

McLeod Russel (MCLRUS)

₹ 348

WHAT'S CHANGED...

PRICE TARGET.....	Unchanged
EPS (FY13E).....	Unchanged
EPS (FY14E).....	Unchanged
EPS (FY15E).....	Introducing at ₹33.6
RATING.....	Changed from Buy to Hold

Lower sales volume but prices remain firm...

McLeod Russel (MRIL) reported a 10.3% increase in its Q3FY13 revenues with margins sliding ~260 bps and earnings increasing by 5.2%. The results were below our expectation due to the lower than expected sales volume. Decline in margins was led by higher power, fuel and employee cost, which increased ~26% and ~15%, respectively. We believe the lower sales volume was due to lower exports though realisations in both domestic and international markets would be higher by ~₹ 20/kg YoY. Going ahead, with Q4 being a seasonally weak quarter for tea companies, we expect realisation from tea to slide to ~₹ 140/kg but remain higher by ~₹ 15/kg YoY. We have a **HOLD** recommendation on the stock.

Lower sales volume impacts growth

Tea realisation was higher by 13.7% to ₹ 173.9/kg in Q3FY13 with sales volume falling to 24.9 million kg (mkg) against 25.5 mkg in Q3FY12. We believe the slowdown in sales volume was higher in exports. MRIL reported ~1.8 mkg dip in own production in 9MFY13. Going ahead, the company plans to make up for the shortfall in sales quantity (~3.7 million kg in 9MFY13) through the purchase of bought leaves. Hence, with prices remaining firm (driven by all-time lowest India's inventory level) and volumes witnessing an up-tick, we expect earnings to increase ~20% and ~12% in FY14E and FY15E, respectively.

Lower domestic production to support prices in weak quarter

The industry witnesses no production in January-March with fresh crops coming from April onwards. Hence, prices witness a slide during Q4. In spite of declining prices on a QoQ basis, prices are expected to be stronger by ~₹ 10-15/kg YoY due to the lowest ever inventory level in the country on account of the overall production declining by ~5 mkg (up to November, 2012, as reported by Tea Board of India).

Stocks discount margin improvement; fairly valued at ₹ 340/share

Though we expect sales volumes to improve from here on and prices to remain firm at current levels (if not increase), we would prefer to wait and see how the prices open for the next season. Hence, we maintain our price target of ₹ 340 valuing MRIL at 11x FY14E EPS with **HOLD** rating.

Exhibit 1: Financial Performance (Standalone)

(₹ Crore)	Q3FY13	Q3FY13E	Q3FY12	Q2FY13	YoY(%)	QoQ(%)
Net Sales	434.1	479.8	393.7	439.1	10.3	-1.1
EBITDA margin (%)	31.4	32.4	34.0	55.6	-262bps	-2413bps
Depreciation	8.1	8.6	7.5	8.4	7.9	-3.2
Interest	14.1	8.1	9.4	12.2	49.8	15.8
Other Income	8.9	5.9	0.0	6.9	NA	28.8
Reported PAT	123.2	144.4	117.1	230.3	5.2	-46.5
EPS (₹)	11.3	13.2	10.7	21.0	5.2	-46.5

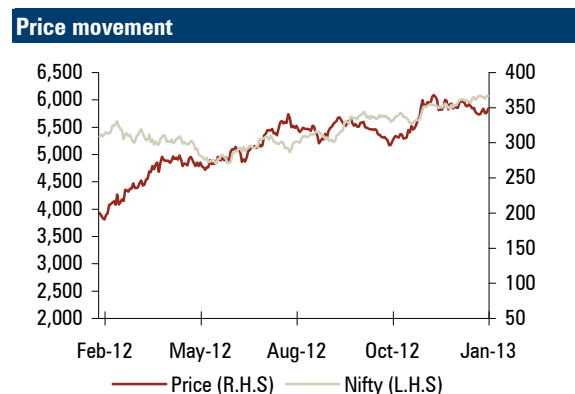
Source: Company, ICICIdirect.com Research

Rating matrix	
Rating	: Hold
Target	: ₹ 340
Target Period	: 12 months
Potential Upside	: -2 %

Key Financials (Consolidate)				
₹ Crore	FY12	FY13E	FY14E	FY15E
Net Sales	1,412.0	1,522.2	1,724.9	1,883.1
EBITDA	389.4	385.5	491.4	545.2
Net Profit	294.3	273.4	329.3	368.1
EPS (₹)	26.9	25.0	30.1	33.6

Valuation summary (Consolidate)				
	FY12	FY13E	FY4E	FY5E
P/E	11.3	12.2	10.1	9.1
Target P/E	13.8	14.8	12.3	11.0
EV / EBITDA	9.0	9.1	7.0	6.3
Price to Book Value	1.9	1.7	1.5	1.3
RoNW(%)	16.8	14.1	15.0	14.8
RoCE (%)	16.4	15.3	17.1	17.0

Stock data	
Market Capitalisation	₹ 3809 crore
Debt (FY12)	₹ 270 crore
Cash (FY12)	₹ 33.4 crore
EV	₹ 4046 crore
52 week H/L	372 / 178
Equity capital	₹ 54.7 Crore
Face value	₹ 5
MF Holding (%)	5.0
FII Holding (%)	33.6



Analyst's name	
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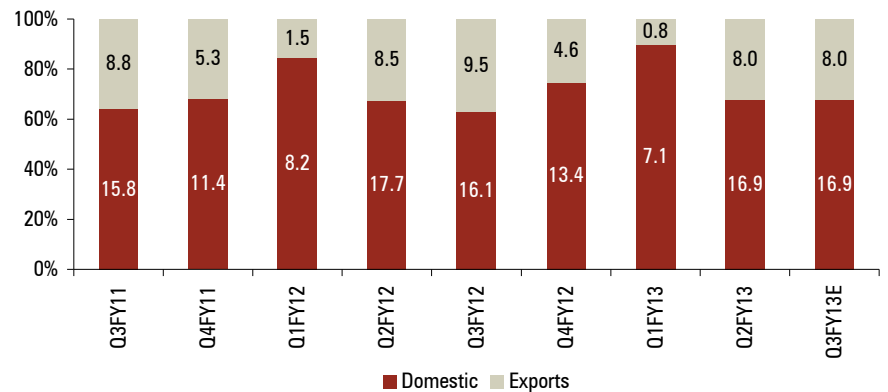
Exhibit 2: Assumptions

	FY11	FY12	FY13E	FY14E	FY15E
Sales volume (in million kg)	73.9	79.3	78.1	83.0	87.2
Domestic (in million kg)	52.9	55.3	54.9	58.1	61.0
Exports (in million kg)	21.0	24.0	21.1	24.9	26.1
Africa + Vietnam (in million kg)	20.8	22	24.5	24.5	25.5
Realization (₹ per kg)	144.7	149.6	163.5	172.4	179.5
Domestic (₹ per kg)	138.2	142.0	152.8	167.0	175.0
Exports (₹ per kg)	156.0	170.0	207.1	185.0	190.0
Production through leaf (in million kg)	9300	8000	8000	8000	8250
Employee cost (₹ per kg)	57.5	57.9	62.0	64.6	66.0

Source: Company, ICICIdirect.com Research

Exhibit 3: Domestic and export volume sales (in million kg)

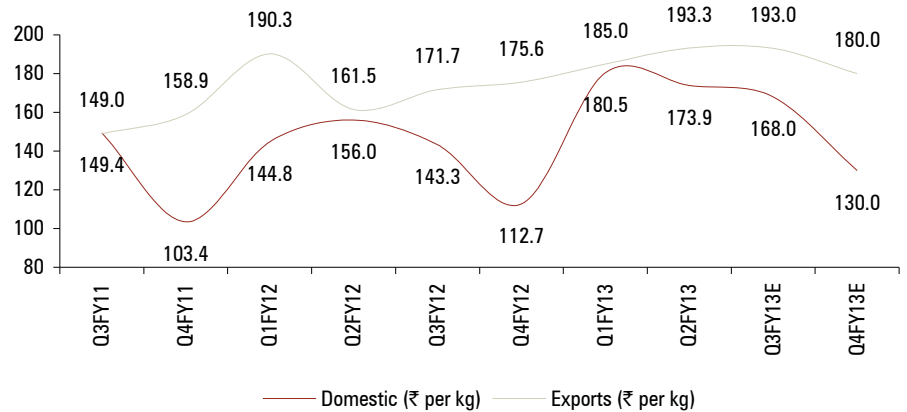
The YoY fall in export sales volume impacted sales growth during the quarter. The company attributes this slowdown in exports to the staggered shipment orders by buyers



Source: Company, ICICIdirect.com Research

Exhibit 4: Sales realisation (per kg) trend

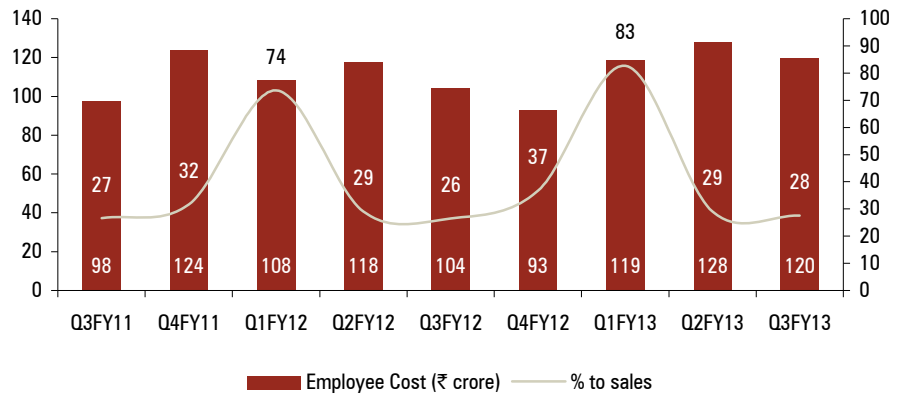
Prices in domestic and exports markets have remained firm due the global shortfall in the system. We expect prices to remain firm in FY14E if production does not catch up with the increasing rate of consumption



Source: Company, ICICIdirect.com Research

We believe that tea being a labour intensive industry and with the recent updates on the shortage of labour in tea gardens, employee cost for the company would continue to remain a concern. However, higher prices would aid in reducing its impact on margins

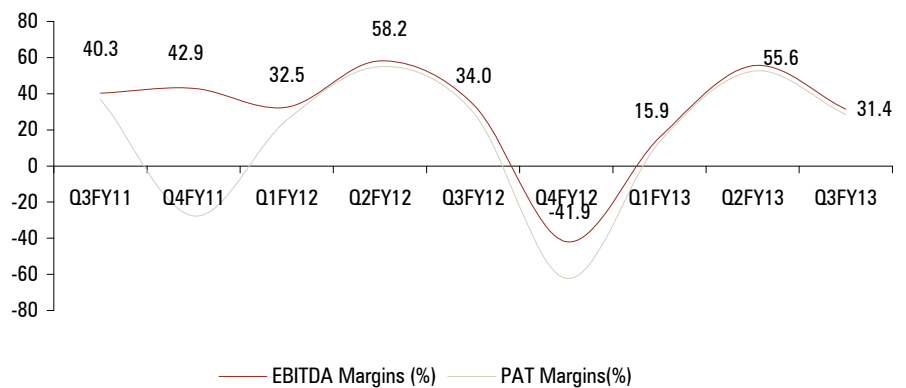
Exhibit 5: Employee cost trend



Source: Company, ICICIdirect.com Research

In spite of rising tea prices, margin expansion has been tough for MRIL. This is due to the increasing power, fuel and employee costs

Exhibit 6: EBITDA and PAT margins (%) trend



Source: Company, ICICIdirect.com Research

Revising Estimates

We are introducing the FY15E numbers, keeping our FY14E unchanged. We expect ~5% increase in sales volume to 87.2 mkg in India and 25.5 million kg from Africa operations for MRIL in FY15E over FY14E. However, we remain cautious on the realisation front expecting a marginal increase of only 4% both in India and Africa. Led by higher sales and improving realisations, we expect margins to remain at around 29% in FY15E in spite of increasing employee cost.

Exhibit 7: Revising Estimates

	FY14E Unchanged	FY15E Introduced
Revenue	1724.9	1883.1
EBITDA	491.4	545.2
EBITDA Margin (%)	28.5	29.0
PAT	329.3	368.1
EPS	30.1	33.6

Source: Company, ICICIdirect.com Research

Financial Summary

Exhibit 8: Profit & Loss Account

	(₹ Crore)			
(Year-end March)	FY12	FY13E	FY14E	FY15E
Total operating Income	1,445.3	1,557.2	1,761.7	1,921.7
Growth (%)	12.2	7.7	13.1	9.1
Raw Material Expenses	146.1	160.0	170.0	185.5
Power & Fuel Expenses	135.3	167.4	169.0	184.5
Employee Expenses	458.9	484.3	536.2	575.2
Marketing Expenses	70.0	70.8	84.5	92.3
Other expenses	245.7	289.2	310.5	339.0
Total Operating Expenditure	1,055.9	1,171.7	1,270.2	1,376.5
EBITDA	389.4	385.5	491.4	545.2
Growth (%)	2.4	-1.0	27.5	10.9
Depreciation	37.0	43.0	49.0	25.8
Interest	56.7	58.9	53.5	53.5
Other Income	41.1	41.9	27.8	0.0
PBT	336.7	325.5	416.8	465.9
Others	0.0	0.0	0.0	0.0
Total Tax	33.8	52.1	87.5	97.8
PAT	294.3	273.4	329.3	368.1
Growth (%)	18.1	-7.1	20.4	11.8
EPS (₹)	26.9	25.0	30.1	33.6

Source: Company, ICICIdirect.com Research

Exhibit 9: Cash Flow Statement

	(₹ Crore)			
(Year-end March)	FY12	FY13E	FY14E	FY15E
Profit before Tax	256.7	325.5	416.8	465.9
Add: Depreciation	0.0	43.0	49.0	25.8
(Inc)/dec in Current Assets	-65.2	-39.6	-240.1	-160.0
Inc/(dec) in CL and Provisions	28.9	-96.8	120.8	-1.0
Others	-6.2	-52.1	-87.5	-97.8
CF from operating activities	214.2	180.1	259.0	232.9
(Inc)/dec in Investments	0.0	0.0	0.0	0.0
(Inc)/dec in Fixed Assets	-113.5	-50.5	-98.0	-91.8
Others	42.5	-43.0	-49.0	-25.8
CF from investing activities	-71.0	-93.5	-147.0	-117.6
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	-39.8	10.0	-20.0	-20.0
Dividend paid & dividend tax	-58.8	-76.2	-76.8	-83.2
Inc/(dec) in Sec. premium	-45.1	0.0	0.0	0.0
Others	0.1	0.0	0.0	0.0
CF from financing activities	-143.7	-66.2	-96.8	-103.2
Net Cash flow	0.6	20.3	15.2	12.1
Opening Cash	31.0	33.4	53.7	69.0
Closing Cash	33.4	53.7	69.0	81.0

Source: Company, ICICIdirect.com Research

Exhibit 10: Balance Sheet (₹ crore)

(Year-end March)	FY12	FY13E	FY14E	FY15E
Equity Capital	54.7	54.7	54.7	54.7
Reserve and Surplus	1691.9	1889.1	2141.6	2426.4
Minority Share	11.7	11.7	11.7	11.7
Non-Current Liability				
Long Term Borrowings	94.0	104.0	84.0	64.0
Deferred Tax Liabilities (Net)	76.9	76.9	76.9	76.9
Long term Provisions	71.9	71.9	71.9	71.9
Current Liabilities				
Short term Borrowings	104.0	104.0	104.0	104.0
Trade Payable	73.1	33.8	95.8	94.2
Other current Liabilities	120.9	130.4	147.7	161.3
Short term provisions	162.0	95.1	136.5	123.7
Total Liabilities	2,461.2	2,571.6	2,924.9	3,188.8
Fixed Assets	1895.3	1925.3	1995.3	2065.3
Tangible Assets	1615.7	1635.7	1675.7	1715.7
Intangible Assets	244.2	244.2	264.2	284.2
Capital WIP	31.4	31.4	31.4	31.4
Intangible assets UD	4.0	14.0	24.0	34.0
Non current assets	19.0	19.0	19.0	19.0
Long term Loans and Advances	151.6	163.5	185.2	202.2
Other non-currents assets	37.8	46.5	52.7	57.5
Current Assets	357.5	417.4	672.7	844.7
Inventory	124.8	169.1	215.6	261.5
Trade Receivable	29.7	84.6	143.7	183.1
Cash & Bank	33.4	53.7	69.0	81.0
Short-term Loans & Liability	127.5	63.4	191.7	261.5
Other current assets	42.1	46.5	0.0	0.0
Application of Funds	2,461.2	2,571.6	2,924.9	3,188.8

Source: Company, ICICIdirect.com Research

Exhibit 11: Ratio Analysis

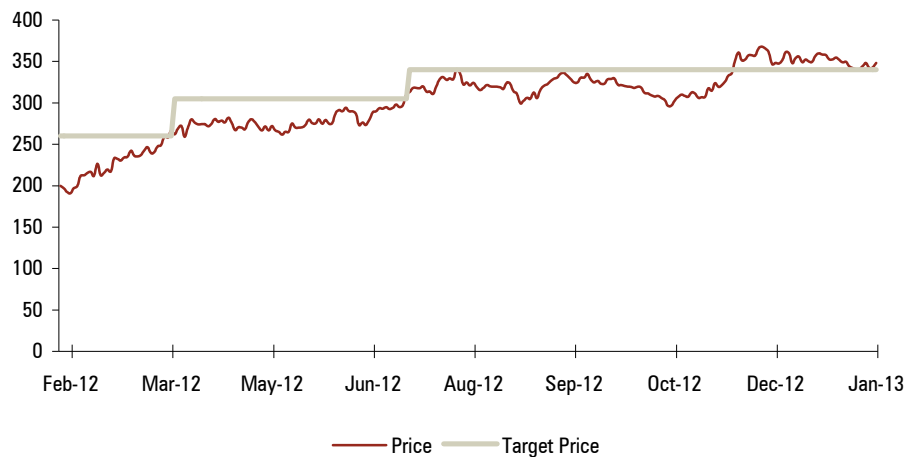
(Year-end March)	FY12	FY13E	FY14E	FY15E
Per share data (₹)				
EPS	26.9	25.0	30.1	33.6
Cash EPS	30.3	28.9	34.6	36.0
BV	159.6	177.6	200.7	226.7
DPS	7.0	7.0	7.0	7.6
Cash Per Share	0.6	1.0	1.3	1.5
Operating Ratios (%)				
EBITDA Margin	27.6	25.3	28.5	29.0
PBT / Total Operating income	23.2	32.0	32.0	32.0
PAT Margin	20.8	18.0	19.1	19.5
Inventory days	31.8	40.0	45.0	50.0
Debtor days	7.6	20.0	30.0	35.0
Creditor days	18.6	8.0	20.0	18.0
Return Ratios (%)				
RoE	16.8	14.1	15.0	14.8
RoCE	16.4	15.3	17.1	17.0
RoIC	15.1	12.4	13.3	13.2
Valuation Ratios (x)				
P/E	12.9	13.9	11.6	10.3
EV / EBITDA	10.2	10.3	8.0	7.1
EV / Net Sales	2.8	2.6	2.3	2.1
Market Cap / Sales	2.7	2.5	2.2	2.0
Price to Book Value	2.2	2.0	1.7	1.5
Solvency Ratios				
Debt/EBITDA	0.1	0.1	0.1	0.1
Debt / Equity	0.5	0.5	0.4	0.3
Current Ratio	0.8	1.1	1.4	1.7
Quick Ratio	0.7	1.0	1.2	1.6

Source: Company, ICICIdirect.com Research

Company Description

McLeod Russel India (MRIL) is the largest tea plantation company in the world with a consolidated production capacity of ~100 million kg of tea per year. They have tea estates in Assam, West Bengal, Vietnam, Uganda and Rwanda. MRIL owns more than 59 high quality tea estates spread across 35,971.3 hectares in Assam and some in the Dooars region of West Bengal. Additionally, in 2008-09, the company forayed into Vietnam and Africa through the acquisition of Phu Ben Tea Co (US \$7 million) and Olyana Holdings LLC, US (US \$2.75 million), respectively, through its UK based subsidiary Borelli Tea Holdings Ltd. The Phu Ben Tea Co and Olyana Holdings have a production capacity of 4.5 million kg and 1.7 million kg of tea per annum, respectively. The bulk tea produced by the company is sold via auctions and direct sales in India. MRIL also exports about one-third of its production to UK, Middle East, CIS, etc.

Exhibit 12: Recommendation History



Source: Company, ICICIdirect.com Research

Exhibit 13: Recent Releases

Date	Event	CMP	Target Price	Rating
26-Mar-12	Event Update	262	305	BUY
4-Apr-12	Q4FY12 Preview	274	305	BUY
27-Nov-12	Q4FY12 Result Update	351	340	HOLD
5-Jul-12	Q1FY13 Preview	313	340	HOLD
31-Jul-12	Q1FY13 Results	321	340	HOLD
8-Oct-12	Q2FY13 Preview	321	340	HOLD
1-Nov-12	Q2FY13 Result Update	310	340	BUY
8-Jan-13	Q3FY13 Preview	322	340	HOLD

Source: Company, ICICIdirect.com Research

ICICIdirect.com Universe (Tea)

Sector / Company	CMP		Rating	M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)			FY12	FY13E	FY14E	FY12	FY13E	FY14E	FY12	FY13E	FY14E	FY12	FY13E	FY14E	FY12	FY13E	FY14E
Jayshree Tea (JAYTEA)	117	120	Hold	338	5.0	22.1	19.1	23.6	5.3	6.1	14.5	6.3	7.3	7.0	4.0	11.1	3.9	15.8	12.0
McLeod Russel (MCLRUS)	348	340	Hold	3,809	26.9	25.0	30.1	12.9	13.9	11.6	10.2	10.3	8.0	16.4	15.3	17.1	16.8	14.1	15.0

Source: Company, ICICIdirect.com Research

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Strong Buy: >15%/20% for large caps/midcaps, respectively, with high conviction;

Buy: > 10%/ 15% for large caps/midcaps, respectively;

Hold: Up to +/-10%;

Sell: -10% or more;



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