PREAPRED BY
Vineet Khatri

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HINDUSTAN FOODS LTD

WHAT ARE THE OPPORTUNITIES AHEAD ?

CONTENTS

INTRODUCTION

- Hindustan Foods Limited is a leading Contract Manufacturer in the FMCG industry
- Hindustan Foods Limited (HFL) has undergone a significant transformation over the past decade, evolving from a food processing company to a diversified contract manufacturer of FMCG products
- The company has strategically expanded its product portfolio, geographical presence, and manufacturing facilities, positioning itself as a leading contract manufacturer in India
- The company operates with three models for providing manufacturing facilities for the client. They are:
  - Dedicated facility: A dedicated plant is set up for the client where only its products are manufactured
  - Shared manufacturing: A common plant is set up where more than one client's manufacturing is done. Usually, the smaller companies go for this as they can get cost optimization via this model
  - End-to-End Manufacturing: HFL helps the client in product design, packaging, and manufacturing. From Idea to Production, HFL takes care of all

BRIEF HISTORY

- Established in 1984
- It was a Joint Venture between Dempo Group & Glaxo India Ltd
- It used to Contract Manufacture only Nutritional Food products
- In 2013, a pivotal moment occurred when the Vanity Case Group acquired HFL, marking the beginning of a new era for the company
- After this, the company diversified into food & non-food categories like personal care, home care, Food & Beverages, Leather Shoes & Accessories
- So, between 1988 & 2013, it had only a single product, and that too only in one manufacturing facility

VANITY GROUP EFFECT

- As soon as Vanity Group entered, the following events happened
  - The capacity of the Goa Plant doubled
  - Big clients like Marico and Pepsi were added
  - **2017:**
  - Acquired a plant from Reckitt Benckiser (India) Ltd in Jammu
  - Onboarded Ponds Exports Ltd (HUL's Company) in Puducherry

- The capacity of the Goa Plant doubled
- Big clients like Marico and Pepsi were added
- **2017:**
- Acquired a plant from Reckitt Benckiser (India) Ltd in Jammu
- Onboarded Ponds Exports Ltd (HUL's Company) in Puducherry
- New Brands like U.S Polo, Hush Puppies, and Arrow were onboarded in clientele
- **2018:**
- Acquired a factory from Vanity Group for Detergent Manufacturing (HUL's Project) in Hyderabad
- Factory in Coimbatore, TN, for Tea & Coffee brands of HUL
- Agreement for Mortien Brand Manufacturing (7 Years)
- **2019:**
- Brownfield project of liquid detergent at Hyderabad Plant
- Acquired Shoe manufacturing company in Mumbai
- Acquired more than 40% stake in ATC Beverages Private Ltd., Mysuru, engaged in the business of manufacturing and distribution of soft drinks, juices, energy drinks, and other beverages
- **2020:**
- Commenced Liquid Detergent manufacturing at Hyderabad

- Commenced merger of Malted Beverages packing unit in Coimbatore for GSKCH (now HUL) and ATC Beverages Private Ltd. into HFL
- **2021:**
- Built a plant to manufacture a Disinfectant Toilet Cleaner in Silvassa for Reckitt Benckiser
- Plant in Silvassa to manufacture Surface Cleaner
- Manufacturing Bath Soaps and Detergent Bars in Hyderabad
- Merger of Malt Beverages making plant in Coimbatore for Hindustan Unilever
- **2022:**
- Strengthened beauty & personal care vertical by acquiring a 100% stake in Aero Care Personal Products LLP
- Acquired Color Cosmetics plant
- Acquired 100% stake in Reckitt Benckiser Scholl India
- Commenced production of ice creams in UP
- **2023:**
- Started mfg. sports & knitted shoes in Tamil Nadu facility
- **2024:**
- Factory set up in Guwahati, Assam for the manufacture of juices
- Company's acquisition of the Baddi factory – Foray in Pharma

    - Upgradation capex in the beverage facility in Mysuru for the new MNC customer
    - Plans to invest up to Rs. 100 Crores to set up, acquire, and invest in area of sports shoe manufacturing. As a part of this capex, the Company has executed a share purchase agreement to acquire 100% share capital of KNS Shoetech Pvt. Ltd.
    - The scope of work for the new ice cream factory being set up in Kundli, Haryana has increased. This will result in an overall capex of ~Rs. 150 crores as against an earlier estimate of Rs. 100 crores. The company expects to commence production by Q3FY25
    - Investment of Rs. 50 crores, planned at Hyderabad plant for expansion
    - The Board has approved to invest up to Rs. 40 crores in the color cosmetics plant located at Silvassa
- We can see that the management has taken recurrent actions to Acquire/Start/Upgrade the facilities.
- Diversification across various segments has been done in the past few years, which is a good step to avoid Industry concentration risk.
- Vanity Group’s involvement has resulted in the multifold growth of the company.
- The objective behind putting this list of all the expansions and upgradations is to give the glimpse that how aggressively company is growing.

WHY DO BRANDS GO FOR CONTRACT MANUFACTURING INSTEAD OF STARTING THEIR OWN FACILITY?

- New Plant is Capital-Intensive in nature
- Regulatory approval is a hassle
- Fixed costs go up for that Brand
- Companies can focus on core business i.e., distribution, branding, marketing, & stuff like that. More time can be allocated to creating brand awareness if manufacturing partners take up manufacturing.
- A new company can leverage expertise in manufacturing of an experienced player like HFL
- The time gap between Idea and Actual production can be reduced, or we can say that the turnaround time for newer products is reduced

RISKS FOR CONTRACT MANUFACTURER

- Client Concentration
- Low margin biz
- Cost pressures might impact biz
- Cannot afford any negative updates with regard to manufacturing defects at any plant
- Regional competitors are many
- Breach of Contract risk
- The downturn in client's product might hamper a plant's ROE

GROWTH TRIGGERS - COMPANY & INDUSTRY

- New Entrepreneurs are coming up with new ideas & brands but due to a shortage of funds, they outsource manufacturing
- Contract Manufacturing is a CYCLE when we talk about onboarding new clients:
    - The better the execution and quality, the more satisfied the client becomes. The more satisfied the client becomes, the more we can attract potential customers by showing a proven track record. The more proven the track record is, the better the chances are converting potential clients. This will again increase the track record of the company's capability and in turn, will attract more customers to partner with the company.
- Customer Stickiness. Long-term partnerships are made.
- The Current phase of Expanding geographies will help the company in a way that now a south Indian project will seem to be feasible as they have some experience of working in that region with other brands
- This will create the ability to create their own product
- Since the company is expanding its product portfolio, the TAM has increased.
- The company has a big competitive advantage in terms of the project execution that it has been doing in various industries for a decade
- Make-in-India will boost the industry & company prospects
- State of art manufacturing facilities with the company.

BUSINESS VALUATION - INVESTMENT THESIS

- The company guided during the Q3FY24 that it will add 800-900 Cr of Gross Block in the coming two years.
- They highlighted that they will reach a gross block amount of 1500 Cr by FY25 & 1800 Cr by FY26 or H1FY27
- Currently, the asset turn guidance as given by the management is between 3-4 times. While forecasting the future revenue, this number has been taken as 3.5 times
- Following is the screenshot taken from the Q3FY24 Transcript, whereby Mr. Sameer Kothari is saying how the revenues and gross block move proportionately. This is to validate the basis of my analysis

Kashyap Javeri: My first question is on the CAPEX on our ice cream facility which is gone up by about 50 crores. Does this commensurately increase output over there also or otherwise why is this about 50 crores increase there?

Sameer Kothari: So Kashyap, just maybe I should take a 30 second gap in explaining to you our business model as far as dedicated size is concerned. So, when it comes to dedicated size, the entire CAPEX is decided in discussions with the customer. Any increase in the CAPEX size is got to do with a scope increase, which means either the customer has asked us to set up some additional facilities or has asked us to increase the capacity of certain lines etc. and that's what is reflecting in this update where we had initially announced that we will be investing around 100 crores CAPEX in this project which has now gone up to 150. It basically means that yes, we are going to probably end up making more ice cream than what we had envisaged, and we'll also probably end up making better ice cream than what we had envisaged. And the better I mean because we're going in for more sophisticated machines than what we had planned earlier. In terms of our bottom lines and our top lines, yes, our asset turn guidance remains the same. So, any increase in our gross block should reflect a commensurate change in our top lines. As far as bottom line is concerned especially for dedicated units since they are ROE based, any kind of increase in the gross block or increase in the CAPEX definitely helps us in earning a little bit more money.

CASE 1 - If Gross Block Target is achieved by FY26

Rs. in Cr.

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25E	2025-26E
REVENUE	772	1407	2040	2598	2755	5255.495	6727.034
GROWTH (%)	57%	82%	45%	27%	6%	91%	28%
OPM (%)	7%	6%	6%	7%	8%	7%	7%
OP PROFITS	54.04	84.42	122.4	181.86	220.4	367.8847	470.8924
PAT MARGINS	3%	3%	2%	3%	3%	3%	3%
PAT	22	37	45	71	93	147	188
GROSS BLOCK	281	319	633	839	1129	1501.57	1922.01
GROWTH (%)		14%	98%	33%	35%	33%	28%

#PAT MARGINS ARE ASSUMED TO BE SAME AS HISTORICAL FIGURES

#ASSET TURNOVER RATIO IS ASSUMED TO BE 3.5 TIMES

#GROWTH IN GROSS BLOCK IS AS PER MANAGEMENT COMMENTARY (Aggressive)

Valuation at the end of FY26

PAT	188
Current Mkt Cap	6,500

If the PE Ratio at that time is:

CASE 1	CASE 2	CASE 3	CASE 4
55	69	75	87

Then, Projected Mkt Cap will be:

CASE 1	CASE 2	CASE 3	CASE 4
10,360	12,997	14,127	16,387

Total Possible Upside

CASE 1	CASE 2	CASE 3	CASE 4	
59%	100%	117%	152%	Abs. Returns
26%	41%	47%	59%	CAGR

#CASE 1 --> Bearish Sentiments

#CASE 2 --> Current PE Multiple sustains

#CASE 3 --> Improved Sentiments

#CASE 4 --> MEDIAN PE Multiple

CASE 2 - If Gross Block Target is achieved by H1FY27

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25E	2025-26E	2026-27E
REVENUE	772	1407	2040	2598	2755	5057.92	6069.504	7890.355
GROWTH (%)	57%	82%	45%	27%	6%	84%	20%	30%
OPM (%)	7%	6%	6%	7%	8%	7%	7%	7%
OP PROFITS	54.04	84.42	122.4	181.86	220.4	354.0544	424.8653	552.3249
PAT MARGINS	3%	3%	2%	3%	3%	3%	3%	3%
PAT	22	37	45	71	93	142	170	221
GROSS BLOCK	281	319	633	839	1129	1445.12	1734.144	2254.387
GROWTH (%)		14%	98%	33%	35%	28%	20%	30%

#PAT MARGINS ARE ASSUMED TO BE SAME AS HISTORICAL FIGURES

#ASSET TURNOVER RATIO IS ASSUMED TO BE 3.5 TIMES

#GROWTH IN GROSS BLOCK IS AS PER MANAGEMENT COMMENTARY (Conservative)

Valuation at the end of FY27

PAT	221
Current Mkt Cap	6,500

If the PE Ratio at that time is:

CASE 1	CASE 2	CASE 3	CASE 4
55	69	75	87

Then, Projected Mkt Cap will be:

CASE 1	CASE 2	CASE 3	CASE 4
12,151	15,244	16,570	19,221

Total Possible Upside

87%	135%	155%	196%	Abs. Returns
23%	33%	37%	44%	CAGR

#CASE 1 --> Bearish Sentiments

#CASE 2 --> Current PE Multiple sustains

#CASE 3 --> Improved Sentiments

#CASE 4 --> MEDIAN PE Multiple

- Subdued FY24 signals for FY25 to be a year with extraordinary growth in the top line and bottom line as it will catch up with the asset turn number of FY24 too.
- Along with gross block, debt levels are also expected to increase.
- If FY25 shows extraordinary growth, the PE exit multiple can be estimated to be on the higher side towards the median PE.
- Other Financial Figures include:
    - 5 Yr Sales growth CAGR is 41%
    - 5 Yr Profit growth CAGR is 51%
    - 5 Yr Stock price CAGR is 47%
    - 5 yr ROE is maintained at 18%