CRISIL IER IndependentEquityResearch

# KRBL Ltd

Detailed Report

Enhancing investment decisions

## Explanation of CRISIL Fundamental and Valuation (CFV) matrix

The CFV Matrix (CRISIL Fundamental and Valuation Matrix) addresses the two important analysis of an investment making process – Analysis of Fundamentals (addressed through Fundamental Grade) and Analysis of Returns (Valuation Grade) The fundamental grade is assigned on a five-point scale from grade 5 (indicating Excellent fundamentals) to grade 1 (Poor fundamentals) The valuation grade is assigned on a five-point scale from grade 5 (indicating strong upside from the current market price (CMP)) to grade 1 (strong downside from the CMP).

| CRISIL Fundamental Grade | Assessment | CRISIL Valuation Grade | Assessment |
|---|---|---|---|
| 5/5 | Excellent fundamentals | 5/5 | Strong upside (>25% from CMP) |
| 4/5 | Superior fundamentals | 4/5 | Upside (10-25% from CMP) |
| 3/5 | Good fundamentals | 3/5 | Align (+-10% from CMP) |
| 2/5 | Moderate fundamentals | 2/5 | Downside (negative 10-25% from CMP) |
| 1/5 | Poor fundamentals | 1/5 | Strong downside (<-25% from CMP) |

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**Last updated: 31 March, 2011**

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Each member of the team involved in the preparation of the grading report, hereby affirms that there exists no conflict of interest that can bias the grading recommendation of the company.

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# KRBL Ltd

## Braving the industry headwinds

| | |
|---|---|
| **Fundamental Grade** | **3/5 (Good fundamentals)** |
| **Valuation Grade** | **5/5 (CMP has strong upside)** |
| **Industry** | **Food Products** |

**April 17, 2012**

| | |
|---|---|
| **Fair Value** | **Rs 31** |
| **CMP** | **Rs 20** |

KRBL is India's leading exporter of branded basmati rice and owns one of the largest rice milling capacities. With lifting of ban on non basmati exports and reduction in minimum export price (MEP) of basmati rice, we believe that volume driven growth is in order in FY13. Further, on account of India's competitive advantage in basmati rice exports, growth in domestic consumption, KRBL's good profitability and strong brand positioning, we assign a fundamental grade of **3/5**, indicating that its fundamentals are **'good'** relative to other listed securities in India.

**Recent industry developments have been positive**

In February 2012, the government announced the reduction in the MEP of basmati rice by US$200 to US$ 700 per tonne. This should make Indian basmati more competitive in the export markets. The government also lifted the ban on export of non basmati rice led by burgeoning domestic supplies. We expect India's non basmati exports to be 3.5-4.0 million tonnes in FY12 and move higher in FY13, provided policy actions remain favourable. Further, in April 2012, direct exports to Iran have resumed (in small quantities) through a bilateral payment mechanism wherein Indian basmati exporters receive payments in Indian rupees.

**KRBL: Relatively healthy profitability in spite of marginal growth**

Consequent to the industry developments, KRBL posted marginal revenue growth of ~6% in 9MFY12. However, the company continues to be one of the better placed with higher-than-industry export realisations, relatively lower gearing and higher profit margins than most players.

**Key monitorables: Global geo-politics and domestic regulations**

Developments in the Middle East will determine the way forward for export. Domestically, the government's policy in respect of continuation of non basmati exports and further reduction in MEP for basmati will be key monitorables. Other key risks include (a) raw material price fluctuations, (b) highly competitive environment, and (c) currency fluctuations.

**Two-year revenue CAGR of 6%**

We expect revenues to register a two-year CAGR of 6% to Rs 17.6 bn in FY13 largely driven by higher volumes particularly on account of non basmati exports. We have revised our FY13 EPS estimate upwards to Rs 5.7 as the company is expected to benefit from lower raw material costs.

**Valuations – the current price has 'strong upside'**

We value KRBL at 5.5x its FY13E EPS, implying a fair value of Rs 31 per share. Accordingly, we assign a valuation grade of **5/5**.

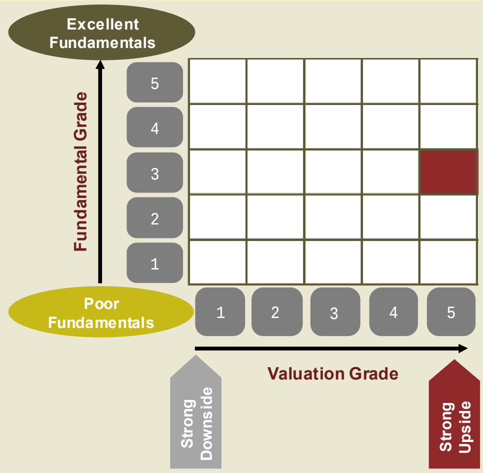
## KEY FORECAST

| (Rs mn) | FY09 | FY10 | FY11 | FY12E | FY13E |
|---|---|---|---|---|---|
| Operating income | 13,212 | 15,929 | 15,586 | 15,990 | 17,589 |
| EBITDA | 2,044 | 2,184 | 2,413 | 2,382 | 2,814 |
| Adj PAT | 656 | 1,250 | 1,199 | 1,087 | 1,391 |
| Adj EPS-Rs | 2.7 | 5.1 | 4.9 | 4.5 | 5.7 |
| EPS growth (%) | 19.0 | 90.4 | (3.4) | (9.6) | 28.0 |
| Dividend yield (%) | 1.2 | 1.8 | 1.8 | 1.5 | 2.0 |
| RoCE (%) | 16.8 | 17.6 | 15.3 | 12.4 | 14.3 |
| RoE (%) | 16.7 | 26.1 | 20.3 | 15.6 | 17.2 |
| PE (x) | 7.4 | 3.9 | 4.0 | 4.4 | 3.5 |
| P/BV (x) | 1.1 | 0.9 | 0.7 | 0.6 | 0.6 |
| EV/EBITDA (x) | 5.1 | 4.8 | 5.7 | 5.4 | 4.4 |

NM: Not meaningful; CMP: Current market price

**Source: Company, CRISIL Research estimates**

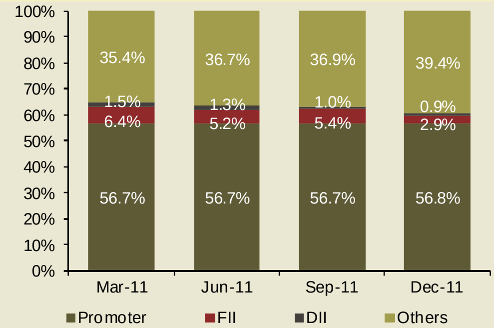
## CFV MATRIX




## KEY STOCK STATISTICS

| | |
|---|---|
| NIFTY/SENSEX | 5207/17095 |
| NSE/BSE ticker | KRBL |
| Face value (Rs per share) | 1 |
| Shares outstanding (mn) | 244 |
| Market cap (Rs mn)/(US$ mn) | 4,834/93 |
| Enterprise value (Rs mn)/(US$ mn) | 12,907/249 |
| 52-week range (Rs)/(H/L) | 34/13 |
| Beta | 1.3 |
| Free float (%) | 43.0 |
| Avg daily volumes (30-days) | 535,678 |
| Avg daily value (30-days) (Rs mn) | 10.7 |

## SHAREHOLDING PATTERN




## PERFORMANCE VIS-À-VIS MARKET

| | Returns | | | |
|---|---|---|---|---|
| | 1-m | 3-m | 6-m | 12-m |
| KRBL | 7% | 16% | -23% | -38% |
| NIFTY | -4% | 7% | 3% | -12% |

## ANALYTICAL CONTACT


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**Table 1: KRBL's business environment**

| Product / Segment | Rice | Energy / Others |
|---|---|---|
| **Revenue contribution (FY11)** | Rice: 94.5%<br>By-products: 4.1% | 1.4% |
| **Revenue contribution (FY13)** | 98.0% | 2.0% |
| **Product / service offering** | ▪ Basmati rice: 20 brands including India Gate, Train, Al Wisam, Quilada, Doon and Nurjahan<br>▪ Recently commenced exports of non basmati rice<br>▪ Bran oil, furfural oil and de-oiled cakes | ▪ Power generation capacity: 55.6 MW<br>o Captive: 12.8 MW<br>o Commercial: 42.8 MW<br>▪ Wind: 39.8 MW; Biomass: 15.8 MW |
| **Geographic presence** | ▪ Revenue contribution: India – 58.1%, Middle East – 37.4%, Others – 4.6%<br>▪ Key export markets: Saudi Arabia, UAE, Kuwait and United States<br>▪ Domestic region-wise revenue share: North – 34%, South – 29%, West – 28%, East – 9% | ▪ Power plants located in Punjab, Uttar Pradesh, Rajasthan, Maharashtra, Tamil Nadu and Karnataka |
| **Market position** | ▪ 25% share in branded basmati exports<br>▪ 30% share in branded basmati in the domestic market<br>▪ Largest branded basmati player in Saudi Arabia | ▪ Self sufficient in captive requirements; thrust on wind energy is purely from commercial perspective |
| **Industry growth expectations** | ▪ Domestic basmati consumption expected to grow at a healthy rate of 15% over the next three to four years<br>▪ Geo-political issues influence basmati exports as the key markets are in the Middle East. However, we expect India to export at least 2-2.5 million tonnes of basmati rice each year<br>▪ Exports of non basmati rice is contingent upon government policies and therefore unpredictable | ▪ Investment in renewable energy expected to remain consistent on account of renewable energy purchase obligations of state utilities<br>▪ Increasing investments in wind energy - favourable tax treatment being one of the biggest reasons |
| **Sales growth (FY08-FY11 – 3-yr CAGR)** | 15.7% | 82.3% |
| **Demand drivers** | ▪ Lifestyle changes: Increasing Indian middle-class population, growth in organized retail, growth in hotels and restaurants boosting domestic demand<br>▪ Increasing preference for basmati in export markets<br>▪ Food scarcity across the globe generating demand for non basmati rice | ▪ Power deficit in the country<br>▪ State utilities are required to purchase at least 5% of the power from renewable energy<br>▪ Carbon credits and renewable energy certificates could provide further upside |
| **Key competitors** | ▪ Domestic and export markets: REI Agro, Kohinoor Foods, LT Foods, unbranded basmati and private labels | ▪ Renewable energy producers in respective states |
| **Key risks** | ▪ Unrest in the Middle East<br>▪ Payment issues associated with Iran<br>▪ Regulatory issues in exports of non basmati rice | ▪ Lower plant load factor, especially in wind energy<br>▪ Regulatory - withdrawal of favourable tax treatment, preferential tariff, etc. |

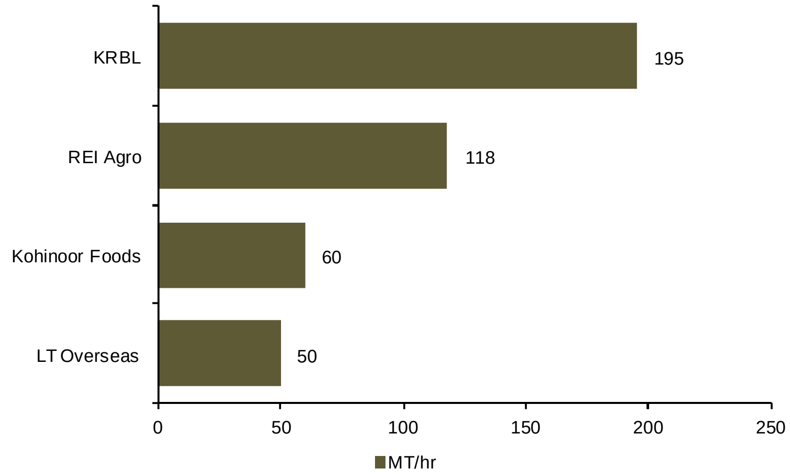
**Source: Company, CRISIL Research**

# Grading Rationale

## Leading basmati player

KRBL is a leading basmati rice player in India; with the largest production capacity of 195 metric tonnes (MT) per hour, it is ahead of its competitors. Being an integrated player, it generates other value-added by-products like bran oil, de-oiled cakes and uses rice husks for captive power plants. KRBL's brands are leaders in key basmati export markets such as Saudi Arabia, UAE, Kuwait and others.

**Figure 1: Ahead of peers in rated milling capacity**




**Source: Company, CRISIL Research**

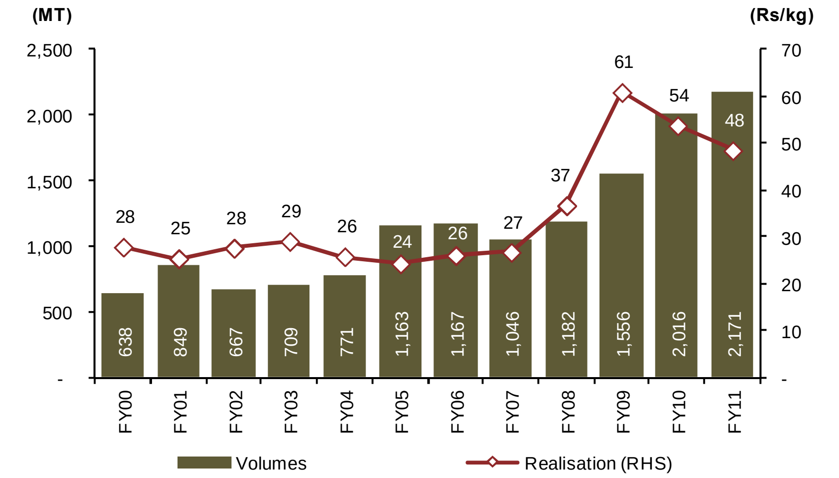
## Good long term prospects for basmati rice industry

Basmati rice industry is attractive, primarily due to the following factors:

- **Global trade flows**: India and Pakistan are the major producers of basmati rice. India exports ~2.0 million tonnes per annum of basmati rice compared to Pakistan's ~0.9 million tonnes per annum. Also, as per our industry sources, India's main basmati variety, PUSA 1121, is better than Pakistan's 'Super' variety. This is a structural advantage that India continues to enjoy.
- **Premium pricing**: Basmati rice is premium long-grain fine-texture rice and one of the most expensive varieties of rice available in the world.
- **Lower regulations**: Due to its premium nature, basmati rice is not subject to strict regulations as faced by normal rice, which is the common man's food.
- **Strong export growth**: Exports of Indian basmati rice in volumes has grown at a CAGR of ~12% between FY00 and FY11, while in value terms it has grown at 18% CAGR to Rs 106 bn from Rs 17 bn in the same period.
- **Lifestyle changes**: With the increasing Indian middle-class population, organised retail and growth in hotels and restaurants, domestic demand for basmati is on the rise.

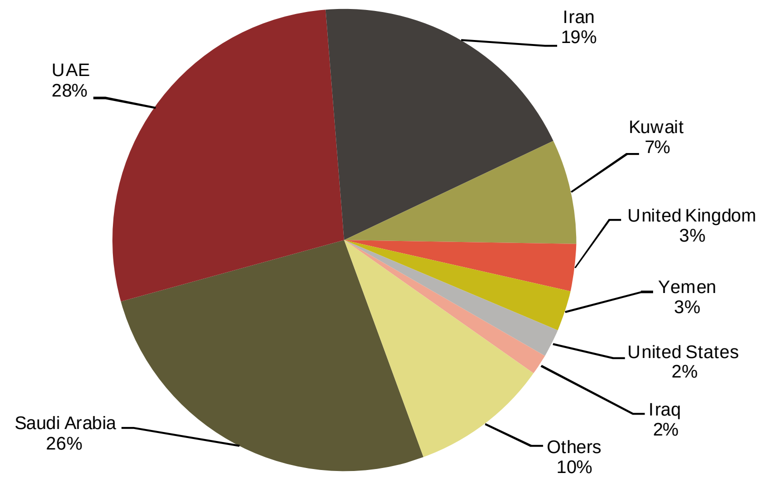
**India and Pakistan are the major producers of basmati rice**

**Figure 2: India's basmati rice exports increase manifold**




**Source: APEDA, CRISIL Research**

**Figure 3: Export destinations for Indian basmati rice (FY11)**




**Source: APEDA, CRISIL Research**

Saudi Arabia, UAE and Iran amongst the leading markets for Indian basmati rice

**Table 2: Significant rise in acreage of basmati rice**

| Acreage (hectares) | 2008 | 2009 | 2010 |
|---|---|---|---|
| Punjab | 537,230 | 792,670 | 738,920 |
| Haryana | 658,490 | 610,730 | 781,400 |
| UP | 271,900 | 254,290 | 377,790 |
| Uttarakhand | 13,300 | 17,520 | 29,880 |
| Others | 33,400 | 34,260 | 40,400 |
| **Total** | **1,514,320** | **1,709,470** | **1,968,390** |

**Source: RMSI**

Area under cultivation for basmati rice has increased consistently, due to increasing demand

It is estimated that acreage under basmati has increased by another 10-15% during 2011 led by Punjab and Haryana.

## 2011: Difficult year for the basmati rice industry

### *Payment issue with Iran has resulted in increased competition in other export markets*

Iran has been the fastest growing buyer for Indian basmati in the past three years with exports rising from 170,947 tonnes in FY09 to 420,403 tonnes in FY11 (accounting for 19% of India's direct export volume in FY11; total export share estimated at ~30%). However, on account of sanctions imposed by the United Nations, the US and the European Union, and increased volatility in the Iranian currency, Iran-based importers are unable to make US dollar payment (primary currency in basmati trade) which is adversely impacting basmati exports.

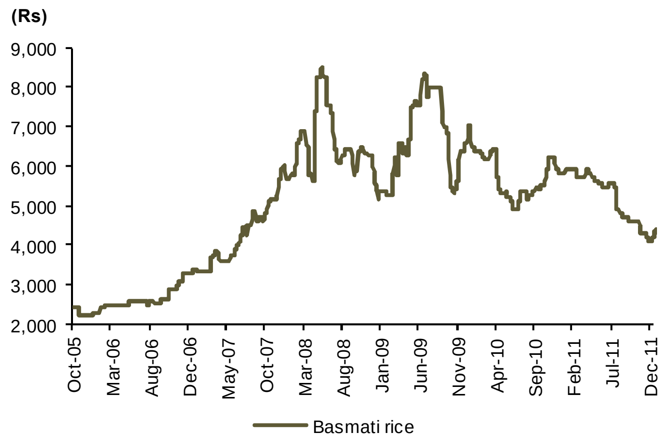
This has increased competition in the traditional markets like Saudi Arabia, UAE, Kuwait as well as in India, as some exports to Iran are being diverted to these countries. Some of the players even exported at a loss to clear the inventory, thereby increasing competitive intensity. According to industry estimates, Iranian buyers have defaulted on payment of about 200,000 tonnes of rice from India. Total value of default is estimated to be US$ 144 mn.

In February 2012, Iran agreed to receive payments from India in INR, for 45% of Iran's oil exports to India. According to our discussion with industry participants, Iran is likely to use the INR to pay for exports from India, which should aid basmati exporters to receive payments. RBI has already issued notification for opening of Special Rupee Vostro Account in Bank Markazi Jomhuri Islami Iran (Iran's Central Bank) to facilitate the settlement of payments between India and Iran. As of April 2012, direct basmati exports to Iran have commenced in small quantities through this payment mechanism.

### *Excess inventory leading to oversupply in the domestic market*

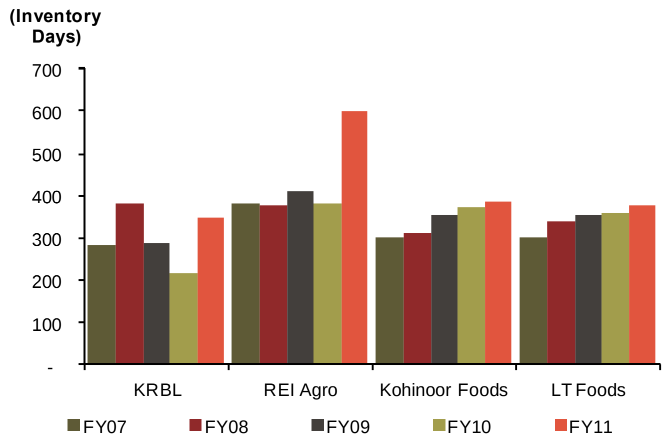
Significant amount of paddy was acquired by the Indian basmati players at the end of FY11, in anticipation of demand growth during FY12. Also, increase in acreage under basmati rice in during FY12 has led to excess supply, which put pressure on domestic prices of basmati rice. Price of basmati rice in India has declined by nearly 28% over 2011 to Rs 4,200 a quintal.

**Figure 4: Basmati prices under pressure**




**Source: Industry, CRISIL Research**

**Figure 5: Players increased inventory in FY11**




**Source: Industry, CRISIL Research**

### *MEP at US$900 per tonne made Indian basmati less competitive*

The Minimum Export Price (MEP) for basmati rice specified by the government, made exports from India less attractive as the prevailing average market prices were lower than the MEP of US$900. The MEP was introduced in 2009 to prevent illegal export of non basmati rice, after its exports were banned by the government. However, considering that non basmati rice export has again been opened in 2011, the MEP has proved to be a bottleneck for basmati exporters. In February 2012, the government reduced the MEP by US$ 200 to US$ 700 per tonne.

**Table 3: Movement of MEP since 2008**

| | USD / tonne |
|---|---|
| March 2008 | 900 |
| March 2008 | 1,100 |
| April 2008 | 1,200 |
| January 2009 | 1,100 |
| August 2009 | 800 |
| September 2009 | 900 |

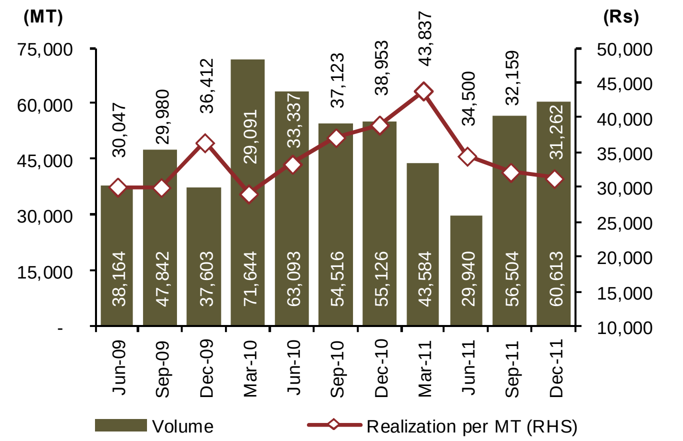
**Source: Directorate General of Foreign Trade**

## Industry trends reflected in KRBL's 9MFY12 performance

KRBL posted modest revenue growth of 6% y-o-y in 9MFY12. While export volumes were higher by 25% compared to the year ago period, realisations were lower by 5%. The domestic market saw a drop in prices on account of excess supply. Consequently, KRBL's domestic realisations declined by 11% on a y-o-y basis.

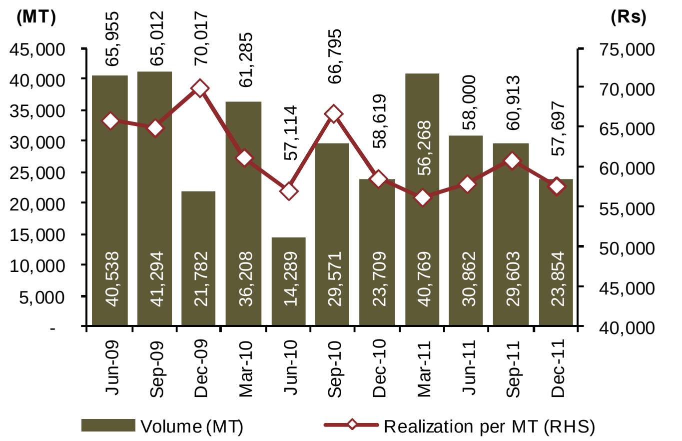
The company also exported 47,660 tonnes of non basmati rice in Q3FY12, primarily to African countries.

**Figure 6: Realisations in domestic market on a downward trend**




**Source: Company, CRISIL Research**

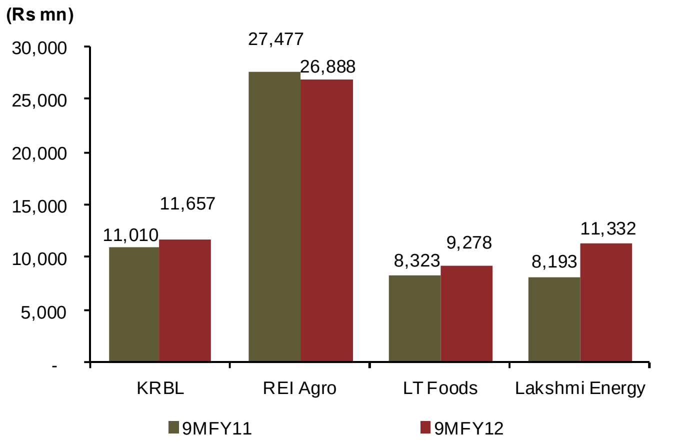
**Figure 7: Export realisations decline in 9MFY12**




**Note:** Figures exclude non basmati exports in Q3FY12

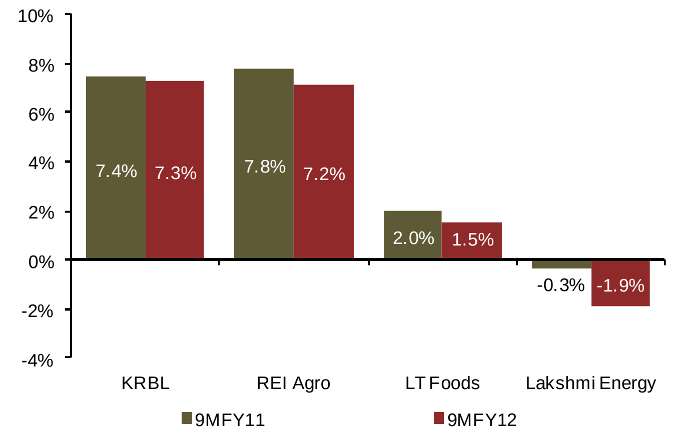
**Source: Company, CRISIL Research**

**Figure 8: Industry sales growth largely flattish in 9MFY12**




**Source: Industry, CRISIL Research**

**Figure 9: KRBL maintains PAT margin**




**Source: Industry, CRISIL Research**

## Recent industry developments have been positive

### *Non basmati export opens another avenue for rice exporters*

In September 2011, the government lifted the three-year ban on export of non basmati rice. Further, expectation of a bumper rice crop in India in 2011-12, weak production outlook for most rice-exporting countries and a weak rupee may drive a sharp increase in India's share in global rice trade. We estimate India's rice exports (including basmati rice) to be nearly 6 million tonnes in 2011-12 that could translate into an additional US$2bn in export revenues for India's rice millers and exporters in 2011-12.

The expected decline in rice production in leading rice exporting nations such as Thailand, Vietnam and Pakistan may also favour India's exporters. Rice production in Thailand, the largest exporter globally, is expected to decline in 2011-12 due to a damaged crop, following floods. The Thai government's decision to increase its minimum purchase price of rice may also reduce the competitiveness of Thai rice globally. White milled Thai rice, for instance, is expected to be priced at US$600 to US$610 per tonne, higher by US$120 to US$150 per tonne over the comparable variety of Indian rice.

During Q3FY12, KRBL exported 47,660 tonnes of non basmati, which accounted for ~23% of revenues in that quarter. We expect KRBL to continue exporting non basmati rice going forward. However, uncertainty over government's decision to continue to allow exports of non basmati rice is a key risk to our assumption.

### *Lowering of MEP expected to boost export volumes*

In February 2012, the government reduced the MEP for basmati rice from US$900 per tonne to US$700 per tonne. We believe this should boost the export volumes for basmati rice and therefore aid in clearing excess inventory with the processors and traders.

## Strong brand results in better pricing

**Strong brand positioning should help offset competition:** KRBL is one of India's largest branded basmati players. Its brand 'India Gate' has been one of the highest exported basmati brands from India over the past few years.

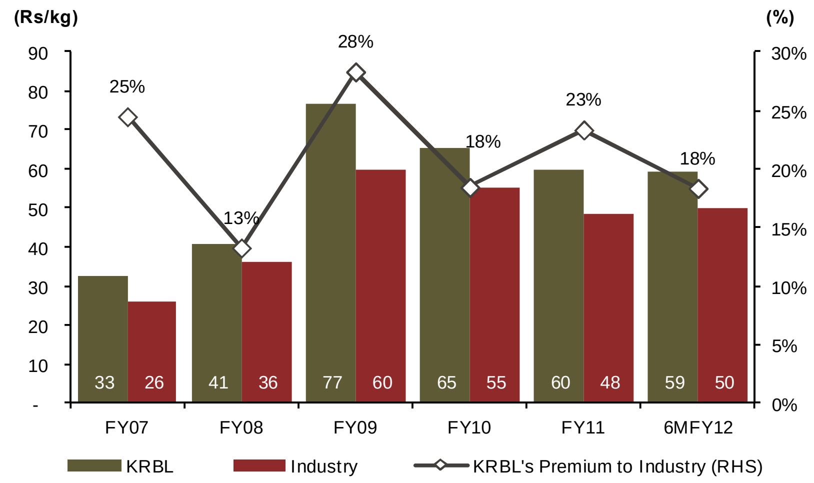
### Table 4: KRBL's top export brands

| FY08 | FY09 | FY10 | FY11 | FY12 |
|---|---|---|---|---|
| India Gate | India Gate | India Gate | India Gate | India Gate |
| Al Wisam | Train | Train | Train | Unity |
| Train | Al Wisam | Al Wisam | Telephone | Al Wisam |
| Telephone | Qilada | Qilada | Al Wisam | Train |
| Qilada | Nur Jahan | Nur Jahan | Qilada | Telephone |

**Source: Company**

**KRBL's brand commands premium pricing:** KRBL's 'India Gate' brand commands a significant premium over most other brands in the industry and contributes to ~40% to its domestic revenues. In the export market, KRBL's average realisation was 18% higher than the industry's during 6MFY12.

### Figure 10: KRBL's export realisation higher than industry's




**Source: APEDA, CRISIL Research**

**Marketing strategy** – venturing into new markets: KRBL's brands are strongly positioned in key markets like Saudi Arabia, UAE, Kuwait and Qatar. KRBL has also increased its presence in non traditional markets in the past few years:

- Nation-wide presence in the United States through some of the leading retailers, catering to the main and ethnic market
- Has tied up with one of the biggest retailers in Canada, and will be present across 1,100 stores
- Has tied up with one of the biggest distributors in Iraq, which is a fast emerging market for basmati rice
- Recently started export of non basmati rice to African countries. KRBL already has a tie up with a leading retailer in South Africa and Mauritius
- Plans to get into private label supply in FY13

KRBL has adopted the strategy of attracting consumers across all price segments with product prices varying from Rs 30 per kg to Rs 149 per kg, thus catering to both price-sensitive and premium consumers. It has a strong distribution network with 40 international distributors including 14 in the Middle East, the world's largest market for basmati rice. KRBL also has 515 nation-wide distributors, who in turn have access to over 575,000 retailers.

## Peer comparison: KRBL stacks up well against the peers

KRBL fares better than its peer group on most parameters on account of its strong brand and relatively conservative debt policy. The company has historically posted higher than industry ROE and lower debt/tonne.

### Table 5: Peer Comparison

| | Sales / Tonne | | | EBITDA / Tonne | | | PAT / Tonne | | |
|---|---|---|---|---|---|---|---|---|---|
| In Rs, unless specified | FY09 | FY10 | FY11 | FY09 | FY10 | FY11 | FY09 | FY10 | FY11 |
| **KRBL** | **42,731** | **45,174** | **45,155** | **7,004** | **6,517** | **7,432** | **2,242** | **3,717** | **3,705** |
| Kohinoor Foods | 43,491 | 42,450 | 44,605 | 3,424 | 4,737 | 4,285 | (1,327) | (458) | (530) |
| LT Foods | 48,854 | 43,595 | 42,308 | 8,632 | 8,014 | 6,621 | 2,119 | 2,168 | 1,461 |
| REI Agro | 48,707 | 55,102 | 56,729 | 9,086 | 9,218 | 11,956 | 1,234 | 2,372 | 4,356 |

| | Debt / Tonne | | | ROE (%) | | | PAT Margin (%) | | |
|---|---|---|---|---|---|---|---|---|---|
| | FY09 | FY10 | FY11 | FY09 | FY10 | FY11 | FY09 | FY10 | FY11 |
| **KRBL** | **20,599** | **18,051** | **27,777** | **16.7** | **26.1** | **20.3** | **5.0** | **7.8** | **7.7** |
| Kohinoor Foods | 51,544 | 51,065 | 57,047 | (11.3) | (4.0) | (5.3) | (2.3) | (0.8) | (0.9) |
| LT Foods | 51,145 | 53,896 | 64,785 | 19.0 | 16.1 | 10.2 | 2.8 | 3.1 | 2.0 |
| REI Agro | 60,234 | 67,557 | 59,437 | 11.4 | 22.1 | 17.8 | 2.5 | 4.2 | 7.6 |

**Source: Company, CRISIL Research**

## Energy division

KRBL's energy division currently has a generation capacity of 55.6 MW. Of this, 13 MW is being used for captive purposes while the rest is sold on a commercial basis to state utilities. The company's investment in wind power is primarily to avail tax benefits.

### Table 6: KRBL's generation capacity

| Plant | Type | Total capacity (MW) | Captive (MW) | Commercial (MW) |
|---|---|---|---|---|
| Dhuri | Biomass | 12.3 | 9.3 | 3.0 |
| Ghaziabad | Biomass | 3.5 | 3.5 | - |
| Maharashtra | Wind | 12.5 | - | 12.5 |
| Rajasthan | Wind | 8.1 | - | 8.1 |
| Tamil Nadu | Wind | 8.1 | - | 8.1 |
| Karnataka | Wind | 11.1 | - | 11.1 |
| **Total** | | **55.6** | **12.8** | **42.8** |

**Source: Company, CRISIL Research**

We view the expansion of the energy division as positive, especially since the thrust is on renewable energy (biomass/wind):

- **Power deficit in India**: The power deficit in India has initiated massive investments in generation capacity in the past five years. We are also comforted by the fact that the KRBL's new projects are of a smaller size (5-10MW) and are spread over different locations.
- **Lower offtake risk**: State utilities in India have a renewable energy purchase obligation of around 5%-8% of their power purchase requirement. Since most of the power sold commercially by KRBL is on a long-term basis, the company's offtake risk is significantly reduced. It should also be noted that renewable energy plants fall under the 'must run' category and therefore are given preference in power procurement by state utilities.
- **Low fuel risk**: Paddy processing yields approximately 22% of husk, which is a primary source of fuel for bio-power generation. The company has no problem in procuring sufficient amount of husk to meet the generation requirements of its biomass plants.
- **Renewable energy incentives**: Two of KRBL's plants (Ghaziabad, Uttar Pradesh and Dhule, Maharashtra) are eligible for carbon credits. The management expects to generate revenues of Rs 15 mn in FY12 through the sale of carbon credits.
- **Tax benefits**: Wind energy qualifies for accelerated depreciation for tax purposes. Due to this, the company's effective tax rate was 17% and 24% in FY10 and FY11, respectively.

During FY12, KRBL is likely to add another 10 MW of wind generation capacity. At this point we are not assigning separate valuation to the company's energy division, as the contribution to its revenue and profits is not significant. During 9MFY12, the Energy division contributed to less than 2% of overall revenues.

## Key risks

### Geo-political issues may affect exports

As Middle East is the biggest export market for basmati rice, there is a risk from uncertain political situation in some countries in the region. Middle East accounts for over 35% of KRBL's revenues and Saudi Arabia, UAE and Kuwait are its top export markets.

### Commodity business carries raw material risk

KRBL typically engages in purchasing both semi-processed rice and paddy, depending upon the demand and price expectations at a given point of time. This exposes the company to fluctuations in raw material prices. Further, while longer inventory holding periods may result in higher realisations (on account of ageing), it results in higher interest costs too.

### Highly competitive industry

Higher realisations per acre, exportability and increasing consumption in the domestic market has led to increased supply of basmati rice through growth of acreage under cultivation. However, this may lead to excess supply situation in the near term, as demand for basmati has not kept pace with supply. Further, as has been seen throughout FY12, the industry is susceptible to geo-political risks.

### Regulatory challenges

The government intervenes in the basmati exports market through MEP. Any increase in MEP by the government may have an adverse impact on industry's volumes. The government banned exports of non-basmati rice in April 2008 to curb inflation. Although historically India has not witnessed any ban on basmati rice exports, any policy change in that regard could have significant impact on the industry.

### Export business subject to currency risks

As KRBL's export revenues averaged ~50% of its total revenues in the past three years, it is subject to the risk of the fluctuations of INR against the US dollar. As per the management, KRBL has a foreign exchange risk management desk and hedges a significant part of its foreign currency exposure, in order to protect itself from foreign currency fluctuations.

### Basmati cultivation exposed to vagaries of nature

Basmati rice typically requires less water for cultivation as compared to normal rice. However, unseasonal rains and floods can still damage the crop. Since major states producing basmati rice (Punjab and Haryana) are well irrigated, scanty rainfall does not pose a major risk to production.

## Financial Outlook

### Revenue growth to be driven by volumes

**Revenues likely to grow at a two-year CAGR of 6% to Rs 17.6 bn in FY13 driven by volume growth in exports as well as domestic market**

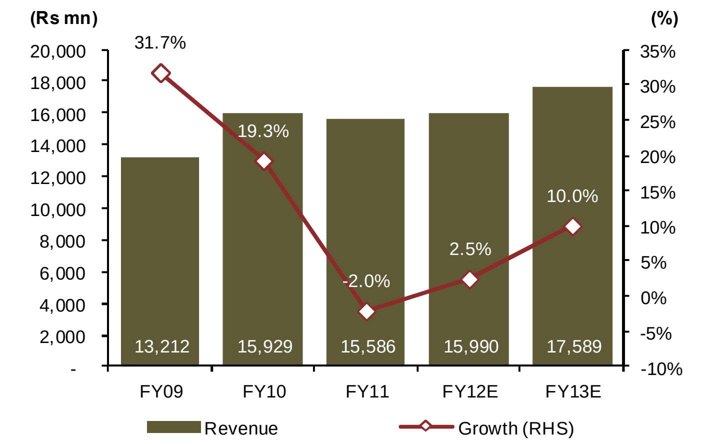
We expect revenue growth to remain flat in FY12 over the previous year on account of lower realisations but higher volumes. Further, revenue in FY13 is also expected to be driven by increase in volumes as blended realisations for the company will remain flat on account of higher proportion of low value non basmati rice exports.

We expect EBITDA margin to be higher by ~80 bps in FY13, compared to our earlier estimates, as the company will benefit from low paddy prices during FY12. Paddy prices have declined from the high of Rs 24/kg in FY11 to Rs 16-17/kg in FY12. Consequently, our EPS estimate for FY13 has also been raised by 10% to 5.7.

**Table 7: Revision in earnings estimates**

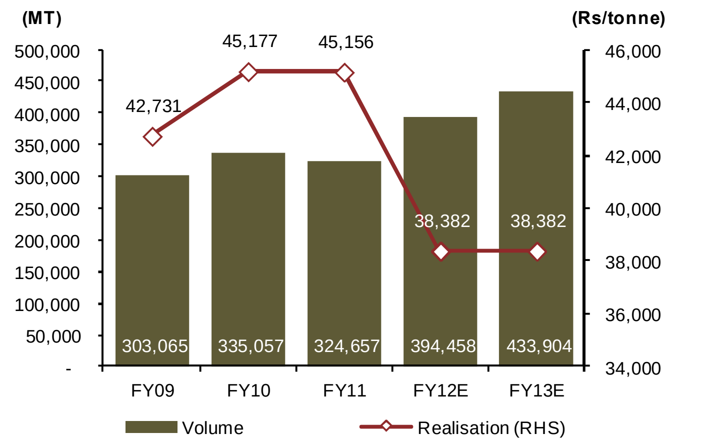
| | | FY13E | | |
|---|---|---|---|---|
| **Particulars** | **Unit** | **Old** | **New** | **% change** |
| Revenues | (Rs mn) | 17,589 | 17,589 | 0.0% |
| EBITDA | (Rs mn) | 2,677 | 2,814 | 5.1% |
| EBITDA margin | % | 15.2% | 16.0% | 78 bps |
| Adj. PAT | (Rs mn) | 1,260 | 1,391 | 10.4% |
| Adj. PAT margin | % | 7.3% | 7.9% | 75 bps |
| Adj. EPS | Rs | 5.2 | 5.7 | 10.4% |

**Figure 11: Revenue growth to be flattish in FY12**



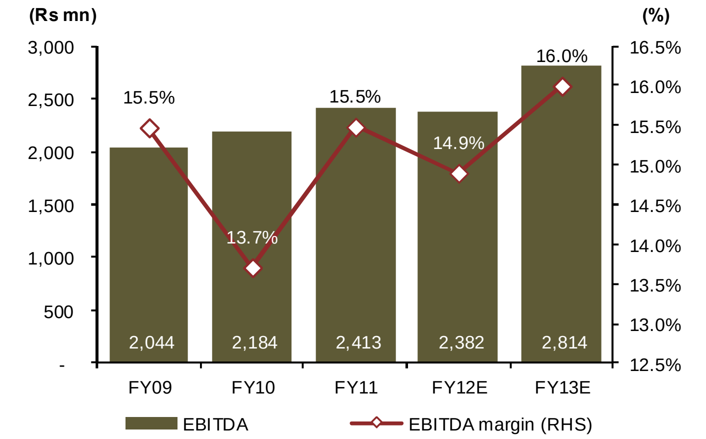

**Source: Company, CRISIL Research**

**Figure 12: Volumes to drive growth going forward**



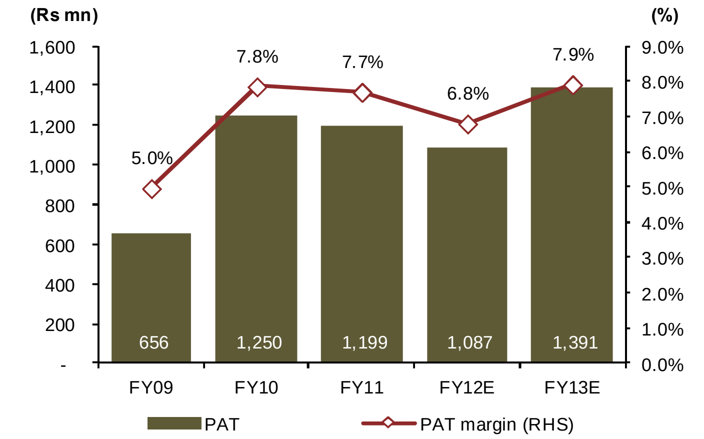

**Source: Company, CRISIL Research**

Figure 13: EBITDA margin to expand in FY13




Source: Company, CRISIL Research

Figure 14: Higher PAT margin on improved operating profits



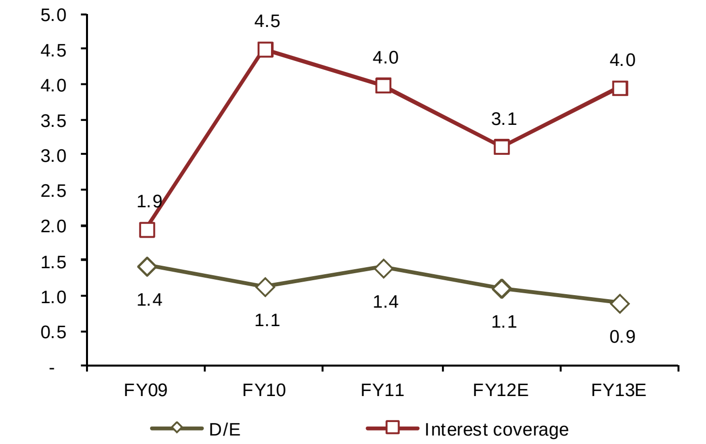

Source: Company, CRISIL Research

## Debt levels to improve on account of low cost inventory

As basmati paddy is required to be stored for about one year, inventory levels are expected to rise with increasing sales volumes. Historically, the company's debt levels are highest in March (end of buying season) and lowest in September (beginning of buying season).

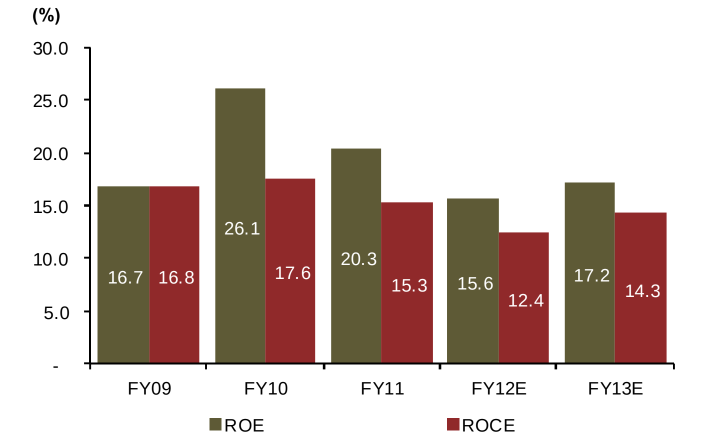
Debt levels for FY12 are expected to decline from Rs 9 bn in FY11 to Rs 8.3 bn. While KRBL is expected to accumulate higher inventory in volume terms compared to FY11, significantly lower paddy prices in FY12 will reduce inventory value and consequently the debt requirement.

Figure 15: D/E to improve in FY13 as debt levels decline




Source: Company, CRISIL Research

Figure 16: ROE and ROCE trend




Source: Company, CRISIL Research

## Management Overview

### Strong management with vast experience, domain expertise

The company's management (led by three brothers - Anil Mittal, Arun Gupta and Anoop Gupta) has more than 25 years of experience in the rice industry and has expanded the business in both scale and scope through various initiatives. These include increase in in-house processing capacity by acquiring the Dhuri (Punjab) plant, increasing vertical integration, broadening distribution channels, expanding the product range and brand portfolio and increasing sales in the domestic and export markets. Revenues of the company grew from Rs 2.6 bn in FY01 to Rs 15.6 bn in FY11.

**Revenues have increased from Rs 2.6 bn in FY01 to Rs 15.6 bn in FY11 under the current management**

The company has established its brand name in the domestic and international markets and is a leading exporter to the Middle East. It has repeatedly bagged the Agricultural & Processed Food Products Export Development Authority (APEDA) trophy for 14 years up to 2009-10 for being India's top basmati rice exporter. Its premium brand 'India Gate' has been awarded India's Most Preferred Basmati Brand, which commands higher premium as compared to other brands in the industry.

### Successful in increasing acreage under contact farming

KRBL initiated the concept of contact farming in Punjab, Uttarakhand and Uttar Pradesh, which helped it procure better quality paddy from farmers. KRBL provides high-yield certified seeds and intensive training for crop cultivation to ensure higher yields and realisations and it currently sources paddy from 75,000 farmers. The company's contract farming initiative helped these farmers to increase acreage from 60,000 acres in FY05 to 240,000 acres in FY11.

### Second-line management

While the company is promoter driven, it has a strong second line of management. KRBL has a professionally strong management and many of the senior management positions (CFO, plant CEO) are held by individuals not related to the promoters.

## Corporate Governance

CRISIL's fundamental grading methodology includes a broad assessment of corporate governance and management quality, apart from other key factors such as industry and business prospects, and financial performance. In this context, CRISIL Research analyses the shareholding structure, board composition, typical board processes, disclosure standards and related-party transactions. Any qualifications by regulators or auditors also serve as useful inputs while assessing a company's corporate governance.

Overall, KRBL's corporate governance conforms to regulatory requirements.

### Board composition

KRBL has 10 board members, five of whom are independent directors. This composition meets the minimum requirements as per Clause 49 of SEBI's listing guidelines. Mr Anil Mittal is the chairman and managing director. Mr Arun Gupta and Mr Anoop Gupta are joint managing directors. Ms Priyanka Mittal (Anil Mittal's daughter) is also a whole-time director. Independent directors include Mr Ashwani Dua (chairman, audit committee) who has extensive experience in rice business. Mr N.K. Gupta (independent director) holds a doctorate in engineering in food technology. Mr Gautam Khaitan has extensive legal experience and specialises in corporate transactions. Other directors are Mr Ashok Chand (whole-time director), Mr Vinod Ahuja (independent director) and Mr Shyam Arora (independent director).

**The positions of chairman and managing director are held by the promoters**

### Board's processes

The board's processes have evolved over the past three-four years; board meeting notices with the agenda and explanatory notes are circulated well in advance. The audit committee is chaired by an independent director. Some independent directors are personally known to the promoters.

Independent directors had earlier highlighted the need for strengthening the internal audit process. The company now has one dedicated person at each of its plants to carry out internal audit and will gradually expand the internal audit team to 15-20 people. In our recent interaction with one of the independent directors, it was highlighted that internal audit has improved while audit reports are comprehensive and regularly circulated among the board members.

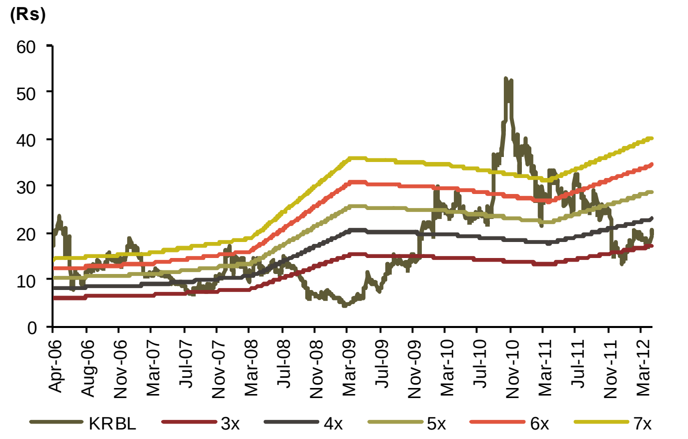
KRBL's promoters have another group company – KRBL Infrastructure Ltd, which is involved in the infrastructure business. This company is constructing an eight-storied building in Noida (near New Delhi), of which two floors are expected to be rented to KRBL on an arm's length basis. The transaction has been discussed at the board level.

## Valuation Grade: 5/5

We continue to value KRBL based on the P/E method. Since the upward revision in our FY13 EPS estimate is on account of one-time inventory gain, we have applied a lower multiple of 5.5x (6.0x earlier) to KRBL's FY13 EPS, and maintained the fair value of Rs 31 per share. Based on the current market price, the valuation grade assigned is **5/5**.

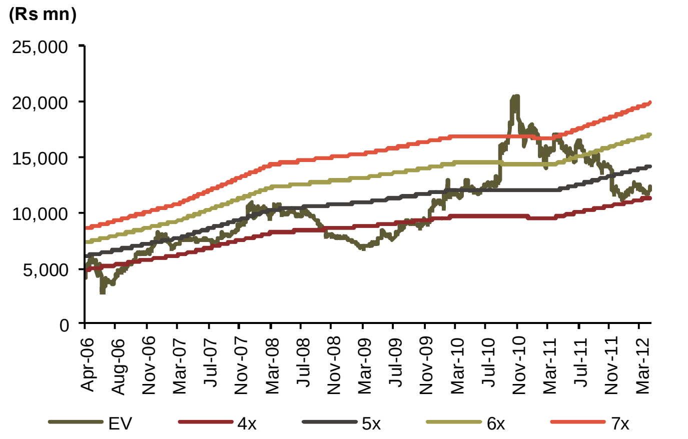
**Our fair value of KRBL is Rs 31 per share and we assign a valuation grade of 5/5**

### One-year forward P/E band



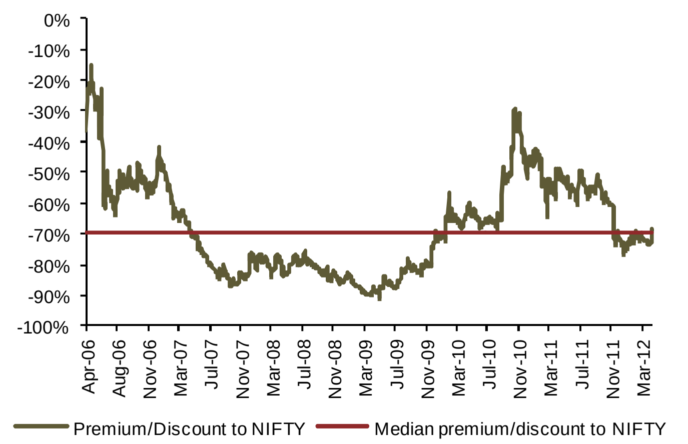

Source: NSE, CRISIL Research

### One-year forward EV/EBITDA band



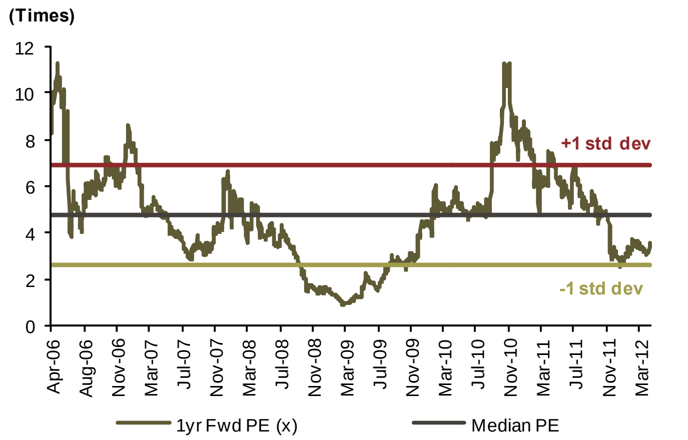

Source: NSE, CRISIL Research

### P/E – premium / discount to NIFTY



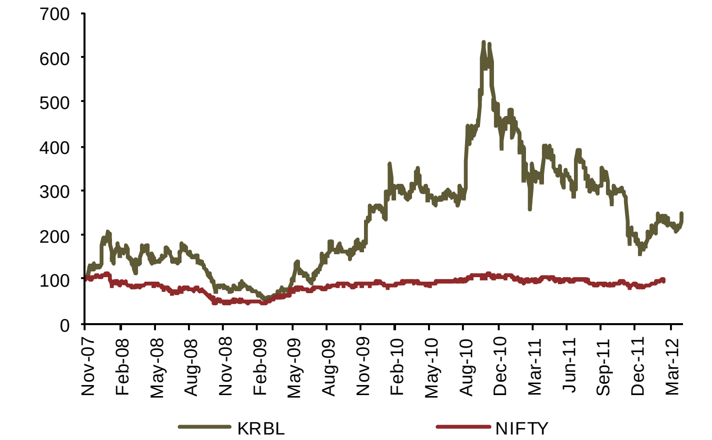

Source: NSE, CRISIL Research

### P/E movement



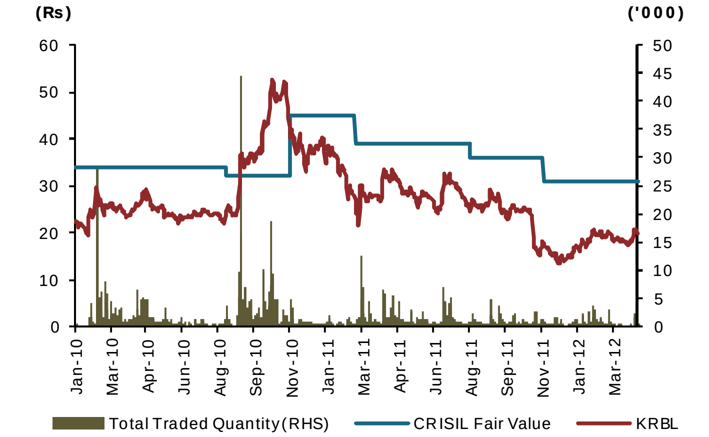

Source: NSE, CRISIL Research

## Share price movement




**Source: Company, CRISIL Research**

## Fair value movement since initiation




**Source: NSE, BSE, CRISIL Research**

## Company Overview

KRBL is a 120-year old firm engaged in the business of grain marketing and agro processing. KRBL is the world's largest rice miller with manufacturing capacity of 195 MT/hour. It is also the world's largest basmati rice exporter with a strong presence in the Middle East.

### Manufacturing facility

The company's manufacturing facilities are located in Dhuri, Punjab (150 TPH) - acquired in 2003 - and Ghaziabad, Uttar Pradesh (45 TPH). Following subsequent refurbishment and re-engineering to suit basmati rice, the Dhuri plant has the world's largest integrated basmati rice milling capacity, way ahead of its immediate competitors in India. Being a fully integrated player, the company generates other value-added by-products like bran oil, de-oiled cakes and uses rice husks for captive power plants.

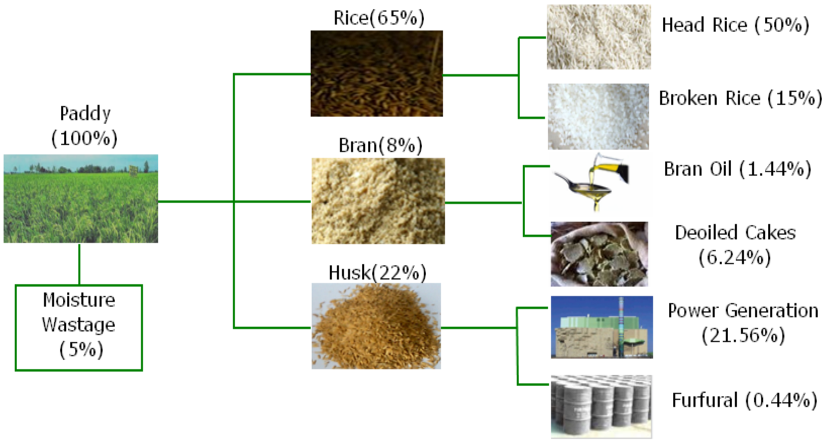
### Energy division

The company's Energy division has grown quickly in the past two years, since the company has entered into commercial sale of power. At present, KRBL's energy portfolio consists of biomass and wind power projects, with a total capacity of 55.6 MW. KRBL intends to expand its installed capacity by 8-10 MW every year for the next three to four years.

**Key milestones**

| | |
|---|---|
| **1889** | KRBL founded at Lyallpur in Faisalabad, Pakistan |
| **1947** | Re-established in India and moved operations to New Delhi |
| **1978** | Commenced exports and pioneered packaged rice |
| **1992** | Established a basmati processing plant at Noida, Uttar Pradesh |
| **1993** | Registered as public limited company; started export of 'India Gate' brand |
| **1995** | Came out with IPO, shares listed on the Bombay Stock Exchange |
| **1997** | Was awarded the prestigious APEDA trophy for being India's leading basmati rice exporter |
| **1999** | Pioneered the concept of contract farming in the states if Uttarakhand, UP and Punjab |
| **2002** | Received the ISO 9002:1994 certification from KPMG for its Ghaziabad plant; listed on the National Stock Exchange |
| **2003** | Acquired a sick rice processing plant in Dhuri (Punjab) for US$3.6mn |
| **2005** | Earned the distinction of being a four-star export house and completed the first phase of revamping its Dhuri plant to commence operations |
| **2006** | Obtained the largest GDR issue of US$12mn in the history of India's rice industry; diversified into wind power generation by setting up the 12.5 MW plant in Dhulia, Maharashtra |
| **2008** | Revenues crossed Rs 10 bn milestone. Dhulia and Ghaziabad plants turned eligible for carbon credits |
| **2010** | Highest ever turnover and net profit (Rs 15.9 bn and Rs 1.2 bn, respectively) |

### KRBL's fully integrated operations




Source: Company, CRISIL Research

## Dhuri Plant – Visit Note

KRBL's integrated rice milling plant is located at Dhuri, Punjab, about 120 kms from Chandigarh. The plant is spread over 140 acres, which includes milling operations, parboiling plant, paddy storage area including silos, grading and packaging, bran oil plant, furfural plant, officer and labour colonies and a 14 MW biomass plant. Rated milling capacity is 150 TPH, but is currently operating at 50% capacity utilisation. There are ~2,000 employees working at the plant. The plant is one of the biggest rice milling plants in India.

### Recently installed parboiling capacity

Source: Company, CRISIL Research

### Silos aid in storing paddy and rice in a moisture controlled environment

Source: Company, CRISIL Research

**Paddy is transported within the plant through conveyor belts till the packaging stage**

Source: Company, CRISIL Research

**Testing lab at the plant**

Source: Company, CRISIL Research

## Ghaziabad Plant – Visit Note

KRBL's Ghaziabad plant is spread over 100 acres and has a milling capacity of 45 TPH. The plant has its own husk fed biomass plant which has a capacity of 3.5 MW. Entire capacity is captive, and sufficient to meet the plant's requirements. Similar to the Dhuri plant, Ghaziabad plant's operations are also integrated - includes milling, parboiling, paddy storage area, grading and packaging, bran oil plant and colony.

**Paddy storage area**

Source: Company, CRISIL Research

**Processed rice storage area**

Source: Company, CRISIL Research

In-house packaging operations

Source: Company, CRISIL Research

Sorting operations

Source: Company, CRISIL Research

## Annexure: Financials

### Income statement

| (Rs mn) | FY09 | FY10 | FY11 | FY12E | FY13E |
|---|---|---|---|---|---|
| **Operating income** | **13,212** | **15,929** | **15,586** | **15,990** | **17,589** |
| **EBITDA** | **2,044** | **2,184** | **2,413** | **2,382** | **2,814** |
| **EBITDA margin** | **15.5%** | **13.7%** | **15.5%** | **14.9%** | **16.0%** |
| Depreciation | 235 | 276 | 360 | 453 | 509 |
| **EBIT** | **1,809** | **1,908** | **2,053** | **1,929** | **2,305** |
| Interest | 930 | 423 | 514 | 618 | 582 |
| **Operating PBT** | **879** | **1,485** | **1,539** | **1,311** | **1,722** |
| Other income | 42 | 20 | 41 | 56 | 62 |
| Exceptional inc/(exp) | (1) | (5) | 4 | - | - |
| **PBT** | **920** | **1,500** | **1,584** | **1,367** | **1,784** |
| Tax provision | 265 | 254 | 381 | 280 | 392 |
| Minority interest | - | - | - | - | - |
| **PAT (Reported)** | **654** | **1,245** | **1,203** | **1,087** | **1,391** |
| Less: Exceptionals | (1) | (5) | 4 | - | - |
| **Adjusted PAT** | **656** | **1,250** | **1,199** | **1,087** | **1,391** |

### Ratios

| | FY09 | FY10 | FY11 | FY12E | FY13E |
|---|---|---|---|---|---|
| **Growth** | | | | | |
| Operating income (%) | 31.7 | 19.3 | (2.0) | 2.5 | 10.0 |
| EBITDA (%) | 32.8 | 6.8 | 10.5 | (1.3) | 18.1 |
| Adj PAT (%) | 19.5 | 90.7 | (4.1) | (9.3) | 28.0 |
| Adj EPS (%) | 19.5 | 90.7 | (4.1) | (9.3) | 28.0 |
| **Profitability** | | | | | |
| EBITDA margin (%) | 15.5 | 13.7 | 15.5 | 14.9 | 16.0 |
| Adj PAT Margin (%) | 5.0 | 7.8 | 7.7 | 6.8 | 7.9 |
| RoE (%) | 16.7 | 26.1 | 20.3 | 15.6 | 17.2 |
| RoCE (%) | 16.8 | 17.6 | 15.3 | 12.4 | 14.3 |
| RoIC (%) | 15.7 | 16.2 | 13.3 | 11.4 | 12.9 |
| **Valuations** | | | | | |
| Price-earnings (x) | 7.4 | 3.9 | 4.0 | 4.4 | 3.5 |
| Price-book (x) | 1.1 | 0.9 | 0.7 | 0.6 | 0.6 |
| EV/EBITDA (x) | 5.1 | 4.8 | 5.7 | 5.4 | 4.4 |
| EV/Sales (x) | 0.8 | 0.7 | 0.9 | 0.8 | 0.7 |
| Dividend payout ratio (%) | 8.7 | 6.9 | 7.1 | 6.7 | 7.0 |
| Dividend yield (%) | 1.2 | 1.8 | 1.8 | 1.5 | 2.0 |
| **B/S ratios** | | | | | |
| Inventory days | 289 | 216 | 351 | 344 | 322 |
| Creditors days | 44 | 52 | 83 | 67 | 63 |
| Debtor days | 20 | 32 | 38 | 36 | 36 |
| Avg. working capital days | 228 | 178 | 229 | 270 | 251 |
| Gross asset turnover (x) | 4.0 | 4.0 | 3.0 | 2.7 | 2.6 |
| Net asset turnover (x) | 5.8 | 5.8 | 4.3 | 4.0 | 4.2 |
| Sales/operating assets (x) | 5.4 | 5.3 | 4.1 | 3.9 | 4.2 |
| Current ratio (x) | 6.4 | 4.9 | 4.6 | 5.6 | 5.7 |
| Debt-equity (x) | 1.4 | 1.1 | 1.4 | 1.1 | 0.9 |
| Net debt/equity (x) | 1.3 | 1.0 | 1.4 | 1.1 | 0.8 |
| Interest coverage | 1.9 | 4.5 | 4.0 | 3.1 | 4.0 |

### Per share

| | FY09 | FY10 | FY11 | FY12E | FY13E |
|---|---|---|---|---|---|
| Adj EPS (Rs) | 2.7 | 5.1 | 4.9 | 4.5 | 5.7 |
| CEPS | 3.7 | 6.3 | 6.4 | 6.3 | 7.8 |
| Book value | 17.3 | 22.0 | 26.5 | 30.6 | 35.9 |
| Dividend (Rs) | 0.2 | 0.4 | 0.3 | 0.3 | 0.4 |
| Actual o/s shares (mn) | 244 | 244 | 244 | 244 | 244 |

### Balance Sheet

| (Rs mn) | FY09 | FY10 | FY11 | FY12E | FY13E |
|---|---|---|---|---|---|
| **Liabilities** | | | | | |
| Equity share capital | 244 | 244 | 244 | 244 | 244 |
| Reserves | 3,981 | 5,110 | 6,214 | 7,215 | 8,493 |
| Minorities | - | - | - | - | - |
| **Networth** | **4,224** | **5,353** | **6,457** | **7,459** | **8,736** |
| Convertible debt | - | - | - | - | - |
| Other debt | 6,012 | 6,048 | 9,018 | 8,268 | 7,818 |
| **Total debt** | **6,012** | **6,048** | **9,018** | **8,268** | **7,818** |
| Deferred tax liability (net) | 84 | 83 | 131 | 131 | 131 |
| **Total liabilities** | **10,320** | **11,485** | **15,606** | **15,858** | **16,685** |
| **Assets** | | | | | |
| Net fixed assets | 2,170 | 3,165 | 3,833 | 3,880 | 4,120 |
| Capital WIP | 341 | 358 | 204 | 204 | 204 |
| **Total fixed assets** | **2,511** | **3,523** | **4,037** | **4,084** | **4,324** |
| **Investments** | **2** | **4** | **87** | **87** | **87** |
| **Current assets** | | | | | |
| Inventory | 7,879 | 7,813 | 12,085 | 12,016 | 12,260 |
| Sundry debtors | 707 | 1,351 | 1,577 | 1,533 | 1,687 |
| Loans and advances | 330 | 375 | 895 | 480 | 528 |
| Cash & bank balance | 334 | 444 | 53 | 195 | 401 |
| Marketable securities | - | - | - | - | - |
| **Total current assets** | **9,249** | **9,983** | **14,610** | **14,224** | **14,875** |
| **Total current liabilities** | **1,442** | **2,035** | **3,145** | **2,554** | **2,619** |
| **Net current assets** | **7,807** | **7,947** | **11,465** | **11,670** | **12,257** |
| **Intangibles/Misc. expenditure** | **-** | **11** | **17** | **17** | **17** |
| **Total assets** | **10,320** | **11,485** | **15,606** | **15,858** | **16,685** |

### Cash flow

| (Rs mn) | FY09 | FY10 | FY11 | FY12E | FY13E |
|---|---|---|---|---|---|
| Pre-tax profit | 921 | 1,505 | 1,580 | 1,367 | 1,784 |
| Total tax paid | (267) | (255) | (333) | (280) | (392) |
| Depreciation | 235 | 276 | 360 | 453 | 509 |
| Working capital changes | 1,137 | (41) | (3,915) | (62) | (381) |
| **Net cash from operations** | **2,026** | **1,485** | **(2,309)** | **1,478** | **1,520** |
| **Cash from investments** | | | | | |
| Capital expenditure | (397) | (1,288) | (874) | (500) | (750) |
| Investments and others | 2 | (2) | (84) | - | - |
| **Net cash from investments** | **(395)** | **(1,290)** | **(958)** | **(500)** | **(750)** |
| **Cash from financing** | | | | | |
| Equity raised/(repaid) | 21 | (31) | (14) | - | - |
| Debt raised/(repaid) | (1,720) | 37 | 2,970 | (750) | (450) |
| Dividend (incl. tax) | (57) | (85) | (85) | (85) | (114) |
| Others (incl extraordinaries) | (1) | (5) | 4 | - | - |
| **Net cash from financing** | **(1,757)** | **(85)** | **2,875** | **(835)** | **(564)** |
| Change in cash position | (126) | 111 | (391) | 142 | 206 |
| Closing cash | 334 | 444 | 53 | 195 | 401 |

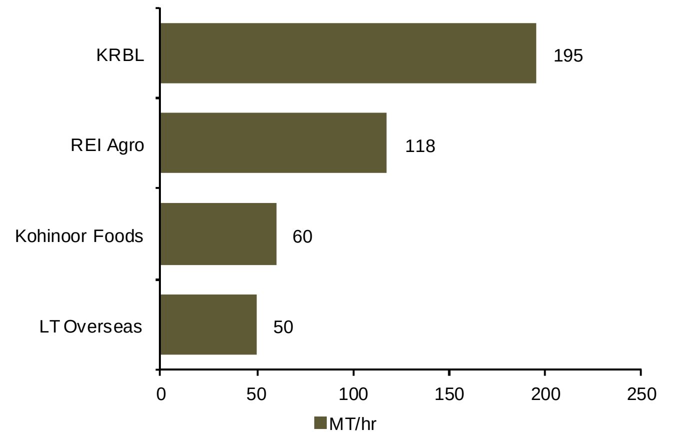
### Quarterly financials

| (Rs mn) | Q3FY11 | Q4FY11 | Q1FY12 | Q2FY12 | Q3FY12 |
|---|---|---|---|---|---|
| **Operating income** | **3,768** | **4,501** | **3,186** | **3,901** | **4,555** |
| Change (q-o-q) | -7% | 19% | -29% | 22% | 17% |
| **EBITDA** | **551** | **647** | **615** | **358** | **717** |
| Change (q-o-q) | 4% | 17% | -5% | -42% | 100% |
| **EBITDA margin** | **14.6%** | **14.4%** | **19.3%** | **9.2%** | **15.7%** |
| PAT | 255 | 300 | 234 | (225) | 239 |
| **Adj PAT** | **275** | **300** | **272** | **181** | **389** |
| Change (q-o-q) | 16% | 9% | -9% | -33% | 115% |
| **Adj PAT margin** | **7.3%** | **6.7%** | **8.5%** | **4.6%** | **8.5%** |
| **Adj EPS** | **1.1** | **1.2** | **1.1** | **0.7** | **1.6** |

**Source: CRISIL Research**

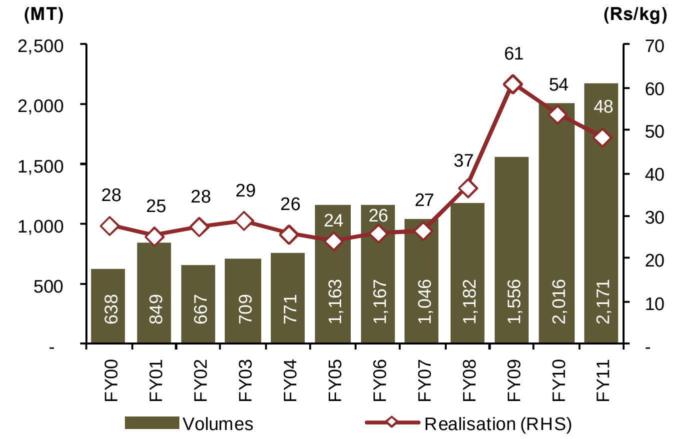
## Focus Charts

### Rated milling capacity of basmati players



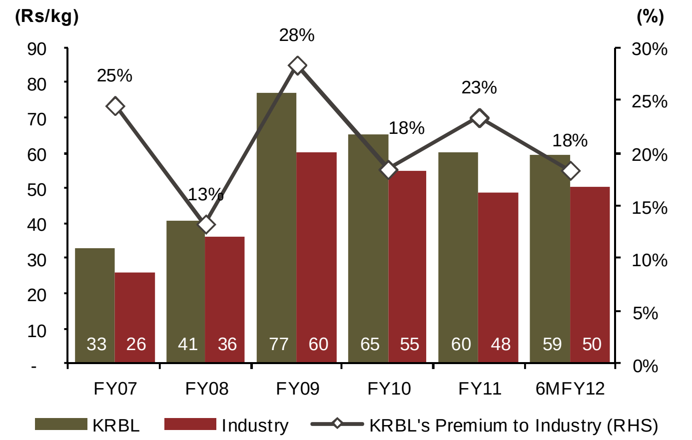

Source: Company, CRISIL Research

### Increasing export of basmati rice



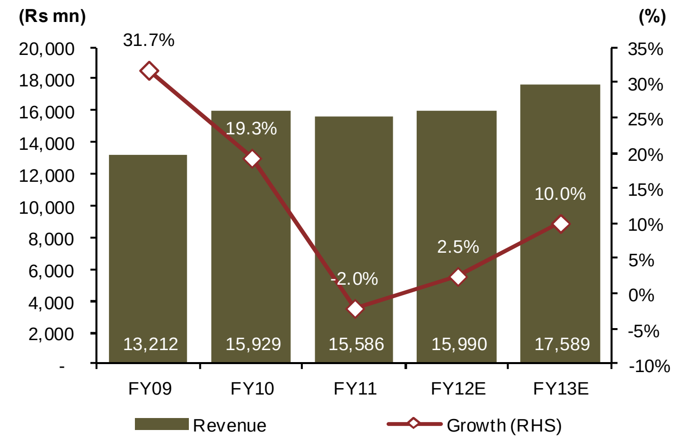

Source: Company, CRISIL Research

### KRBL's export realisation higher than industry's



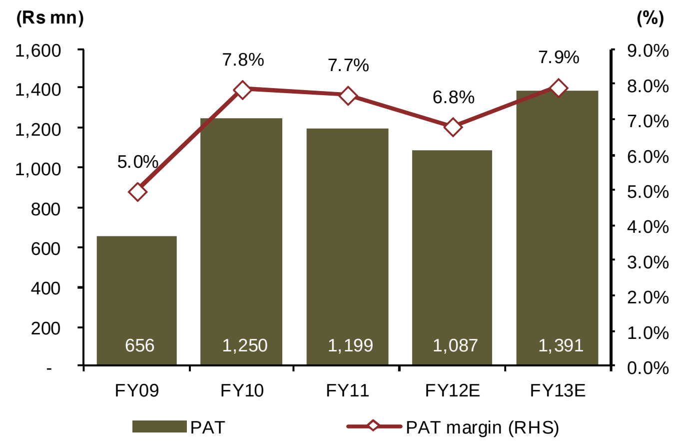

Source: Company, CRISIL Research

### Revenue growth trend



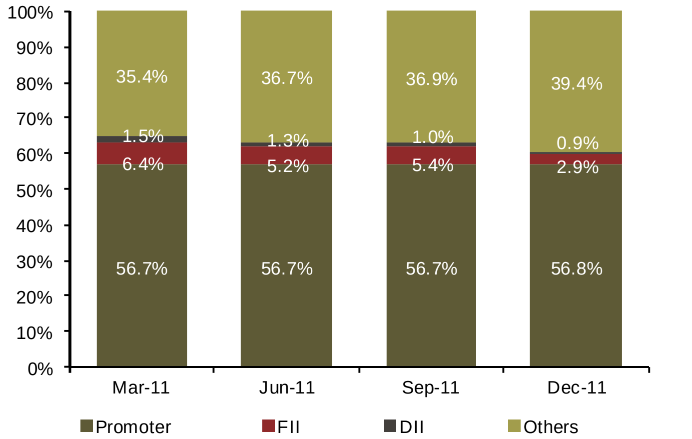

Source: Company, CRISIL Research

### PAT and PAT margin trend




Source: Company, CRISIL Research

### Shareholding pattern over the quarters




Source: Company, CRISIL Research

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## Our Capabilities

## Making Markets Function Better

### Economy and Industry Research

- Largest team of economy and industry research analysts in India
- Coverage on 70 industries and 139 sub-sectors; provide growth forecasts, profitability analysis, emerging trends, expected investments, industry structure and regulatory frameworks
- 90 per cent of India's commercial banks use our industry research for credit decisions
- Special coverage on key growth sectors including real estate, infrastructure, logistics, and financial services
- Inputs to India's leading corporates in market sizing, demand forecasting, and project feasibility
- Published the first India-focused report on Ultra High Net-worth Individuals
- All opinions and forecasts reviewed by a highly qualified panel with over 200 years of cumulative experience
- Largest independent equity research house in India, focusing on small and mid-cap companies; coverage exceeds 100 companies
- Released company reports on all 1,401 companies listed and traded on the National Stock Exchange; a global first for any stock exchange
- First research house to release exchange-commissioned equity research reports in India

### Funds and Fixed Income Research

- Largest and most comprehensive database on India's debt market, covering more than 14,000 securities
- Largest provider of fixed income valuations in India
- Value more than Rs.33 trillion (USD 650 billion) of Indian debt securities, comprising 85 per cent of outstanding securities
- Sole provider of fixed income and hybrid indices to mutual funds and insurance companies; we maintain 12 standard indices and over 80 customised indices
- Ranking of Indian mutual fund schemes covering 73 per cent of assets under management and Rs.5 trillion (USD100 billion) by value
- Retained by India's Employees' Provident Fund Organisation, the world's largest retirement scheme
- covering over 50 million individuals, for selecting fund managers and monitoring their performance

### Equity and Company Research

- Largest independent equity research house in India, focusing on small and mid-cap companies; coverage exceeds 100 companies
- Released company reports on all 1,401 companies listed and traded on the National Stock Exchange; a global first for any stock exchange
- First research house to release exchange-commissioned equity research reports in India
- Assigned the first IPO grade in India

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