JM FINANCIAL

Prataap Snacks | BUY

A shining star in the snacking space

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Prataap Snacks, owner of the 'Yellow Diamond' brand, has established a sizeable presence in the Indian Snacks industry over the past few years by capturing a reasonable share in the Extruded Snacks space through its product innovations, intelligent marketing campaign and focus on distribution which has helped quadruple its market share over a 6-year period. This drove 27% revenue CAGR over FY13-17 but the company's current scale is still way too small at INR9bn p.a. when compared to the size of the opportunity; the organised snacks market is a c.INR220bn (c.$3.5bn) one. We believe Prataap can easily sustain high-teens revenue growth rate over next few years – its high exposure to faster-growing sub-segments and market-share gain opportunities being some of the tailwinds in this regard. Efforts on improving margin-profile of the Namkeens portfolio and efficiency gains from GST should also help the company maintain its operating margin at 8.5-9.5% over the coming years. Strong growth prospects, improving margin-profile and healthy balance sheet drive our liking for the stock - our DCF-based target price works out to INR1,390/share. BUY.

- **A clear high-teens revenue growth opportunity:** The attractiveness of Prataap's business model is premised on its strong revenue growth traction - its growth rate of 27% p.a. over FY13-17 is 2x that of the industry's (organised segment); our analysis suggests that Prataap has still quite a few levers available that would help drive high-teen revenue CAGR over the coming few years: 1) Increasing penetration in North and West regions while enhancing footprints in Southern markets which presently contributes a mere 9-10% to overall revenues – its 'Rings' product being the key growth and market share driver in this regard. 2) Scaling-up its recent foray into newer segments like sweet-snacking and the healthier salty-snacks space. 3) Entry into hitherto untapped modern-trade channel using the newly-launched healthier snacks portfolio. 4) Further market share gains in core categories through innovative marketing and distribution expansion. We are building 18.6% revenue CAGR over FY17-22E (lower in FY18E due to a few disruptions, 19-20% over FY18-22E); this would imply a 150bps market share gains in Extruded Snacks – Prataap's 600bps share-gain over 2010-16 makes this forecast look quite an achievable one, in our view.
- **Double-digit operating margin an achievable target over the medium-term; Cash-generation potential is healthy as well:** Prataap's EBITDA margin has been volatile in the past largely on account of high input-costs inflation; margin has now recovered back to near double-digit level in 1HFY18 aided by a more benign input-costs environment, improvement in Namkeen segment's margin-profile, grammage changes and efficiency gains from GST implementation which has also equalised tax-incidence vis-a-vis regional players who hitherto benefitted from lower tax rates in some of their respective states of operations. These factors together with scale benefit would help the company sustain its operating margin at the higher band in the coming years, we believe. In our view, as Prataap's manufacturing gets more distributed once it achieves scale across regions, savings in distribution costs would also accrue and contribute to margin. We believe higher margin plus strict control on working capital (down from 13% to 7% over FY12-17) would help Prataap generate healthy FCF and grow ROIC to high-teens level over the coming 3-4 years.

Recommendation and Price Target	
Current Reco.	BUY
Previous Reco.	NR
Current Price Target (12M)	1,390
Upside/(Downside)	19.0%
Previous Price Target	NA
Change	NA

Key Data – DIAMOND IN	
Current Market Price	INR1,168
Market cap (bn)	INR27.4/US$0.4
Free Float	21%
Shares in issue (mn)	22.45
Diluted share (mn)	22.45
3-mon avg daily val (mn)	INR47.0/US$0.7
52-week range	1,404/1,102
Sensex/Nifty	34,771/10,700
Rs/US$	64.3

Price Performance			
%	1M	6M	12M
Absolute	-13.4	-2.8	NA
Relative*	-17.3	-9.3	NA

* To the BSE Sensex

Financial Summary					(INR mn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net Sales	7,572	9,039	10,407	12,557	14,997
Sales growth (%)	35.5%	19.4%	15.1%	20.7%	19.4%
EBITDA	565	409	898	1,097	1,373
EBITDA (%)	7.5%	4.5%	8.6%	8.7%	9.2%
Adjusted net profit	317	85	440	602	748
EPS (INR)	21.1	5.6	18.8	25.7	31.9
EPS growth (%)	238.1%	-73.6%	236.8%	36.8%	24.3%
ROIC (%)	15.5%	4.3%	13.1%	14.5%	16.9%
ROE (%)	15.7%	3.7%	11.7%	11.2%	12.7%
PE (x)	55.3	209.6	62.2	45.5	36.6
Price/Book Value (x)	8.1	7.5	5.3	4.9	4.4
EV/EBITDA (x)	31.9	45.3	28.6	23.2	18.4
Dividend Yield (%)	0.0%	0.0%	0.1%	0.4%	0.6%

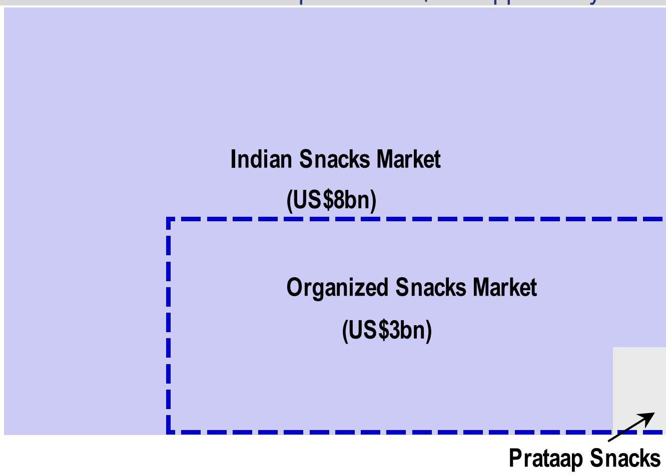
Source: Company data, JM Financial. Note: Valuations as of 16/Jan/2018

Please see Appendix I at the end of this

Please see Appendix I at the end of this report for Important Disclosures and

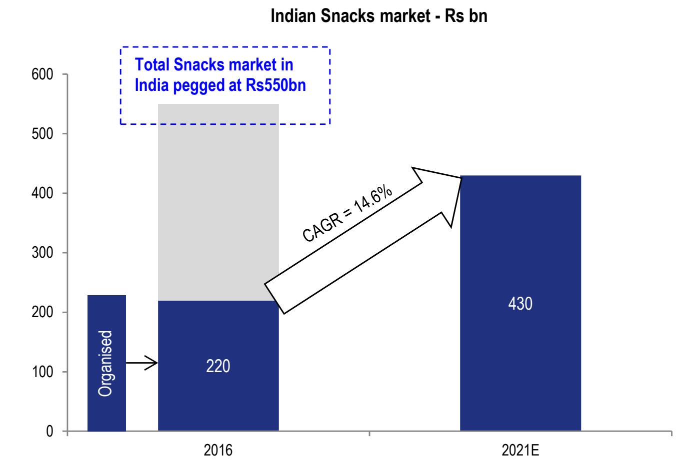
Key Snapshot Charts

Exhibit 1. Indian snacks market presents US$8bn opportunity



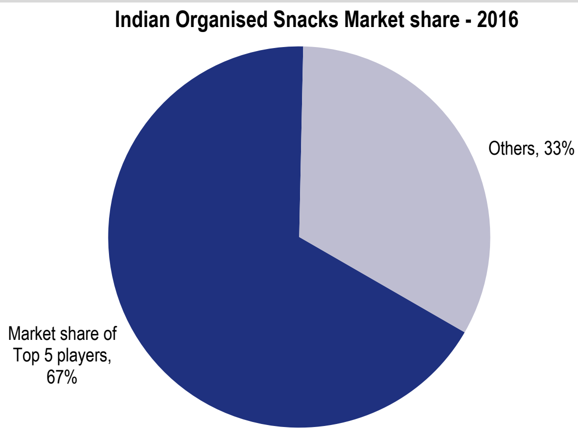
Source: Company, JM Financial

Exhibit 2. Organised snacks segment expected to grow in mid-teens



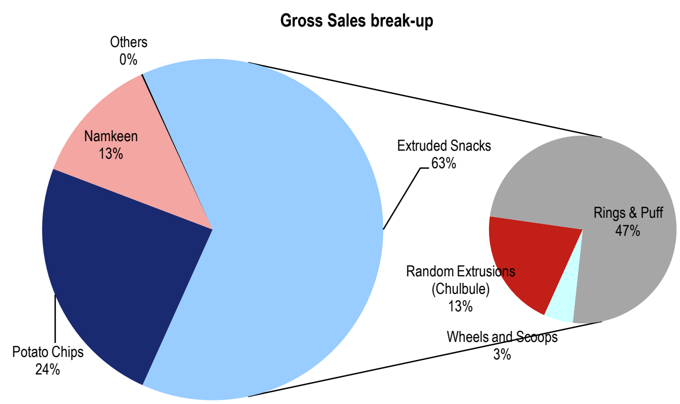
Source: Company, JM Financial

Exhibit 3. Top 5 players constitute mere 65% of organised snacks market.



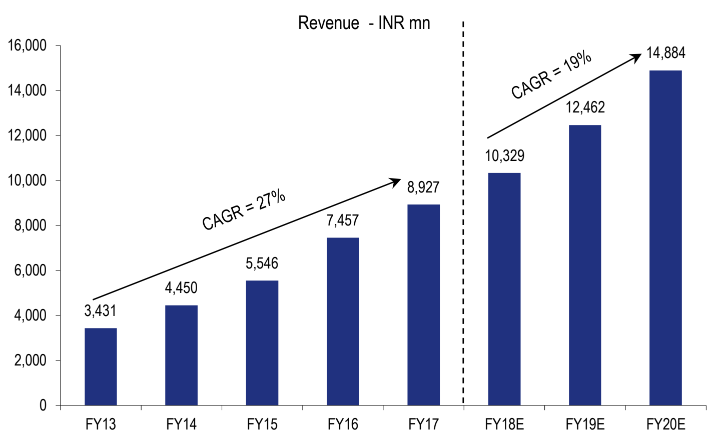
Source: Company, JM Financial

Exhibit 4. High-growth extruded snacks segment constitutes 63% of Prataap's turnover.



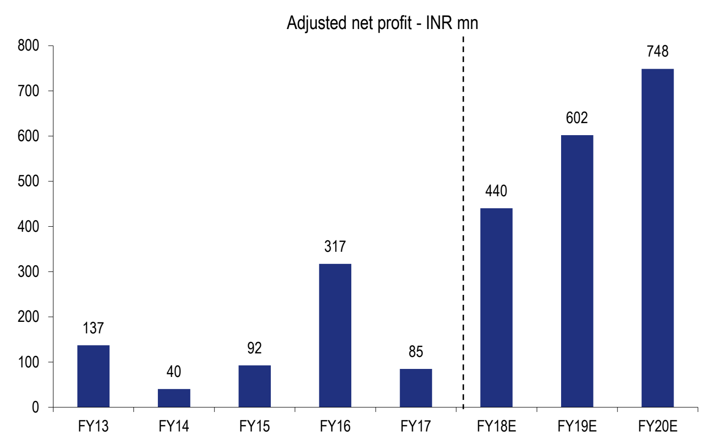
Source: Company, JM Financial

Exhibit 5. Expecting revenue CAGR of 19% over FY17-20…



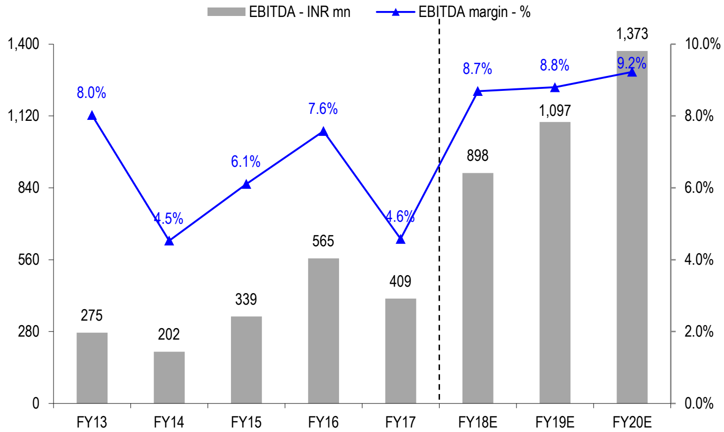
Source: Company, JM Financial

Exhibit 6. …which should help achieve healthy profits



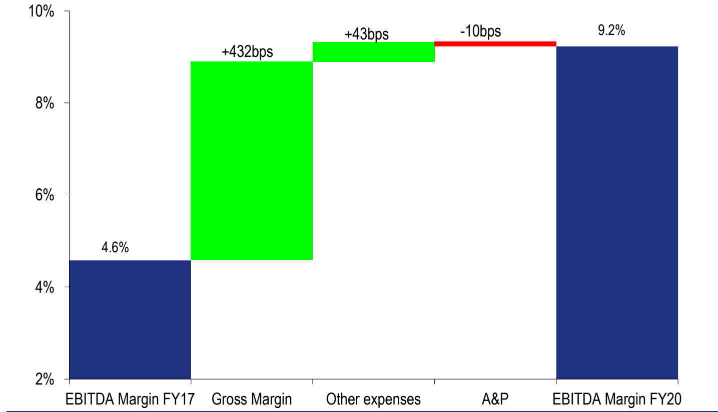
Source: Company, JM Financial

Exhibit 7. EBITDA margin to be maintained at 8-10% range



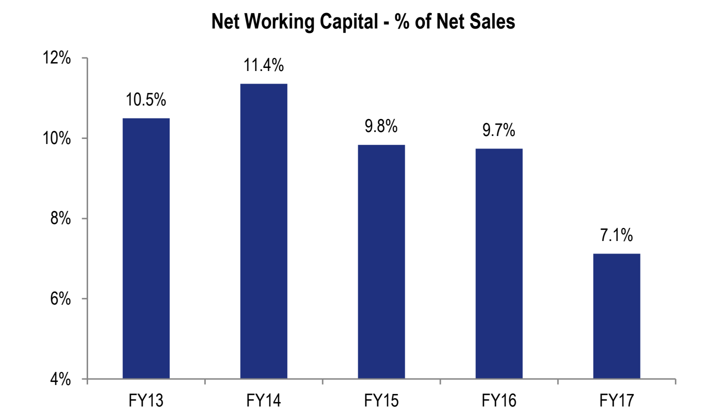
Source: Company, JM Financial

Exhibit 8. GPM gains to be the key driver for operating margin



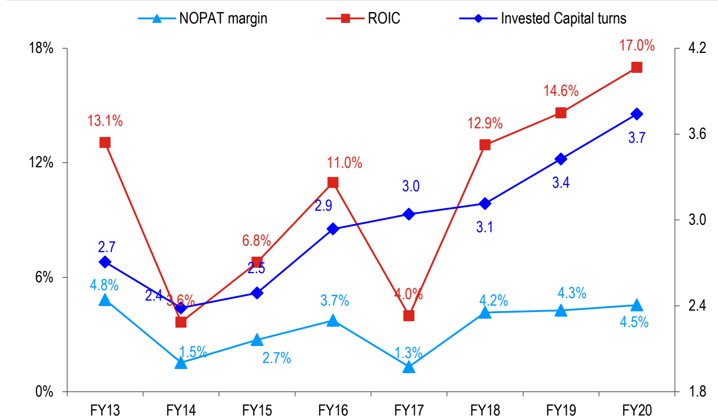
Source: Company, JM Financial

Exhibit 9. Achieved consistent reduction in net working capital



Source: Company, JM Financial

Exhibit 10. Expect ROIC to touch 17% by FY20



Source: Company, JM Financial

Value-based play to leverage the larger packaged snacks opportunity; profitability turnaround on the back of enhanced scale would be a major value driver

Prataap Snacks, best known for its brand, Yellow Diamond Chips, has, over the past decade and a half, scaled-up its revenue base to INR9bn by expanding its presence in savoury snacks category. Interestingly, the revenue build-up has happened through constant product innovation and geographic expansion – evident from the fact that potato chips which constituted c.56% of its turnover in FY12 now contributes less than one-fourth of its revenues. These measures have helped achieve 39% revenue CAGR over FY12-17, though profitability has remained volatile in the past. Continued thrust on product innovation and growth opportunities within the industry should ensure healthy growth for the company, in our view.

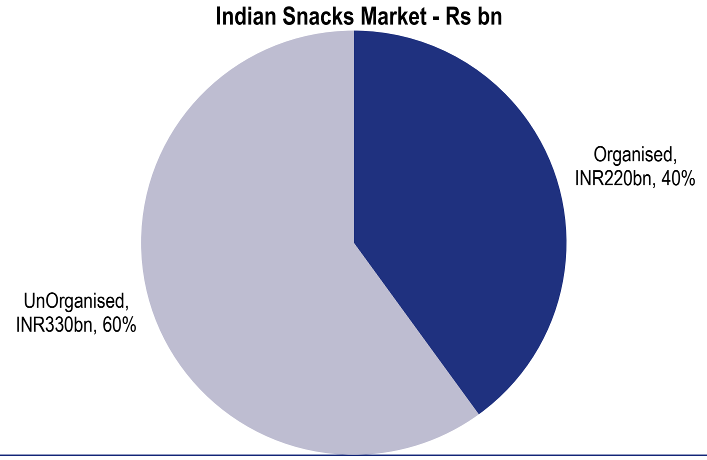
However, the level of optimum margin that Prataap can earn would be the key driver of value and, as per our analysis, once Prataap reaches a reasonable scale, a double-digit margin appears quite sustainable. There is a possibility of a healthy increase in operating margin (as witnessed in the case of Britannia but the quantum is expected to be much lower) as the company enhances scale of operations and resorts to distributed manufacturing which could help drive efficiencies across supply-chain and distribution costs. Given the focus on product innovation, intelligent marketing, delivery of higher value to consumers and cost efficiencies, we remain confident of the company achieving a much better level of profitability. We initiate with a BUY.

High-teens revenue CAGR quite possible over next 3 years given high scope for penetration and market share gains

- Large industry size but remains characterised by under-penetration: The Indian Packaged snacks market is pegged at INR550bn in size overall, and is characterised by a large number of unorganised players across all product segments. Snack preferences in India differ across regions - this trend has led to mushrooming of several companies in different regions. The smaller players typically have a slim portfolio of products and usually operate in a single category.

  Of the INR550bn total market, the unorganised segment is pegged at INR330bn representing 60%. The unorganised market largely caters to snacks that can be easily prepared. At present, there is a gradual shift in favour of the organised segment in the backdrop of increased competitive activities, cost pressures and shift in consumer preferences. With the implementation of GST from July'17, tax-evasion in business operations has become more difficult; this will, over time, reduce the advantage that unorganised players hitherto enjoyed. It is estimated that the market share between organised and unorganised players will be nearly equal in the next 5-7 years, presenting a huge growth opportunity for players in the organised segment.

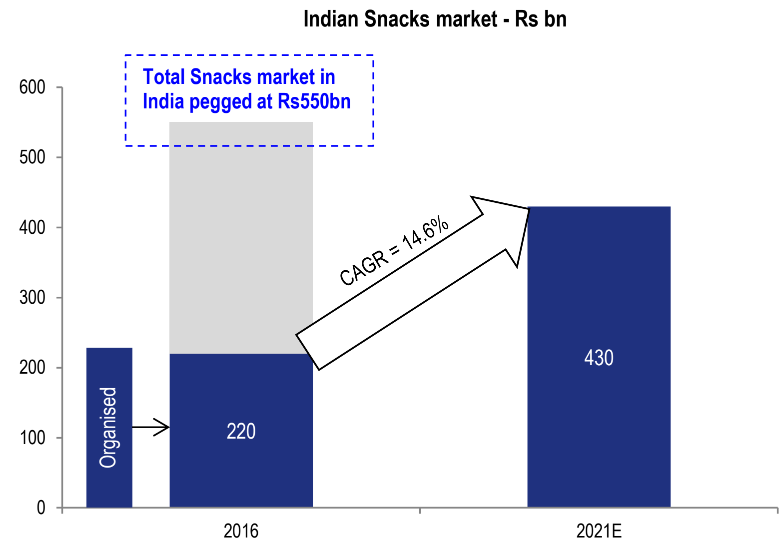
Exhibit 11. Indian Snacks Market remains largely unorganised



Source: Company, JM Financial

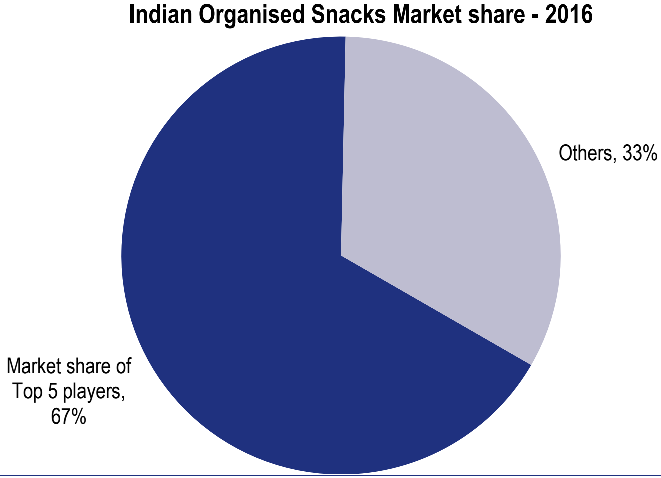
- **Organised snacks market presents an attractive mid-teens growth opportunity driven by increasing penetration and conversion:** Indian organised snacks market size is estimated at INR220bn in 2016. It is expected to post a 14-15% CAGR over the next 5 years and touch INR430bn by 2020. Growth is expected to be led by conversion from unorganised to organised segment and increasing penetration in Southern and Eastern markets which currently contribute only 38% of the total snacks market. All three major segments viz. Chips, Extruded snacks and Namkeen are expected to grow at healthy rates.

Exhibit 12. Organised snacks market expected to post 14-15% CAGR over next 5 years



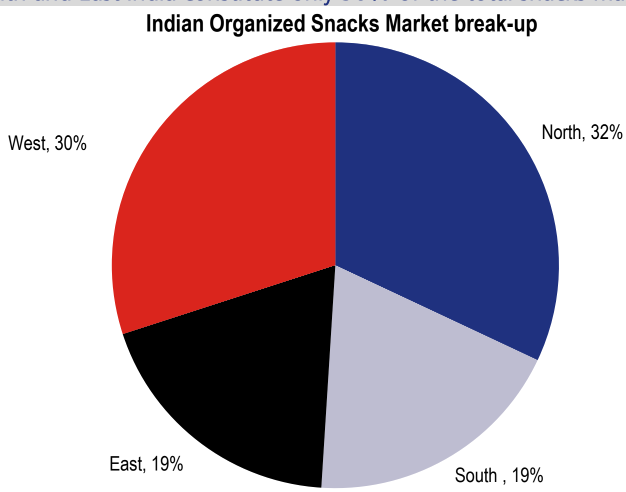
Source: Company, JM Financial

Exhibit 13. Even within organised market top 5 players have a mere 67% share; remaining market remains quite fragmented with each player having <2% market share



Source: Company, JM Financial

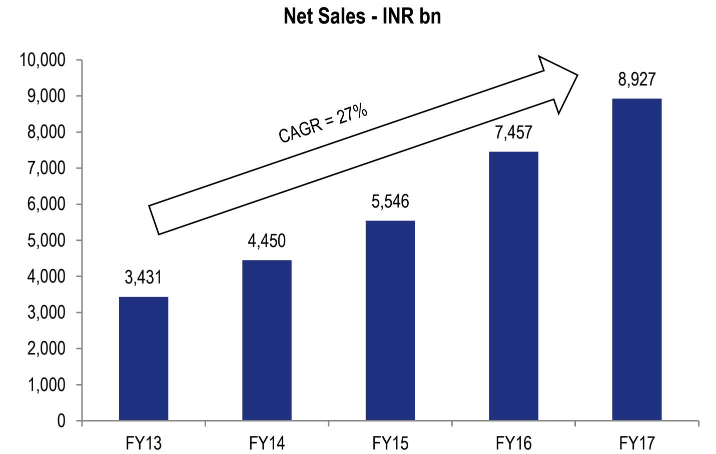
Exhibit 14. South and East India constitute only 38% of the total snacks market



Source: Company, JM Financial

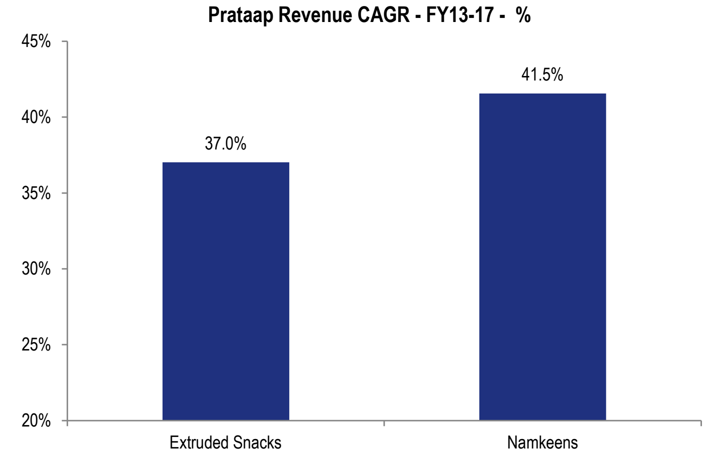
- **Prataap's presence in high growth categories and track-record of market share gains should help maintain healthy revenue growth rates:** While industry growth rates are attractive, the snacks segment is also characterised by high competitive intensity given presence of large competitors such as PepsiCo and ITC. However, Prataap's historical track-record of consistent gains in market share, commitment to new launches (new variants in existing products and entering new segments), innovative marketing campaigns and focus on expanding and leveraging its existing distribution network drive our confidence on healthy revenue growth sustaining over the medium term. Our confidence stems from:
  - **Strong 27% revenue CAGR over FY13-17; growth driven by Namkeen and Extruded Snacks:** Prataap Snacks' revenue has nearly trebled over FY13-17 to INR9bn reflecting a CAGR of 27%. The growth was achieved despite a subdued performance from Potato Chips segment which constituted 42% of its sales in FY13 and posted a mere 10% CAGR during the period. However, this was compensated by Extruded Snacks segment which posted a 37% CAGR in sales and now accounts for c.63% of its revenue (vs c.47% in FY13). Sales of Namkeen posted a 41.5% CAGR though from a relatively smaller base and accounted for 12% of gross sales in FY17. Both Namkeen and Extruded Snacks are high growth categories and expected to outperform growth of the Chips segment. Increased presence in Extruded Snacks and Namkeen augurs well for Prataap Snacks we believe.

Exhibit 15. Prataap posted 27% revenue CAGR over FY13-17 …



Source: Company, JM Financial

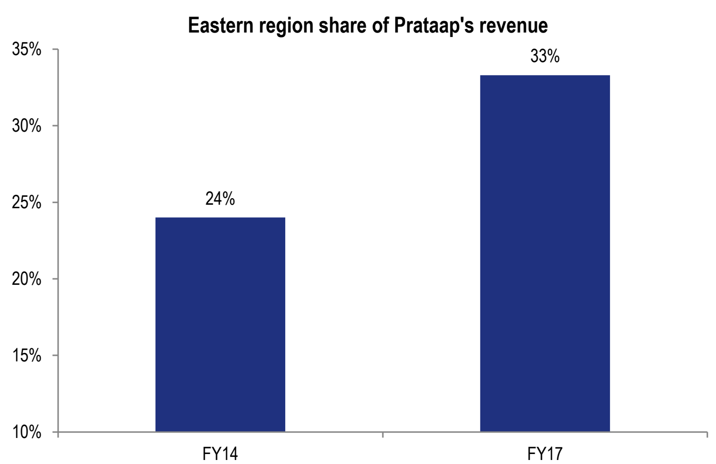
Exhibit 16. …aided by healthy growth in extruded snacks and Namkeens



Source: Company, JM Financial

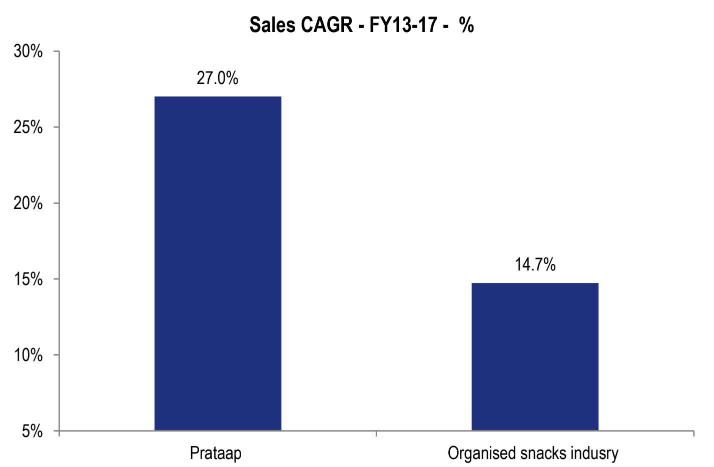
- **Prataap's revenues have grown at c.2x the industry pace aided by innovative marketing and share gains in extruded snacks:** Over 2012-16, the snacks industry has registered a 14.7% CAGR while Prataap Snacks has grown at nearly double the pace i.e. 27% CAGR. As per our analysis, this implies a market share gain of nearly 200bps in the overall organised snacks industry. A similar analysis for extruded snacks sub-category implies a near c.500bps market share gain over the period of 4 years. As per the company, expansion of its Rings product in the Eastern market aided in driving this share gain - share of eastern region in total revenues have increased from 24% in FY14 to 33.3% in FY17.

Exhibit 17. Scaling-up presence in Eatern region…



Source: Company, JM Financial

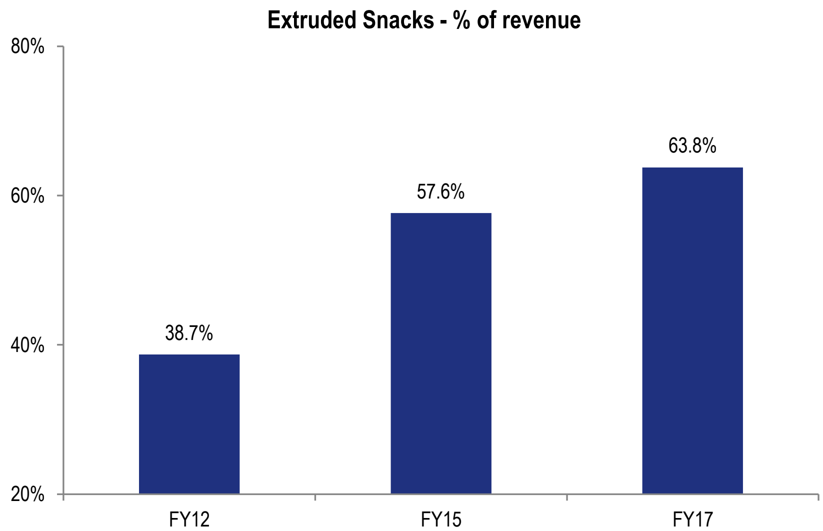
Exhibit 18. …has partially aided in driving market share gains



Source: Company, JM Financial

Prataap launched the corn rings variant (which drove market share gains) of shaped extruded snacks in FY12 under the sub-brand Rings. The product was primarily targeted at children and hence a toy was included in the pack as a key product proposition. The company tied up with popular children's TV channels and pragrammes to promote this product through select cartoons, programmes and movie marketing. These strategies worked well and helped the company gain market leadership in the corn rings segment despite it being a relatively late entrant in the segment. This product was the primary driver of revenues over past 5 years and has aided in enhancing the share of extruded snacks from 38.5% to 63.5% over FY12-17.

Exhibit 19. Extruded snacks has been instrumental in driving Prataap's revenue growth over past few years

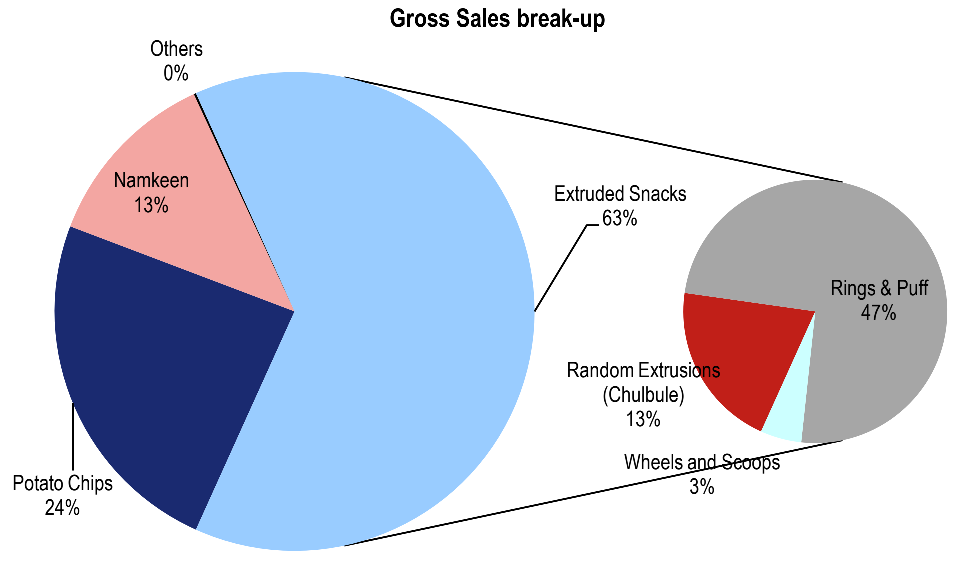


Source: Company, JM Financial

- **Higher salience of faster growth sub-categories and new launches should help Prataap outpace industry growth:** Indian organised snacks industry is expected to register a healthy 14-15% CAGR over next 5 years aided by a shift from unorganised to organised segment on increased penetration and accessibility. Prataap, given its smaller scale of operations and thrust on innovations, can outpace these growth rates significantly as done in the past, we believe. We cite the following drivers:

  Market share gains in existing portfolio: Prataap has, over the past 6 years, enhanced its market share in the overall snacks category from mere 1% in 2010 to 4% in 2016. However, it still remains a small player in the overall context which provides large headroom for growth – less than one-seventh the size of PepsiCo and just about one-fifth the size of Haldiram (taking the three Haldiram together). Interestingly, >75% of Prataap's portfolio consists of fast-growing extruded snacks and namkeen segments while chips segment which is expected to have a relatively lower growth potential constitutes <25% of revenues. Presently, portfolio concentration towards products with relatively higher growth potential should itself help the company outpace industry growth, we believe. Coupled with this, Prataap's focus on driving higher value for customers and consistent delivery of new product launches should help drive share gains within existing sub-segments as well.

Exhibit 20. Extruded snacks and namkeens now constitute >75% of portfolio



Source: Company, JM Financial

Entry in healthy snacks and sweet snacks sub-segments help build future growth drivers: For sustaining its existing high growth trajectory in future as well, Prataap is now focussing on two important areas, viz. driving presence in channels like Modern Trade and entering the sweet snacks category by leveraging its existing distribution network.

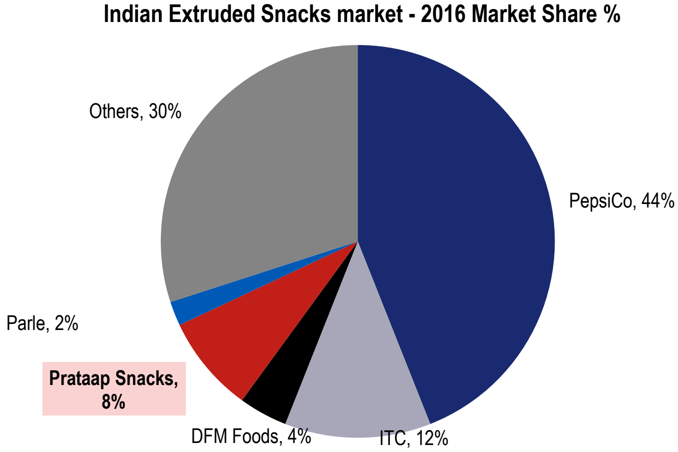
So far, Prataap has focussed on its core-set of value-conscious customers and hence derived >80% of its sales from the INR5 price point. The company is now looking to also enter new age channels like Modern Trade by leveraging the health and wellness trend. Given growing demand for healthier snacking options, Prataap has put in place a plan to grow in the healthier snack segment through the introduction of Chips made from healthier ingredients like hummus and lentils. It is stepping-up research and development efforts on the product attributes that are most valued by consumers, including taste, nutrition, food-safety and convenience. This would allow the company to better serve the increasing demand from consumers for healthier, tastier and higher quality food products and gain market share in the process.

Enhancing geographical penetration: Prataap Snacks' current focus is on increasing penetration in the markets where it currently operates viz. North and West zones particularly in Rajasthan, Punjab and Uttar Pradesh by replicating its product proposition that has historically helped its brand growth. It is also planning to increase presence in the relatively newer Southern market, by using its Ring product to gain market share. Southern region contributed merely 9-10% of sales in FY17 and presents huge scope for expansion. The company also intends to appoint more super stockists to strengthen its existing sales infrastructure and increase its advertising activities to build brand awareness in key geographies.

- **Projecting high-teens revenue CAGR over next 5 years; market share gains of 150bps in extruded snacks:** We are building in c.19% revenue CAGR over FY17-20 which is quite in-line with growth rate witnessed in FY17 (impacted by demonetisation) and much lower relative to 27% CAGR witnessed over FY13-17. Extention of its extruded snacks portfolio to southern markets and scaling-up its Namkeen category are expected to be the key driver for growth. We are also projecting a successful launch of choco-pie though contribution would still be limited at the end of three years (<3% in FY20).

  Our estimates imply c.150bps share gain by Prataap Snacks over the next 5 years relative to nearly 6ppt gain in share that the company has achieved over past 6 years. Interestingly, the company is still in process of gaining scale in the Southern region which is a larger market relative to Eastern region for Extruded snacks category. Coupled with this, entry in the modern trade channel, launch of new variants and focus on distribution expansion should help drive market share gains in our view. It is also important to note that top 5 players constitute 67% of the market and balance 30% remains quite fragmented with none of the individual players having a market share in excess of 2%. Gradual market share gains from these smaller players seems quite achievable, in our view, especially given the huge scope for distribution led expansion. Despite the 150bps gain, it would still remain below ITC's market share.

Exhibit 21. Prataap Snacks has 8% market share in extruded snacks category and is the third largest player.



Source: Company, JM Financial

Exhibit 22. Our estimates imply a 150bps market share gain over next 5 years relative to 600bps achieved over past 6 years in Extruded snacks

INR mn	FY17	FY22	Cagr
Prataap - Sales at Company level (Extruded Snacks)	5,694	13,561	19.0%
Prataap - Sales at MRP level	8,134	19,373	19.0%
Estd CAGR for the Industry			15.0%
Market share for Prataap	8.0%	9.5%	
Mkt size based on Prataaps' data	101,670	204,169	

Source: Company, JM Financial

Double-digit margin highly probable over the medium term.

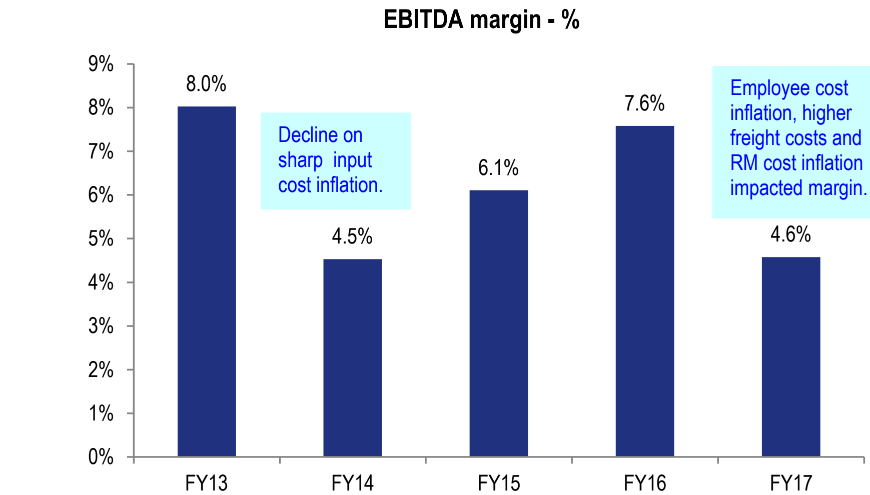
- Operating margin volatility in the past has raised investor concerns….: Historically, Prataap had high volatility in its earnings performance largely driven by sharp inflation in its key raw materials – potato (c.14% of RM cost base in FY17) and edible palm oil (30% of its RM cost base in FY17). Its EBITDA margin has swung in the 4-8% band over past 4 years with sharp expansion or contraction seen every year.

  Operating margin fell to trough levels of c.4.5% in two out of the past four years - FY14 and FY17. Interestingly the reasons for the nose-dive in margin are quite different – FY14 was purely on account of inflation in input costs viz. potato and edible oils while FY17 operating margin was also impacted by other factors (in addition to RM cost inflation) viz.,

  - High inflation in employee costs.
  - Sharp increase in freight costs on enhanced turnover in the Southern region which had to be serviced from Indore facility on account of capacity constraints.
  - Increase in contractual labour costs on wage settlement in Guwahati factory.

  The sharp contraction was also partially attributable to deceleration in revenue growth post demonetisation. Lower throughput adversely impacted absorption of fixed cost which was built up to support a higher revenue base.

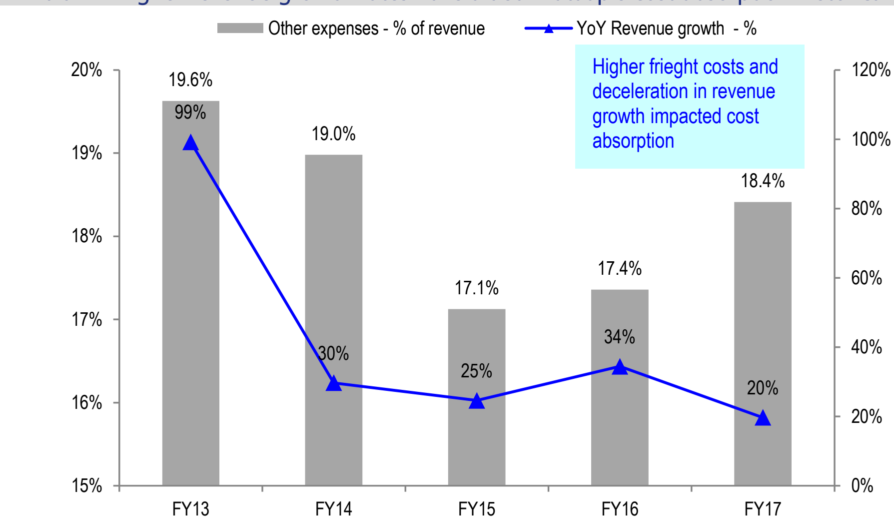
Exhibit 23. Operating margin has been sensitive to cost inflation in the past given limited pricing power.



Source: Company, JM Financial

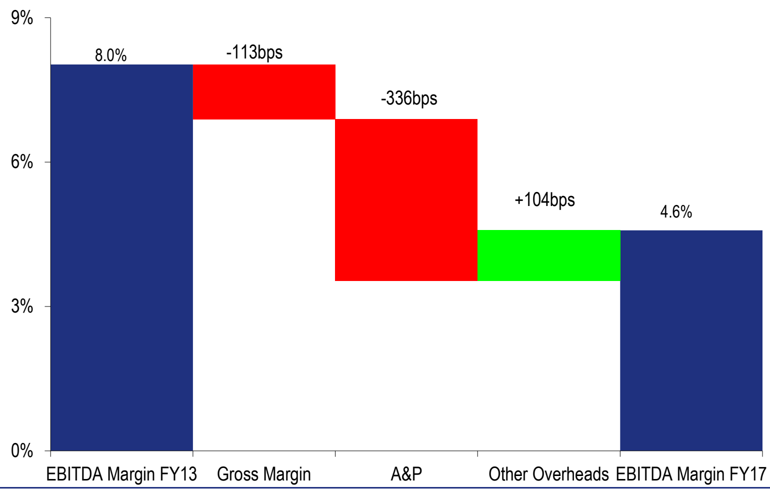
- ….however, its efforts that drove savings in other expenses were overshadowed by incremental investments in A&P spends: Over FY13-17, Prataap's EBITDA margin has been quite volatile on steep changes in raw material costs and higher personnel costs. Its interesting to note, however, during this period Prataap's investments behind A&P spends grew 14x and increased by c.340bps as a percentage of sales. Excluding the investments behind A&P spends, EBITDA margin was near flattish despite 113bps contraction in gross margin and 123bps increase in staff costs (as % of sales) – largely on 120bps reduction in other expenses (aided by positive operating leverage) and higher other operating income. In our view, the opportunities for scale-led efficiencies could be higher over a longer term once revenue growth rates normalises.

Exhibit 24. Higher revenue growth rates have aided Prataap's cost absorption historically



Source: Company, JM Financial

Exhibit 25. GPM compression was largely negated by savings in other overheads; Investment behind A&P spends impacted operating margin over FY13-17

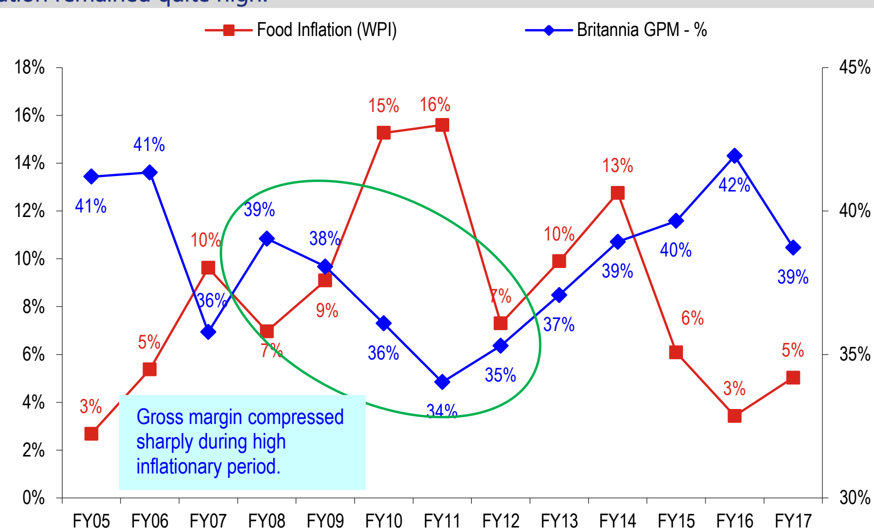


Source: Company, JM Financial

- **Operating margin near double-digit in 1HFY18; maintaining closer to these levels possible:** Given the historical volatility, the level of optimum margin that the business can achieve over a business cycle remains uncertain and historical performance probably implies margin potential to be much lower. The fact that packaged snacks industry has an inherently lower gross margin given high competition from the unorganised and illicit players could probably lead some scepticism on the potential for margin expansion remains in Prataap's case.

  However, the snacks industry appears to be quite similar to biscuits industry (also has similarly well-entrenched unorganised competition) which has recently witnessed a strong premiumisation trend driving higher margin for Britannia. During the period of high food inflation and intense competition, Britannia's gross margin compressed sharply – c.500bps compression over FY08-11. However, as food inflation stabilised and the company embarked on its premiumisation agenda, its gross margin crossed 40% (42% in FY16 under Igaap).

Exhibit 26. Britannia's gross margin witnessed sharp compression over FY08-11 when food inflation remained quite high.

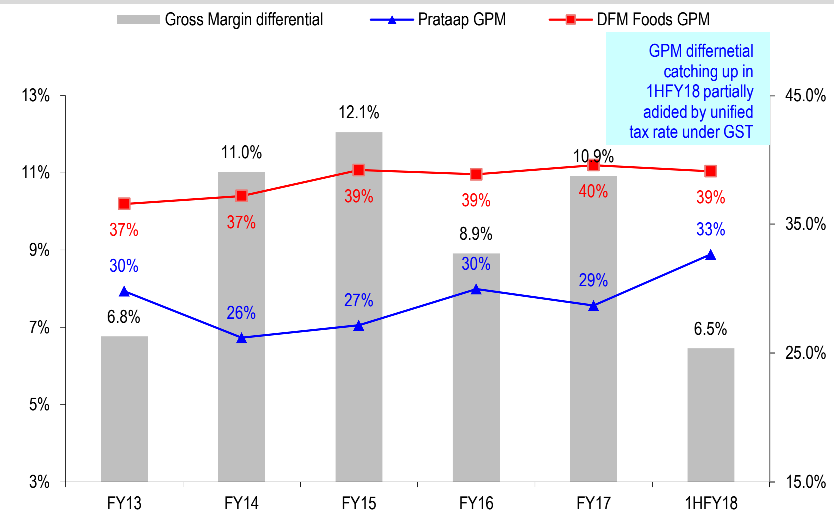


Source: Company, JM Financial

In our view, a similar trend can also play our for Prataap Snacks and as edible oil prices stabilise, the company could post sustained margin expansion. It is interesting to note here that Prataap's immediate competitor viz. DFM Foods has clocked gross margin in the range of 35-40% over FY13 to FY16 while Prataap's GPM has been around 26-30% over the same period. The reasons for the differences were,

- Prataap snacks derive revenues across regions with north/east/west accounting for 30%/33%/30% of turnover. It has scaled-up its revenues in a quick span of time and given manufacturing presence largely in central India, it had to appoint super-stockists across regions. DFM Foods' presence is largely in Northern region (c.80% of its turnover) and hence direct distribution is quite feasible for the company which helps save some channel margin.
- DFM Foods, with its operations largely in Northern region, was subjected to a much lower VAT rate (5%) while the average VAT rate for Prataap Snacks stood at 8-9%.
- Prataap Snacks has a higher proportion of Namkeens in its portfolio which is a voloume-led lower gross margin segment while DFM Foods portfolio largely consisted of Rings (Extruded Snacks).

Exhibit 27. Prataap's gross margin differential vs DFM has nearly-halved in 1HFY18 vs peak level seen in FY15

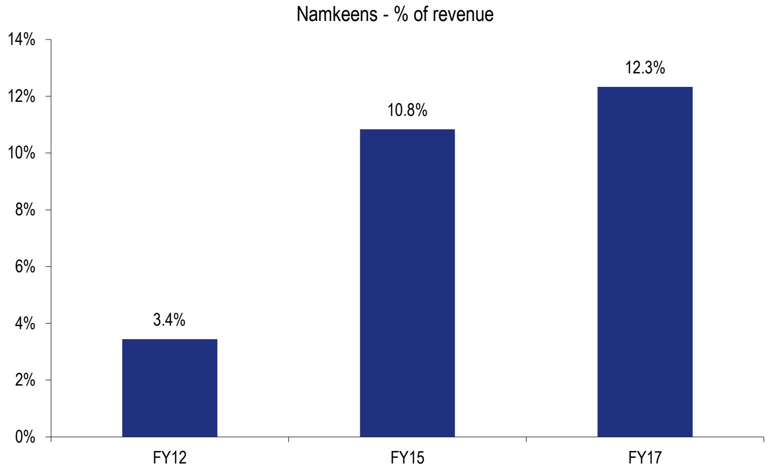


Source: Company, JM Financial

The GPM differential has fallen to 580bps in 2QFY18 as GST implementation has now equalised the tax incidence across regions. Interestingly, the company has clocked a 9.4% EBITDA margin in 1HFY18 and expects the margin to be largely in the range of 8-10% henceforth. The sharp increase in EBITDA margin was a result of benign raw material cost environment, cost efficiencies in GST regime and some grammage adjustments which should aid margin in future as well.

With GST now equalising tax incidence across regions, it creates a level playing field for national players like Prataap and is expected to be detrimental for some of the regional players hitherto enjoying lower tax incidences. Coupled with improved margin in Namkeens portfolio and price increases, we expect Prataap Snacks to sustain EBITDA margin in the 8-10% range in near future.

Exhibit 28. Increased contribution from Namkeens had adversely impacted gross margin historically



Source: Company, JM Financial

- Double-digit margin on a sustainable basis quite possible as scale increases: While we expect operating margin to be in the 8-10% range over medium-term, the possibility of company achieving a double-digit margin on a sustainable basis also remains high in our view. The scale-up in margin could follow a somewhat similar pattern that we have witnessed in Britannia. As the scale of operation increases, the company would be looking at establishing distributed manufacturing facilities which would help gain a larger share of the retail price by eliminating the incremental middle-men in the supply chain as well as reduce freight costs. Furthermore, the possibility of premiumisation of product portfolio also remains high given new launches are now on the health and wellness platform which command higher operating margin; its sweet snacks venture is also expected to have a higher gross margin.

Possibility of mid-teens ROIC and strong cash generation would help sustain the premium valuation multiple.

- Investments in enhancing scale of operations / distribution reach and one-off events impacted profitability in FY17: Investments on capacity, brand-building, product portfolio diversification, scaling-up presence in Namkeen segment, RM cost inflation and distribution expansion have adversely impacted Prataap's profitability in FY17. In addition to this, revenue growth rate also sharply decelerated towards the end of FY17 on account of demonetisation exercise which led to sub-optimal absorption of overheads and staff costs. While the company scaled-up RoE to a healthy level of 15.6% in FY16, ROE fell sharply in FY17 to a mere 3.7% on account of high RM costs (resulting in 129bps GPM compression) and increased overheads relating to a new facility in Guwahati.

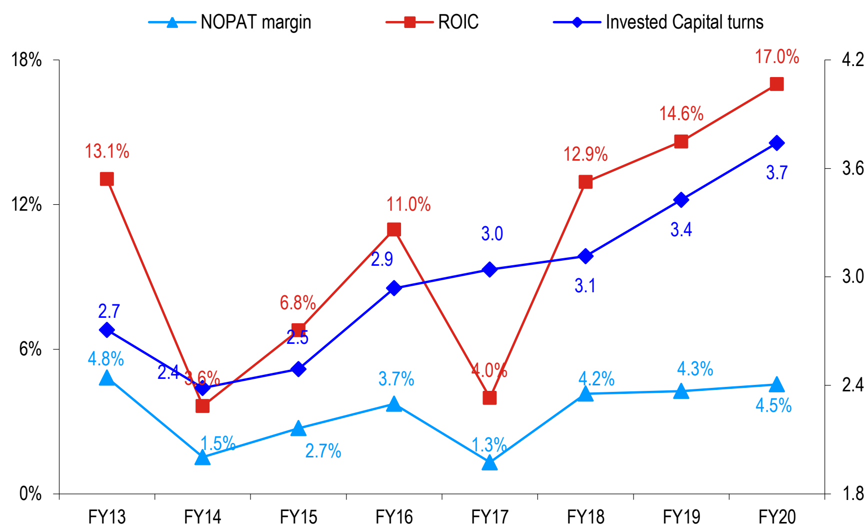
- Profitability now back to healthy levels: After a sharp dip in profitability in FY17, EBITDA margin has now touched near double-digit level in 1HFY18 aided by improved realisations and a benign raw material cost environment. As discussed earlier, given tax incidence now being similar across regions, a more well-diversified portfolio and capacities ramped up in Southern region, we expect Prataap to maintain EBITDA margin in 8-10% range over the medium term. Benefits of higher scale of operation and efforts on portfolio premiumisation should also help drive EBITDA margin in the future.

- We expect ROIC to cross 15% by FY20: Volatility in profitability has evidently impacted the return ratios for Prataap and ROIC has fluctuated between 4-14% over FY12-17. The lower ROIC has, however, overshadowed the efficiencies achieved in asset utilisation during this period. The company's total asset turns increased from 1.7x in FY12 to 3.0x in FY17 despite high investments in capital expenditure – gross fixed assets increased 4x during the period. This was largely driven by enhanced throughput (sales grew 5.2x) and by efficiency in working capital management – net working capital declined from 13.2% of sales to 7.1% by FY17. Decline in NWC was largely led by better inventory management which led to a steep decline in inventory days - fell from 54 days of sales in FY12 to 32 days in FY17.

Prataap has, in fact, achieved 15% ROIC in 1HFY18 itself (based on opening invested capital) on the back of improvement in profitability with EBITDA margin touching near double-digit levels. However, we are building in operating margin in the range of 8.5-9.5% over the next two years given volatility in raw material costs and limited pricing power in core value portfolio. In our view, the improvement in return ratio would be completely driven by better utilisation of fixed assets (through enhanced scale of operations) and further improvement in working capital.

At NOPAT margin of 4.5% (clocked 4.8% in FY13 and 3.7% in FY16), gross fixed asset turns of 3.2x and net working capital of c.6% of sales, Prataap can clock a 17% ROIC in FY20, on our estimates. ROE is expected to remain lower at 12%, though, given high net cash on balance sheet.

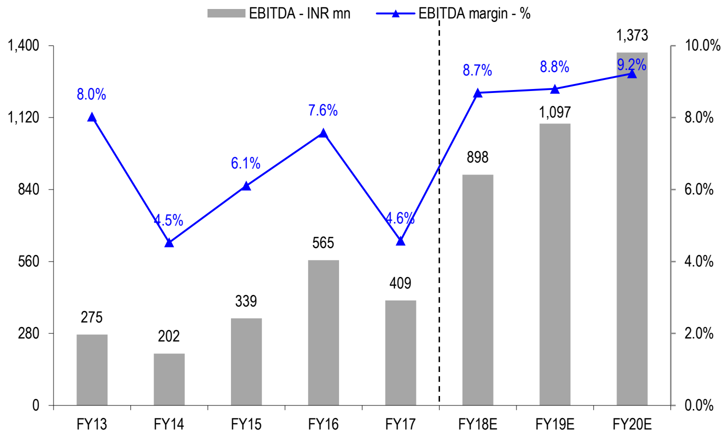
Exhibit 29. ROIC to touch 17% by FY20



Source: Company, JM Financial

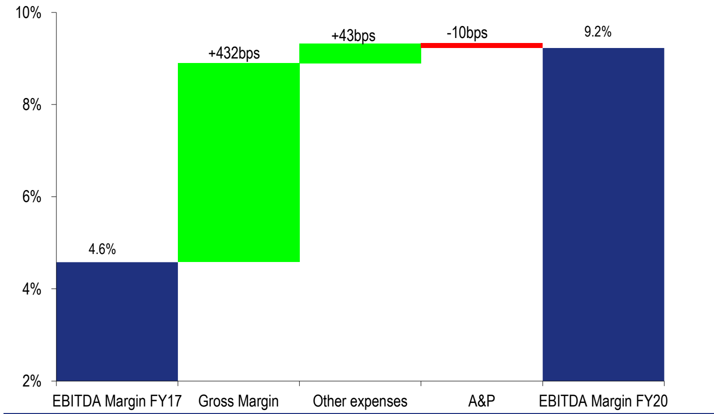
- **Higher operating margin to aid cash generation as well:** Prataap has recorded positive operating cash flows in each of the past 6 years though free cash flows have been negative on account of investment in capital employed and volatile margin. With margin volatility now largely addressed and limited requirement of capital expenditures, we see inherently healthy free cash flow generation potential for the company. On our estimates, Prataap can generate free cash flow of in excess of INR100mn in each year over next three years.

Exhibit 30. Operating margin to sustain above 8% levels



Source: Company, JM Financial

Exhibit 31. Gross margin gains to aid operating margin



Source: Company, JM Financial

Our DCF based price target at INR1,390 provides c.19% upside

- At current market price of INR1,168, Prataap is trading at c.24x on NTM EV/EBITDA and 48x NTM earnings. Near-term financials, in our view, do not entirely capture the high revenue growth opportunity and the huge potential for improvement in Prataap's profitability metrics.
- We resort to DCF methodology for valuation as it not only captures the long-term revenue growth potential and hence the higher scale that Prataap can achieve over a period of time, but also the possibility of driving higher margin in the future as well as improvement in asset-turns. Our DCF based target price works out to INR1,390/share. Our DCF based methodology is divided in three phases:
  - Explicit period of 10 years where we are forecasting c.31% FCFF CAGR over FY19-29E.
  - Fade period where we forecast free cash flow growth to slowly fade to 7% levels over a 10-year period.
  - Terminal value based on 6% terminal growth rate.
- Our DCF is based on Prataap delivering 11-12% EBITDA margin by the end of explicit period on a sustainable basis. As discussed earlier, we believe there is a higher probability of operating margin being in double-digit levels once scale of operations increases and efficiencies are delivered.
- WACC for the business is estimated at 12%.

Exhibit 32. With estimates of c.31% free cash flow CAGR over FY19-FY29, we arrive at a DCF based price target of INR1390

	FY16	FY17	FY18E	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E	FY29E	CAGR
Year for fade period	11	12	13	14	15	16	17	18	19	20					
Year for explicit period			0	0	1	2	3	4	5	6	7	8	9	10	
Explicit Forecast															
EBIT	385	159	572	728	939	1,178	1,472	1,793	2,134	2,531	2,967	3,517	4,093	4,761	
Tax Rate	0.7%	23.5%	26.3%	29.7%	30.8%	31.9%	31.9%	31.9%	31.9%	31.9%	31.9%	31.9%	31.9%	31.9%	
NOPAT	**383**	**121**	**422**	**512**	**650**	**803**	**1,003**	**1,221**	**1,453**	**1,724**	**2,020**	**2,395**	**2,787**	**3,243**	**20.3%**
Depreciation	180	250	326	369	434	509	593	686	788	899	1,018	1,143	1,285	1,443	
Change in net working capital	-181	91	-119	-77	-116	-108	-115	-171	-185	-210	-208	-234	-263	-297	
Capex	-323	-786	-516	-623	-670	-797	-843	-987	-1,006	-1,173	-1,151	-1,314	-1,465	-1,635	
Free Cash Flow	59	-324	112	180	298	407	638	749	1,050	1,240	1,679	1,991	2,344	2,754	31.3%
Discount Factor					0.89	0.80	0.71	0.64	0.57	0.51	0.45	0.40	0.36	0.32	
Discounted FCFF					266	324	454	476	596	628	759	804	845	887	

Fade Period	FY30	FY31	FY32	FY33	FY34	FY35	FY36	FY37	FY38	FY39
FCFF	3,206	3,700	4,231	4,793	5,380	5,983	6,590	7,189	7,768	8,312
% growth	16.4%	15.4%	14.3%	13.3%	12.2%	11.2%	10.1%	9.1%	8.0%	7.0%
Discount factor	0.3	0.3	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1
Discounted FCFF	922	950	970	981	983	976	960	935	902	862

Valuation	
PV of explicit forecast	6,039
PV of Fade period	9,439
PV of terminal value	15,222
Enterprise Value	30,701
Less:	
Net Debt	-1,918
Minority interest	
Value attributable to equity shareho	32,619
No. of shares - mn	23
Share price - Rs	1391
WACC	11.0%
Terminal growth rate	6.0%
EPS - 1 yr fwd	31.9
P/E	43.6
EBITDA - 1 yr fwd	1,373
EV/EBITDA	22.4

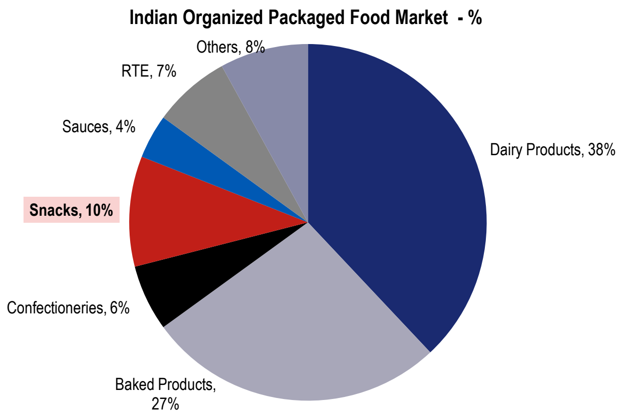
Source: Company, JM Financial

Indian packaged foods industry overview

- **Snacks constitute 10% of the Indian organised Packaged Foods market: Indian packaged foods market includes ready-to-eat / cook foods aimed at providing convenience to consumers.** They have a higher shelf-life as they usually undergo certain degree of processing to increase taste, stability etc. It includes bakery products, canned / dried processed food, frozen processed food, meal replacement products, dairy products, snacks, confectioneries, beverages, etc. Prataap Snacks mainly operates in snacks segment which constitutes 10% of the organised Indian packaged foods market.

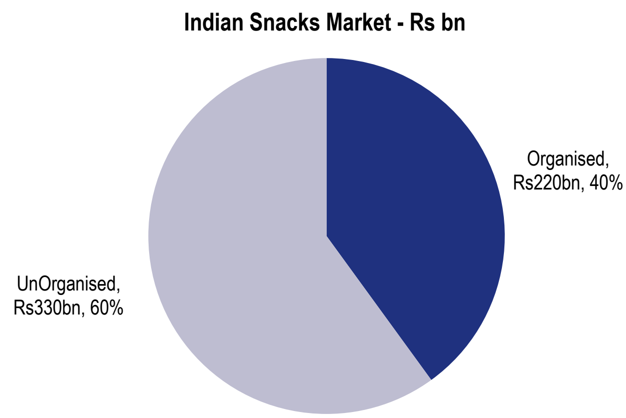
  The Indian organised packaged snack and savouries market is pegged at INR550bn. The market is characterised by large number of unorganised players operating across product segments. Snack preferences differ across regions and many small players operate in each market catering to particular type of snack with a slim portfolio of product on that account. On account of these reasons, only 40% of the snacks market is organised and this also presents a huge growth opportunity for organised players.

Exhibit 33. Snacks constituted 10% of organised packaged foods segment



Source: Company, JM Financial

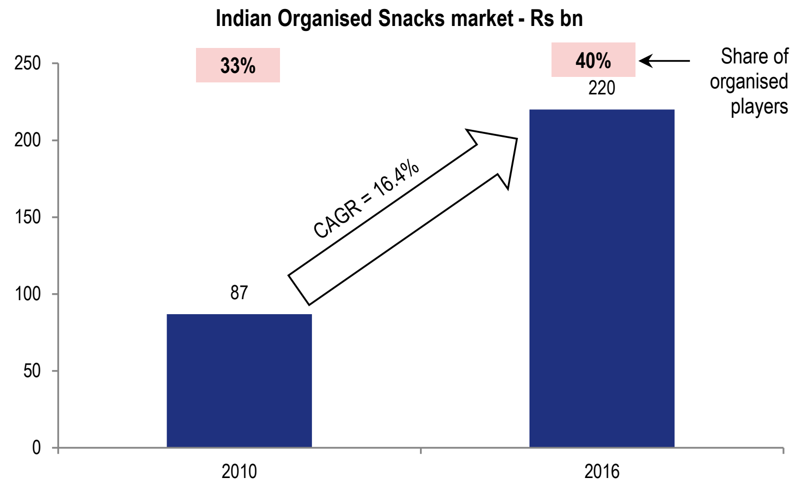
Exhibit 34. Unorganised segment still constitutes 60% of the total market



Source: Company, JM Financial

- **Indian organised snacks market growing at 16.4% CAGR:** The Indian organised snacks market stood at INR220bn as at the end of 2016 and has grown at 16.4% CAGR over past 6 years. High growth has been aided by overall growth in processed foods segment and a trend towards consolidation. Aided by better infrastructure and technology, organised players have been able to re-create traditional Indian snacks and products which has aided in increasing their market share. Large FMCG companies characterized by large portfolio of products, aggressive advertisements and active R&D have been able to drive leadership position in several product categories. They have been able to better navigate cost pressures and increased competition which has aided gradual shift towards organised players across segments.

Exhibit 35. Indian organised snacks market pegged at INR220bn, expected to grow at 16.4% CAGR



Source: Company, JM Financial

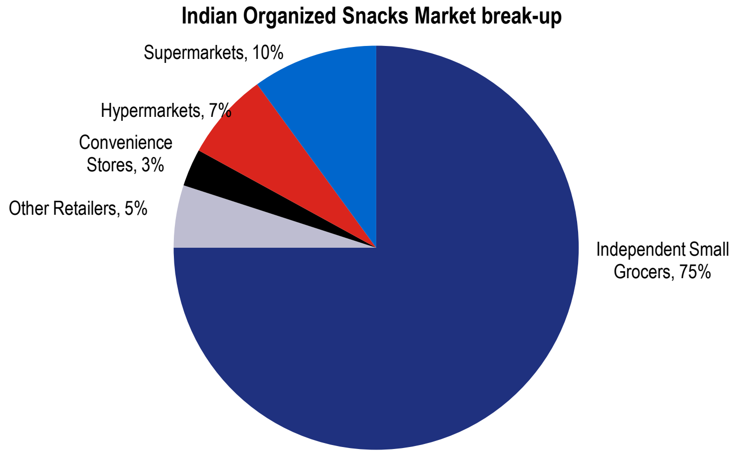
- Traditional Snacks and Namkeen market still have the largest share of the Indian Snacks market: Traditional Snacks and Namkeen still account for the highest share in the Indian organized snacks market- 36% in 2016. Chips now accounts for 30% while Extruded Snacks constitute 32%. Higher availability and easy accessibility have aided in driving growth. PepsiCo India, with Lays' Chips and Kurkure (Extruded Snacks) in its portfolio, is the market leader with c.30% market share. Medium-sized companies like Balaji Wafers and Prataap Snacks are also gaining visibility across India.

- Independent grocers account for 75% of Snack sales in India: Due to the structure of the Indian retail market, there is a large presence of unorganised small grocery stores and petty shops that cater to the daily demands of consumers. These shops are present in residential areas, and stock essential products and are targeted by companies to attain maximum consumer-reach. These independent grocery stores account for c.75% of the total snacks sales and typically stock the most popular products and SKUs of each category. Petty shops usually stock the smallest SKU size product which is more popular in the rural markets.

  There is an increasing trend towards modern retail trade in urban markets. Consumers are attracted by factors such as size of the outlets, multiple options and varieties, presence of imported products, offers and discounts and the option to purchase all products under one roof. Hence, snack companies are also increasingly offloading their products through hypermarkets and supermarkets. This provides opportunities to display larger varieties and get more SKUs, launch new products and flavours, sell multi-packs through offers, etc. Snack companies typically stock medium-sized and large sized packets to cater to this segment of consumers.

  However, the domination of small grocery stores is expected to continue for the next five to ten years. E-tailing of snacks is still in a nascent stage and snack companies may not look at this in a big way since snacks are typically impulse purchases.

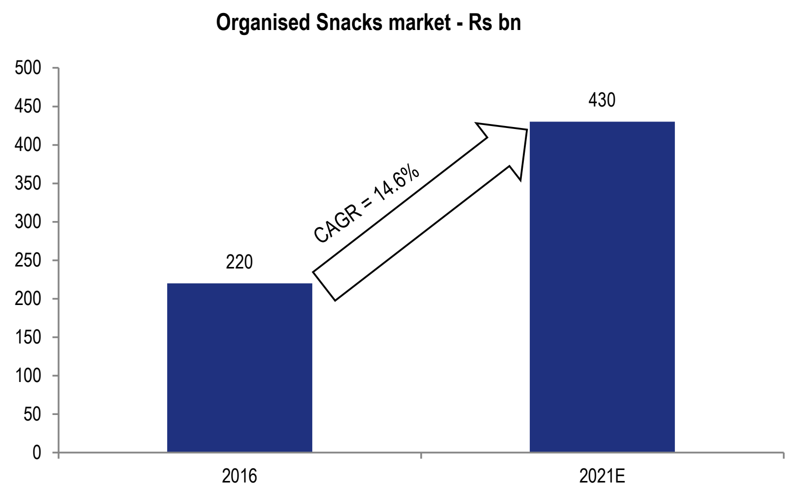
Exhibit 36. As the purchases are impulse driven, Independent small grocers dominate the sales channel for snacks



Source: Company, JM Financial

- **Organised Snacks market estimated to grow at a CAGR of c.14.6% over the next 5 years:** The market for Organised Snacks in India is estimated to grow at about 14.6% CAGR, between 2016 and 2021. Some of the traditional segments such as chips, nuts and popcorn are expected to witness only moderate growth of about 10% as these categories have reached near maturity with limited scope for new offerings. The market for Namkeen is expected to witness the highest growth, at 17.8% over 2016-2021 driven by shift from unorganised sector to the organised sector, and also by higher penetration in Southern and Eastern markets.

Exhibit 37. Organised snacks market is expected to maintain a healthy growth rate over next 5 years



Source: Company, JM Financial

- **PepsiCo is the largest player in the Organised Indian Snacking space:** PepsiCo, driven by its brands Lays (Chips) and Kurkure (Extruded Snacks) has a strong 30% market share in the Indian organized snacks market. Its brands are present in all the 3 segments viz. Chips, Extruded Snacks and Namkeen with >40% market share in Chips and Extruded Snacks. A large portfolio of products, innovative flavours, extensive distribution network, regular new product launches, aggressive advertisement and promotion and celebrity endorsements have helped PepsiCo gain dominance in these categories.

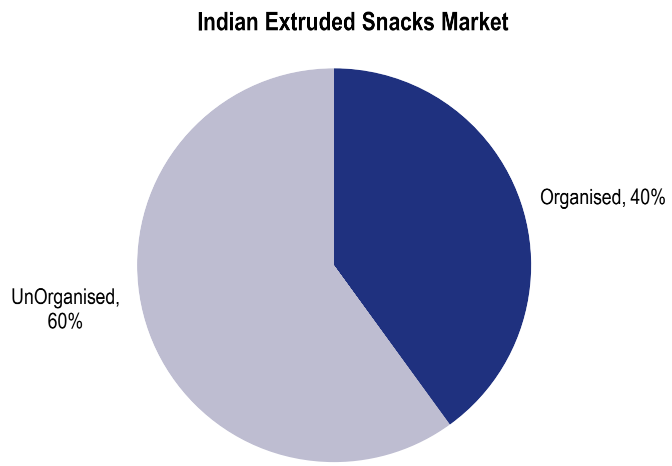
  In addition to PepsiCo, strong growth has also been witnessed by players like Balaji Wafers and Prataap Snacks. These companies account for 7% and 4% market share in organised snacks market respectively. Balaji Wafers was started in Western India and despite its marketing spending being much lesser than PepsiCo, it has been able to dominate the market for Chips in this regions with c.60% market share. Prataap Snacks has established presence in Western and North Indian markets and is currently increasing penetration in Southern markets as well. Prataap Snacks is the market leader in the Rings part of Extruded Snacks segment.

At an overall level, the products of Prataap Snacks at the INR5 price point contained up to 25% more grammage than that of the market leader. This is critical for the price conscious middle-class Indian consumer and has been one of the key factors that led the growth of medium-sized companies, especially in semi-urban and rural markets.

Extruded Snacks

- **Extruded snacks have become one of the preferred snacking choice of consumers:** Extrusion technologies have an important role in the food industry as an efficient manufacturing process. The products developed by this process are known as Extruded Snacks and they differ in colour, shape, and texture. Extruded food products are mainly corn flour and potato-based but a combination of flours can also be used. Fast-paced lifestyle, high disposable income, rising urbanisation, and transforming food culture have attributed to the growth and demand of the Indian snacks market, including Extruded Snacks.
- **Extruded Snacks market has grown at 14.4% CAGR:** Extruded Snacks market is valued at INR174.6bn and has registered c.14.4% CAGR over past 6 years. Only 40% of the overall extruded snacks market is organized pegging the organized market at INR69.6bn and implying high scope for penetration led growth.

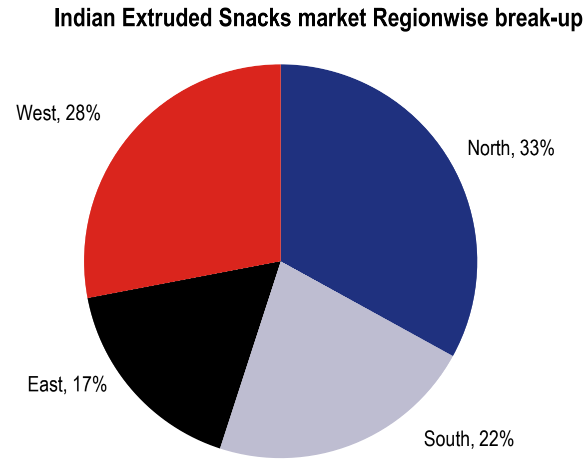
Exhibit 38. Unorganised segment accounts for 60% of Extruded snacks



Source: Company, JM Financial

Northern and Western India are the largest markets for Extruded Snacks. Both these regions also witnessed the fiercest competitive action in both the organised and unorganised segments. Small pack size is imperative to push sales volumes, especially in the rural markets, where penetration is minimal. Even in extruded snacks, the products that are sold across the various regions vary depending on what is native to the region and the typical flavours enjoyed in that region.

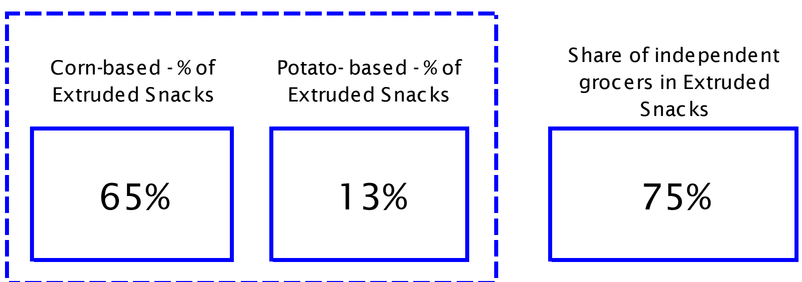
Exhibit 39. Region-wise split of extruded snacks market



Source: Company, JM Financial

Rings is one of the key varieties of Extruded Snacks segment and including corn rings, it accounts for about 8-10% of the total Extruded Snacks market. This segment is entirely targeted at children. There are various types of Corn-based Extruded Snacks but the most common one is the puffed variety. Variants such as cheese balls, cheese puffs, and spicy corn puffs are popular. Fryums are also a popular category in the market, with a large presence of unorganised players.

Exhibit 40. Brief snapshot of the Extruded Snacks market

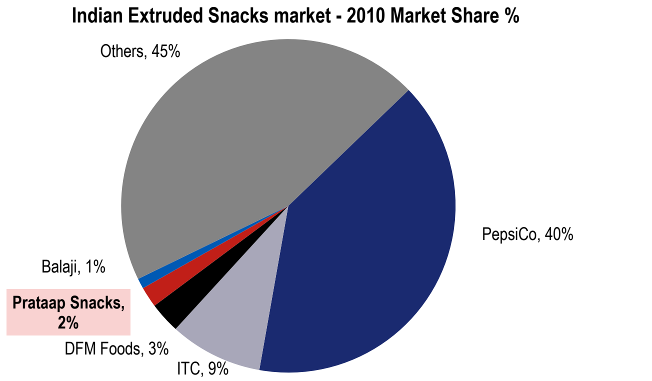


Source: Company, JM Financial

Organised Extruded Snacks is expected to grow at c.15% CAGR (2016-21) over next five years driven by market growth and share gains from the unorganized sector.

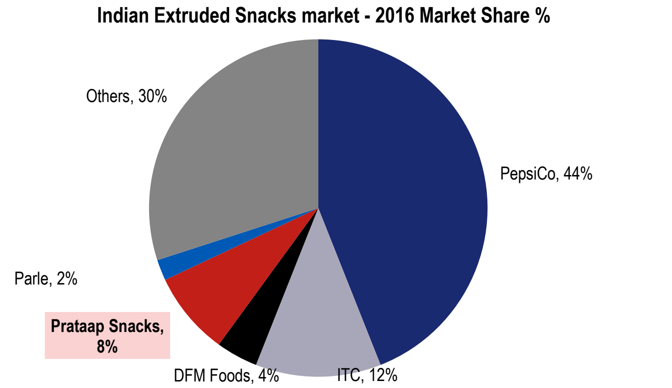
- PepsiCo is the overall market leader; Prataap Snacks leads in Corn-rings category: PepsiCo is the market leader with a 44% value share in 2016 with their 15-year-old brand Kurkure. Medium-sized companies like Prataap Snacks, Balaji Wafers and DFM Foods are strong in certain regional pockets and offer better prices than the major companies to help increase penetration across the country. The presence of such players is high in Western India indicating the intensity in level of competition in that region. By expanding their product portfolio and penetrating newer markets, these companies have been garnering market shares over the last two to three years and clocking high growth rate. Prataap Snacks is the market leader in corn-rings with Rings, followed by DFM Foods with 'Crax'. Medium-sized companies, including Prataap Snacks and SM Foods, have been moving towards expanding across the entire country and challenging the large companies. Smaller companies have thus far been typically confined to a city or a few cities in a region.

Exhibit 41. Extruded Snacks: Market share 2010



Source: Company, JM Financial

Exhibit 42. Extruded Snacks: Market share 2016

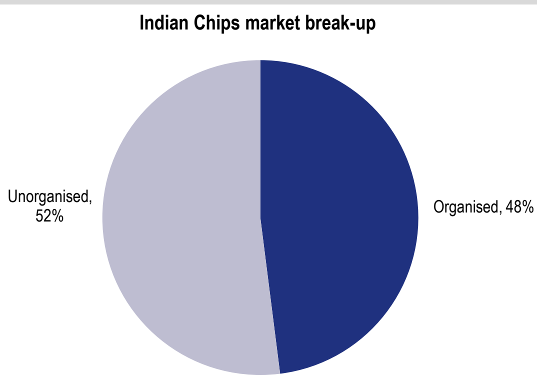


Source: Company, JM Financial

Chips

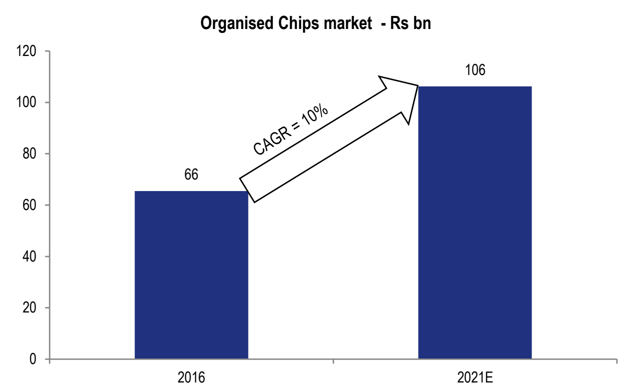
- **Chips market in India is a sizeable one; Valued at INR137.6bn**: There are a large number of players in the market operating at national level as well as regional level. In addition to potato chips, tapioca chips and banana chips are the top varieties consumed in the country. Potato is the most popular variety and accounts for more than 90% of the total chips market. Indian chips market has grown at 10% p.a. over past 6 years. A large variety of SKUs, new and innovative tastes targeting traditional as well as global flavours, ease of availability across all shops, multi-pack sales and aggressive promotions through celebrities are some of the prime reasons for the success of the chips segment in India.

Exhibit 43. Indian Chips market: Organised segment constitutes 47% of the total market.



Source: Company, JM Financial

Exhibit 44. Organised Chips market is expected to grow at 10% CAGR



Source: Company, JM Financial

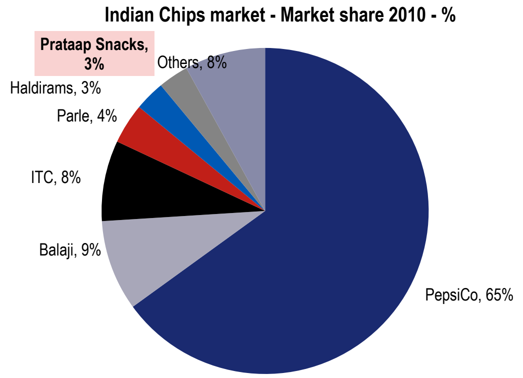
Indian organised chips market is pegged at INR65.5bn and constitutes 48% of the total chips market. North and West account for 63% of the total organized market while South and East constitute merely 37%. A large number of chips manufacturers are based in Madhya Pradesh, from where they serve Northern and Western markets, while some companies cater to Eastern market as well.

Potato chips are very popular in Northern and Western India, while South India sees a mixed demand for potato chips, tapioca chips and banana chips, with banana chips being particularly popular in Kerala. As taste is the major factor that determines success of a product, companies prefer to experiment with local tastes in addition to standard flavours. Organized Chips market is estimated to register c.10% CAGR over the next 5 years. Growth rates are expected to be relatively lower in this category as Chips is a relatively more matured market compared to the other sub-segments.

- **PepsiCo is the leader in the Chips market as well:** The market share of market leader PepisoCo ('Lays') has declined over the past few years with mid-sized companies such as

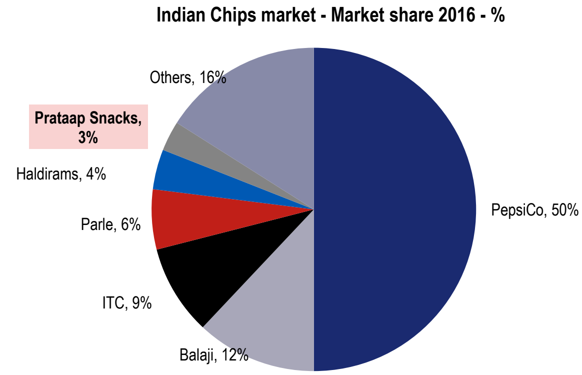
Balaji Wafers and Prataap Snacks chipping away market share from PepsiCo. Aggressive pricing and increasing availability across various types of outlets have aided growth in these companies.

Exhibit 45. Chips market: Market share 2010



Source: Company, JM Financial

Exhibit 46. Chips market: Market share 2016



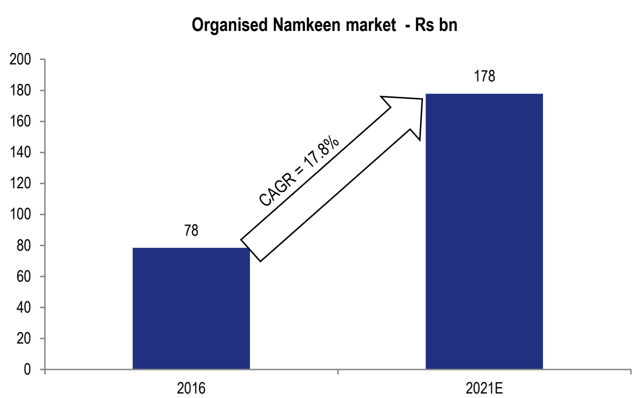
Source: Company, JM Financial

Namkeen

- **Expected to register highest growth rate amongst Snacks sub-segments at 17.8% CAGR:** Namkeen (traditional Indian savoury snacks) covers a broad range of products that are traditionally consumed in India and most of these products were hitherto cooked at home. However, on account of changes in lifestyles, consumers are now opting for convenience and are choosing to purchase these products instead. This has resulted in the Indian market experiencing high growth over the last few years. Moong Dal and Aloo Bhujia are the most popular products in the segments. Due to the varied eating habits across India, the preference for traditional snacks varies across the country. Namkeen market has grown at 14% CAGR over the past 6 years and it is pegged at c.INR224bn at present. Organised penetration is very low at 35% as most of these products can be prepared at home as well as by local condiment shops. North and West India are the major consumers of Namkeen accounting for 61% of organised market.

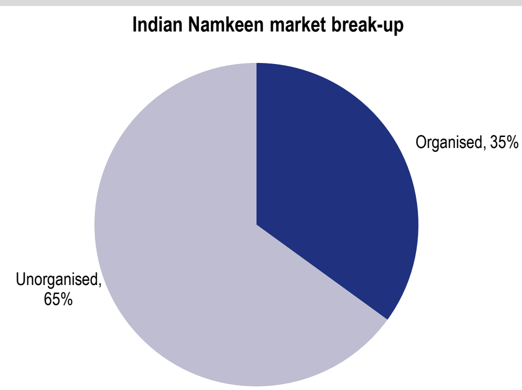
  Organised Namkeen market is expected to register 17.8% CAGR over next 5 years and would be the fastest growing sub-segment. Presence of huge number of unorganised players, attractive packaging and flexible price points are expected to fuel the growth of the Namkeen market.

Exhibit 47. Namkeen expected to be the fastest growing sub-segment in the Snacks space



Source: Company, JM Financial

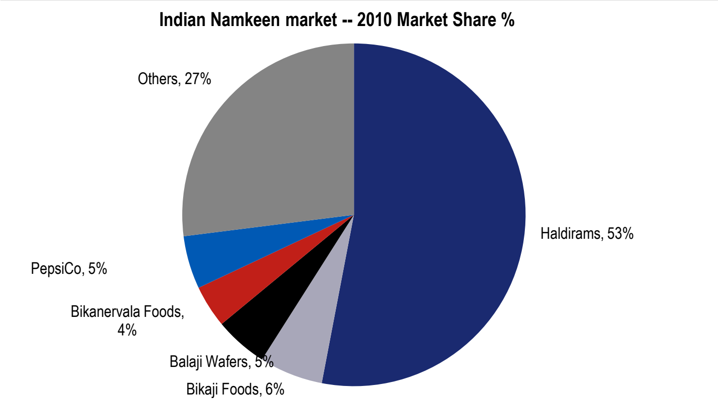
Exhibit 48. Unorganised segment accounts for 65% of the namkeen market



Source: Company, JM Financial

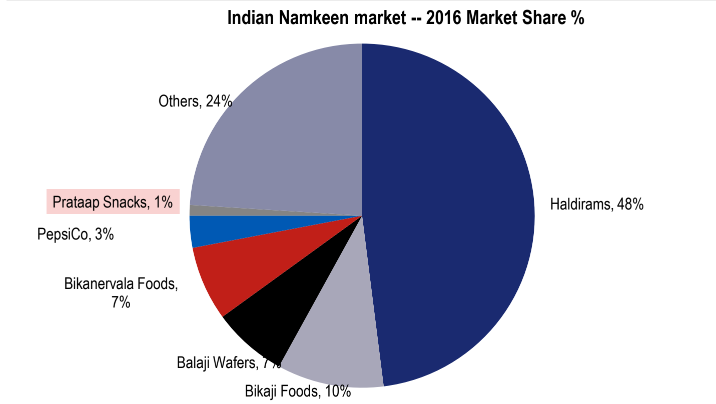
Haldirams is the undisputed market leader in Namkeen market with 48% market share and has always been associated with packaged traditional snacks and sweets in India and abroad. Bikaji Food, Balaji Wafers and Bikanervala Foods are other companies in the Namkeen market with market share of 10%, 7% and 6% respectively. Prataap Snacks has a strong presence in Eastern and Western markets. Since the traditional snacks in Southern India are quite different from the other regions, certain players such as MTR and Maiyas have a strong presence in that part of the country.

Exhibit 49. Namkeen market: Market share in 2010



Source: Company, JM Financial

Exhibit 50. Namkeen market: Market share in 2016



Source: Company, JM Financial

Business overview:

- 6th largest Indian snack food company: Prataap Snacks is the 6th largest snack-food company in India in terms of revenues in 2016 and is also amongst the fastest growing companies in the Indian organised snack market over 2010 to 2016. Prataap Snacks is present in 3 major savoury snacks categories in India; the products are sold under the 'Yellow Diamond' brand.

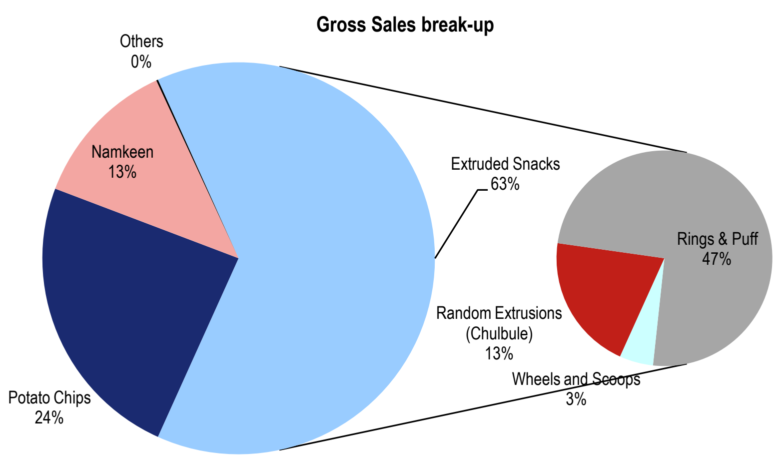
  In FY12, it acquired the manufacturing business of its group company, Prakash Snacks Private Limited, pursuant to a business transfer agreement dated September 28, 2011. Pursuant to such arrangement, the company acquired the 'Yellow Diamond' brand and the snack-foods business under such brand for an aggregate consideration of INR320mn as a going concern in an outright slump sale on an "as-is-where-is" basis. The purchase of the business included contracts, goodwill, licences and approvals, IP rights, immoveable and moveable assets rights relating to the business, all records pertaining to the business and certain agreed upon liabilities.

  The company has, over the years, leveraged its understanding of target markets and consumer segments, product innovation capabilities, extensive distribution network, strategically located manufacturing facilities, and has focused its marketing and promotional activities to establish and scale-up the 'Yellow Diamond' brand across India.

  The company's product portfolio includes three categories:

  - Extruded Snacks - c.63% of revenues: These are processed, reconstituted and shaped potato or cereal based snacks and may be flavoured or unflavoured. The Extruded Snacks portfolio includes two sub-categories: 1) Shaped Extruded Snacks - includes Puffs, Rings and Pellets products; and 2) Random Extruded Snacks (sold under the 'Chulbule' brand).
  - Chips - c.24% of revenues: Includes fried, sliced chips / crisps made from potatoes, hummus, lentils etc. It includes flavoured and unflavoured chips, and may be standard chips, thick-cut and / or crinkle-cut. Potato Chips under the 'Yellow Diamond' brand were introduced in FY05.
  - Namkeen - c.13% of revenues: These are a type of traditional savoury Indian snack which includes products such as moong dal, masala or fried nuts, sev and chaklis.

Exhibit 51. Prataap Snacks: Gross sales break-up



Source: Company, JM Financial

Exhibit 52. Prataap's product portfolio

Product Category	Launch year	Flavours	SKUs
		Extruded Snacks	
Chulbule 	FY06	Tangy Tomato, Teekha Tadka, Noodle Masala, Taza Tomato, Achari Chatka, Tango Mango and Cream 'N' Onion	INR5, INR10, and INR20
Rings 	FY12	Masala, Tomato, Mango Chutney, and Chilli Cheese	INR5 and INR15
Puffs 	FY10	Cocktail, Tomato, Pudina, and Punjabi Tadka	INR5
Wheels 	FY10	Chatpata Masala and Tomato Ketchup	INR 5
Scoops 	FY10	Masala and Tomato	INR5
		Potato Chips	
Potato Chips 	FY05	Plain Salted, Cream 'n' Onion, Tom-Chi, Nimbu Masala, Yummy Masala, Tangy Tomato, Tasty Punch, Plain Upvas, Black Pepper and Magic Masala	INR5, INR10, and INR20
		Namkeen	
Namkeen 	FY12	Moong Dal, Chana Dal, Chana Masala – Heeng Jeera flavour, All-in-One, Aloo Bhujia, Bhujia Sev, Punjabi Tadka, Ratlami Sev, Tasty Shing Bhujia, Mixture, Falahari Chivda – Meetha and sweet and salty flavours, Khatta Meetha, Banana Wafers –Black Pepper and Salted flavours, Cornflake Mixture, Bhel, Plain Sev Mamra, Garlic Sev Mamra, Masala Matar, Chana Choor and Peanuts – Classic and Salt and Pepper flavours.	INR5, INR10, INR30 and INR70

Source: Company, JM Financial

Exhibit 53. Prataap Snacks evolution timeline

Calendar Year	Particulars
2002	Incorporation of Prakash Snacks Private Limited.
2004	Set up a plant to manufacture potato chips in Indore.
2006	Installed a plant to manufacture Chulbule (random extruded snacks) in Indore.
2009	Incorporation of Prataap Snacks Pvt. Ltd.
2010	The plant at Indore for manufacturing extruded snacks received ISO 22000:2005 certification.
	Incorporation of wholly owned subsidiary Pure N Sure Food Bites Pvt. Ltd.
2011	Prataap Snacks, by way of slump sale, took over the business of Prakash Snacks
	Commissioned plants to manufacture Rings and Namkeen in Indore
	Acquired brand Yellow Diamond from Prakash Snacks
	Investment by Sequoia aggregating to INR620mn
2012	Setting-up of a new plant to manufacture Potato Chips in Indore.
	Investment by Sequoia aggregating to INR120mn
2013	Investment by Sequoia aggregating to INR300mn.
2014	Commissioned a plant to manufacture Rings, Chulbule and Pellets at Guwahati.
	Further INR250mn investment by Sequoia.
2015	Increased the capacity of Chulbule and Rings manufacturing plants in Indore
	Commissioned a new plant to manufacture rings at Guwahati.
2016	The plants at Indore for manufacturing potato chips and namkeen received ISO 22000:2005 certification.
	Conversion into a public limited company and change of name to Prataap Snacks Limited.

Source: Company, JM Financial

- **Prataap Snacks' diversified portfolio helps cater to wide-range of consumers segments:** Prataap Snacks seeks to differentiate from competitors through launch of new products, introducing new flavours targeted at addressing consumer taste, market trends and maximising value to consumers. Diversified product portfolio enables the company to cater to a wide range of taste preferences and consumer segments, including adults, youth and children - Extruded Snacks category are primarily targeted at the youth and children while Potato Chips and Namkeen category are for all consumer segments. This lowers the risk of volatility in revenues on shifts in consumer preferences and market trends. Its brand philosophy is based on delivering higher value to consumers, as reflected by the regular introduction of new flavours, relatively high grammage, and inclusion of promotional items such as toys to offer more value in products.
- **Pan-India distribution network supported by strategically located manufacturing facilities:** The company's wide spread and integrated sales and distribution network enables it to reach a wide range of consumers and ensure effective market penetration. As of March 31, 2017, its distribution network included 205 super stockists across 26 States and one Union Territory in India and approximately 3,400 distributors. Prataap Snacks owns and operates three manufacturing facilities - one located at Indore (Madhya Pradesh) and the other two located at Guwahati (Assam). These facilities have access to cost efficient transportation to major markets and help the company benefit from transportation cost efficiencies from reverse logistics arrangements. The company has also engaged two facilities on contract manufacturing basis, located at Bengaluru (Karnataka) and at

Kolkata (West Bengal). In FY17, revenue from traded goods contributed 2.83% of revenue from operations.

- Packaging material is the largest component in COGS: Prataap's raw material requirements include ingredients required for production of snack foods including oil, potatoes, corn, rice and gram as well as packaging and labelling materials. Various kinds of toys are also procured (as part of Rings packaging) from various suppliers.

  Packaging Material: Film accounts for the largest part of raw material costs and are used as packaging material. Snack foods are sold in film packaging and cardboard boxes are used for bulk shipments. Products are sourced from local suppliers. Packaging materials accounted for c.15.8% of revenuein FY17.

  Rings Toys: Toys are offered as part of the promotional campaign for Rings. The variety of toys to be included in the packaging is determined on the basis of festivals and promotional schemes undertaken at that point in time. Toys are generally sourced through local suppliers.

  Other key raw materials: Potatoes, oil and corn are the other key raw materials and are sourced domestically from local suppliers. Potatoes are sourced through short term or spot purchase arrangements at variable prices from Indore and nearby areas which are known for their quality potatoes and are stored in cold storage facilities leased by the company. Potatoes are also procured from Maharashtra and Gujarat largely for immediate consumption. Oil and corn are also purchased from local suppliers.

- Owns three manufacturing facilities with total annual capacity of 80,500 MT: As of the date of prospectus, Prataap owned and operated three manufacturing facilities in India - one at Indore (Madhya Pradesh), and two other facilities at Guwahati (Assam). The second facility at Guwahati started commercial operations from April 1, 2016. The aggregate estimated annual installed capacity for these owned and operated manufacturing facilities was 80,500 MT. In addition, it also engages two facilities on a contract manufacturing basis in Bengaluru (Karnataka) and Kolkata (West Bengal). The entire capacity of the Bengaluru facility is now exclusively dedicated towards the manufacture of Prataap's products with effect from August 1, 2016 while the Kolkata facility is non-exclusive. As of March 31, 2017, the estimated installed production capacity of the Bengaluru contract manufacturing facility was 2,760 MT.

- Innovative marketing initiatives have helped drive growth: The company intends to increase its marketing and advertising activities to further strengthen brand awareness and achieve higher recall for its brands, especially in semi-urban and rural markets. It has carried out several successful campaigns in the past like using "Chhota Bheem" (a popular Indian cartoon) and related characters on Rings packaging, using characters of "Ben 10", and "Roll No. 21", popular animated series amongst children, for promotion of its products on Cartoon Network etc. The company currently has a tie-up with Viacom 18 Media Private Limited, the entity that operates the popular children's entertainment channel 'Nickelodeon', to use the cartoon characters 'Motu Patlu' on its Rings packaging.

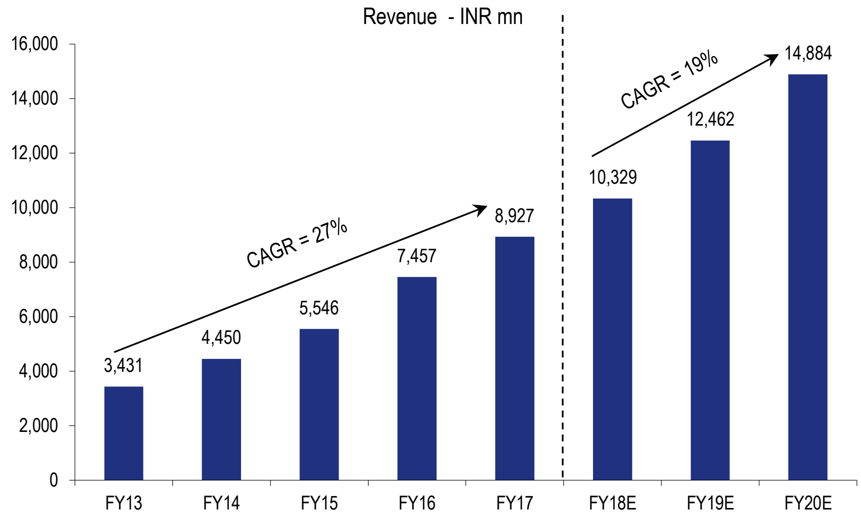
  Further, the company also sells Potato Chips, Chulbule (Extruded Snacks) and Namkeen, to both adults and youth with the 'Dildaar Hai Hum' campaign through television. It intends to use some part of the net proceeds for advertising and marketing activities to increase brand awareness of Yellow Diamond by engaging in direct promotional initiatives and advertising products through hoardings in key geographies as well as through television and radio advertisements.

Key Financials Summary

- **Revenue trends:** Prataap has delivered a net sales CAGR of 27% over FY13-17 aided by consistent innovation and scaling-up of extruded snacks segment. The extruded snacks segment which contributed 64% of revenues in FY17 achieved 37% revenue CAGR over the same period. The Namkeens segment also grew quite well at 41% CAGR though partly aided by a lower base. Potato chips segment lagged with a mere 10% CAGR.

  We are expecting the company to report a revenue CAGR of c.19% over FY17-20 – expecting FY18 revenue growth to be lower at 15.7% as the trajectory got impacted by GST implementation led disruption in the wholesale channel. We expect the company's revenue growth trajectory to pick-up in FY19 and FY20 to 20% CAGR but would still remain lower relative to 27% CAGR seen historically.

Exhibit 54. Revenue growth trends expected to remain healthy

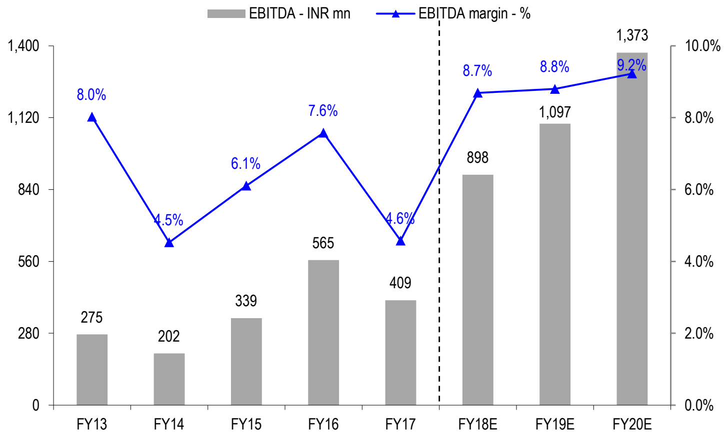


Source: Company, JM Financial

- **EBITDA trend: EBITDA has, though, clocked a mere 10.4% CAGR over FY13-17 and stood at INR409mn in FY17.** EBITDA margin contracted by 345bps to 4.6% over FY13-17 (EBITDA margin stood at 8% in FY13). EBITDA margin was impacted by high RM cost inflation and some constraints in capacity in Southern region leading to higher freight costs.

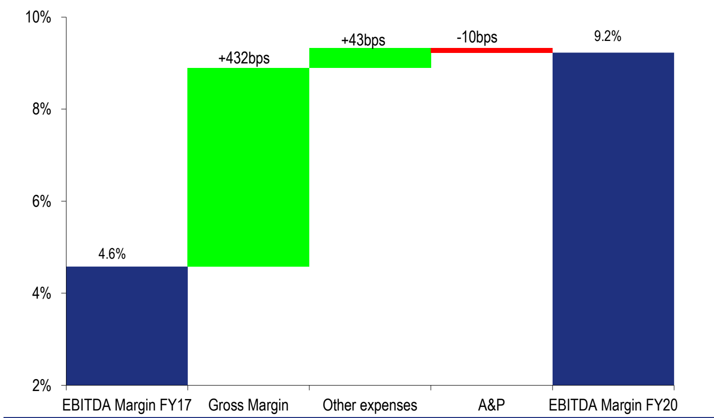
  We expect EBITDA to post a c.50% CAGR over FY17-20 aided by sharp margin expansion – EBITDA margin to expand by 465bps to 9.2%. This would be largely attributable to positive operating leverage.

Exhibit 55. Sharp rebound in EBITDA margin in FY18 expected …



Source: Company, JM Financial

Exhibit 56. …aided by pricing actions, more stable input-costs environment and level-playing field under the GST regime

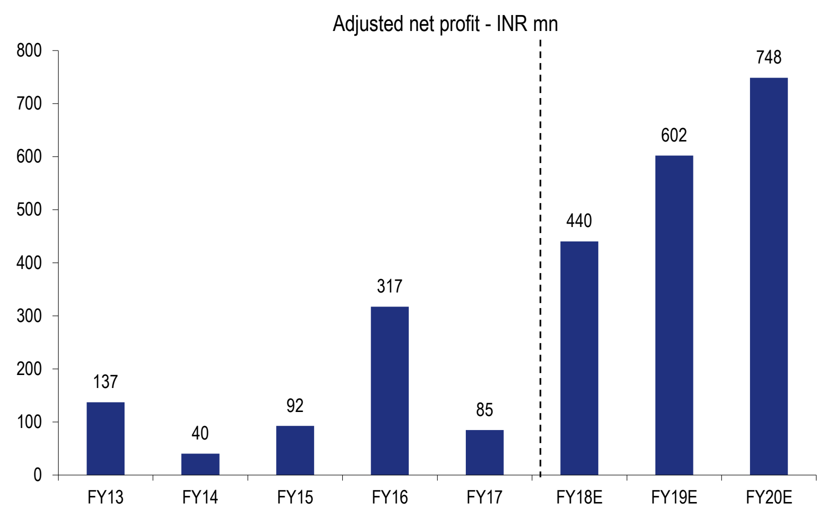


Source: Company, JM Financial

- **Adjusted net profit trend:** Adjusted profit has posted a 28.4% CAGR over FY12-17 from INR117mn in FY12 to INR317mn in FY17. However, net profit fell to a mere INR85mn in FY17 on sharp margin compression (as explained earlier).

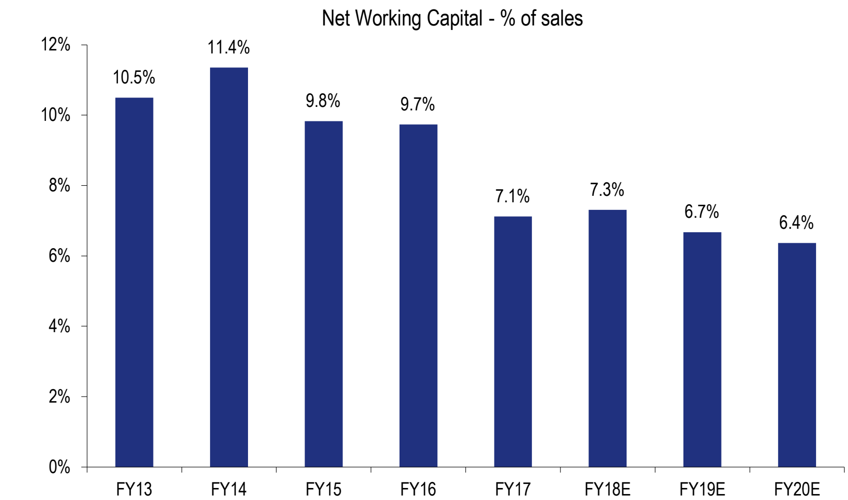
  As operating margin has now reached near double-digit levels in 1HFY18, we expect Prataap to post a profit CAGR of 107% over FY17-20 partially on lower base (net profit CAGR at 30% over FY18-20)

Exhibit 57. Adjusted net profit trends



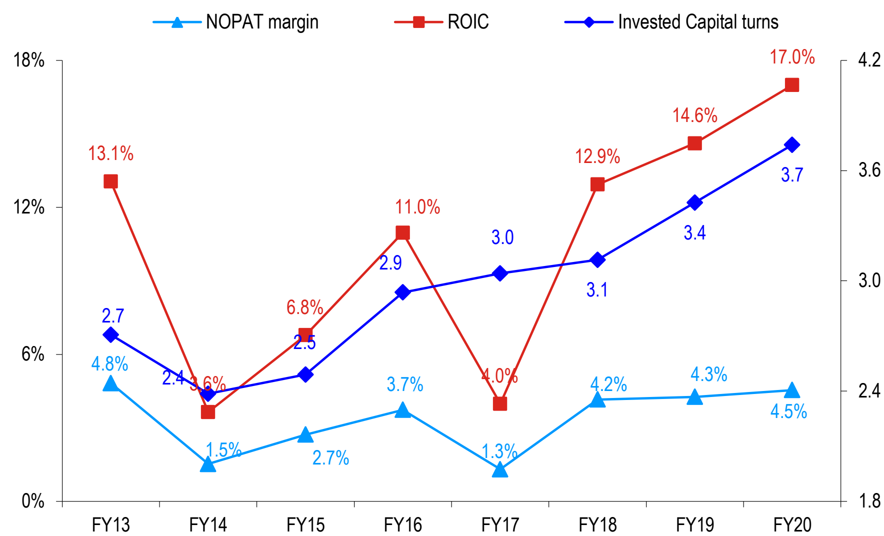
Source: Company, JM Financial

Exhibit 58. Prataap has consistently driven efficiencies in net working capital which we expect to continue in future as well.



Source: Company, JM Financial

Exhibit 59. Forecasting ROIC to improve to mid-teens level by FY20



Source: Company, JM Financial

Exhibit 60. Key PNL snapshot (INR mn)

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Net Sales	3,431	4,450	5,546	7,457	8,927	10,329	12,462	14,884
Other Operational Income	7	7	42	115	112	78	95	113
Net Revenue	**3,438**	**4,456**	**5,588**	**7,572**	**9,039**	**10,407**	**12,557**	**14,997**
YoY growth	99.1%	29.6%	25.4%	35.5%	19.4%	15.1%	20.7%	19.4%
COGS	2,408	3,284	4,040	5,222	6,366	6,955	8,384	9,972
Gross Profit	**1,030**	**1,172**	**1,548**	**2,350**	**2,673**	**3,452**	**4,173**	**5,025**
Gross margin % - excl op other income	29.8%	26.2%	27.2%	30.0%	28.7%	32.7%	32.7%	33.0%
bps change	-239 bps	-363 bps	97 bps	282 bps	-129 bps	398 bps	6 bps	28 bps
Staff Costs	55	89	137	187	253	331	399	476
% of sales	1.6%	2.0%	2.5%	2.5%	2.8%	3.2%	3.2%	3.2%
Advertisement & Promotions	26	36	122	303	368	426	520	629
% of sales	0.8%	0.8%	2.2%	4.1%	4.1%	4.1%	4.2%	4.2%
Other Expenditure	673	845	950	1,295	1,644	1,798	2,157	2,547
% of sales	19.6%	19.0%	17.1%	17.4%	18.4%	17.4%	17.3%	17.1%
EBITDA	**275**	**202**	**339**	**565**	**409**	**898**	**1,097**	**1,373**
YoY growth	51.5%	-26.8%	68.0%	66.9%	-27.7%	119.7%	22.2%	25.2%
% margin	8.0%	4.5%	6.1%	7.6%	4.6%	8.7%	8.8%	9.2%
bps change	-253 bps	-349 bps	158 bps	147 bps	-300 bps	411 bps	11 bps	43 bps
Depreciation	68	117	153	180	250	326	369	434
EBIT	**207**	**85**	**185**	**385**	**159**	**572**	**728**	**939**
YoY growth	34.6%	-59.0%	118.5%	108.0%	-58.8%	260.2%	27.3%	29.0%
Interest	36	47	63	59	45	40	0	0
Other Income	7	12	18	7	15	65	128	143
PBT before exceptional items	**178**	**50**	**140**	**334**	**129**	**597**	**856**	**1,082**
Exceptional Income / (Expense)	0	0	-10	-58	0	0	0	0
PBT after exceptional items	178	50	130	276	129	597	856	1,082
Tax	30	-4	31	2	30	157	254	333
Tax rate %	16.6%	-8.3%	23.8%	0.7%	23.5%	26.3%	29.7%	30.8%
Profit After Tax	**149**	**54**	**99**	**274**	**99**	**440**	**602**	**748**
YoY growth	17.8%	-63.7%	83.3%	176.4%	-63.9%	345.0%	36.8%	24.3%
Less: Preference Dividend	12	14	14	14	14	0	0	0
Net Profit	**137**	**40**	**85**	**260**	**85**	**440**	**602**	**748**
YoY growth	17.1%	-70.8%	112.5%	205.5%	-67.3%	418.4%	36.8%	24.3%
Profit adjusted for exceptional items	**137**	**40**	**92**	**317**	**85**	**440**	**602**	**748**
YoY growth	17.1%	-70.7%	130.8%	243.6%	-73.2%	418.4%	36.8%	24.3%

Source: Company, JM Financial

Key risks

- **A swift shift in consumer preferences towards healthier food products:** Prataap's portfolio of products consists of Indian and western snacks that are characterized by higher convenience and is customised to suit Indian palate. These snacks are, however, consumed in smaller quantities or completely avoided by people with increased health consciousness given the higher fat content in these food products. Increased instances of lifestyle diseases especially related to unhealthy food habits is also leading to increased health consciousness amongst consumers. Acceleration in this pace of shifting of consumers towards healthy products could adversely impact revenue growth for the industry. However, given the high presence of unorganised segment, there appears to be lower risk of such an eventuality happening in the near term. Furthermore, the snacks companies would, in our view, innovate and adapt their portfolio as consumer preferences change in order to stay relevant.
- **Incremental taxes being levied on packaged foods with higher fat content:** Indian regulatory authorities have, in recent times, displayed intentions of enhancing taxes on food products which are unhealthy and are witnessing increased consumption. Carbonated soft drinks is one such example which is taxed at higher rates relative to other packaged foods and beverages. While such a tax does not appear to be under contemplation at present, the possibility of higher taxes cannot ignored in future and could adversely impact revenues for this industry.
- **Sharp rise in competitive intensity:** Given Prataap's limited presence in categories like potato chips, random extruded snacks (Kurkure) excluding rings and Namkeens which are competing directly with the larger players like PepsiCo, ITC and Haldirams and its higher focus on value segment, it has not yet witnessed aggressive competition from the larger players (though, it has been facing tough competition from regional players like Balaji and unorganised segment). However, as the company gains scale, it will have to directly compete with the larger players and its quest for market share gains could impact the overall industry profitability, in our view. However, such an event has a lower probability in our view given the industry is already characterised by lower profitability and Prataap's focus remains on creating more innovative products rather than competing in the existing segments with incumbents.
- **Risks related to contamination of products or negative publicity with respect to products:** Prataap Snacks is subjected to normal risks relating to food and beverage industry including contamination of raw materials, consumer product liability claims, product tampering, labelling errors, product recalls etc. These issues could adversely impact the reputation and could result in high legal liabilities for the company.
- **Loss of business or potential adverse publicity from spurious or imitation products:** Within India, there also remains a risk of other companies passing off their products as products as products of Prataap Snacks and also includes risks of spurious or imitation products. These issues could take time to resolve and will have a negative impact on the company's revenues in the interim period. Low quality of spurious products could also adversely impact the reputation of the company.
- **Stringent food safety, consumer goods, health and safety laws and regulations:** Prataap Snacks' operations are subject to stringent health and safety laws as its products are meant for human consumption and are therefore subject to various industry specific regulations. There may also be additional regulatory requirements due to changes in governmental policies. Any changes in these laws could entail additional costs and liabilities related to compliance and could negatively impact profitability of the company.

Financial Tables (Consolidated)

Profit & Loss Statement					(INR mn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Sales	**7,457**	**8,927**	**10,329**	**12,462**	**14,884**
Sales Growth	34.4%	19.7%	15.7%	20.7%	19.4%
Other Operating Income	115	112	78	95	113
Total Revenue	**7,572**	**9,039**	**10,407**	**12,557**	**14,997**
Cost of Goods Sold/Op. Exp.	5,222	6,366	6,955	8,384	9,972
Personnel cost	187	253	331	399	476
Other expenses	1,598	2,012	2,224	2,678	3,176
EBITDA	**565**	**409**	**898**	**1,097**	**1,373**
EBITDA margin (%)	7.6%	4.6%	8.7%	8.8%	9.2%
EBITDA Growth (%)	66.9%	-27.7%	119.7%	22.2%	25.2%
Depn & Amort	180	250	326	369	434
EBIT	385	159	572	728	939
Other Income	7	15	65	128	143
Finance Cost	59	45	40	0	0
PBT before Excep & Forex	334	129	597	856	1,082
Excep & forex Inc/Loss(-)	-58	0	0	0	0
PBT	276	129	597	856	1,082
Taxes	2	30	157	254	333
Extraordinary Inc/Loss(-)	0	0	0	0	0
Assoc. Profit/Min. Int.(-)	-14	-14	0	0	0
Reported Net profit	260	85	440	602	748
Adjusted Net Profit	**317**	**85**	**440**	**602**	**748**
Net Margin (%)	4.3%	1.0%	4.3%	4.8%	5.0%
Diluted share capital (mn)	15.0	15.2	23.5	23.5	23.5
Diluted EPS (INR)	**21.1**	**5.6**	**18.8**	**25.7**	**31.9**
Diluted EPS Growth	238.1%	-73.6%	236.8%	36.8%	24.3%
Total Dividend + Tax	0	0	44	120	187
Dividend Per Share (Rs)	0.0	0.0	1.6	4.3	6.6

Source: Company, JM Financial

Balance Sheet					(INR mn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Shareholders' Fund	2,161	2,372	5,125	5,606	6,168
Share capital	3	19	117	117	117
Reserves & Surplus	2,158	2,353	5,007	5,489	6,050
Preference Share Capital	12	12	0	0	0
Minority Interest	0	0	0	0	0
Total Loans	544	804	0	0	0
Def. Tax Liab / Assets (-)	55	85	93	116	146
Total - Equity & Liab	**2,772**	**3,272**	**5,217**	**5,722**	**6,314**
Net Fixed Assets	1,985	2,526	2,717	2,972	3,207
Gross Fixed Assets	2,214	2,785	3,301	3,925	4,594
Intangible Assets	0	0	0	0	0
Less: Depn. & Amort.	532	777	1,102	1,471	1,905
Capital WIP	303	518	518	518	518
Investments	0	0	0	0	0
Current Assets	1,429	1,745	3,568	4,037	4,636
Inventories	685	789	877	1,024	1,183
Sundry Debtors	183	197	255	273	326
Cash & Bank Balances	61	111	1,745	1,918	2,158
Loans & Advances	482	575	613	740	884
Other Current Assets	18	74	78	82	86
Current Liab. & Prov.	642	999	1,068	1,287	1,530
Current Liabilities	630	979	1,042	1,256	1,493
Provisions & Others	12	20	26	31	37
Net Current Assets	786	746	2,500	2,750	3,106
Application of Funds	**2,771**	**3,272**	**5,217**	**5,722**	**6,314**

Source: Company, JM Financial

Cash Flow statement					(INR mn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Profit before Tax	334	129	597	856	1,082
Depn. & Amort.	180	250	326	369	434
Net Interest Exp. / Inc. (-)	52	29	-25	-128	-143
Inc (-) / Dec in WCap.	-60	50	-119	-77	-116
Others	0	14	0	0	0
Taxes Paid	-72	-46	-149	-231	-303
Operating Cash Flow	**433**	**426**	**629**	**788**	**954**
Capex	-463	-586	-516	-623	-670
Free Cash Flow	-30	-160	113	165	285
-Inc/dec in investments	-6	-10	0	0	0
Others	3	-102	65	128	143
Investing Cash Flow	**-466**	**-698**	**-451**	**-495**	**-527**
Inc/(dec) in capital	0	112	2,345	0	0
Dividend+Tax Thereon	0	0	-44	-120	-187
Inc/dec in loans	93	261	-804	0	0
Others	-42	-50	-40	0	0
Financing Cash Flow	**51**	**323**	**1,457**	**-120**	**-187**
Inc / Dec (-) in Cash	18	51	1,634	173	240
Opening cash balance	43	61	111	1,745	1,918
Closing cash balance	61	111	1,745	1,918	2,158

Source: Company, JM Financial

Dupont Analysis					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net Margin	4.3%	1.0%	4.3%	4.8%	5.0%
Asset Turnover (x)	2.9	3.0	2.4	2.3	2.5
Leverage Factor (x)	1.3	1.3	1.1	1.0	1.0
RoE	15.7%	3.7%	11.7%	11.2%	12.7%

Key Ratios					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
BV/Share (INR)	143.8	155.6	218.5	239.0	263.0
ROIC (%)	15.5%	4.3%	13.1%	14.5%	16.9%
ROE (%)	15.7%	3.7%	11.7%	11.2%	12.7%
Net Debt-equity ratio (x)	0.2	0.3	-0.3	-0.3	-0.3
PER	55.3	209.6	62.2	45.5	36.6
PBV	8.1	7.5	5.3	4.9	4.4
EV/EBITDA	31.9	45.3	28.6	23.2	18.4
EV/Net Sales	2.4	2.1	2.5	2.0	1.7
Debtor days	9	8	9	8	8
Inventory days	34	32	31	30	29
Creditor days	33	41	40	40	40

Source: Company, JM Financial

APPENDIX I

JM Financial Institutional Securities Limited

Corporate Identity Number: U65192MH1995PLC092522
Member of BSE Ltd. and National Stock Exchange of India Ltd. and Metropolitan Stock Exchange of India Ltd.
SEBI Registration Nos.: BSE - INZ010012532, NSE - INZ230012536 and MSEI - INZ260012539, Research Analyst – INH000000610
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Definition of ratings	
Rating	Meaning
Buy	Total expected returns of more than 15%. Total expected return includes dividend yields.
Hold	Price expected to move in the range of 10% downside to 15% upside from the current market price.
Sell	Price expected to move downwards by more than 10%

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