

DFM Foods Ltd.

Strong recovery in sales & gross margins

DFM Foods Ltd (DFM) reported sales grew by ~12% YoY in Q2FY23 to Rs. 1,650 mn with a sharp improvement in gross margins. DFM gained ~20 bps QoQ share in the extruded market in its focus geographies and ~20 bps on pan India level supported by significant investments in brand building, go-to-market initiatives, talent augmentation and technology investments. Company's gross margins in Q2FY23 (excluding portfolio expansion) improved to ~40.2% vs ~38.8% YoY & ~36.1% QoQ, due softening of commodity prices and ongoing company wide cost management programme. We expect gross margins to improve further going forward with the full benefit from softening of raw material prices and sales growth to improve with the increased contribution from new launches and also growth in the existing products. Company has completed implementation of an integrated ERP that covers the business end to end, including procurement, production, quality & sales. Management's focus on multi-product, multi-channel and multi-geography approach is expected to drive sustainable and profitable growth ahead. We remain positive on the company's mid to long-term potential but with the increase in the stock price post the delisting announcement made by the company, we revise our rating to "Accumulate" from "Buy".

H1FY23 Earnings Key Highlights

- In H1FY23 company reported ~20.7% YoY increase in sales on the back of post covid recovery, aided by sales & marketing investment.
- Gross margin in H1FY23 declined by ~111 bps YoY to ~36.5%. Gross margins in Q1FY23 got impacted due to a sharp inflation in almost all the key raw materials used by the company. However now with the softening of raw material prices margins have improved in Q2FY23.
- Company reported EBITDA loss of ~Rs. 255 mn compared to profit of Rs. 12 mn YoY. EBITDA margins were impacted mainly due to lower gross margins, increase in employee expenditure & higher advertisement & marketing spends.
- In H1FY23 advertising and marketing spends increased to ~9.6% vs ~7.2% YoY of sales.
- Investment in Go to market expansion in H1FY23 was at 3.3% of net sales vs 2.4% YoY.
- Company reported a PAT loss of ~Rs. 264 mn vs. ~Rs 49 mn YoY.
- Net working capital continued to be negative. Company incurred capex of ~Rs. 42 mn vs ~Rs 181 mn YoY.

Outlook and Valuation:

DFM being a market leader in extruded snacks segment in the country possess huge headroom to grow which is visible in its focus on strengthening its current product portfolio in existing geographies, expansion into new geographies, investment in brand through increased advertising and visibility and building larger pack (Rs 10 & above) portfolio. **We have valued the stock at 2.5xSep'24e Sales (from earlier 30xFY24e EPS) to arrive at a target price of Rs.419, implying upside of ~13% based on the CMP. We thus revise our rating to "Accumulate" from "Buy" on the stock.**

Y/E March (Rs Mn)	Q2FY23	Q2FY22	YoY(%)	Q1FY23	QoQ(%)	Q2FY23E	Var. (%)
Net sales	1,650	1,471	12.1%	1,459	13.1%	1,707	-3%
COGS	1,016	922	10.2%	959	5.9%		
Gross Profit	634	549	15.4%	500	26.8%		
Gross Profit Margin	38.4%	37.3%	109 Bps	34.3%	415 Bps		
EBITDA	-101	-1		-144		1	
EBITDA Margin (%)	-6.1%	0.0%		-9.8%		0.1%	
Depreciation	37	38	-3.4%	35	4.5%		
Interest	21.3	20.2	5.4%	23	-7.4%		
Other income	11	18	-40.8%	10	7.1%		
PBT	-149	-41		-192			
Provision for tax	-38	-10		-48			
Tax rate (%)	-25.8%	-23.7%		-25.0%			
Reported PAT	-110	-31		-144		-34	
PAT Margin (%)	-6.7%	-2.1%		-9.9%		-2.0%	

Source: Company, SMIFS Institutional Research Estimates

Y/E March (Rs mn)	Revenue	YoY (%)	EBITDA	EBITDA (%)	Adj.PAT	YoY (%)	Adj.EPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY21	5,241	3.2%	556	10.6%	287	17.5%	5.7	17.7%	15.1%	53.5	27.0
FY22	5,545	5.8%	-171	-3.1%	-248	-	-4.9	-15.0%	-7.2%	-	-
FY23E	6,543	18.0%	59	0.9%	-79	-	-1.6	-5.3%	-0.6%	-	318.8
FY24E	7,851	20.0%	695	8.9%	394	-	7.8	24.5%	18.6%	47.4	26.6
FY25E	9,029	15.0%	989	11.0%	619	57.2%	12.3	30.6%	24.6%	30.1	18.2

Source: Company, SMIFS Institutional Research Estimates



Rating: Accumulate Upside: 13%
Current Price: 371 Target Price: 419

Earlier recommendation

Previous Rating: Buy
Previous Target Price: 283

Market data

Bloomberg: DFMF IN
52-week H/L (Rs): 390/187
Mcap (Rs bn/USD mn): 18.66/230.3
Shares outstanding (mn): 50.3
Free float: 26.30%
Avg. daily vol. 3mth (in '000): 167.32
Face Value (Rs): 2
Group: S&P BSE Smallcap
Source: Bloomberg, SMIFS Research

Shareholding pattern (%)

	Sep-22	Jun-22	Mar-22	Dec-21
Promoter	73.70	73.70	73.70	73.70
FII	0.82	0.37	0.36	0.32
DII	3.39	3.39	3.40	3.17
Public/Others	22.09	22.54	22.54	22.67

Promoters Pledging

% of o/s shares 0 0 0 0

Source: BSE

Price performance (%)

	1M	3M	12M	36M
BSE SmallCap	1.5	2.7	-0.9	117.3
DFM Foods	-0.4	22.7	21.1	50.6

*as on 16th Nov 2022; Source: AceEquity, SMIFS research

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Other Key Takeaways

- ✓ **Sales Growth:** Sales grew by ~12% YoY at Rs 1,650 mn on the back of post Covid recovery, aided by sales & marketing investments.
- ✓ **Gross Margins:** Reported gross margins for Q2FY23 was at ~38.4% vs ~37.3% YoY & 34.3% QoQ. Gross margins (excluding portfolio expansion) for Q2FY23 was at ~40.2% vs ~38.8% YoY & ~36.1% QoQ. Margins improved on both YoY & QoQ basis led by softening of commodity prices and on-going company wide cost management.
- ✓ **Brand Investment:** Continued investment in brand building through increased advertising and marketing spends increasing to ~9.9% vs ~9% YoY & ~9.2% QoQ of net sales. In H1FY23 it grew by ~61% YoY at ~Rs 297.6 mn.
- ✓ **Market share gain:** In Q2FY23 company gained ~20 bps market share in focus geographies & ~20 bps pan India supported by significant investments in brand building, go-to market initiatives, talent augmentation and technology investment.
- ✓ **Resilient product portfolio:** Company made rapid progress in building Fritts, Curls and Natkhat to diversify and strengthen the core portfolio while driving share gain and growth. Company also increased salience of higher price points.
- ✓ **Go-to-Market:** Weighted distribution of Natkhat, Curls and Fritts increased between ~120 bps and 770 bps YoY in its core geography.
- ✓ **Contribution of latest product launch:** In Q2FY23 portfolio mix of latest product launches was at ~21% vs ~11% YoY & ~19% QoQ of sales. Latest product launches include potato chips, higher price points pack of Rs 10 & above, new festive pack (launched at price points of Rs 65, Rs 100 and Rs 200), Bowls and Noodles.
- ✓ **New segment success:** Successfully scaling up Potato Chips in 3 states (UP, Uttarakhand and Haryana).
- ✓ **Go-to-Market:** Increased investment in go to market expansion at ~3.3% vs ~2.4% YoY & ~3.4% QoQ of net sales.
- ✓ **Negative working capital continues:** Company continued to operate on a negative working capital cycle.

Update on Delisting of equity shares of the company

Company has got approval from shareholders through postal ballot on Oct 1st, 2022 for delisting of equity shares of the company from NSE and BSE. Now the company is in process of getting necessary approvals for voluntary delisting of equity shares from both the stock exchanges i.e NSE and BSE. Post the receipt of approvals from both the stock exchanges a detailed public announcement will be made in the newspapers and letter of offer will be dispatched to the public shareholders.

Outlook and Valuation

- ✓ Management has been continuously working towards scaling up of business through investments in various advertisements and marketing strategies which continued in H1FY23. ***Company's growth outperformed the industry growth which led to market share gains in both focus geographies as well as on a pan India level.*** Investments towards brand building led by higher advertising & marketing spends are impacting margins of the company in the short term but ***we believe these should benefit the company in the medium to long term.*** The recent ***reduction in prices of some of the raw materials*** should have positive impact on the margins in the upcoming quarters.
- ✓ Company's continuous efforts to diversify its product portfolio with new launches and increase salience of products with price points of Rs 10 & above ***should help the company to achieve profitable growth going forward.*** DFM's major revenue use to come from Rs. 5 Sku but now company has upgraded its presence to higher-price points like Rs. 10, 20, 25 segment which expanded its reach to diverse age groups.
- ✓ DFM's healthy balance sheet, negative working capital, management's strong vision would help in gaining high growth & market share in the packaged snacks category in India.
- ✓ ***We have valued the stock at 2.5xSep'24 Sales (from earlier 30xFY24e EPS) to arrive at a target price of Rs 419, implying upside of ~13% based on the CMP over the next 9-12 months.*** We thus revise our rating to "Accumulate" from 'Buy' on the stock.

Key risks: 1. Competition from organized & unorganized players. 2. Geographical concentration. 3. Volatility in raw material prices.

Quarterly financials, operating metrics and key performance indicators

Fig 2: Quarterly Financials

Y/E March(Rs mn)	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23
Net Sales	1,354	1,325	1,105	1,471	1,553	1,416	1,459	1,650
COGS	802	781	686	922	988	893	959	1,016
Advertisement	56	94	51	134	115	199	134	164
Employee Costs	126	137	134	142	167	159	184	205
Other Expenditure	205	248	221	274	309	320	326	366
EBITDA	165	65	12	-1	-26	-156	-144	-101
Depreciation	32	38	39	38	33	34	35	37
Interest	25	26	27	20	21	21	23	21
Other Income	19	12	32	18	14	14	10	11
PBT	128	14	-22	-41	-67	-197	-192	-149
Tax	33	5	-5	-10	-16	-49	-48	-38
Tax rate (%)	25.8%	34.3%	-22.1%	-23.7%	-24.1%	-24.8%	-25.0%	-25.8%
Reported PAT	95	9	-17	-31	-51	-148	-144	-110
Extraordinary Items	-	-	-	-	-	-	-	-
Share of profit/ (loss) in JV	-	-	-	-	-	-	-	-
Adjusted PAT	95	9	-17	-31	-51	-148	-144	-110
YoY Growth (%)								
Revenue	1%	21%	-4%	4%	15%	7%	32%	12%
EBITDA	126%	209%	-92%	-	-	-	-	-
Adj. PAT	192%	-	-	-	-	-	-	-
QoQ Growth (%)								
Revenue	-4%	-2%	-17%	33%	6%	-9%	3%	13%
EBITDA	-25%	-61%	-81%	-	-	-	-	-
Adj. PAT	-34%	-91%	-	-	-	-	-	-
Margin (%)								
Gross margin (%)	40.8%	41.1%	37.9%	37.3%	36.4%	36.9%	34.3%	38.4%
Adv/revenue (%)	4.2%	7.1%	4.7%	9.1%	7.4%	14.1%	9.2%	9.9%
Employee cost/revenue (%)	9.3%	10.3%	12.2%	9.6%	10.7%	11.2%	12.6%	12.4%
Other expenses/revenue (%)	15.1%	18.7%	20.0%	18.6%	19.9%	22.6%	22.4%	22.2%
EBITDA margin (%)	12.2%	4.9%	1.1%	0.0%	-1.7%	-11.0%	-9.8%	-6.1%
PAT margin (%)	6.9%	1.2%	-1.5%	-2.1%	-3.2%	-10.5%	-9.9%	-6.7%

Source: Company, SMIFS Institutional Research Estimates

Financial Statements

Income Statement					
YE March (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net Sales	5,241	5,545	6,543	7,851	9,029
COGS	3,119	3,489	4,083	4,789	5,498
% of sales	59.5%	62.9%	62.4%	61.0%	60.9%
Employee Expenditure	543	602	762	824	903
% of sales	10.4%	10.9%	11.7%	10.5%	10.0%
Other Exp.	1023	1624	1639	1543	1639
% of sales	19.5%	29.3%	25.1%	19.7%	18.2%
EBITDA	556	-171	59	695	989
Other Income	69	77	64	55	54
Depreciation & Amortisation	132	144	142	143	153
Core PBT	494	-238	-19	607	890
Interest Expenses	108	89	86	78	59
PBT	386	-327	-105	529	831
Tax	99	-80	-27	135	212
Tax Rate (%)	25.6%	-24.3%	-25.5%	25.5%	25.5%
Reported PAT	287	-248	-79	394	619
Exceptional Items	0	0	0	0	0
Minority Interest	0	0	0	0	0
Adjusted PAT	287	-248	-79	394	619

Source: Company, SMIFS Institutional Research Estimates

Key Ratios					
YE March (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Growth ratios (%)					
Net sales	3.2%	5.8%	18.0%	20.0%	15.0%
EBITDA	33.4%	-130.7%	-	-	42.3%
Adj. PAT	17.5%	-186.3%	-	-	57.2%
Margin Ratio (%)					
Gross Profit	40.5%	37.1%	37.6%	39.0%	39.1%
EBITDA Margin	10.6%	-3.1%	0.9%	8.9%	11.0%
EBIT Margin	9.4%	-4.3%	-0.3%	7.7%	9.9%
Core PBT Margin	6.0%	-7.3%	-2.6%	6.0%	8.6%
Adj PAT Margin	5.5%	-4.5%	-1.2%	5.0%	6.9%
Return Ratio (%)					
ROE	17.7%	-15.0%	-5.3%	24.5%	30.6%
ROCE	15.1%	-7.2%	-0.6%	18.6%	24.6%
Turnover Ratio days (days)					
Gross Block Turnover (x)	2.6	2.6	2.8	3.0	3.1
Inventory Period	31	34	31	30	30
Debtors Period	3	4	4	4	4
Creditors	65	82	70	65	65
Cash Conversion Cycle	-31	-44	-35	-31	-31
Solvency Ratio (%)					
Debt-equity (x)	0.4	0.6	0.6	0.4	0.3
Net Debt-equity (x)	-0.1	0.2	0.2	0.2	0.0
Gross Debt/EBITDA	1.4	-5.3	14.7	1.1	0.6
Current Ratio	1.7	1.0	0.9	1.1	1.3
Interest coverage ratio (%)	4.6	-2.7	-0.2	7.7	15.1
Per share (Rs)					
EPS (Reported)	5.7	-4.9	-1.6	7.8	12.3
Adj EPS	5.7	-4.9	-1.6	7.8	12.3
CEPS	8.3	-2.1	1.3	10.7	15.3
Book value	35.4	30.4	28.8	35.2	45.3
Dividend					
DPS (Rs)	1.0	0.0	0.0	1.2	1.8
Dividend Payout (%)	17.5%	-	0.0%	15.0%	15.0%
Dividend Yield (%)	0.3%	0.0%	0.0%	0.3%	0.5%
Valuation					
P/E	53.5	-	-	47.4	30.1
P/BV	8.6	10.8	12.9	10.5	8.2
EV/EBITDA	27.0	-	318.8	26.6	18.2
EV/Sales	2.9	3.0	2.9	2.4	2.0
Adj M.Cap/Core PBT	45.0	-	-	37.5	22.4
Adj M.Cap/AOCF	50.6	-	276.5	33.3	20.5

Source: Company, SMIFS Institutional Research Estimates

Balance Sheet					
YE March (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Sources of funds					
Capital	101	101	101	101	101
Reserves & Surplus	1680	1427	1348	1671	2179
Shareholders' Funds	1781	1527	1449	1772	2279
Total Debt	796	914	864	764	574
Other Non-Current Liabilities	649	342	355	363	372
Total Liabilities	3,226	2,784	2,668	2,899	3,226
Application of funds					
Net Block	1,615	1,617	1,754	2,021	2,068
Capital WIP	183	338	210	0	0
Non-current Asset	727	558	577	600	623
Investments	202	215	215	515	715
Inventories	265	325	347	394	452
Sundry Debtors	40	65	72	86	99
Other Current Assets	111	102	108	118	135
Cash & Bank Balances	888	675	539	401	547
Other Financial Assets	12	12	13	16	18
Total Current Assets	1,518	1,394	1,294	1,530	1,966
Sundry Creditors	556	784	783	853	979
Other Current Liabilities	261	339	384	398	452
Total Current Liabilities	817	1,123	1,167	1,251	1,431
Net Current Assets	701	270	127	279	535
Total Assets	3,226	2,784	2,668	2,899	3,226

Source: Company, SMIFS Institutional Research Estimates

Cash Flow					
YE March (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Operating profit before WC changes	596	-132	123	750	1,043
Net change in working capital	-107	175	1	-4	75
Income Tax Paid	-100	-6	27	-135	-212
Cash flow from operating activities (a)	389	38	151	611	906
Adjusted OCF	281	-51	65	533	847
Capital expenditure	-97	-245	-150	-200	-200
Adjusted Free Cash Flow	184	-296	-85	333	647
Cash flow from investing activities (b)	-244	9	50	-350	-400
Debt issuance (repayment)	-122	110	-50	-100	-190
Interest & lease expenses	-83	-65	-86	-78	-59
Dividend Paid	-1	-51	0	-71	-111
Other financial activities	-18	-37	0	0	0
Cash flow from financing activities (c)	-224	-43	-136	-249	-360
Net change in cash (a+b+c)	-79	3	65	12	146

Source: Company, SMIFS Institutional Research Estimates

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