September 2021

Initiating Coverage

Edelweiss
Ideas create, values protect

Varun Beverages

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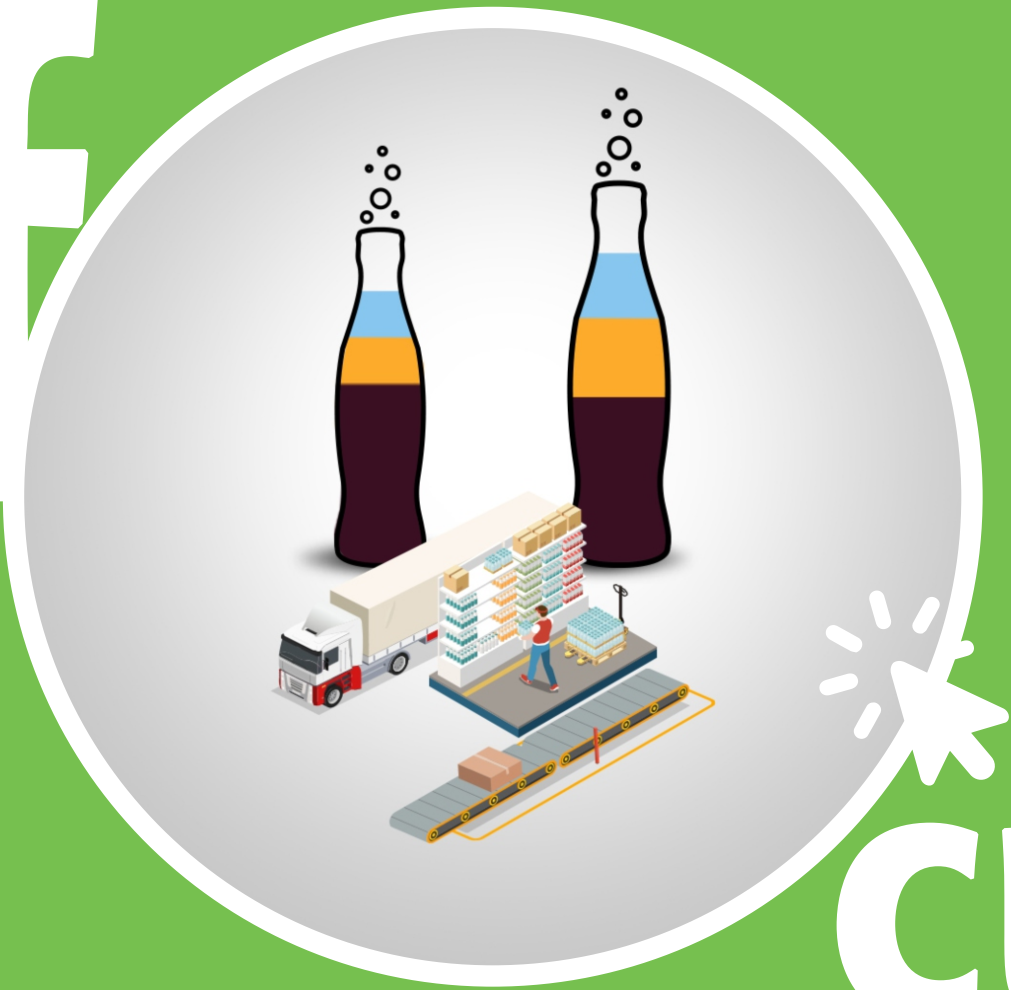

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Packed with fizz

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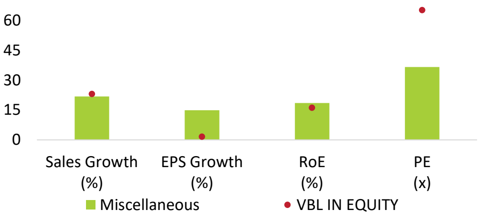
VARUN BEVERAGES

INITIATING COVERAGE

KEY DATA

Rating	BUY
Sector relative	Outperformer
Price (INR)	908
12 month price target (INR)	1,063
Market cap (INR bn/USD bn)	393/5.4
Free float/Foreign ownership (%)	31.6/19.4

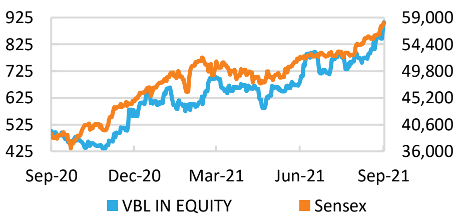
INVESTMENT METRICS



FINANCIALS (INR mn)

Year to December	CY20A	CY21E	CY22E	CY23E
Revenue	64,501	79,306	97,623	1,07,756
EBITDA	12,019	15,592	21,407	24,096
Adjusted profit	3,955	6,020	10,427	12,547
Diluted EPS (INR)	13.7	13.9	24.1	29.0
EPS growth (%)	(15.7)	1.5	75.8	108.4
RoAE (%)	11.5	16.0	25.3	25.6
P/E (x)	66.2	65.2	37.7	31.3
EV/EBITDA (x)	35.2	26.8	19.3	16.8
Dividend yield (%)	0.3	0.3	0.6	0.6

PRICE PERFORMANCE



Explore:

Financial model
Podcast
Corporate access
Video

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Varun Beverages' (VBL) prowess in scaling existing and acquired territories has prompted PepsiCo to transfer majority of its India business to VBL (85%+; CY16: 45%). Growth outlook remains robust driven by: a) rising visi cooler penetration & outlet additions; b) scale-up in acquired South & West regions; and c) vibrant product portfolio, which provide VBL firepower to meet its 10% organic volume target.

Driven by: a) further improvement in return ratios (ROCE - CY13: 5%, CY19: 17%, CY23E: 25%); and b) significant cash generation (net debt falling from INR30bn to INR12bn over CY20-23), we expect discount to FMCG companies to narrow further and thus assign 42x FY23E PE (30% discount) to VBL. Initiate with 'BUY' and TP of INR1,063.

Distribution heft; best-in-class execution and margins

VBL, PepsiCo's largest franchisee (second-largest globally outside US), has since inception made significant investments in production and distribution. A testimony to its distribution heft is its 30% rural volume share, comparable with FMCG companies, despite lower penetration of the beverage category. In addition, VBL's best-in-class execution is reflected in its strong organic volume growth. As a result, PepsiCo has been incrementally transferring a larger pie of its business to VBL (85%+ now, CY16: 45%). Despite these investments, VBL's margins are the best in India among major bottlers and one of the best globally as well.

Organic growth potential high; portfolio synced to emerging trends

VBL has multiple levers to drive its 10% organic volume growth target (we also build in the same): 1) Addition of visi coolers to existing outlets and distribution expansion–VBL reaches 2mn outlets (average 5mn for FMCG companies). VBL intends to add 0.1mn outlets per annum. 2) Scale-up of recently acquired South & West territories where market share is lower than pan-India average. 3) VBL's product mix has evolved in sync with shift in consumer preferences, clearly visible in its recent product launches. The company has an extensive beverage portfolio among all major companies, helping it capture upcoming trends.

Outlook and valuations: Cash generation phase; initiate with 'BUY'

With VBL having completed acquisition of potential territories in India, we believe, spending on acquisitions ahead will be lower. Hence, VBL will see a phase of strong cash flow generation - net debt falling from INR30bn to INR12bn over CY20-23.

The improvement in return ratios over the past decade (ROCE increased from 5% in CY13 to 17% in CY19 and further to 25% by CY23E) has settled the argument related to the nature of its business. VBL's business parameters are way superior to global bottling companies, whereas FMCG companies have a marginally better return profile. Though the premium over global bottlers is justified, the discount to Indian FMCG companies is higher than what fundamentals indicate. We expect discount to FMCG companies to narrow further and thus assign 42x FY23E PE (30% discount) to VBL. Initiate with **'BUY'** and TP of INR1,063. Growth slowdown is key risk.

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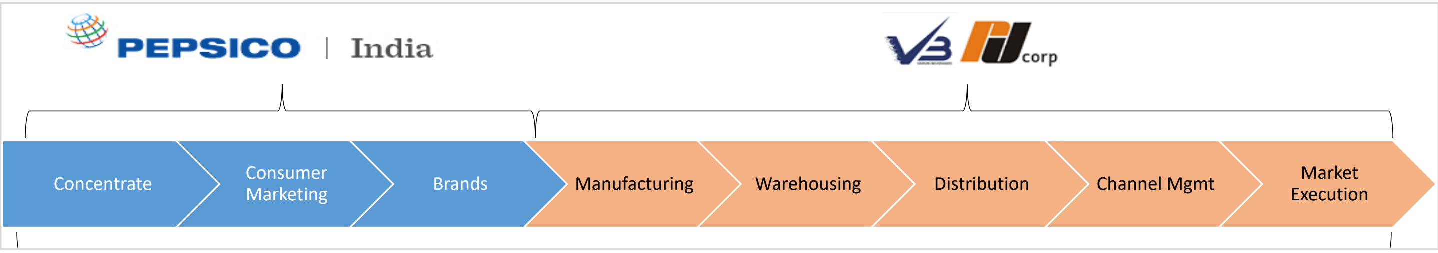
Executive Summary

Strategic association with PepsiCo to drive growth

PepsiCo offers brands, concentrates and ATL marketing support to VBL, which then takes complete control over the manufacturing and supply chain processes, and targets market share gains via BTL marketing activities. VBL has over 29 years of association with PepsiCo and considering that it accounts for 85%+ of PepsiCo's beverage sales volume in India, the two cumulatively are responsible for delivering products to customers in India.

Exhibit 1: PepsiCo and VBL India operations split



Source: Company, Edelweiss Research

Bottling is a pivotal step between high volume beverage production and distribution in smaller units to consumers. Operations require investments in multiple plants close to consumption and also in delivery fleet and refrigeration. Moreover, given the share of traditional channel in India, distribution is a critical element in the success of a brand in the beverage category.

Distribution heft; best-in-class execution

VBL has, over the past two decades, made significant investments in: a) production (31 plants across the country); and b) distribution – largest distribution infra across all franchisees in India of PepsiCo. Its network is located to maximize penetration across territories. A testimony to VBL's distribution heft is that the share of its sales coming from rural areas is comparable to other FMCG companies, despite the lower penetration of the beverage category.

In addition to its extensive distribution, VBL's execution or go-to-market strategy is best in class in the beverage industry. This reflects in its strong organic volume growth. As a result, PepsiCo has incrementally given a larger part of its business to VBL–share of PepsiCo business has increased from 45% in CY16 to 85% plus in CY20. Despite these investments and extensive network, VBL's margins are the best in India among major bottlers and one of the best globally as well.

High organic growth potential; portfolio synced to emerging trends

VBL has multiple levers to drive 10% its organic volume growth target (we also build in the same): 1) VC addition and distribution expansion--Addition of visi cooler (VC) to existing outlets where VBL reaches (only ~40% have VCs). Addition of VC itself helps drive outlet volumes driven by display and higher consumption due to chilling. Also, VBL reaches ~2mn outlets versus an average reach of 5mn for FMCG companies (India universe 10mn+). VBL intends to add 0.1mn outlets per annum, which itself can drive 5% volume growth. 2) Scale-up of recently acquired South & West territories where market share is lower than PepsiCo's pan-India average. 3) VBL's product mix and introduction are aimed at reducing concentration risk towards CSD and help diversify its portfolio given the shift in consumer preferences. This is clearly visible in its product launches over the past three years. Also, compared to other major beverage companies, VBL has the most extensive beverage portfolio. This helps the company capture emerging trends. Also, increase in consumption remains a long-term growth driver–per capita beverage consumption has posted 18% CAGR over the past decade. Still India's consumption lags even nations with lower incomes.

Phase of cash flow generation ahead

With the company having completed acquisition of majority potential territories (now controls 85% plus of PepsiCo's volumes in India), incrementally spend on acquisitions will be much lower. In addition, post the acquisition of South & West territories, VBL is operating at a peak month utilization of just 60%, limiting major capex spends for capacity. Hence, we believe, the company will see a phase of strong cash flow generation--estimate FCF over CY21-23 to be higher than CY12-20 with net debt expected to reduce from INR30bn (CY20) to INR12bn (CY23), even after keeping a buffer for acquisitions.

Outlook and valuations: Phase of cash generation; initiate with 'BUY'

We build in 10% CAGR in India volumes over CY19-23 and 7% CAGR in international territories (9% overall). We estimate 170bps EBITDA margin improvement in India driven by higher scale and integration of South & West territories. For international subsidiaries, we expect a moderation in margins from levels seen in CY20, but still ~290bps higher than CY19. Overall, the 14% EBITDA CAGR over CY19-23, along with the significant reduction in interest expenses we factor in (debt repayment), is expected to drive 28% CAGR in PAT over CY19-23.

The improvement in return ratios over the past decade has settled the argument related to the nature of the company's business. If we compare VBL's business parameters, they are way superior to global bottling companies, whereas FMCG companies have a marginally better return profile. Also, a key differentiation versus global peers is the market size it caters to (population of ~1.35bn). Another aspect unique to India is the distribution split of beverage category (~90% general trade) which renders VBL's execution much more vital and strategic versus other global markets.

Though this premium over global bottlers is justified, the discount to Indian FMCG companies is higher than what fundamentals suggest. We expect discount to FMCG companies to narrow further and thus assign 42x FY23E PE (30% discount) to VBL. Initiate with **'BUY'** and TP of INR1,063.

Exhibit 2: Comparison of VBL with related peers

Parameter	Variable	VBL	India FMCG	Global Bottlers
Growth	Revenue CAGR FY20-23	11	11	5
Growth	EBITDA CAGR FY20-23	14	15	7
Margin	FY23 EBITDA Margin	22	17	20
Return profile	FY23 Post tax RoCE	17	25	14
Cash flow yield	FY23E FCFF Yield	2.4	1.7	NM
FY23E PE	Median	35	58	8
FY23E EV/EBITDA	Median	18	35	7

Source: Company, Bloomberg, Edelweiss Research

The Story in Charts

Exhibit 3: Extensive distribution infrastructure in place

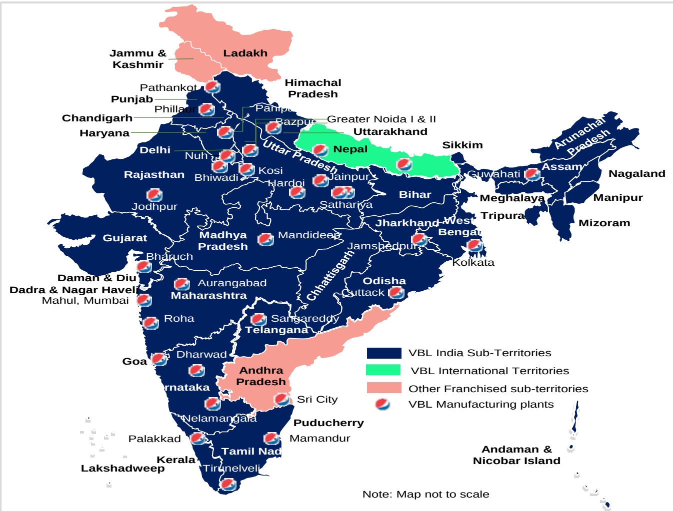


Exhibit 4: Network plus execution has driven organic growth

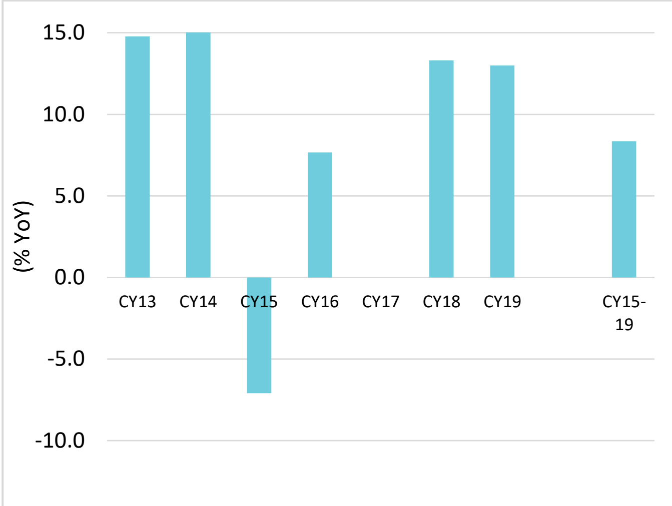


Exhibit 5: Share of PepsiCo's business on the rise

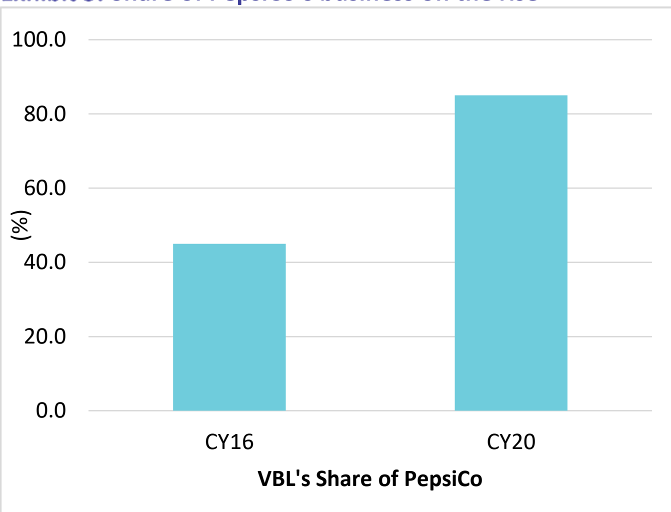


Exhibit 6: Expansion potential to help achieve organic growth

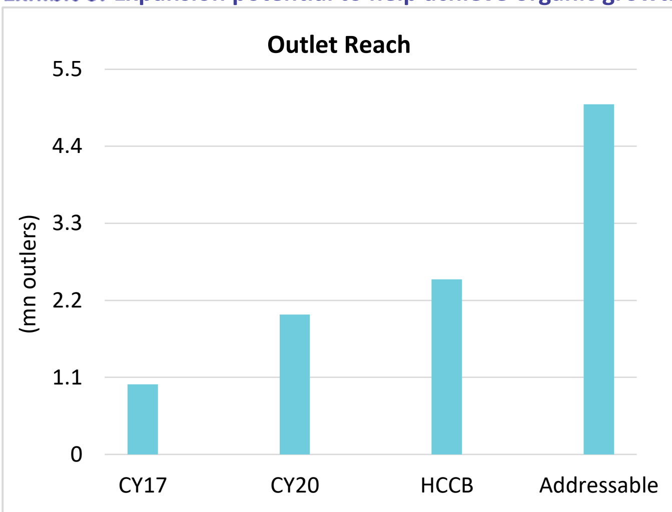


Exhibit 7: Significant improvement in return ratios

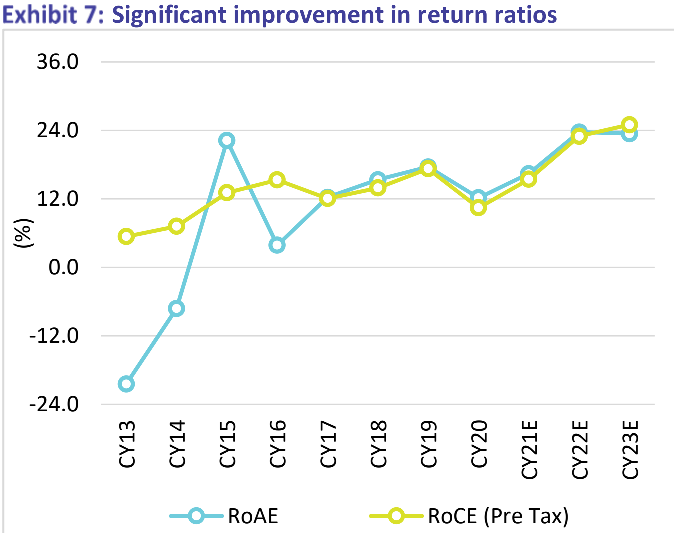
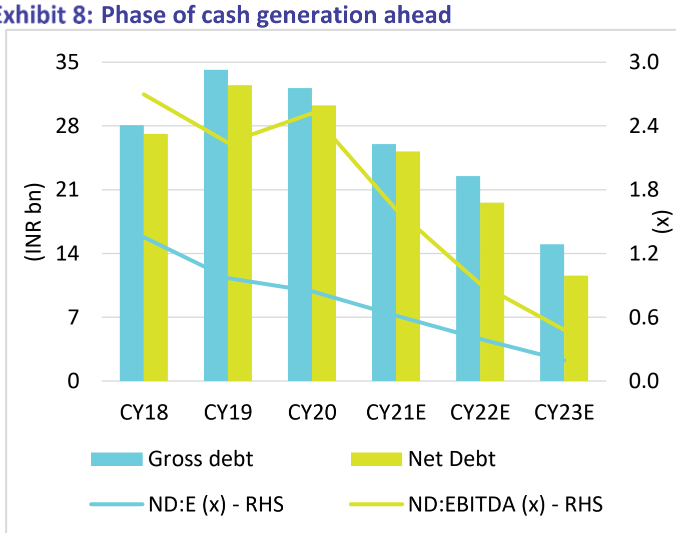


Exhibit 8: Phase of cash generation ahead



Source: Company, Edelweiss Research

Financial Statements

Income Statement (INR mn)

Year to December	CY20A	CY21E	CY22E	CY23E
Total operating income	64,501	79,306	97,623	1,07,756
Gross profit	36,862	44,252	54,020	59,519
Employee costs	8,897	9,658	10,417	11,234
Other expenses	15,946	19,003	22,196	24,189
EBITDA	12,019	15,592	21,407	24,096
Depreciation	5,287	5,651	6,077	6,625
Less: Interest expense	2,811	2,124	1,788	1,398
Add: Other income	370	484	629	916
Profit before tax	4,290	8,302	14,172	16,989
Prov for tax	52	1,998	3,462	4,159
Less: Other adj	0	0	0	0
Reported profit	3,955	6,020	10,427	12,547
Less: Excp.item (net)	0	0	0	0
Adjusted profit	3,955	6,020	10,427	12,547
Diluted shares o/s	289	433	433	433
Adjusted diluted EPS	13.7	13.9	24.1	29.0
DPS (INR)	2.5	3.0	5.0	5.0
Tax rate (%)	1.2	24.1	24.4	24.5

Balance Sheet (INR mn)

Year to December	CY20A	CY21E	CY22E	CY23E
Share capital	2,887	4,330	4,330	4,330
Reserves	32,353	35,631	43,893	54,275
Shareholders funds	35,240	39,961	48,224	58,606
Minority interest	648	931	1,213	1,496
Borrowings	32,161	26,000	22,500	15,000
Trade payables	5,114	4,907	6,104	6,753
Other liabs & prov	9,020	10,535	12,472	13,544
Total liabilities	84,474	84,080	92,661	97,769
Net block	58,272	57,621	59,544	61,669
Intangible assets	5,814	5,814	5,814	5,814
Capital WIP	668	668	668	668
Total fixed assets	64,754	64,103	66,026	68,151
Non current inv	0	0	0	0
Cash/cash equivalent	1,901	801	2,917	3,413
Sundry debtors	2,418	2,379	2,929	3,233
Loans & advances	4,151	4,758	5,857	6,465
Other assets	11,215	12,002	14,897	16,472
Total assets	84,474	84,080	92,661	97,769

Important Ratios (%)

Year to December	CY20A	CY21E	CY22E	CY23E
India CSD (%)	(13.7)	20.0	30.0	8.0
India NCB (%)	(18.8)	40.0	20.0	15.0
India PDW (%)	(23.7)	40.0	20.0	15.0
EBITDA margin (%)	18.6	19.7	21.9	22.4
Net profit margin (%)	6.1	7.6	10.7	11.6
Revenue growth (% YoY)	(9.5)	23.0	23.1	10.4
EBITDA growth (% YoY)	(17.0)	29.7	37.3	12.6
Adj. profit growth (%)	(15.7)	52.2	73.2	20.3

Free Cash Flow (INR mn)

Year to December	CY20A	CY21E	CY22E	CY23E
Reported profit	3,955	6,020	10,427	12,547
Add: Depreciation	5,287	5,651	6,077	6,625
Interest (net of tax)	2,777	1,612	1,351	1,056
Others	(16)	2,792	4,181	4,784
Less: Changes in WC	(1,108)	(593)	(1,006)	(544)
Operating cash flow	10,120	13,485	17,569	20,309
Less: Capex	(5,597)	(5,000)	(8,000)	(8,750)
Free cash flow	4,523	8,485	9,569	11,559

Assumptions (%)

Year to December	CY20A	CY21E	CY22E	CY23E
GDP (YoY %)	4.8	(6.0)	7.0	6.0
Repo rate (%)	4.4	3.5	3.5	4.0
USD/INR (average)	70.7	75.0	73.0	72.0
Sub Volume (%)	(1.4)	15.0	7.0	7.0
India Margin (%)	17.6	19.8	22.6	23.1
Sub Margin (%)	21.8	19.2	19.1	19.0
Capex (INR mn)	5,597	5,000	8,000	8,750

Key Ratios

Year to December	CY20A	CY21E	CY22E	CY23E
RoE (%)	11.5	16.0	25.3	25.6
RoCE (%)	10.5	15.5	22.8	25.9
Inventory days	120	98	88	85
Receivable days	12	11	10	10
Payable days	65	52	47	44
Working cap (% sales)	9.0	7.4	7.4	7.4
Gross debt/equity (x)	0.9	0.6	0.5	0.2
Net debt/equity (x)	0.8	0.6	0.4	0.2
Interest coverage (x)	2.4	4.7	8.6	12.5

Valuation Metrics

Year to December	CY20A	CY21E	CY22E	CY23E
Diluted P/E (x)	66.2	65.2	37.7	31.3
Price/BV (x)	7.4	9.8	8.1	6.7
EV/EBITDA (x)	35.2	26.8	19.3	16.8
Dividend yield (%)	0.3	0.3	0.6	0.6

Source: Company and Edelweiss estimates

Valuation Drivers

Year to December	CY20A	CY21E	CY22E	CY23E
EPS growth (%)	(15.7)	1.5	75.8	108.4
RoE (%)	11.5	16.0	25.3	25.6
EBITDA growth (%)	(17.0)	29.7	37.3	12.6
Payout ratio (%)	18.2	21.6	20.8	17.3

Investment Rationale

- VBL's track record of scaling its existing and acquired territories has seen PepsiCo transfer majority of its India business to VBL (85%+ now, 45% in CY16).
- Growth outlook remains robust driven by: a) rising visi cooler penetration and outlet additions; b) scale-up in acquired South & West territories; and c) extensive product portfolio, all of which can help VBL achieve its 10% organic volume target.
- With VBL having completed acquisition of potential territories in India, we believe, spending on acquisitions ahead will be much lower. Hence, the company will see a phase of strong cash flow generation--estimate FCF over CY21-23 to be higher than CY12-20 with net debt expected to reduce from INR30bn (CY20) to INR12bn (CY23).

Distribution heft; best-in-class execution

A strategic association with PepsiCo to drive growth

PepsiCo offers brands, concentrates and ATL (above the line) marketing support to VBL, which then takes complete control over the manufacturing and supply chain processes and targets market share gains via BTL (below the line) marketing activities. VBL has over 29 years of association with PepsiCo and considering that it accounts for 85%+ of PepsiCo's beverage sales volume in India, the two cumulatively are responsible for delivering products to customers in the country.

Exhibit 9: PepsiCo and VBL India operations split

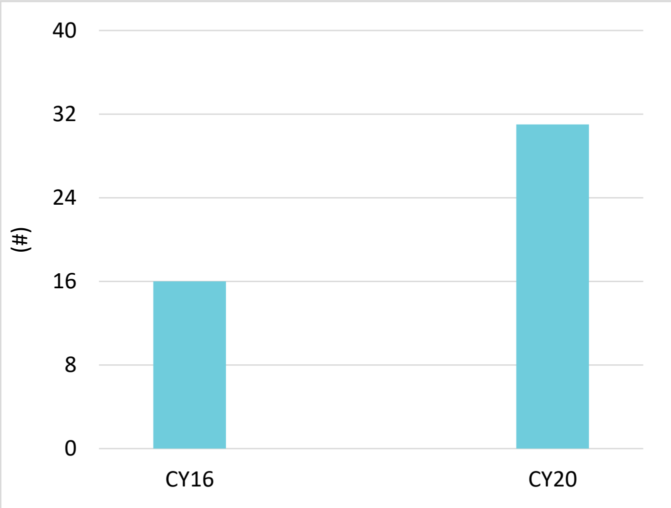
Source: Company, Edelweiss Research

Wide distribution infrastructure in place

The soft drinks distribution entails relatively complex distribution because of the nature of the packaging, refrigeration requirements and limited shelf life. Bottling is a pivotal step between high volume beverage production and distribution in smaller units to consumers. Operations require investment in multiple plants close to consumption and also in delivery fleet and refrigeration.

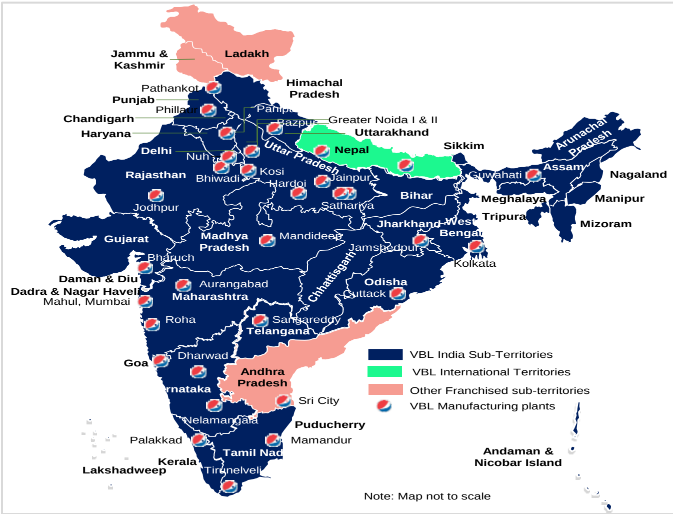
VBL has, over the past two decades, made significant investments in: a) **production facilities -** over the past five years it has nearly doubled the number of production facilities (including inorganic) driving faster reach and reducing freight cost; and b) **distribution** - in logistics (vehicles) and refrigeration (visi coolers) to create a well-entrenched distribution network which covers urban, semi-urban and rural markets.

Exhibit 10: Expansion in production facilities



Source: Company, Edelweiss Research, Note: Data for India

Exhibit 11: Widespread across the country



Source: Company, Edelweiss Research

Exhibit 12: VBL's distribution infrastructure

Distribution	CY16	CY17	CY18	CY19	CY20
Visi-Coolers	4,58,000	4,74,500	5,50,000+	7,75,000+	8,00,000+
Distribution Vehicles	2,024	2100+	2400+	2500+	2500+
Primary distributors	1,186	1000+	1100+	1500+	1500+
Depots	71	72	80+	90+	90+

Source: Company, Edelweiss Research

VBL's production capabilities and distribution network enable it to effectively respond to competitive pressures, market demand and evolving consumer preferences across targeted territories.

Exhibit 13: VBL has a much denser network vs. HCCB for same reach

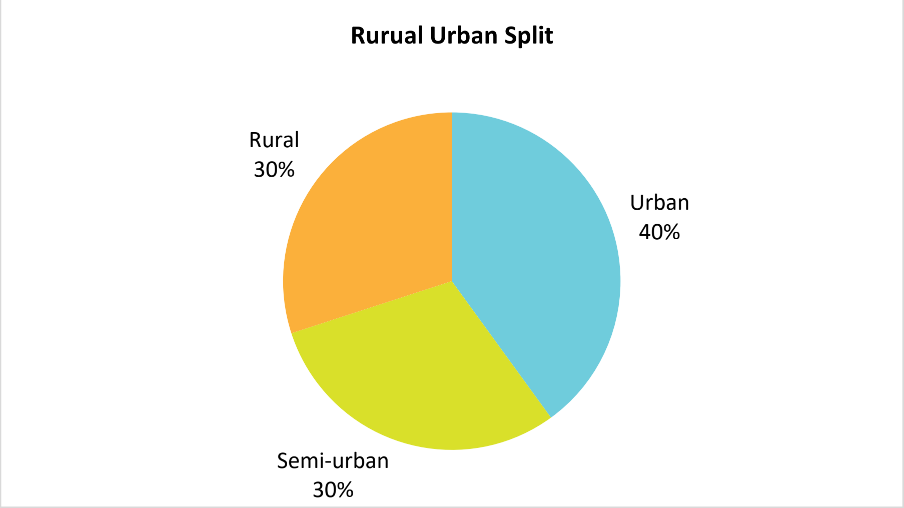
	HCCB	VBL
Factories (#)	15	31
Warehouses (#)	32	90+
Retailers (mn outlets)	2.5	2+
States + UT (#)	25	34
% of Brand business	60	85

Source: Edelweiss Research, Note: HCCB - Hindustan Coca-Cola Beverages Pvt. Ltd.

Extensive rural reach comparable to many FMCG companies

VBL has a strong sales and distribution network with its reach straddled across various point of sales – grocery stores, modern trade, e-commerce channels, bars and restaurants. To increase penetration, it has also installed >800,000 visi coolers across its territories.

Exhibit 14: Rural and semi-urban dominate mix



Source: Company, Edelweiss Research

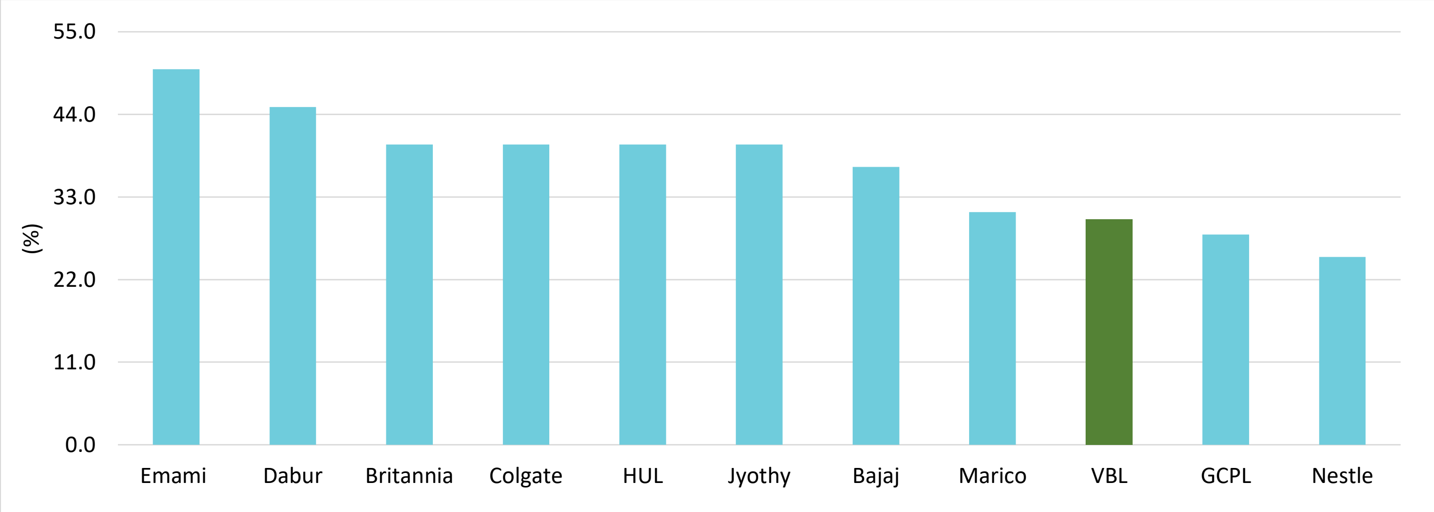
Note: Share based on volumes

The company's strong region specific sales team also reaches out directly to multiple outlets – on trade as well as off-trade channels. The distribution network is located to maximize market penetration across licensed sub-territories in India with an increased focus on higher growth markets such as semi-urban and rural sub-territories.

One of the biggest challenges for the Indian soft drink industry is penetration in rural markets, which form about 67% of the country's total population. In addition to the vast population, reaching rural consumers in the vast geography of the country poses significant challenges in distribution. Making carbonated drinks available to this vast population in chilled form is also a challenge.

A testimony to VBL's distribution heft is a reflection of its sales from rural areas, which is at present comparable to other FMCG companies despite the beverage category being underpenetrated than other major consumption categories like biscuits, home & personal care etc.

Exhibit 15: VBL's rural reach comparable to many FMCG companies despite lower penetration of overall beverage category



Source: Company, Edelweiss Research

Note: For rural reach considered only rural areas as disclosed by VBL. VBL's share represents rural contribution to volumes.

Best-in-class execution reflects in volume growth and increased share of territories

Given the share of traditional channel in beverage sales (kiranas), distribution becomes a critical element in the success of a brand in the beverage category. Availability and display become as important, if not more, than brand visibility. Eventually, this is a business of execution i.e., ensuring seamless availability across territories. In addition, increasing throughput in existing stores and additional touchpoints are also critical aspects.

Exhibit 16: India beverage market channel split

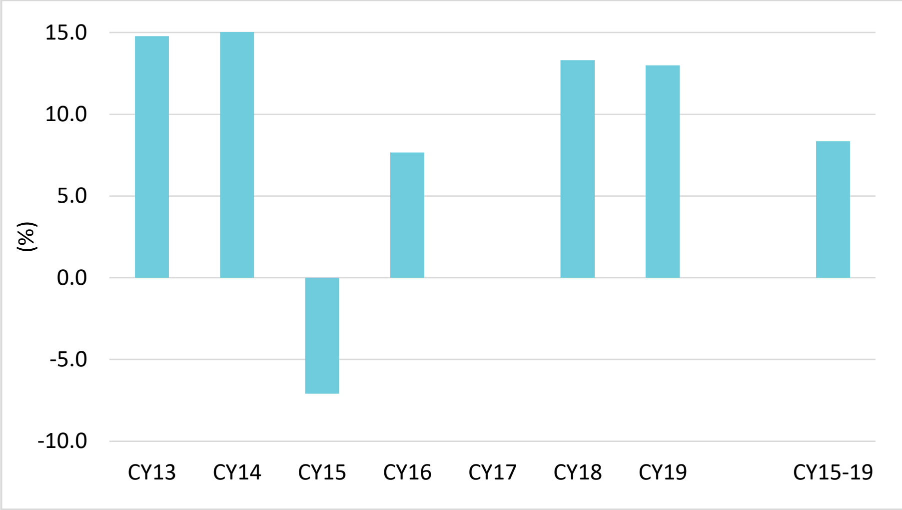
Source: Technopak, Edelweiss Research

To drive better penetration and market share, VBL uses its distribution network to regularly make its products available. It has kept adding visi coolers which helps drive incremental sales per outlet. The company's sales team works closely with PepsiCo to develop and implement local advertising and marketing strategies. VBL drives sales growth via: (i) ensuring ready availability of products; (ii) expanding distribution reach into tier III- IV geographies; (iii) introducing new flavours targeted at expanding consumer segment; (iv) efficient distribution and logistics support; and (v) implementing effective local marketing and product promotions.

It focuses on customer level marketing including managing distributor and retailer relationships, special occasion-based marketing at points of sale and implementing promotional activities to strengthen its distribution network. This apart, VBL also works with PepsiCo's active product development team to strategize new product launches in India.

Also, VBL has historically driven strong volume growth organically as it has acquired any new territories. Overall, the business has been able to drive a consistent volume growth over the past decade driven by its execution and go-to-market strategy.

Exhibit 17: Strong organic volume growth trends

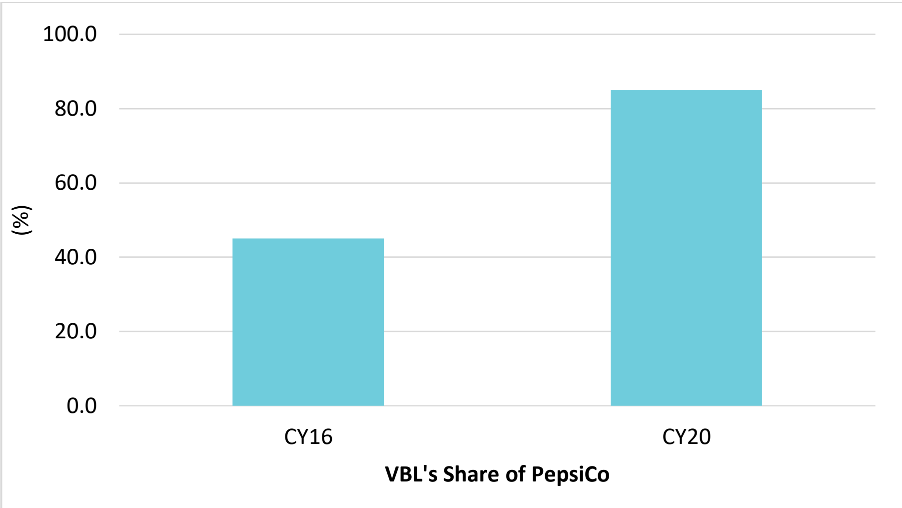


Source: Company, Edelweiss Research

VBL's demonstrated ability to grow PepsiCo product sales in its territories and sub-territories has led to PepsiCo India licensing additional franchises to VBL, including sub-territories in India that were earlier directly operated by PepsiCo or by third-party bottlers.

The importance of execution is clearly visible in the territories that VBL has acquired from other franchisees and Pepsi itself where post acquisition volumes in these territories have seen significant improvement. A case in point is the territories VBL acquired from SMV Group (acquired in CY17, start of CY18); these territories posted volume growth much higher than VBL's growth in CY19.

Exhibit 18: VBL's share of Pepsi business



Source: Company, Edelweiss Research

Over the past two and half decades, VBL has expanded the number of PepsiCo licensed territories and sub-territories, produced and distributed wider range of PepsiCo beverages, introduced various SKUs in its portfolio and expanded its distribution network.

Exhibit 19: Expanding territory portfolio

Year	Territory (India)	Countries
1995	Certain designated parts of 2 States & 1 UT	1
2005	5 States & 1 UT	2
2015	17 states & 2 UTs	4
2016	17 states & 2 UTs	6
2018	21 states & 2 UTs	6
2019	27 states and 7 UTs	6

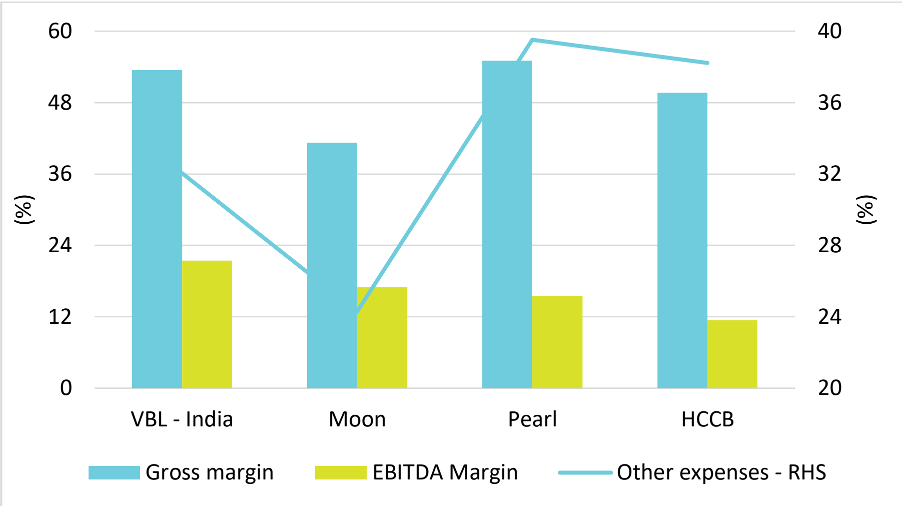
Source: Company, Edelweiss Research

Execution along with efficiency – best in class margins

Despite its significant investment in people and infrastructure, VBL has managed to achieve best-in-class margin across all major bottlers in India. The company has always been a cost focused and efficient operator in running day-to-day business.

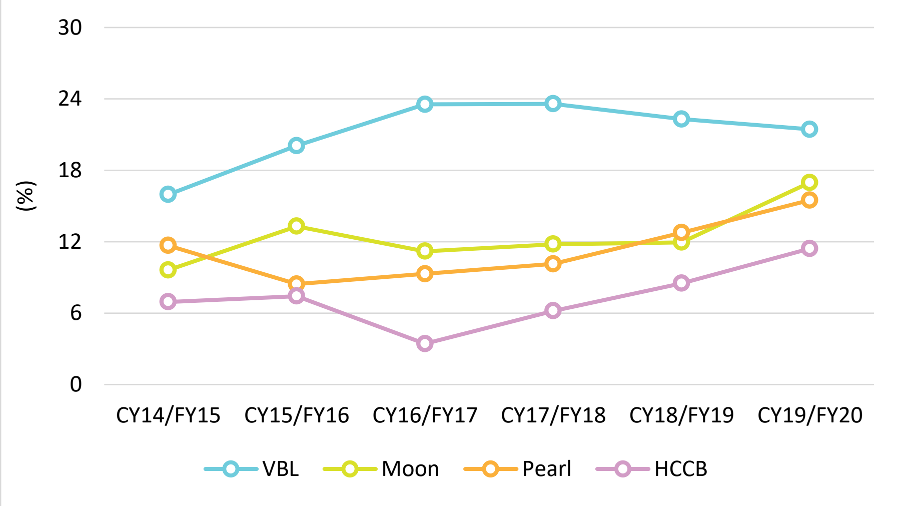
VBL has also made significant investments in establishing a robust back-end infrastructure, be it manufacturing of preforms, crowns, caps, shrink-wrap films, corrugated boxes and plastic crates. This ensures limited reliance on third-party vendors. It also helps the company harness operating leverage benefits, thereby boosting margin.

Exhibit 20: VBL's margin a combination of higher GM and lower other expenses



Source: Company, MCA, Edelweiss Research, Note: Other expenses includes employee costs

Exhibit 21: Consistently clocking best-in-class EBITDA margin



Source: Company, MCA, Edelweiss Research

Exhibit 22: VBL's per case India margin analysis

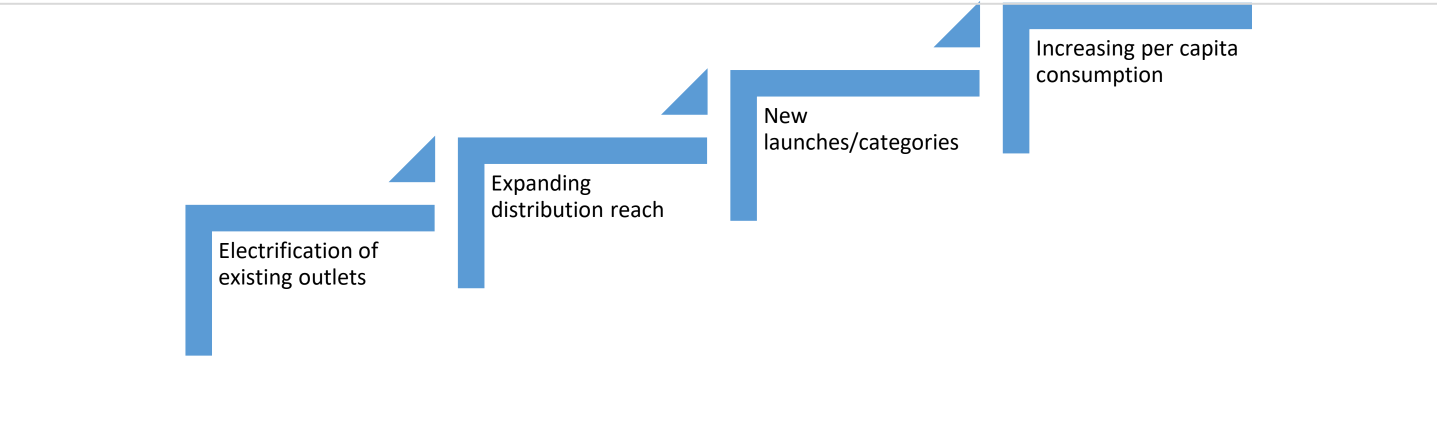
	CY12	CY13	CY14	CY15	CY16	CY17	CY18	CY19
India								
Cases	114	133	144	209	225	224	274	403
Revenue (Net of Excise)	127	131	140	137	132	137	141	139
Total RM Cost	75	78	81	71	61	63	65	65
Gross Profit	52	53	59	66	72	74	76	75
Gross margin (%)	*40.7*	*40.8*	*42.0*	*48.1*	*54.2*	*54.1*	*54.1*	*53.5*
Employee Cost	9	9	10	12	12	14	15	16
Power & Fuel	6	6	6	5	6	6	6	5
Repairs	2	3	4	4	4	4	4	3
Sales & Promotion	0	1	1	1	1	1	1	2
Freight & Distribution	0	5	6	8	10	8	11	11
Other Variable	1	2	2	2	2	3	3	2
Other Fixed expenses	16	9	8	6	6	7	6	6
Other Expenditure	26	27	26	27	28	28	30	29
EBITDA	17	17	22	28	31	32	31	30

Source: Company, Edelweiss Research

Organic growth potential high; portfolio synced to emerging trends

VBL has multiple levers to drive volume growth in existing categories for sustainable future.

Exhibit 23: Multiple levers to drive volume growth



Source: Edelweiss research

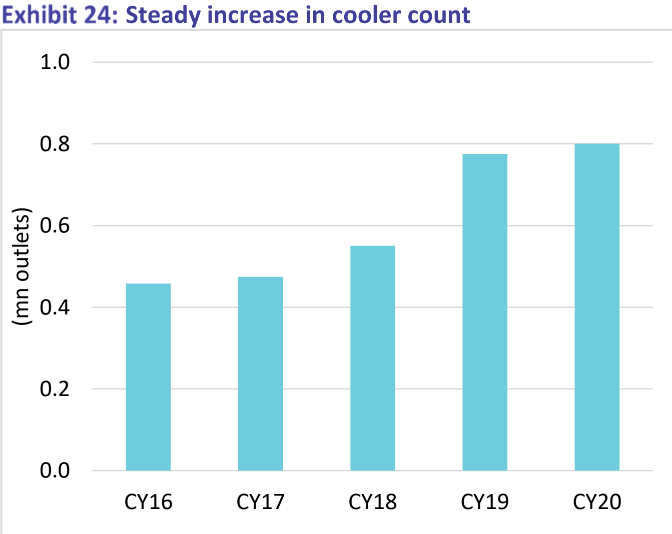
Cooler addition and outlet expansion remain immediate growth drivers

India is not a 'soft drink' market. It is a 'cold-drink' market. Refrigeration is a key element in this tropical country, and it needs to be enhanced

The first lever remains addition of visi coolers in existing outlets where VBL reaches. Coolers play an integral role in a brand's plans for success. Increasing cooler coverage and the number of cooler doors among retailers is important to ensure that a wide variety of products are properly displayed, while strengthening merchandising capacity in the traditional sales channel to significantly improve point-of-sale execution. Refrigeration is a key element in this tropical country and it needs to be enhanced. While visibility and taste are important in a country like India, availability is extremely vital.

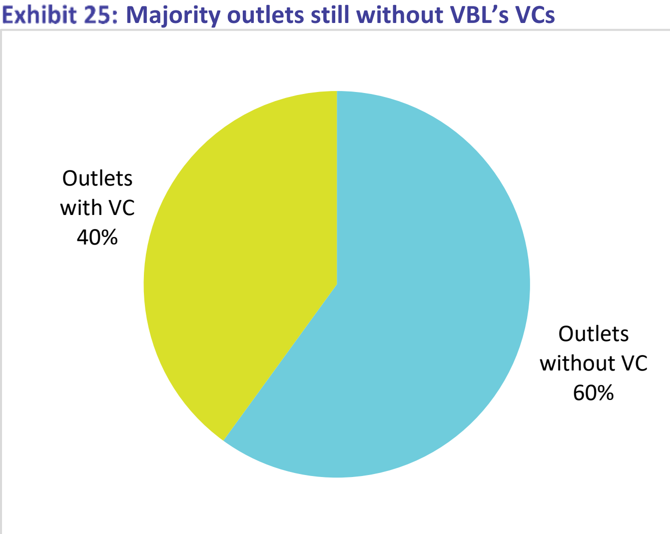
As a starting point, ~60% of VBL's outlets are still without VBL's VC. This is due to either infrastructure reasons like non-availability of regular electricity supply or stocking of competitor VC. However, for outlets which don't have any VC, given that the cost of the machine is borne by VBL, the issue mainly boils down to infrastructure issues, which are improving driven by rising electrification in the country.

Exhibit 24: Steady increase in cooler count



Source: Company, Edelweiss Research

Exhibit 25: Majority outlets still without VBL's VCs

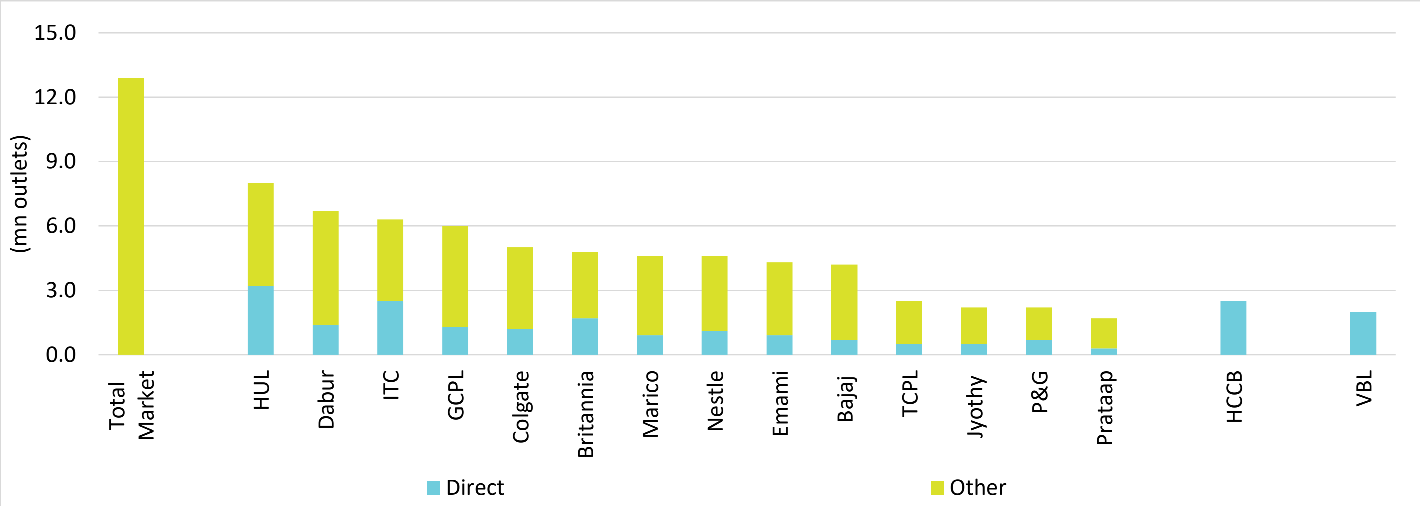


Source: Company, Edelweiss Research

Once a visi cooler is installed, the customer executive (from VBL) tries to get the Pepsi products placed prominently at the front. Addition of a visi cooler itself helps drive outlet volumes driven by prominent display and higher consumption due to chilling of products. This remains a low hanging fruit for VBL to drive volume growth. It is targeting to add ~40,000 visi coolers per annum to improve penetration.

VBL currently reaches only ~2mn outlets pan-India. HCCB, Coco-Cola's largest bottler, has a reach of ~2.5mn outlets (serves 60% of Coca Cola's territories vs. 85% plus that VBL serves for PepsiCo), which is naturally an extension available for VBL. In addition, if we look at the total addressable market, India's population of retail outlets is ~13mn and major FMCG companies on average reach in excess of 5mn outlets. While many of these outlets may not be relevant from beverage stocking perspective, even if we consider the current reach of major FMCG players as VBL's potential, then it still implies a penetration of less than 50%, enhancing growth visibility for many years ahead.

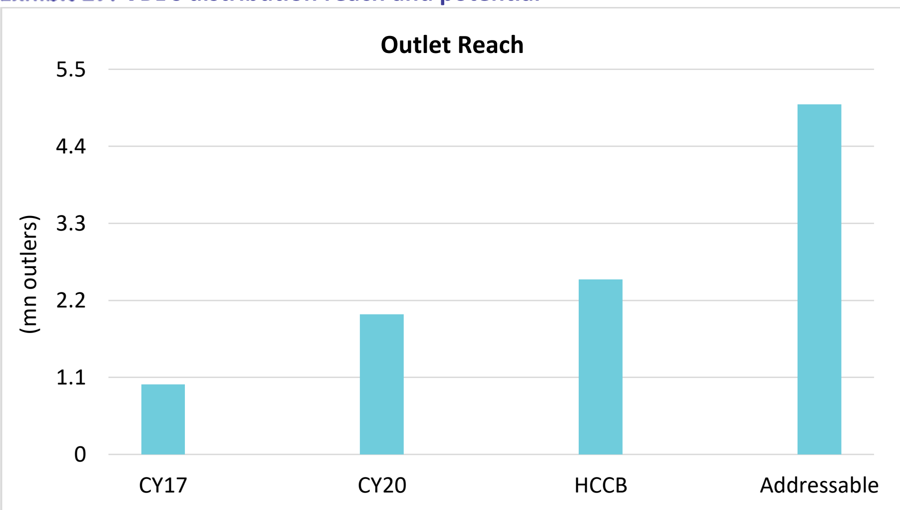
Exhibit 26: VBL's outlet reach has huge potential for expansion



Source: Company, Edelweiss Research

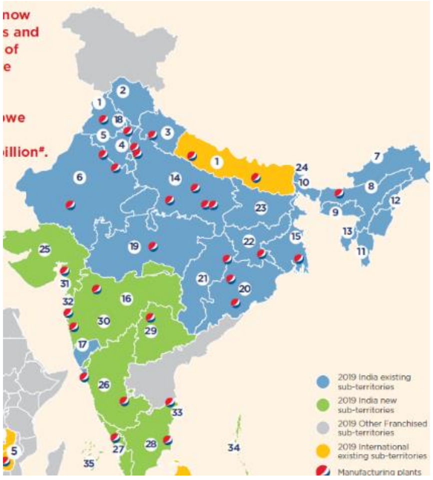
VBL itself is targeting to add around 0.1mn outlets additionally per annum. On a base of 2mn outlets it currently reaches, that drives a growth of 5%.

Exhibit 27: VBL's distribution reach and potential



Source: Company, Edelweiss Research

Note: Addressable reach is an Edelweiss estimate



South & West: Potential volume drivers driven by expanding reach

The South and West territories were operated by PepsiCo before VBL acquired them in CY19. Distribution and volumes were downsized, before VBL took over. Also, PepsiCo's current market share in South & West is lower than its national average.

VBL has in its previous acquisitions of territories successfully managed to scale-up volumes and market share – seen in the case of territories acquired from SMV Beverages in CY18. According to management, the biggest improvement it needs to focus on is to increase the number of outlets in South and West, which were not being served during PepsiCo's time. The company is addressing this by adding more people, vehicles, distributors and visi coolers.

As per VBL, it has not even reached 50-60% of the outlets and will take around two more years to reach full penetration. Also, since acquisition in May 2019, VBL has still not had the opportunity to drive sales as it has missed out on the peak season due to covid.

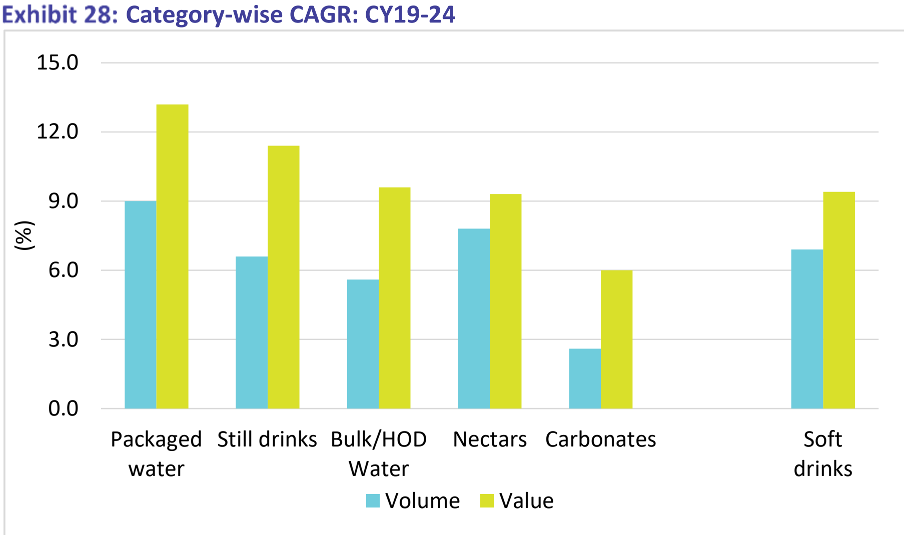
Portfolio synced to emerging trends; extensive NCB portfolio

In India, non-cola flavours are more popular and their growth rate has traditionally been higher than cola flavours. To capitalise on this, VBL is gearing to enhance penetration and distribution reach of Mountain Dew as well as introduce new variants of Seven-Up.

In addition, consumer preference for healthy beverages is prompting companies to re-examine their product strategies and launch products suited to the next generation of consumers. Given the shift in consumer preferences and lifestyles, carbonated beverages are expected to lose market share to healthier beverages.

With rising number of health conscious consumers, India has been witnessing significant growth in the NCB segment in recent times, with new products getting introduced regularly in the market. This segment majorly comprises juice-based product variants.

Exhibit 28: Category-wise CAGR: CY19-24



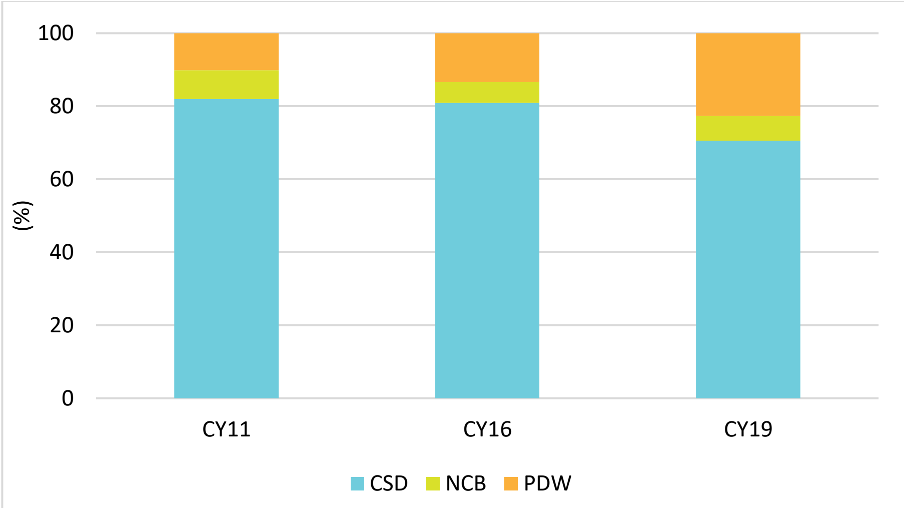
Source: Company, Edelweiss Research

Note: Estimates are pre covid impact

PepsiCo, given the background of losing market share in Tropicana juice, transferred the sales and distribution rights to VBL in 2018. VBL also took up the rights for Gatorade and Quaker Oats Milk. PepsiCo has since discontinued Quaker Oats Milk and VBL has thus launched dairy via the Cream Bell segment. VBL has recently commenced production at Pathankot for manufacturing Tropicana juices.

The company's future strategy for NCB segment includes: 1) enhancing market penetration and availability through a widespread distribution network; 2) developing brand preferences via sampling and visibility programmes; and 3) launching new and novel flavours introduced by PepsiCo.

Exhibit 29: VBL's volume mix



Source: Company, Edelweiss Research

Note: CSD – Carbonated Soft Drinks, NCB - Non Carbonated Beverages, PDW – Packaged Drinking Water

VBL's product mix and introduction of new products is aimed towards reducing concentration risk and diversifying its portfolio. This is clearly visible in its product launches over the past three years. Majority of the new launches have been in the non CSD category. In fact, it has entered new categories like energy drink, dairy, etc. *(See Exhibit below)*.

Exhibit 30: Product portfolio evolution

Product	Sub-brands	CY16	CY17	CY18	CY19	CY20
Carbonated soft drinks						
Pepsi-Cola	Pepsi	Yes	Yes	Yes	Yes	Yes
	Pepsi Max	Yes	Yes	No	No	No
	Diet Pepsi	Yes	Yes	Yes	Yes	Yes
	Pepsi Black	No	Yes	Yes	Yes	Yes
Seven-Up	Seven-Up	Yes	Yes	Yes	Yes	Yes
	Seven-Up Nimbooz Masala Soda*	Yes	Yes	Yes	Yes	Yes
	Seven-Up Revive	Yes	No	No	No	No
Mountain Dew	Mountain Dew	Yes	Yes	Yes	Yes	Yes
Mirinda	Mirinda	Yes	Yes	Yes	Yes	Yes
	Mirinda Lemon	No	Yes	Yes	No	No
Evervess	Evervess	Yes	Yes	Yes	Yes	Yes
	Teem Soda	Yes	Yes	Yes	No	No
	Duke's Soda	Yes	Yes	Yes	Yes	Yes
NCB+ PDW+ Others						
Tropicana Slice	Tropicana Slice	Yes	Yes	Yes	Yes	Yes
Seven-Up Nimbooz	Seven-Up Nimbooz	Yes	Yes	Yes	Yes	Yes
Tropicana Frutz	Tropicana Frutz	Yes	Yes	Yes	Yes	Yes
Tropicana	Tropicana Delight	No	No	Yes	Yes	Yes
Tropicana	Tropicana Essentials	No	No	Yes	Yes	Yes
Aquafina	Aquafina	Yes	Yes	Yes	Yes	Yes
Aquavess	Aquavess	No	No	No	Yes	Yes
Sting	Sting	No	No	Yes	Yes	Yes
Gatorade	Gatorade	No	No	Yes	Yes	Yes
Lipton Ice Tea	Lipton Ice Tea	No	No	No	Yes	Yes
Dairy						
Quaker Oats Milk	Quaker Oats Milk	No	No	Yes	No	No
Mango Shake	Mango Shake	No	No	No	Yes	Yes
Cold Coffee	Cold Coffee	No	No	No	Yes	Yes
Belgian Choco Shake	Belgian Choco Shake	No	No	No	Yes	Yes

Source: Company, Edelweiss Research

Note: Seven-Up Nimbooz Masala Soda is a carbonated juice based beverage. VBL has in CY21 introduced Mountain Dew Ice under this category.

Note: Brands/sub-brands mentioned above are not present in all territories and certain sub-brands are territory specific.

Compared to other major beverage companies, VBL has the most extensive beverage portfolio. This helps the company capture any emerging trends.

Exhibit 31: Product portfolio comparison

	CSD	Juices	Water	Sports	Energy	VAD*
VBL	Y	Y	Y	Y	Y	Y
Coca-Cola	Y	Y	Y	Y	N	Y
Parle Agro	Y	Y	Y	N	N	Y
Dabur	N	Y	N	Y	N	N
Amul	N	N	Y	N	N	Y
Red Bull	N	N	N	N	Y	N
Hector Beverages	N	Y	N	N	N	N

Source: Company, Edelweiss Research

Note: VAD refers to value-added dairy

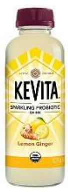
VBL's distribution network, on the back of existing CSD coverage, is much stronger than other major competitors focused on the juice category. Also, it has a huge number of visi coolers in the market, which competition does not have. It thus plans to leverage these aspects to drive volumes in juice/NCB category.

In addition to driving growth from its existing portfolio, there is always the optionality of new launches flowing in from PepsiCo's global portfolio which can be channelled through VBL's existing distribution. Management though does not have plans to launch any new category immediately.

Exhibit 32: Potential launches from PepsiCo's global portfolio

Brand	Category
Pure Leaf	Iced Tea
Bubbly	Sparkling water
Naked	Juices and smoothies
Brisk	Tea and juice brand
Kevita	Fermented probiotic and kombucha beverages
O.N.E	Pure coconut water
MUG	Root Beer

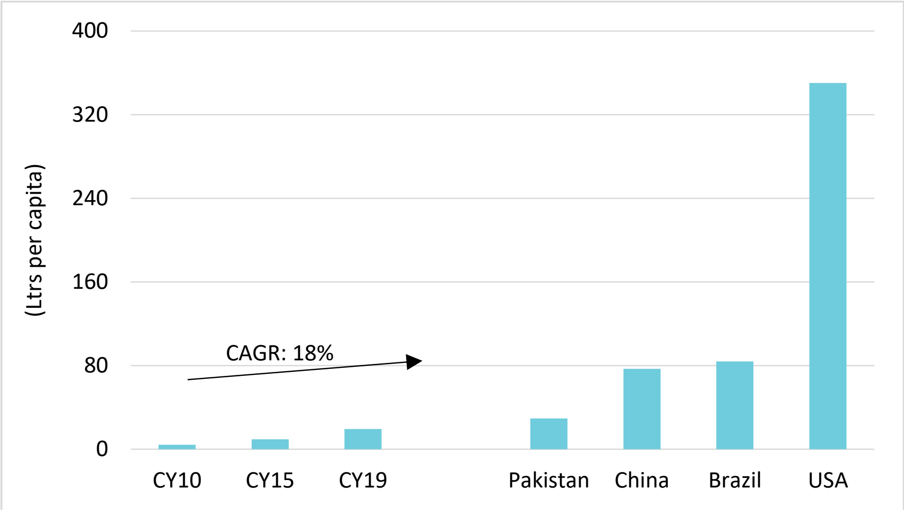
Source: Company, Edelweiss Research, Note: List of products is not exhaustive



Improving per capita consumption also remains a long term growth driver

India's per capita consumption of soft drinks/beverages, is a long-term volume driver. India's per capita consumption has posted 16% CAGR over the past decade and despite this, it is much below global average and not even comparable to beverage-heavy markets like the US. While India's consumption patterns are partially different, there's still significant room for growth even adjusted for the same. In fact, India's consumption is lower than many African and Asian countries with lower per capita incomes.

Exhibit 33: Per capita soft drink consumption

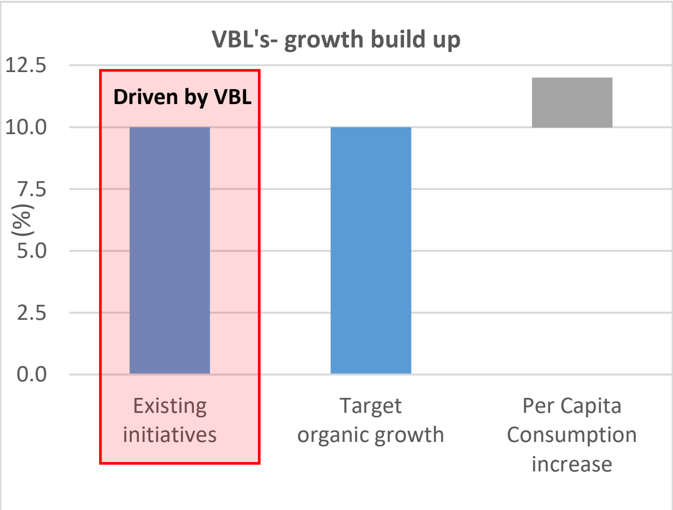


Source: Company, Edelweiss Research, Euromonitor, Nielsen

Note: Includes CSD, Juices and bottled water. For per capita consumption comparison data for CY19

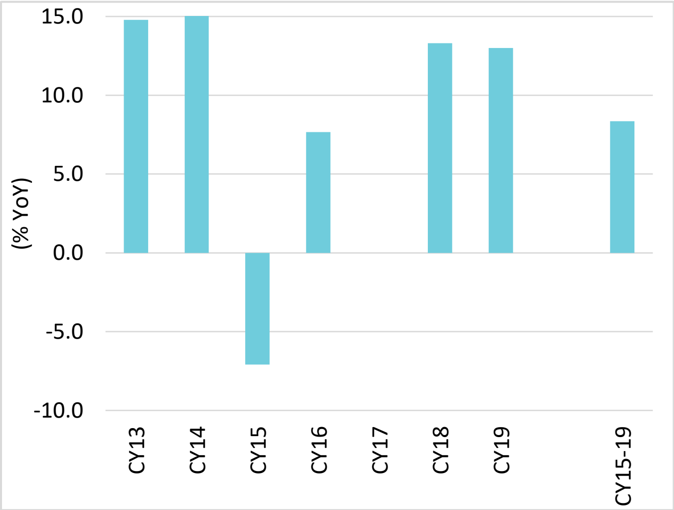
Overall, VBL has multiple drivers in place to achieve its 10% organic volume growth target. We believe, implementation of existing distribution expansion effort and its extensive portfolio can help VBL achieve it.

Exhibit 34: Majority growth target driven by VBL's execution



Source: Company, Edelweiss Research

Exhibit 35: Organic volume growth - delivered in past too



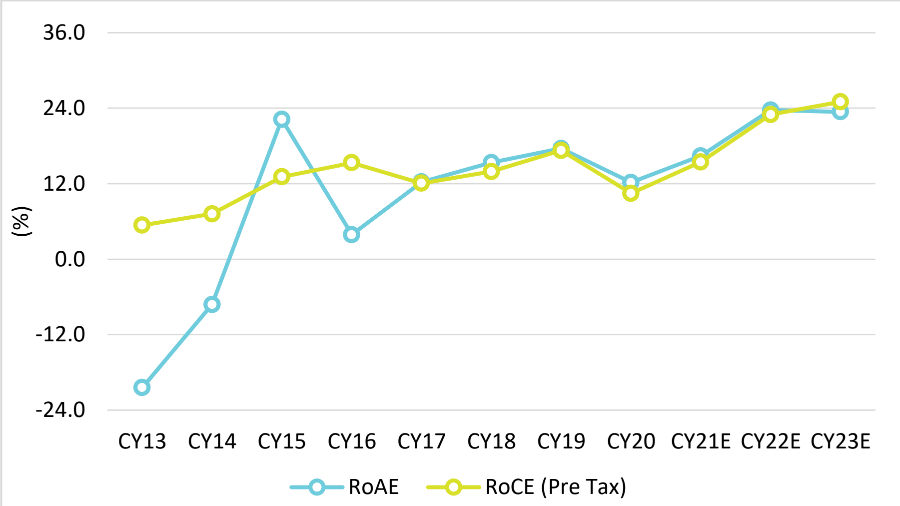
Source: Company, Edelweiss Research

Phase of cash flow generation ahead

VBL's acquisition strategy has been to identify territories that offer growth opportunities for PepsiCo's products and are located contiguous/in close proximity to its existing licensed territories and sub-territories so that they avail freight, transportation and distribution cost efficiencies and operating leverage. The company has also laid down detailed guidelines for acquisitions that it makes (Link).

Acquisitions have been a key component of VBL's growth strategy for many years and substantially accelerated its growth rate and cash flows. Despite spending more than half of its capex on inorganic acquisitions, the company has been prudent in what it has paid and more importantly successfully managed to turnaround operations.

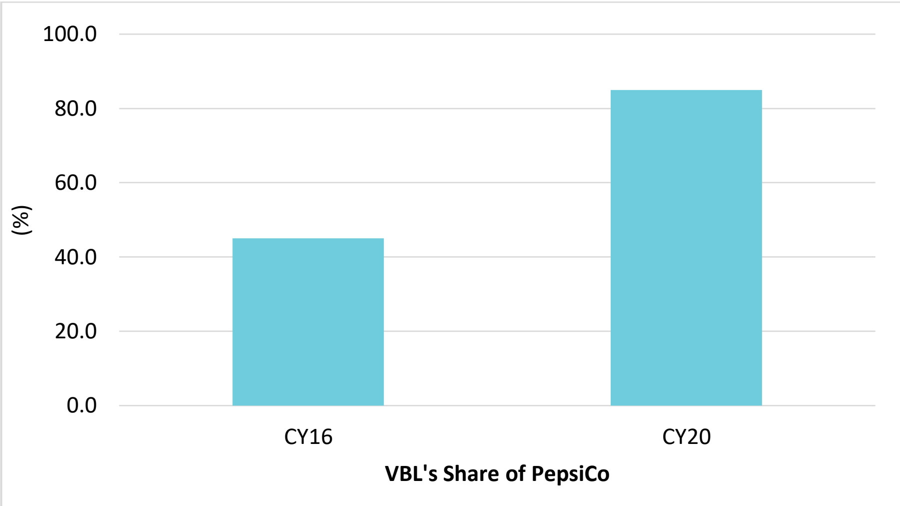
Exhibit 36: Significant improvement in return ratios



Source: Company, Edelweiss Research

In recent years, as part of PepsiCo strategy of consolidating certain PepsiCo-operated territories in India under long-term bottling partners, VBL expanded its operations in India through the acquisition of additional territories. The company has been acquiring territories, which has used up majority of its cash flows. Post the acquisition in CY19 of the South and West regions, VBL now operates more than 85% of PepsiCo's India business.

Exhibit 37: VBL's share of PepsiCo India business



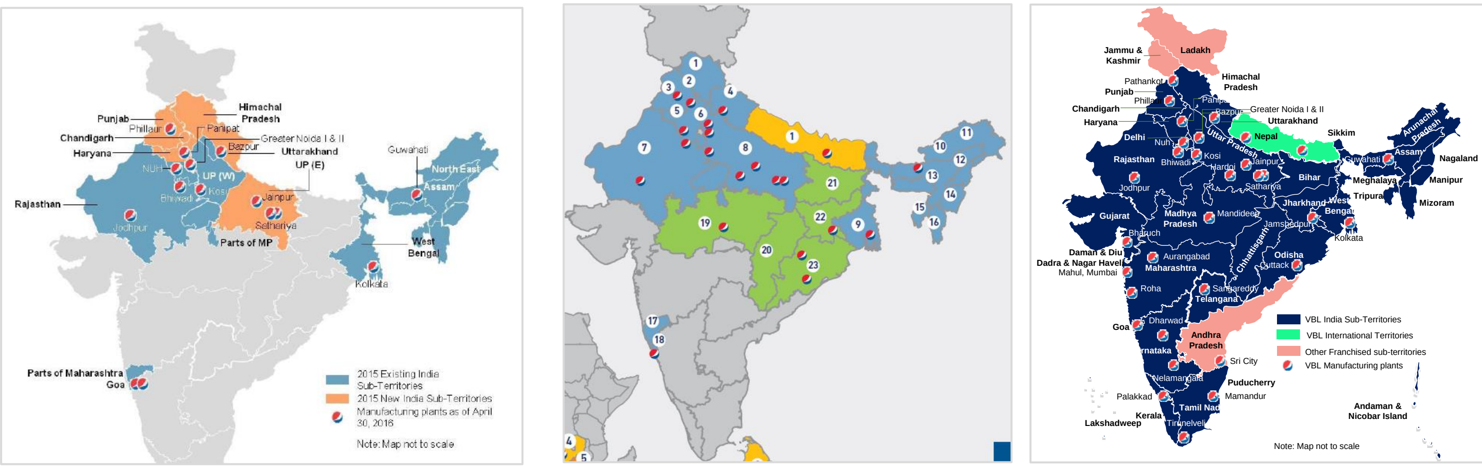
Source: Company, Edelweiss Research

Exhibit 38: VBL's territory acquisition

Date	Company	Value (INR mn)	Territory/Plants
Jan-13	Pearl Drinks Limited	2,940	Delhi, India (excluding trans Yamuna area)
Nov-14	PepsiCo India	11,584	Parts of UP, Uttarakhand, HP, Haryana and the Union Territory of Chandigarh. Also acquired four factories.
Nov-14	Aradhana Drinks and Beverages	1,101	Punjab
Apr-16	NRVS Enterprises Private Limited	500	Manufacturing plant located at Jaunpur, Uttar Pradesh
Mar-16	Dhillion Kool Drinks and Beverages	574	Manufacturing plant located at Phillaur, Punjab
Sep-17	SMV Beverages	832	State of Odisha including a production facility
Sep-17	SMV Agencies	470	Parts of the state of Madhya Pradesh including a production facility
Jan-18	SMV Beverages Private Limited	150	State of Chhattisgarh
Jan-18	Lumbini Beverages Private Limited	450	State of Bihar
Jan-18	SMV Beverages Private Limited	438	Production facility in Odisha
Mar-18	SMV Agencies Private Limited	552	State of Jharkhand including a production facility
Apr-18	Steel City Beverages Private Limited	101	Production facility in Jharkhand
Feb-19	SMV Beverages and Nectar Beverages	150	13 districts in Karnataka, 14 districts in Maharashtra & 3 districts in Madhya Pradesh
May-19	PepsiCo Holdings	15,930	South and West regions - 7 states, 5 UT and 9 production facilities
Oct-19	Nectar beverages	747	Manufacturing plant located at Dharwad, Karnataka
Oct-19	Prathishta Business Solutions	200	Manufacturing plant located at Tirunelveli, Tamil Nadu
Total		**36,719**	

Source: Company, Edelweiss Research

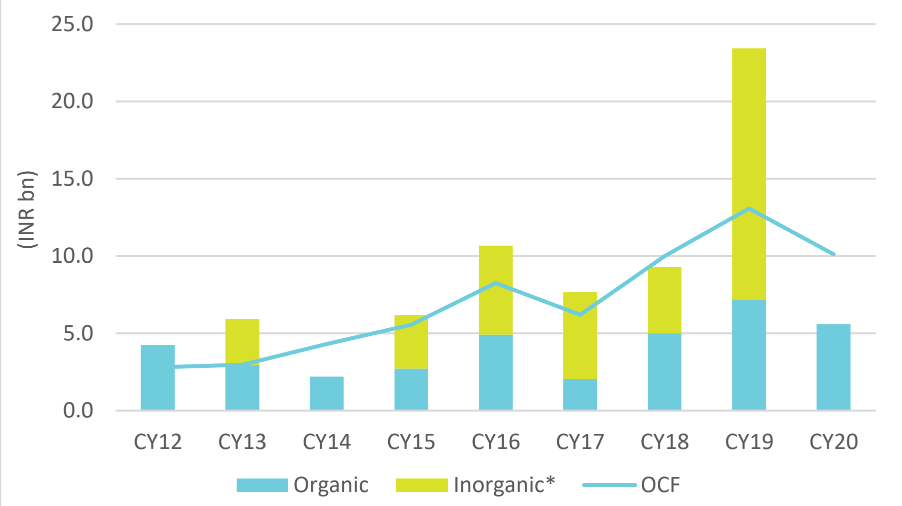
Exhibit 39: Evolution of VBL's territories



Source: Company, Edelweiss Research

A major part of VBL's capex over the past decade was driven by its territory expansion aspirations and entry into new international geographies. Also, a lot of the initial organic expansion was directed towards building capacity in each region, majority of which has been completed. If we look at VBL's cash flow profile, we see that the business generates significant cash flows, excluding acquisitions.

Exhibit 40: Strong cash flow generation trend excluding acquisitions



Source: Company, Edelweiss research

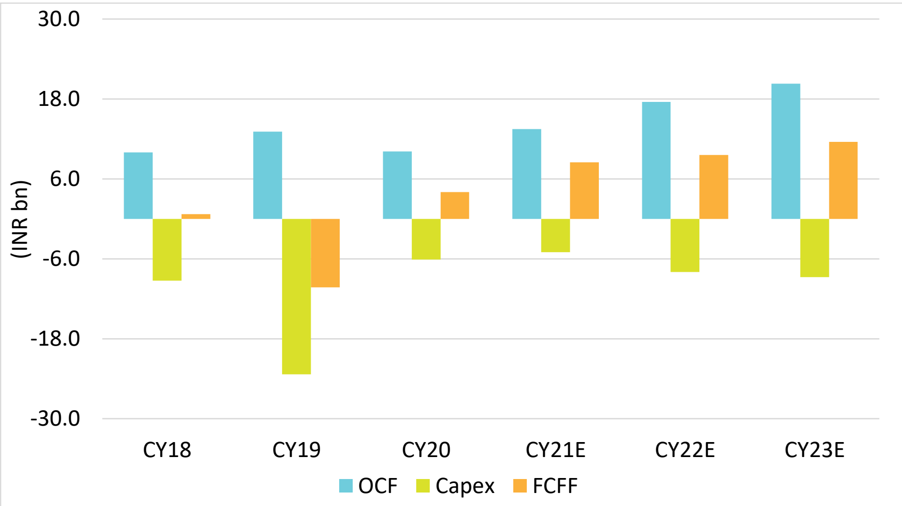
Note: Inorganic includes acquisition of territories, investment in subsidiaries and entry into new geographies. Investment in existing geographies is counted as organic. The reason for the high organic capex in CY18,CY19 is due to the investment in Pathankot facility (~INR5bn). VBL's normalized organic capex run rate is around INR4bn.

With the company having completed acquisition of majority potential territories (now controls 85% plus of Pepsi's volumes in India), incremental spends on acquisitions are expected to be much lower than earlier. While there is a possibility of further acquisitions in certain geographies in South East Asia or Africa, the estimated outlays as per us would be lower than previous acquisitions. Also, relative to VBL's cash flow profile, these would be met via internal cash generation itself.

In addition, post the acquisition of South & West territories, VBL is operating at a peak month utilization of below 60%, limiting major capex spends. The company will, in the coming two-three years, need additional capex on another plant for Tropicana. VBL has given an organic capex guidance of 1x depreciation.

Thus, we believe, incrementally VBL will see a phase of strong cash flow generation.

Exhibit 41: Cash flow trends



Source: Company, Edelweiss Research

Valuations

- The improvement in return ratios over the past decade has settled the argument related to the nature of VBL's business away from pure manufacturing. Also, stability in margin along with the share of business for PepsiCo that VBL handles makes it a near proxy for the portfolio of beverage brands it manages.
- VBL's business parameters are way superior to global bottling companies, whereas FMCG companies have a marginally better return profile. Though this premium over global bottlers is justified, the discount to Indian FMCG companies is higher than what fundamentals indicate.
- We expect discount to FMCG companies to narrow further and thus assign 42x FY23E PE (30% discount) to VBL. Initiate with 'BUY' and TP of INR1,063.

Since listing, a lot of debate has centred on the ideal multiple for VBL as though the business operated one of the largest consumer brands, initial return ratios and investments (asset turns) were more manufacturing/packaging aligned. However, improvement in return ratios over the past decade has settled the argument towards the nature of the company's business away from pure manufacturing/commodity. The stability/improvement in gross margin and the proportion of business that it now handles is also a reflection of the same. Also, the extension of Pepsi's contract with VBL till CY39 and the latter's current dominance impart visibility to the company's business continuity. All this does make VBL a near proxy for the portfolio of beverage brands it handles.

There are two buckets of valuation to consider for VBL: 1) versus global bottlers; and 2) versus FMCG and brand franchise companies in India.

Comparing VBL to major global bottlers, we notice that the key differentiator for VBL is the market it addresses which is a combination of presence in India and also the share of business of PepsiCo that VBL controls (85%+). Such a large market with a current low per capita consumption gives it a longer growth visibility than any of the other bottlers globally.

Exhibit 42: Comparison with global bottlers

Company	Markets	Population (mn)	Coolers (mn)	Production units	Employees ('000)	Volumes (bn cases)	Volume Mix (%)		
							Sparkling/CSD	Still/NCB	Water
Coca-Cola European Partners	13	>300	>1	48	22	2.3			
Coca-Cola Amatil	6	~295	>0.5	32	11	0.6			
Coca-Cola EuroPacific	19	~595	>1.5	80	33	2.9	~60	~34	~6
Coca-Cola Icecek AS	10	~400	1	26	10	1.2	82	7	11
Arca Continental	5	124	0.9	46	62	2.2	80	9	11
Coca-Cola FEMSA	10	265	NA	49	80+	3.2	80	6	14
Pepsi Cola Products Philippines	1	111	NA	NA	3.3	NA	74	26	
Varun Beverages	6	~1,350	0.8	37	~10	0.4	73	6	21

Source: Company, Edelweiss Research,

Note: Coca-Cola European Partners recently acquired Coca-Cola Amatil to form Coca Cola EuroPacfic Partners

Another aspect unique to India is the distribution split of beverage category (~90% general trade) which makes VBL's execution much more important and strategic versus other global markets.

If we compare VBL's business parameters with other peers we see that his business is much superior to global bottling companies, whereas FMCG companies have a marginally better return profile.

Exhibit 43: Comparison of VBL with related peers

Parameter	Variable	VBL	India FMCG	Global Bottlers
Growth	Revenue CAGR FY20-23	11	11	5
Growth	EBITDA CAGR FY20-23	14	15	7
Margin	FY23 EBITDA Margin	22	17	20
Return profile	FY23 Post tax RoCE	17	25	14
Cash flow yield	FY23E FCFF Yield	2.4	1.7	NM
FY23E PE	Median	35	58	8
FY23E EV/EBITDA	Median	18	35	7

Source: Company, Bloomberg, Edelweiss Research

Note: For VBL estimates are Edelweiss estimates. For India FMCG and Global Bottlers from Bloomberg. FY20-23 for VBL corresponds to CY19-22 and FY23 corresponds to CY22.

For companies considered, see detailed valuation table below

Though this premium over global bottlers is justified, the discount to Indian FMCG companies is higher than what fundamentals suggest.

We expect discount to FMCG companies to narrow further and thus assign 42x FY23E PE (30% discount) to VBL. Initiate with 'BUY' and TP of INR1,063.

We initiate with **'BUY'** recommendation. Our consideration for discount to Indian FMCG businesses will be driven by the above factors.

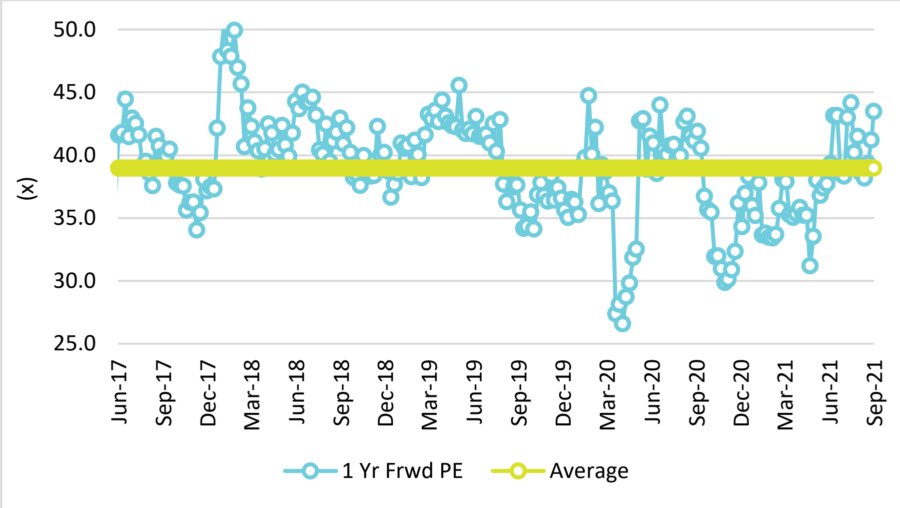
Exhibit 44: VBL's valuation

	FY23E
FY23E EPS (INR)	25
Target P/E	42
TP (INR)	**1,063**
CMP (INR)	908
Upside (%)	17.2

Source: Company, Edelweiss Research

Note: FY23E EPS is weighted average of CY22 and CY23

Exhibit 45: VBL's historical trading range



Source: Bloomberg, Edelweiss Research

Exhibit 46: Global valuation summary

Company Name	M Cap (USD bn)	FY20-23E Sales CAGR (%)	FY20-23E EBITDA CAGR (%)	FY20 EBITDA margin (%)	P/E (x) FY20	FY21	FY22E	FY23E	FY24E	EV/EBITDA (x) FY20	FY21E	FY22E	FY23E	FY24E	RoCE-FY22 (%)
Global Brand owners															
Coca-Cola Co/The	245	4	6	32	28	30	25	23	21	24	24	22	20	19	17
PepsiCo Inc	217	6	6	19	30	29	25	23	21	19	19	17	16	15	18
Monster Beverage Corp	52	13	13	36	44	37	36	32	29	32	28	25	22	20	49
Keurig Dr Pepper Inc	51	5	11	28	40	33	22	20	19	20	19	16	15	NA	7
Suntory Beverage & Food Ltd	13	1	4	14	18	22	20	19	17	8	9	8	7	7	9
Britvic PLC	4	1	13	14	NM	NM	NM	NM	NM	16	15	13	12	11	16
Average		**5**	**9**	**24**	**32**	**30**	**25**	**23**	**21**	**20**	**19**	**17**	**15**	**14**	**19**
Median		**5**	**9**	**24**	**30**	**30**	**25**	**23**	**21**	**20**	**19**	**16**	**15**	**15**	**16**
Indian Food and Beverages Comapnies															
Nestle India Ltd	27	7	13	24	98	94	91	81	68	64	58	52	45	40	88
Dabur India Ltd	16	12	13	21	78	67	60	52	46	62	56	49	43	38	27
United Breweries Ltd	6	6	14	14	96	363	94	56	45	47	109	48	32	27	12
Britannia Industries Ltd	13	11	15	16	71	53	55	48	42	54	39	40	35	32	40
Tata Consumer Products Ltd	11	14	19	14	174	86	72	58	50	61	51	43	37	32	9
Jubilant Foodworks Ltd	7	12	17	22	195	236	112	84	69	63	72	49	39	34	24
United Spirits Ltd	7	5	5	17	88	150	63	48	41	35	52	37	30	27	16
Burger King India Ltd	1	20	34	12	NM	NM	NM	286	100	61	422	44	25	20	NA
Westlife Development Ltd	1	8	15	14	NM	NM	NM	110	71	42	193	45	28	24	NA
Average		**10**	**16**	**17**	**114**	**150**	**78**	**91**	**59**	**54**	**117**	**45**	**35**	**30**	**31**
Median		**11**	**15**	**16**	**96**	**94**	**72**	**58**	**50**	**61**	**58**	**45**	**35**	**32**	**24**
Global Bottlers															
Coca-Cola Europacific Partne	27	9	14	17	29	41	22	18	17	NA	NA	NA	NA	NA	NA
Coca-Cola HBC AG	13	4	6	16	NM	NM	NM	NM	NM	10	10	9	8	8	14
Coca-Cola Femsa SAB de CV	12	2	6	18	5	5	4	4	4	8	8	7	7	NA	11
Arca Continental SAB de CV	11	5	9	18	1	1	1	1	1	0	0	0	0	0	10
Tingyi Cayman Islands Holdi	10	6	5	13	20	18	20	18	16	9	8	8	7	7	27
Coca-Cola Consolidated Inc	4	NA	NA	9	NM	NM	NM	NM	NM	11	NA	NA	NA	NA	NA
Coca-Cola Bottlers Japan Hol	3	(1)	84	1	NM	NM	NM	NM	NM	42	9	7	7	6	NA
Coca-Cola Icecek AS	3	22	26	20	21	15	11	9	9	10	7	6	5	5	21
Embotelladora Andina SA	2	4	2	20	5	7	7	6	5	6	6	6	6	5	13
Average		**7**	**19**	**15**	**14**	**15**	**11**	**9**	**9**	**12**	**7**	**6**	**6**	**5**	**16**
Median		**5**	**7**	**17**	**13**	**11**	**9**	**8**	**7**	**9**	**8**	**7**	**7**	**6**	**13**

Source: Bloomberg, Edelweiss Research

Financial Outlook

- We build in 10% CAGR in India volumes over CY19-23 and 7% CAGR for international operations with overall growth of 9%.
- We estimate 14% EBITDA CAGR over CY19-23 driven by 170bps margin improvement in India riding benefits of higher scale and integration of South & West territories. For international subsidiaries, we expect a moderation in margins from levels seen in CY20, but still ~290bps higher than CY19.
- Overall, the 14% growth in EBITDA, along with reduction in interest expenses we factor in (debt repayment), is expected to drive 28% PAT CAGR over CY19-23. With majority of the large-ticket acquisitions behind, we expect the company to generate strong cash flows over CY21-23 and estimate net debt to dip to INR11.6bn in CY23 (CY20: 30.3bn).
- We expect no major capex needs and with the business still at ~60% utilization, we expect asset turns to further improve along with an improvement in margins driven by operating leverage. We estimate ROCE at 25% by CY23 (CY19: 17%).

Exhibit 47: India volume split

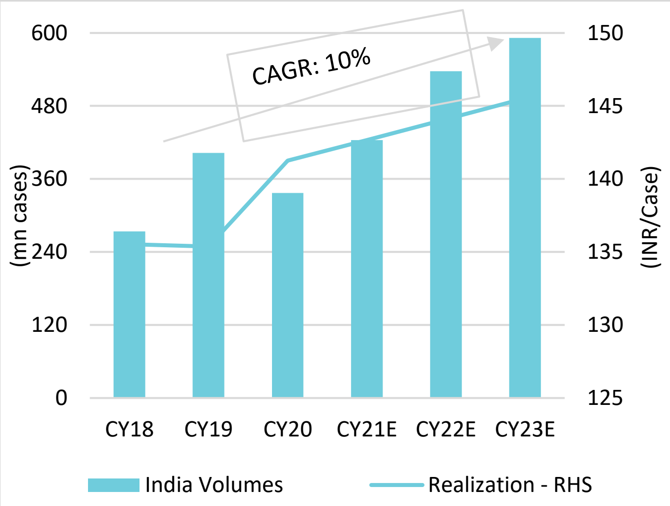
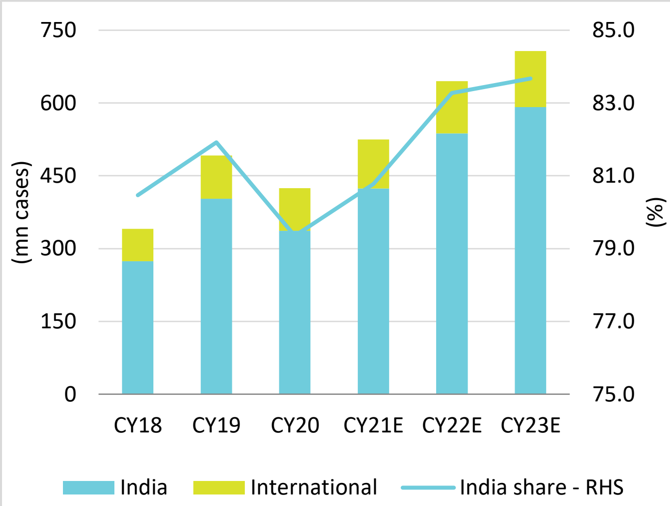


Exhibit 48: Volume split by geography

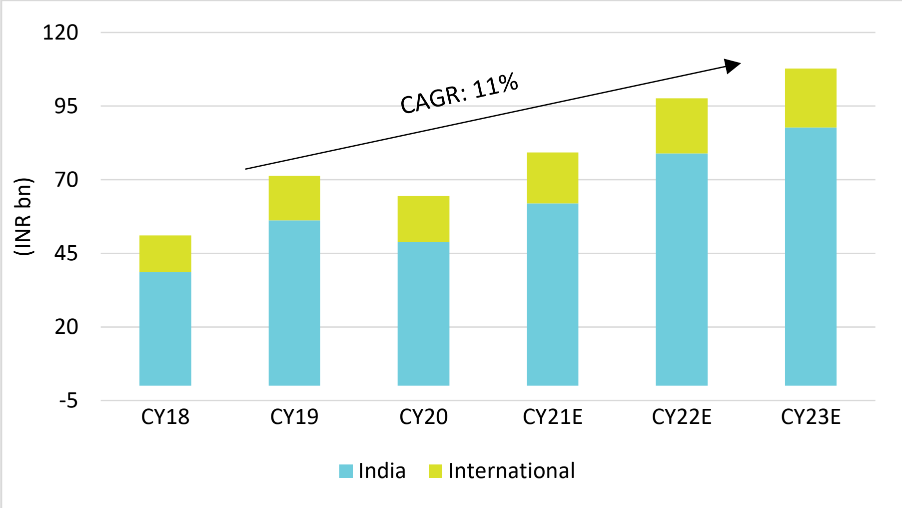


Source: Company, Edelweiss Research

We build in 10% CAGR in India volumes over CY19-23 aided by expectation of higher growth in the NCB category. The growth we build in is consistent with management's target of 10% organic volume growth. This also includes the benefit of South & West integration (acquired in May 2019). We expect a slight improvement in realization driven by higher growth in the NCB segment. Historically, VBL's water mix has increased from 9% in CY12 to 23% in CY19 driven by its higher share in acquired territories in India and launch in Sri Lanka and Morocco.

For international operations, we estimate 7% volume CAGR over CY19-23. Historically, international geographies have seen higher growth (CY16-19 CAGR: 20%) primarily driven by Zimbabwe. Overall, we build in consolidated volume growth of 9%.

Exhibit 49: Revenue split by geography

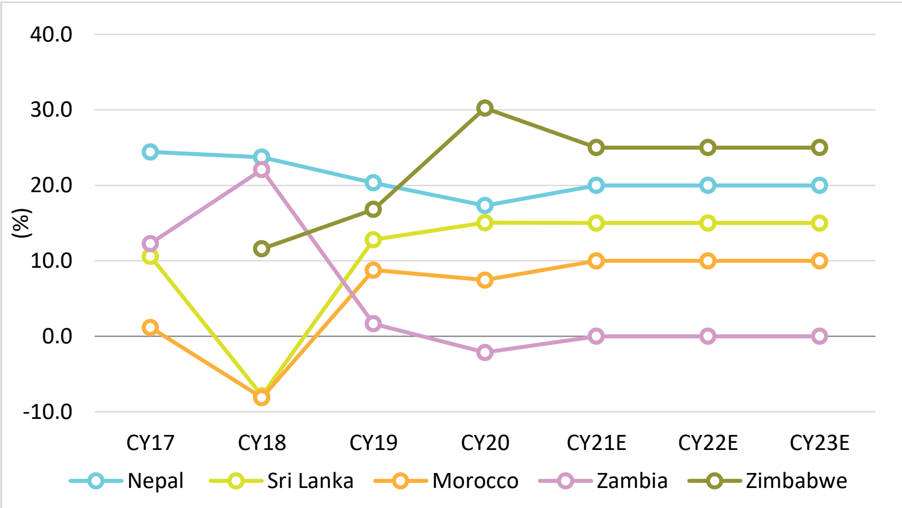


Source: Company, Edelweiss Research

With realizations more of less constant, revenue growth is similar to the volume improvement. We build in 11% revenue CAGR over CY19-23, with international operations growing at 7% and India business clocking 12% growth.

While VBL's margins in India have been consistent at 22-23% (CY16-CY18, CY19 had impact of consolidation and CY20 was impacted by covid), its international operations have seen a significant turnaround, with margins improving from 12% in CY18 to 22% in CY20. This has primarily been driven by the turnaround in margins in Zimbabwe and also the improvement in Morocco & Sri Lanka.

Exhibit 50: International subsidiaries--Margin trend



Source: Company, Edelweiss Research

Overall, we estimate 14% EBITDA CAGR over CY19-23 driven by 170bps margin improvement in India riding benefits of higher scale and integration of South & West territories. For international subsidiaries, we expect a moderation in margins from levels seen in CY20, but still ~290bps higher than CY19.

Exhibit 51: EBITDA margin trend by geography

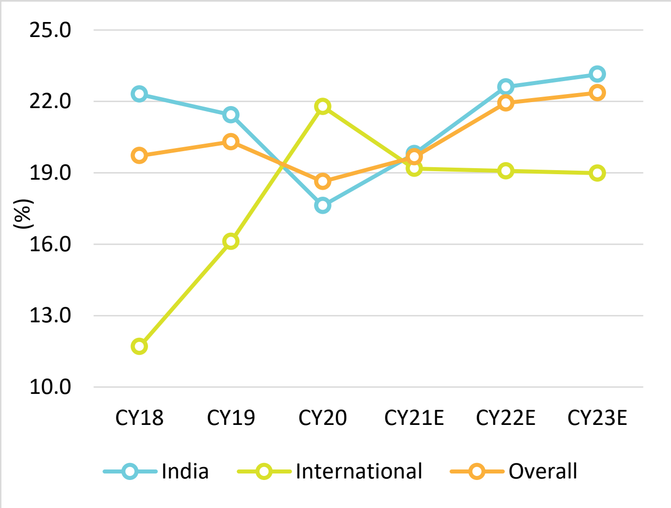
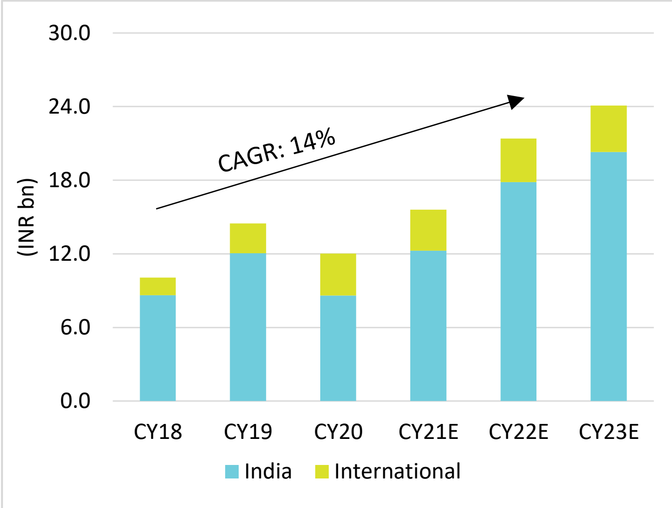


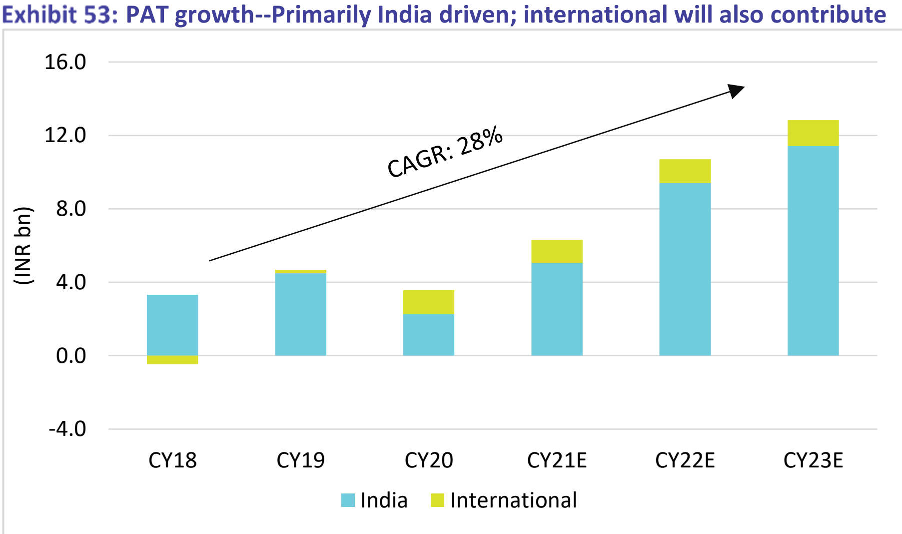
Exhibit 52: EBITDA by geography



Source: Company, Edelweiss Research

Overall, the 14% growth in EBITDA, along with reduction in interest expenses we factor in (debt repayment), is expected to drive 28% PAT CAGR over CY19-23. With the turnaround in profitability of international subsidiaries (primarily by Zimbabwe), we expect international operations to contribute 11% to PAT by CY23E versus being loss making earlier.

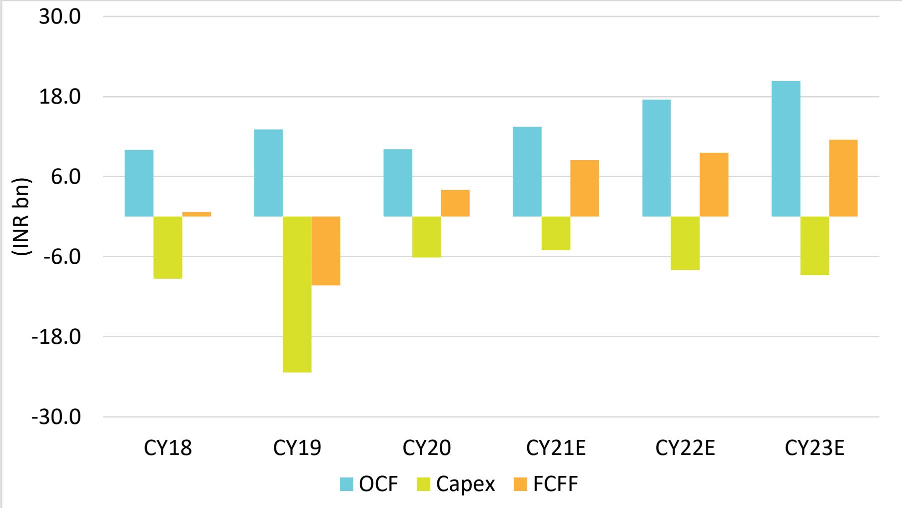
Exhibit 53: PAT growth--Primarily India driven; international will also contribute



Source: Company, Edelweiss Research

A large part of VBL's cash flow had been invested in inorganic opportunities (expansion in new territories in India and international geographies). Incrementally, with majority of the large-ticket acquisitions behind, we expect the company to generate strong cash flows over CY21-23. We still build in INR6bn over CY22-23 for any acquisitions VBL may consider. Factoring that also, we estimate the company to generate FCF of INR30bn over CY21-23 versus INR11bn over CY12-20.

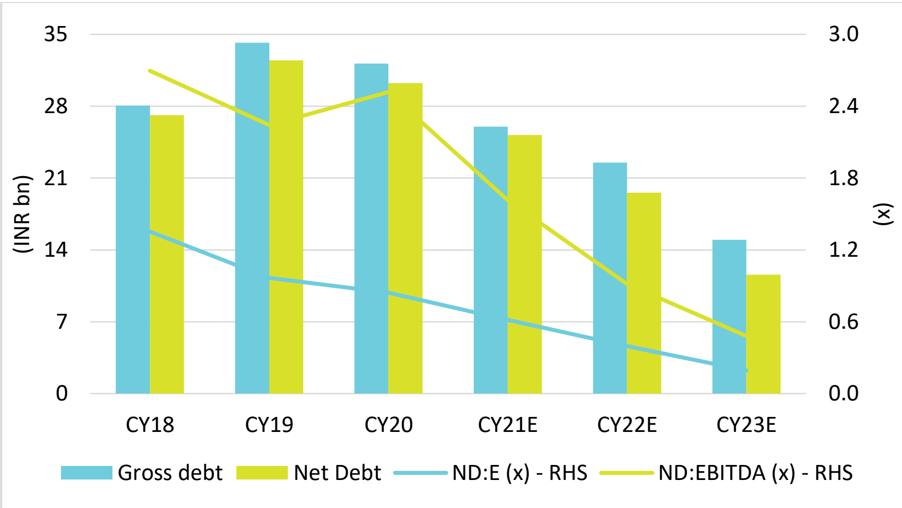
Exhibit 54: Cash flow trends



Source: Company, Edelweiss Research

As a result of the strong cash generation, we expect VBL to use incremental cash flows towards debt repayment. At the end of CY20, VBL had debt outstanding of INR32bn and it has repaid INR5bn worth debt by H1CY21. We expect majority of the cash flows to be deployed towards debt repayment and hence expect net debt to dip to INR11.6bn in CY23 (CY20: INR30.3bn). While it does contemplate acquisitions, the size of any further acquisition will be nowhere close to earlier ones and will be easily funded via internal cash flows.

Exhibit 55: Debt to fall driven by limited capex

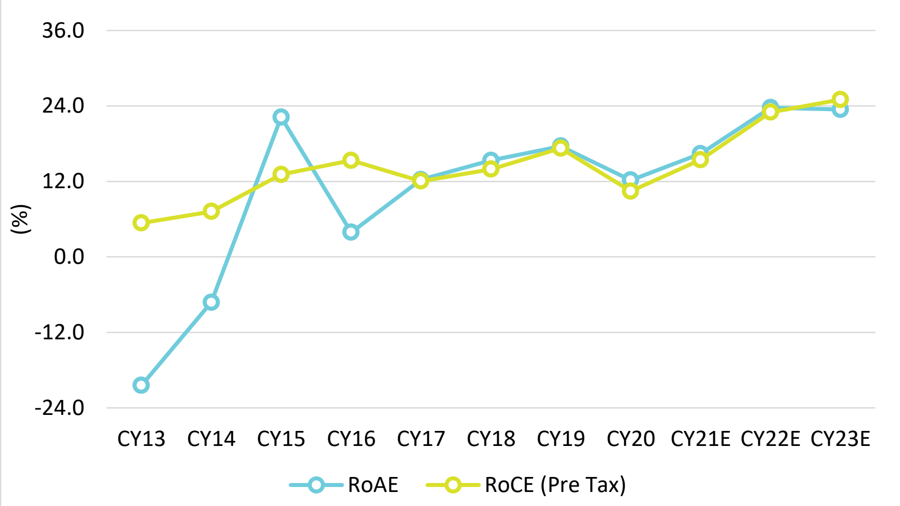


Source: Company, Edelweiss Research

Overall, VBL has posted significant improvement in return rations over the past decade as ROCE has moved from just 5% in CY13 to 17% by CY19. This has been driven by better a combination of efficiencies, operating leverage benefits and also improvement in asset utilization as the acquired territories have scaled up.

Going forward, we expect no major capex needs and with the business still at ~60% utilization, we expect asset turns to further improve along with an improvement in margins driven by operating leverage. We thus estimate VBL's ROCE to touch 25% by CY23.

Exhibit 56: Significant improvement in return ratios



Source: Company, Edelweiss Research

Exhibit 57: Du Pont analysis (Consolidated)

	CY13	CY14	CY15	CY16	CY17	CY18	CY19	CY20	CY21E	CY22E	CY23E
Common Size (% of Revenues)											
Revenues	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Gross Profit	43.3	45.0	49.4	55.0	54.8	56.0	54.8	57.1	55.8	55.3	55.2
Employee Cost	8.7	8.7	9.5	10.9	11.6	11.4	11.4	13.8	12.2	10.7	10.4
Power & Fuel	4.8	4.5	3.9	4.0	4.0	3.8	3.9	4.1	4.0	4.0	4.0
Repairs	2.6	2.7	2.8	2.9	2.8	2.8	2.5	3.1	2.6	2.2	2.1
Sales & Promotion	0.9	1.7	1.6	1.7	2.0	2.2	1.7	1.8	1.9	1.8	1.8
Freight & Distribution	7.4	6.8	6.9	7.5	6.5	8.1	8.1	9.3	8.8	8.8	8.8
Other Variable	1.5	1.5	1.5	1.6	1.7	1.6	1.1	1.2	1.2	1.2	1.2
Other Fixed expenses	3.6	3.7	4.6	5.6	5.3	6.4	5.9	5.2	5.4	4.7	4.6
Other Expenditure	20.8	20.9	21.3	23.5	22.3	24.9	23.2	24.7	24.0	22.7	22.4
EBITDA	13.8	15.4	18.6	20.6	20.9	19.7	20.3	18.6	19.7	21.9	22.4
Depreciation	8.7	8.4	9.4	8.3	8.7	7.5	6.9	8.2	7.1	6.2	6.1
EBIT	5.1	7.1	9.2	12.3	12.2	12.2	13.5	10.4	12.5	15.7	16.2
Interest	8.1	7.5	5.0	11.3	5.4	4.4	4.3	4.4	2.7	1.8	1.3
Other Income	0.8	0.6	1.4	0.9	0.3	0.4	0.6	0.6	0.6	0.6	0.8
PAT (% of Revenues) - A	-1.9	-0.8	3.3	1.2	5.3	5.7	6.6	6.6	7.9	11.0	11.9
Total Asset Turnover - B	0.9	0.9	1.2	1.1	0.9	1.0	1.2	0.9	1.1	1.3	1.4
Leverage Multiplier - C	12.6	9.9	5.7	3.0	2.5	2.6	2.3	2.1	1.9	1.6	1.4
RoAE (%)	-20.4	-7.2	22.2	3.9	12.3	15.3	17.6	12.2	16.4	23.7	23.4

Source: Company, Edelweiss Research

Key Risks

Termination or non-renewal of PepsiCo India's agreements

VBL's agreements with PepsiCo India are valid for till May 2039, and the parties can renew their respective agreements for successive terms of five years each. PepsiCo India / PepsiCo Inc. are entitled to unilaterally terminate these agreements. In addition, the franchises are on non-exclusive basis and PepsiCo is entitled to undertake production, distribution or sale of PepsiCo products and brands either by itself or appoint other third-party franchisees for these territories and sub-territories licensed to VBL. However, in case of termination PepsiCo is required to provide a written notice of at least one year prior to expiration of such agreements. Also, there is a call option in place for PepsiCo to purchase the assets of VBL at an agreed price plus or minus 30% depending on the reason of termination.

Price paid for concentrate

The concentrate is purchased from PepsiCo or its authorised suppliers at a price determined price by PepsiCo. The price of concentrate is linked to MRP of products and is mutually decided taking into cognizance any adverse change in input cost or the tax structure. In a scenario where the terms changes, it may impact VBL's COGS.

Exposure to seasonal variation

Approximately 45% of sales of PepsiCo beverages happens during April – June. Bad weather conditions, including disturbed summers, untimely rains during peak sales season of summer or other internal/external factors may adversely affect sales volumes, thereby impacting annual performance.

Consumption pattern change or overall slowdown impact on growth

A slowdown in growth driven by significant changes in consumer preferences, leading to permanent loss of volumes. Also, overall slowdown in the industry either due to higher taxes and weak macro also remains a risk as the category is still relatively discretionary.

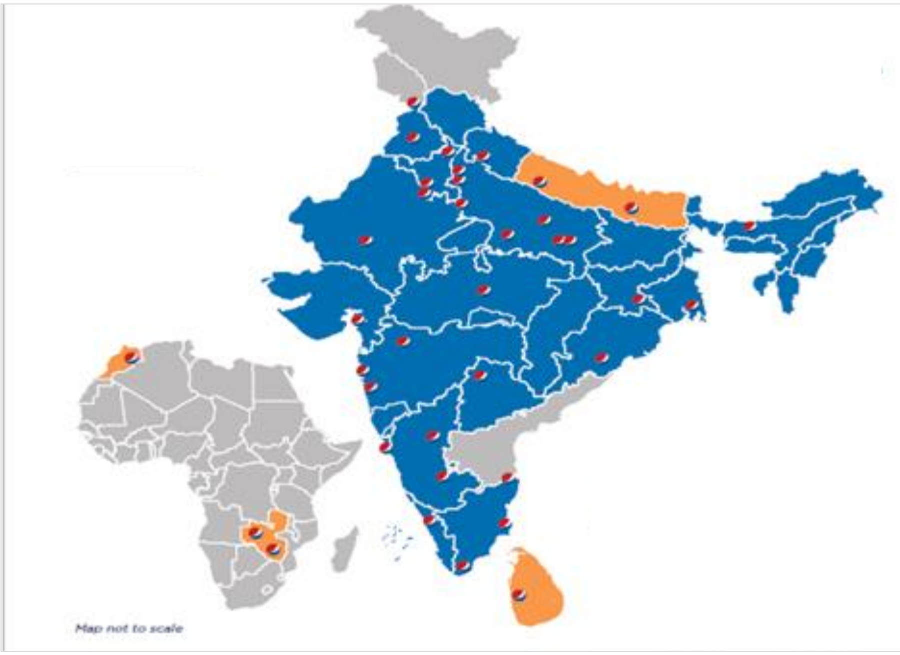
Undertaking acquisitions which drives leverage much higher

We build in VBL to undertake certain acquisitions in the coming years which if acquired at the right price will have the potential to add value, as has been the case in the past. However, any acquisition which requires investments beyond the internal cash flows generated by the company remains a risk.

Company Description

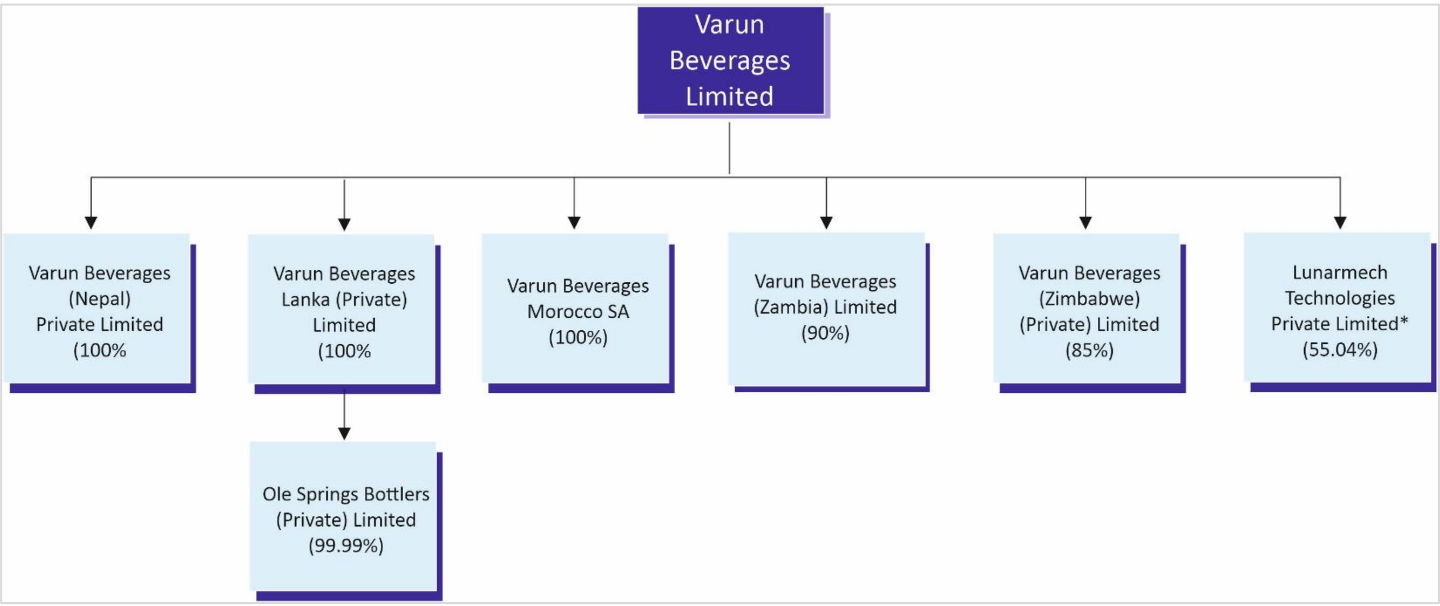
VBL is the second largest franchisee in the world (outside US) of carbonated soft drinks and non-carbonated beverages sold under trademarks owned by PepsiCo. The company is also involved in the production and distribution of CSDs, NCBs and packaged drinking water. VBL's operations span across 6 countries – 3 in the Indian Subcontinent (India, Sri Lanka, Nepal), which contributed ~81% to total revenue, and 3 in Africa (Morocco, Zambia, Zimbabwe), which contributed ~19% of revenue in CY20.

Exhibit 58: VBL's presence



Source: Company, Edelweiss research

Exhibit 59: VBL's holding structure



Source: Company, Edelweiss Research

VBL has over 29 years strategic association PepsiCo and accounts for 85%+ of PepsiCo 's beverage sales volume in India. VBL has expanded the number of PepsiCo licensed territories and sub-territories, produced and distributed wider range of PepsiCo beverages, introduced various SKUs in its portfolio and expanded its distribution network and is currently present in 27 States and 7 UTs.

Business model

VBL's business model involves end-to-end execution responsibilities i.e. from manufacturing, distribution and warehousing, customer management and in-market execution, to managing cash flows and future growth.

Exhibit 60: Business model summary

Source: Company, Edelweiss Research

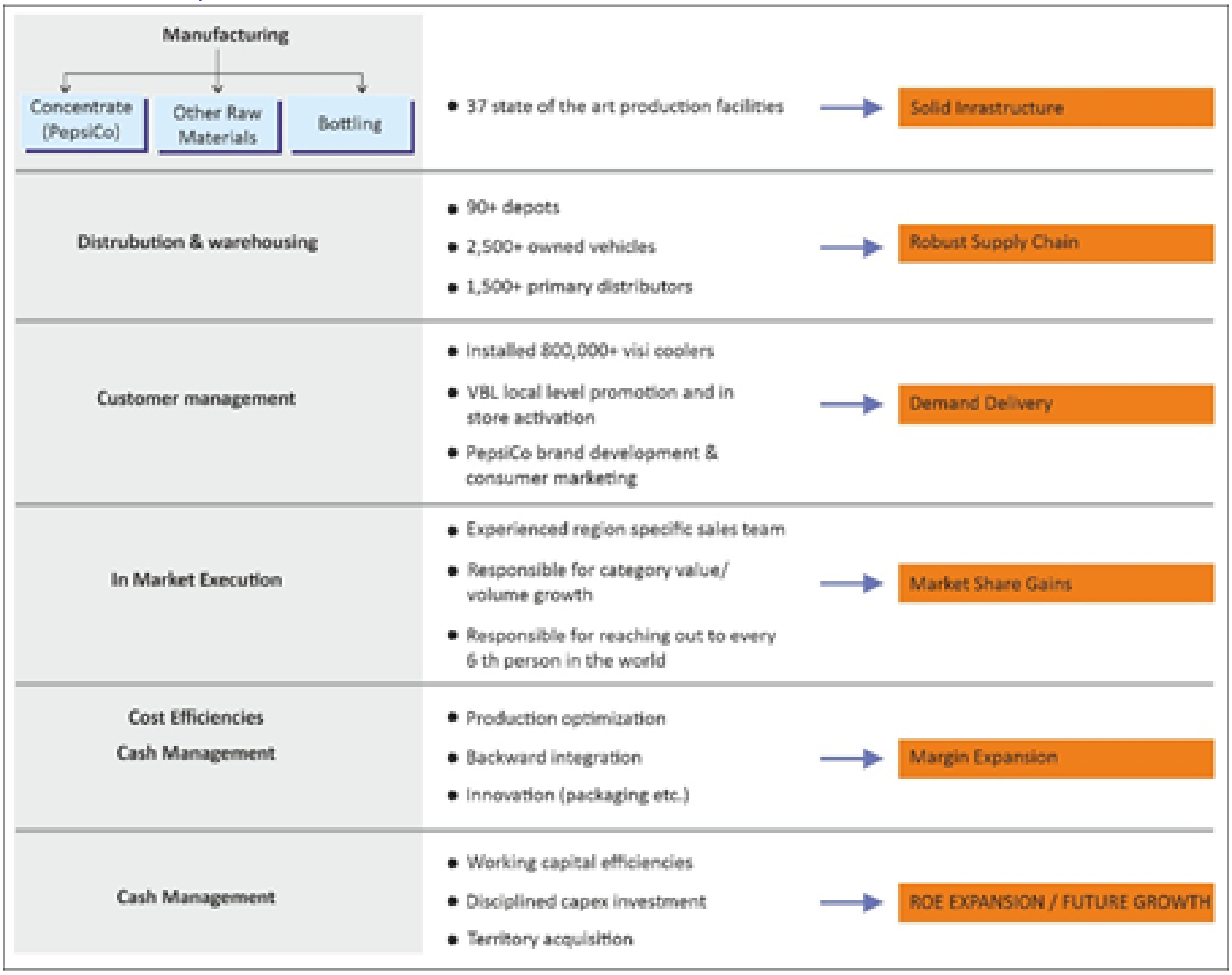
PepsiCo offers brands, concentrates and ATL marketing support to VBL, which then takes complete control over the manufacturing and supply chain processes, driving market share gains through BTL marketing, enhancing cost efficiencies and managing capital allocation strategies.

VBL procures raw material (concentrate from PepsiCo and sugar/other raw materials from approved suppliers), manages manufacturing, bottling and packaging at its production facilities, transports finished goods to the warehouses in trucks and delivers them to the retail outlets through its extensive distribution reach, and also in some cases directly. The products are stored by the retailer in visi-coolers provided and owned by VBL.

VBL's distribution network covers urban, semi-urban and rural markets, addressing demands of a wide range of consumers. The distribution network is located to maximize market penetration across licensed sub-territories in India, with an increased focus on higher growth markets such as semi-urban and rural sub territories. It has 31 manufacturing facilities (As of CY20).

Other than PepsiCo providing the concentrate, consumer marketing and brands to VBL, it has complete control over the manufacturing and supply chain process, driving market share and cost efficiencies.

Exhibit 61: VBL's key functions



Source: Company, Edelweiss Research

Products

The various PepsiCo brands manufactured and distributed by VBL include Pepsi, Pepsi Black, Diet Pepsi, Pepsi Max, Mirinda Lemon, Mirinda Orange, Mountain Dew, Mountain Dew Ice, Slice Fizzy, Seven-Up, Seven-Up Nimbooz Masala Soda, Teem, Sting, Evervess, Tropicana Slice, Tropicana Juices (100%, Delight and Essentials), Seven-Up Nimbooz, Gatorade, as well as packaged drinking water under the brand Aquafina and dairy under the brand Creambell.

Exhibit 62: VBL's product portfolio

Source: Company, Edelweiss Research

Exhibit 63: Key brand and country

Flavor	India	Nepal	Sri Lanka	Zimbabwe	Zambia	Morocco
Pepsi	Yes	Yes	Yes	Yes	Yes	Yes
Mirinda	Yes	Yes	Yes	Yes	Yes	Yes
7 UP	Yes	Yes	Yes	Yes	Yes	Yes
Mountain Dew	Yes	Yes	Yes	Yes	Yes	Yes
Sting	Yes		Yes	Yes		
Slice	Yes	Yes				
Tropicana	Yes					
Aquafina	Yes	Yes	Yes	Yes	Yes	Yes

Source: Company, Edelweiss Research

Exhibit 64: Key events

Year	Event
1991	Bottling and Trademark Licensing Agreement with PepsiCo through a Group Company
1995	Incorporated Varun Beverages Limited as a Public Limited Company
1996	Commenced operations in Jaipur
1998	PepsiCo acquired 26% stake in Devyani Beverages Limited (Merged with VBL in 2004)
1999	Started operations in Alwar, Jodhpur and Kosi
2011 & 2012	-Investment by Standard Chartered PE in Varun Beverages (International) Limited (VBIL) -PepsiCo sold 26% stake in VBL to VBIL (Merged with VBL in 2012)
2012	-Sub-territories of Goa, three districts of Maharashtra and North-East India were consolidated, subsequent to merger of a group company. -Also, three companies having the territories of Nepal, Sri Lanka and Morocco became subsidiaries
2013	Acquired the Delhi sub territory (remaining parts)
2014 & 2015	Capital infusion of INR4.5bn by Promoter Group
2015	-Received investment from AION Investment -Acquired PepsiCo's India sub-territories in parts of Uttar Pradesh, Uttarakhand
2016	-Acquired 60% shareholding in Varun Beverages (Zambia) Limited - IPO of the company
2017	Acquired PepsiCo's India sub territories across the states of Madhya Pradesh (certain parts) and Odisha
2018	-Acquired PepsiCo's India sub-territories in the state of Jharkhand (with production facilities), Chhattisgarh and Bihar -Acquired sales and distribution rights of Tropicana, Gatorade and Quaker Oats Milk -Set up a Greenfield production facility in Nepal and Zimbabwe
2019	-Acquired PepsiCo India's previously franchised territories of parts of Maharashtra (14 districts), parts of Karnataka (13 districts) and parts of Madhya Pradesh (3 districts) -Acquired PepsiCo India's sub-territories across seven states – Gujarat, parts of Maharashtra, parts of Karnataka, Kerala, Tamil Nadu, Telangana and parts of Andhra Pradesh and five union territories of Daman & Diu, Dadra and Nagar Haveli, Puducherry (except Yanam), Andaman & Nicobar Islands and Lakshadweep - Concluded QIP of INR9bn to finance the acquisition of PepsiCo's territories

Source: Company, Edelweiss Research

Management Overview

Key managerial personnel

Exhibit 65: Key management

Name	Title	Qualification	Key Highlights
Ravi Jaipuria	Promoter & Chairman	He has completed higher secondary education from Delhi Public School, Mathura Road, New Delhi	He is the promoter of the Company and has over three decades of experience in conceptualizing, executing, developing and expanding food, beverages and dairy business in South Asia and Africa.
Varun Jaipuria	Whole Time Director	He holds a bachelor's degree in international business from the Regent's University, London and has also completed a program for leadership development at the Harvard Business School.	He has 12 years of experience in the soft drinks industry and has been with the Company since 2009 and has been responsible for the development of Company's new business initiatives that includes implementation of sales automation tools
Raj Gandhi	Whole Time Director	He holds a bachelor's degree in commerce from the University of Delhi and is a member of the Institute of Chartered Accountants of India.	He has 28 years of experience with the Group out of total experience of 40 years and has been key in strategizing diversification, expansion, mergers and acquisitions, capex fundingand institutional relationship. He also has experience in the field of finance, strategy, governance, legal, mergers and acquisitions.
Kapil Agarwal	Chief Executive Officer	He holds a bachelor's degree in commerce from the University of Lucknow and has attended the post-graduation diploma course in business management from the Institute of Management Technology, Ghaziabad.	He has been associated with the Company since incorporation and currently heads the operations and management. He has 29 years of experience with the group in sales and marketing
Rajinder Jeet Singh Bagga	Whole-time Director	He holds a master's degree in mechanical engineering from the Indian Institute of Technology, Kanpur	He has been associated with the Company since 1996 and is currently heading technical operations since 2003. He has an experience of 24 years with the Company in managing technical operations and execution of projects.

Source: Company, Edelweiss Research

Exhibit 66: Board of Directors

Name	Designation	Date of appointment
Ravi Kant Jaipuria	Promoter & Chairman	Jun-95
Varun Jaipuria	Whole-time Director	Jan-09
Raj Pal Gandhi	Whole-time Director	Oct-04
Kapil Agarwal	Whole-time Director and CEO	Jan-12
Rajinder Jeet Singh Bagga	Whole-time Director	May-19
Dr. Naresh Trehan	Independent Director	Dec-15
Pradeep Sardana	Independent Director	Mar-16
Dr. Ravi Gupta	Independent Director	Mar-18
Rashmi Dhariwal	Independent Director	Mar-18
Sita Khosla	Independent Director	Feb-18

Source: Company, Edelweiss Research

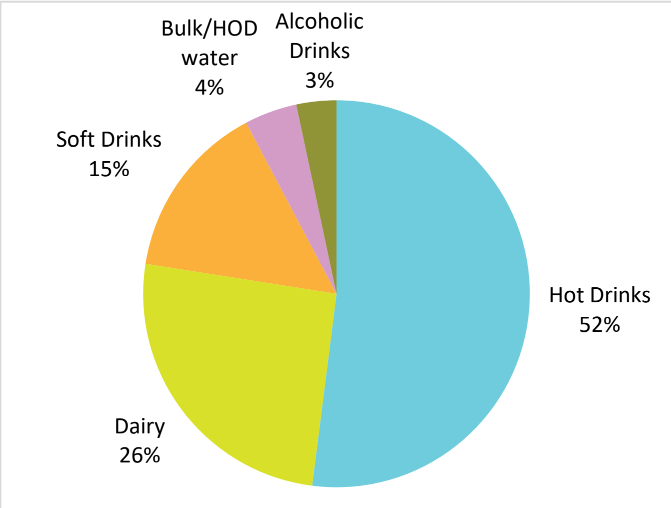
Key ESG initiatives:

- VBL recycles ~66% of PET chips it consumes. According to management, these recycled chips can be used to make products catering to diverse industries and are being put to different end-uses.
- VBL engaged with TUV India to verify its water mass balance. It has also undertaken several other initiatives towards water conservation and water recharge. These include rainwater harvesting, adoption, development and maintenance of ponds and waste water management for optimal water consumption. Water consumption in CY20 fell to 3.68mn KL (CY19: 4.12mn KL).
- The company has a CSR committee in place of which Mr. Ravi Jaipuria is the Chairman. VBL had met its commitment towards CSR spends in CY20.
- VBL has been continuously improving on resource use efficiencies, especially that of common resources such as water, fuel and energy. It has utilized environment friendly fuels like biomass for steam generation and installed solar panels in the plant for generating clean energy.
- The company has significantly reduced weight of the closure and preforms over the period of time to contribute towards environment sustainability.
- VBL has put in place codes and policies for various aspects of its business (Link).

Industry Outlook

The soft drink industry is part of the larger beverage market in India which also includes hot drinks and dairy, which make up the largest segment of the beverage market.

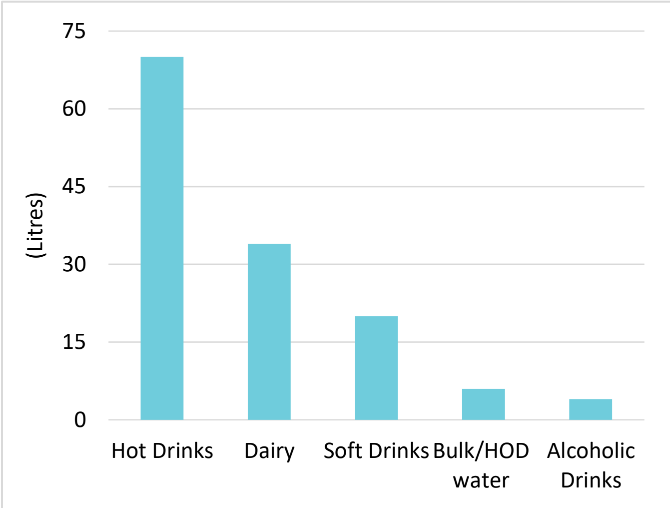
Exhibit 67: Commercial beverage market share



Source: Company, Edelweiss Research

Note: Market share based on volumes, Data for CY18

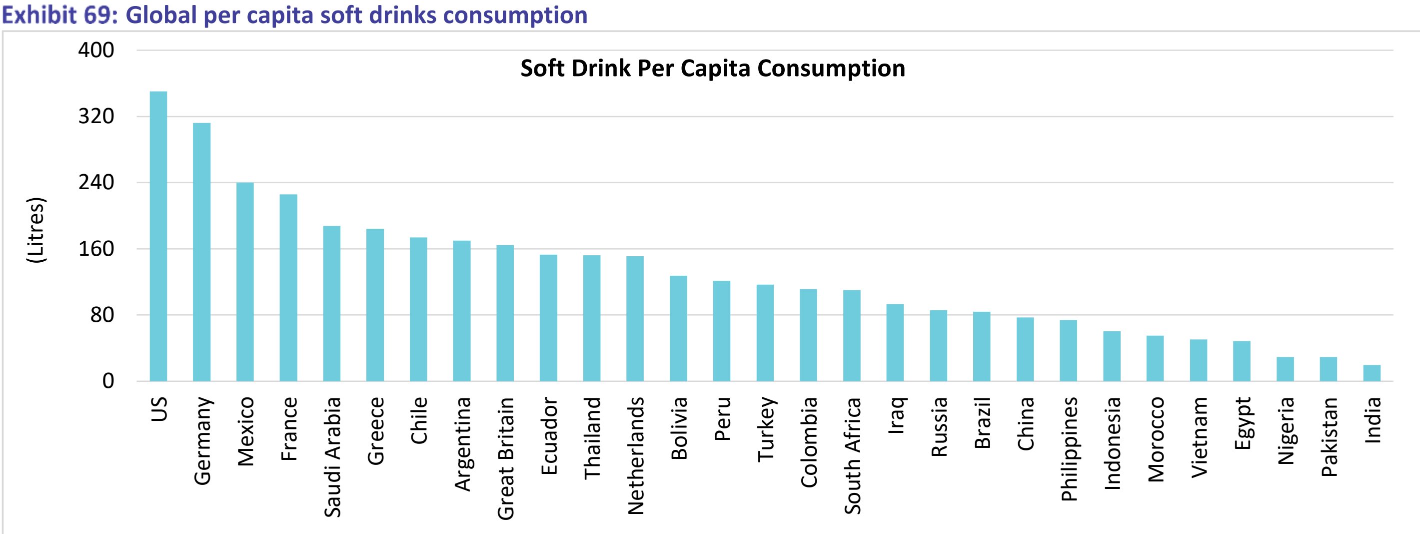
Exhibit 68: Per capita consumption



Source: Company, Edelweiss Research

Indian beverage consumption is dominated by tea, coffee and dairy, whereas consumption of soft drinks still remains nascent in India as it remains occasion based. India's soft drink consumption lags even other developing nations with lower per capita consumption.

Exhibit 69: Global per capita soft drinks consumption



Source: Coca-Cola İçecek, Edelweiss Research

Note: Includes sparkling soft drinks, ready-to-drink tea, energy drinks, juices, packaged water

The soft drink market in India is further bifurcated into carbonates, packaged water, still drinks, nectars etc.

Exhibit 70: Soft drinks--Market bifurcation

	INR bn	% Share	Per Capita Litres
Carbonates	567	45	5.0
Packaged Water	386	30	12.0
Still Drinks	190	15	2.0
Nectars	35	3	0.2
Juice	19	1	0.1
Sports Drink	19	1	0.2
Fruit Powders	15	1	0.5
Squash/Syrups	15	1	0.2
Energy Drinks	12	1	0.0
Others	9	1	0.0
Total Soft Drinks	**1,266**	**100**	**20.0**

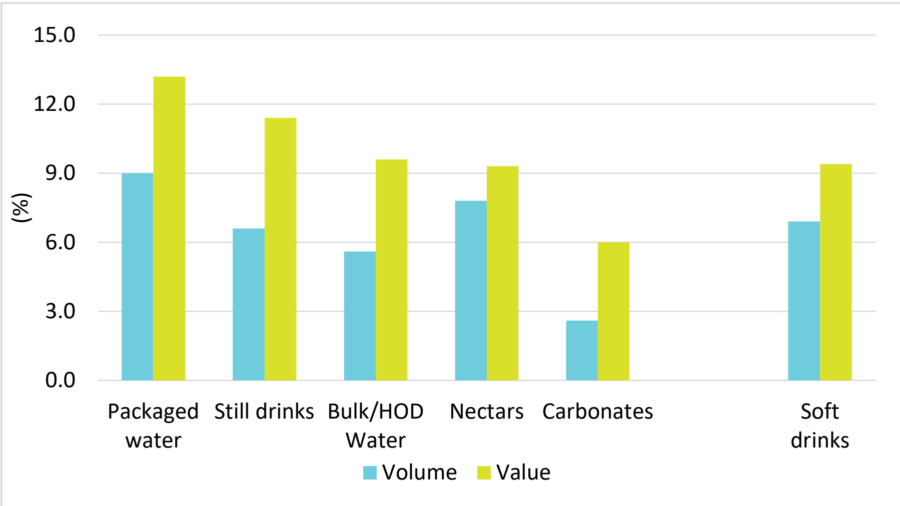
Source: Company, Edelweiss Research

Note: Data for CY18. Excludes Bulk/HOD water.

Unlike in the US, where carbonated drinks are often a substitute for water, in India soft drinks and particularly carbonated beverages are used more for occasional consumption. Their pricing is considered premium.

With the increasing number of health conscious consumers, India has been witnessing significant growth in non-carbonated beverage segment in recent times. Even in terms of future outlook, growth for the NCB beverage segment is expected to outpace the carbonate beverage segment. This category has lost its momentum recently due to perception towards these drinks and high tax burdens. Health-conscious millennials have been leaning towards healthy beverage options such as juices. Juices are among the biggest beneficiaries of changing consumer preferences towards soft drinks, with growing awareness on the risks of regular and high consumption of sugary drinks.

Exhibit 71: Growth by category (CY19-24)

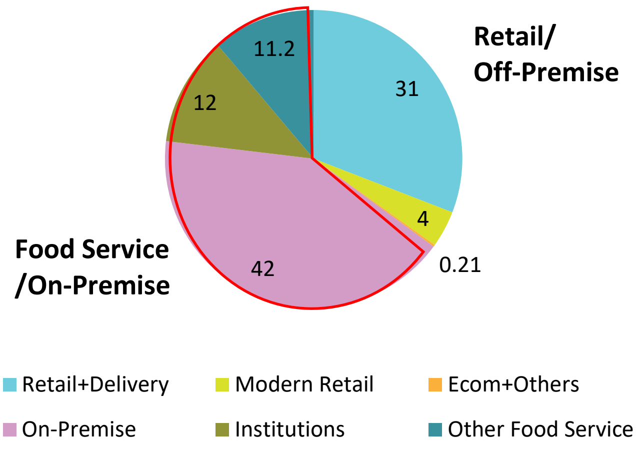


Source: Company, Edelweiss Research

Segmentation by distribution

Distribution of packaged beverages is driven by the traditional formats. The soft drink distribution market is divided into Retail and Food Service (also referred to as off trade and on trade respectively). In the retail channel, traditional retail (Kirana shops) was the largest channel in the Indian soft drinks sector. E-commerce channel contributes ~1% of the total retail market.

Exhibit 72: Soft drink industry--channel split



Source: Company, Edelweiss Research

Note: Data for CY18

Key players:

Thums up was introduced in 1977 to offset the withdrawal of Coca-Cola. After Coca-Cola re-entered in 1993, it bought Thums Up from Parle Bisleri along with Maaza, Limca, Citra and Gold Spot, of which the last two were discontinued

Coca-Cola, PepsiCo, Parle Agro and Dabur are the major soft drinks beverage companies in India.

Coca Cola was the first major cola company to enter India in 1970, before exiting the country in 1977 due to changes in government policies. Parle, which was facing stiff competition from Coca Cola, then took over by launching new carbonated drinks such as Thums Up, Gold Spot and Limca. After PepsiCo entered India in 1989 and Coca-Cola re-entered India in 1993, both have continued to dominate the Indian soft drink market.

Exhibit 73: key categories

	Coca Cola	Pepsi Co	Parle Agro	Dabur	ITC	Others key brands
Cola Carbonates	Thums Up Coca Cola	Pepsi	Frio			
Lemon/Lime Carbonates	Sprite Limca	7-Up Mountain Dew	Frio			
Orange Carbonates	Fanta	Mirinda	Frio			
Soda	Kinley	Evervess, Duke's	Bailey			Bisleri Soda
Mango Drink	Maaza	Slice	Frooti			Bisleri Fonzo
Fruit Juice	Minute Maid	Tropicana	Appy Fizz*	Real, Real Activ Réal FizzIn*	B Natural	
Packaged Water	Kinley	Aquafina	Bailey			Bisleri, Oxyrich, Himalayan

Source: Edelweiss Research

*Note: Considered major brands in each category. *Carbonated juice beverage.*

The carbonates segment of the soft drinks industry is India is dominated by multinationals Coca-Cola and PepsiCo, which together hold more than 90% of the total off-trade market. Coca-Cola held a ~60% share of the market, with a product portfolio including Thums Up, Coca-Cola, Sprite, Limca and Fanta. PepsiCo was the second largest player in the market, with a ~30% share.

Exhibit 74: PepsiCo market share and key brands

	Volume	Value	Key Brands
Carbonated Beverages	28%	30%	Pepsi, Mountain Dew
Juices	20%	20%	Tropicana
Still Drinks	11%	12%	Slice
Nectars	20%	20%	Tropicana
Sports Drink	3%	3%	Gatorade
Energy Drinks	24%	9%	Sting
Packaged Water	5%	5%	Aquafina, Evervess
Total Soft Drinks	9%	18%	

Source: Edelweiss Research, Company,

Note: Data for CY18

Global Industry

The global soft drinks industry market size was ~USD945bn in 2021 with US making up the largest market at USD414bn. The global market is dominated by the two cola giants Coca Cola and PepsiCo with Coca Cola being the overall leader in the soft drink category and also across sub-categories like carbonates and juices. Nestle is the global leader in packaged drinking water. PepsiCo in addition to being a number two player in many categories also has a sizeable contribution of its business from Food, unlike Coca Cola.

Exhibit 75: Global category leaders

Category	No.1	No.2
Carbonates	Coca Cola	PepsiCo
Bottled Water	Nestle SA	Coca Cola
Energy Drinks	Monster	Red Bull
Juices	Coca Cola	PepsiCo
Overall Soft Drinks	Coca Cola	PepsiCo

Source: Edelweiss Research, Press articles

The trend over the last decade has been to increase portfolio and reduce share of carbonated drinks. As a result, portfolio of all major beverage companies have seen a sizeable expansion over the past decade. Recently, there is a focus on trimming portfolio and eliminating unprofitable brands seen with PepsiCo's divesture of Tropicana and other juice brands in North America. Last year, the Coca-Cola Company abolished a number of brands, including tab diet soda, dicoco coconut water, odwara fruit juice and smoothies. The industry is currently focusing on a smaller number of categories, including energy drinks, coffee and traditional soft drinks.

Additional Data

Management

Chairman	Ravi Jaipuria
Director	Varun Jaipuria
Director	Raj Pal Gandhi
CEO	Kapil Agarwal
Auditor	Walker Chandiok and APAS

Holdings – Top 10*

	% Holding		% Holding
Government Pens	2.92	Capital Group	1.72
Norges Bank	2.86	Sundaram AMC	1.23
Nippon Life Ind	2.41	Tata AMC	0.95
Stichting	2.19	Vanguard	0.87
Nordea Bank	2.06	CDPQ	0.61

Latest public data

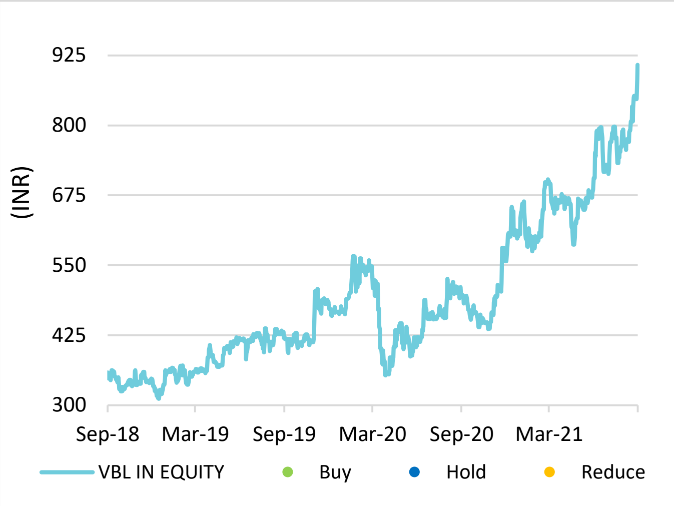
Recent Company Research

Date	Title	Price	Reco

Recent Sector Research

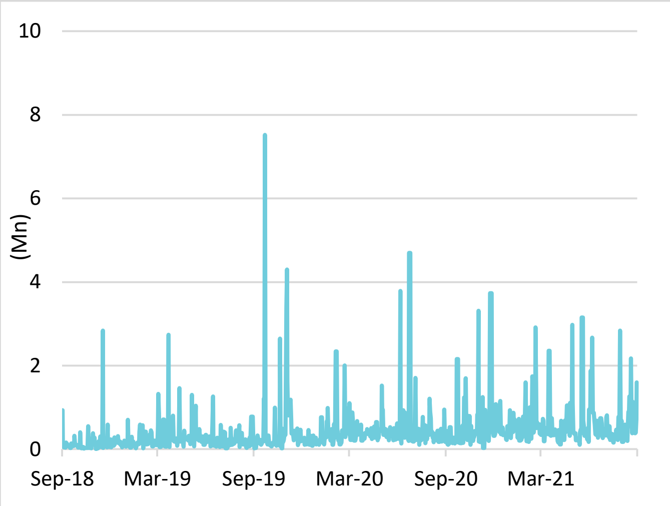
Date	Name of Co./Sector	Title
16-Aug-21	SHEELA FOAM LTD	Input cost headwind; banking on exports; *Result Update*
16-Aug-21	Polyplex corp	Margin pressure dims prospects; *Result Update*
16-Aug-21	Balkrishna Industries	Solid demand traction; *Company Update*

Rating Interpretation



Source: Bloomberg, Edelweiss research

Daily Volume



Source: Bloomberg

Rating Distribution: Edelweiss Research Coverage

	Buy	Hold	Reduce	Total
Rating Distribution*	173	55	19	248
	>50bn	**>10bn and <50bn**	**<10bn**	**Total**
Market Cap (INR)	215	42	4	261

**1 stocks under review*

Rating Rationale

Rating	Expected absolute returns over 12 months
Buy:	>15%
Hold:	>15% and <-5%
Reduce:	<-5%

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