



5 MINUTE STOCK IDEA

BY SMART SYNC INVESTMENT ADVISORY SERVICES

VARUN BEVERAGES LTD

WHAT WE LIKE

STRONG MARKET REACH & PRESENCE

- Covers 1/6th of World Population
- Presence in 6 countries (India, Sri Lanka, Nepal, Morocco, Zambia & Zimbabwe) & 27 Indian States (accounts for 85% of PepsiCo India sales)
- ~2 Million retail outlets, 37 Manufacturing Units
- 90+ depots, 1500+ primary distributors
- Operates brands across various segments:



SYMBIOTIC RELATIONSHIP WITH PEPSICO

| VBL – Demand Delivery | 29 yrs + Association | PepsiCo – Demand Creation |
|---|----------------------|---|
| <ul style="list-style-type: none"> • Production Facilities • Sales & Distribution – GTM & Logistics • In-outlet Management – Visi-Coolers • Consumer Push Management (BTL) - Market Share Gains | | <ul style="list-style-type: none"> • Trademarks • Formulation through Concentrate • Product & Packaging innovation through investment in R&D • Consumer Pull Management (ATL) - Brand Development |

LEADING BRANDS IN OTHER SEGMENTS

VBL operates Tropicana which is one of the top 3 juice brands in India. With the continued focus on health consciousness, there is a lot of scope for market expansion and capture for VBL here. It also operates Gatorade, a sports drink industry leader, which is expected to grow fast with the rise of sports/fitness awareness in India.

GREEN INITIATIVES

VBL has engaged with GEM Enviro Management Pvt Ltd for phased implementation of 100% recycling of used PET bottles. During the year CY20, 43,700+ MT of PET waste was recycled (66% of total PET resin used) and during Q1 CY2021, 17,900+ MT of PET waste was recycled.

WHAT WE DON'T LIKE

CONTINUOUS CAPEX REQUIREMENT PUTS STRAIN ON BALANCE SHEET

Due to aggressive expansion both organic and inorganic, the company is in constant need of funds for Capex. Operations have been producing cash over Rs 1000 Cr/year for last 3 CY. But that is not enough for company's Capex requirements. That's why even after raising 1100 CR in IPO in 2016, the company had to go for a QIP of 900 Cr in 2019. And debt of 3216 Cr in CY2020 end is on a higher side. Although VBL is making efforts to reduce debt, any dip in demand can further deteriorate the Balance Sheet quality.

RISK FROM REGULATORY CHANGES

Government regulations is always an overhang on the beverage industry. The two major concerns being the content of soft drinks, and increasing environmental concerns in India about ground water depletion and discharge of effluents by bottling plants. Another concern is related to disposal of plastic. VBL at present has tied up for recycling of 66% of its PET bottles and is expected to increase this to 100% over the medium term.

IMPACT OF COVID-19

The soft drinks industry was hit hard from COVID-19 with the shutdown of on-the-go consumption. This forced the companies to pivot and promote large packs for home consumption. Although VBL has seen a big rise in home consumption, the rise has not been able to cover for the decline from on-the-go which will stay down till public spaces with the most outside consumption like cinemas and restaurants remain closed.

HIGH COMPETITION IN NEW SEGMENTS

VBL faces tough competition in its brands Creambell (from Amul) and Sting (from Red Bull & Monster). In the case of both brands, rivals are long entrenched and so capturing market share will be very difficult. Although Sting is priced almost 5 times lower than both rival brands, it has to reinvent the consumer perception reinforced for decades by Red Bull & Monster.

VALUATION

We at SSS, believe that the valuation in May 2021 is overheated. At 71 times trailing earnings, the price factors in a lot of growth in earnings going ahead. The valuation multiples may contract if earnings growth don't match expectations. So, at this price, there is almost no margin of safety.

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