Stock Update

CCL Products Ltd.

January 23, 2023

RETAILRESEARCH

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CCL Products Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Coffee	Rs. 532	Buy in Rs. 528-538 band and add further on dips in Rs. 475-484 band	Rs. 587	Rs. 627	2-3 quarters

HDFC Scrip Code	CCLROEQNR
BSE Code	519600
NSE Code	CCL
Bloomberg	CCL IN
CMP (Jan 20, 2023)	532
Equity Capital (RsCr)	26.6
Face Value (Rs)	2
Equity Share O/S (Cr)	13.3
Market Cap (RsCr)	7083
Book Value (Rs)	102
Avg. 52 Wk Volumes	386286
52 Week High	572
52 Week Low	315

Share holding Pattern % (December, 2022)	
Promoters	46.26
Institutions	29.39
Non Institutions	24.35
Total	100.0

* Refer at the end for explanation on Risk Ratings

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Our Take:

CCL Products Ltd. (CCL) is in the business of converting raw coffee beans into instant coffee granules/powder. The company is not only India's largest coffee processor, but it has the world's largest single location plant and has top private label instant coffee manufacturers across the globe as its clients. While prima facie it looks like a commodity conversion business, unlike tea or other commodities, coffee processing is a specialist job as the flavour and consistency has to be maintained batch after batch irrespective of the input quality or grade. Not many companies have been successful in doing this and hence, globally, coffee business has very little competition and high profitability.

Worldwide CCL's coffee is being consumed at the rate of 1,000 cups per second. CCL exports its processed coffee to more than 90 countries and supports more than 250 brands with sustainable supplies — both quality and quantity. CCL has on offer more than 1000 recipes for the clients to choose from. It has a combined state-of-the-art manufacturing capacity of ~54,000 MTPA, which is spread over Duggirala (Guntur District of AP), Kuvvakolli (Chittoor District, AP), Switzerland, and Vietnam. Having succeeded in placing their coffee on the world markets, CCL launched its 'Continental Coffee' brand for the Indian market, which should act as a major growth catalyst, going ahead. With the help of its rich experience in the international markets, it has developed 250+ blends, claiming they are superior to its competitors' blends.

Valuation & Recommendation:

CCL is amongst the largest green coffee bean processors globally. It is India's largest exporter of instant coffee (38% market share) and world's leading supplier to private labels. Over the past two decades, it has increased its capacity by 15x without diluting equity and has also managed to keep its debt in check. Its business model is strong and robust, by virtue of it being a sticky business; it has the best-in-class technology, superior economies of scale and resilient margins. With commercialisation of incremental capacity (16,500 MTPA) at Vietnam, the management is confident on achieving 20-25% volume growth in FY23 and 15-20% volume growth in FY24 respectively. In addition to 16,000 MT greenfield expansion at Chitoor announced in Q1FY23, the company has announced another 6,000 MT Freeze Dried Coffee (FDC) expansion at Vietnam on the back of written commitment from a client for five years for ~50% of the expanded capacity. Such aggressive expansions demonstrates strong traction that CCL is witnessing in order inquiries across various markets. With these capacity additions, CCL's capacity is likely to reach ~76,000 MT by FY25 which could result in robust 20%+ volume growth over next 3-4 years.

We expect revenue and earnings to grow at a CAGR of 28% and 27% respectively over FY22-25E on the account of a) doubling of Vietnam Capacity (company enjoys tax break here), b) upcoming capacities at Chitoor (Q1FY25) and Vietnam (FDC, Q3FY25) b) higher share of small packs & packing capacity ramp-up, and c) increasing share of India branded business in the overall revenue mix. With enhanced revenue growth visibility, the stock is likely to re-rate if the company continues to maintain a strong margin profile, and the high expected debt levels due to planned capacity additions may not impact valuations to a great extent.

We think the base case fair value of the stock is Rs. 587 (22x Sept'24E EPS) and the bull case fair value of is Rs 627 (23.5x Sept'24E EPS). Investors can buy the stock in Rs 528-538 band (20x Sept'24E EPS) and add more on dips in Rs. 475-484 (18x Sept'24E EPS).

Financial Summary

Particulars (Rs Cr)	Q3FY23	Q3FY22	YoY-%	Q2FY23	QoQ-%	FY21	FY22	FY23E	FY24E	FY25E
Net Revenues	535	423	26%	507	6%	1242	1462	2098	2484	3035
EBITDA	101	92	10%	98	3%	298	331	403	514	634
APAT	73	58	26%	58	26%	182	204	257	332	421
Diluted EPS (Rs)	5.5	4.4	26%	4.3	26%	13.7	15.4	19.3	25.0	31.7
P/E (x)						39.1	34.8	27.7	21.4	16.9
EV/EBITDA						25.1	23.0	19.3	15.4	12.4
RoE-%						18.1	17.5	19.0	21.0	22.5

(Source: Company, HDFC sec)

Q3FY23 Result Highlights

In Q3FY23, CCL reported 26.5%/5.7% YoY/QoQ revenue growth. The volume was lower at ~5-6% on account of maintenance shutdown of Indian plant and partial production of Vietnam plant (additional capacity). However, the management is confident of making up for lower growth with incremental volumes from Vietnam, and maintained its volume growth guidance of 20-25% for FY23 and 15-20% for FY24. 9MFY23 volume growth stood at ~18% YoY.

High coffee inflation resulted in ~20% increase in realisations, which optically drove EBITDA margin 310bps lower to 18.8% but as the company operates on cost plus model, there was limited impact on EBITDA/kg.

Interest cost increased 200% YoY to Rs 11 Cr on account of higher interest cost, commissioning of capacities and increase in working capital requirements. PAT grew by 26% YoY on account of lower tax. India operations tax rate was lower in Q3FY23 as it came under MAT after claiming additional depreciation as per IT Act pertaining to the packing capacity.

Capex, Capex and some more Capex: CCL has already started trial runs and will commercialise the new 16,500 MT of capacity in Vietnam (taking the total capacity in Vietnam to ~30,000 MT). In Q1FY23 it had announced plan of another ~16,000MT of spray dried capacity near its Chittoor plant which will cost ~Rs 320 Cr. The capex is likely to be funded by both, debt and internal accruals. According to the management, the plant will be commissioned by the end of FY24 and is expected to generate RoE of ~20% which is higher than its existing ROE, given the modern technology at the new plant.

Further, in Q3FY23, the company has announced expansion plan for addition of 6,000 MT of Freeze Dried (FD) capacity in Vietnam. This plant is expected to get commercialized by Q3FY25. The cost is around USD 50 mn which includes the debt of USD 30 mn. The reason for this expansion are: a) the existing FD capacity has been pre-booked till FY24, and b) commitment by an existing customer to procure ~3000 MT p.a. or 50% of the capacity for five years. The increasing wallet share from existing customer demonstrates CCL's credibility as supplier.

Post this expansion Vietnam will have total capacity of 36,000 MT split between 30,000 MT of spray dried (SD) and 6,000 MT freeze dried coffee (FDC). On consolidated level, post ongoing expansion, CCL's total capacity would stand at 76,000 MT giving an assurance of ~18-20% volume growth over next 3-4 years. While the capex would stretch the debt on books and limit the FCF in near term, the company's ability of generating cash as demonstrated by past track record gives us confidence about the long term viability of its model.

CCL is the second largest manufacturer for private label behind Nestle. Post capacity expansion, CCL's capacity would be more than 2x the third largest player.

Disruptions caused by Covid-19 and Ukraine war have caused various large players to de-risk their supply chains by reducing over dependence on any particular country/region. In this scenario, CCL with its ability to source and supply from any part of the world stands to gain market share.

Domestic business is ready for a takeoff: The performance of domestic branded coffee business (under Continental brand) was subdued in Q3FY23 on account of restructuring in domestic business. However, CCL has guided domestic business revenue of Rs 250 Cr (~25%+YoY growth) in FY23, out of which 70% will be branded coffee business. The segment has been operating at break-even level and expected to turn profitable in FY23. The company is currently re-investing all profits back into the business and is enhancing its presence in the domestic market by widening its distribution network and conducting mass media campaigns to support its product launches.

Key Risks

Currency volatility: CCL derives ~90% of its revenue through exports, thus being exposed to currency fluctuations. However, ~75% of its raw material is also imported and hence it creates a natural hedge for all transactions taking place in US dollars.

Duty changes across operating countries: CCL supplies coffee to over 90 countries from India and Vietnam. Any unfavorable change in import or export duty rates in any country or imposition of non-tariff barriers could impact the competitiveness of supply from Vietnam and/or India.

Slower ramp-up in branded business: The company is cautiously expanding its Continental brand in the domestic market. Although it has been well-received so far, any adverse customer response could impact the growth prospects and financials.

Credit risk: With ~95% of CCL's business being B2B in nature, the company is exposed to credit risks. However, most of the business is repetitive and with established clientele. The company does not have record of any major bad debts in its history.

Supply chain disruptions: In a year of high uncertainty in the macro environment and geopolitical relations, disruptions in the supply chain are an important risk to monitor.

Covid recurrence could impact demand for coffee while Vietnam supplies could also get impacted due to lockdowns, etc.

Company Background

CCL was formed in 1994 and commenced its commercial operations in 1995. It is an 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. CCL has adopted Swiss and Brazilian technologies at its plants, which have been purchased from world renowned pioneers in turnkey instant/soluble coffee technologies. This has enabled it to produce international quality soluble coffee with over 250 blends, which are currently being exported to more than 90 countries worldwide. Today, the company is India's largest manufacturer and exporter (38% market share) of instant coffee and the largest player in the private label market (with 10% market share). CCL operates through four plants: two in India and one each in Vietnam and Switzerland.

CCL Products Ltd.

Financials

Income Statement

Particulars (Rs Cr)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Net Revenues	**1139**	**1242**	**1462**	**2098**	**2484**	**3035**
Growth (%)	5.3%	9.1%	17.7%	43.5%	18.4%	22.2%
Operating Expenses	853	945	1131	1695	1990	2428
EBITDA	**286**	**298**	**331**	**403**	**494**	**607**
Growth (%)	16.5%	4.2%	11.2%	21.7%	22.7%	22.8%
EBITDA Margin (%)	***25.1%***	***24.0%***	***22.6%***	***19.2%***	***19.9%***	***20.0%***
Depreciation	47	49	57	77	96	110
Other Income	4	3	4	6	7	9
EBIT	**243**	**252**	**278**	**332**	**406**	**507**
Interest expenses	18	17	16	36	45	53
PBT	225	235	261	296	360	454
Tax	59	53	57	49	56	64
APAT	**166**	**182**	**204**	**247**	**304**	**390**
Growth (%)	7.1%	9.9%	12.1%	21.0%	23.1%	28.3%
EPS	**12.5**	**13.7**	**15.4**	**18.6**	**22.9**	**29.3**

Balance Sheet

As at March	FY20	FY21	FY22	FY23E	FY24E	FY25E
SOURCE OF FUNDS						
Share Capital	27	27	27	27	27	27
Reserves	902	1061	1224	1418	1643	1940
Shareholders' Funds	**928**	**1087**	**1251**	**1445**	**1669**	**1966**
Borrowings	392	475	561	701	841	808
Net Deferred Taxes	46	49	73	73	73	73
Other Non-Current Liabilities	9	5	4	8	10	12
Total Source of Funds	**1376**	**1617**	**1895**	**2337**	**2704**	**2964**
APPLICATION OF FUNDS						
Net Block	724	798	882	1230	1524	1644
CWIP	100	149	160	80	40	20
Investments	1	0	0	0	0	0
Long Term Loans & Advances	48	50	36	76	89	109
Total Non-Current Assets	**873**	**997**	**1079**	**1386**	**1653**	**1773**
Inventories	260	320	519	632	749	832
Trade Receivables	268	299	320	431	476	590
Cash & Equivalents	39	120	56	47	16	8
Other Current Assets	69	52	96	118	136	150
Total Current Assets	**636**	**791**	**991**	**1228**	**1377**	**1579**
Trade Payables	25	20	46	63	68	91
Other Current Liab & Provisions	109	151	129	213	258	297
Total Current Liabilities	**134**	**171**	**175**	**277**	**326**	**389**
Net Current Assets	502	620	817	952	1051	1191
Total Application of Funds	**1376**	**1617**	**1895**	**2337**	**2704**	**2964**

Cash Flow Statement

Particulars (Rs Cr)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Reported PBT	225.3	234.8	261.3	296.1	360.1	453.8
Interest Expenses	47.1	49.4	57.5	77.1	96.2	109.7
Depreciation	65.6	53.5	84.5	78.5	129.3	144.8
Working Capital Change	-147.1	-91.5	-206.2	-145.5	-129.5	-154.9
Tax Paid	-53.5	-25.9	-39.0	-48.9	-55.8	-63.5
OPERATING CASH FLOW (a)	**90.3**	**170.9**	**100.7**	**180.2**	**304.1**	**380.2**
Capex	-63.8	-154.6	-189.9	-240.0	-350.0	-210.0
Free Cash Flow	26.5	16.3	-89.3	-59.8	-45.9	170.2
Investments and Others	-24.8	1.8	0.0	0.0	0.0	0.0
INVESTING CASH FLOW (b)	**-88.4**	**-152.8**	**-189.9**	**-240.0**	**-350.0**	**-210.0**
Debt Issuance / (Repaid)	52.6	90.3	91.6	140.0	140.0	-32.7
Interest Expenses	-40.8	155.0	151.5	125.0	45.0	-21.0
Share Capital Issuance	0.0	0.0	0.0	0.0	0.0	0.0
Dividend	-89.8	-26.6	-66.5	-53.2	-79.8	-93.1
Others	0.0	0.0	0.0	0.0	0.0	0.0
FINANCING CASH FLOW (c)	**-37.2**	**63.7**	**25.1**	**50.8**	**14.7**	**-178.6**
NET CASH FLOW (a+b+c)	**-35.3**	**81.8**	**-64.2**	**-9.0**	**-31.2**	**-8.4**

One-year Share Price Chart

Key Ratios

Particulars	FY20	FY21	FY22	FY23E	FY24E	FY25E
Profitability Ratios (%)						
EBITDA Margin	25.1	24.0	22.6	19.2	19.9	20.0
EBIT Margin	21.4	20.3	19.0	15.8	16.3	16.7
APAT Margin	14.6	14.7	14.0	11.8	12.2	12.9
RoE	18.8	18.1	17.5	18.3	19.5	21.5
RoCE	18.9	17.5	16.5	16.8	17.4	19.2
Solvency Ratio (x)						
Net Debt/EBITDA (x)	1.2	1.2	1.5	1.6	1.7	1.3
Net D/E	0.4	0.3	0.4	0.5	0.5	0.4
Per Share Data (in Rs)						
EPS	12.5	13.7	15.4	18.6	22.9	29.3
CEPS	16.0	17.4	19.7	24.4	30.1	37.6
BV	69.8	81.7	94.0	108.6	125.5	147.8
Dividend	4.3	2.0	5.0	4.0	6.0	7.0
Turnover Ratio						
Cash Conversion Cycle (days)	186.8	203.6	232.6	197.5	194.8	182.3
Debtor days	85.9	87.7	79.8	75.0	70.0	71.0
Inventory days	111.4	123.5	167.5	136.1	137.3	125.0
Creditors days	10.5	7.7	14.7	13.6	12.5	13.8
Valuation (x)						
P/E	42.7	38.9	34.7	28.7	23.3	18.2
P/BV	7.6	6.5	5.7	4.9	4.2	3.6
EV/EBITDA	26.0	25.0	22.9	19.2	16.0	13.0
EV / Revenues	6.5	6.0	5.2	3.7	3.2	2.6
Dividend Yield (%)	0.8%	0.4%	0.9%	0.8%	1.1%	1.3%

(Source: Company, HDFC sec)

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HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

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