



## Premiumization drives gains in challenging operating environment

Gains market share; various cost cutting initiatives undertaken

- n ABD is gaining market share; 26%+ volume growth in FY14.
- n IMFL industry's operating context gets more challenging.
- n ABD is managing cost inflation through Premiumization and Value Engineering.

Following are the key insights from our meeting with Mr Deepak Roy, Executive Vice Chairman and CEO of Allied Blenders and Distillers (ABD).

- n **ABD gains market share; 25%+ volume growth; EBITDA doubles:** In a sluggish industry growth context (industry volume growth of ~5%), ABD has gained market share with a second consecutive year of stellar volume growth. After posting 26% volume growth in FY14, it is set to deliver 28-29% volume growth in FY15. Revenue is expected to clock 32% YoY growth in FY15, with near doubling of EBITDA to INR2b. ABD expects to maintain this trajectory for FY16 as well. A sharp improvement in profitability despite the inflationary raw material environment and consistent increase in state excise duties is commendable, in our view. It is largely driven by the success of its premium brand *Officer's Choice Blue*, which has crossed 7m cases within three years of launch. We estimate EBITDA/case of INR250 for this brand.
- n **Industry operating context gets more challenging:** The operating environment for IMFL industry is getting more challenging given the penchant of state governments to treat this "sin" industry as a money spinner. Excise duty has seen 15-20% hike, with several state governments taking more drastic steps. For instance, a) Assam increased the excise duty by 70%, b) Orissa has demanded reduction in prices by 30%, c) Madhya Pradesh has demanded that prices should be the lowest offered anywhere in India plus 10% margins, d) Jharkhand has increased the licence fee for higher production of liquor and e) Telangana is contemplating re-introduction of country liquor to boost state's revenue. The Central government has also brought contract bottling of spirits under the service tax net. Government's decision to exclude liquor industry from the GST framework will result in higher costs as industry will no longer be able to avail the setoffs. Thus, the overall costs of doing business are on the rise, while price increases have been relatively difficult to come by, exerting pressure on industry's profitability.
- n **ABD manages cost inflation via Premiumization and Value Engineering:** Given the aforementioned challenging context, company still managed to improve profitability, largely driven by Premiumization and Value Engineering measures to control costs. Some of the initiatives taken include: a) increasing the contribution of in-house manufacturing. As per management, it can save INR15/case due to lower outsourcing of manufacturing operations, b) backward integration: given the significant volatility in input costs, it is looking at backward integration – manufacturing of raw materials. Thus, it will result in higher capital investments and consequent increase in leverage. We believe that the payback period for a distillation facility typically ranges from seven to eight years. c) Improved logistics planning and inventory management.

### Allied Blenders and Distillers (ABD)



**Mr Deepak Roy**  
Executive Vice Chairman  
and CEO

Mr Roy is a veteran of the Wine and Spirits industry, with over 23 years of experience in the alcohol industry. He has executed various assignments in leading multinationals like Glaxo, Ranbaxy, CPC, Warner Hindustan, UB Group and Diageo. In 1993, Mr Roy was appointed as the founding CEO of Diageo's India business. Before joining Diageo, he had garnered a decade of experience with the UB Group.

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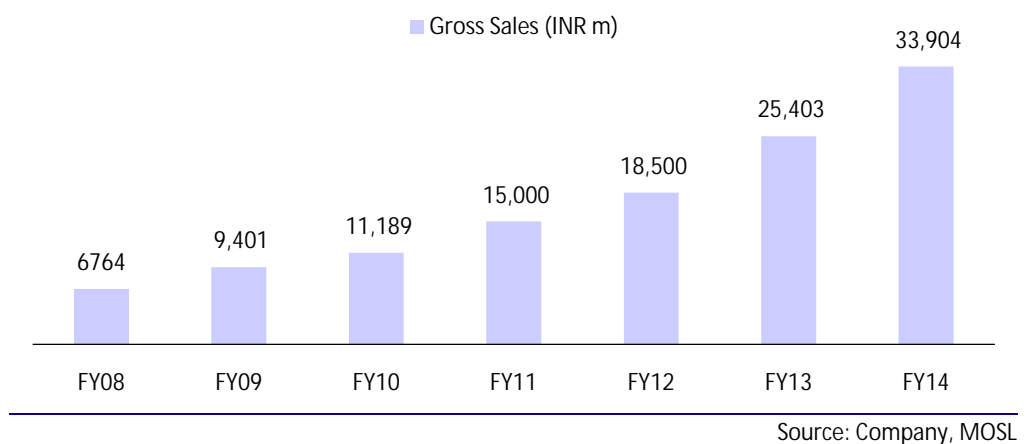
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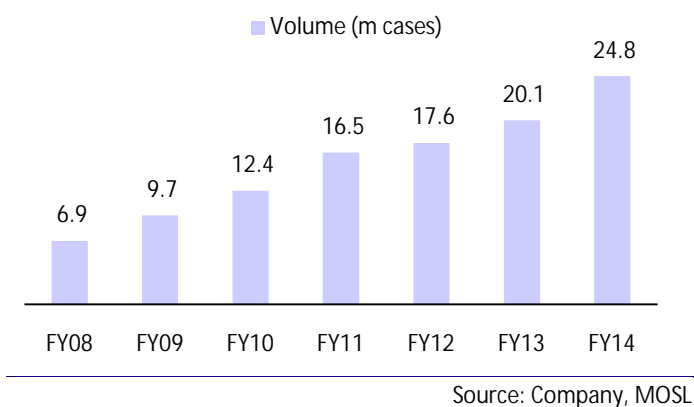
### Other takeaways

- ü Only premium brands are showing resilience in an otherwise muted industry volume growth scenario.
  - ü Expect industry volumes to grow in 6-7% range for the next three years.
  - ü EBITDA/case of Semi-Premium segment has come off from INR300-350/case to INR200-250/case band.
  - ü Vacating lower end brands will be a difficult proposition as it will impair the absorption of fixed overheads.
  - ü With MNCs controlling 70% of the market, industry's operating profitability should see some improvement.
- n Implications for UNSP:** Despite rising raw material costs and higher excise duty, ABD managed to expand its margins. ABD's success story underscores the importance of driving Premiumization to maintain/improve profitability in a challenging operating environment. We expect UNSP to improve its margins led by mix change, cost rationalization on packaging and overheads as well as lower leverage post debt repayment. UNSP remains our top pick with a target price of INR4,250.

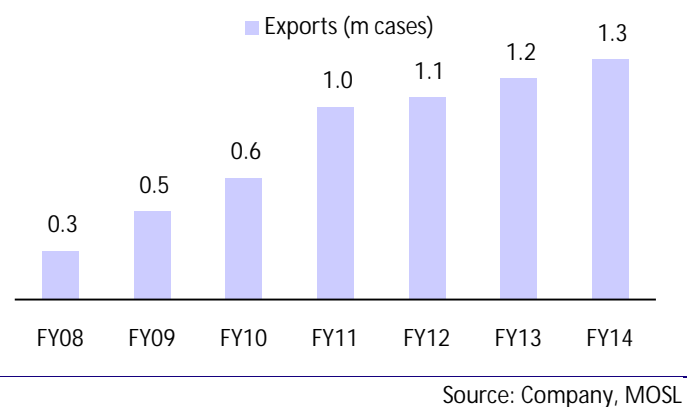
**Exhibit 1: ABD's gross sales posted 32% CAGR over FY10-14**



**Exhibit 2: Volumes doubled in last four years**



**Exhibit 3: With exports of 1.3m cases in FY14**



**Exhibit 4: ABD's product profile**

Category	Brand Name	Description
Whisky	Officer Choice	i. Flagship brand - Growing at 14% CAGR over the last 5 years
		ii. Market Share of 32% in regular whisky segment
	Officer Choice Blue	i. Premium variant of Officer Choice Whisky
	Officer Choice Black	
Brandy	Kryon Premium Brandy	i. Market share of 20% and 13% in Andhra Pradesh and Kerala resp.
	Lord and Master Brandy	
	Officer Choice Brandy	
Rum	Jolly Roger	i. Premium offering in the dark rum segment
Vodka	Wodka Gorbatschow	
	Class 21	

Source: Company, MOSL

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