

BUY

TP: Rs 2,185 | ▲ 39%

ZYDUS WELLNESS

Consumer Staples

29 June 2022

In a sweet spot !!!

- Accelerated launch of innovative products, growing international footprint, and expanding customer base augur well for the company
- Leading niche wellness brands (Sugar Free, Everyuth, Glucon-D, Nycil) and low market penetration rates offer long-term growth opportunity
- Retain BUY with TP of Rs 2,185 as we like company's focus on distribution expansion and growth longevity with strong positioning

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We interacted with ZYWL CFO, Umesh Parikh to gain a perspective on the company's growth prospects and sector outlook. Key takeaways:

Brand can grow double-digit: Average penetration level of the combined portfolio brands stands at ~20% (12-24% across categories) signifies higher growth headroom versus its FMCG peers. Theoretically, increase in penetration is one of the growth planks for a category's growth longevity. Further, management's quest towards improving brand awareness (ad spends at ~14% of revenue) and four-five new product/variants launches will not only improve penetration but also support double-digit growth in the foreseeable future.

Aggressive distribution expansion: ZYWL aims to widen direct distribution coverage from 2.25mn currently to 3.5mn-4mn by FY25 and direct reach from 0.55mn to about 1mn. We believe that restructuring of the distribution channel will continue to yield benefits as consumer sentiments improve and penetration levels rise across categories in which the company operates, especially considering its market-leading position in five of its six segments.

Strong outlook for international business: ZYWL's Sugar Free and Complian brands constitute 93% of international business. The company has entered new markets such as Hong Kong, Lebanon, Zimbabwe, Muscat, Ethiopia and Australia in FY22. Management has guided for high-double-digit growth in the international business, likely crossing Rs 1bn in revenue in FY23. The target is to have 8-10% of revenue from the business in the next 4-5 years from ~4% in FY22.

Positive surprise awaited; retain BUY: ZYWL is trading at ~23x FY24E EPS. We retain BUY and our TP of Rs 2,185, set at ~31x FY24E EPS on the back of new launches, increasing distribution strength, a broader presence through existing brands, its ability to cater to white spaces, and a strong gross margin which gives it the leeway to spend more on brand building. We are also positive on ZYWL's debt reduction measures, faster FCF generation and superior execution.

Key changes

Target	Rating
◀ ▶	◀ ▶

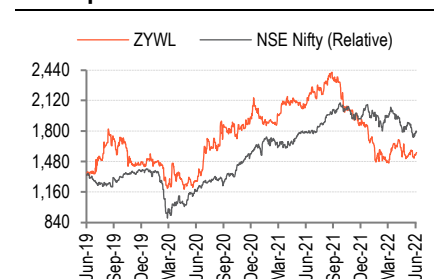
Ticker/Price	ZYWL IN/Rs 1,575
Market cap	US\$ 1.3bn
Free float	35%
3M ADV	US\$ 0.7mn
52wk high/low	Rs 2,477/Rs 1,430
Promoter/FPI/DII	65%/3%/25%

Source: NSE | Price as of 29 Jun 2022

Key financials

Y/E 31 Mar	FY22P	FY23E	FY24E
Total revenue (Rs mn)	20,091	22,045	24,534
EBITDA (Rs mn)	3,448	4,056	4,711
Adj. net profit (Rs mn)	3,098	3,657	4,442
Adj. EPS (Rs)	48.4	57.4	69.5
Consensus EPS (Rs)	48.8	64.3	74.0
Adj. ROAE (%)	5.9	6.9	7.8
Adj. P/E (x)	32.5	27.4	22.7
EV/EBITDA (x)	31.7	25.4	21.3
Adj. EPS growth (%)	(19.3)	18.0	21.2

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance

Source: NSE



Other management meet takeaways

Complan

- ZYWL's health food drinks category declined 2% YoY. Company expects the segment to grow 5-7% in the near-term.
- Hindustan Unilever Limited (HUL) has taken price cuts in Horlicks and Boost portfolio. For instance, Horlicks 500gm price cut by Rs 40 and is currently priced at Rs 199. The same grammage pack of Complan is available at Rs 209. As per ZYWL management, the company will refrain from price reduction strategy. The company will rather reduce the grammage, cut down the trade spends, focus more on promotions and new launches to gain market share.
- Sachets forms ~15% of the malt segment. Off-late, ZYWL has become aggressive in sachets category to drive volume growth.
- Company is maintaining its market share of 5%.
- Erosion of market share is less for Complan compared to its competitor. However, Bournvita might have gained some market share.
- Complan is strong in East and South and in states like West Bengal, Bihar, Orissa and Tamil Nadu. ZYWL has launched Complan in UP and Bihar across price points. UP is witnessing double digit growth and Bihar performance has been satisfactory.
- ZYWL has relaunched 'Complan Nutrigro', a health supplement targeted at the age group of 2-6 years with a focus on the original positioning of helping children grow stronger. The product was earlier launched but could not meet success due to covid and many doctors could not meet MR (medical representative). Doctors have now started meeting MR and company plans to achieve 20% growth in next 2 years.
- With the introduction of Complan Nutrigro, the company is exploring white spaces in the health drinks market.

Sugar Free

- The portfolio has posted a healthy double-digit CAGR growth over last two years.
- The cannibalisation of Sugar Free Gold (stagnant) from Sugar Free Green (strong growth).
- The category is facing challenges as the second Covid-19 wave particularly affected the diabetic population and put pressure on related consumption.
- Sugarlite continued to grow in high double digits during the year with consistent support on the ATL (above the line) and digital front to recruit new consumers into the "healthier sugar" segment.
- Took price hike of 6-7% across SKUs in Nov-Dec 21'.

- The company is moving the segment towards the healthy lifestyle product category where the non-diabetic person can also consume it. The price hike will be taken accordingly as ZYWL focuses on increasing the consumption from non-diabetic consumers.
- Earlier, diabetic patients prefer not to consume the sugar at all. And due to myths revolving around Sugar Free, doctors were not prescribing Sugar Free. However, ZYWL has tied-up with top diabeticians of 15 major cities to break the myths regarding consumption of Sugar Free.

Glucon-D

- Q1FY23 witnessed strong summer season as 90% of the revenue comes in Jan-June.
- Immunovolt is delivering steady growth, supported by campaigns and distribution drives. The market share is 28-30%.
- Glucose has two categories, flavor and plain. The flavored glucose is higher margin business compared to plain. ZYWL has 75% contribution from flavored glucose and 25% from plain.
- The category was Rs 10bn in 2019, which has reduced to Rs 8bn currently. Management expects category to grow to Rs 10bn by FY25.
- New products will be launched next year. Current focus is to drive the existing category.

Nycil

- Nycil brand sales were impacted due to a) decline in the category, b) covid, as it restricted people from moving out, and c) small players gained market share (start-up companies which offered huge trade discounts and discounts on the products). Management expects the small players to quit the system sooner.
- However, the brand has retained its leadership position in the prickly heat segment (maintained its #1 position with 33.7% market share per Nielsen MAT Mar 2022 report) supported by consumer offers and ATL initiatives.
- Management is hopeful of gaining market share owing to the intense summer season in Q1.
- Innovations of different product line on the anvil to increase the growth.

Everyuth

- Per management, the company has launched Everyuth body lotion in Nov 21' and has received strong customer response.
- ZYWL also launched the Everyuth Tan Removal scrub and face pack which met with great success.
- Everyuth scrubs and pel-offs are growing ahead of the category growth.
- Company is schedule to launch new product/variants in 6 months' time.

Nutralite

- Created new identity for the Food service / Horeca segment – opportunity to widen offerings in the segment. 75% of the contribution comes from the institution.
- ZYWL has launched Nutralite Doodhshakti butter and ghee products, Nutralite doodhshakti proteins, Nutralite Mayonnaise and Nutralite choco spread.
- Average price hike of 40-60% to offset increase in milk and palm oil prices. The company will pass-on the benefit with the decline in cost inflation.

International Business

- The company has started introducing newer products like EverYuth in geographies in Middle East and Africa, Nycil, Glucon-D and Nutralite in South East Asia and South Asia.
- In addition, ZYWL is also setting-up a subsidiary in Bangladesh and will commence operation by end of 2022. Company is also evaluating setting-up a manufacturing base/subsidiary in South Africa. These initiatives will further drive the international business going forward.

Rural Penetration

- Rural sales contribution increased to 17-18% of sales from 13-14% earlier.
- ZYWL's rural go-to-market strategy and SKU differentiation can help increase rural penetration.

Growth Guidance

- Management guided strong double-digit growth in top-line and 100-150bps improvement in operating margin for FY23 and FY24. Company is targeting 20% operating margin in 2-2.5 years.

A&P Spends

- Media spends was rationalized to ~12% in FY21 and FY22 to counter inflation and protect its margins. The media spends will increase to 13-14% going forward.

Tax Rate

- Due to unabsorbed Goodwill and depreciation, company will continue to have a tax-free status till FY24. Thereafter, company will be taxable.

Net Debt free by Q4FY23

- Company is targeting to be net-debt free by Q4FY23 and gross debt free by June 2023.

Valuation methodology

ZYWL is a unique play on India's emerging health & wellness category and enjoys market leadership in various niche segments with limited competition from large FMCG companies. The stock is currently trading at ~23x FY24E EPS. We retain BUY and our TP of Rs 2,185 (set at ~31x FY24E EPS) on the back of new launches, increasing distribution strength, a broader presence through existing brands, its ability to cater to white spaces, and a strong gross margin which gives it the leeway to spend more on brand building. We are also positive on ZYWL's debt reduction measures, faster FCF generation and superior execution.

Key risks

Key downside risks to our estimates are:

- failure to realise expected merger benefits,
- failure of new launches,
- aggressive competition from start-ups,
- inability to scale up acquired brands which were typically difficult for FMCG incumbents,
- raw material price increases, and
- economic slowdown/pandemic risk.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Zydus Wellness	ZYWL IN	1.3	1,575	2,185	BUY

Source: BOBCAPS Research, NSE | Price as of 29 Jun 2022

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22P	FY23E	FY24E
Total revenue	17,668	18,667	20,091	22,045	24,534
EBITDA	3,211	3,444	3,448	4,056	4,711
Depreciation	(264)	(252)	(236)	(338)	(375)
EBIT	2,947	3,192	3,211	3,718	4,336
Net interest inc./(exp.)	(1,399)	(838)	(255)	(181)	(32)
Other inc./(exp.)	107	89	104	109	119
Exceptional items	44	1,321	0	0	0
EBT	1,717	3,783	3,077	3,665	4,442
Income taxes	205	65	29	0	0
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	1,943	3,867	3,098	3,657	4,442
Adjustments	0	0	0	0	0
Adjusted net profit	1,943	3,867	3,098	3,657	4,442

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22P	FY23E	FY24E
Accounts payables	5,045	4,386	3,643	5,197	5,727
Other current liabilities	429	297	677	353	393
Provisions	259	312	347	367	409
Debt funds	15,558	5,991	3,815	815	15
Other liabilities	0	0	0	0	0
Equity capital	577	636	636	636	636
Reserves & surplus	34,030	45,042	47,804	51,420	55,804
Shareholders' fund	34,607	45,678	48,440	52,056	56,440
Total liab. and equities	55,897	56,664	56,922	58,788	62,984
Cash and cash eq.	824	2,527	1,698	2,544	5,644
Accounts receivables	1,182	943	1,423	1,102	1,227
Inventories	2,923	3,647	3,616	4,133	4,549
Other current assets	1,396	1,166	919	1,347	1,499
Investments	40,304	39,200	39,470	39,470	39,470
Net fixed assets	2,047	1,996	2,445	2,726	2,902
CWIP	35	37	119	51	57
Intangible assets	5,488	5,478	5,455	5,455	5,455
Deferred tax assets, net	0	0	0	0	0
Other assets	1,697	1,670	478	1,960	2,181
Total assets	55,897	56,664	56,624	58,788	62,984

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22P	FY23E	FY24E
Cash flow from operations	1,606	3,109	1,512	5,927	4,736
Capital expenditures	(169)	(203)	(767)	(551)	(557)
Change in investments	(643)	1,104	(270)	0	0
Other investing cash flows	49	37	1,215	(1,481)	(221)
Cash flow from investing	843	4,047	1,690	3,895	3,958
Equities issued/Others	(1,171)	7,233	(305)	(2)	(19)
Debt raised/repaid	(484)	(9,567)	(2,176)	(3,000)	(800)
Interest expenses	0	0	0	0	0
Dividends paid	(28)	(28)	(31)	(38)	(38)
Other financing cash flows	22	18	(8)	(8)	0
Cash flow from financing	(819)	1,703	(829)	846	3,100
Chg in cash & cash eq.	1,643	824	2,527	1,698	2,544
Closing cash & cash eq.	824	2,527	1,698	2,544	5,644

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22P	FY23E	FY24E
Reported EPS	31.9	18.9	48.4	57.4	69.5
Adjusted EPS	31.9	18.9	48.4	57.4	69.5
Dividend per share	0.4	0.4	0.4	0.5	0.5
Book value per share	600.2	717.9	761.3	818.1	887.0

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22P	FY23E	FY24E
EV/Sales	6.0	6.1	5.4	4.7	4.1
EV/EBITDA	32.9	33.3	31.7	25.4	21.3
Adjusted P/E	49.4	83.1	32.5	27.4	22.7
P/BV	2.6	2.2	2.1	1.9	1.8

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22P	FY23E	FY24E
Tax burden (Net profit/PBT)	111.9	102.2	100.9	100.0	100.0
Interest burden (PBT/EBIT)	56.2	115.3	92.8	95.8	99.7
EBIT margin (EBIT/Revenue)	17.3	17.6	16.5	17.4	18.2
Asset turnover (Rev./Avg TA)	189.3	188.3	193.1	194.5	173.2
Leverage (Avg TA/Avg Equity)	0.3	0.2	0.2	0.2	0.3
Adjusted ROAE	5.6	9.6	6.6	7.3	8.2

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22P	FY23E	FY24E
YoY growth (%)					
Revenue	109.6	5.7	7.6	9.7	11.3
EBITDA	73.7	7.3	0.1	17.7	16.1
Adjusted EPS	3.9	81.5	(19.3)	18.0	21.2
Profitability & Return ratios (%)					
EBITDA margin	18.2	18.4	17.2	18.4	19.2
EBIT margin	16.7	17.1	16.0	16.9	17.7
Adjusted profit margin	11.0	20.7	15.4	16.6	18.1
Adjusted ROAE	3.7	2.3	5.9	6.9	7.8
ROCE	6.9	6.8	6.4	7.3	8.1
Working capital days (days)					
Receivables	24	18	26	18	18
Inventory	135	155	133	150	150
Payables	126	104	79	104	104
Ratios (x)					
Gross asset turnover	0.4	0.4	0.4	0.4	0.4
Current ratio	1.2	1.7	2.0	1.6	2.0
Net interest coverage ratio	2.2	3.9	13.0	21.2	137.6
Adjusted debt/equity	0.4	0.1	0.0	0.0	(0.1)

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

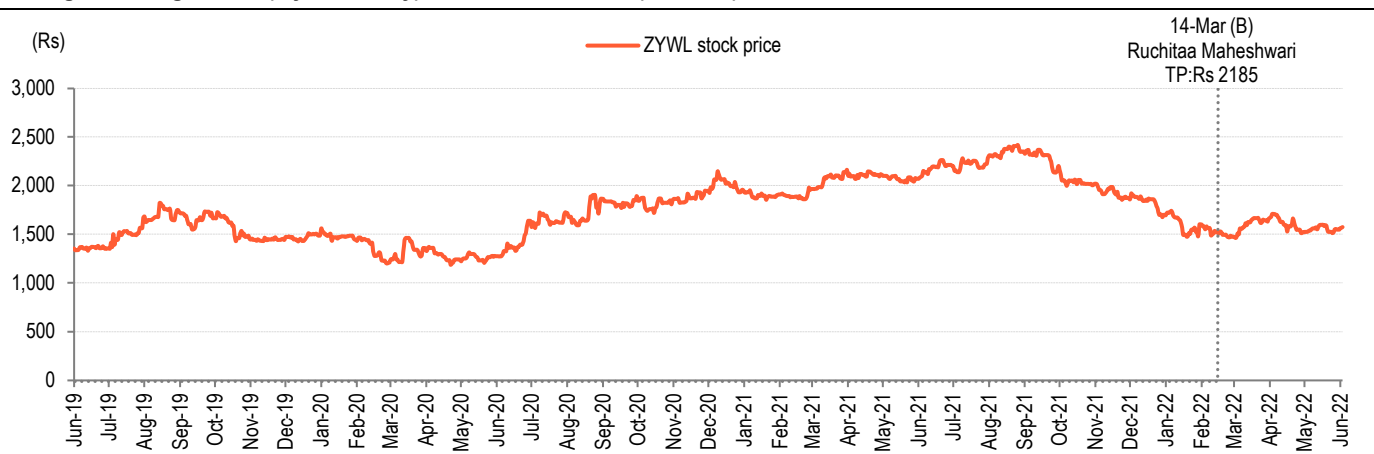
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): ZYDUS WELLNESS (ZYWL IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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