

DAIRY INDUSTRY INSIGHTS- INDIA



RASHESHWAR

CONSULTANTS PRIVATE LIMITED

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1) India Dairy Industry

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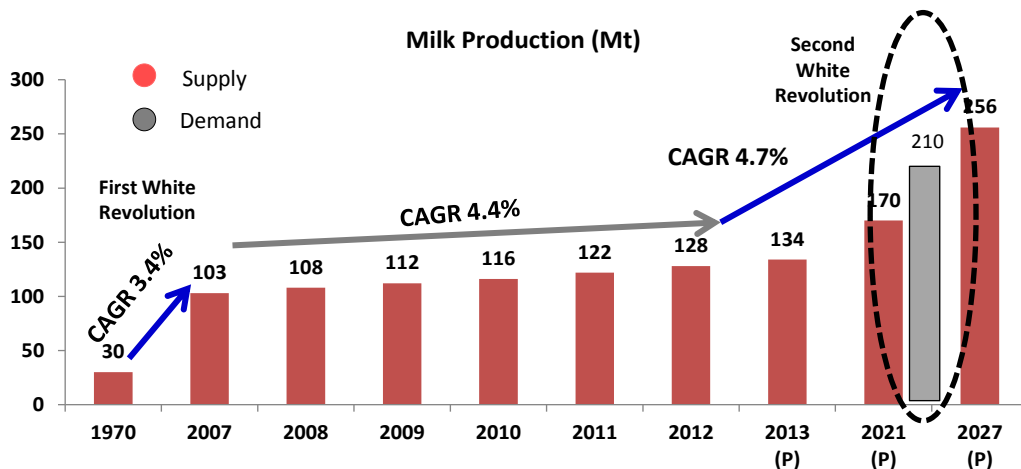
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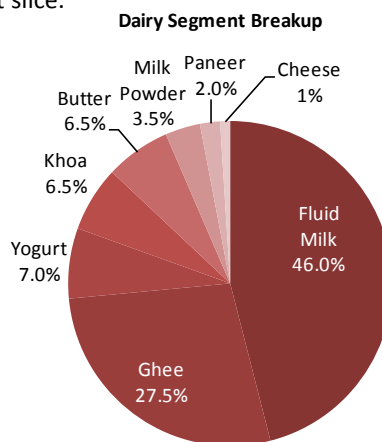
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- **World's Largest producer of dairy products:** India is the world's largest producer of dairy products by volume, accounting for about 17% of the world's total milk production and housing the world's largest dairy herd. India has neither been an active importer nor an exporter of dairy products. The country's share in global trade is at minor levels of 0.3% and 0.4% of exports and imports respectively, directly attributed by the fact that India is also the world's largest consumer of dairy products, consuming almost 100% of its own milk production.
- **First & Second White Revolution:** From producing 30 Mn tons of milk per annum in 1970 to producing 128 Mn tons in 2012, India's dairy industry has come a long way post independence. The credit can largely be given to the **"First White Revolution"** post 1970 where we saw a strengthening of production, procurement, infrastructure and technology transfer within this industry. India expects to double its milk production by 2027 with the launch of the National Dairy Plan (NDP) in 2012 which is a multi-state initiative implemented to increase the productivity of existing animals through a focused programme for breeding and feeding. This initiative is being called the **"Second White Revolution"**. The government plans to spend INR 22.42 Bn for the first phase of this scheme lasting 6 years.
- **Demand & Supply:** Today, this sector is characterized by high fragmentation. It is dominated by the unorganized sector which controls approximately 80% of the total market, comprising of almost 70 Mn households. Over the last decade, India experienced strong growth in demand (8%) for milk and dairy products which was approximately twice of supply (3-4%), driven largely due to a rise in disposable income. This demand for milk is expected to touch 210 Mn tons by 2021, while the supply is touted to be at 170 Mn tons by 2021, hence making India a net importer. The dairy industry is currently estimated to have reached a market size of more than USD 48.5 Bn and is anticipated to reach USD 118 Bn by 2017.



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- **Dairy Product Mix:** The Dairy Industry is expected to grow at a rate of 3-4% over the next few years. However, the value added products are expected to grow at a higher rate, especially cheese and frozen yogurt which are expected to grow at a rate of 20-25%. The Dairy Industry constitutes a wide portfolio of products illustrated below with fluid milk constituting the largest slice.



- **Ghee:** It is expected to grow at a CAGR of 14% from FY11 to FY17.
- **Yogurt:** The organised yogurt currently with a market size of INR 7,500 Mn is expected to be INR 12,000 Mn by 2015 growing at a CAGR of 40 - 45%. Within this segment frozen yogurt market expected to grow at a CAGR of 70 -80% over the next three years.
- **Khoa & Butter:** India produces ~1.5 Mn tons of Khoa annually (FY12). Both khoa and butter have a market share of 6.5%.
- **Milk Powder:** Price of skimmed milk powder in 2010 was INR 120 per kg in the wholesale market and currently stands at INR 230 per kg i.e. an increase of nearly 92% in three years.
- **Paneer:** 80% of paneer is sold as loose paneer by local Milk Vendors. About 5% milk of total milk production in India is converted into paneer.
- **Cheese** market is expected to grow at a rate of 25% per annum. Currently, out of the over 3,000 varieties of cheese available across the world only 30-40 are manufactured or sold in India with only 5% household penetration.

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■ Industry Growth Drivers

- ❑ Growing income and consumption
- ❑ Rapid urbanization
- ❑ Favourable demographics

■ Industry Challenges

- ❑ Inadequate supply of feed and fodder
- ❑ Shortage of cold storage units
- ❑ Poor supply chain and distribution facility
- ❑ Rise in packaging costs
- ❑ Volatile milk prices

II) Profitability & Valuation of Dairy Sector Companies

- The gross margins in the fluid milk business are very minuscule whereas the value added products like cheese, yogurt, ice creams etc. have gross margins going up to 20% to 25%. The EBITDA margins in this sector range between 6% to 10%.
- The raw material cost i.e. the milk prices constitute the major part of the operating expenses. The dairy business is highly sensitive to these prices which have been quite volatile in the last year. The rise in raw material prices is gradually passed on to the customers thereby maintaining the overall margins.

Comparable Companies										INR Mn		
Company Name	Net Sales	EBITDA			PAT	Market cap	Debt	Cash	EV	Sales x	EBITDA x	P/E x
		EBITDA	Margin									
Nestle India	91,011	19,683	21.6%	11,171	4,82,141	11,895	7,494	4,86,543	5.3	24.7	43.2	
Kwality Dairy	42,819	2,404	5.6%	1,053	7,437	8,628	324	15,741	0.4	6.5	7.1	
Hatsun Agro	24,514	1,823	7.4%	838	32,385	3,016	355	35,046	1.4	19.2	38.7	
Heritage Foods	16,787	1,037	6.2%	532	4,702	779	384	5,097	0.3	4.9	8.8	
Moder Dairies	6,068	190	3.1%	115	255	1,582	20	1,816	0.3	9.6	2.2	
Milkfood	3,807	201	5.3%	40	517	754	12	1,260	0.3	6.3	12.8	
Vadilal Industries	3,510	346	9.9%	11	924	1,342	45	2,221	0.6	6.4	NA	
Amrit Corp	612	-11	-1.8%	75	1,099	156	78	1,177	1.9	NA	14.7	
Mean									1.3	11.1	18.2	
Median									0.5	6.5	12.8	

Source: Company filings, National Stock Exchange (NSE), www.moneycontrol.com

- Owing to a diversified product portfolio and large scale of operations, Nestle enjoys high margins and consequently high valuation multiples vis-a-vis its peers who are primarily regional players.

III) Recent M&A Activity

- The last 6 years have seen major activity in this sector. With rising disposable incomes of the middle class, urbanisation and demand for milk plus value added products, the sector has become a hot spot for PE activity.
- The sector has attracted over INR 28 Bn investment from the PE funds in last 6 years.
 - Carlyle capital invested INR 1,100 Mn in Tirumala Milk in June 2010 and exited the investment in 2013 at approximately INR 3,600 Mn with a ~3x return in just 3 years.

Comparable Transactions												INR Mn	
Transaction	Date	Stake	Trans.		Equity			Sales	EBITDA	PAT	Sales x	EBITDA x	P/E x
			Amount	EV	Value	Debt	Cash						
Motilal Oswal exits Parag Milk	10-Jan-14	15%	2,000	13,333	888			NA	NA	NA	NA	NA	NA
Lactalis invests in Tirumala Milk	08-Jan-14	100%	18,000	18,000	NA	NA	NA	NA	NA	NA	NA	NA	NA
Godrej Agrovet divest in Creamline	25-Nov-13	65%	2,500	3,846	3,372	553	79	7,050	437	NA	0.5	8.8	NA
Hatsun acquires Jyothi Dairy	30-Oct-13	100%	650	650	NA	NA	NA	1,000	NA	NA	0.7	NA	NA
Rabo Equity invests in Prabhat Dairy	27-Aug-13	NA	800	NA	NA	520	2	2,870	NA	103	NA	NA	NA
Nestle Acquires Indocon	04-Feb-13	26%	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Premji invests In Heritage Foods	05-Dec-12	5%	NA	NA	NA	98	33	16,060	1,057	500	NA	NA	NA
Kotak divests in Heritage foods	31-Oct-12	6%	250	4,433	NA	NA	NA	16,060	1,057	500	0.3	4.2	NA
IDFC invests in Parag Milk	18-Sep-12	20%	1,550	7,750	NA	NA	NA	10,000	800	NA	0.8	9.7	NA
Amul invests in Delhi Milk Scheme	13-Sep-12	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
R. Gandhi invests in Ind. Progressive	01-Sep-10	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Carlyle invests in Tirumala milk	03-Jun-10	20%	1,100	5,500	5,218	448	166	4,729	299	1,347	1.2	18.4	3.9
Motilal Oswal invests in Parag Milk	03-Jun-08	10-12%	600	NA	NA	NA	NA	3,043	293	114	NA	NA	NA
Kotak invests in Heritage foods	04-Jan-08	NA	500	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Ladderup invests in Parag Milk	01-Jan-08	NA	NA	NA	NA	NA	NA	3,043	293	114	NA	NA	NA
Mean											0.7	10.3	3.9
Median											0.7	9.2	3.9

Source: Company filings, Newspaper articles

Notes:

1. The comparable companies data is based on Trailing Twelve Months (TTM) data i.e. 1st Jan 2013 to 31st Dec 2013.
2. Net sales and EBITDA do not include other income.
3. PAT includes other income.
4. Market-cap is calculated as the product of closing share price from NSE / BSE dated 25th Feb 2014 and number of share outstanding as at 31st Dec 2013.
5. Debt includes short term borrowings, long term borrowings, preference shares and minority interest.
6. Enterprise value is calculated as sum of market-cap and debt less cash and cash equivalents.
7. P/E ratio for Vadilal Industries is NA as it is marginally PAT positive.
8. EV/EBITDA multiple for Amrit Corp is NA as it has negative EBITDA.
9. In comparable transactions the stake bought by a company is assumed to be bought at the total EV valuation.

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