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Formidable Franchise at cheap valuations

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What does KRBL do?

KRBL is into selling of branded Basmati rice.



What is Basmati rice?

- Rice is an agricultural commodity
- Total Production of rice in the world (2017-18) was 487 Mn Ton
- Total Basmati rice production in India (2017-18) = 9 Mn Tonnes (2% of global rice production)

What is Basmati Rice?

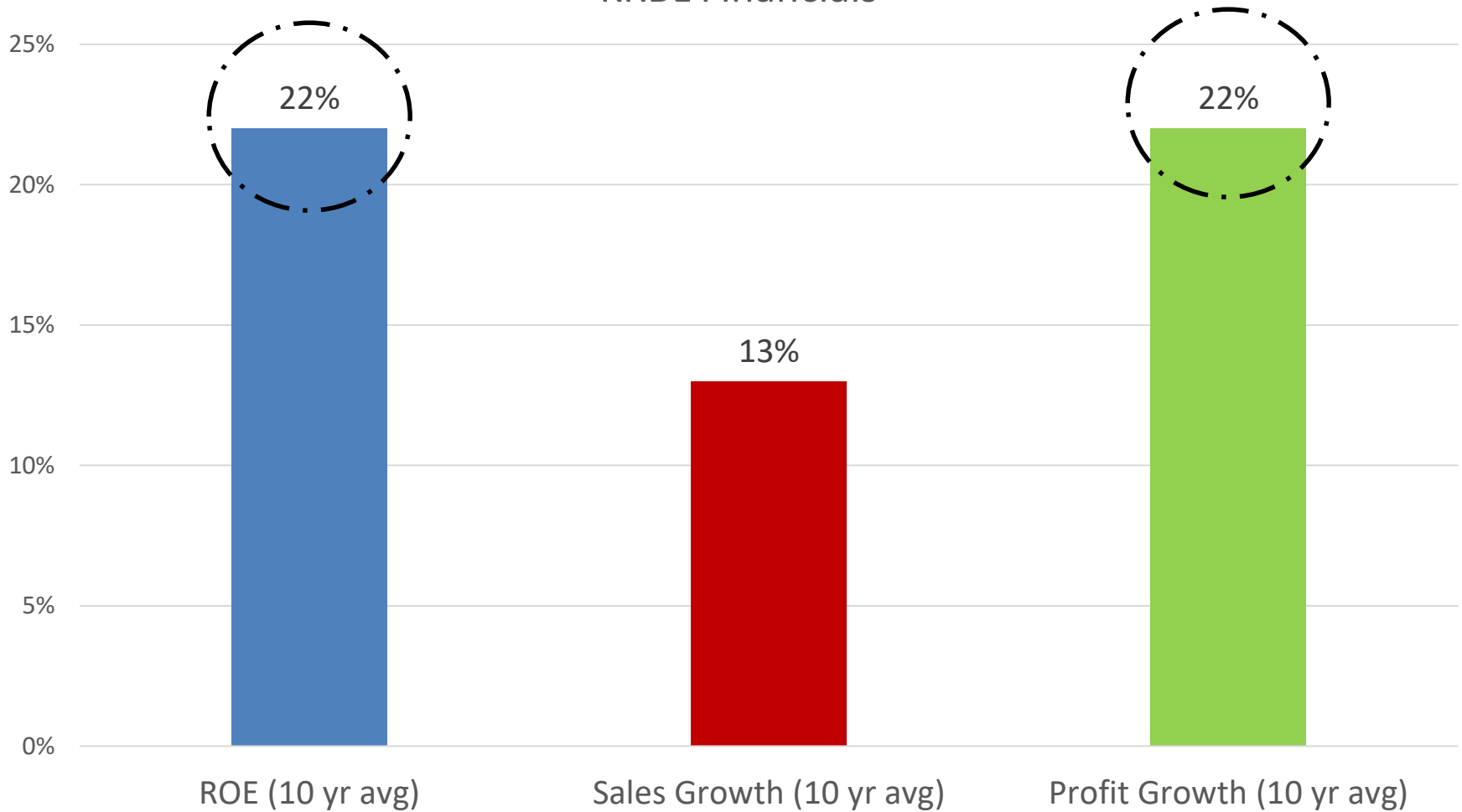
- Basmati rice is a premium variety of rice, preferred by millions of consumers over other varieties of rice.

What is unique about Basmati rice?

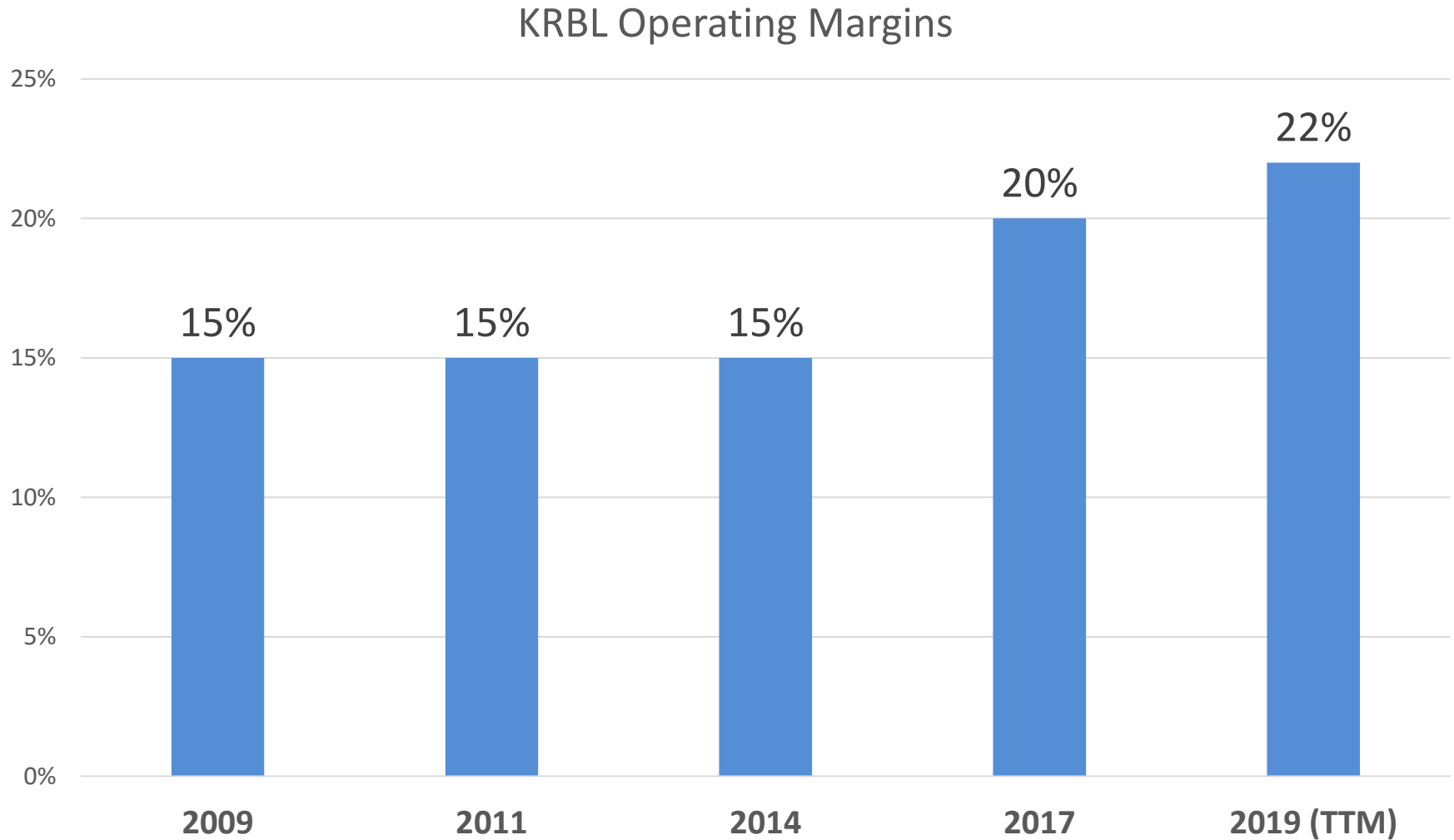
- Basmati is a long-grained aromatic rice
- Basmati rice is a GI (geographical indication) tagged product produced in the Gangetic plains – i.e. only in India and Pakistan

KRBL Story in numbers ...

KRBL Financials

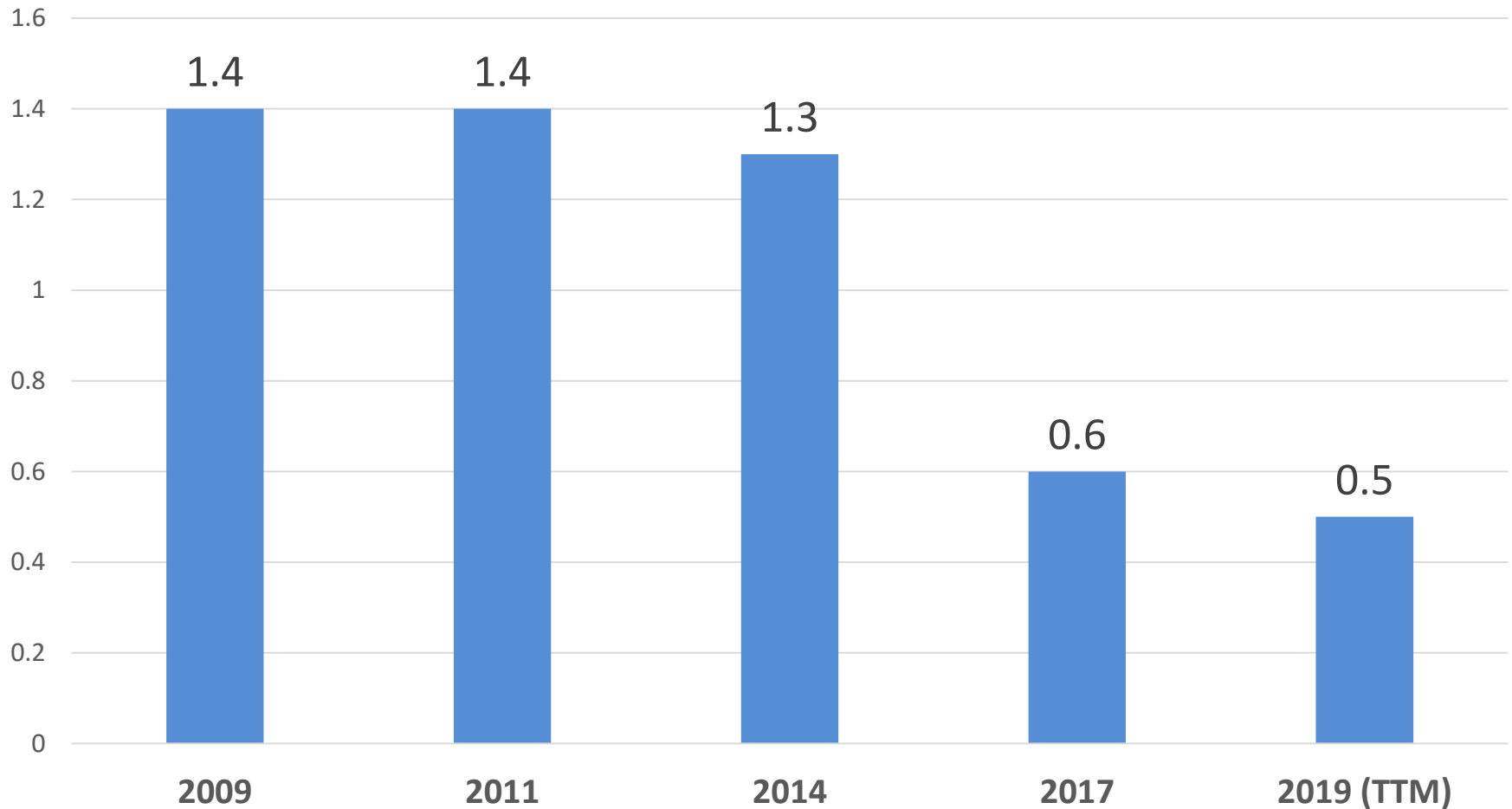


KRBL Operating Margins (Continuous improvement)

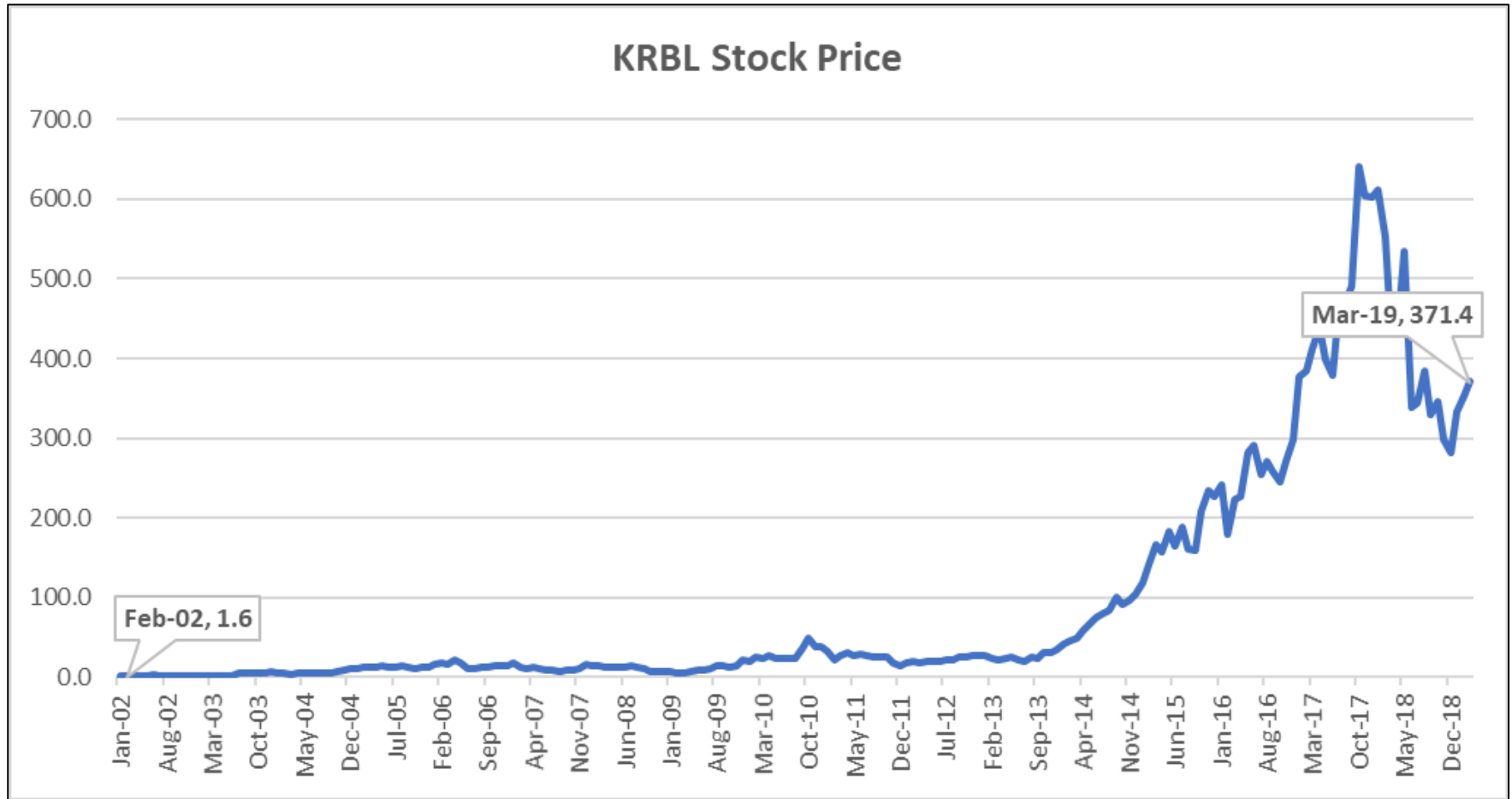


Debt to Equity Ratio – Steady Improvement

KRBL Debt to Equity Ratio



Wealth Creation – KRBL Ltd

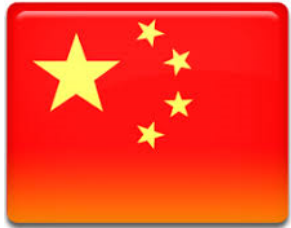


KRBL has gone up 230 times in the last 16 years

What is the market for Basmati rice?

- The major rice eating regions of the world include

Sticky Rice



China, Japan, South East Asia

Non-sticky rice



India, Africa, Gulf Countries

- On top of this, each region has their own varieties of rice
- Each region's consumer has their own preferences of rice variety.
- Basmati rice is an aspirational product for consumers in
 - India, Gulf countries and Africa

How India became the Basmati King

- Basmati rice is traditionally grown in India since centuries
- However, Basmati is a difficult crop to grow and it remained luxury food for the rich for a long time
- Traditional Basmati varieties grow very tall – up to 1.5 m
- Lodging due to strong winds is quite common



Invention of PUSA 1121

- Around 2003, the Indian Agricultural Research Institute (IARI) made a new type of Basmati – PUSA 1121 through hybridization process

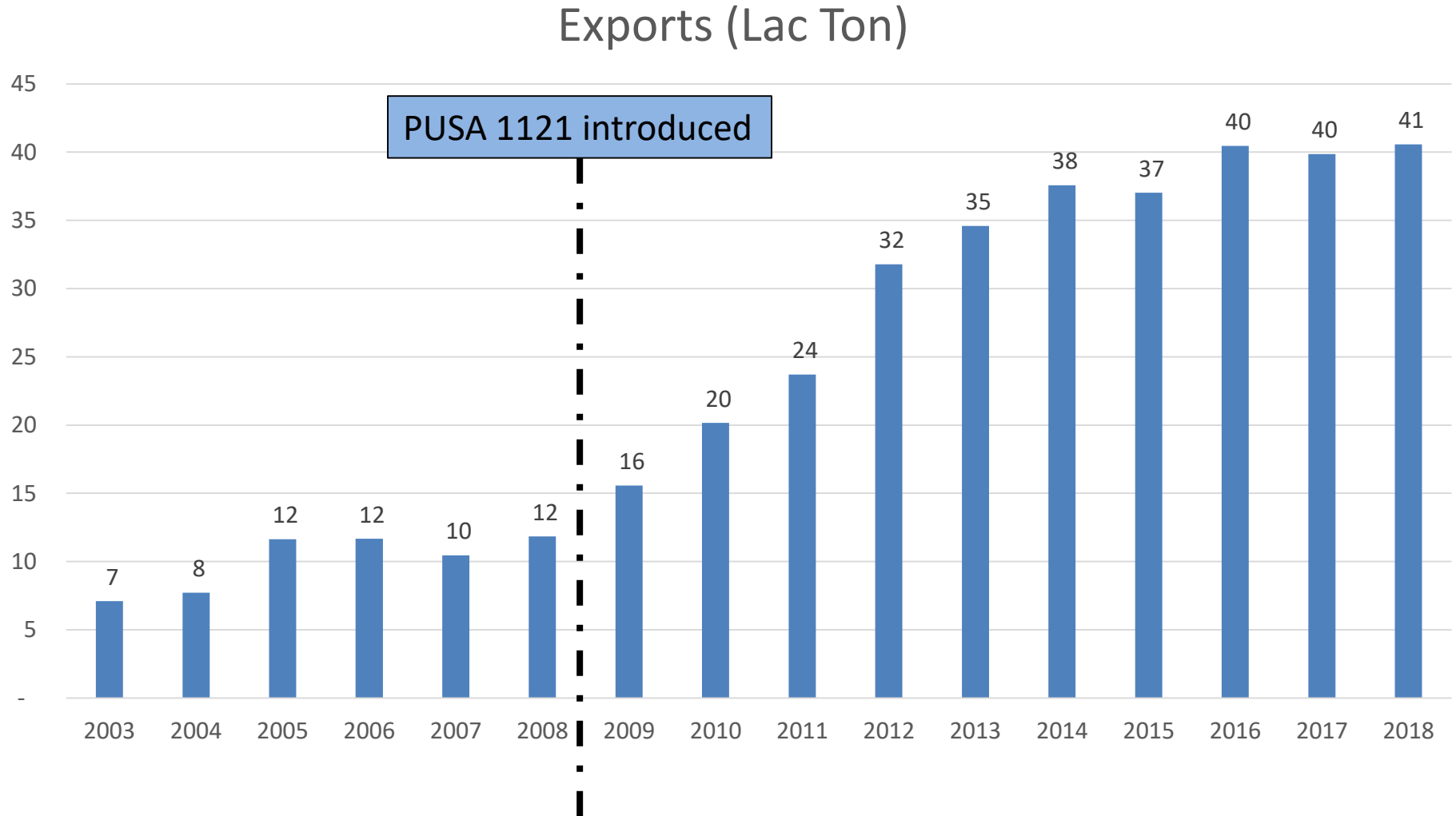
	Traditional Basmati	PUSA 1121
Height	1.5 m	1.2 m
Maturity Time	160 days	140 days
Water Requirement	5000 Ltr/Kg	1000 Ltr/Kg
Yield	2.5 Ton/Ha	12 Ton/Ha

- Invention of PUSA 1121 transformed Basmati farming
- However, there was one more problem
- PUSA 1121 seed was not recognized as Basmati since its immediate parent was not a traditional Basmati seed

India becomes Basmati rice bowl of the World

- Scientific definition of Basmati formalized in 2005
 - Length 6.61-7.5 mm or more
 - Length to width ratio > 3
 - On cooking – Length should increase by 2 times or more
 - Cooked rice – should have distinct aroma, grains should be separate
- PUSA 1121 was notified as Basmati rice in 2008
- KRBL had already positioned itself to benefit from this notification
- In the next 10 years, India's share in global Basmati exports significantly increased

Indian Basmati – Growth in Exports



KRBL – Farm to Plate

- KRBL is present across the entire Basmati rice value chain
- Right from seed development to procurement to rice milling to rice grading/packaging to branded retailing
- KRBL was the pioneer in the development of PUSA 1121 seed
- KRBL has a 300 Ha seed development farm
- It has a program of contact farming with 90,000 farmers



KRBL – Basmati Rice Procurement

- Basmati rice is grown only during May to October.
- All the procurement happens in the months of Oct/Nov
- Procurer has to judge on the spot paddy quality, yield and price



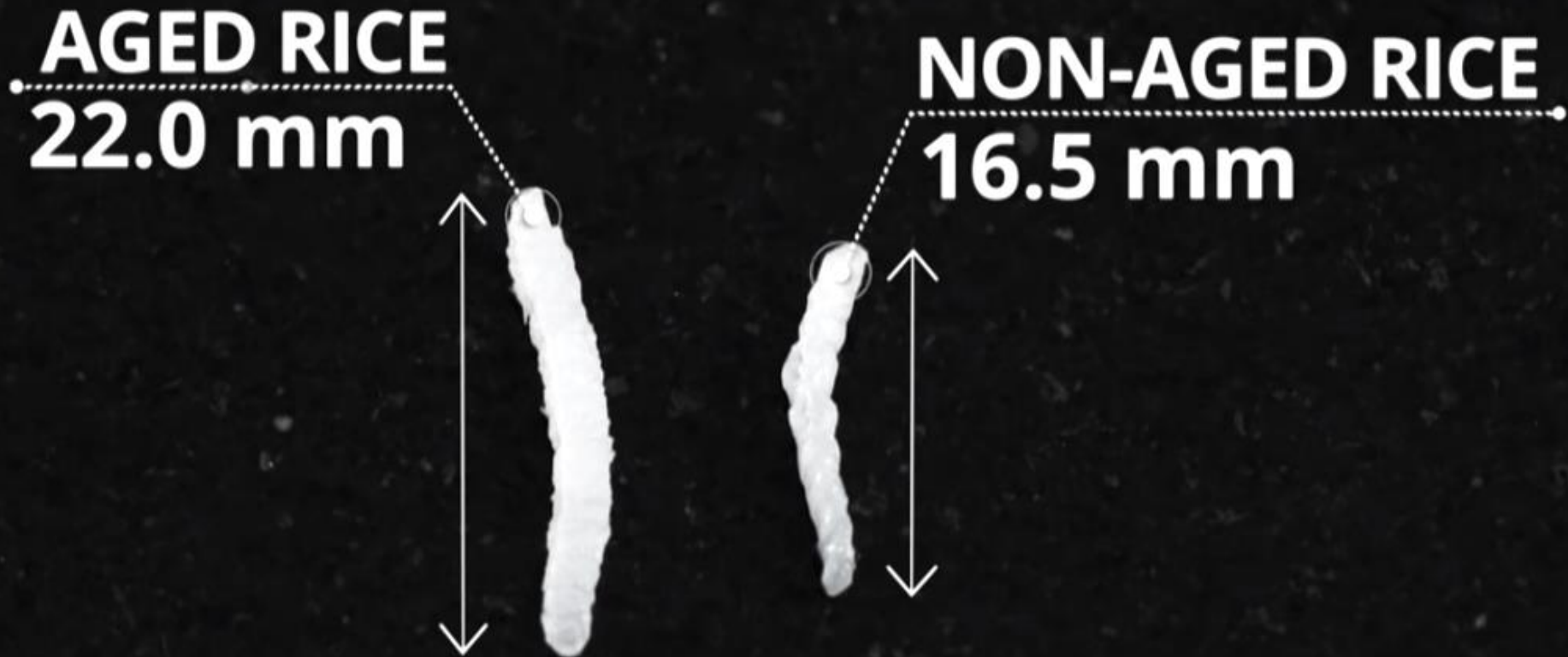
KRBL – Unloading, testing

- Procurement season consisting of only 2 months means unloading, quality testing, grading of the procured paddy is a massive exercise



KRBL – Ageing of rice

- Characteristics of Basmati rice enhance significantly if ageing is carried out – i.e. stored in warehouses for 2 years

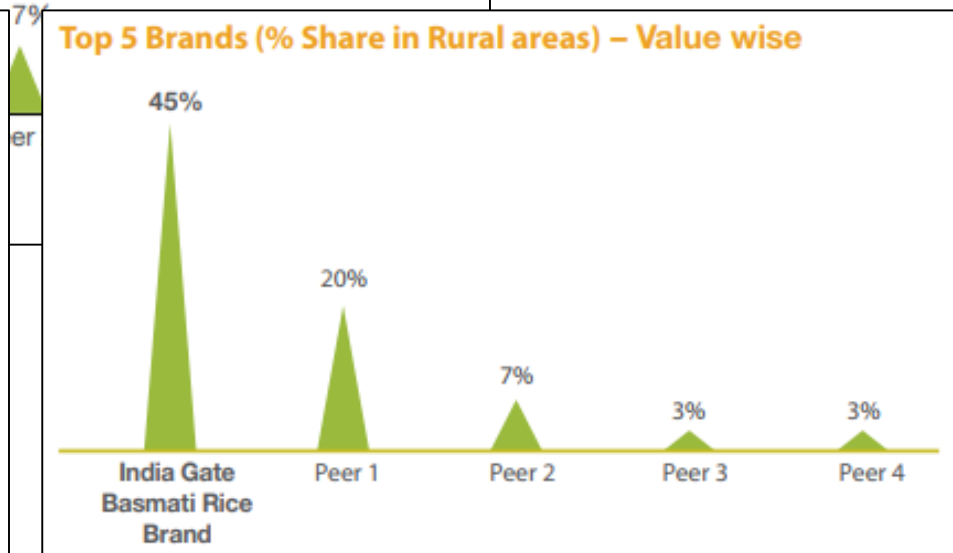
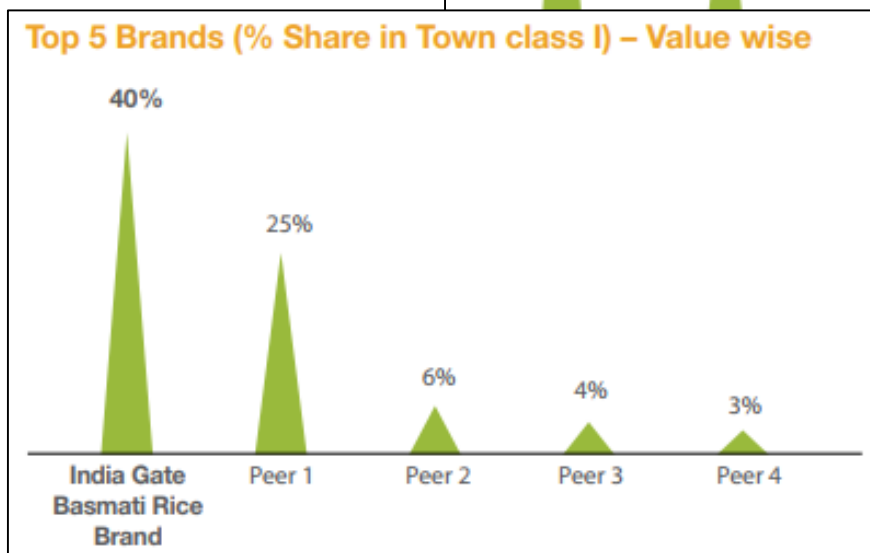
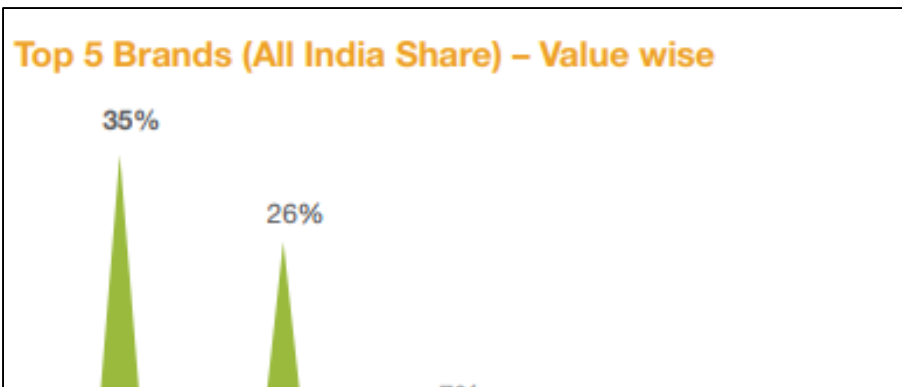




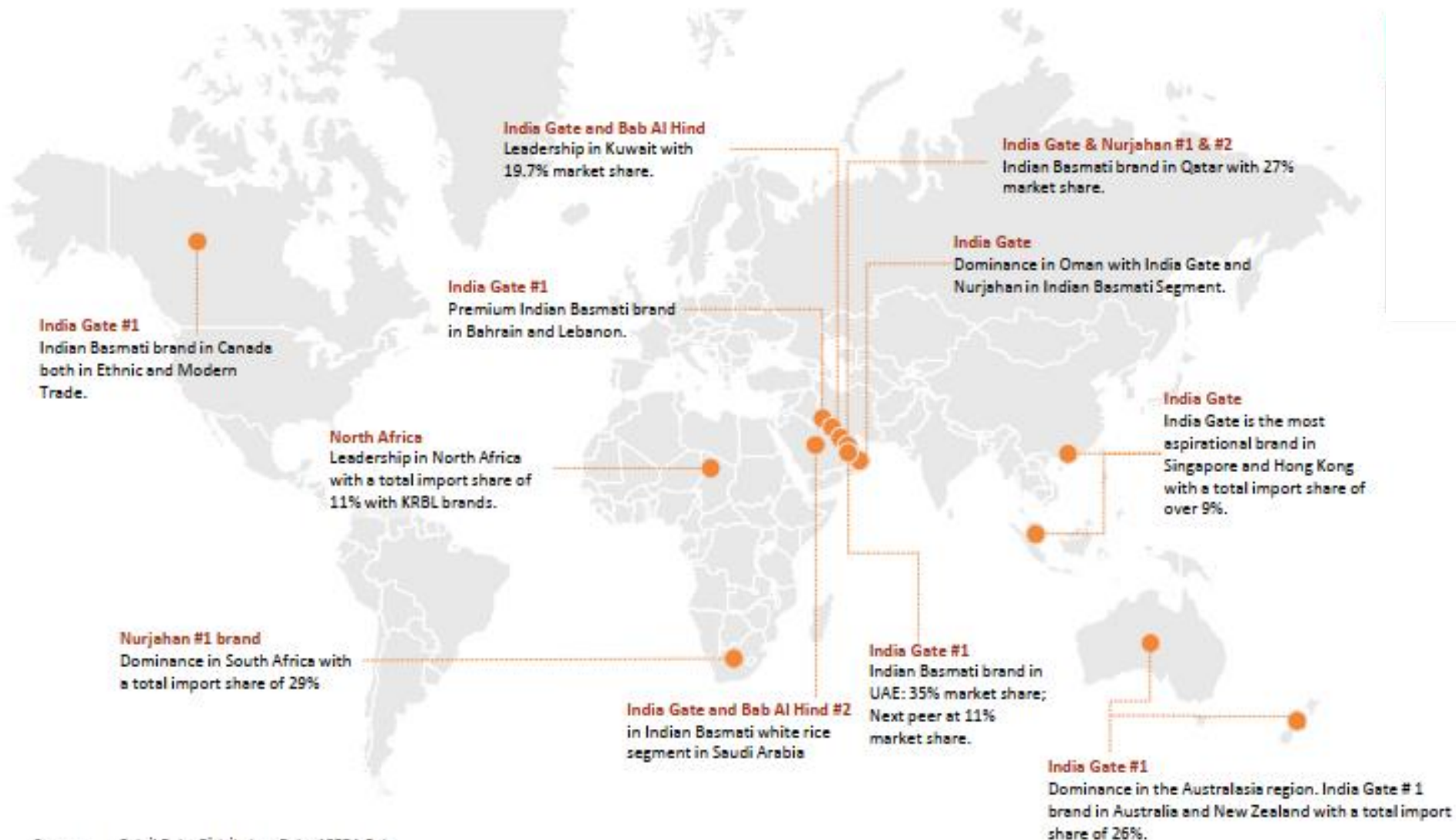
KRBL – Brands



KRBL Market Share in India



The strength of KRBL Brand



Source: Retail Data, Distributors Data, APEDA Data

KRBL – Presence across price points



How is Basmati rice sold?

Traditional Retail



- Shopkeeper has direct influence on customer choice
- Customer is physically away from the product he buys
- Brand naturally plays a smaller role
Shopkeeper's recommendation given weightage

Modern Retail



- Customer makes his own choice of the product/brand.
- Naturally, customer automatically makes a choice based on brand, quality, aroma apart from just price
- Organized brands have an advantage

Peers of KRBL (India Gate Basmati)

Extract from QIP document of LT Foods (Daawat Brand)

Competition

We face competition from other large basmati rice companies including KRBL Limited, Kohinoor Foods Limited, Lakshmi Energy & Foods Limited and various smaller unorganized processors. As basmati rice is a product that is protected by geographic indications internationally, we face limited competition on a global scale. However, we face competition from a few basmati rice companies in Pakistan which contributes approximately 10% of the world's basmati rice (Source: ICRA Report). In addition, certain types of fragrant rice

- In India, 50% of the market is with unorganized players
- It is interesting to note that the big multi-national FMCG players have not been successful in Basmati rice segment

HUL signs agreement with LT Foods for the sale of its Rice brands Gold Seal Indus Valley & Rozana

17-03-2016

The deal envisages transfer of the brands and inventory for a consideration of Rs 25 Crores,

HUL began exporting premium Basmati rice in 1985 under the brand 'Gold Seal Indus Valley' to various countries in the Middle East and Europe, which was subsequently extended to other brands and geographies. With the business operating across 21 countries, the current portfolio comprises

Peer comparison

	KRBL	Kohinoor	LT Foods	Chaman Lal Setia	Lakshmi
Operating Margins	22%	3%	10%	9%	-46%
Return on Equity (10 year avg.)	22%	6%	14%	27%	-ve
Debt to Equity Ratio	0.5	-ve networth	1.3	0.4	2
PAT Growth (10 yrs.)	22%	Loss	14%	23%	N/A

- Amongst its peers, KRBL has the best financial profile.
- Chaman Lal Setia comes close but, let us look at what Chaman Lal Setia has to say about KRBL

Competition speaking on KRBL

This is what a KRBL competitor – Chaman Lala Setia had to say about KRBL in one of the earnings calls on 11th Jun 2018

Q – With increasing spends on advertising, what is your estimate about margin improvement? (11th Jun 2018; Min 86:00 onwards)

Ans – KRBL with its branded products is able to command a higher price of around Rs 3 /Kg (5-10% higher realization). We are making margins of around 10% whereas KRBL is able to make margins of 20%. So, scope for improving margins is considerable.

Q – What was the impact of the newly introduced GST? (Min 68:00 onwards)

And – There is 0% tax on rice. Only branded rice attracts 5% GST.

We sell to wholesalers who want unbranded rice. India Gate (KRBL) and Daawat (LT Foods) brands are winners and retailers have to stock these brands because they sell

Basmati Consumption Patters in India

Though precise data is not easily available, we can derive intelligent estimates (for 2018)

Basmati Paddy Production (A)	9 Mn Tons
De-husked rice recovery (Est at 70%) (B)	6.3 Mn Tons
India's Population (C)	1.3 Bn people
Basmati Rice Export (E)	4.1 Mn Tons
Domestic Consumption (D)	2.2 Mn Ton
Per Capita Rice consumption (Actual)	75 Kg
Per Capita <u>Basmati Rice</u> consumption (Est)	=D/C = 1.7 Kg

This means Indian middle class (20% of population) eats Basmati rice 7 weeks out of 52 weeks in the year

Consumption Trends in India

Table 4: Middle class consumption - top 10 countries, 2015, 2020, and 2030 (PPP, constant 2011 trillion \$ and global share)

Country	2015	Share (%)	Country	2020	Share (%)	Country	2030	Shares (%)
U.S.	4.7	13	China	6.8	16	China	14.3	22
China	4.2	12	U.S.	4.7	11	India	10.7	17
Japan	2.1	6	India	3.7	9	U.S.	4.7	7
India	1.9	5	Japan	2.1	5	Indonesia	2.4	4
Russia	1.5	4	Russia	1.6	4	Japan	2.1	3
Germany	1.5	4	Germany	1.5	4	Russia	1.6	3
Brazil	1.2	3	Indonesia	1.3	3	Germany	1.5	2
U.K.	1.1	3	Brazil	1.2	3	Mexico	1.3	2
France	1.1	3	U.K.	1.2	3	Brazil	1.3	2
Italy	0.9	3	France	1.1	3	U.K.	1.2	2

Homi Kharas, Brookings Institute, Working Paper 100; Feb 2017

- Various studies suggest Indian middle class consumption is expected to increase rapidly in the next decade
- Basmati supply rather than demand will remain the constraint

Valuation – KRBL

Market Cap (27.03.2019)	\$ 1.2 Bn
(Inventory – Net Debt)	=(0.48-0.22) \$ Bn = \$ 0.26 Bn
Enterprise Value (EV)	\$ 0.92 Bn
Operating EBIT	\$ 110 Mn
Adj. EBIT*	\$ 98 Mn
EV/EBIT multiple	9.2

KRBL is available at a valuation of 9 times operating earnings

*Assuming KRBL operating margin falls from 22% to 20%.

What are the risks?

Risk No. 1

- Cum PAT over 10 yrs. = Rs 2,217 Cr
- Cum FCF over 10 yrs. = Rs 130 Cr
- KRBL seems to be guzzling cash

- Where is the problem? Usual suspects?
 - Receivable Days has stayed between 30-40 days in last 10 yrs.
 - Inventory Turnover has stayed between 1.5-2.0 in last 10 yrs.
 - Fixed Assets: Increased from 217 Cr (2009) to 982 Cr (2018)
- Basmati rice needs ageing to enhance its aroma and its taste. As KRBL grows, its working capital needs increase
- Taking advantage of capital subsidies and tax breaks, KRBL invested in renewable energy ~ Rs 700 Cr

What are the risks?

Risk No. 2

- Tax Demand Notice of Rs 1169 Cr Equivalent to 2 years of PBT
- The tax demand notice pertains to disallowance of paddy rice purchases from farmers for the years 2010 to 2017
- The management position is that since the said purchases were made directly from farmers of Uttar Pradesh state, the payment was made in cash. KRBL also has 3rd party documentary evidence to support the purchases.
- Similar payments for paddy rice purchases from the states of Punjab and Haryana were made through banking channels because middle men were involved (as required by State Law)

What are the risks?

Risk No. 3

KRBL drops 18% after ED arrests former director in Agusta scam

Former director Gautam Khaitan has reportedly been arrested by ED in connection to the AgustaWestland helicopter scam.

June 25, 2018 14:25 IST | India Infoline News Service

- The former director was made to resign from the board in Apr-2014 when his name first figured in the VVIP Chopper scam
- It is also alleged that one of the step-down subsidiaries was used to route the slush funds by the middlemen

What are the risks?

Risk No. 4

- Interest-Free loans from the directors to KRBL

Rs Cr	2014	2015	2016	2017	2018
Interest free loans by directors to KRBL	0	35	49	55	49

- KRBL has a strong balance sheet and existing outstanding loans from reputed financial institutions
- Why KRBL needs interest free loans from its directors is a mystery

To summarize

A high quality franchise with

- Superior execution to peers
- Better than industry financial metrics (ROE, debt profile, profitability etc.)
- Established brands across the globe
- Admired by peers
- In an industry which is structurally growing
- Leading position in the high potential domestic market

Available at a earnings multiple (EV/operating EBIT) of 9

THANK YOU

Valuation – KRBL

Market Cap (27.03.2019)	Rs 8125 Cr
(Inventory – Net Debt)	=3365-1560 = Rs 1805 Cr
Enterprise Value (EV)	Rs 6320 Cr
Operating EBIT	Rs 758 Cr
Adj. EBIT*	Rs 689 Cr
EV/EBIT multiple	9.2

KRBL is available at a valuation of 9 times operating earnings

*Assuming KRBL operating margin falls from 22% to 20%.