



KWALITY WALL'S™

NOT RATED

Kwality Ltd

Milking profits

Company Report

Last Price (INR)	48
Bloomberg code	KLD IN
Reuters code	KDAI BO
Avg. Vol. (3m)	397,246
Avg. Val.(3m)(INRmn)	16.4
52-wk H/L (INR)	58.0 / 27.6
Sensex	28,885
MCAP (INRbn/USDmn)	10.43 / 168

Shareholding (%)	12/14	1/15
Promoters	74.9	69.6
MFs, Fls, Banks	0.1	0.1
FIIIs	0.5	0.5
Public	24.5	29.9
Others	-	-

Stock Performance



Absolute	13.7	17.9	-1.5
Rel. to Sensex	13.6	12.7	-10.0

	23,946	36,923	45,783
Sales			
YoY (%)	49	54	54
EBITDA (%)	7%	7%	7%
A.PAT	910	965	1,266
Sh o/s (diluted)	203	203	203
A.EPS (INR)	4.5	4.8	6.2
YoY (%)	98	6	6
D/E (x)	3.7	3.7	3.7
P/E (x)	10.6	10.0	7.6
EV/E (x)	9.8	8.6	7.2
RoCE (%)	19%	17%	18%
RoE (%)	51%	35%	32%

Quarterly Trends*	03/14	06/14	09/14	12/14
Sales (INRmn)	13,211	13,275	12,977	12,897
PAT (INRmn)	363	341	366	361

*Standalone

We hosted an investor roadshow for Kwality Ltd. The company has emerged as one of the established processors of dairy products in the private sector. It is undertaking expansion with the doubling of its processing capacity over the next two years. The most critical aspect for the Indian dairy industry is direct sourcing, which Kwality plans to raise from the current 15% to 50% in three years. Similarly, it plans to increase focus on retail sales (18% of sales in FY14), as they fetch better margins. To achieve this, it is working towards brand development and seeking to enhance its product portfolio. The company has had a good run with a strong revenue CAGR of 44% and PAT CAGR of 63% over FY10–FY14. It has strong RoEs upwards of 30%.

An established processor of dairy products in the private sector

Kwality has emerged as one of the established processors of dairy products in the private sector. It has six milk processing units and 24 milk chilling centers across Haryana, Punjab, Rajasthan and UP. The company has a processing capacity of 3mn liters of milk per day. It plans to double capacity to around 6mn liters per day over the next three years with c0.75mn liters per day for value-added products (such as flavored milk), which fetch better margins than years.

Changing procurement, sales mix to improve margins

The biggest challenge for the dairy industry is to manage milk procurement to process and maintain the procurement's consistency. Dairies achieve better consistency when they directly source from farmers compared to those sourcing from aggregators. The company's current sourcing mix is 15% from farmers. It plans to increase this to 25% and eventually aims to take it to 50%. Similarly, on the sales side, Kwality currently has 75% of its sales to clients compared to retail clients that give better margins. It is aiming to change the mix to 50% to retail sales over the next three years.

Focus on brand development, enhancement of product portfolio

Kwality is working towards brand development and is seeking to enhance its product portfolio. Branded products currently account for 37% of the total sales. The company plans to launch flavored milk in the next couple of months. It is also setting up facilities for products such as variants of cheese, drinking yogurt and cream in tetra packs. These value-added products should improve margins, as compared to the commoditized milk sales.

Revenue CAGR of 44%; PAT CAGR of 63% from FY10–FY14

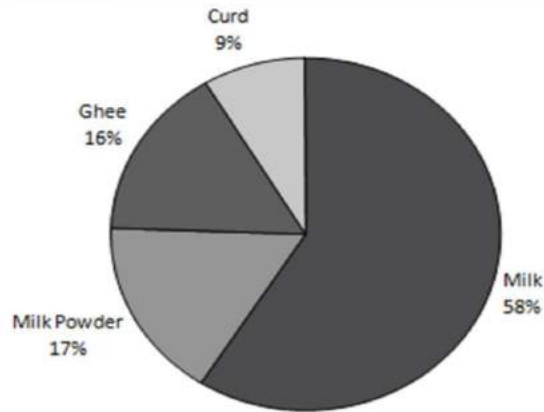
A strong revenue CAGR of 44% and PAT CAGR of 63% over FY10–FY14 translates into a good run for Kwality. It has strong RoEs upwards of 30%, though RoCEs are lower due to leverage. The company has debt equity of 2.5x with debt of INR1bn in FY14. However, free cash flows are a challenge owing to high working capital and capex. The stock is trading at 6.2x FY16f, as per Bloomberg consensus estimates.

Exhibit 1: Product profile of Kwality

Segment	Product
Milk	Full Cream, Skimmed, Pouched
Ghee	Butter, Pure Ghee, Cow Ghee, Low Fat Ghee
Milk Powder	Skimmed Milk, Whole Milk, DairyWhitener
Curd	Set curd, Pouched Curd, <u>Chas</u>

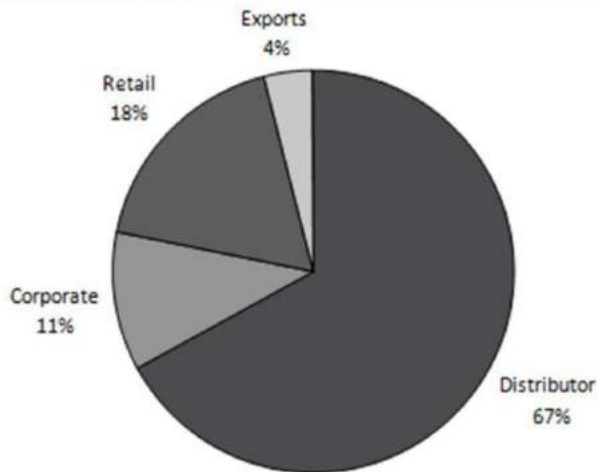
Source: WealthZap Research Services

Exhibit 2: Revenue mix of Kwality



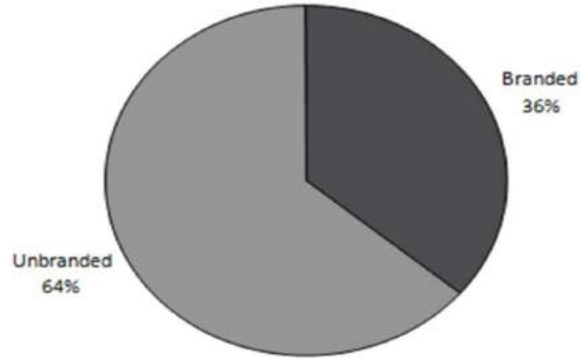
Source: WealthZap Research Services

Exhibit 3: Revenue mix by customer type



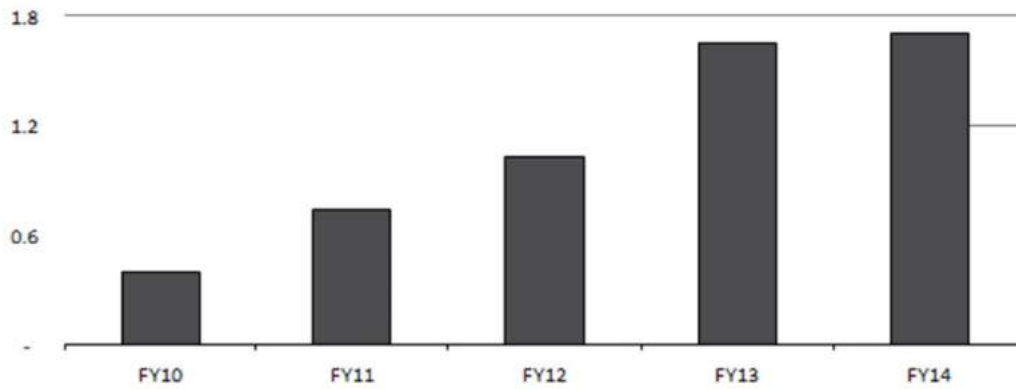
Source: WealthZap Research Services

Exhibit 4: Revenue mix between branded and unbranded products



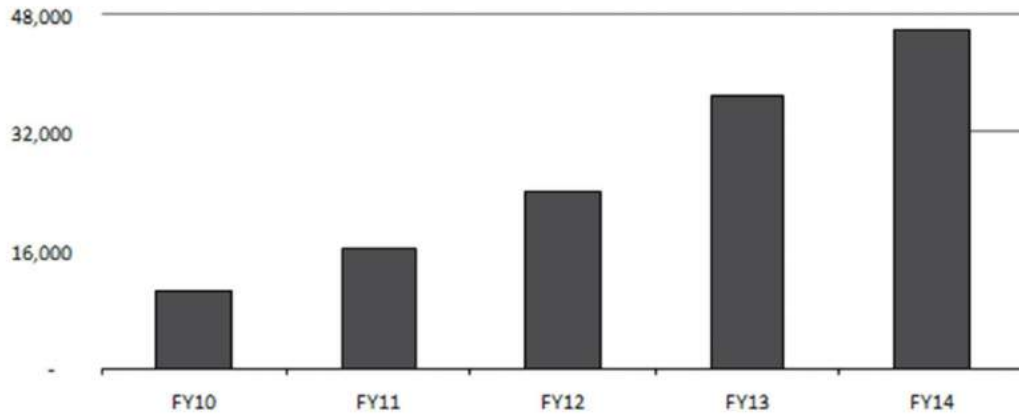
Source: WealthZap Research Services

Exhibit 5: Trend in milk procurement (mn, tonnes)



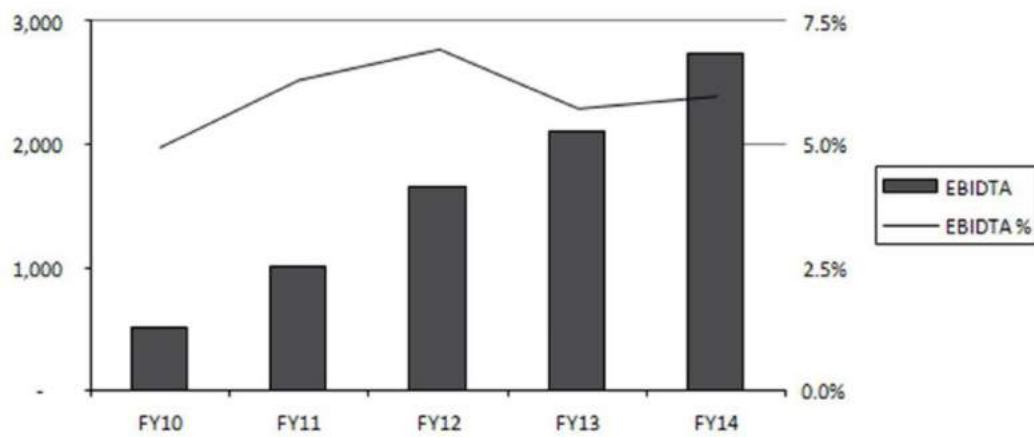
Source: WealthZap Research Services

Exhibit 6: Trend in sales (INR, mn)



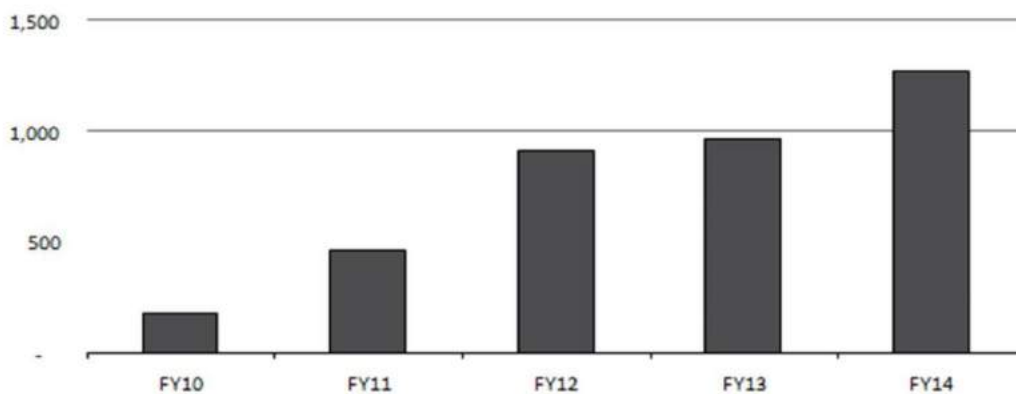
Source: WealthZap Research Services

Exhibit 7: Trend in EBIDTA (INR, mn) and EBIDTA margins (%)



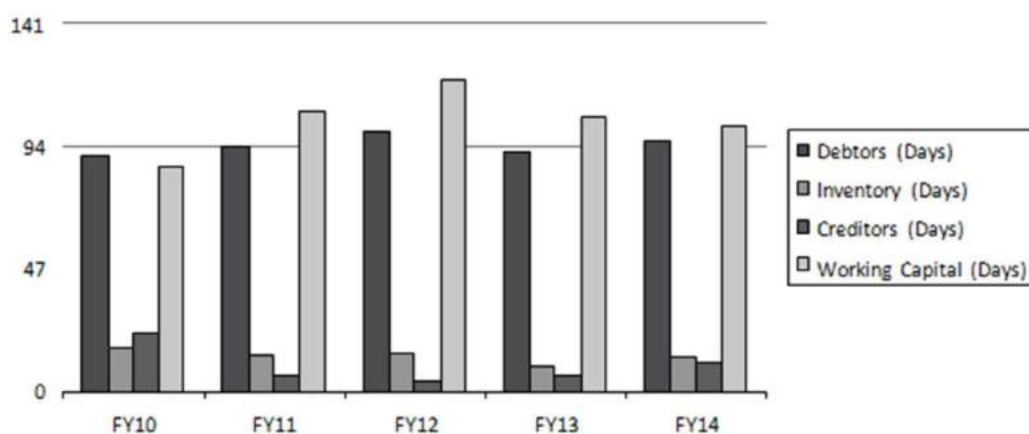
Source: WealthZap Research Services

Exhibit 8: Trend in PAT (INR, mn)



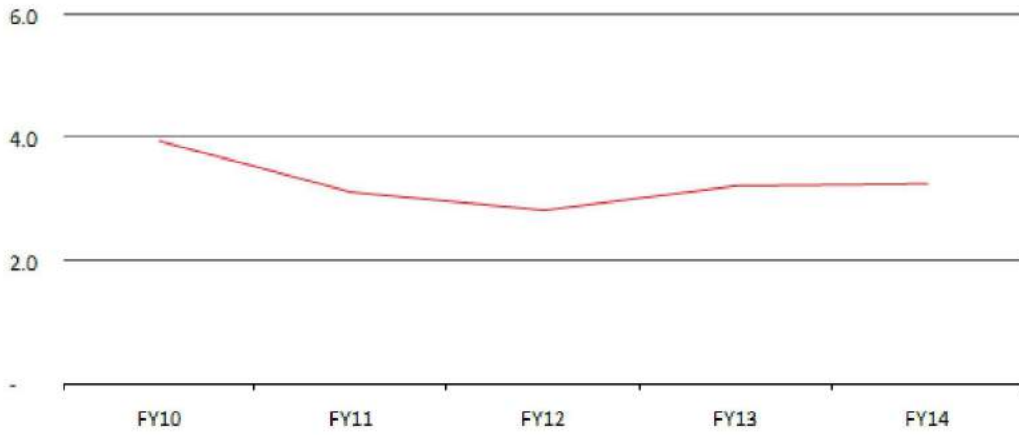
Source: WealthZap Research Services

Exhibit 9: Trend in the working capital cycle



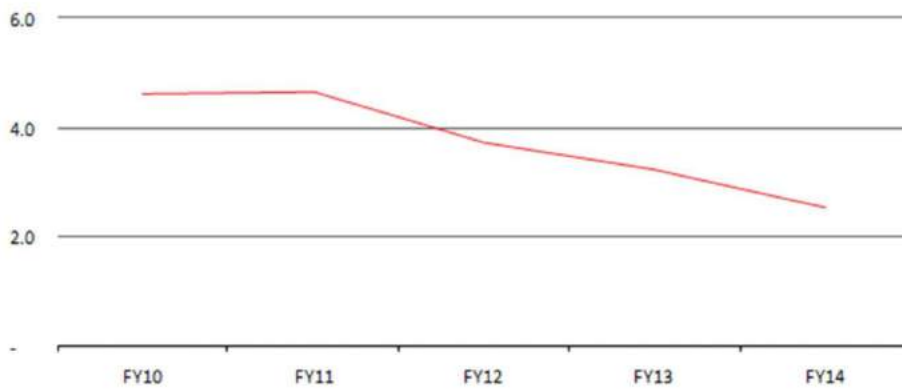
Source: WealthZap Research Services

Exhibit 10: Trend in asset turn



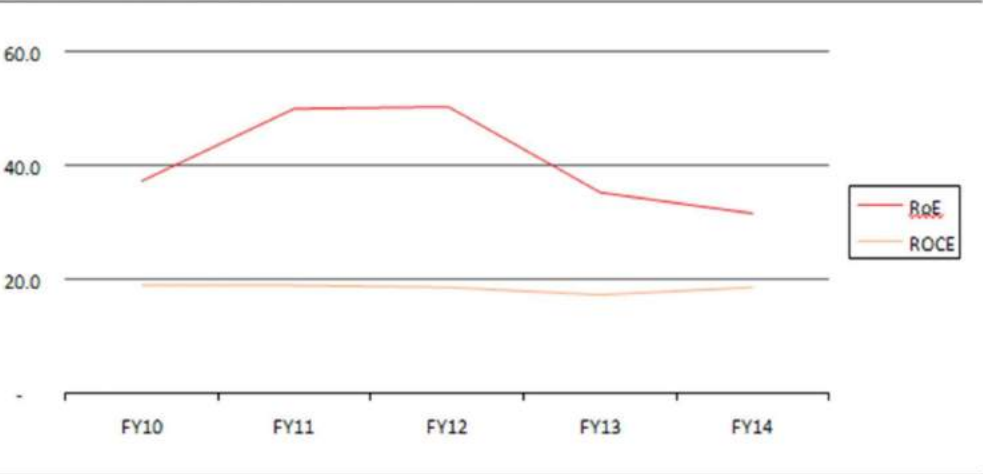
Source: WealthZap Research Services

Exhibit 11: Trend in debt/equity ratio



Source: WealthZap Research Services

Exhibit 12: Trend in return ratios



Source: WealthZap Research Services

Exhibit 13: Income statement

INRmn	FY10	FY11	FY12	FY13	FY14
Net sales	10,540.9	16,080.4	23,946.3	36,922.9	45,780.5
Expenditure	-	-	-	-	-
Material costs	9,787.9	14,594.2	21,671.7	33,736.0	41,799.5
Employee cost	21.1	39.1	85.6	134.8	179.5
Others	210.6	437.0	536.3	942.8	1,069.3
EBITDA	521.3	1,010.1	1,652.7	2,109.3	2,732.2
% of net sales	4.9%	6.3%	6.9%	5.7%	6.0%
Depreciation	18.3	35.3	75.0	102.9	129.1
EBIT	503.0	974.8	1,577.7	2,006.4	2,603.1
Interest & finance charges	206.8	371.2	651.9	928.9	1,137.4
Other income	1.3	2.1	0.9	7.2	39.5
Profit before tax	297.5	605.7	926.7	1,084.7	1,505.2
Tax	118.0	146.3	16.8	119.4	238.8
Profit after tax	179.5	459.4	909.9	965.3	1,266.4
EPS INR	0.9	2.3	4.5	4.8	6.2

Source: WealthZap Research Services

Exhibit 14: Balance sheet

INRmn	FY10	FY11	FY12	FY13	FY14
Liabilities					
Share capital	182.0	203.2	203.2	203.2	203.2
Reserves	292.8	707.3	1,593.5	2,535.2	3,777.7
Net worth	474.8	910.5	1,796.7	2,738.4	3,980.9
Deferred tax	5.6	8.5	4.7	(11.6)	(7.9)
Loans	2,189.0	4,245.1	6,665.8	8,807.1	10,123.3
Long-term	1,682.6	3,425.7	5,518.1	7,579.9	8,998.8
Short-term	506.4	819.4	1,147.7	1,227.2	1,124.5
Capital employed	2,669.4	5,164.1	8,467.2	11,533.9	14,096.3
Assets					
Gross fixed assets	322.0	597.4	891.4	1,083.1	1,473.8
Less: Depreciation	143.5	178.3	251.3	353.8	482.6
Net fixed assets	178.5	419.1	640.1	729.3	991.2
Capital WIP	3.9	-	0.9	86.1	220.0
Investments	-	-	14.3	56.5	62.7
Current assets	3,237.2	5,169.8	8,221.6	11,495.5	14,534.5
Inventory	485.7	634.2	987.4	986.6	1,674.8
Sundry debtors	2,618.0	4,146.1	6,562.4	9,309.0	11,999.9
Cash & bank balances	21.8	15.0	89.0	306.0	127.2
Loans & advances	111.7	369.8	385.9	583.9	323.9
Others	-	4.7	196.9	310.0	408.7
Current liabilities	750.2	424.8	409.7	833.5	1,712.1
Sundry creditors	615.3	258.6	255.1	583.0	1,361.6
Other liabilities	-	3.4	3.1	5.6	7.5
Provisions	134.9	162.8	151.5	244.9	343.0
Net current assets	2,487.0	4,745.0	7,811.9	10,662.0	12,822.4
Capital employed	2,669.4	5,164.1	8,467.2	11,533.9	14,096.3

Source: WealthZap Research Services

Exhibit 15: Cash flow statement

INRmn	FY10	FY11	FY12	FY13	FY14
OP/(Loss) before tax	503	975	1,578	2,006	2,603
Interest/Dividends received	1	2	1	7	40
Depreciation & amortization	18	35	75	103	129
Direct taxes paid	-118	-146	-17	-119	-239
(Inc)/Dec in working capital	-2,465	-2,265	-2,993	-2,633	-2,339
CF from oper. activity	-2,061	-1,399	-1,356	-636	194
Other items	321	-22	-7	-20	0
CF after other items	-1,739	-1,421	-1,363	-656	194
(Inc)/Dec in FA+CWIP	-201	-272	-297	-277	-525
(Pur)/Sale of invest.	0	0	-14	-42	-6
CF from inv. activity	-201	-272	-311	-320	-531
Change in equity	0	21	0	0	0
Inc/(Dec) in debt	2,189	2,056	2,421	2,141	1,316
Interest paid	-207	-371	-652	-929	-1,137
Dividends paid	-20	-20	-20	-20	-20
CF from fin. activity	1,962	1,686	1,749	1,192	158
Inc/(Dec) in cash	22	-7	74	217	-179
Add: Beginning balance	0	22	15	89	306
Closing balance	22	15	89	306	127

Source: WealthZap Research Services

Exhibit 16: Key ratios

	FY10	FY11	FY12	FY13	FY14
EPS	1.0	2.3	4.5	4.8	6.2
Cash EPS	1.1	2.4	4.8	5.3	6.9
Book value per share	2.6	4.5	8.8	13.5	19.6
DPS	0.1	0.1	0.1	0.1	0.1
P/E	48.2	21.0	10.6	10.0	7.6
EV/EBITDA	22.7	13.8	9.8	8.6	7.2
Price to book value	18.2	10.6	5.4	3.5	2.4
Dividend yield (%)	0.2	0.2	0.2	0.2	0.2
RoE	37%	50%	51%	35%	32%
RoCE	19%	19%	19%	17%	18%
Debtors (Days)	91	94	100	92	96
Inventory (Days)	23	6	4	6	12
Creditors (Days)	86	108	119	105	102
Asset turnover (x)	3.9	3.1	2.8	3.2	3.2
Debt/Equity (x)	4.6	4.7	3.7	3.2	2.5

Source: WealthZap Research Services

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