



VISIT NOTE

# CCL PRODUCTS INDIA

## Volume growth vital

India Equity Research | Miscellaneous



We recently met Mr. C. Srishant, Managing Director of CCL Products (CCL), to get an update on the company and the industry. CCL is expecting 10–20% volume-led growth in FY19; however, falling green coffee prices (down ~15% YoY) are likely to affect revenue. With stable conversion margins and an improved product mix, EBITDA/PAT growth would outpace top-line growth. Management is also excited about its foray into retailing its own brand (FY19E sales of INR1bn) which offers a strong growth opportunity over next 3–4 years along with the potential improvement in the product mix and a strong customer connect. We revisit our estimates and model in lower volume growth of ~10% for FY19 and 18% for FY20 amid delays in commissioning the freeze dry capacity. Hence, cutting estimates for FY19 by 16% and FY20 by 12%. With an FY18–20E earnings CAGR of 20% and ROCE of 28%, as well as the expectation of strong cash flows, we maintain BUY while revising down the target price to INR384 from INR437.

### Business on track

In Vietnam, CCL commenced the supply of agglomerated coffee in Q4FY18, which will support its growth in FY19. The company maintained its top-line and bottom-line guidance of 10–20% growth. In India, its new freeze dried capacity is likely to be commissioned in September 2018, which is expected to drive growth going forward. Superior operating leverage at the Vietnam facility and an improving product mix in India as well as Vietnam will spur overall EBITDA margin in our view.

### Commissioning of freeze dried capacity to drive growth from FY19

CCL's India capacity is running at an optimum utilisation rate while future growth hinges on the value-add mix and commissioning of the freeze dried capacity scheduled for September 2018. Utilization of the Vietnam capacity is currently ~70%, which management estimates would surpass 80% in FY19 and drive growth at subsidiaries.

### Outlook and valuations: Well poised for growth; maintain 'BUY'

We believe a resilient business model, rising utilisation with a sustained market share gain, focus on branded business and capacity expansion in the value-added segment put CCL in a sweet spot to post sales/PAT CAGR of 18%/28% over FY18–20E. We maintain 'BUY' with a target price of INR437 based on 24x FY20E EPS.

#### Financials

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Net revenue	9,765	11,380	11,843	14,392
EBITDA	2,323	2,389	2,693	3,260
Adjusted Profit	1,346	1,481	1,702	2,127
Adjusted diluted EPS (INR)	10.1	11.1	12.8	16.0
Diluted P/E (x)	28.1	25.5	22.2	17.8
EV/EBITDA (x)	16.5	16.8	14.4	11.7
ROAE (%)	23.6	21.7	21.5	23.1

#### EDELWEISS RATINGS

Absolute Rating	BUY
Investment Characteristics	Growth

#### MARKET DATA (R: CCLP.BO, B: CCLP IN)

CMP	: INR 284
Target Price	: INR 384
52-week range (INR)	: 355 / 253
Share in issue (mn)	: 133.0
M cap (INR bn/USD mn)	: 38 / 560
Avg. Daily Vol. BSE/NSE ('000)	: 100.6

#### SHARE HOLDING PATTERN (%)

	Current	Q3FY18	Q2FY18
Promoters *	45.0	45.0	45.0
MF's, FI's & BKs	3.7	3.7	4.2
FII's	25.3	25.3	24.5
Others	26.0	26.0	26.3
* Promoters pledged shares (% of share in issue)	:		NIL

#### PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	(2.1)	(5.6)	(3.5)
3 months	0.1	(1.4)	(1.6)
12 months	7.6	(1.8)	(9.4)

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### **Key highlights of our meeting**

#### **India plant operating at full utilization; ramp-up in Vietnam facility to drive volume growth**

The company's India plant (capacity of 20,000mt of spray dry including 3,000mt of agglomerated coffee) is operating at almost full utilisation with limited scope for volume growth. However, the expected increase in capacity utilisation at its Vietnam facility (capacity of 10,000mt including 4,000mt of agglomerated coffee) from 70% in FY18 to 90% in FY19 will drive volume growth in FY19.

#### **Revenue contribution from new freeze dried capacity may spill over to FY20**

CCL expects its new freeze dried capacity of 5,000mt in India to be commissioned by September this year. However, customer approval from the new facility generally takes 3–6 months, which may hinder revenue generation. Out of the planned INR3bn capex, the company has already spent INR2.4bn on this facility alone. The facility might contribute for a quarter (i.e. Q4FY19); however, we are not factoring in a significant revenue contribution from this new facility in FY19 either.

#### **Fall in green coffee prices by ~15% would affect revenue growth while...**

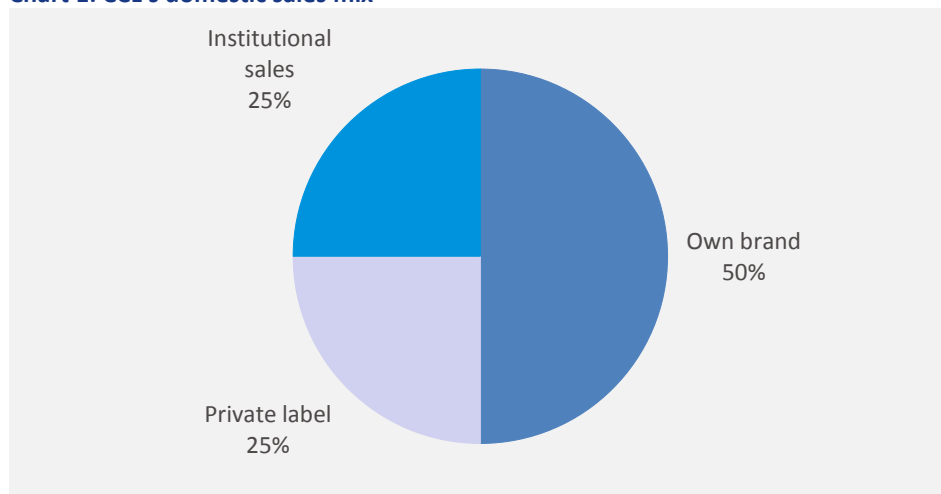
Green coffee prices have corrected from an average of USD2/kg previous year to US\$1.7/ kg in current year and according to management, the prices are expected to hover in a range of USD1.6–1.7/kg. The fall in prices (~15% in average realization) would erode revenue.

#### **...back-to-back agreements insulate against fluctuating global coffee prices**

CCL's back-to-back pacts for final products and raw materials insulate it from fluctuating global coffee prices. The company operates on a fixed margin basis and thus eliminates the risk of volatility in coffee prices. In India, it imports green coffee beans from Vietnam, Indonesia, and African countries, as well as procures them from the domestic market. This strategy has turned in a consistent EBITDA margin over the years despite volatility in coffee prices.

#### **Targeting INR1bn revenue from domestic branded in FY19**

In FY18, the domestic business generated revenue of INR460mn, falling short of INR800mn guidance. The miss was mainly on account of strategy adopted by the new chief executive officer (CEO) of M/s. Continental Coffee Private Limited, Mr. Praveen Jaipurkar. However management is confident about achieving revenue of INR1bn in FY19 from branded sales. It includes ~50% under its own brand which generates high margins, 25% from private label like railways and the balance 25% from institutional sales to customers such as Reliance. The retail business is likely to generate a high margin of ~30%, but not in its initial years of operations due to focus on branding and advertising.

**Chart 1: CCL's domestic sales mix**

Source: Company, Edelweiss research

#### **Switzerland breaks even**

Revenue from this plant stood at INR770mn, thereby already breaking even. A local has been appointed to look into the prospects of selling coffee in Switzerland with focus on adding new customers. The company is also getting orders from a couple of companies that are reducing manufacturing and increasing outsourcing. However, as the EU duty issues still persist, this plant is just 10–20% utilised.

#### **Additional capex of INR500–600mn for capacity expansion in Vietnam**

To achieve sustained growth, management plans to invest INR500–600mn to raise its capacity in Vietnam from 10,000mt to 13,500mt. This will drive volume growth in FY20–21.

#### **Margins in freeze dry may come under pressure while spray dry may see margin expansion**

In light of the significant capacity addition globally, management is expecting margins in freeze dry to come down from ~30% to 20–24%. Tata Coffee and a few other global players are building up freeze dry capacity. However, management expects margins on spray dry to inch up from ~12% at present to 15–16% by FYXX amid sustained demand growth.

## Miscellaneous

### Change in Estimates

	FY19E			FY20E			Comments
	New	Old	% change	New	Old	% change	
Net Revenue	11,843	14,040	(15.6)	14,392	15,902	(9.5)	Due to fall in raw material prices
EBITDA	2,693	3,248	(17.1)	3,260	3,718	(12.3)	Due to fall in raw material prices and lower volume growth
<i>EBITDA Margin</i>	22.7	23.1		22.6	23.4		
Adjusted Profit After Tax	1,702	2,017	(15.6)	2,127	2,422	(12.2)	Due to lower operating profit
<i>Net Profit Margin</i>	14.4	14.4		14.8	15.2		
Capex	736	736	0.0	500	500	0.0	

## Company Description

CCL was formed set up in 1994 and commenced commercial operations in 1995. It is a profit making, export oriented unit (EoU) with the ability to import green coffee into India from any part of the world and export the same to any part of the world, free of all duties.

The company is in a position to offer a range of in-house products to customers. Its state-of-the-art soluble instant coffee manufacturing plant is located at Duggirala Mandal, Guntur District, Andhra Pradesh, with current combined capacity of 20000MT/PA. CCL has adapted Brazilian technology, purchased from world renowned pioneers in turnkey instant/soluble coffee technology at its plant. This adaptation of technology has enabled CCL to produce international quality soluble coffee. To cater to specific markets, the company has expanded capacity in Switzerland and Vietnam during FY11 and FY14, respectively.

CCL's 3,000MT plant in Switzerland is facing issues on account of unfavorable European Union regulations. This has so far acted as a roadblock for growth and profitability of Swiss operations. Management is exploring options to turn the plant profitable. In FY18, the Swiss operations did break-even. The company has invested ~INR0.50bn and there is no debt in the Swiss operation.

## Investment Theme

CCL Products (CCL) is India's largest manufacturer and exporter of instant coffee. The company's cost-efficient business model, rich experience and long-standing relationships with customers give it an edge over competitors. Coffee processing is a challenging business wherein getting the perfect blend is crucial, which the company has successfully mastered. The newly commissioned green field Vietnam facility with proximity to raw material and customers as well as tax benefits is expected to propel growth and lead to significant cost savings. Moreover, the company's recent entry in the domestic branded coffee segment via Continental is bound to aid margin expansion. Resilient business model, capacity addition in India and Vietnam and sharpening brand focus in India place CCL in a sweet spot to post sales and PAT CAGR of 12% and 20% over FY18-20E, respectively. We estimate RoCE to improve from 23.6% in FY18 to 27.6% in FY20E.

## Key Risks

Sharp currency movement. However, it imports ~75% of raw material, which provides natural hedge.

Change in duty structure: Unfavourable change in duty rates in any country could impact the competitiveness of supply from Vietnam/India.

Swiss plant duty issue: CCL's Swiss plant is operating at sub-optimal utilisation level because of non-competitive pricing of supplies from Switzerland to the EU. Import duty levied by the EU on Swiss coffee is 9.0%, whereas only 3.3% is charged on coffee supplies from India. However, CCL has taken steps to avoid the adverse duty impact.

Ramp up of Continental brand: FY14 was the first year of Continental brand and adverse customer response could impact the growth prospects as well as financials.

## Financial Statements

## Key Assumptions

Year to March	FY17	FY18	FY19E	FY20E
<b>Macro</b>				
GDP(Y-o-Y %)	6.6	6.5	7.1	7.6
Inflation (Avg)	4.5	3.8	4.5	5.0
Repo rate (exit rate)	6.3	6.0	6.0	6.5
USD/INR (Avg)	67.1	64.5	66.0	66.0
<b>Company</b>				
Raw Material (% net rev)	56.5	60.7	60.0	59.7
India capacity (MT)	20,000	20,000	25,000	25,000
Vietnam capacity (MT)	10,000	10,000	10,000	13,500
India's cap. Util. (%)	77.0	87.0	70.0	82.0
Vietnam's cap. util. (%)	60.0	70.0	90.0	80.0
Std sales (INR mn)	7,141	8,247	7,050	8,258
Subs. sales (INR mn)	2,472	2,882	4,504	5,773
Std realis. (INR/Kg)	464	474	403	403
Subs. realis. (INR/Kg)	437	448	500	535
Std. EBITDA margin (%)	23.7	20.0	17.9	17.5
Subs. EBITDA margin (%)	24.0	23.7	25.4	25.2
Other exp (% net rev)	15.6	14.2	12.7	13.4
Int (% of avg G.debt)	7.2	3.8	3.7	5.0
Net borrowings (INR mn)	474	2,273	1,033	181
Employee cost (% of rev)	4.1	4.2	4.6	4.3
Tax rate as % of PBT	28.8	26.6	25.0	25.0
Debtor days	54	55	53	46
Inventory days	110	97	100	96
Payable days	8	6	10	14
Cash conversion cycle	156	146	142	128
Capex (INR mn)	(183)	(2,382)	(736)	(500)
Dep. (% gross block)	5.1	4.5	4.0	4.2

## Income statement

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Net revenue	9,765	11,380	11,843	14,392
Materials costs	5,519	6,906	7,101	8,585
Gross profit	4,246	4,474	4,742	5,806
Employee costs	401	475	542	624
Other Expenses	1,521	1,610	1,507	1,923
Operating expenses	1,923	2,085	2,049	2,547
Total operating expenses	7,442	8,991	9,150	11,132
EBITDA	2,323	2,389	2,693	3,260
Depreciation	333	341	383	423
EBIT	1,990	2,048	2,310	2,836
Less: Interest Expense	112	78	91	65
Add: Other income	12.28	48.49	50.00	65.00
Profit Before Tax	1,891	2,018	2,269	2,836
Less: Provision for Tax	545	537	567	709
Reported Profit	1,346	1,481	1,702	2,127
Adjusted Profit	1,346	1,481	1,702	2,127
Shares o /s (mn)	133	133	133	133
Adjusted Basic EPS	10.1	11.1	12.8	16.0
Diluted shares o/s (mn)	133	133	133	133
Adjusted Diluted EPS	10.1	11.1	12.8	16.0
Adjusted Cash EPS	12.8	13.8	15.7	19.2
Dividend per share (DPS)	2.5	3.0	4.0	4.0
Dividend Payout Ratio(%)	29.7	32.4	37.6	30.1

## Common size metrics

Year to March	FY17	FY18	FY19E	FY20E
Gross margin	43.5	39.3	40.0	40.3
Operating expenses	19.7	18.3	17.3	17.7
EBITDA margins	23.8	21.0	22.7	22.6
EBIT margins	20.4	18.0	19.5	19.7
Interest Expense	1.1	0.7	0.8	0.5
Net Profit margins	13.8	13.0	14.4	14.8

## Growth ratios (%)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	4.8	16.5	4.1	21.5
EBITDA	13.5	2.8	12.7	21.0
PBT	13.4	6.7	12.4	25.0
Adjusted Profit	10.2	10.1	14.9	25.0
EPS	10.2	10.0	14.9	25.0

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18	FY19E	FY20E	
Share capital	266	266	266	266	
Reserves & Surplus	6,017	7,133	8,194	9,679	
Shareholders' funds	6,283	7,399	8,460	9,945	
Long term borrowings	26	1,817	-	-	
Short term borrowings	985	1,266	1,817	817	
Total Borrowings	1,010	3,084	1,817	817	
Long Term Liabilities	-	(1)	-	-	
Def. Tax Liability (net)	382	392	392	392	
<b>Sources of funds</b>	<b>7,676</b>	<b>10,874</b>	<b>10,669</b>	<b>11,155</b>	
Gross Block	6,457	6,577	9,577	10,077	
Net Block	3,932	3,711	6,328	6,405	
Capital work in progress	2	2,264	-	-	
Intangible Assets	1	-	-	-	
Total Fixed Assets	3,934	5,975	6,328	6,405	
Non current investments	15	15	15	15	
Cash and Equivalents	536	811	784	637	
Inventories	1,828	1,832	2,043	2,470	
Sundry Debtors	1,627	1,820	1,622	1,971	
Loans & Advances	27	34	37	41	
Other Current Assets	515	849	849	849	
Current Assets (ex cash)	3,996	4,535	4,551	5,331	
Trade payable	122	103	292	353	
Other Current Liab	684	358	718	880	
Total Current Liab	806	461	1,009	1,233	
Net Curr Assets-ex cash	3,190	4,074	3,542	4,098	
<b>Uses of funds</b>	<b>7,676</b>	<b>10,874</b>	<b>10,669</b>	<b>11,155</b>	
BVPS (INR)	47.2	55.6	63.6	74.8	

Free cash flow		(INR mn)			
Year to March	FY17	FY18	FY19E	FY20E	
Reported Profit	1,346	1,481	1,702	2,127	
Add: Depreciation	333	341	383	423	
Interest (Net of Tax)	75	52	61	44	
Others	(29)	(52)	(61)	(44)	
Less: Changes in WC	674	883	(532)	556	
Operating cash flow	1,050	939	2,617	1,994	
Less: Capex	183	2,382	736	500	
<b>Free Cash Flow</b>	<b>868</b>	<b>(1,443)</b>	<b>1,881</b>	<b>1,494</b>	

Cash flow metrics		FY17	FY18	FY19E	FY20E
Year to March					
Operating cash flow		1,050	939	2,617	1,994
Financing cash flow		(874)	2,269	(1,908)	(2,641)
Investing cash flow		(197)	(2,382)	(736)	(500)
Net cash Flow		(21)	826	(27)	(1,147)
Capex		(183)	(2,382)	(736)	(500)
Dividend paid		(133)	(400)	(533)	(533)

Profitability and efficiency ratios		FY17	FY18	FY19E	FY20E
Year to March					
ROACE (%)		27.6	23.6	22.7	27.6
ROAE (%)		23.6	21.7	21.5	23.1
Inventory Days		110	97	100	96
ROA		17.8	16.0	15.8	19.5
Debtors Days		54	55	53	46
Payable Days		8	6	10	14
Cash Conversion Cycle		156	146	142	128
Current Ratio		5.6	11.6	5.3	4.8
Gross Debt/EBITDA		0.4	1.3	0.7	0.3
Gross Debt/Equity		0.2	0.4	0.2	0.1
Adjusted Debt/Equity		0.2	0.4	0.2	0.1
Interest Coverage Ratio		17.8	26.2	25.4	43.4
LT debt /Cap empl. (%)		13.2	28.4	17.0	7.3
Debt / Cap employed (%)		28.6	36.2	30.2	21.9

Operating ratios		FY17	FY18	FY19E	FY20E
Year to March					
Total Asset Turnover		1.3	1.2	1.1	1.3
Fixed Asset Turnover		2.4	3.0	2.4	2.3
Equity Turnover		1.7	1.7	1.5	1.6

Valuation parameters		FY17	FY18	FY19E	FY20E
Year to March					
Adj. Diluted EPS (INR)		10.1	11.1	12.8	16.0
Y-o-Y growth (%)		10.2	10.0	14.9	25.0
Adjusted Cash EPS (INR)		12.8	13.8	15.7	19.2
Diluted P/E (x)		28.1	25.5	22.2	17.8
P/B (x)		6.0	5.1	4.5	3.8
EV / Sales (x)		3.9	3.5	3.3	2.6
EV / EBITDA (x)		16.5	16.8	14.4	11.7
Dividend Yield (%)		0.9	1.1	1.4	1.4

### Peer comparison valuation

Name	Market cap (USD mn)	Core EV/EBITDA (X)		Diluted P/E (X)		ROAE (%)	
		FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
CCL Products India	560	-	-	22.2	17.8	21.5	23.1
AIA Engineering	2,163	-	-	28.5	24.3	15.7	16.3
Allcargo Logistics Ltd	412	6.3	5.5	10.9	9.0	11.0	12.3
Apar Industries Ltd	404	-	-	13.5	10.9	17.2	18.7
Opto Circuits India Ltd	45	-	-	-	-	-	-
Sintex Industries Ltd	149	11.6	8.4	3.6	2.3	6.1	8.5
Median	-	-	-	12.2	10.0	13.4	14.3
AVERAGE	-	3.0	2.3	13.1	10.7	11.9	13.1

Source: Edelweiss research



## Additional Data

### Directors Data

Challa Rajendra Prasad	Chairman	Challa Srishant	Managing Director
I J Rao	Director	K Chandrahas	Director
Vipin K Singhal	Director	K K Sarma	Director
B Mohan Krishna	Director	J. Rambabu IAS	Director
G.V. Krishna Rau	Director	Ms. Shantha Prasad Challa	Director
Ms. Kulsoom Noor Saifullah	Director	Dr. Lanka Krishnanand	Director

Auditors - M.Anandam

*\*as per last available data*

### Holding – Top10

	Perc. Holding		Perc. Holding
Challa shantha prasa	13.72	Srishant challa	10.23
Soumya challa	9.89	Prasad challa rajend	9.67
Capital group compan	8	Fiam group trust	4.15
Fmr llc	2.21	Georgalis helenna	1.59
Malabar india fund I	1.57	Fund india whizdom	1.46

*\*as per last available data*

### Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

*\*as per last available data*

### Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
24 Jul 2017	Challa Rajendra Prasad	Buy	100000.00
24 Jul 2017	Challa Srishant	Buy	56234.00
24 Jul 2017	Challa Soumya	Buy	50000.00
19 Jun 2017	Challa Rajendra Prasad	Buy	15110.00
19 Jun 2017	Challa Srishant	Buy	15038.00

*\*as per last available data*

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### Coverage group(s) of stocks by primary analyst(s): Miscellaneous

AIA Engineering, Apar Industries Ltd, Aarti Industries, Agro Tech Foods, Balkrishna Industries, CCL Products India, Essel Propack, Orient Refractories, Supreme Industries, Solar Industries, SRF, Vesuvius India, VIP Industries

#### Recent Research

Date	Company	Title	Price (INR)	Recos
31-May-18	<b>Apar Industries</b>	All-round robust growth ; <i>Result Update</i>	706	Buy
22-May-18	<b>VIP Industries</b>	Well-rounded volume growth; strong margin beat; <i>Result Update</i>	394	Buy
21-May-18	<b>Amara Raja Batteries</b>	Strong auto volumes; weak industrial drags margin; <i>Result Update</i>	832	Buy

#### Distribution of Ratings / Market Cap

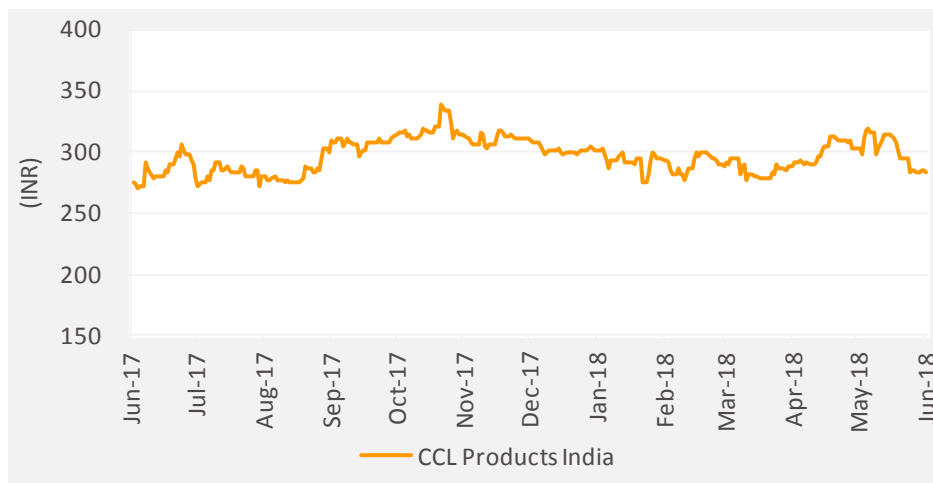
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

#### Rating Interpretation

Rating	Expected to
<b>Buy</b>	appreciate more than 15% over a 12-month period
<b>Hold</b>	appreciate up to 15% over a 12-month period
<b>Reduce</b>	depreciate more than 5% over a 12-month period

One year price chart



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