

### Weak demand, elevated RM/PM prices cut margin

VST Industries Q3FY24 print was weakest; revenues grew modestly at 4.8% to Rs3.45bn while EBITDA/PAT declined by 24.1%/32.0% led by higher sales from leaf tobacco exports (27% revenue contribution Vs 15% in FY23). Despite weak base Q3 cigarette volumes cut by ~4% YoY due to persistent weakness in rural demand and weaker RSFT portfolio, yet leaf tobacco exports grew 30%. Higher leaf tobacco and packaging (filter rod) prices resulted in 379bp cut in gross margins to 41.6% (-379bp QoQ). With higher employee/other expenses at 8.5%/19.1% EBITDA margin cut to 19.8% (-753bp), lowest since FY11. Management opined RM prices to remain elevated in Q3 as well, yet it expects some relief through rationalizing cost structure. The company expects gradual recovery in demand to be led by, (1) focus on core markets - UP/WB/Bihar/AP/TG (~70% of sales) to improve volumes, (2) launched Demi-slim priced at Rs10 under Edition in the RSFT segment, (3) expects rural markets to bounce back, and (4) stable taxation. We cut our FY24E/25E earnings and retain BUY with a revised DCF-based TP Rs3,943 (implying 16.3x avg. FY25E/FY26E EPS).

#### Decline in volumes at 7% as VST's portfolio tilted towards DSFT, core remains strong

VST's Q3FY24 revenues grew modestly at 4.8% to Rs3.45bn on the back of moderated growth in core markets such as UP/Bihar/AP/TG/WB which contribute ~70% of sales. Q3 cigarette volumes cut by 4% due to persistent weakness in rural demand and weaker RSFT portfolio, yet leaf tobacco exports grew 30% YoY. The company expects gradual recovery in demand to be led by, (1) focus on core markets - UP/WB/Bihar/AP/TG (~70% of sales) to improve volumes, (2) launched Demi-slim priced at Rs10 under Edition in the RSFT segment, (3) expects rural markets to bounce back, and (4) stable taxation. We believe slower than industry growth may force VST to redraw its growth strategy driven by expanding its RSFT portfolio to expand consumer base as newer consumers now pick up Rs10 price point due to coinage issue.

#### Sharp erosion in gross/EBITDA margins to 41.6%/19.8% led by change in product mix

Gross margins fell sharply to 41.6% - (571bp) (cut by 379bp QoQ) due to higher leaf tobacco and packaging material (filter rods) prices and leaf tobacco exports. With higher employee and other expenses at 8.5%/19.1% EBITDA margin cut to 19.8% (-465bp). We reckon cost saving measures undertaken by VST may show up in the medium term margins to remain under pressure as packaging material (paper, cigarette rods and shippers) remain inflationary. Further, environmental restrictions led the company to consolidate its manufacturing shifting to Toopran unit (outside city limit) which may help in operational synergies in medium term.

#### Valuation and risks

We have been highlighting that the renewed focus for VST was driven by, (1) expanding its direct coverage by investing feet-on-the-street, (2) improve trade visibility, and (3) cut wholesale discounts to strengthen its 'Total brand' perception in the trade. However demand recovery in rural underway, its dominant business in DSFT segment saw weaker growth, yet VST is now building its RSFT portfolio launching Demi-slimes under Edition brand. We expect rural demand to bounce back with a lag and expect VST to launch more products in RSFT segment other than "Edition". Though near term demand would improve gradually, higher leaf tobacco exports and packaging material prices put pressure on margins. To mitigate cost pressure, VST has already rationalized trade discounts to settle for low single-digit volume growth in FY24. With erosion in margins we cut earnings for FY24E/25E by 11.7%/0.5% and retain BUY with a revised DCF-based TP Rs3,943 (implying 16.3x avg. FY25E/FY26E EPS). Risks – Changes in cigarette taxation and disruption in supply chain.

#### Financial and valuation summary

YE Mar (Rs mn)	3QFY24A	3QFY23A	YoY (%)	2QFY24A	QoQ (%)	FY24E	FY25E	FY26E
Revenues	3,618	3,454	4.8	3,481	3.9	13,548	14,570	15,811
EBITDA	716	944	(24.1)	775	(7.6)	3,577	4,445	4,916
EBITDA margin (%)	19.8	27.3	(753bp)	22.3	(251bp)	26.4	30.5	31.1
Adj. Net profit	537	790	(32.0)	760	(29.3)	2,786	3,511	3,944
Adj. EPS (Rs)	34.8	51.2	(32.0)	49.2	(29.3)	180.4	227.4	255.4
EPS growth (%)						(14.8)	26.0	12.3
PE (x)						20.2	16.0	14.2
EV/EBITDA (x)						14.3	11.3	9.9
PBV (x)						4.5	4.0	3.6
RoE (%)						23.0	26.5	26.5
RoCE (%)						23.0	26.5	26.5

Source: Company, Centrum Broking

Please see Disclaimer for analyst certifications and all other important disclosures.

#### Result Update

India I Consumer

23 January, 2024

**BUY**

Price: Rs3,636

Target Price: Rs3,943

Forecast return: 8%

Institutional Research

#### Market Data

Bloomberg:	VST IN
52 week H/L:	4,328/2,910
Market cap:	Rs56.1bn
Shares Outstanding:	15.4mn
Free float:	33.4%
Avg. daily vol. 3mth:	28,449

Source: Bloomberg

#### Changes in the report

Rating:	Unchanged
Target price:	Up 0.1% to Rs3,943
EPS:	FY24E 180.4, 11.7% cut FY25E 227.4, 0.5% cut

Source: Centrum Broking

#### Shareholding pattern

	Dec-23	Sep-23	Jun-23	Mar-23
Promoter	32.2	32.2	32.2	32.2
FIIs	1.4	1.4	1.6	1.6
DIIIs	17.5	17.5	17.2	16.9
Public/other	48.9	48.9	49.1	49.3

Source: BSE

#### Centrum estimates vs Actual results

YE Mar (Rs mn)	Centrum Q3FY24	Actual Q3FY24	Variance (%)
Revenue	3,551	3,618	1.9
EBITDA	870	716	(17.7)
EBITDA margin %	24.5	19.8	-471bps
Other Income	224	95	(57.8)
Interest	-	-	-
Depreciation	79	101	26.7
PBT	1,015	710	(30.0)
Tax	236	173	(26.8)
Rep. PAT	778	537	(31.0)
Adj. PAT	778	537	(31.0)

Source: Bloomberg, Centrum Broking



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Consumer

## Thesis Snapshot

### Estimate revision

YE Mar (Rs mn)	FY24E New	FY24E Old	% chg	FY25E New	FY25E Old	% chg
Revenue	13,548.4	13,548	-	14,570.2	14,570	-
EBITDA	3,576.8	4,068	(12.1)	4,445.3	4,445	-
EBITDA margin %	26.4	30.0	-363 bp	30.5	30.5	0 bp
Adj. PAT	2,786	3,157	(11.7)	3,511	3,529	(0.5)
Diluted EPS (Rs)	180.4	204.4	(11.7)	227.4	228.5	(0.5)

Source: Centrum Broking

### VST Industries versus NIFTY Midcap 100

	1m	6m	1 year
VST IN	7.0	(0.4)	15.1
NIFTY Midcap 100	6.6	30.6	54.5

Source: Bloomberg, NSE

### Key assumptions

Y/E Mar	FY24E	FY25E
Volume growth	(4.0)	4.0

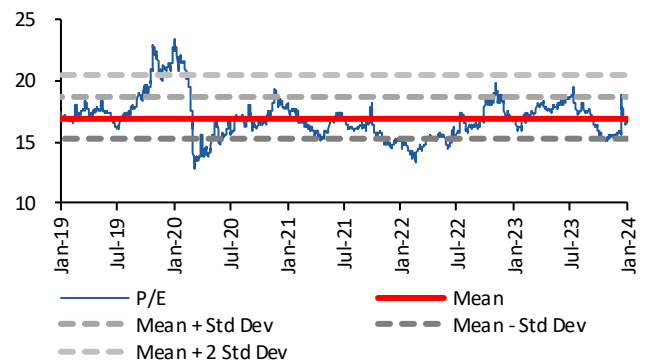
Source: Centrum Broking

### Valuations

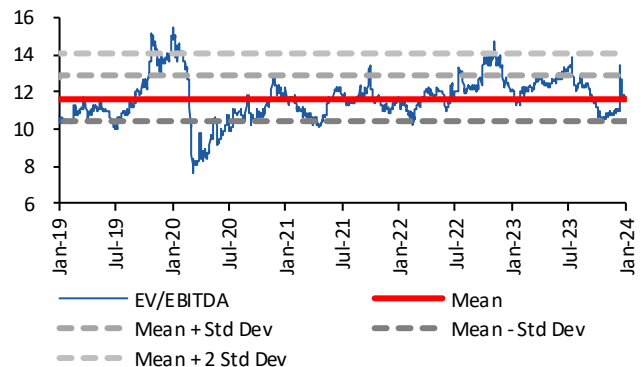
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Valuations	Rs/share
DCF-based target price	3,943
WACC (%)	9.0
Terminal growth rate (%)	3.0

### P/E mean and standard deviation



### EV/EBITDA mean and standard deviation



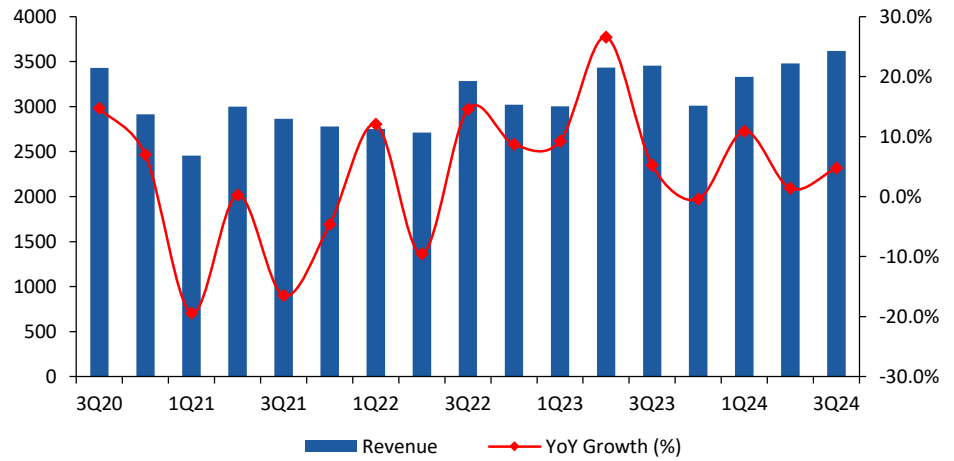
Source: Bloomberg, Centrum Broking

### Peer comparison

Company	Mkt Cap		CAGR (FY24-26E)			P/E (x)			EV/EBITDA (x)			ROE(%)		
	(Rs bn)	Sales	EBITDA	EPS	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E	
ITC	5,844.0	11.3	13.5	11.5	30.0	26.2	23.3	24.9	21.6	19.0	29.0	30.0	32.1	
Godfrey Phillip	114.1	13.3	15.0	21.1	18.0	14.3	12.3	11.6	9.4	7.8	20.6	21.9	21.3	
<b>VST Industries</b>	<b>56.1</b>	<b>8.0</b>	<b>17.2</b>	<b>19.0</b>	<b>17.2</b>	<b>20.2</b>	<b>16.0</b>	<b>13.7</b>	<b>14.3</b>	<b>11.3</b>	<b>29.0</b>	<b>23.0</b>	<b>26.5</b>	

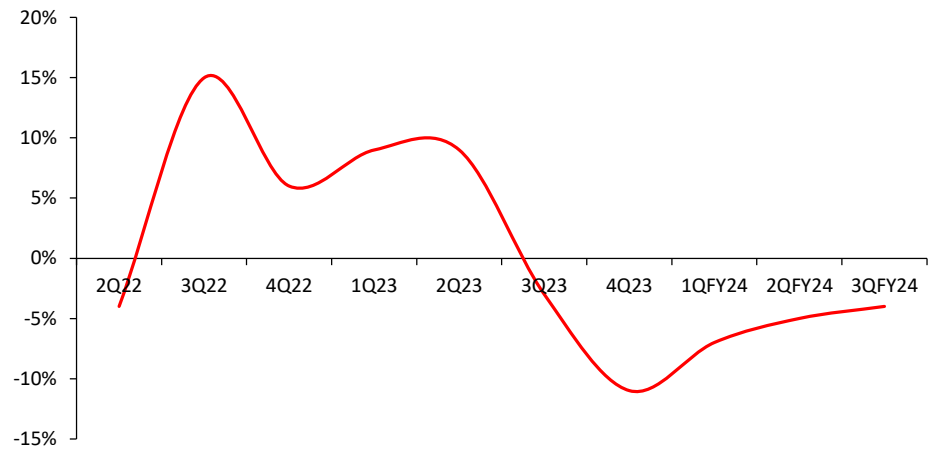
Source: Company, Centrum Broking

**Exhibit 1: Revenue Growth on YoY**



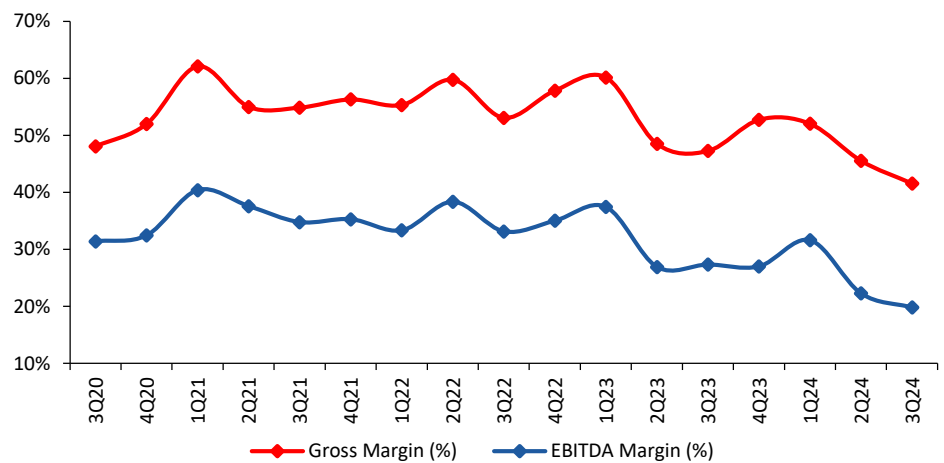
Source: Company, Centrum Broking

**Exhibit 2: Volume Growth on YoY**

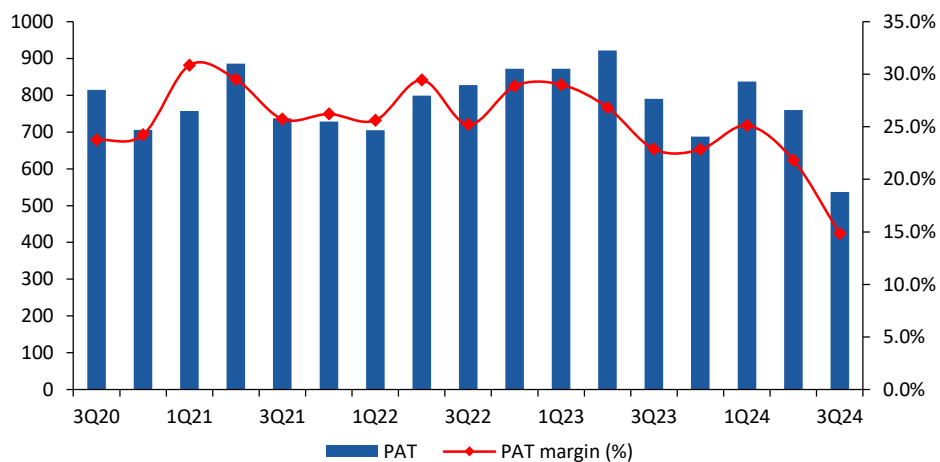


Source: Company, Centrum Broking

**Exhibit 3: Gross Vs EBITDA Margin Trend**



Source: Company, Centrum Broking

**Exhibit 4: PAT margin trend on Quarterly basis**

Source: Company, Centrum Broking

**Exhibit 5: Quarterly financials – Standalone**

(Rs mn)	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24
<b>Net Sales</b>	<b>3021</b>	<b>3005</b>	<b>3434</b>	<b>3,454</b>	<b>3,009</b>	<b>3,331</b>	<b>3,481</b>	<b>3,618</b>
Cost of goods sold	1273	1198	1768	1821	1422	1598	1896	2,115
Employee Expenses	273	303	291	310	300	303	321	336
Other Exp	417	380	451	380	474	379	490	452
<b>Operating Profit (Core EBITDA)</b>	<b>1057</b>	<b>1124</b>	<b>924</b>	<b>944</b>	<b>812</b>	<b>1052</b>	<b>775</b>	<b>716</b>
Depreciation	88	72	72	74	84	81	91	100
<b>EBIT</b>	<b>969</b>	<b>1052</b>	<b>852</b>	<b>869</b>	<b>728</b>	<b>971</b>	<b>684</b>	<b>615</b>
Interest	0	0	0	0	0	0	0	0
Other Income	181	119	335	164	169	122	307	95
<b>Profit Before Tax</b>	<b>1150</b>	<b>1171</b>	<b>1188</b>	<b>1033</b>	<b>898</b>	<b>1093</b>	<b>991</b>	<b>710</b>
Tax	278	299	266	243	211	256	232	173
Tax rate (%)	24.2	25.6	22.4	23.5	37.7	23.4	23.4	24.3
<b>Adjusted PAT</b>	<b>872</b>	<b>871</b>	<b>922</b>	<b>790</b>	<b>687</b>	<b>837</b>	<b>760</b>	<b>537</b>
<b>Growth (%)</b>								
Net Sales	8.7	9.2	26.6	5.2	(0.4)	10.9	1.4	4.8
EBITDA	7.9	22.7	(11.2)	(13.2)	(23.2)	(6.4)	(16.1)	(24.1)
Adj. PAT	19.7	23.7	15.4	(4.5)	(21.2)	(3.9)	(17.6)	(32.0)
<b>Margin (%)</b>								
Gross Margin	57.8	60.1	48.5	47.3	52.7	52.0	45.5	41.6
EBITDA	35.0	37.4	26.9	27.3	27.0	31.6	22.3	19.8
EBIT	32.1	35.0	24.8	25.2	24.2	29.2	19.6	17.0
PAT	28.9	29.0	26.8	22.9	22.8	25.1	21.8	14.8

Source: Company Data, Centrum Broking

P&L					
YE Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
<b>Revenues</b>	<b>11,766</b>	<b>12,901</b>	<b>13,548</b>	<b>14,570</b>	<b>15,811</b>
Operating Expense	5,439	6,210	7,221	6,570	7,053
Employee cost	1,164	1,203	1,233	1,588	1,739
Others	1,063	1,685	1,517	1,967	2,103
<b>EBITDA</b>	<b>4,101</b>	<b>3,804</b>	<b>3,577</b>	<b>4,445</b>	<b>4,916</b>
Depreciation & Amortisation	301	302	412	437	468
<b>EBIT</b>	<b>3,800</b>	<b>3,502</b>	<b>3,165</b>	<b>4,008</b>	<b>4,448</b>
Interest expenses	0	0	0	0	0
Other income	482	787	525	642	775
<b>PBT</b>	<b>4,282</b>	<b>4,289</b>	<b>3,690</b>	<b>4,650</b>	<b>5,223</b>
Taxes	1,080	1,019	904	1,139	1,280
Effective tax rate (%)	25.2	23.8	24.5	24.5	24.5
<b>PAT</b>	<b>3,203</b>	<b>3,270</b>	<b>2,786</b>	<b>3,511</b>	<b>3,944</b>
Minority/Associates	0	0	0	0	0
<b>Recurring PAT</b>	<b>3,203</b>	<b>3,270</b>	<b>2,786</b>	<b>3,511</b>	<b>3,944</b>
Extraordinary items	0	0	0	0	0
<b>Reported PAT</b>	<b>3,203</b>	<b>3,270</b>	<b>2,786</b>	<b>3,511</b>	<b>3,944</b>

Ratios					
YE Mar	FY22A	FY23A	FY24E	FY25E	FY26E
<b>Growth (%)</b>					
Revenue	6.0	9.6	5.0	7.5	8.5
EBITDA	0.2	(7.3)	(6.0)	24.3	10.6
Adj. EPS	3.0	2.1	(14.8)	26.0	12.3
<b>Margins (%)</b>					
Gross	56.4	51.9	48.0	56.7	56.9
EBITDA	34.9	29.5	26.4	30.5	31.1
EBIT	32.3	27.1	23.4	27.5	28.1
Adjusted PAT	27.2	25.3	20.6	24.1	24.9
<b>Returns (%)</b>					
ROE	31.8	29.0	23.0	26.5	26.5
ROCE	31.8	29.0	23.0	26.5	26.5
ROIC	175.1	49.4	31.0	38.7	41.0
<b>Turnover (days)</b>					
Gross block turnover ratio (x)	2.8	1.5	1.5	1.5	1.5
Debtors	8	11	11	11	11
Inventory	211	190	180	211	212
Creditors	83	59	58	67	60
Net working capital	201	107	116	144	163
<b>Solvency (x)</b>					
Net debt-equity	(0.7)	(0.3)	(0.4)	(0.4)	(0.5)
Interest coverage ratio	0.0	0.0	0.0	0.0	0.0
Net debt/EBITDA	(1.9)	(1.0)	(1.4)	(1.4)	(1.5)
<b>Per share (Rs)</b>					
Adjusted EPS	207.4	211.7	180.4	227.4	255.4
BVPS	695.7	764.0	804.4	912.5	1,017.5
CEPS	226.9	231.3	207.1	255.7	285.7
DPS	140.0	140.0	119.3	150.3	168.9
Dividend payout (%)	67.5	66.1	66.1	66.1	66.1
<b>Valuation (x)</b>					
P/E	17.5	17.2	20.2	16.0	14.2
P/BV	5.2	4.8	4.5	4.0	3.6
EV/EBITDA	11.8	13.7	14.3	11.3	9.9
Dividend yield (%)	3.8	3.8	3.3	4.1	4.6

Source: Company, Centrum Broking

Balance sheet					
YE Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Equity share capital	154	154	154	154	154
Reserves & surplus	10,589	11,643	12,267	13,936	15,558
Shareholders fund	10,743	11,797	12,421	14,090	15,713
Minority Interest	0	0	0	0	0
Total debt	0	0	0	0	0
Non Current Liabilities	230	215	215	215	215
Def tax liab. (net)	(216)	(178)	(178)	(178)	(178)
<b>Total liabilities</b>	<b>10,757</b>	<b>11,834</b>	<b>12,458</b>	<b>14,127</b>	<b>15,749</b>
Gross block	4,162	8,416	8,957	9,599	10,364
Less: acc. Depreciation	(2,212)	(2,514)	(2,926)	(3,363)	(3,831)
Net block	1,950	5,901	6,032	6,235	6,532
Capital WIP	105	3	3	3	3
Net fixed assets	2,054	5,905	6,035	6,239	6,536
Non Current Assets	185	116	116	116	116
Investments	2,031	2,018	2,018	2,018	2,018
Inventories	2,956	3,493	3,463	3,816	4,091
Sundry debtors	333	432	410	462	490
Cash & Cash Equivalents	7,830	3,954	4,914	6,016	7,459
Loans & advances	4	0	0	0	0
Other current assets	297	441	458	493	535
Trade payables	1,034	968	1,259	1,055	1,179
Other current liab.	3,900	3,556	3,698	3,977	4,316
Provisions	0	0	0	0	0
Net current assets	6,487	3,795	4,289	5,755	7,080
<b>Total assets</b>	<b>10,757</b>	<b>11,834</b>	<b>12,458</b>	<b>14,127</b>	<b>15,749</b>

Cashflow					
YE Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Profit Before Tax	4,576	4,590	3,577	4,445	4,916
Depreciation & Amortisation	0	0	0	0	0
Net Interest	0	0	0	0	0
Net Change – WC	(743)	(1,837)	467	(364)	117
Direct taxes	(1,061)	(939)	(904)	(1,139)	(1,280)
<b>Net cash from operations</b>	<b>2,772</b>	<b>1,815</b>	<b>3,140</b>	<b>2,942</b>	<b>3,754</b>
Capital expenditure	(482)	(4,038)	(542)	(641)	(765)
Acquisitions, net	0	0	0	0	0
Investments	(556)	4,311	0	0	0
Others	81	194	525	642	775
<b>Net cash from investing</b>	<b>(958)</b>	<b>467</b>	<b>(17)</b>	<b>1</b>	<b>10</b>
<b>FCF</b>	<b>1,815</b>	<b>2,282</b>	<b>3,123</b>	<b>2,944</b>	<b>3,764</b>
Issue of share capital	(107)	(82)	0	0	0
Increase/(decrease) in debt	0	0	0	0	0
Dividend paid	(1,760)	(2,154)	(2,162)	(1,842)	(2,321)
Interest paid	0	0	0	0	0
Others	0	0	0	0	0
<b>Net cash from financing</b>	<b>(1,866)</b>	<b>(2,236)</b>	<b>(2,162)</b>	<b>(1,842)</b>	<b>(2,321)</b>
Net change in Cash	(52)	46	961	1,102	1,443

Source: Company, Centrum Broking

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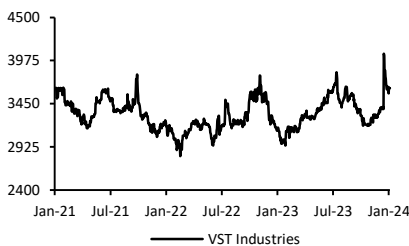
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**VST Industries**



Source: Bloomberg

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