	17,578	21,196	33,468	47,724
Growth (%)	59.6	34.0	20.6	57.9	42.6
EBITDA	(515)	(197)	199	855	1,683
EBITDA margin (%)	(3.9)	(1.1)	0.9	2.6	3.5
Growth (%)	NM	NM	NM	329.7	96.8
Depreciation & amortization	475	603	665	749	839
EBIT	(990)	(800)	(466)	106	843
EBIT margin (%)	(7.5)	(4.5)	(2.2)	0.3	1.8
Interest	319	611	504	462	562
Other income	352	227	90	90	90
Profit before tax	(958)	(1,184)	(880)	(266)	371
Tax	(0)	1	-	-	-
Minority Interest	40	115	21	21	21
Profit/loss of associate company	(9)	(11)	(11)	(11)	(11)
Adjusted net profit	(892)	(1,128)	(870)	(256)	381
Adjusted net margin (%)	(6.8)	(6.4)	(4.1)	(0.8)	0.8
Reported net profit	(1,024)	(1,128)	(870)	(256)	381
Reported net margin (%)	(6.8)	(6.4)	(4.1)	(0.8)	0.8
Adjusted EPS (INR)	(0.5)	(0.6)	(0.5)	(0.1)	0.2
Growth (%)	NM	NM	NM	NM	NM

CASH FLOW STATEMENT

(INR Millions)

Year ending March	FY15	FY16	FY17E	FY18E	FY19E
Net profit before tax	(1,088)	(1,231)	(880)	(266)	371
Depreciation & amortization	490	603	665	749	839
Change in working cap Inc/dec	(1,378)	963	(433)	(2,387)	(3,450)
Others	(456)	305	633	1,248	2,176
Operating cash flow	**(2,431)**	**640**	**(14)**	**(656)**	**(64)**
Capex	(592)	(988)	(800)	(2,000)	(1,000)
Free cash flow (FCF)	**(3,023)**	**(348)**	**(814)**	**(2,656)**	**(1,064)**
Investments	(2,721)	798	-	-	-
Others	1,386	556	90	90	90
Cash flow from investing	**(1,927)**	**366**	**(710)**	**(1,910)**	**(910)**
Equity issue	80	2	5,008	0	0
Debt issue (net)	4,754	(673)	(1,596)	730	1,371
Dividend & tax thereon	-	-	-	-	-
Other financing cash flows	(206)	(484)	(504)	(462)	(562)
Cash flow from financing	**4,627**	**(1,154)**	**2,908**	**268**	**809**
NET CASH FLOWS	268	(149)	2,184	(2,298)	(165)
Opening cash	104	373	300	2,484	186
Closing cash	373	225	2,484	186	21

BALANCE SHEET

(INR Millions)

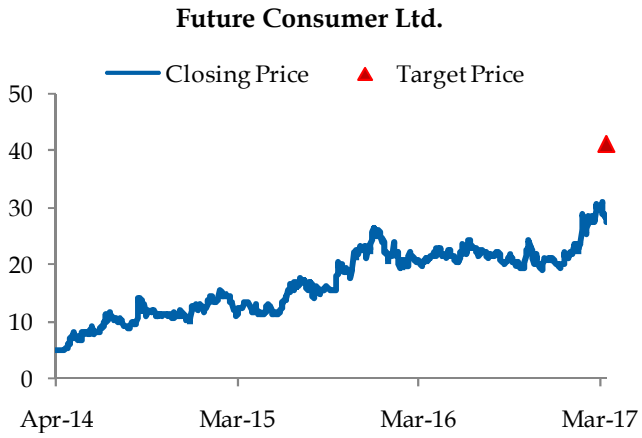
Year ending March	FY15	FY16	FY17E	FY18E	FY19E
SOURCE OF FUNDS					
Share capital*	9,943	9,945	11,267	11,267	11,267
Reserve & Surplus	(2,247)	(3,179)	(363)	(619)	(237)
Total shareholder's funds	**7,696**	**6,765**	**10,904**	**10,648**	**11,030**
Minority Interest	338	215	215	215	215
Debt	6,735	6,080	4,483	5,213	6,584
Other long term liabilities/provisions	159	158	158	158	158
TOTAL	**14,928**	**13,217**	**15,760**	**16,234**	**17,986**
APPLICATION OF FUNDS					
Gross block	7,375	8,613	9,413	11,413	12,413
Less: Accumulated depreciation	2,178	2,710	3,376	4,125	4,965
Net block	5,197	5,902	6,037	7,288	7,448
Goodwill on consolidation	3,685	3,642	3,642	3,642	3,642
Capital WIP	505	435	435	435	435
Investments	1,694	453	453	453	453
Other non-current assets	-	2	2	2	2
Total current assets	5,388	4,453	7,205	7,594	10,541
Inventories	1,115	1,224	1,451	2,255	3,180
Debtors	1,546	1,791	2,149	3,393	4,838
Cash & cash equivalents	433	300	2,484	186	21
Loans & advances	2,201	1,119	1,102	1,740	2,482
Other current assets	93	20	20	20	20
Total current liabilities	1,541	1,670	2,014	3,179	4,534
Net current assets	3,847	2,784	5,192	4,415	6,007
Net deferred tax (asset)	-	-	-	-	-
TOTAL	**14,928**	**13,217**	**15,760**	**16,234**	**17,986**

*Assumes full dilution

KEY RATIOS

Year ending March	FY15	FY16	FY17E	FY18E	FY19E
PROFITABILITY RATIOS					
EBITDA Margin (%)	(3.9)	(1.1)	0.9	2.6	3.5
Adjusted net margin (%)	(6.8)	(6.4)	(4.1)	(0.8)	0.8
Return on capital employed (%)	(7.3)	(5.1)	(2.9)	0.6	4.0
Return on equity (%)	(11.3)	(15.6)	(9.8)	(2.4)	3.5
EFFICIENCY RATIOS					
Asset Turnover	1.2	1.5	1.7	2.2	2.8
Debt to equity	0.9	0.8	0.5	0.5	0.6
Net debt to equity	0.8	0.8	0.2	0.5	0.6
Interest coverage	(3.1)	(1.3)	(0.9)	0.2	1.5
Debtor days	43.0	37.2	37.0	37.0	37.0
Inventory days	35.7	30.3	30.0	30.0	30.0
PER SHARE DATA					
Adjusted EPS (INR)	(0.5)	(0.6)	(0.5)	(0.1)	0.2
Book value per share (INR)	4.1	3.6	5.8	5.7	5.9
DPS (INR)	-	-	-	-	-
VALUATION RATIOS					
P/E	NM	NM	NM	NM	142.7
P/BV	7.1	8.0	5.0	5.1	4.9
EV/EBITDA	NM	NM	252.3	62.3	32.5
Dividend Yield (%)	-	-	-	-	-

Recommendation History



Date	Rating	Target Price	Closing Price
30-Mar-17	ACCUMULATE	41	29

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ACCUMULATE: Expected point to point returns of 15% or more

NEUTRAL: Expected point to point returns in the range of -10% and +15%

REDUCE: Expected point to point decline of 10% or more

NOT RATED: Not in regular research coverage

SUSPENDED: The rating as well as the target price has been suspended temporarily. This could be due to events that made coverage impracticable or to comply with applicable regulations and/or company policies.

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