



VST INDUSTRIES LIMITED

VST Industries Limited

Research report as on 4-11-2022

CMP: 3,593.30 INR

Market Capitalisation : 5530 Cr

PEE AAR SECURITIES LTD.

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Introduction

- VST Industries is engaged in manufacture and trading of Cigarettes, Tobacco and Tobacco products.
- India is the second largest tobacco consuming country in the world
- VST, based out of Hyderabad, is an associate of British American Tobacco Plc which holds a 32.2% stake in the company.
- Founded in the year 1930, VST Industries got its name through its founder Vazir Sultan and now they are the third-largest player in the Indian Cigarette Market with over 90 years of operations. The market share of VST Industries stands at 9% in the legal cigarette market and 5% in the overall cigarette market in terms of value.
- 2 Manufacturing facilities in Hyderabad and Toopran
- Value creation during the decade has been Compounded Annual Growth Rate (CAGR), 9.8% in Earnings Per Share (EPS) and 6.2% in Dividend Per Share (DPS).

- Vst operates mainly in the lower end categories and the company sells cigarettes at different price levels ranging from 4 to 10 per stick. Also, the company intends to enter into the higher tranche of the consumer segment by launching the 84 mm cigar under the brand Edition.
- VST derives most of its revenue from the southern and eastern states, now the company has forayed into the central states which would increase its market share. Company continues to expand its geographic footprint by entering new markets such as Gujarat and Maharashtra while strengthening presence in already existing geographies
- The company manufactures Cigarette and unmanufactured tobacco in its two manufacturing units at Hyderabad and Toopran, Telangana. The company spends 0.53% of its sale on R&D. In the R&D division, the company focuses on developing quality blends with innovative filter variants for new brands, which have been well accepted by consumers in the marketplace.

Brand Portfolio

NEW-AGE BRANDS

Total

First mover in capsule segment with very innovative product concepts. Gained widespread popularity with modern adult consumers across the country. Leader in the capsule segment and the 2nd brand in the cigarette category with a near pan-India presence.



Editions

VST's 1st successful king size brand with a strong presence in South India



GROWTH HERITAGE BRANDS

Charms

A generational brand with a multi-region presence



Special

Strong presence in East



Moments

Strong presence in North India



Total's New Brand Architecture

Total has created a record of being the most successful new brand in the last three decades. Total has heralded a new wave of innovation in the Indian cigarette category.



A New Variant Catering to Consumers' Preferences

We developed Total Royal Twist, a kesar & saunf variant of Total.

Geographic Footprint



Strengths

Strong Entry Barrier

There are many entry barriers in this business because of government regulations. Government don't issue a license to new companies to manufacture cigarettes. So it a very concentrated industry.

Strong Financial risk profile

The financial risk profile is driven by a strong capital structure (debt-free status since 2003), steady cash accrual, and superior liquidity. Healthy portfolio of investments (mainly in debt mutual funds), and cash and bank balance supports liquidity.

Established market position with reputed brands

VST is an established player in the cigarette industry with over 8 decades of operations. It is the third largest player in the Indian cigarette market, with significant presence in West Bengal, Andhra Pradesh, Telangana, Bihar, and Uttar Pradesh. The company has a portfolio of reputed brands.

Strong brand loyalty and adequate pricing power will continue to support the business risk profile over the medium term.

Weaknesses

- **Small market share and risk of regional concentration in revenue**
Though VST is the third-largest player in the Indian cigarette market, it has a small market share of over 9% in terms of volume. Operations remain concentrated in southern and eastern India, despite significant increase in market reach in northern states such as Uttar Pradesh. To improve its market share and increase geographical diversity, VST has also entered into new geographies, such as Punjab and Central India.
- **Regulatory restrictions could have an impact on long term revenue growth of the Company**
The cigarette industry continues to be highly vulnerable to changes in government policies and regulations. The Company operates under increasingly stringent regulatory regime (COTPA guidelines on packaging and labelling, advertising and promotion).
- **No Advertisements** In view of the provisions of COTPA, various restrictions such as ban on advertising in print, visual media and outdoors, regulation of in-store advertising, prohibition of sale of cigarettes to persons below the age of 18 years, etc. have been in force. Printing of pictorial warnings on cigarette packets, came into effect from 31st May 2009 were further revised and the pictorial warning covering 85% of the front and back side of the packets was implemented w.e.f. 1st April 2016

Tax Implications

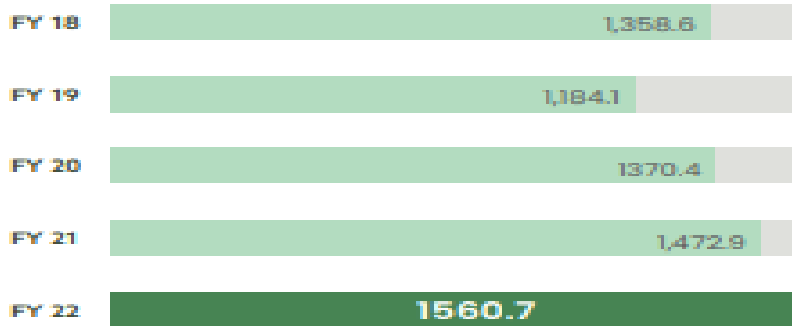
- Earlier tobacco could be seen as a 'need' available for everyone. Research over the years has brought to light the harmful effects of smoking, this in turn prompted the government to take action. The restrictions that have been put in place to minimize the harmful effects of smoking.
- These started out as increasing awareness among Indians to increasing taxes then to banning advertisements and currently using the product itself to advertise its harmful effects. Cigarettes are classified as Sin goods under the GST regime and Currently taxed at 28% and an additional cess up to 21%. The high taxation on cigarettes has resulted in expanding illegal cigarette market. Currently, the illegal market has 28% share in Tobacco Industry.
- It unfortunately has boosted illegal foreign cigarettes coming into the country through the border. This is done in order to avoid taxes. These activities further affect the legal cigarette industry.
- Excise duty is charged on the manufacturing of cigarettes, bidi, and other chewing tobacco products at different rates.
 - Cigarette – 64%
 - Bidi – 22%
 - Chewing products – 81%
- Illegal non duty paid cigarettes continue to benefit from large price gap (>70% vs. tax paid cigarettes) and remain a threat for legal players.

Financials

₹ in Lakhs

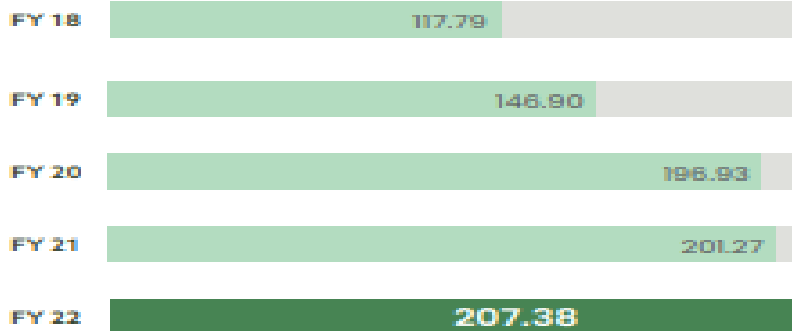
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue from operation - Cigarette	143369	138528	146140	178731	198325	110788	94382	113034	127173	134662
Less: excise duty	95739	84203	88692	117984	133891	41106	8510	13107	36191	38250
Net revenue from operation - Cigarette	47630	54325	57448	60747	64434	69682	85872	99927	90982	96412
Revenue from operation - Others	19238	24593	26168	27568	27805	25076	24029	24008	20116	21404
Total revenue from operation - Net	66868	78918	83616	88315	92239	94758	109901	123935	111098	117816
Operating profit	15781	19154	21067	20638	21082	25483	31177	37289	37551	38154
Other income (Net)	2625	3244	1809	2020	2008	2462	3890	4736	4179	4667
Profit before tax & extraordinary item	18406	22398	22876	22658	23090	27945	35067	42025	41730	42821
Profit after tax & extraordinary item	12625	15015	15221	15311	15153	18189	22684	30409	31079	32023
Other comprehensive income after tax	-	-	-	-	(129)	62	(63)	(418)	162	(72)
Total comprehensive income	12625	15015	15221	15311	15024	18251	22621	29991	31241	31951

Revenue from operations (₹ in Crores)



📈 6.0% 📈 3.5%

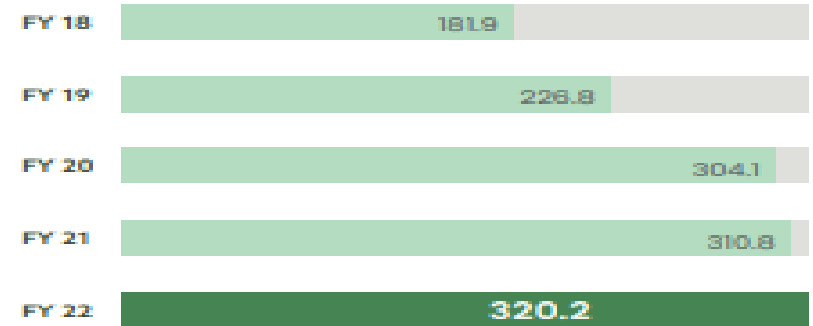
Earnings Per Share (₹)



📈 3.0% 📈 15.2%

📈 y-o-y 📈 5 year CAGR

PAT (₹ in Crores)



📈 3.0% 📈 15.2%

Dividend Per Share (₹)



📈 22.8% 📈 15.9%

Key Ratios

S. No.	Particulars	Numerator	Denominator	31 st March, 2022	31 st March, 2021
1.	Current Ratio (in times)	Current Assets	Current Liabilities	2.3	2.4
2.	Debt-Equity Ratio (in times)	Not Applicable			
3.	Debt Service Coverage Ratio (in times)	Not Applicable			
4.	Return on Equity (%)	Net profit after tax	Average Equity	31.8	36.0
5.	Inventory Turnover Ratio (in times)	Cost of goods sold	Average Inventory	1.7	1.6
6.	Trade Receivables Turnover Ratio (in times) *	Sales (on credit)	Average Trade Receivables	8.8	13.1
7.	Trade Payables Turnover Ratio (in times)	Purchases	Average Trade Payables	4.8	4.1
8.	Net capital Turnover Ratio (in times)	Sales	Working Capital (Total Current Assets less Total Current Liabilities)	2.4	2.0
9.	Net Profit Ratio (%)	Profit after tax	Sales	20.5	21.1
10.	Return on Capital employed (%)	Profit before tax	Capital Employed (Net worth less Deferred tax Assets)	40.7	45.6
11.	Return on Investments (%)	Income from Investments	Average Investments	4.2	4.3

Key Ratios Analysis

- The company has delivered a **poor sales growth** of **5.02%** over past five years. But the **Compounded Profit Growth has been 16%** over the last 5 years. Since the company enjoys pricing power, the sales volume has not increased by good rates but the company has increased its prices per stick to earn profits.
- Company is almost **debt free**.
- Company has a good **Return on equity** (ROE) track record: 3 Years ROE 36.0%
- **Dividend payout ratio** is **65%** - It was paying out quite a large proportion of its free cash flows. By paying out so much of its cash flows could indicate that the company has good reserves of cash and bank balance but limited opportunities for investment and growth.
- **Return on Capital Employed** : The ROCE measures the ability of a firm to generate profits from its total capital (shareholder capital plus debt capital) employed in the company. VST has **40.7%** ROCE for the latest year. The ROCE of the company has reduced sharply over the decade ,i.e., 62.3% in 2013 to 40.7% in 2022.
- **Inventory turnover ratio**: - Inventory Turnover ratio is an activity ratio and is a tool to evaluate the liquidity of a company's inventory. It measures how many times a company has sold and replaced its inventory during a certain period of time. VST Industries has an Inventory turnover ratio of **1.7 times** which shows that the management is **inefficient** in relation to its Inventory and working capital management.

Conclusion

Hold

- **VST Industries Limited** share price has fallen short of rise in market price, with a share price rise of 4.57% over five years, which is below the market return. The last year hasn't been great either, with the stock up just 8.39%.
- Markets are sometimes efficient, but prices do not always reflect underlying business performance. One imperfect but simple way to consider how the market perception of a company has shifted is to compare the change in the earnings per share (EPS) with the share price movement.
- Over half a decade, VST Industries managed to grow its earnings per share at 16% a year. The EPS growth is more impressive than the yearly share price gain of 4.57% over the same period. So it seems the market hasn't been so enthusiastic about the stock over the period.

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