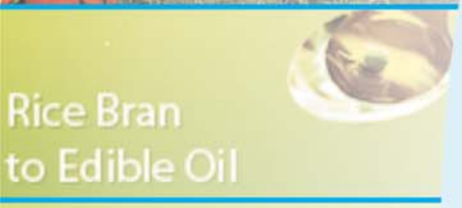
Batlivala & Karani

B&K SECURITIES
WE UNDERSTAND MONEY

SECTOR REPORT

5th March 2007



Indian Rice Industry

"Greener on the other side"

- We expect the rice sector to grow at an increasing momentum, as food processing is gradually gaining industry status in India. This change is driven by dominance of agriculture in Indian economy which produces 22% of the total world's rice production. The continuing improvement in logistics, development in retail and increase in the per capita income would further support the growth.
- As the sector gets more transparent margins will be under pressure which remains our biggest concern.
- The international vagaries would affect the demand-supply situation in the industry, as rice accounts for 13% of total agricultural exports from India, consisting of 22% basmati and 78% non-basmati rice.
- Indian rice industry is largely fragmented and hence suffers from inefficient production processes, as these players lack latest techniques and expensive machines required for rice processing. The fact that there has been no set precedence of increase in margins is yet another area of concern.
- Due to lack of transparency with respect to management of rice trade and rice being a commodity, the valuation of the same cannot be expected to exceed that of other commodity players.

Companies

	Recom.	CMP	Target Price	EPS (Rs.)				EPS CAGR (%)	PER (x)			
Initiating Coverage		(Rs.)	(Rs.)	FY06	FY07E	FY08E	FY09E	FY06-09E	FY06	FY07E	FY08E	FY09E
KRBL	MP	125	154	15.2	23.7	30.7	36.5	33.8	8.2	5.3	4.1	3.4
Kohinoor Foods	MP	69	66	10.6	13.2	11.0	12.8	6.3	6.5	5.0	6.3	5.4
REI Agro	Sell	193	145	17.0	15.5	17.0	21.0	7.3	11.4	12.5	11.3	9.2
Not Rated				FY04	FY05	FY06	FY07*	FY04-07*	FY04	FY05	FY06	FY07*
LT Overseas	NR	44	NA	7.6	6.9	6.7	20.3	38.7	5.7	6.4	6.6	2.2
Lakshmi Energy	NR	161	NA	1.9	3.4	7.7	16.0	103.4	76.7	41.2	18.5	10.1

*Annualised

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Investment arguments

Agriculture is one of the most important economic sectors of India. It contributes 19% to the GDP and nearly 65-70% of the population depends on agriculture for livelihood. India is the largest producer of sugarcane, milk, coconut, spices and cashews and the second largest producer of rice, wheat, pulses, fruits and vegetables. Rice is a low fat and high energy food.

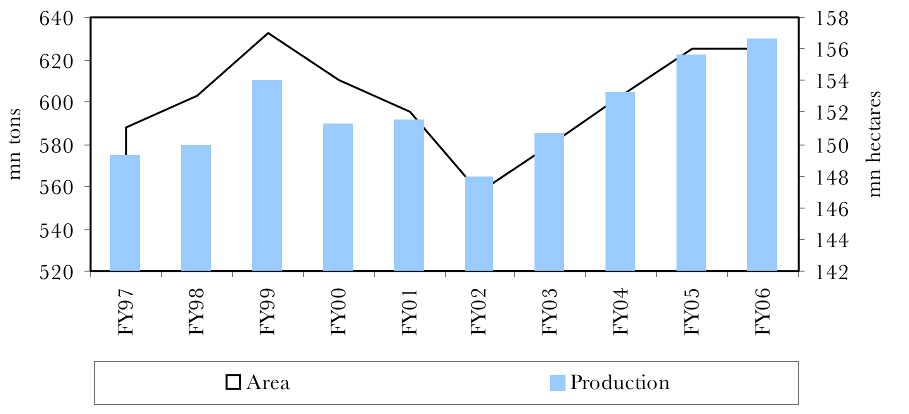
- **Rice – Staple food**

Dominance of rice as staple food for 50% of world's population

On the demand side, the global rice market is about US$ 120 bn (approx. Rs. 5.4 trillion) and is expected to grow annually at an average rate of 2-3% for the next 10 years (as per United States Department of Agriculture). Rice is cultivated in 113 countries and is ranked as the third principal staple food in the world after wheat and maize. It is consumed as staple food by half of the world's population and is considered to be the principal source of nutrition, calories as well as dietary needs.

On the supply side, the total production of rice globally is around 405 mn tonnes which is obtained by processing around 634 mn tonnes of paddy cultivated on more than 150 mn hectares of land.

Global paddy production and area



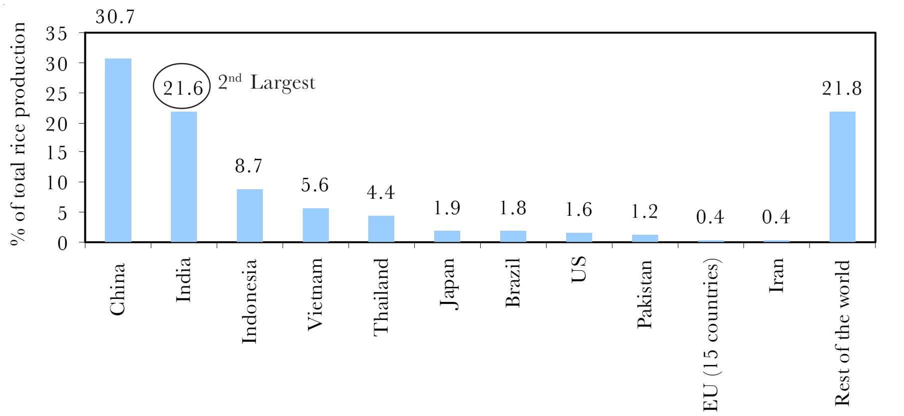
Source: Company (REI Agro)

- **India – Second largest producer of rice**

India producing 22% of world total rice

India is the second largest producer of rice in the world after China. India and China together account for about 50% of the world's rice growing area and 56% of rice production. Approximately 22% of the total world rice production is obtained from India. This is done by processing 132 mn tonnes of paddy and accounts for nearly 1/3rd of India's agriculture production.

World rice production (Average 1994-2004)



Source: Company

- **Scope for scalability**

Opportunities for organised business to grow

Both the basmati and non-basmati sectors present the organised players with tremendous opportunities since organised players have a low presence of 35% in the share of basmati and 5% in the share of non-basmati segment. The former is a high margin export oriented segment while the latter provides the alternative of value-added products derived while processing. The fragmented players lack the technology and expertise in procurement process required for these high end activities. Hence, the large players have the scope to take up the advantage and capture the market.

There are more than 139,000 rice processing mills in India processing about 132 mn tonnes of paddy. Out of this, a little over 25% (35,000) are classified as modernised rice mills.

Technology: Large organised players have the accessibility to infuse the latest technology for efficient and effective production. New machinery needs substantial capital, which typically large players can afford to invest. Latest technology reduces production cost per unit and thus helps in achieving economies of scale.

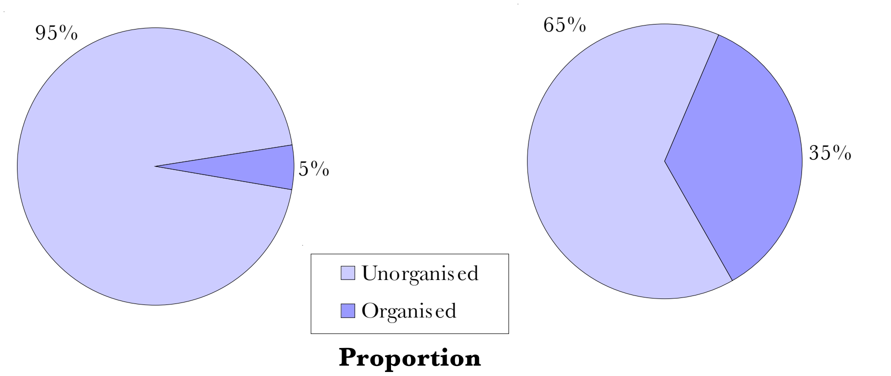
Comparative advantage with organised players

Quality: Small millers use old traditional methods to obtain rice by processing paddy. Processes like grading and sorting for size and colour, are not available to them. This affects the quality of rice produced from these mills.

Effective procurement: Quality is the most important characteristic for maintaining brand recognition in the market. This requires effective procurement process for paddy. Large players can procure the bulk volume through upfront payments to farmers and middlemen.

Break-up of rice industry

Non-basmati **Basmati**



Source: B&K Research

- **Growing organised Indian food chain**

Organised retail to boost the trade further

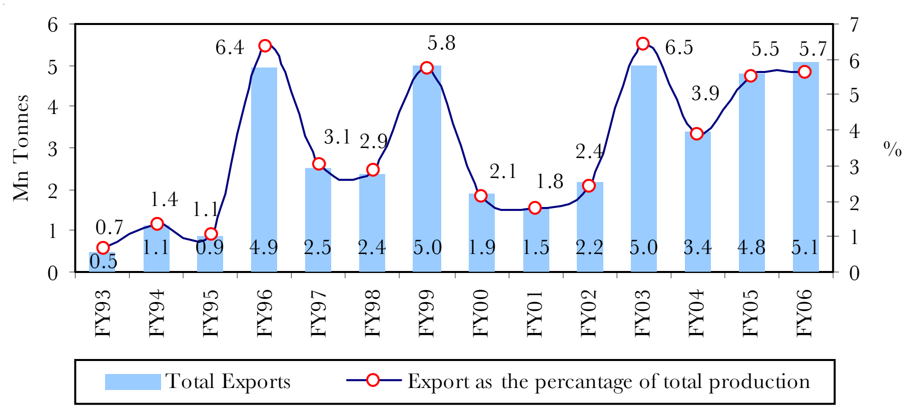
The Indian food chain lacks the adequate presence of large retailers and commodity processors at present. Now the scenario is changing with large corporate houses like ITC, Reliance and Bharti getting active in the Indian food chain following relaxation in regulatory and policy environment.

- **Export potential**

Acceptance of Indian rice in the global markets

Rice accounts for 13% of overall agricultural exports and approx 1.6% of total exports from India. India is exporting both basmati rice and non-basmati rice to various countries in the world. For the period FY00-06, exports have grown at a CAGR of 19.6%. We expect this growth rate to be maintained in exports.

Exports and Exports as the % of production



Source: All India Rice Exporters Association

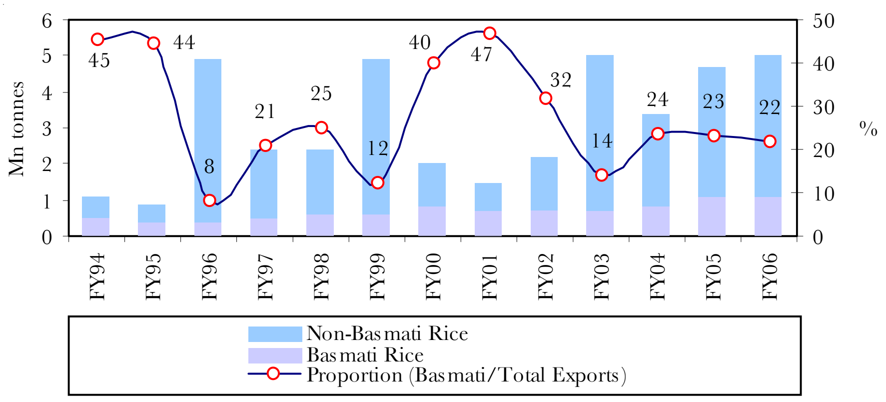
India – Largest producer and exporter of basmati rice

India is the largest producer and exporter of basmati rice. During FY06, 1.1 mn tonnes of basmati rice were exported for a total sum of Rs. 30.3 bn. Exports of basmati rice grew at a CAGR of 9.4% between FY00-06. India has a natural competitive edge considering that basmati can be grown only in India and Pakistan. In fact, Indian basmati rice is well recognised in the international market because of its quality. The government has formulated an aggressive export promotion policy to further develop the basmati rice by adoption of improved production technology and new high yield seeds.

Level of non-basmati exports → depends on production → depends on weather conditions

India is also exporting substantial quantity of non-basmati rice to various countries in the world. However, the export of non-basmati rice has been fluctuating year-to-year due to weather conditions affecting the production of non-basmati rice. The exports of non-basmati rice have grown at a CAGR of 21.7% for FY00-06.

Export (Basmati vs. Non-basmati)



Source: All India Rice Exporters Association

- **Demand projections**

Improving disposable income to further the demand

Global rice production is expected to double from 405 mn tonnes to 800 mn tonnes by 2030 to meet the increasing demand on account of continued growth in population and increasing disposable incomes of urban areas.

Investment concerns

- **Capital intensive**

High working capital required

While harvest and production of rice is seasonal, the sales are done throughout the year. This requires maintenance of high raw material and finished goods inventory. Therefore, there is need for large warehousing facilities. Companies require substantial working capital to make upfront cash payments at the mandis for bulk procurement and also for stocking/ageing the rice for enhancing the end product quality.

Turnover ratios (FY06)

Particulars	Working capital/Sales	Capital employed/Sales	Debtors turnover ratio	Inventory turnover ratio
REI Agro	1.1	1.5	3.9	1.6
KRBL	0.8	1.0	5.1	1.9
Kohinoor Foods	0.7	0.9	8.7	1.8

- **Raw material availability**

Seasonal availability of paddy

Agricultural commodities like rice are largely dependent on factors such as rain water availability, irrigational facilities, insect manifestation and change in crop patterns. These factors are beyond the control of companies.

Adverse changes in climatic conditions and above factors can lead to a shortage of produce resulting in lower profitability and even loss in some cases. Purchasing skill of individual companies may also have an impact on their individual purchases as a lot of renowned players are expanding their processing facilities.

- **Competition**

Low entry barrier

Due to easy entry at low capacity levels, various players from the unorganised market present stiff competition to the existing companies. An increasing numbers of players with cheap variants of rice take up the market at lower prices. Many large players are also expanding capacities which could lead to increase in competition resulting in competitive pricing.

- **Commodity business**

Rice still traded as commodity

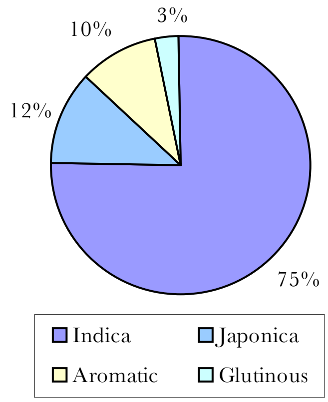
Processed rice is still an evolving industry in India and has a long way to go before achieving a full-fledged industry status. Rice is still sold in the market as a commodity with only a limited number of large players dealing in the organised trade. Hence, the market forces governing the product are similar to that in case of any other commodity business. The demand and supply play the most pivotal role in determining the dynamics of the business.

- **Low margin**

Margins dependent on level of value added

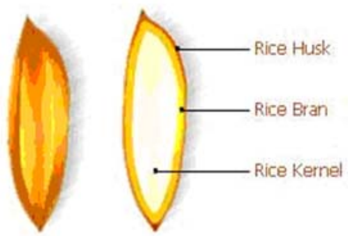
Rice industry has low EBITDA margins of 7-8% due to high material cost component at around 80% of revenue. But the major development in the form of branding of products as any other retail product is expected to improve the margins going forward. This will be largely on account of improved realisations.

Rice varieties



Source: Company (REI)

Rice grain



Source: Coagro

Rice industry

About rice

Rice is the common name for the type "Oryza" (grass). From an early history in the Asian areas rice has spread and is now grown on all continents except Antarctica. Rice is high in complex carbohydrates, contains almost no fat, is cholesterol free and is low in sodium. It is a good source of vitamins, minerals and protein.

Varieties of rice

Rice has nearly 140, 000 varieties grown worldwide, major being **Indica, Japonica, Aromatic and Glutinous**.

Treated rice

Rice is treated to impart new characteristics through various processes, whereby it gains added properties and qualities. These can be categorised as:

White rice or raw milled rice: It is also known as polished rice because most of the outer layers like husk and bran are removed from the kernel, through the milling process.

Brown rice: The only difference between these two varieties is the milling; milling removes both the husk and the bran layer of the kernel. In brown rice, only the husk is removed while the bran layer remains.

Through the milling process, brown rice becomes white rice. Because of the bran layer, brown rice contains more nutrients than white rice. In particular, brown rice is very high in fibre and vitamin B.

Parboiled rice or sella: Parboiled rice is raw rice treated through a process wherein the ingredients and aroma of the bran are forced into the rice. It undergoes a special process of boiling and steaming to capture the nutritive value of bran in the rice. Sella rice is generally consumed in the Middle East.

Global market (US$ 120 bn i.e. Rs. 5.4 trillion)

Demand-supply gap in global market

Particulars (Mn tonnes)	FY02	FY03	FY04	FY05	FY06
Production	398.4	380.8	391.4	401.1	405.3
Consumption	411.2	411.4	415.1	413.3	413.6

Source: LT Overseas (Prospectus)

Indian market (US$ 23 bn i.e. Rs. 1 trillion)

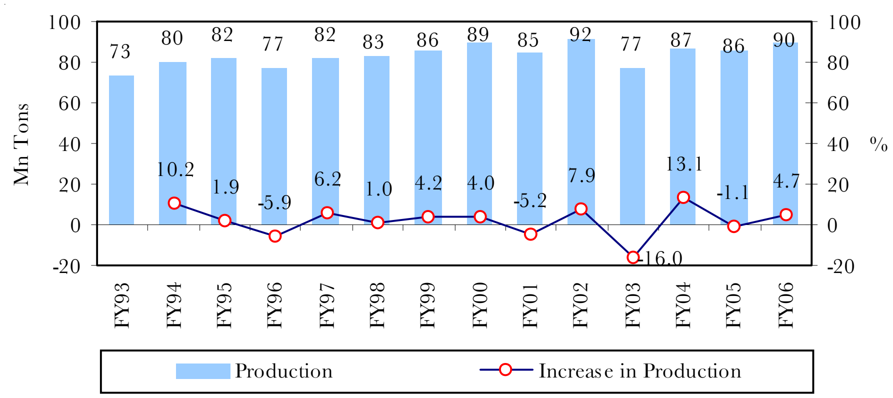
Rice production

Basmati: Non-basmati ratio of 5:95

The rice industry in India is broadly divided into two segments i.e. basmati rice and non-basmati rice with the total size of Rs. 1 trillion (Basmati rice – Rs. 45 bn, non-basmati rice – Rs. 955 bn). It is a complex industry with the presence of both the large scale as well as small scale production units.

Unorganised and regional players dominate the non-basmati rice processing segment. The Indian rice market is growing at the rate of 3-4% of which the basmati rice market is growing at a rate of 6% with branded basmati is growing at 15% p.a.

Rice production – India



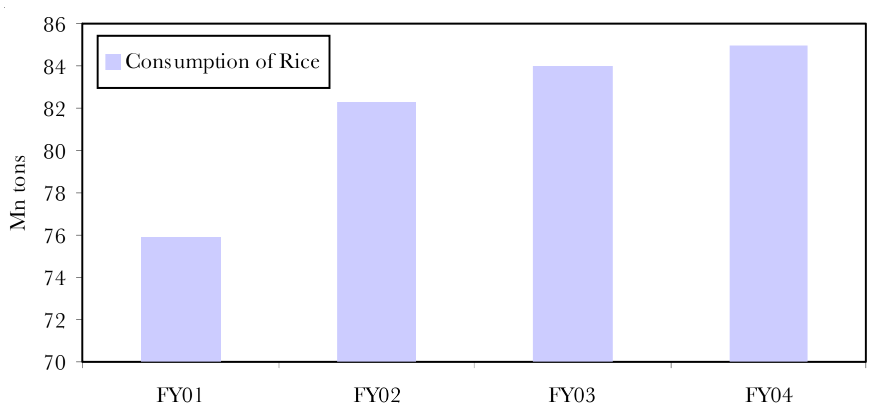
Source: All India Rice Exporters Association

Rice consumption

Supply-demand gap in India

Demand for food grain in low income countries like India is determined by two-basic factors viz. population growth and income level. There is good demand for both basmati and non-basmati rice. Consumption within India is almost 85 mn tonnes of the total rice processed.

Rice consumption – India



Source: Foreign agricultural services

Major paddy producing regions in India

In India, paddy is grown under varying altitude and climate conditions making it the perfect country to produce the same. In eastern and southern regions of the country, the mean temperature is found favourable for rice cultivation throughout the year. Hence, two crops of rice are grown in a year in these regions.

In northern and western parts of the country, where rainfall is high and winter temperature is fairly low, only one crop of rice is grown during the month from May to November.

The productivity of basmati paddy in India is around 1,400-2,100 kg/hectare against the yield of non-basmati paddy of 4,500-5,000 kg/hectares.

Basmati rice

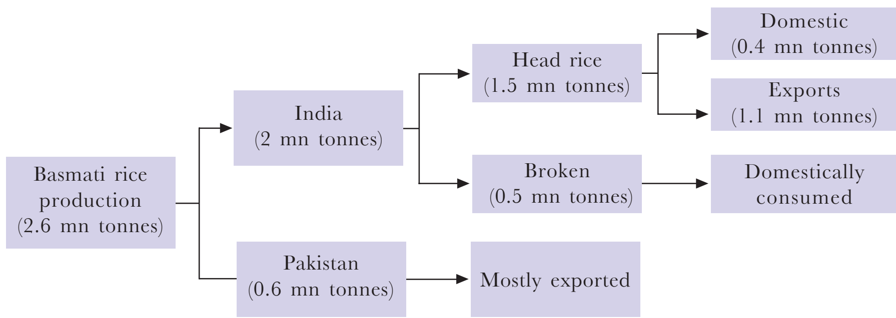
(Represented by KRBL, Kohinoor Foods, REI Agro and LT Overseas)

India and Pakistan – the only basmati producing nations

It is premium rice because of its super fine kerenals, exquitite aroma, sweet taste, silky texture, linear elongation with least breadth and swelling. It is also renowned for its flavour, when cooked. It is a lifestyle product and like all other lifestyle products, the purchase decision is highly influenced by a high degree of recall value in the minds of the consumers. The gap between demand and supply will continue to widen because of the growing offtake of the basmati rice resulting into huge opportunity for players in the basmati rice segment.

Basmati is patent-protected with a recent WTO ruling as a result of which only particular varieties grown in India and Pakistan can be marked as 'Basmati rice'.

Basmati rice industry



Source: B&K Research

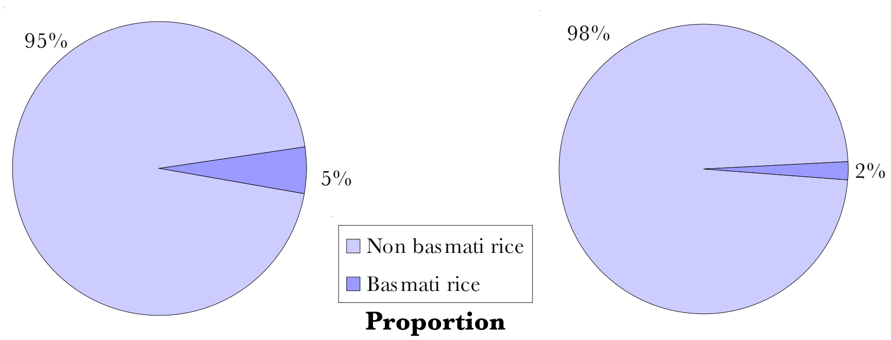
India catering to 75% of global basmati demand

Basmati rice commands business dynamics which are totally different from non-basmati rice. The basmati rice market worldwide is Rs. 60 bn which is being catered to by India (Rs. 45 bn) and Pakistan (Rs. 15 bn). In India, basmati rice market is estimated to be around Rs. 10 bn which consists of branded and unbranded basmati rice contributing 33% and 67%, respectively. Consumption of basmati rice has grown with a CAGR of 26% between FY01-04. Around 35% of processing is controlled by **organised players** and major sourcing of basmati paddy is done from Haryana, Uttar Pradesh, Punjab and Uttaranchal having a share of 50%, 25%, 18% and 7%, respectively.

Basmati rice composition – Domestic

In terms of value

In terms of quantum



Source: B&K Research

The principal aspects of the basmati rice business comprises of:

- **Paddy trade**

Basmati paddy traded through mandis

Paddy for basmati rice is sold directly through the government controlled mandis and do not depend on the Minimum Support Price (MSP) fixed by the government. Though the market is organised, it is fragmented into numerous traders and various agents. Basmati is a stable crop and it does not require much rainfall as compared to non-basmati. Prices of basmati paddy remain relatively stable and have not fluctuated substantially over the last decade. It enjoys a high export orientation and the government's export-import policy can affect the prices.

- **Distribution**

The distribution of basmati rice in India comprises of wholesaler, retailers and dealers. The movement of finished product begins from the plant to wholesalers who, in turn, sell to retailers and dealers. In the present scenario, there is a gradual shift towards branding basmati and selling it through large retail malls, concentrating little on the wholesalers. Basmati rice demand is expected to increase constantly across a number of countries, signifying immense potential for growth.

- **Exports**

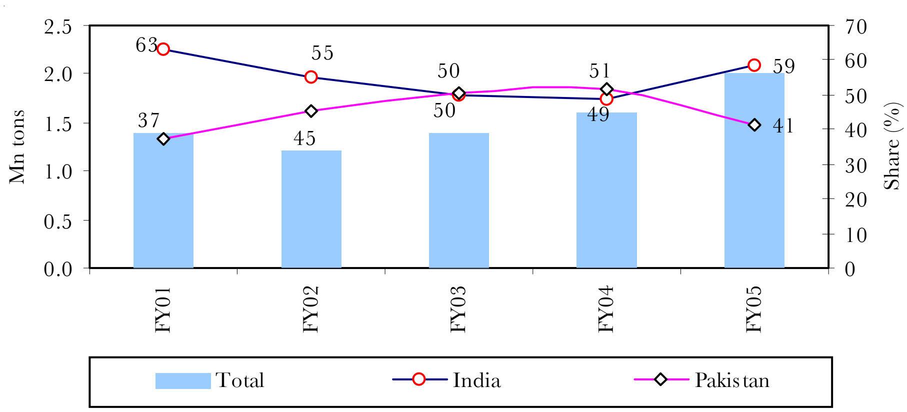
Growth expected at 6-8% p.a.

The government is aggressively promoting export of basmati rice as compared to non-basmati. In the non-basmati rice the government first uses it for self-sufficiency and discourages imports, through tariffs. The export market for basmati rice is expected to grow at 6-8% due to strong demand from Saudi Arabia and other Gulf countries where the customers have higher preference for basmati rice. Saudi Arabia is the major export market for Indian basmati rice with the total size of approximately Rs. 30 bn.

- **Natural competitive edge**

The foothills of the Himalayas provide the distinct natural conditions and the soil required for the cultivation of this scented rice. India and Pakistan are the only two countries in the world producing basmati rice. The trade in basmati rice over the last five years has been:

Total basmati and proportion of India and Pakistan



Source: APEDA

- **Ageing**

18-24 months of ageing required

Ageing is the period between paddy procurement and processing. The fragrance and cooking qualities of basmati rice are enhanced with ageing. In fact, for basmati rice to be marketable, the product needs to be aged for 18 to 24 months as fully matured basmati rice fetches a premium realisation. Due to the ageing, companies need to have high inventory levels making the basmati processing a highly capital-intensive business.

Paddy procurement period – September to March

The procurement season typically commences in September each year with inventory being piled up till February and March, which mark the end of the procurement season. Companies need to procure the paddy during this period only to get high quality paddy at the lowest cost. In case the procurement goes beyond the season, costs could go up by 15-20% with comparative lower quality of paddy. Thus, the companies need to maintain high stocks throughout the year which creates a demand for higher working capital.

SWOT analysis

Strengths

- Geographical constraint – limited supply.
- Inelastic demand – low substitutability.
- Branding – better price realisation.

Opportunities

- Greater assess to world market.
- High consumer's demand-income increasing and going for quality products.

SWOT

Weakness

- Little differentiation-low net margins.
- High working capital requirement due to ageing.

Threats

- Appreciation of rupee – reduces realisations on exports.
- Improved performance by Pakistan exports.
- Emergence of low cost synthetic substitutes.

Basmati supply chain (Paddy)

Agents – Key link between the farmer and the miller

Agro commodities business requires efficient procurement of raw material for maintaining the quality of the final product. Large organised players have the advantage because the company deals through 'Atriyas' (agent). Farmers bring their products to the "Mandis", whereby open mandis atriyas buy the requisite paddy from the mandis on behalf of the company. Thus, the atriyas play the significant role in the procurement of paddy and ultimately become advantage to the large players.

Different stages for supply chain

Farmer → Mandi → Atriyas

↓

Consumers ← Distributor/Retailers ← Millers

Non-basmati rice (Represented by LEAF and KRBL)

Regulations and policies

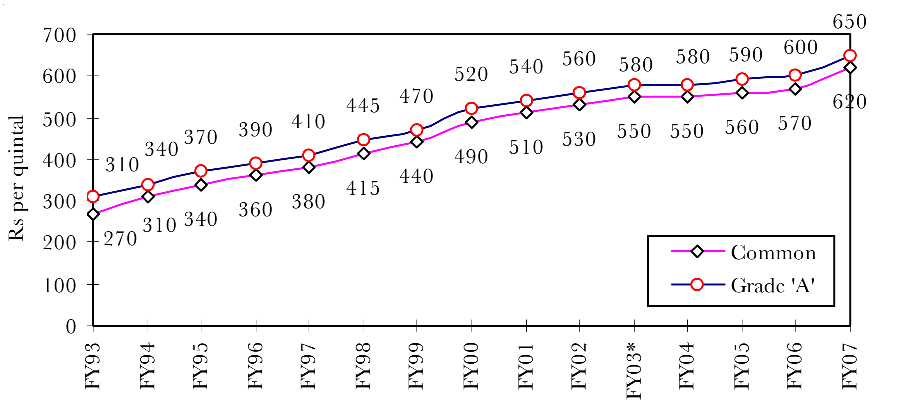
- **Minimum Support Price (MSP)**

FCI procures paddy on behalf of GoI

Price of paddy is controlled by the government, by way of Minimum Support Price (MSP). To encourage the farmers to increase production, Government of India (GoI) announces MSP well in advance i.e. around sowing time of the crop. This assurance of the price is modulated through 'agriculture produce markets' locally called 'Mandis'.

Food Corporation of India (FCI) is the organisation which undertakes procurement of paddy on behalf of GoI throughout the country. FCI purchases approx. 20-25% of the total rice production of the country both under levy from the rice mills and directly in the form of paddy from the farmers. The GoI classifies rice into two categories viz. common (length to breadth ratio less than 2.5) and Grade A (length to breadth ratio more than 2.5).

Paddy MSP



(*FY03 includes Rs. 20/quintal as DR (Drought Relief))

Source: Agricoop

Rice is procured by the government through statutory levy on rice millers and rice dealers. The percentage of levy on rice is fixed by the state governments with the approval of central government taking into account requirements for the central pool, domestic consumption and marketable surplus. GoI before commencement of every Kharif marketing season fixes levy rates on rice.

- **Central Issue Price (CIP)**

The population in India is divided in two categories of Above Poverty Line (APL) and Below Poverty Line (BPL). The government supplies the rice through Targeted Public Distribution System (TPDS). The CIP is fixed on the recommendation of Commission on Agriculture Costs and Prices (CACP) and are highly subsidised for making available food grains for families under BPL.

Indian rice processing peer group

Particular	KRBL	Kohinoor Foods	REI Agro	LT Overseas	Lakshmi Energy
Incorporated	1993	1989	1994	1990	1990
Areas of Operation	Basmati andnon-basmati	Basmati	Basmati	Basmati	Non-basmati
Total capacity(TPH)	**195.0**	**40.0**	**61.0**	**30.5**	**2,100.0***
Basmati	82.5	40.0	61.0	30.5	–
Non-basmati	112.5				2,100*
Brands					
Rankings	**As per AC Nielsen ORG-MARG (#)**				
(domestic market)	India Gate (21.8%)	Kohinoor (20.4%) Charminar (6.1%)		Daawat (17.5%)	
Premium	Doon	Kohinoor	Kasauti	Daawat	
Popular	India Gate	Trophy, Charminar, Falcon	Hungama, Mr. Miller, Real Magic	–	
Mass	Football, Aarti	–	Hasnraj, Mazaa	–	
Industry position	Largest manufacturing facilities	Ruling the market with the "Super brand" Kohinoor	Leadership in regards to turnover	–	Largest non-basmati players

* TPD

(#) Lal Killa (9.6) and Shri Lal Mahal (3.4) of Shri Lal Mahal Group and Amar Singh Chawalwala have also been ranked whereas REI Agro has not considered in the rankings.

Basic Information

Company	Basic Information				Year Ended	Financials											
	Rec.	Price	Market Cap			Net Sales (Rs mn)				Reported N/P (Rs mn)				Adjusted EPS (Rs)			
			(Rs mn)	(US$ mn)		FY06	FY07E	FY08E	FY09E	FY06	FY07E	FY08E	FY09E	FY06	FY07E	FY08E	FY09E
KRBL	M.P	125	3,033	69	Mar	7,248	9,331	11,507	12,879	325	577	747	887	15.2	23.7	30.7	36.5
Kohinoor Foods	M.P	69	1,356	31	Mar	5,399	6,011	6,712	7,515	208	270	327	377	10.6	13.8	11.0	12.8
REI Agro	Sell	193	8,652	196	Mar	9,440	9,315	10,713	12,476	660	694	809	997	17.0	15.5	17.0	21.0

Source: B&K Research

Valuations

Company	PER(x)			EV/Sales (x)			EV/EBITDA (x)		
	FY07E	FY08E	FY09E	FY07E	FY08E	FY09E	FY07E	FY08E	FY09E
KRBL	5.3	4.1	3.4	0.8	0.7	0.7	5.9	5.2	4.7
Kohinoor Foods	5	6.3	5.4	0.8	0.6	0.6	8.3	6.3	5.9
REI Agro	12.5	11.3	9.2	1.8	1.6	1.5	9.3	8.2	7.3

Companies

Share Data

Mkt. Cap.	Rs. 3 bn (US$ 69 mn)
Price	Rs. 125
Target Price	Rs. 154
BSE Sensex	12886
Reuters	KRBL.BO
Bloomberg	KRB IN
Daily Volume	US$ 1.2 mn (Rs. 53.1 mn)
52-week High/Low	Rs. 244/76
Issued Shares	24.3 mn

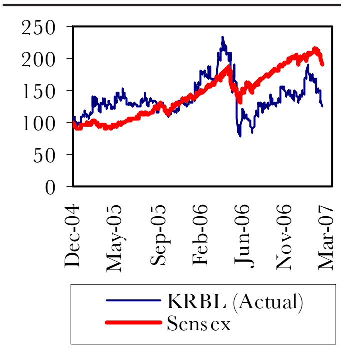
Valuation Ratios

Year to 31 Mar.	2008E	2009E
EPS (Rs.)	30.7	36.5
+/- (%)	29.6	18.7
PER (x)	4.1	3.4
PBV (x)	0.8	0.7
Dividend/Yield (%)	2.2	2.4
EV/Sales (x)	0.7	0.7
EV/EBITDA (x)	5.2	4.7

Shareholding Pattern (%)

Promoters	50
FIIs	1
MFs	4
ADRs/GDRs/Other Foreign	14
Public & Others	31

Relative Performance



KRBL

Market Performer

Bigger the Better

Khushi Ram and Behari Lal Ltd. (KRBL), was incorporated in 1993 as a trading company for agro products. It is the oldest rice miller and the largest exporter of basmati rice, in India as the promoter family has been in this business for over 115 years. The company's organic and inorganic growth plans have made it the largest processor of rice. We are initiating coverage with a Market Performer.

Year to March	FY06	FY07E	FY08E	FY09E	CAGR (%)
P&L Data (Rs. mn)					**FY06-09E**
Net Sales	7,248	9,331	11,507	12,879	21.1
Operating Profit	826	1,290	1,625	1,860	31.1
Net Profit	320	577	747	887	40.4
Margins (%)					
EBITDA	11.4	13.8	14.1	14.4	–
Net Profit	4.5	6.2	6.5	6.9	–
Balance Sheet (Rs. mn)					
Total Assets	7,547	9,027	10,664	12,174	17.3
Shareholders' Funds	2,664	3,171	3,842	4,645	20.4
Per Share Data (Rs.)					
EPS	15.2	23.7	30.7	36.5	33.8
CEPS	20.8	30.1	37.8	44.0	28.3
Dividend	2.0	3.0	4.0	5.0	35.7
Return (%)					
RoE	14.6	19.8	21.3	20.9	–
RoCE	12.7	15.2	16.4	16.4	–

- KRBL's acquisition of Dhuri plant from Oswal Agro and its subsequent expansion makes it the largest processor of rice with a total capacity of 195 TPH. This has helped the company in expanding its product portfolio to include non-basmati rice and value-added by-products (such as bran oil, furfural oil and power) in addition to basmati rice.
- KRBL has a volume share of 23% in totality and **'India Gate',** its major brand has a market share of 21.8%, in India (2005). (AC Nielsen ORG-MARG)
- The company's operating margins have improved with the concentration on high margin branded products as compared to private label products.
- At the current market price of Rs. 125, the stock is trading at 5.3x FY07E, 4.1x FY08E and 3.4x FY09E earnings. We believe the stock is fairly valued at these levels and hence at 5x FY08E EPS of Rs. 30.7 we give a target price of Rs. 154. We initiate coverage with a Market Performer rating.

Investment arguments

KRBL has expanded its business mix by foraying into non-basmati rice and by-products (value-added products like power and oil) which would be obtained from its Dhuri plant. It was previously deriving maximum of the revenues from the basmati rice by processing the same at its facility located in Ghaziabad. **'India Gate'** and **'Heritage'** are the two major brands of the company, contributing around 21% of the total revenues.

- **Largest processing facility – Dhuri plant**

  KRBL has invested a sum of Rs. 1.1 bn to acquire a plant in Dhuri. The capacity of the plant stands at 150 TPH, acquired from Oswal Agro Furane. The market value of the assets taken over by the company of the Dhuri plant, stood at around Rs. 2.8 bn. The production from the plant commenced in October 2006. This facility has actually helped the company to reduce its dependence of the trading activity with the improvement in the margins with the effective utilisation of raw material and its by-products.

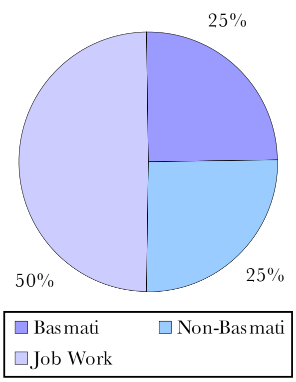
  The company has the largest capacity for rice processing after acquisition and expansion of its Dhuri plant. The new plant will be used for to produce the following:

  1. Basmati rice – 25%

  2. Non-basmati rice – 75%

  Of this 2/3rd will be job work for FCI and 1/3rd will be sold in the market.

Capacity utilisation – Dhuri plant



Source: Company

By-product processing to add to the bottomline

- **Value-added products**

  Dhuri plant being an integrated plant helps the company to process its by-products like bran, husk and nakku at a single location. Bran oil, furfural oil and power are the three major value-added products that company gets after further processing of by-products. The company uses its by-products such as bran and husk for extraction of edible oil and power. The power generated will be used for captive consumption and surplus will be sold in the market. It has 10.5 MW, 10 TPD and 42 TPD capacity for power, furfural and rice bran oil, respectively, at Dhuri (Punjab) which would ultimately contribute to the bottomline of the company. KRBL has planned to add a bran oil refinery by the end of December 2007 with the total capex of Rs. 1-1.2 bn which would ultimately improve the oil realisations from Rs. 32/unit to more than Rs. 100/unit.

Integrated vs. Non-integrated

Input*	Non-integrated			Integrated		
By-products	Proportion (%)	Rate per unit	Amount (Rs.)	Proportion (%)	Rate per unit	Amount (Rs.)
Bran	8.0	5.5	44.0	–	–	–
Bran oil	–	–	–	1.4	32.0	46.0
Husk	22.0	1.5	33.0	–	–	–
Furfural	–	–	–	0.4	50.0	22.0
Power	–	–	–	21.6	3.5	75.0
Deoiled cakes	–	–	–	6.2	2.5	16.0
Moisture	5.0	–	–	5.0	–	–
By-products value addition	–		**77.0**			**159.0**

Source: Company ***100 kgs of paddy = (Head rice 50% and Broken rice 15%).**

Power generation at different locations to reduce cost and also generate additional revenues

- **Power plant**

Dhuri: KRBL is expected to derive additional revenue by selling its power generated from the plant at Dhuri with a capacity of 10.5 MW at a prefixed tariff of Rs. 3.49/ unit for promotion of non-conventional energy. It is expected that the captive consumption and sale of power generated from such plant will be in the ratio of 1:1. The capex required for the same is Rs. 640 mn and is being funded through debt and internal accruals of Rs. 500 mn and Rs. 140 mn, respectively.

Ghaziabad: The power cost of the company is expected to decline, due to captive consumption of power generated from its 3.6 MW power plant. The plant is also eligible for carbon credits worth Rs. 8 mn p.a. and would be operational by March 2007. The cost saving would result in improvement in EBITDA margins.

Dhulia: The company is also focusing on power generation from wind farms and has made expansion in this area by setting up a 12.5 MW power plant at Dhulia (Maharashtra) which has been commissioned in September 2006. It has already signed Power Purchase Agreement (PPA) agreement with Maharashtra State Electricity Board (MSEB) for sale of wind power for 13 years at the tariff rate of Rs. 3.50/unit and annual increment of Re. 0.15/unit. The company shall also derive depreciation and tax benefits from this area. The company can generate carbon credits worth Rs. 6 mn p.a. from this plant.

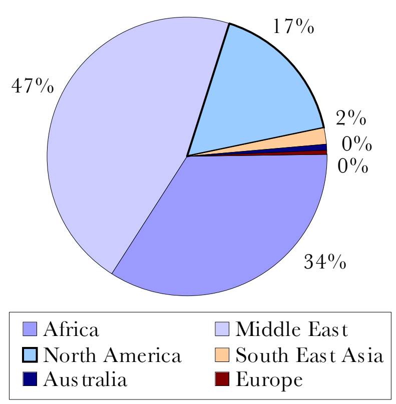
Total revenue generated from the above three projects shall have a 100% tax relief.

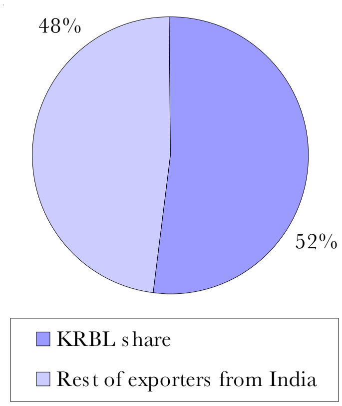
- **International presence**

KRBL has an international presence with almost 54% of the revenues being generated from the overseas market. The export income has grown at a CAGR of 13.2% between FY00-06. Contribution of India's basmati rice exports to USA stands around 2 % and KRBL commands 50% of the total basmati exports to the US.

The total basmati rice export from India is mainly to Middle East contributing 75%. In Middle East, Saudi Arabia is the biggest market for Indian basmati rice with contribution of 60% of the total imports in the region. The company currently has a market share of 10% in Saudi Arabia, which is expected to grow further with the expansion of parboiled unit at Dhuri supplying its product mainly to this market.

Contribution by KRBL in global and USA markets





Source: Company

- **Contract farming**

45% of paddy from contract farming

KRBL currently obtains about 45% of its basmati paddy requirements through contract farming. The company has entered into an agreement to undertake contract farming in an area of 180,000 acres by 2010 which is presently done on 87,000 acres of land. It has also established 750 acres seed farm along with 4 TPH seed plant for supplying quality seed to farmers and its agri-division, which works closely with the farmers during each stage of paddy cultivation. The Punjab government has also given the approval to set up 10 mandis to the company.

- **Strong brand recall**

83% of revenues from branded sales

The company has brands like **India Gate, Doon, Nurjahan, Bemisal, Aarti, Indian Farm** and **Unity** in basmati rice segment. Branded rice contributes around 83% of KRBL's revenue. In the Indian branded rice market, the company contributes 30% and its brand India Gate occupies 22% of market share. KRBL also has plans lined up to sell non-basmati rice in branded form. Though branding, the company is looking at getting itself into a position to pass on the rise in raw material prices to consumers.

Valuations

The factors poised to contribute to the growth of the company are:

Expanding the product range

KRBL has broadened its business mix by focusing on non-basmati rice, in addition to the basmati rice, its traditional revenue generating activity. The company is concentrating on increasing its share in the non-basmati segment, as the same accounts for 98% of the total rice production in the domestic market which is mostly dominated by small and medium sized unorganised players. The company's Dhuri plant is now fully integrated for producing bran oil, furfural oil and power. The company will further expand the plant by adding oil refinery.

Benefits of scale

KRBL also expects a robust growth both in the topline as well as the bottomline mainly due to volume play, as it has the highest processing capacity in the country.

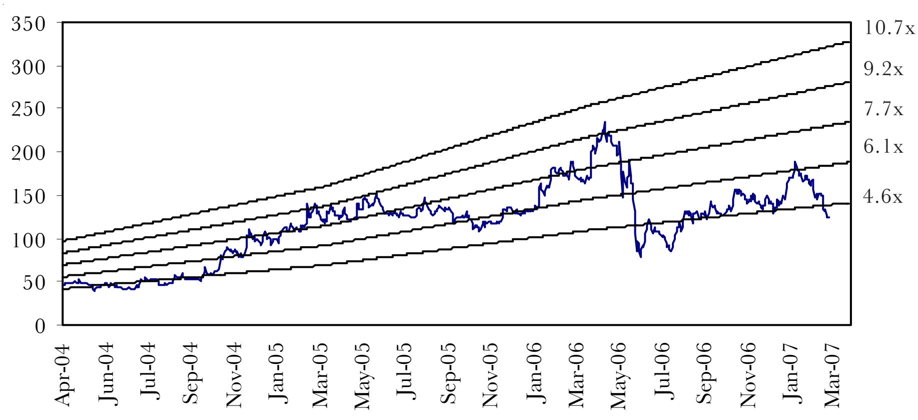
Increase in exports

The company is also concentrating on the sale of its branded products in the export markets which is expected to improve the margins further, as compared to private labels exports.

Improvement in margins

By-products generated from the job work for FCI would provide enough scope to operate oil refinery, power plant, etc. at the optimum level. Although, the increase of focus in non-basmati rice would generate lower margins but the overall margins of the company is expected to improve on account of rising exports and increased contribution from the sale of value-added products.

PER Band



At the current market price of Rs. 125, the stock is trading at 5.3x FY07E, 4.1x FY08E and 3.4x FY09E. We believe the stock is fairly valued at these levels. We are initiating coverage with a Market Performer rating at a target price of Rs. 154 at 5x FY08E EPS of Rs. 30.7.

Business overview

Background

Largest rice miller in India

KRBL is the largest rice miller in the world and the oldest in India. It is one of the major players in the branded food industry and also the largest exporter of basmati rice from the country.

KRBL was started as a partnership firm in the year 1988 under the name and style M/s. K.B. Overseas, the partners being Mr. Anil K. Mittal, Mr. Anoop K. Gupta and Mr. Arun K. Gupta. KRBL was incorporated in 1993 by the partners of the firm with the intention to takeover the operations and businesses of the partnership firm.

The promoters of the company hail from an old business family engaged in the trading of agro products since 1889 in Lyallpur (presently in Pakistan).The family operated as commission agents and traders of various agro products after the partition of the country and split in the family. The processing activity of the firm started in 1992 before which they were a merchant exporter of rice along with the group firm M/s. Khushiram Beharilal (Export Division).

Promoters/Management

Mr. Anil Kumar Mittal (55), Chairman-cum-Managing Director of the company has an experience of more than 34 years. He is responsible for the formulation and implementation of marketing strategies in the organisation.

Experienced management

Mr. Arun Kumar Gupta (49), Joint Managing Director has an experience of more than 25 years and plays an active role in operations of the plant, especially in procuring good quality paddy.

Mr. Anoop Kumar Gupta (47), Joint Managing Director with the experience of 24 years, manages the accounts, finance and administration departments.

Equity history (Nos. mn)

Duration	Issued capital	Increase	Face value (Rs.)	Particulars
1993-95	7.2	-	10.0	Inception of the company
1995-99	9.9	2.7	10.0	Public issue
1999-03	14.9	5.0	10.0	Preferential issue
2003-05	17.9	3.0	10.0	Preferential issue
2005-06*	21.3	3.4	10.0	Issue of 3.4 mn equity share against 1.7 mn GDRs.
2006-07#	24.3	3.0	10.0	Conversion of warrants

* KRBL issued 3.43 mn shares at a price of Rs. 155.08 to raise Rs. 531.7 mn in exchange of 1.71 mn GDR's issued at a price of US$ 7/GDR in February 2006. The conversion was 2 shares each for a single GDR. The GDRs are listed on the Luxembourg Stock Exchange.

#The company has also issued 3 mn equity shares (12% post issue stake) to Reliance Commodities (P.) Ltd. DMCC, (Dubai, UAE) by converting 3 mn zero coupon warrants in 1QFY07 at a price of Rs. 90/share.

Omar Ali Balsharaf Trading, one of the leading super market chain and FMCG trader in Saudi Arabia has also taken 6% stake through the preferential allotment at Rs. 90/share.

Manufacturing facilities

- **Rice:** The company has two rice processing facilities one in **Dhuri** (Punjab) and **Dadri, Ghaziabad** (UP) with the capacity of 150 TPH and 45 TPH, respectively. The facility in Ghaziabad is only for basmati rice processing. The company utilises its Dhuri facility for basmati rice, non-basmati rice and for the job work of FCI (non-basmati) with the proportion of 25%, 25% and 50%, respectively. This gives the company enough scope to foray into non-basmati rice processing and effective utilisation of by-products generated from non-basmati rice processing.
- **Power:** The company has already entered into power generation activity with its first wind farm at Dhulia (Maharashtra) with the capacity of 12.5 MW. It has also started utilising its by-product husk for power generation at two locations at Dhuri (Punjab) and Dadri (UP) with the capacity of 10.5 MW and 3.6 MW.
- **Oil:** It has also started generating revenues from 2 types of oil i.e. furfural and bran oil with the capacity of 10 TPD and 42 TPD, respectively, through utilisation of bran.
- **Packaging unit:** It has two units one each in Alipur (Delhi) and Gandhidham, Kandla (Gujarat) for grading, sorting and packaging of basmati rice and various other by-products.

Production capacities

Product	Facility location	Capacity	Storage space
Paddy processing (TPH)#	(a) Dhuri (Punjab)	150	132 acres open storage and 4 lacs sq.ft. warehouse. (@)Mill area .68 mn sq yards
	(b) Ghaziabad (U.P)	45	150,000 MT space for storage and 7 lacs sq.ft. warehouse. Mill area .45 mn sq. yards
Total		**195**	
Power (MW)			
From wind farm	Dhulia (Maharashtra)	12.5	
From husk	(a) Dhuri (Punjab)	10.5	
	(b) Ghaziabad	3.6	
Total		**26.6**	
Furfural oil (TPD)	Dhuri (Punjab)	10	
Bran oil (TPD)	Dhuri (Punjab)	42	
Packaging unit (TPH)*	(a) Alipur (Delhi)	30	1.2 lacs sqft ware house.
	(b) Gandhi dam (Kandla)	40	1.3 lacs sqft ware house.
Total		**70**	

Note: # Paddy milling. *Rice processing/packaging facilities (Domestic sales). @Another 6 lacs sq.ft. under construction.

Source: Company

Procurement & Distribution network

Developing mandis

KRBL procures its raw material in two ways firstly from contact farming and secondly from purchase from mandis. The government has granted 10 mandis to KRBL at different locations in Punjab. Out of these 10 mandis, 2 will be developed by the end of FY07 and the remaining 8 will be developed by the end of FY08. Punjab, Haryana, Uttaranchal and Uttar Pradesh (combined) are the major states for procurement of paddy in the proportion of 20:30:50.

Procurement states

States	Contract farming	Mandis	Total
UP and Uttaranchal	40	10	50
Haryana	0	30	30
Punjab	4	16	20

It also has a wide spread presence for distribution of its finished goods through 2 lakhs retailers supported by 71 distributors and 454 dealers in the domestic market. KRBL has also entered into agreements with retail chains like Big Bazaar, D'mart, Nil Giri, Food Land, Shoppe Rite, V-Mart, Vishal Mega Mart, Spencer Plaza and Reliance Retail to expand its products reach for its customers.

Brands

KRBL has over the years launched a number of brands in the domestic and export markets. The company is catering to variety of customers around the globe with around 29 brands in different segments. It has a brand valuation of Rs. 2.8 bn valued by Trisys a Kolkata-based research agency.

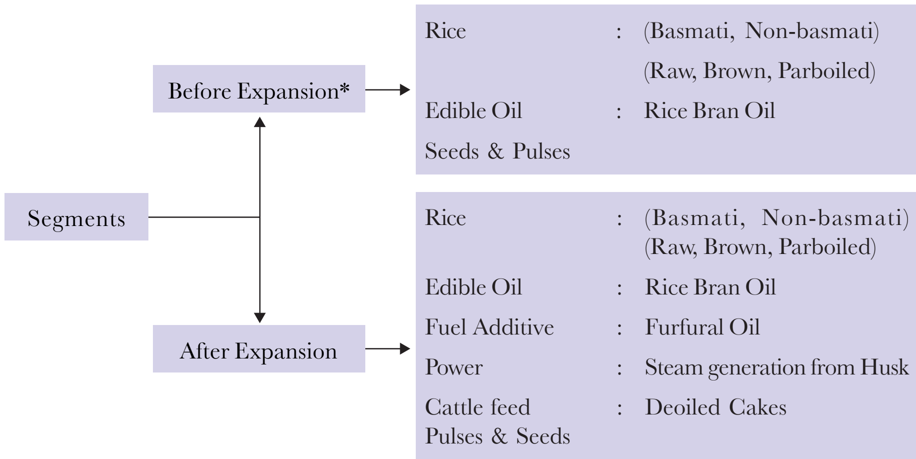
India Gate – largest selling rice brand in India

Domestic market: In the domestic market, **India Gate, Doon, Nur Jahan**, **Bemisal, Royal, Lotus, Aarati,** etc. are the most famous brands of the company contributing around 35% of the domestic sales. Its brand India Gate has been ranked as the largest selling brand in the domestic market in 2005 and has contributed 42% in total revenues of the company.

Export market: In the export markets, the key brands generating maximum revenues are **India Gate, Doon, Nur Jahan, Al Wissam, Al Bustan, Indian Farm, etc.** India Gate is marketed under the name of "Babal Hind" in world's largest basmati market, Saudi Arabia, with its partner, Omar Ali Balsharaf Trading and is the second largest brand in Saudi Arabia. It plays a dominant position in the North American markets also.

Change in business mix

Non-basmati to complement basmati processing



Note: *Before expansion KRBL was in non-basmati rice as trading activity.

KRBL derives revenues from rice and selling its by-products. It has now evolved from basmati into a rice company with a profitable presence in downstream products also. The company's business model comprises basmati rice on one hand and the downstream by-product generation of rice bran oil, furfural, power generation and cattle feed on the other.

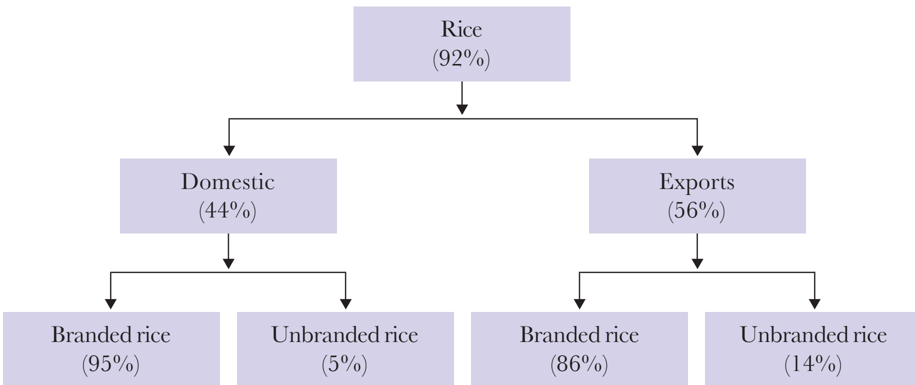
- Rice constitutes both basmati and non-basmati rice. The company only processed the basmati rice earlier but with the expansion of Dhuri plant it has started processing the non-basmati rice also. Till FY06, the company was just purchasing non-basmati rice from various millers and selling it into the market.
- Dhuri plant gives KRBL the opportunity to strengthen its bottomline by expanding its portfolio to add power, bran oil and furfural oil in the revenue mix.

Business segment

KRBL operates in the single segment of rice processing and selling of related by-products. The company sells its products both in domestic and export markets with the proportion of 46:54 in the favour of exports. The company is meeting the demand of around 25 states in India and 11 countries across the globe and the revenues have increased by 73% in domestic market and 26% in export market between FY05-06.

Business model – Rice

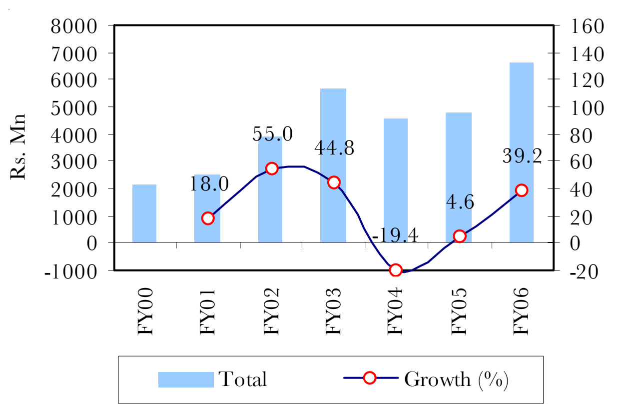
92% revenues from rice



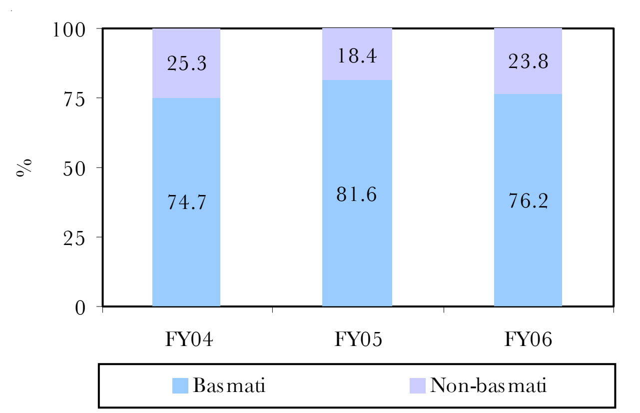
Price range:
Basmati – Rs. 20-80/kg
Non-basmati – Rs. 15-25/kg

Rice: It constitutes both basmati and non-basmati rice. KRBL plays a significant role in the rice industry. It is currently in the business of selling basmati rice after processing paddy and trading non-basmati rice. But with the expansion of Dhuri plant, it has also started processing non-basmati rice. Rice constituted 92% of the total revenue in FY06 as sales increased by 39% from Rs. 4.8 bn in FY05 to Rs. 6.6 bn in FY06. Major portion was derived from domestic market which increased by 68% and exports increased by 23% during FY06. The proportion of basmati and non-basmati rice in total rice is 76:24 for FY06. Going forward, the proportion will be almost same, to maintain the growth and pace of margins. The products of the company are available in the range of Rs. 20-80/kg and Rs. 15-25/kg for basmati and non-basmati, respectively. Average realisation is Rs. 23.5/kg for domestic.

Rice – Revenue and growth (%)

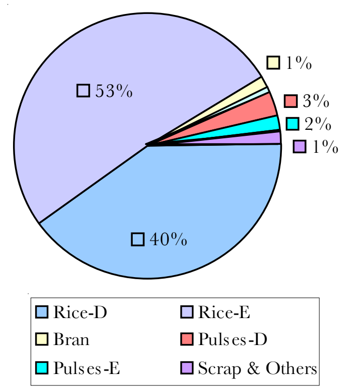


Basmati and non-basmati mix



Source: Company

Revenue break-up (FY06)



Source: Company

Value-added products: The company until FY05 was selling its entire husk and bran production, at prices of Rs. 1.5/kg and Rs. 5/kg, respectively but, from FY06, the same are further processed to obtain bran and furfural oil which have higher realisation as well as high margins. In FY06, rice bran (including bran oil) and furfural oil contributed 1.5% and 0.4%, respectively, amounting to a total of Rs. 140 mn.

Others: KRBL also offers variety of products such as **Pulses, Paddy, Seed and Scrap and others** in addition to its main product, rice. In FY03, it forayed into sale of its quality rice seeds and wheat seeds, which have grown at a CAGR of 35% since FY03, amounting to Rs. 32 mn in FY06. Pulses and scrap constituted 4.6% and 1.3% in the total revenues of the company amounting to Rs. 332 mn and Rs. 94 mn, respectively.

Exports

KRBL enjoys 11% share of India's total basmati exports, with the major portion being exported under its own brands (86% in FY06 as compared to 75% in FY05). This fetches higher realisations and flexibility in transferring the hike in paddy cost to the consumers. Export revenues as a percentage of sales have declined from 63% in FY04 to 54% in FY06 because of reduction in exports under private label (from 25% in FY04 to 14% in FY06). However, this has resulted in high realisation on account of increase in branded sales. But the total exports increased by 26% from Rs. 3.1 bn in FY05 to Rs. 3.9 bn in FY06.

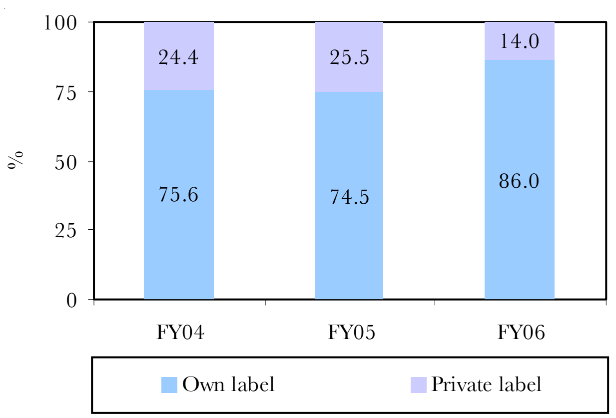
Marketing alliance in Saudi Arabia

It has good demand in the export market such as Saudi Arabia, Kuwait and USA and enjoys 10%, 10% and 50% of the market share, respectively.

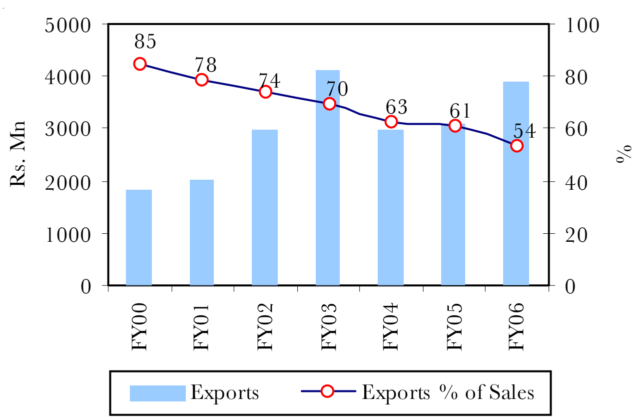
It has also entered into a marketing alliance with Omar Ali Balsharaf Trading (a leading super market chain and FMCG trader in Saudi Arabia) for strengthening the company's presence in world's biggest basmati rice market and increasing its share in this market. The company is enhancing its direct presence in the large retail stores to further strengthen the direct sales of its own brands, resulting in improvement in the margins, visibility and reputation.

The average realisation from basmati and non-basmati rice is Rs. 29.6/kg and Rs. 11.78/kg in FY06.

Own and private labels in exports



Exports and Exports as % of sales



Source: Company

Benefits – Due to Dhuri plant

The company has received various exemptions from the Punjab government in view of the investment made in the Dhuri plant:

- No mandi tax till 2015 (as against the existing rate of 4%).
- No rural development cess till 2015 (as against the existing of 1%).
- Exemption from Agricultural and Processed Food Products Export Development Authority (APEDA) registration to 0.1% (as against 1%).
- No electricity duty.
- No land registration fees up to 250 acres (as against the existing of 6%).
- Allowance on 10 private mandis to be treated at par with government operated mandis for direct procurement.

These concessions/exemptions have resulted in lower raw material costs, strengthening the company's edge in a competitive market place.

Financial analysis

- **Revenue**

  Revenues of the company are expected to post a CAGR of 21% from Rs. 7.2 bn in FY06 to Rs. 12.9 bn in FY09E. The growth will be on account of increase in capacity utilisation because of the completion of the refurbishment and expansion programme of Dhuri and other plant locations. There has been a reduction in export sales on account of lower sales in the private label. The company expects the exports to increase on account of increase in branded product sales, which realises higher price.

- **Margins**

  The EBITDA margin is expected to increase by 300 basis points to 14.4% for FY09E from the current level of 11.4% for FY06. The increase is expected to be on account of the following:

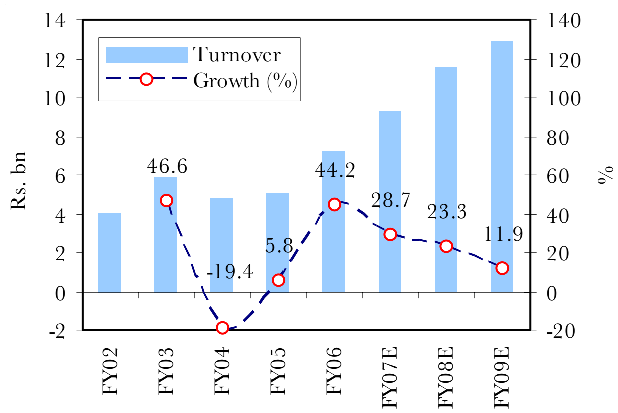
  Increase in capacity utilisation post completion of expansion in capacities.

  Increase in sales of branded products in the overseas market which has higher realisation and higher margins as compared to sales in the domestic market and sales under private label in the overseas market.

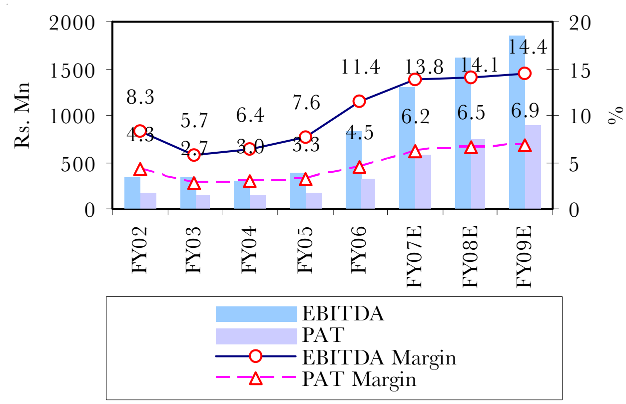
  Increase in revenue from value-added products on account of higher production due to completion of the expansion programme.

The increase in EBITDA margins will also lead to growth in PAT margins which is expected to grow from 4.5% in FY06 up to 7% by FY09.

Turnover and its growth (%)



Earnings and its margins (%)

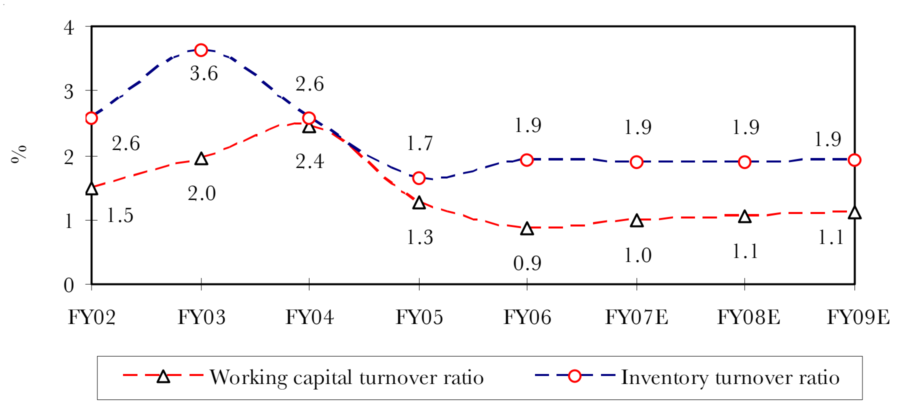


Source: Company

Turnover ratio

Working capital turnover ratio of the company has decreased from 3.6 in FY03 to 1.9 in FY06. Inventory and Debtors levels to sales are expected to be maintained at the current levels.

Working capital and Inventory turnover ratio



Source: Company

Financial highlights (9 Monthly)

(Rs. mn)	3QFY06	3QFY07	YoY (%)	9MFY06	9MFY07	YoY (%)
Net Sales	**2,148**	**2,795**	**30.1**	**5,435**	**6,976**	**28.3**
EBITDA	**266**	**385**	**44.6**	**645**	**994**	**54.1**
EBITDA Margins (%)	12.4	13.3	–	11.9	13.7	–
Other Income	11	14	31.5	25	36	45.2
Interest	(83)	(151)	82.2	(194)	(336)	73.2
Depreciation	(35)	(50)	40.7	(82)	(119)	44.8
PBT	159	199	25.0	394	576	46.2
Tax	(54)	(9)	(84.1)	(131)	(94)	(28.1)
Adjusted PAT	**105**	**190**	**80.6**	**263**	**482**	**83.0**
PAT Margins (%)	4.9	6.8	–	4.8	6.7	–
EPS (Rs.)	6	8	–	15	20	–

Detailed financials

Income Statement

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Net sales	**5,895**	**4,754**	**5,027**	**7,248**	**9,331**	**11,507**	**12,879**
Growth (%)	46.6	-19.4	5.8	44.2	28.7	23.3	11.9
Operating expenses	5,561	4,451	4,643	6,440	8,061	9,904	11,043
% to net sales	94.3	93.6	92.4	88.9	86.4	86.1	85.7
Raw material cost	4,492	3,582	3,645	4,940	6,307	8,097	9,085
RM as % of cost	80.8	80.5	78.5	76.7	78.2	81.8	82.3
RM as % of Net sales	76.2	75.3	72.5	68.2	67.6	70.4	70.5
Finished Goods purchased	265	203	295	591	467	230	129
% of Net Sales	4.5	4.3	5.9	8.1	5.0	2.0	1.0
Employee expenses	59	60	68	94	121	127	142
% of Net Sales	1.0	1.3	1.3	1.3	1.3	1.1	1.1
Power & Fuel	74	91	118	126	164	209	251
% of Net Sales	1.3	1.9	2.3	1.7	1.8	1.8	2.0
Selling & Distribution expenses	111	47	104	186	294	383	457
% of Net Sales	1.9	1.0	2.1	2.6	3.2	3.3	3.6
Administrative expenses	114	112	127	173	261	322	386
% of Net Sales	2.0	2.5	2.7	2.7	3.2	3.3	3.5
Other expenses	446	357	287	331	447	536	592
% of Net Sales	9.9	10.0	7.9	6.7	7.1	6.6	6.5
Operating Profit	334	303	384	807	1,270	1,603	1,836
Operating profit Margin (%)	5.7	6.4	7.6	11.1	13.6	13.9	14.3
Other Operating Income	0	0	0	18	20	22	24
EBITDA	**334**	**303**	**384**	**826**	**1,290**	**1,625**	**1,860**
EBITDA Margin (%)	5.7	6.4	7.6	11.4	13.8	14.1	14.4
Depreciation	57	72	74	119	156	172	182
Other income	72	35	32	57	76	98	121
EBIT	**349**	**266**	**342**	**764**	**1,210**	**1,551**	**1,799**
Interest paid	131	54	86	278	329	410	446
Pre-tax profit (before non-recurring items)	218	212	256	486	881	1,141	1,353
Pre-tax profit (after non-recurring items)	218	212	256	486	881	1,141	1,353
Tax (current + deferred)	59	67	92	162	304	393	466
Net profit	**159**	**145**	**165**	**325**	**577**	**747**	**887**
PAT Margin (%)	2.7	3.0	3.2	4.4	6.2	6.5	6.9

Balance Sheet

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Current assets	2,409	2,600	4,145	6,075	7,672	9,294	10,839
Net fixed assets	611	810	1,082	1,472	1,354	1,370	1,335
Total assets	**3,020**	**3,410**	**5,227**	**7,547**	**9,027**	**10,664**	**12,174**
Current liabilities	366	185	428	285	345	427	458
Total debt	1,563	1,701	2,959	4,519	5,271	5,946	6,375
- Short term	1,507	1,587	2,664	3,838	4,572	5,178	5,538
- Long term	56	114	295	681	698	768	837
Other non-current liabilities	5	28	57	80	241	449	696
Total liabilities	**1,934**	**1,914**	**3,443**	**4,883**	**5,856**	**6,822**	**7,529**
Share capital	137	177	332	471	244	244	244
Reserves & surplus	950	1,319	1,451	2,193	2,927	3,598	4,401
- Retained Earnings	793	898	1,020	1,285	1,792	2,463	3,266
Less: Misc. expenditure	(2)	(1)	0	0	0	0	0
Shareholders' funds	1,086	1,495	1,783	2,664	3,171	3,842	4,645
Total equity & liabilities	**3,020**	**3,410**	**5,227**	**7,547**	**9,027**	**10,664**	**12,174**
Capital employed	**2,654**	**3,224**	**4,799**	**7,262**	**8,682**	**10,237**	**11,716**

Cash Flow Statement

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Pre-tax profit	218	212	256	486	881	1,141	1,353
Depreciation	47	67	70	116	145	164	174
Chg in working capital	(255)	(235)	(1,402)	(1,547)	(1,959)	(1,707)	(1,388)
Total tax paid	(20)	(76)	(62)	(128)	(127)	(175)	(211)
Cash flow from oper. (a)	**(10)**	**(32)**	**(1,138)**	**(1,072)**	**(1,060)**	**(577)**	**(72)**
Capital expenditure	(184)	(266)	(341)	(507)	(27)	(180)	(139)
Other investing activities	0	(17)	0	0	(0)	(0)	(0)
Cash flow from inv. (b)	**(184)**	**(283)**	**(341)**	**(507)**	**(27)**	**(180)**	**(139)**
Free cash flow (a+b)	**(194)**	**(314)**	**(1,479)**	**(1,579)**	**(1,087)**	**(756)**	**(211)**
Equity raised/(repaid)	5	304	166	615	(0)	0	0
Debt raised/(repaid)	288	138	1,258	1,560	752	676	429
Dividend (incl. tax)	(24)	(34)	(20)	(41)	(55)	(69)	(76)
Cash flow from fin. (c)	**268**	**409**	**1,403**	**2,135**	**696**	**606**	**352**
Net chg in cash (a+b+c)	**75**	**94**	**(76)**	**555**	**(391)**	**(150)**	**142**

KRBL

Income Statement

Yr. ended 31 Mar. (Rs. mn)	FY06	FY07E	FY08E	FY09E
Net sales	7,248	9,331	11,507	12,879
Growth (%)	44.2	28.7	23.3	11.9
Operating expenses	(6,440)	(8,061)	(9,904)	(11,043)
Operating profit	807	1,270	1,603	1,836
Other operating income	18	20	22	24
EBITDA	**826**	**1,290**	**1,625**	**1,860**
Growth (%)	115.1	56.2	26.0	14.5
Depreciation	(119)	(156)	(172)	(182)
Other income	57	76	98	121
EBIT	**764**	**1,210**	**1,551**	**1,799**
Interest paid	(278)	(329)	(410)	(446)
Pre-tax profit	486	881	1,141	1,353
(before non-recurring items)				
Pre-tax profit	486	881	1,141	1,353
(after non-recurring items)				
Tax (current + deferred)	(162)	(304)	(393)	(466)
Net profit	**325**	**577**	**747**	**887**
Adjusted net profit	325	577	747	887
Growth (%)	97.3	77.6	29.6	18.7
Prior period adjustments	(4)			
Net income	**320**	**577**	**747**	**887**

Balance Sheet

Yr. ended 31 Mar. (Rs. mn)	FY06	FY07E	FY08E	FY09E
Current assets	6,075	7,673	9,294	10,839
Net fixed assets	1,472	1,354	1,370	1,335
Total assets	**7,547**	**9,027**	**10,664**	**12,174**
Current liabilities	285	345	427	458
Total Debt	4,519	5,271	5,946	6,375
Other non-current liabilities	80	241	449	696
Total liabilities	**4,883**	**5,856**	**6,822**	**7,529**
Share capital	471	244	244	244
Reserves & surplus	2,193	2,927	3,598	4,401
Shareholders' funds	2,664	3,171	3,842	4,645
Total equity & liabilities	**7,547**	**9,027**	**10,664**	**12,174**
Capital employed	**7,262**	**8,682**	**10,237**	**11,716**

Cash Flow Statement

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Pre-tax profit	486	881	1,141	1,353
Depreciation	116	145	164	174
Chg in working capital	(1,547)	(1,959)	(1,707)	(1,388)
Total tax paid	(128)	(127)	(175)	(211)
Cash flow from oper. (a)	**(1,072)**	**(1,060)**	**(577)**	**(72)**
Capital expenditure	(507)	(27)	(180)	(139)
Cash flow from inv. (b)	**(507)**	**(27)**	**(180)**	**(139)**
Free cash flow (a+b)	**(1,579)**	**(1,087)**	**(756)**	**(211)**
Equity raised/(repaid)	615	0		
Debt raised/(repaid)	1,560	752	676	429
Dividend (incl. tax)	(41)	(55)	(69)	(76)
Cash flow from fin. (c)	**2,135**	**696**	**606**	**352**
Net chg in cash (a+b+c)	**555**	**(391)**	**(150)**	**142**

Key Ratios

Yr. ended 31 Mar. (%)	FY06	FY07E	FY08E	FY09E
EPS (Rs.)	15.2	23.7	30.7	36.5
EPS growth	66.3	55.7	29.6	18.7
EBITDA margin	11.4	13.8	14.1	14.4
EBIT margin	10.5	13.0	13.5	14.0
ROCE	12.7	15.2	16.4	16.4
Net debt/Equity	144.5	157.4	151.4	131.4

Valuations

Yr. ended 31 Mar. (x)	FY06	FY07E	FY08E	FY09E
PER	8.2	5.3	4.1	3.4
PCE	6.0	4.1	3.3	2.8
Price/Book	1.0	1.0	0.8	0.7
Yield (%)	1.8	2.0	2.2	2.4
EV/Net sales	0.9	0.8	0.7	0.7
EV/EBITDA	7.9	5.9	5.2	4.7

Du Pont Analysis – ROE

Yr. ended 31 Mar. (x)	FY06	FY07E	FY08E	FY09E
Net margin (%)	4.5	6.2	6.5	6.9
Asset turnover	1.1	1.1	1.2	1.1
Leverage factor	2.9	2.8	2.8	2.7
Return on equity (%)	14.6	19.8	21.3	20.9

Kohinoor Foods

Market Performer

"Kohinoor" The Super brand

Kohinoor Foods Ltd. (KFL) is the only integrated player in food industry. The company had recently gone on a major expansion drive to capture global markets and the growth in the food chain business, thereby leading to increased demand for Ready-to-Eat products. We are initiating coverage with a Market Performer.

Year to March	FY06	FY07E	FY08E	FY09E	CAGR (%)
P&L data (Rs. mn)					**FY06-09E**
Net Sales	5,399	6,011	6,712	7,515	11.7
Operating Profit	433	575	675	778	21.5
Net Profit	208	270	327	377	22.0
Margins (%)					
EBITDA	8.0	9.6	10.1	10.4	–
Net Profit	3.9	4.5	4.9	5.0	–
Balance Sheet Data (Rs. mn)					
Total Assets	5,254	5,573	6,274	6,939	9.7
Shareholders' Funds	1,184	1,410	2,504	2,769	32.7
Per Share Data (Rs.)					
EPS	10.6	13.8	11.0	12.8	6.3
CEPS	15	19	16	18	7.2
Dividend	2.2	2.5	3.0	3.5	16.7
Returns (%)					
RoE	18.5	20.8	16.7	14.3	–
RoCE	8.9	10.1	10.5	10.9	–

- It is the only Indian integrated food company having control on the entire value chain along with global manufacturing and servicing capabilities. The company has credible infrastructure and supplying capabilities along with shelf ready packaging.
- The value-added Ready-to-Eat market has enormous potential for expansion. The export potential for ethnic Indian food is expected to increase significantly. KFL foresees enhanced profitability through improved efficiencies and focus on high margins generating segment i.e. Branded Food segment.
- It is focusing on enhancing the branding of **Kohinoor** by foraying into new markets and expects to add 10 new countries in its global presence by the end of FY09. It has a diversified business model spread over varied customer groups and countries.
- At the current market price of Rs. 69, the stock is trading at 5x FY07E, 6.3x FY08E and 5.4x FY09E earnings. The stock has discounted the upsides at these valuations. We value the company at 6x FY08E EPS of Rs. 11 and give a target price of Rs. 66. We initiate coverage with a Market Performer rating.

Share Data

Mkt. Cap.	Rs. 1.4 bn (US$ 31 mn)
Price	Rs. 69
Target Price	Rs. 66
BSE Sensex	12886
Reuters	SATN.BO
Bloomberg	KFL IN
Daily Volume	US$ 0.2 mn (Rs. 8.8 mn)
52-week High/Low	Rs. 112/52
Issued Shares	20 mn

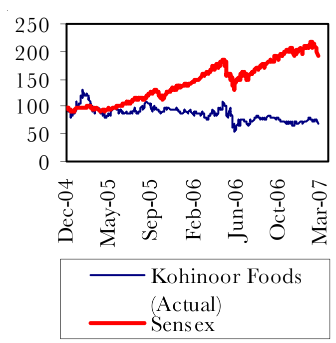
Valuation Ratios

Year to 31 Mar.	2008E	2009E
EPS (Rs.)	11.0	12.8
+/- (%)	(19.8)	15.5
PER (x)	6.3	5.4
PBV (x)	0.8	0.7
Dividend/Yield (%)	4.3	5.1
EV/Sales (x)	0.6	0.6
EV/EBITDA (x)	6.3	5.9

Shareholding Pattern (%)

Promoters	44
FIIs	7
MFs	6
Institutions	3
Public & Others	40

Relative Performance



Investment arguments

Kohinoor is changing its image as an integrated player from a commodity player. Its flagship brand "Kohinoor" has worldwide recognition for its authentic and quality food offerings. It has been awarded the "Super Brand" status in 2005-06 in rice category.

Growth in earnings and margins

- **Potential in Ready-to-Eat (RTE) market**

Demand influenced by changing tastes and lifestyle

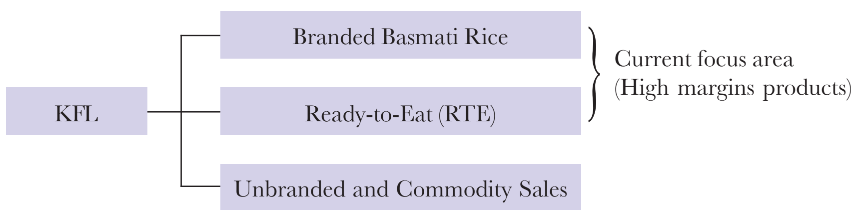
The ready-to-eat market is gaining momentum due to increase in its demand mainly from UK, USA and European nations. The RTE industry is expected to witness a significant growth in the domestic market too, mainly on account of large number of modern retail chains being set-up and also the changing lifestyle of the masses.

- **Change in the business mix**

KFL gradually shifted its focus to Branded Food segment in FY05 from unbranded sales and trading in commodities. Though, the latter were the traditional business activities of the company and had maximum contribution in the topline but the margins were relatively low at around 2-3%. The revenues from branded and unbranded sales were in the ratio of 55:45 for FY06 which is expected to be 78:22 by FY09E.

Spectrum of business

Branded revenues to increase from 55% to 78%



Source: Company

Branded basmati rice: The revenue (domestic and exports) from this stream is currently around 51% and is expected to increase to 70% over the next two-three years, as the company is making continuous efforts to tap the opportunities available in the export markets. The company is targeting at least 10% of the market share in Saudi Arabia.

Huge potential in export market

RTE: KFL entered the food business with the launch of its products under ambient foods and expanded the product portfolio with frozen foods. It further plans to foray into chilled food. The quantum of revenues from frozen and chilled food is expected to be 4 times and 8 times that of ambient food sales. There is a huge demand of RTE products in UK and USA, the largest markets for such products and the company is betting big to have a substantial market share in such market.

- **Export oriented**

Eye on export market for further growth

KFL earned a substantial portion of its revenues i.e. approximately 55%, amounting to Rs. 3 bn in FY06, from the export markets. The company is poised to increase its revenues from the export markets further to 72% by FY09E through sale of RTE products and branded basmati rice in the Europe and Middle East, respectively.

In the global markets (like Saudi Arabia and Europe) also there is ample scope to grow. KFL has appointed its distributor "**Al-hokair**" in Saudi Arabia to garner at least 10% of the market share of the total market estimated at Rs. 30 bn, by FY09. The UK facility has been made fully operational which will be catering to the European markets.

- **Tapping the opportunities in unorganised market**

  KFL being one of the organised players is making continuous efforts to tap the unorganised market, on the back of its brand, latest machinery for making quality rice through paddy processing, vast distribution network, global presence and other economies of scale.

Support system

- **Brand recognition**

To become first "Global Culinary Brand"

Kohinoor Foods Limited is emerging as a global food company with its flagship brand **"Kohinoor"** which has been awarded as a "**Super brand"**. It is the only Indian brand with presence in 47 countries marketed through own distribution and available on more than 30,000 retail outlets located overseas. It is focusing on becoming the first "truly global culinary brand" in the world. It has emerged as the largest selling brand in India with a market share of 38% in Indian branded basmati market worth US$ 100 mn (Source: AMGF Brand Study – Ernst & Young 2004).

- **Global presence**

Infrastructure to tap the global market

KFL has global infrastructure in the form of subsidiaries, joint ventures, processing facilities and distribution network. It has two subsidiaries one each in US and UK, a rice polishing mill in UK and a joint venture in UAE. The company has a distribution network in 45 countries supplying products to 60 countries.

- **Knowledge resource**

Market Knowledge – the distinguishing feature

KFL incurs a lot of expenditure on research and development to obtain customers, suppliers and farmers feedback to increase the quality of product and services rendered to customers and to increase the capabilities of procuring the raw materials and other supplies at best quality as well as price. It has also gained knowledge in respect of the operating style of modern retailing and global marketing techniques to have better margins while entering into any agreement with them or starting their own operations of the same level and size.

Investment concerns

- **International conditions**

  While major part of revenues (55% of revenues) are derived through export sales, the same is highly sensitive to government regulations.

- **Competition**

  Entry of large players in the retail segment may also lead to some of these players considering backward integration in certain areas like food processing, thereby creating direct competition for the company coupled with loss of sales.

- **Preference for home cooked food in India**

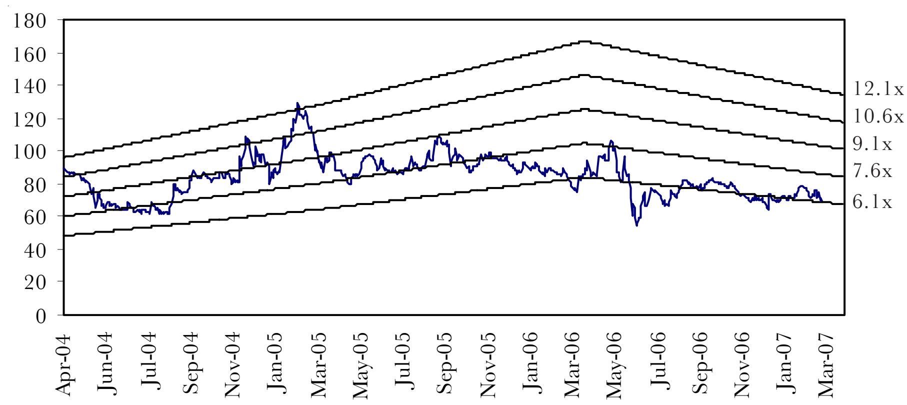
  The scenario in Indian markets for RTE products has not been a great success. The consumer still prefers the traditional style of cooking. The company might find it difficult to build a market for RTE products in the manner they have done for their branded basmati.

Valuations

The growth of the company is expected to be driven by the following factors:

- Aggressive plans to explore new avenues in the international market for its products both for rice and Ready-to Eat.
- Goal to achieve a market share of 10% of the worlds largest branded basmati rice market (Saudi Arabia) estimated to be Rs. 30 bn by FY09.
- UK rice processing facility will help the company in maximising its revenues at a lower cost as it will be catering to the European markets.
- KFL has expanded its capacity for ambient food and has set-up a new facility for frozen food to cater the European markets considered as the largest market for such foods. It also plans to enter chilled food business as the market for the same is considered to be 4 times and 2 times larger than that of ambient and frozen foods, respectively.
- Modern retail format stores are the biggest opportunity in recent times, backed by the retail growth in semi- urban and rural India. KFL is entering into tie-up arrangements with large players in the retail as it has keen understanding of International retailing trends and merchandising at retail shelves. It also has its portfolio designed to cater such formats.

PER Band



At the current market price of Rs. 69, the stock is trading at 5x FY07E, 6.3x FY08E and 5.4x FY09E earnings. The stock has discounted the upsides at these valuations. We value the company at 6x FY08E EPS of Rs. 11 and give a target price of Rs. 66. We initiate coverage with a Market Performer rating.

Business overview

Background

"Kohinoor Brand" captures 38% market share

Incorporated in 1989, Kohinoor Foods Limited (KFL) erstwhile known as Satnam Overseas Limited got listed in 1994 and is a prominent player, emerging as a global food processing company. It has made significant presence in Branded Basmati and Ready-to-Eat (RTE) products. RTE segment consists of ambient, frozen and chilled food, and KFL is currently into ambient and frozen food business with plans to enter the chilled food segment within the next two years. KFL has three processing facilities with capacities of around 48 TPH at two units for rice processing and 50,000 meals/day and 20 MT/day for ambient and frozen food, respectively, for the third unit. KFL revenues for the FY06 were in the ratio of 45:55 from domestic and export markets.

In the domestic branded basmati rice market, Kohinoor brand is enjoying 38% market share as per TNS-Ernst & Young. It also enjoys 52% (in value terms) and 49% (in volume terms) of the total organised basmati rice market in modern retail format stores in India as per ACNielsen ORG-MARG which makes the company a market leader in its industry.

Management

KFL was founded by Late Tirath Ram Arora in the year 1976 and is being now managed by Mr. Jugal Kishore Arora (Chairman and Managing Director) having three decades of experience in the basmati rice industry, Mr. Satnam Arora (Joint Managing Director) is responsible for managing the company's subsidiary and joint ventures abroad and Mr. Gurnam Arora (Joint Managing Director) manages the company's marketing and branding of Kohinoor.

Equity history (Nos. mn)

Duration	Issued capital	Increase	Face value (Rs.)	Particulars
1992-93	8.0	–	10.0	–
1993-94	10.0	2.0	10.0	Issued to existing shareholders.
1994-98	14.0	4.0	10.0	In 2005, issuance of another 4 mn of equity share.
1998-05	19.6	5.6	10.0	In 1998, the company has allotted 5.6 mn equity share as bonus issue in the ratio of 2:5.

Associate companies

Group enterprise	Country	Incorporated	Holding Structure	Principal Activity
Rich Rice Raisers Factory L.L.C	Dubai (UAE)	2000	Joint venture (25%)	Engaged in selling of company's products in UAE.
Satnam Overseas Ltd. INC	New Jersey (USA)	2000	Wholly owned	Engaged in wholesale business of rice and other agro products imported from India and serving the entire US markets.
Indo European Foods Ltd.	Felixstone (UK)	2002	Wholly owned	Started rice processing in FY06 and deals in RTE and allied food products.

Processing facilities

KFL has 3 processing facilities, out of which 2 are for rice processing and 1 for RTE products.

Processing of paddy is being done in Murthal (Haryana) and Felixstone (UK) with the capacity of 40 TPH and 8 TPH, respectively. KFL also had a **rice processing capacity** of 8 TPH in Amritsar (Punjab) which has been shifted to Murthal to concentrate its facilities at one place and derive benefits of lower stock requirement, fixed cost, working capital requirement and concentrating of management at a single place.

Processing facility at UK started commercial production in July 2006

The plant at UK has started commercial production in July 2006 and the capex for it was around US$ 6 mn for acquiring land and setting up of building. The sourcing of raw material for UK facility is done from India in the form of semi- processed rice to avoid duty, as import of fully processed rice in UK attracts the same. The semi-processed rice (brown rice) is further processed (white polishing) and sold in the European markets from there. Europe is considered to be the 2nd largest market for basmati rice in the world.

Fully modernised plant

RTE has the total capacity of 50,000 meals/day for ambient food and 20,000 kg/ day for frozen food segment. Frozen food capacity has been set up in July 2006 by the company with the capex of Rs. 250 mn at Bahalgarh (Sonepat, Haryana).

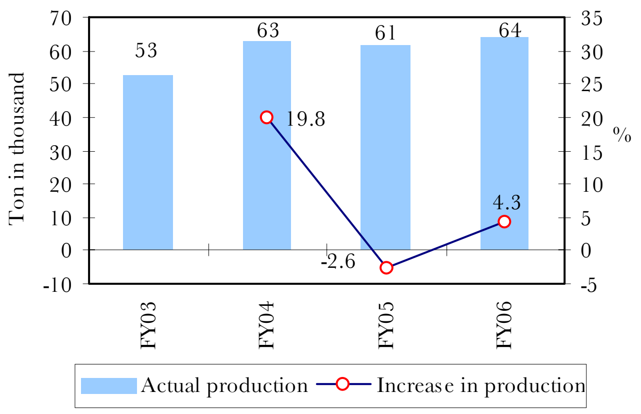
The manufacturing facilities at Murthal and Bahalgarh are fully automated plants, the former being one of the largest basmati rice mill in India.UK is also considered as the largest market for Indian foods.

The company has packaging capabilities in its existing facilities and is not dependent on outside packaging of its products. Flat & SUP Aluminum Retort Pouches, Microwaveable Transparent Retort Pouches, Multi Layer barrier Trays, Glass Jars, Aluminum Heat Sealable Containers, High Barrier Microwaveable Rigid Cups and PP Jars are the different forms of packaging done by the company for its products.

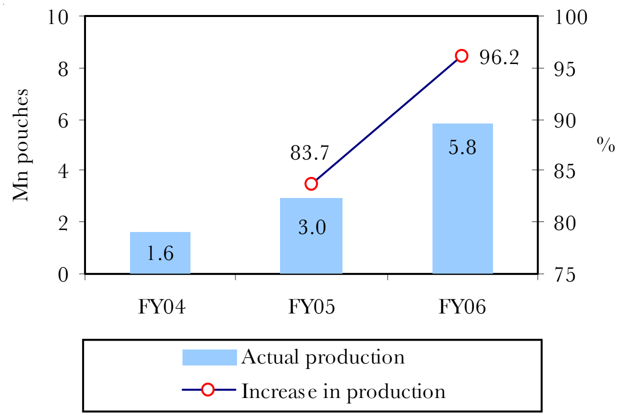
In-house capabilities

Particulars	Location	Area (Mn sq.ft.)	Capacity (TPH)
Rice	Murthal (Haryana)	1.29	40
	Felixstone (UK)	0.14	8
	Total		**48**
RTE			**(Per day)**
Ambient (meals)	Bahalgarh (Sonepat, Haryana)		50,000
Frozen (Kg)	Bahalgarh (Sonepat, Haryana)		20,000

Growth in production



Growth in ambient food



Source: Company

Global presence

USA operations

The company had formed its wholly owned subsidiary in USA in 2000 as S.O.L. Inc.

It achieved a turnover of US$ 3.6 mn in FY05-06.

The US operation mainly consists of marketing & distribution with dedicated warehousing capabilities in **New Jersey, Houston, Marryland, Chicago and San Francisco.**

It was previously marketing its products through distributors but has recently set-up its own distribution channel.

The company has also introduced 3 product lines with more than 35 SKU's (Stock Keeping Units) in the overseas markets.

Due to huge opportunity available for Indian foods, it is expected to improve its position to No.3 in two years time from 6th position, currently.

UK operations

It has formed a wholly owned subsidiary in UK in 2001 named Indo European Foods Limited. It started with a capacity of 8 TPH for rice polishing (to save import duty of 120 pound per tonne).The facility covers an area of 140 thousand sq.ft. It also has adequate space for further expansion (plans to set-up a chilled food plant).

It started commercial production on July 2005 and accounted for a turnover of 4.6 mn pounds in FY05-06.

The total funds invested by the company in its UK operations amounts to Rs. 290 mn.

The company is expected to achieve economies of scale by end of FY07, on account of 100% utilisation of its capacities from such plant.

Dubai operations

In FY01, the company entered into a joint venture with Rich Rice Raiser Factory L.L.C (RRR) in Dubai to augment its marketing strengths in the Middle East region. The joint venture is with Sunny General Trading which hold 75% stake and has distribution network for food products in UAE for the past 15 years.

RRR has a small rice processing facility besides a full fledged marketing office in Dubai.

The company presently caters to the markets of Iran and plans to enter the Iraqi market soon.

Due to the huge on-going infrastructural development and opening up of the food service sector, there is enormous scope for frozen food products.

Distribution network

Self sufficient distribution base

The products of the companies are available in 60 countries worldwide, with a distribution network in 47 countries.

India: The distribution network is strong consisting of 130 distributors, 500 stockists and 220,000 retailers. In Indian markets too it has arrangements with the domestic institutional clientele which consists of ITC Sheraton Hotels and many more. It also has co-promotion strategy with leading Indian companies like IOCL, Coke (India) Ltd., Duncan Tea and Sandesh Group.

Rest of the world: The distribution network consists of 48 distributors, 5 stockists and 30,000 retailers. KFL also has tie-up arrangements with leading global retail chains.

KFL has deployed almost around US$ 7 mn for strengthening its position in the US markets and has opened its own distribution offices at five locations in US for achieving such purpose.

Major clientele

The company is having a huge clientele both in the overseas market and domestic market in the form of tie-up arrangements along with some as prestigious institutional buyers.

Clients

International	Domestic
- TESCO, ASDA, Somerfield & Costco in UK	- Pantaloon Retail (Food Bazar)
- Wal-Mart, Krogers & Whole Foods in USA	- Reliance Retail
- Hankyu, Daimaru, Takshimaya and Seijo Ishi in Japan	- Pizza Hut
- Carrefour and Almayalal in the Middle East	- Spencer's
- Tiger Foods Brands (South Africa)	- Amway India
- Royal Emirates (UAE)	- Taj Group of Hotels
- Singapore Airlines	- Oberoi Group of Hotels
- Malaysia Airlines	–

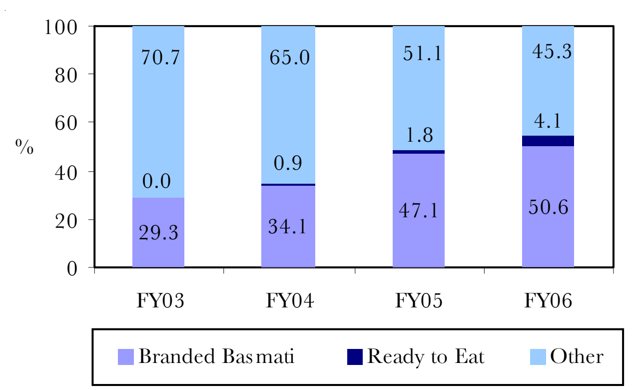
Business segment

51: Branded Basmati
4: RTE
45: Commodities

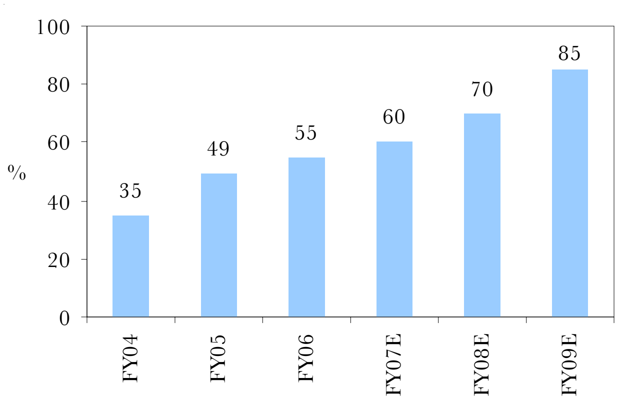
The company has food processing as its sole segment with a business mix of Branded Basmati, RTE and unbranded & commodity sales.

KFL is concentrating on Branded Foods consisting of Branded Basmati and RTE. The major revenue contributors are Basmati Rice, RTE and unbranded & commodities (including non-branded rice) with contribution of 51%, 4% and 45%, respectively, in FY06. The contribution of branded basmati and RTE has increased by 7% and 130%, respectively, whereas the contribution of unbranded & commodities (including non-branded rice) in the total sales has decreased by 11% over FY05.

Sales mix



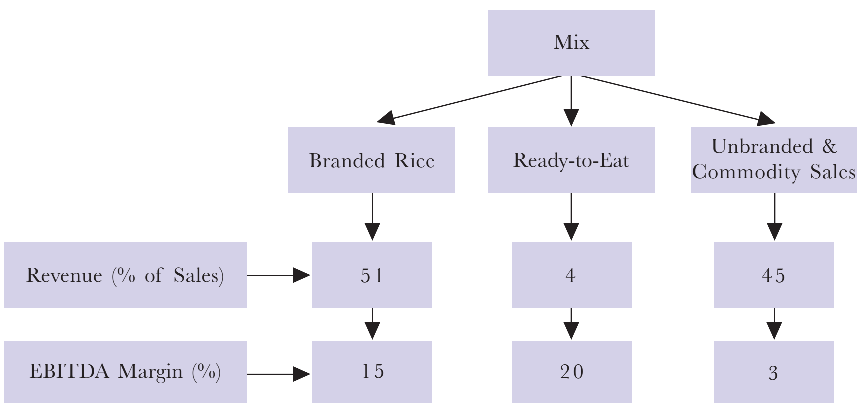
% of branded sales



Source: Company

Note: Others consists of unbranded & commodities (including non-branded rice).

Business mix



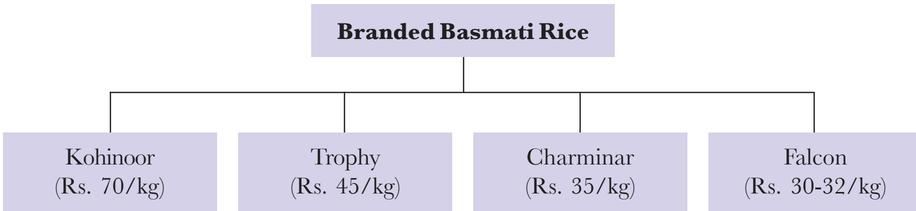
Source: B&K Research

Branded rice

Higher disposable incomes and changing taste to derive demand

Branded rice division of the company mainly comprises of branded basmati rice. Overall, it contributes 51% of the total revenue and 15% of EBITDA margin. The demand for the basmati rice is increasing due to the consumer's taste and increase in their disposable income. Due to these factors a shift in the preferences is seen resulting in higher demand for the company's products in the domestic market. KFL in addition to Kohinoor has other brands, like **Trophy, Charminar, Rose and Falcon** severing to diverse customer base.

Major brands and prices



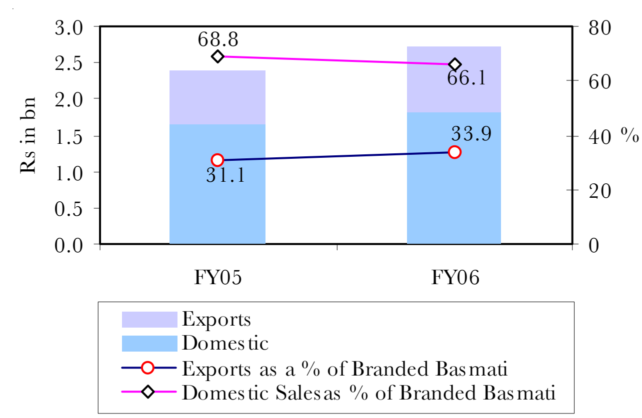
Source: Company

66% revenues obtained from domestic market in rice segment

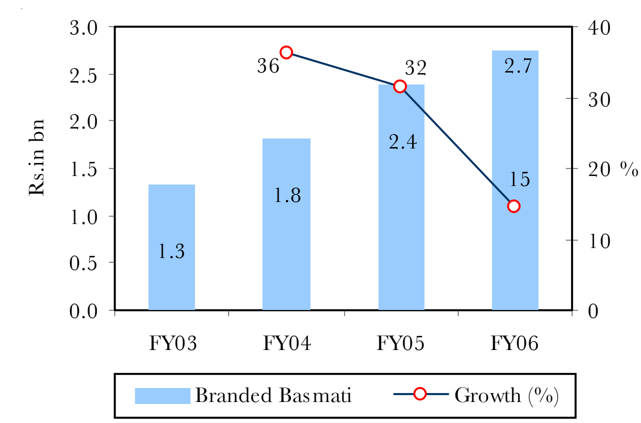
The company's branded basmati sales increased by 14.7% y-o-y to Rs. 2.7 bn in FY06 compared to Rs. 2.4 bn in FY05. Out of this, 66% is obtained from domestic market and rest form export market. The domestic and export market for branded basmati rice increased by 10% to Rs. 1.8 bn and 25% to Rs. 929 mn, respectively, in FY06.

With the increase in the distribution network and strong brand presence in the market, KFL expects to increase its total market share in the domestic branded basmati share from 38% to 42% by FY09. And also expects to take it to 60% in FY09 from 52% (December 2005) in the modern retail format in the domestic market.

Total branded sales



Branded basmati sales and its growth



Source: Company

Ready-to-Eat (RTE)

This segment consists mainly of ambient, frozen and chilled foods. This segment has grown at a CAGR of 111% between FY03-06

Capacity for ambient food increase from 50,000 pouches to 1 lacs pouches

The company ventured into RTE foods in FY04 in both domestic and overseas markets through ambient food. This segment has tremendous opportunities and has grown from Rs. 91 mn (FY05) to Rs. 224 mn (FY06) i.e. a rise of almost 143%. The company expects its food business to contribute 15% of its turnover by FY09, due to onset of modern retail chains in India coupled with the lifestyle change. Capacity for ambient food is 50,000 pouches at its Bahalgarh plant which is expected to increase to 1,00,000 pouches by the end of FY08. KFL has set up the frozen food facility with the capacity of 20 TPD which will further add the revenues from this division in coming years to come.

Food business

Ready-to-Eat (RTE)

Ambient Food (Ventured in FY04) | Frozen food (Ventured in FY07) | Chilled Foods (Plans to enter)

Ambient Food:

- Heat & Eat Curries
- Rice Treat- Microwaveable rice
- Rice & Curry- Ready meals
- Cooking Sauces
- Cooking Pastes
- Chutney
- Spices powder
- Whole spices
- Seasonings

Frozen food:

Gourmet ready meals:

- Snacks (cocktail samosas, aloo bonda, paneer tikka, idli, medu vada, Punjabi samosas, seekh kebab, shami kebab, vegetable pakora, etc.).
- Indian breads (aloo paratha, paneer parathas, peas parathas, plain naans, garlic butter naan, amritsari kulchas, peshawari naan, etc.).
- Ready meals (Hyderabadi vegetables biryani, paneer tikka biryani, Madurai lemon rice, Chinese fried rice and soya keema biryani)
- Curries (peshawari dal makhani, mutter paneer, palak paneer, mumbai pav bhaji).
- Cut vegetables (all sorts of pre cut vegetables).

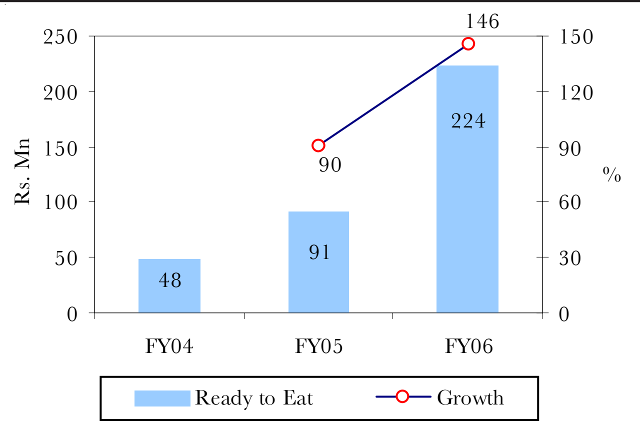
The company has dispatched its 1st consignment of two shipment one each to Singapore and Mauritius in the 2nd quarter of FY07. It is further expected to have shipment of frozen foods to 8-10 countries by the end of FY07.

Commodity and unbranded sales

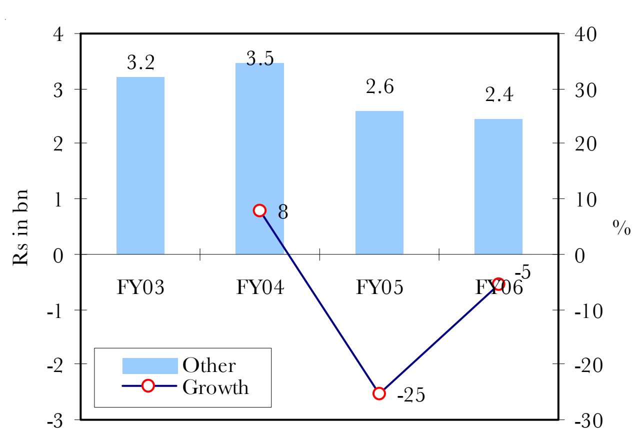
Reduced focus on commodity segment

KFL also deals in commodity and unbranded products. The major portion includes non-branded basmati and non-basmati rice. Company is supplying these articles to certain dealers who in turns supply the same to consumers. KFL is reducing its focus from this segment though has large contribution in the topline because it contains very low EBITDA margins of 3%. It has been reduced by 4.3% from Rs. 2.6 bn in FY05 to Rs. 2.5 bn in FY06. Commodities include pulses, namkeen, spices, wheat and flour.

Revenues from Ready-to-Eat and its growth (%)



Revenues from others and its growth



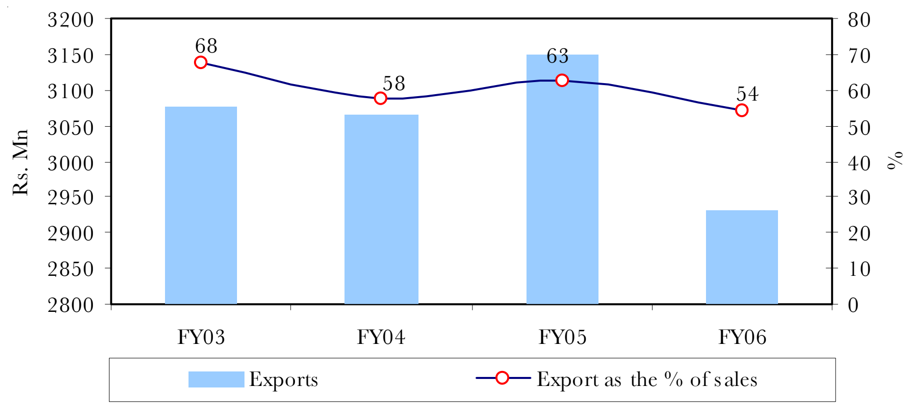
Source: Company

Exports

Avaliable in more than 60 countries

KFL export revenue is around 55% amounting to Rs. 3 bn. The products of the company are available in more than 60 countries including Canada, Singapore, South Africa, UK and USA, through its distribution network. KFL forayed into new markets such as Australia, China, Iran and Japan for expanding its reach in the global markets.

Exports and exports as % of sales



Source: Company

Saudi Arabia – Largest market for basmati at Rs. 30 bn

Rice: KFL has entered the key market for Indian basmati rice which is said to be Middle East (Saudi Arabia in specific) because of huge demand and higher price realisations as compared to the other markets. The export of basmati rice from India to Saudi Arabia is estimated to be around 65% of the total basmati rice exports. The market size of Indian basmati rice in Saudi Arabia is around 6 lacs tonnes valuing Rs. 30 bn. The company is also exporting its products in UK, USA, and South Africa.

Planning for chilled food plant at UK

RTE: KFL is exporting its good of this segment to countries like UK, US, South Africa, Japan and Australia. The company is planning to setup a chilled food plant in its existing facility in UK (which has sufficient space for expansion) by FY08, as the same is expected to be one of the largest markets for chilled food. The chilled food market is expected to be 2 times bigger than that of the frozen food market which in turn is 4 times bigger than that of the ambient food market.

Food industry

RTE expected to post a CAGR of 22% between FY06-10

The Global Food industry is estimated to be a US$ 5 trillion market of which 80% is contributed by processed foods i.e. around Rs. 180 trillion, out of which, RTE food is estimated to be around Rs. 4.5 bn consisting of Rs. 0.5 bn, Rs. 1.6 bn and Rs. 2.4 bn for ambient, frozen and chilled food, respectively. This market is expected to post a CAGR of 22% between FY06-10 and will be around Rs. 9.9 bn.

India is the 2nd largest producer of both vegetables (99 mn tonnes) and fruits (50 mn tonnes) after China and Brazil, respectively. The total Indian food retail sales and sales of microwaveable rice in UK in 2005 was around Rs. 40 bn and Rs. 4.3 bn, respectively, with the sale of microwaveable rice expected to grow further by 35% annually. The domestic market of the same is expected to be around US$ 25 mn in FY08 and Rs. 5 bn by FY09 with a CAGR of around 100% in the next three years. McKinsey has estimated the RTE market in India to post a CAGR of around 200% over the next two years.

Future plans

- KFL plans to increase it existence in 7 and 30 new countries by FY07 and FY09, respectively.
- It also plans to add 60 Stock Keeping Units (SKUs) from the present level of 150 SKUs by FY08 with the expansion of its capacity for ambient food to 75,000 meals per day.
- The company is focusing on food service and is in talks with major player for tie-up arrangements like:

Agreements

Arrangements with	Papa John	Emirates Flight Catering, Dubai	Barista	Costa Coffee	Oberoi Flight Services
For	Frozen Soups	Sauces	Ambient Pastas	Extension as a commissary	Indian snacks for international flight catering

- It is also planning to enter into new markets for further penetration in mainstream retail chains like:
  - Morrissons, Sainsbury and Waitrose (UK).
  - Target (UK).
  - NETTO (Holland).

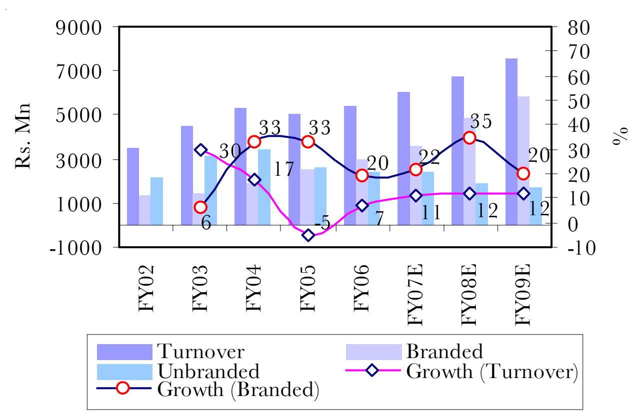
It is also in talks with large players like S&A Foods and Gazebo in UK and Sunrise in Australia for strategic tie-up.

Financial analysis

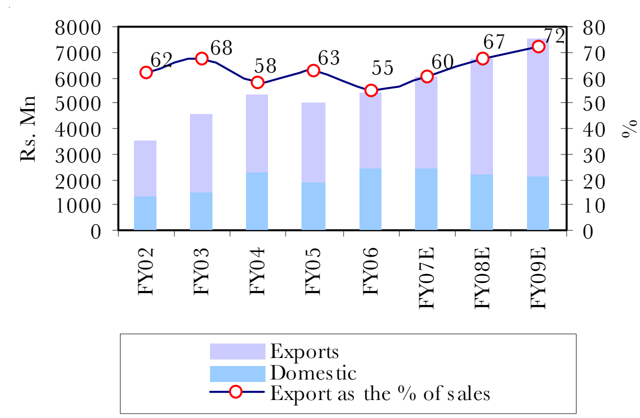
Revenues

- The net sales of the company were Rs. 5.4 bn in FY06, an increase of 7.3% over FY05. The same is expected to be around Rs. 7.5 bn by FY09E at a CAGR of 11.7% for FY06-09E. The expected revenues will be achieved on account of revenues from new geographical regions such as Saudi Arabia and from new product segment of frozen foods.
- Branded sales contributed almost 55% of the total revenues for FY06 as against a share of 35% in FY05. The same is expected to increase to 78% by FY09E. The CAGR growth is expected to be 25.3% between FY06-09E. Higher sales of branded products are expected on account of increase in sales from branded basmati rice and increase sales from European markets.
- Though, the company has reported a decline in export revenues by 6.9% at Rs. 2.9 bn for FY06 as against Rs. 3.2 bn for FY05 the same is expected to improve on account of increase in exports of branded foods consisting of basmati and frozen foods. It is expected that the contributions from export will be around 72% by FY09E. The decline in export revenues was on account of shift in focus from commodity business to branded food business. The commodity business contributed the maximum sales in the total revenues of the company until FY05.

Turnover and Growth



Exports and % of sales for exports



Source: Company

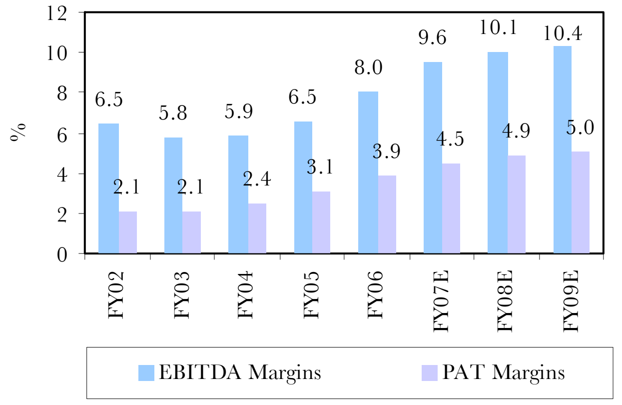
Margins

- The EBITDA margin of the company increased from 6.5% in FY05 to 8% in FY06 on account of favourable product mix shift and is expected to be 10.4% by FY09E.
- The net profit increased from Rs. 155 mn in FY05 to Rs. 208 mn in FY06, a growth of 34.4% on account of increase in branded business. The growth in CAGR between FY06-09E is expected to be 22%.
- The net margin increased from 3.1% in FY05 to 3.9% in FY06 and is further expected to improve to 5% by FY09E.

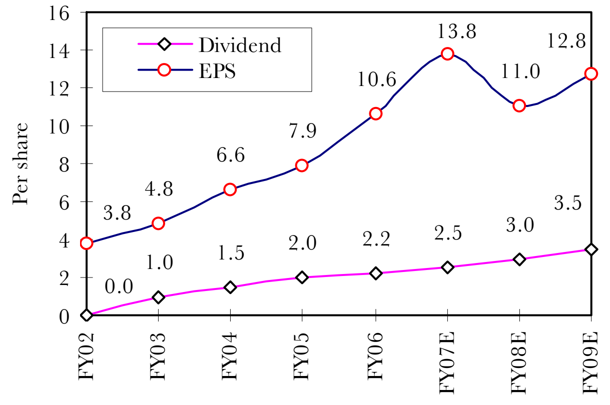
Investor returns

- The reported EPS for FY06 was Rs. 10.6 as against an EPS of Rs. 7.9 for FY05. The EPS for FY09E is expected to be Rs. 12.8. CAGR in EPS between FY06-09E is expected to be 6%.
- The RoE has increased by 310 bps from 15.4% in FY05 to 18.5% in FY06 and is further expected to improve to 14.3% by FY09E.

EBITDA and PAT margins



EPS and DPS



Source: Company

Financial highlights (9 Monthly)

(Rs. mn)	3QFY06	3QFY07	YoY (%)	9MFY06	9MFY07	YoY (%)
Net Sales	**1,404**	**1,816**	**29.3**	**3,344**	**4,142**	**23.9**
EBITDA	**136**	**186**	**36.9**	**354**	**422**	**19.2**
EBITDA Margins (%)	9.7	9.7	–	10.6	9.6	–
Other Income	9	5	(43.3)	17	17	(1.2)
Interest	(52)	(55)	6.1	(112)	(140)	25.4
Depreciation	(30)	(30)	0.0	(60)	(73)	20.8
PBT	62	105	68.6	199	226	13.5
Tax	(8)	(25)	233.3	(33)	(48)	46.2
Adjusted PAT	**55**	**80**	**46.2**	**167**	**178**	**7.1**
PAT Margins (%)	3.9	4.2	–	5.0	4.0	–
EPS (Rs.)	2.8	4.1	–	8.5	9.1	–

Detailed financials

Income Statement

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Net sales	**4534**	**5316**	**5036**	**5399**	**6011**	**6712**	**7515**
Growth (%)	29.6	17.2	(5.3)	7.2	11.3	11.7	12.0
Operating expenses	4273	5004	4708	4966	5436	6037	6737
% to net sales	30.6	17.1	(5.9)	5.5	9.5	11.1	11.6
Raw material cost	3438	4165	3926	4055	4403	4834	5298
RM as % of cost	80.5	83.2	83.4	81.6	81.0	80.1	78.6
RM as % of Net sales	75.8	78.4	78.0	75.1	73.2	72.0	70.5
Packing material consumed	140	158	159	198	217	251	312
% of Net Sales	3.1	3.0	3.2	3.7	3.6	3.7	4.1
Employee expenses	44	53	61	86	120	134	158
% of Net Sales	1.0	1.0	1.2	1.6	2.0	2.0	2.1
Power & Fuel	52	62	69	72	72	81	94
% of Net Sales	1.2	1.2	1.4	1.3	1.2	1.2	1.3
Selling & Distribution exp.	347	384	301	355	391	470	571
% of Net Sales	7.7	7.2	6.0	6.6	6.5	7.0	7.6
Administrative expenses	67	92	94	103	120	134	150
% of Net Sales	1.5	1.7	1.9	1.9	2.0	2.0	2.0
Other expenses	185	91	98	97	113	134	154
% of Net Sales	4.1	1.7	1.9	1.8	1.9	2.0	2.1
EBITDA	**261**	**311**	**328**	**433**	**575**	**675**	**778**
EBITDA Margin (%)	5.8	5.9	6.5	8.0	9.6	10.1	10.4
Depreciation	42	52	58	83	105	142	164
Other income	55	35	46	29	25	21	16
EBIT	**274**	**295**	**316**	**379**	**495**	**553**	**630**
Interest paid	163	121	101	102	133	113	125
Pre-tax profit (before non-recurring items)	111	174	215	277	361	440	505
Pre-tax profit (after non-recurring items)	111	174	215	277	361	440	505
Tax (current + deferred)	16	45	60	69	92	113	127
Net profit	**95**	**130**	**155**	**208**	**270**	**327**	**377**
PAT Margin (%)	2.1	2.4	3.1	3.9	4.5	4.9	5.0

Balance Sheet

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Current assets	3054	3068	3656	4479	4801	5344	6116
Investments	65	65	129	207	207	207	207
Net fixed assets	341	404	447	568	565	724	616
Total assets	**3461**	**3537**	**4232**	**5254**	**5573**	**6274**	**6939**
Current liabilities	149	233	471	488	583	765	880
Total Debt	2440	2327	2665	3553	3556	2982	3270
- Short term	53	19	18	30	35	38	40
- Long term	2387	2308	2647	3523	3521	2945	3230
Other non-current liabilities	27	31	37	30	25	23	20
Total liabilities	**2616**	**2592**	**3172**	**4070**	**4164**	**3770**	**4170**
Share capital	196	196	196	196	196	296	296
Reserves & surplus	657	754	864	1023	1241	2229	2490
- Retained Earnings	657	754	864	1023	1241	2229	2490
Less: Misc. expenditure	(8)	(4)	0	(35)	(28)	(21)	(17)
Shareholders' funds	845	945	1060	1184	1410	2504	2769
Total equity & liabilities	**3461**	**3537**	**4232**	**5254**	**5573**	**6274**	**6939**
Capital employed	**3311**	**3303**	**3761**	**4767**	**4991**	**5509**	**6059**

Cash Flow Statement

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Pre-tax profit	111	174	215	277	361	440	505
Depreciation	41	46	48	70	93	132	155
Chg in working capital	(523)	34	(432)	(616)	(469)	(501)	(793)
Total tax paid	0	0	0	0	(47)	(51)	(88)
Cash flow from oper. (a)	**(370)**	**254**	**(170)**	**(269)**	**(61)**	**21**	**(222)**
Capital expenditure	(100)	(108)	(91)	(190)	(90)	(290)	(47)
Chg in investments	(13)	0	(64)	(77)	0	0	0
Other investing activities	(0)	(0)	0	(0)	5	12	2
Cash flow from inv. (b)	**(113)**	**(108)**	**(155)**	**(268)**	**(85)**	**(278)**	**(45)**
Free cash flow (a+b)	**(483)**	**146**	**(325)**	**(537)**	**(147)**	**(257)**	**(267)**
Equity raised/(repaid)	4	4	4	(35)	7	857	3
Debt raised/(repaid)	487	(113)	338	888	3	(574)	287
Dividend (incl. tax)	(7)	(22)	(33)	(45)	(49)	(56)	(101)
Cash flow from fin. (c)	**484**	**(131)**	**309**	**809**	**(39)**	**227**	**190**
Net chg in cash (a+b+c)	**1**	**15**	**(16)**	**272**	**(186)**	**(30)**	**(77)**

Kohinoor Foods

Income Statement

Yr. ended 31 Mar. (Rs. mn)	FY06	FY07E	FY08E	FY09E
Net sales	5,399	6,011	6,712	7,515
Growth (%)	7.2	11.3	11.7	12.0
Operating expenses	(4,966)	(5,436)	(6,037)	(6,737)
Operating profit	433	575	675	778
EBITDA	**433**	**575**	**675**	**778**
Growth (%)	32.0	32.7	17.3	15.3
Depreciation	(83)	(105)	(142)	(164)
Other income	29	25	21	16
EBIT	**379**	**495**	**553**	**630**
Interest paid	(102)	(133)	(113)	(125)
Pre-tax profit	277	361	440	505
(before non-recurring items)				
Pre-tax profit	277	361	440	505
(after non-recurring items)				
Tax (current + deferred)	(69)	(92)	(113)	(127)
Net profit	**208**	**270**	**327**	**377**
Adjusted net profit	208	270	327	377
Growth (%)	34.4	29.7	21.1	15.5
Net income	**208**	**270**	**327**	**377**

Balance Sheet

Yr. ended 31 Mar. (Rs. mn)	FY06	FY07E	FY08E	FY09E
Current assets	4,479	4,801	5,344	6,116
Investments	207	207	207	207
Net fixed assets	568	565	724	616
Total assets	**5,254**	**5,573**	**6,274**	**6,939**
Current liabilities	488	583	765	880
Total Debt	3,553	3,556	2,982	3,270
Other non-current liabilities	30	25	23	20
Total liabilities	4,070	4,164	3,770	4,170
Share capital	196	196	296	296
Reserves & surplus	1,023	1,241	2,229	2,490
Less: Misc. expenditure	(35)	(28)	(21)	(17)
Shareholders' funds	1,184	1,410	2,504	2,769
Total equity & liabilities	**5,254**	**5,573**	**6,274**	**6,939**
Capital Empolyed	**4,767**	**4,991**	**5,509**	**6,059**

Cash Flow Statement

Yr. ended 31 Mar. (Rs. mn)	FY06	FY07E	FY08E	FY09E
Pre-tax profit	277	361	440	505
Depreciation	70	93	132	155
Chg in working capital	(616)	(469)	(501)	(793)
Total tax paid	0	(47)	(51)	(88)
Other operating activities				
Cash flow from oper. (a)	**(269)**	**(61)**	**21**	**(222)**
Capital expenditure	(190)	(90)	(290)	(47)
Chg in investments	(77)			
Other investing activities	0	5	12	2
Cash flow from inv. (b)	**(268)**	**(85)**	**(278)**	**(45)**
Free cash flow (a+b)	**(537)**	**(147)**	**(257)**	**(267)**
Equity raised/(repaid)	(35)	7	857	3
Debt raised/(repaid)	888	3	(574)	287
Dividend (incl. tax)	(45)	(49)	(56)	(101)
Cash flow from fin. (c)	**809**	**(39)**	**227**	**190**
Net chg in cash (a+b+c)	**272**	**(186)**	**(30)**	**(77)**

Key Ratios

Yr. ended 31 Mar. (%)	FY06	FY07E	FY08E	FY09E
EPS (Rs.)	10.6	13.8	11.0	12.8
EPS growth	34.4	29.7	(19.8)	15.5
EBITDA margin	8.0	9.6	10.1	10.4
EBIT margin	7.0	8.2	8.2	8.4
ROCE	8.9	10.1	10.5	10.9
Net debt/Equity	273.9	243.4	115.3	117.4

Valuations

Yr. ended 31 Mar. (x)	FY06	FY07E	FY08E	FY09E
PER	6.5	5.0	6.3	5.4
PCE	4.7	3.6	4.4	3.8
Price/Book	1.1	1.0	0.8	0.7
Yield (%)	3.2	3.6	4.3	5.1
EV/Net sales	0.9	0.8	0.6	0.6
EV/EBITDA	10.6	8.3	6.3	5.9

Du Pont Analysis – ROE

Yr. ended 31 Mar. (x)	FY06	FY07E	FY08E	FY09E
Net margin (%)	3.9	4.5	4.9	5.0
Asset turnover	1.1	1.1	1.1	1.1
Leverage factor	4.2	4.2	3.0	2.5
Return on equity (%)	18.5	20.8	16.7	14.3

Share Data

Mkt. Cap.	Rs.8.6 bn (US$ 196 mn)
Price	Rs. 193
Target Price	Rs. 145
BSE Sensex	12886
Reuters	REAG.BO
Bloomberg	REIA IN
Daily Volume	US$ 2.6 mn (Rs. 115.1 mn)
52-week High/Low	Rs. 216/59
Issued Shares	45 mn

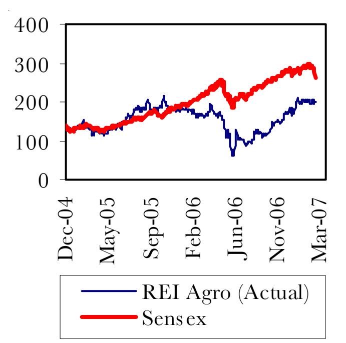
Valuation Ratios

Year to 31 Mar.	2008E	2009E
EPS (Rs.)	17.0	21.0
+/- (%)	9.9	23.4
PER (x)	11.3	9.2
PBV (x)	1.6	1.4
Dividend/Yield (%)	1.4	1.4
EV/Sales (x)	1.6	1.5
EV/EBITDA (x)	8.2	7.3

Shareholding Pattern (%)

Promoters	43
FIIs	8
ADRs/GDRs/Other Foreign	12
Institutions	5
Public & Others	32

Relative Performance



REI Agro

Sell

Cultivating brands

REI Agro has emerged as the leading basmati rice processor in India and is enhancing its capacities to cater the growing demands in the market, particularly from modern retail stores and exports. Its product range varies from premium to popular to mass consumption products. The company is taking active steps to increase market share through branding and marketing exercises. We are initiating coverage with a Sell in the light of expensive valuations.

Year to March	FY06	FY07E	FY08E	FY09E	CAGR (%)
P&L data (Rs. mn)					**(FY06-09E)**
Net Sales	9,440	9,315	10,713	12,476	9.7
Operating Profit	1,340	1,428	1,671	1,971	13.7
EBITDA	1,487	1,793	2,114	2,584	20.2
Net Profit	660	694	809	997	14.7
Margins (%)					
Operating Profit	14.2	15.3	15.6	15.8	–
EBITDA	15.5	18.5	19.0	19.7	–
Net Profit	7.0	7.4	7.5	8.0	–
Balance Sheet Data (Rs. mn)					
Total Assets	11,790	14,304	16,382	19,217	17.7
Shareholders' Funds	3,259	4,790	5,883	6,730	27.3
Per Share Data (Rs.)					
EPS	17.0	15.5	17.0	21.0	7.3
CEPS	19.4	18.8	20.9	26.2	10.5
Dividend	2.3	2.5	2.8	2.8	6.5
Returns (%)					
RoE	26.8	17.2	15.2	15.8	–
RoCE	15.3	13.1	13.0	13.5	–

- The company is now focusing more on branding of its own products as compared to trading the products. The company products are available in the range of Rs. 7-77/kg for mass, popular and premium segments.
- With an expansion of business portfolio in the retail segment, the company expects to increase its topline and improve margins. It plans to start with presence of retail chains in the NCR region before moving to a pan-India reach.
- At the current market price of Rs. 193, the stock is trading at 12.5x FY07E, 11.3x FY08E and 9.2x FY09E earnings. We believe the stock is expensive and the fair value at 8.5x FY08E EPS of Rs. 17 should be Rs. 145. We initiate coverage with a Sell.

Investment arguments

REI Agro has achieved the leadership position in the rice industry in a short span of time. Since its inception it has been a dividend paying company and has therefore given its investors, an adequate return on their investments along with capital appreciation.

Overall growth

- **Business mix complement each other**

De-risking the porfolio

The diversification into wind energy will help the company to de-risk its dependence on a single business of basmati rice. Wind farms not only contribute to the bottomline but generate free cash flows that can be used for working capital requirement in basmati rice business thus, improving the operating margin of the company. Wind Energy generation is a stable business, requiring no fuel; also the cost of the plant is frozen at the time of the project commissioning, secured by the power purchase agreement even before actual sales. This is exactly the same in basmati rice business, which also enjoys stable paddy prices. Both businesses are fragmented with the a few large and focused players.

- **Shift from unorganised to organised**

There is a continuous shift of market share from unorganised to organised players as these big players offer quality products at affordable prices. This trend is expected to benefit the company in the form of increased revenues.

Basmati rice growth

- **Capacity expansion**

Planning to increase the capacity from 61 TPH to 90 TPH by FY09

REI has total production capacities of 61 TPH and 32 TPH for basmati and parboiled rice, respectively, in Bawal (Haryana). The capacity utilisation of the plant is expected to be 74% and 76% by the end of FY07E and FY08E, respectively. The company has utilised 73% of the total capacity in FY06. This huge scale of operations would further strengthen REI's competitive advantage through increased economies of scale. The company is planning to have a total capacity of 90 TPH by FY09.

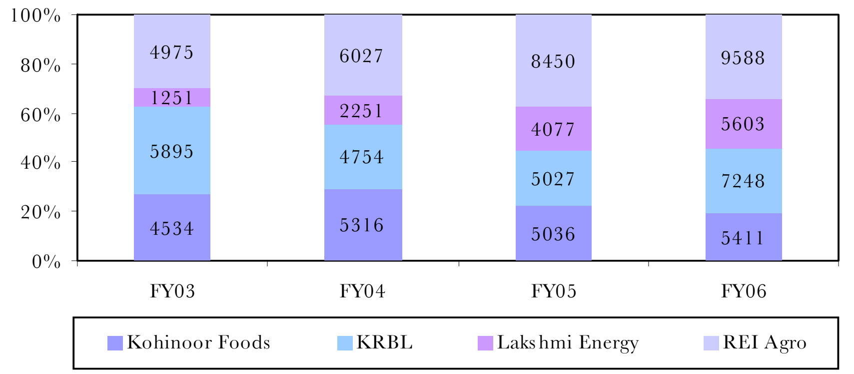
- **Second largest processor of basmati rice**

2nd to KRBL in terms of capacity

REI processes 61 TPH of basmati rice, making it the second largest processor after KRBL (81 TPH). It captures 20% of the total basmati rice market in terms of sales and processes 14% of total production in India. REI is further expected to maintain such position mainly on account of the huge demand of the branded basmati rice both in domestic and export markets.

Among the 4 major organised players (Kohinoor Foods, KRBL, Lakshmi Energy and REI), REI's revenues are the highest.

Comparative sales



Source: Company

Targeting on all the segments of the society

- **Focusing on the branded segment**

  The company is focusing on high margin branded rice segment. REI Agro initially embarked upon a low-cost approach in this regards and targeted the mass and popular market segments in the first leg. The company's contribution from branded sales is expected to go up to 48% by FY09E. Economy segments have the brands like **Hansraj & Raindrop** followed by the **Mr. Miller & Hungama** in midrange and **Kasauti & Real Magic** in premium segment. The product portfolio consists of broken, branded, unbranded and parboiled rice at the selling prices of Rs. 19, Rs. 46, Rs. 44 and Rs. 23/kg, respectively.

Parboiled rice has huge potential in export market

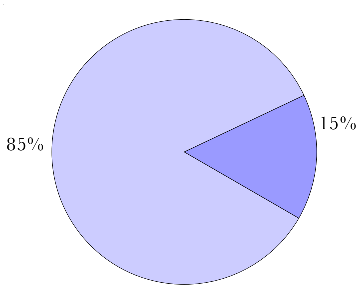
- **Parboiled rice milling to boost exports realisation**

  The company commissioned one of India's largest parboiling facility in January 2005 in Haryana with an aggregate capacity of 230,000 TPA. Parboiled rice has a huge demand in the Middle East markets. It contributed 10% of the exports revenue in FY06.

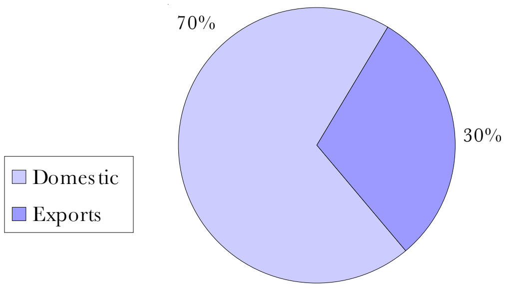
  Export market contributed around 15% of the total revenue in FY06 which grew by 42% from Rs. 838 mn in FY05 to Rs. 1,443 mn in FY06 and is further expected to grow to 30% in FY09. The yield or recovery rate from parboiled rice is high at around 61% as compared to raw rice which yields only 44% of the total paddy. This high recovery rate ultimately contributes in the form of improved bottomline even though the realisations may be lower.

Export sales

FY06



FY09E



Source: Company

- **Yield enhancement**

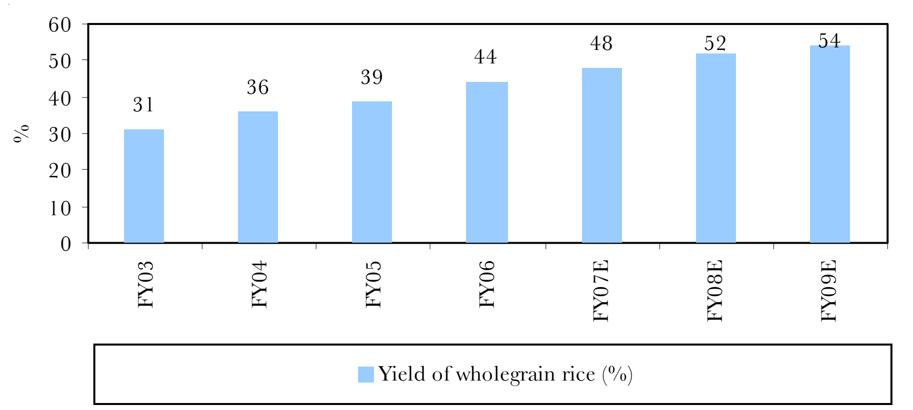
The company has been able to control proportion of broken rice, thereby increasing full rice recovery. Full rice is sold in the market at a premium of nearly 100 % over broken rice.

The company has increased the ageing period from 5.8 months in FY05 to 8.1 months in FY06, which resulted in an improvement in the yield of rice from 39% in FY05 to 44% in FY06 and would further increase up to 54% by FY09.

Ageing improves the quality and realisation of rice

REI has an expertise in purchasing the right quality paddy and ageing it for the desired period (expects to increase it to 14 months in the coming years). The company is making deliberate effort to reduce the distributor's role in ageing of basmati; the entire ageing cycle would be done by the company. The increase in the ageing period from 8 to 14 months needs high inventory level and additional working capital requirement. It becomes positive for the company, as it has the ability to raise working capital loans cheaper than its distributors and hence, benefit from such initiative.

Yield enhancement



Source: Company

Power generation growth

- **Wind farm business**

Wind energy business hold immense potential in India, as it is the cheapest source of power. Wind energy is a free and renewable energy resource and has low gestation period of mere three-six months compared to gestation period of a couple of years for a thermal power plant. REI has the total installed capacity of 35.9 MW and plans to install another 10 MW plant in March 2007 in Gujarat with the capex of Rs. 550 mn. Operating margin from the wind energy business was 85% in FY05 and 95% in FY06 with the further expansion in the wind farm these levels will continue to remain the same. The units generated from the wind farm fetch carbon credit and 50,000 Certified Emission Reduction (CER) have been credited to the Rajasthan plant and the same for Maharashtra plant has been initiated. Wind farms also give the advantage of depreciation claims and income tax benefits on income generated from the business. The company hasn't accounted for CER credits as intangible assets in its books as it plans to book the same on cash basis. The CER rate is expected to improve drastically in the future.

Total installed capacity of 35.9 MW

Other strengths

- **Distribution network**

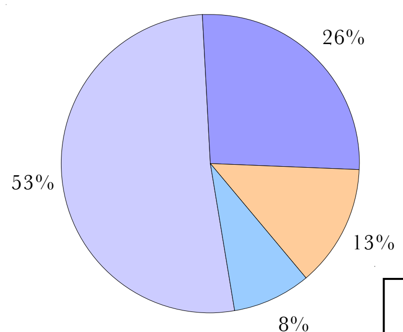
Focusing on strengthening the distribution network

REI's distribution network involves 435 distributors and retail reach of over 1 lac outlets. The company's efforts to reduce dependence on select channels and thereby reducing risk of concentrated sales. The company has tied up with 3 large trading houses (Baba Kher, Al-Muhaidi and Umar-Kasam) in Middle East which consumes 65% of India's basmati exports.

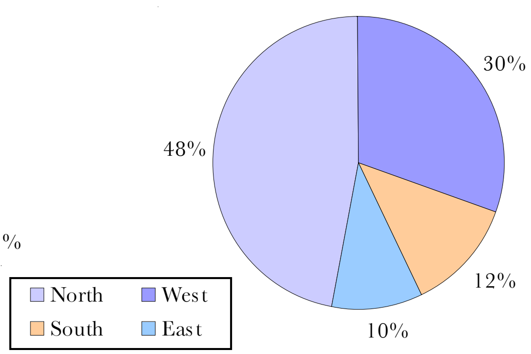
Distribution breakup – Region-wise

Region	FY03	FY04	FY05	FY06
North	192	204	230	206
South	27	31	38	53
East & Central	23	27	30	44
West	62	70	92	132
Total	**304**	**332**	**390**	**435**

Region-wise – Sales



Distributors

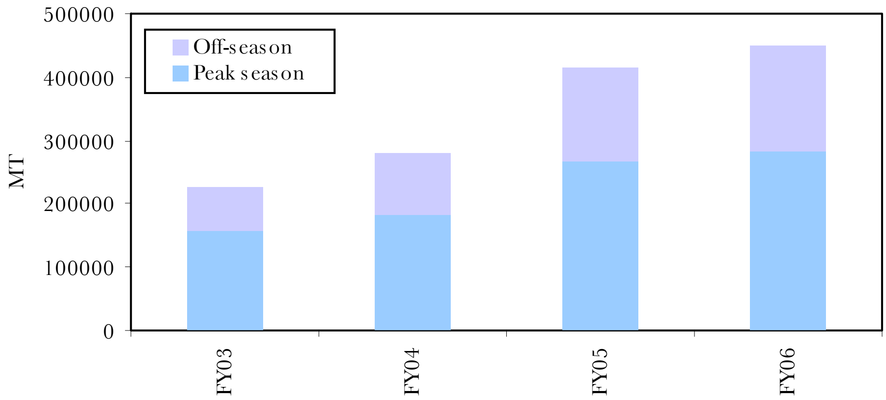


Source: Company

- **Preferred buyer status**

REI enjoys presence in 130 organised government-controlled grain markets (mandis) in India out of a total of 200 in the basmati belt (northern India) through its trained middlemen (pukka atriyas). This enables it to monitor paddy quality and prices. It purchases large quantities of paddy and makes upfront payment. This grants the "preferred buyer status" to the company.

Procurement of raw material



Source: Company

- **Subsidiary formation**

Going into retail with its own subsidiary

The company intends to set up two 100% subsidiary companies namely **REI Retail Limited** and **REI Foods And Beverages Limited.**

REI Retail Limited would focus on the market currently being addressed by India's unorganised retail sector by setting up neighbourhood convenience stores having an area of around 2,000 sq.ft. each across North India in FY07. Through REI Foods And Beverages Limited, the company plans to acquire assets of a reputed juice manufacturer based in Western India, to enter the growing food and beverages sector which would also complement its retail business which is in the pipeline.

Investment concerns

Working capital intensive

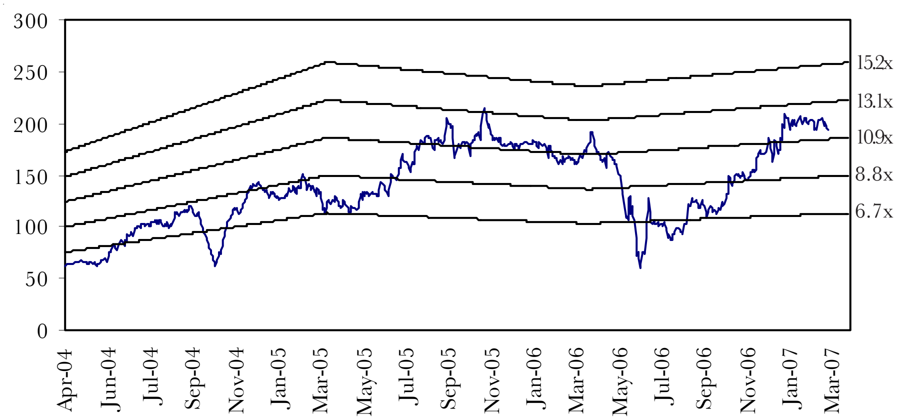
REI has increased the ageing period of inventory to improve the quality of its products which has resulted in higher working capital requirement. The company has to therefore take higher financial leverage to meet its huge working capital requirement resulting into higher finance cost having a negative impact on the bottomline of the company.

Valuations

The company is progressing towards strong growth due to the following factors:

- **Shift towards basmati rice:** The demand for the basmati rice is increasing due to increase in the disposable incomes, changing consumer's preferences and demand for premium products, which will ultimately have positive impact on the company's basmati rice sales.
- **Growth prospects in exports:** India is the world's largest exporter of basmati rice. Middle East remains the major export market for Indian basmati rice and within it, Saudi Arabia accounts for the major chunk of imports from India. REI has entered the export market with parboiled rice which has high demand in the Middle East because of its nutritive values.
- **Wind farm:** The company is also concentrating in the Wind Energy business which has high growth prospective. The cost of wind power generation is the lowest among both renewable and non-renewable power generation source. Revenue has grown by 230% from Rs. 63 mn in FY05 to Rs. 147 mn in FY06. REI is looking forward to invest heavily in wind farm in the coming years as it generates high return.

PER Band



At the current market price of Rs. 193, the stock is trading at 12.5x FY07E, 11.3x FY08E and 9.2x FY09E earnings. We believe the stock is expensive and the fair value at 8.5x FY08E EPS of Rs. 17 should be Rs. 145. We initiate coverage with a Sell.

Business overview

Background

Largest parboiling plant in India

REI Agro Limited was established in 1994 by Mr. Sanjay Jhunjhunwala and Mr. Sandip Jhunjhunwala and became public limited company in 1996. The company has emerged as the leading basmati rice processor and captures 20% total basmati rice market. With the public issue company had started its first rice grading unit at Bawal with a capacity of 73,920 TPA and went into backward integration as rice miller in 1998. REI started branding of broken rice in 2001 with the brands like **Masti** and **Maaza** for mass segment. In 2004, the company set up its first wind farm in Rajasthan with the capacity of 7.5 MW, through which the company diversified its product portfolio. It set up a wind farm in Maharashtra with 15.8 MW and augmented it to 22.4 MW.

The company has constructed one of the largest parboiling plants in India with the total capacity of 32 TPH. With the modest beginning, the company has become the largest processor in the industry in a short span of 12 years with a total installed milling capacity of 49 TPH which increased to 61 TPH in September 2006.

Success path

Phase (Years)	Events	Conclusion
I – 1994-96	- Incorporation	10 TPH
II – 1996-02	- Rice Grading Unit (Bawal)	Rs. 72.5 mn
	- IPO	
	- Backward integration to rice milling	
	- Capacity expansion	15 TPH
	- Branding of Broken Rice	
III – 2002-04	- Capacity expansion	12 TPH
	- Bonus issue	1:1
	- Emerged as the largest processor in the world	For Basmati Rice
	- Introduced products in different segment	Branded Products
	- Wind farm in Rajasthan	7.5 MW
IV – 2004-06	- Parboiled facility	0.24 mn tonnes/annum
	- Wind farm in Maharashtra	12.5 MW
	- FCCB issue	US$ 32.2 mn
	- Expansion of wind farm capacity in Maharashtra	9.9 MW
V - 2006 & beyond	- GDR issue	US$ 30.2 mn
	- Expansion of milling capacity	24 TPH {12TPH each in Feb & Sep. '06}
	- Capacity in Tamil Nadu	6 MW

Management

Mr. Sanjay Jhunjhunwala, CMD is the promoter of the company, largely responsible for its growth in operations since inception and also being the driving force behind building the export market.

Mr. Sundip Jhunjhunwala, Vice-Chairman and Managing Director, is the co-promoter of the company. He oversees the overall operational activities.

Equity history (Nos. mn)

Duration	Issued capital	Increase	Face value (Rs.)	Particulars
1996	4.4	–	10.0	
	4.5	0.1	10.0	Issued to government institutions.
02-03	14.8	10.3	10.0	Public issue.
03-04	29.6	14.8	10.0	Bonus issue in the ratio of 1:1.
04-05	33.4	3.8	10.0	Preferential issue.
05-06	38.8	5.4	10.0	Issue of 7.5 mn equity shares against 3.8 mn GDRs. FCCB conversion 1.7 mn. Cancellation of 3.8 mn shares.
06-07	44.8	6.0	10.0	Conversion of FCCB.

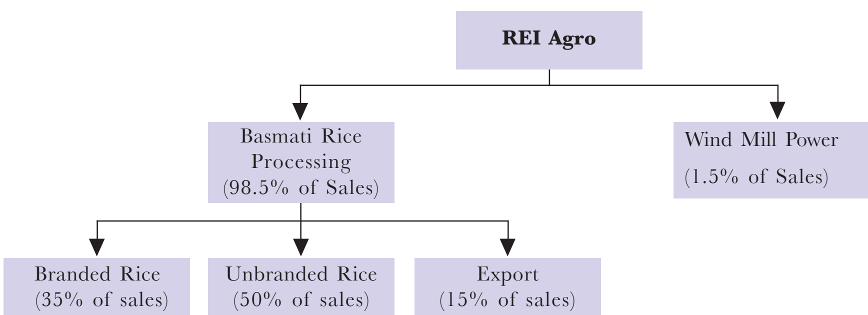
Business segment

REI has two business segments:

1. Rice processing.
2. Wind farm.

Business segments

Complementing business segments



Source: Company

Capacity allocation

Ongoing expansion in windpower generation

Rice: REI has a manufacturing plant for rice processing in Bawal (Haryana) with a capacity of 61 TPH for basmati rice and 32 MTPH for parboiled rice.

Wind power: The company has 3 plants in wind farm generation. It has already installed the 35.9 MW capacity with total capex of Rs. 2 bn approximately. The company is presently installing another 10 MW in Gujarat.

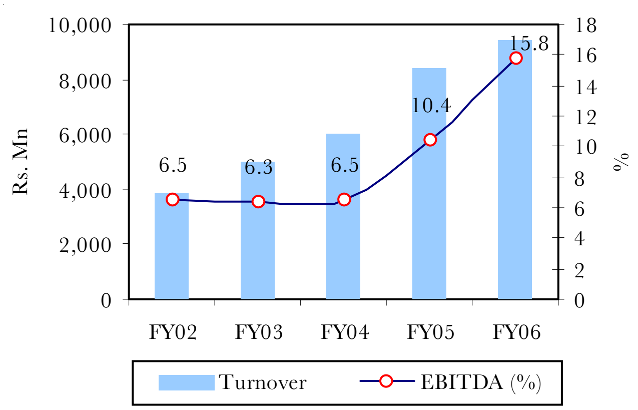
Manufacturing facilities

Location	Nature	Installed capacity
Bawal, Haryana	Rice processing	61 TPH
Jaisalmer, Rajasthan	Wind farm	7.5 MW
Dhule, Maharashtra	Wind farm	22.4 MW
Tamil Nadu	Wind farm	6 MW

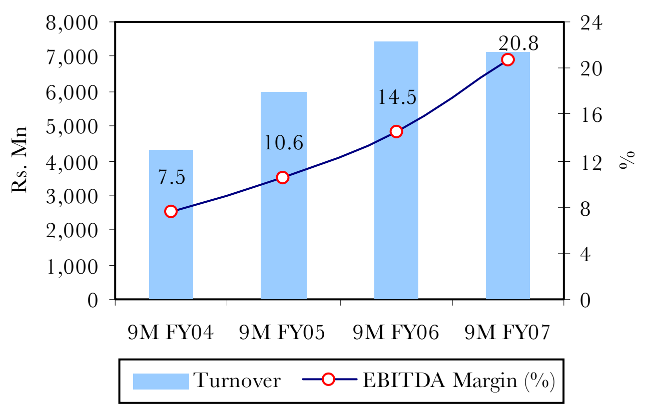
Historical performance

The company's topline and EBITDA has grown at a CAGR of 25% and 55.7%, respectively, for the period FY02-06. The major growth factors have been increased concentration on the branded basmati and low operational cost in wind power generation. Bottomline CAGR of the company was 76.3% for the same period.

Annually



9 Months



Source: Company

Business segments

REI has two segments **Rice** (a part of food processing industry) and **Wind Power Generation.**

Rice

The company mainly deals in branded basmati rice. Rice contributed almost 98.5% in the total revenues of the company and has grown with a CAGR of 23% between FY03-06. Branded rice, unbranded rice and exports have grown with a CAGR of 61%, 5% and 97%, respectively, between FY03-06.

With the further expansion in the production capacity from 49 TPH to 61 TPH at Bawal unit, it will further contribute to the topline.

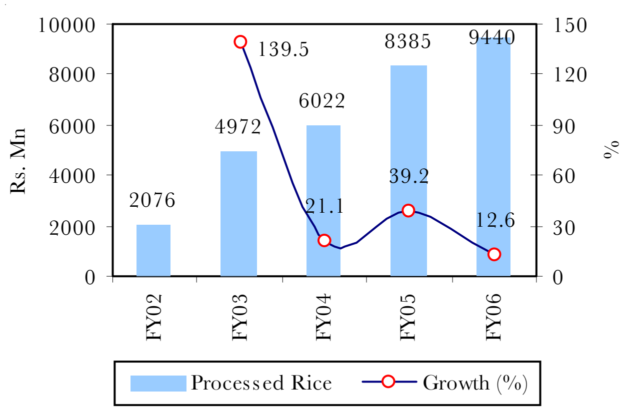
REI has the 32 TPH of capacity for parboiled rice mainly for export purpose. Parboiled rice has a good demand in Saudi Arabia and other gulf countries because of its nutritive value. It grew with a CAGR of 184% between FY02-06 and contributed 15% of the total sales in FY06.

Exports

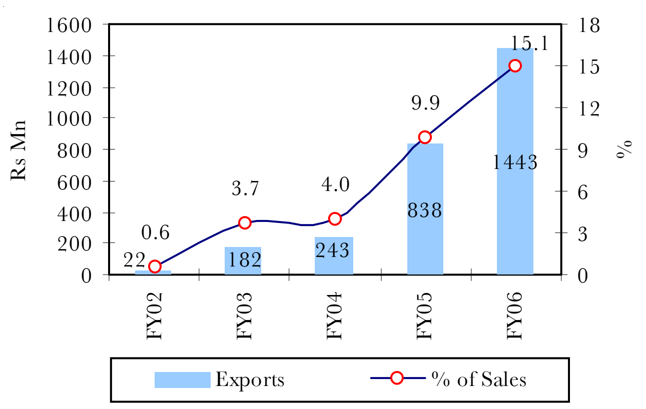
Future in exports

REI has largest facility for parboiled rice. The company has registered significant growth in the export market due to the huge demand for parboiled rice which is expected to increase further. The contribution of parboiled rice and Mr. Miller (a popular brand) in the exports stands around 10% and 5%, respectively. Its export market mainly consists of Saudi Arabia, Dubai, USA and European Union.

Rice – Growth (%)



Export and exports % of sales



Source: Company

Product range

REI Agro Limited has entered the branded market in the year 2001. The company had strategically decided to enter the branding space with the launch of branded broken rice. In fact, the company was the first to start branding of broken rice for the mass brands. It started branding of whole grain in the year 2004. Premium rice **(Kasauti, Real Magic)** represents the highest quality of rice followed by the popular brands. REI has product range according to the purchasing power and preference of the consumer. This helps the company to improve both its revenue and margins. The company's products are available from Rs. 7 to Rs. 77/ kg, while packs are available in sizes ranging from 100 gm to 50 kgs.

The quality of the premium rice is better than that of the popular variety in terms of:

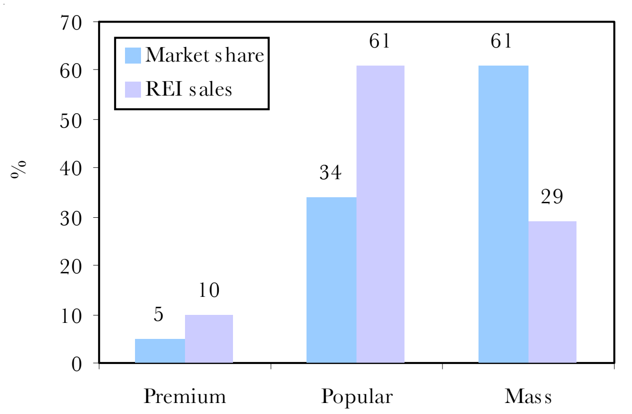
- Longer grain.
- Higher ageing/maturity of the grain.

Brand portfolio (FY06)

Segments	Brand name	Launch date	Retail price (Rs./kg)
Premium	Kasauti	Dec. '04	77
	Real Magic	Nov. '04	70
Popular	Mr. Miller	Apr. '04	62
	Hungama	Apr. '04	55
Mass	Hansraj	Dec. '04	50
	Masti	Apr. '01	7-25*
	Maaza	Apr. '01	7-25*

*Depending on the size of grain.
Source: Company

Sales mix



REI Argo's brand portfolio comprises of Premium, Popular and Mass brands. In Indian market, the consumption pattern for different categories of branded basmati constitutes of 5%, 34%, and 61% in favour of premium, popular and mass brands, respectively. The company's presence can be felt at all the levels of consumption behaviours, due to its superior quality and competitive price range. The proportion of REI's premium segment sales is 10% which is much higher than that of the overall market at 5%.

Wind farm business

Cash flows from wind farm business to help meet the working capital requirment

REI has diversified its portfolio from its existing rice processing business in FY04 through the commissioning of wind power generation in Rajasthan and Maharashtra. The company has a total capacity of 35.9 MW with 7.5 MW, 22.4 MW and 6 MW power generation capacities in Jaisalmer (Rajasthan), Dhule (Maharashtra) and Tamil Nadu, respectively. It contributed Rs. 147 mn in other operating income in FY06 which grew by 133% over Rs. 63 mn in FY05. Operating margin from the wind energy business was 85% in FY05 and 95% in FY06. REI is further expanding its capacity of wind farm by 10 MW in FY07 at a total capex of approximately Rs. 550 mn. The company has extensive plans in wind farm. It plans to increase the installed capacity by 10 MW each year which would drive the growth in margins. The realisation from the power plant is expected to meet the high working capital requirement of rice-processing operations. Though, requiring a huge initial capital outlay, such facility involves only a nominal working capital for its day-to-day operations and is a source of consistent fast cash inflows.

Selling agreements

State specific agreement

The company has signed a Power Purchase Agreements (PPA) with the Maharashtra Electricity Development Authority (MEDA) for 13 years from the time of commencement of the project. The rate is Rs. 3.5/KWH with the escalation rate of 15 paisa per unit hike for subsequent years to come. The tariff structure in Rajasthan under PPA is Rs. 3.32/

KWH for the base year in FY05 with a 2% increase per KWH every year on the base year up to 10th year, after this the tariff for remaining 10 years is the 10th year rate. The tariff rate from Tamil Nadu government is Rs. 3.5/KWH.

Major benefits from wind powers project

Tax-free profits

REI is eligible for 100% tax exemption on the revenue earned from the wind farm business. This exemption will be for a period of 15 years of operations, with the company having the choice to select any 10 consecutive years.

Accelerated depreciation

The company has received a depreciation benefit of 80% of the entire costs of the project in the very first year and remaining 20% can be claimed in the next year for computation of taxable income. It is not only for the wind farm business but entity as a whole, thereby, reducing the tax on the profits earned out of the rice business also.

With the combination of above two benefits, the company is able to reduce taxable profits by enhanced depreciation and thus take the advantage of the tax-free benefits.

Wind power capacity, December 2005 (Global)

Country	MW	% share
Germany	18,428	32
Spain	10,027	17
US	9,149	16
India	**4,430**	**8**
Denmark	3,122	5
Total	**59,084**	

Wind power industry

Wind power generation has a tremendous potential for growth in India on account of short gestation period of three-six months for installing wind farm as compared to a larger gestation period for a thermal power plant. It involves higher capital expenditure in the form of cost of land and equipments, were as the operational cost is nominal as it does not require fuel. This form of power generation is pollution free and made available at the cheapest cost as compared to other sources of power generation.

The demand-supply gap for power is currently estimated to be around 40,000 MW and the Central Electricity Authority (CEA) has projected a demand of about 240,000 MW by 2012. As compared to demand, the total capacity is only at 125,000 MW presently; which is expected to augment by at least 10,000 MW per year. With the government initiating the power sector reforms a few years back notably the Electricity Act 2003, there has been a transformation of power sector into competitive market from the traditional monopoly market.

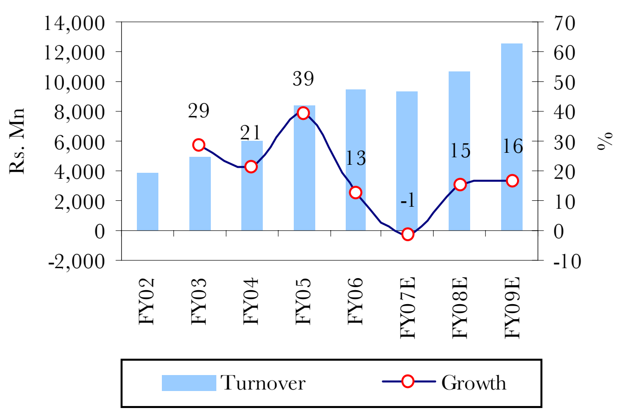
Capacity expansion is imperative in the scenario of a constantly increasing demand-supply gap. The power projects are becoming unviable mainly due to the rising prices of depleting reserves of non-renewable fuels such as oils & natural gas. The Indian government is encouraging the generation of wind farm power projects, by providing significant tax incentives to the companies willing to venture into such projects. As a result, India has emerged as one of the top 5 generators of wind power with around 8% of global market.

Financials

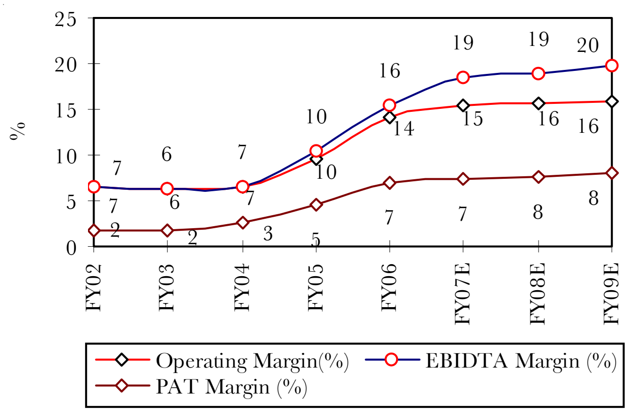
Revenues and earning

REI is expected to post a CAGR of 9.7%, 20.2% and 14.7% for the revenues, EBITDA and PAT, respectively, between FY06-09E. The major factor that has improved the margins is the addition of wind farm into the business which requires a low operational cost and generates high revenue realisation. The company has discontinued the trading business in current year which has contributed approximately Rs. 1.6 bn in revenues in FY06. This would impact the topline in FY07E and it will not show a similar growth. Branded rice portion in terms of sales will further increase which ultimately would improve the EBITDA and PAT levels.

Turnover and Growth



Operating and Net margins

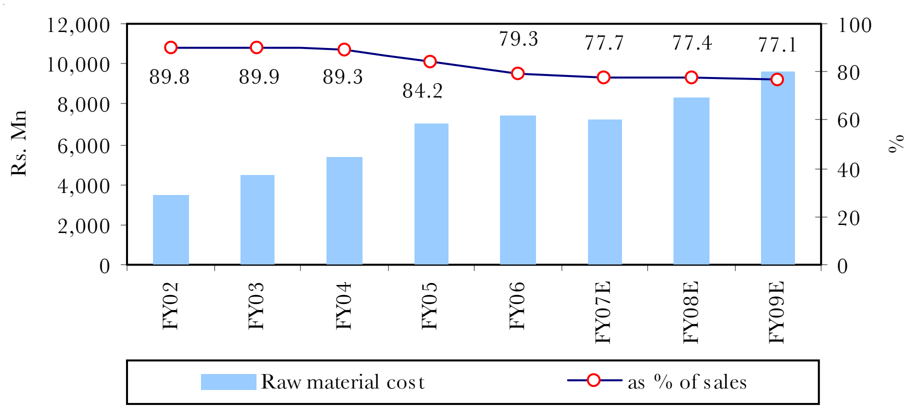


Source: Company

Raw material costs

The major component for rice processing is paddy, and the prices of this largely depend upon the climate conditions of the region. Commodity players have to cope up with raw material prices as they are usually unable to pass on the price changes to the end consumer. Due to larger scale and size, the company has enabled itself to collect a large quantity of quality paddy during the peak season to take the price advantage.

Raw material cost to sales

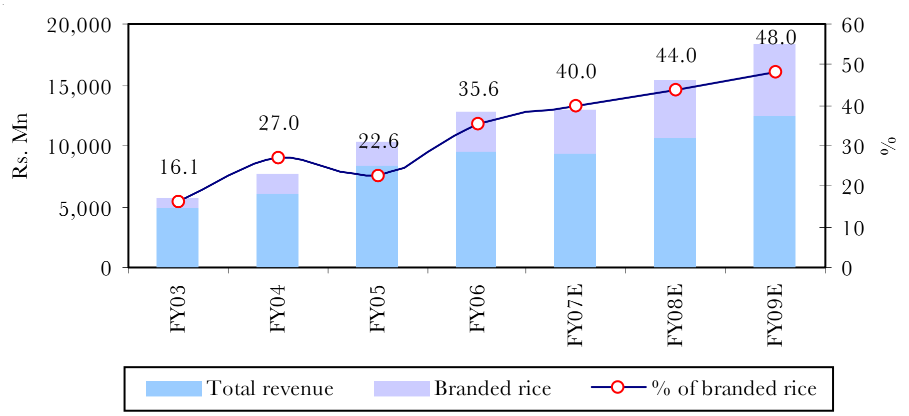


Source: Company

Enhanced branding

Branded rice sale of the company has increased significantly by 77% from Rs. 1.9 bn in FY05 to Rs. 3.4 bn in FY06. The share of branded rice in total revenues was around 36% in FY06 is expected to improve further to 44% and 48% in FY08E and FY09E, respectively. The margins and average realisation from the rice is expected to rise on account of increase in sales of branded products.

Branded sales



Source: Company

Financial highlights (9 Monthly)

(Rs. mn)	3QFY06	3QFY07	YoY (%)	9MFY06	9MFY07	YoY (%)
Net Sales	**1646**	**2317**	**40.8**	**7339**	**6896**	**(6.0)**
Operating Expenses	1284	1798	40.0	6342	5675	(10.5)
Operating Margins (%)	21.9	22.4	–	13.6	17.7	–
Other operating income	2	90	4235.2	84	268	218.4
EBITDA	**363**	**609**	**67.6**	**1082**	**1489**	**37.6**
EBITDA Margins (%)	20.9	25.3	–	14.6	21.3	–
Other Income	0	0	(100.0)	1	0	(86.3)
Interest	(74)	(188)	155.2	(258)	(446)	72.7
Depreciation	(24)	(37)	52.7	(67)	(114)	70.1
PBT	265	384	44.6	758	929	22.5
Tax	(85)	(131)	53.5	(245)	(315)	28.5
Adjusted PAT	**180**	**253**	**40.5**	**513**	**614**	**19.7**
PAT Margins (%)	10.9	10.5	–	7.0	8.6	
EPS (Rs.)	4	6*	–	13	14*	–

*On diluted capital of 44.8 mn shares.

Detailed financials

Income Statement

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Net sales	**4975**	**6026**	**8387**	**9440**	**9315**	**10713**	**12476**
Growth (%)	28.7	21.1	39.2	12.6	(1.3)	15.0	16.5
Operating expenses	4659	5633	7577	8100	7887	9041	10504
% to net sales	93.7	93.5	90.3	85.8	84.7	84.4	84.2
Raw material cost	4342	5336	6211	6205	7235	8296	9619
RM as % of cost	93.2	94.7	82.0	76.6	91.7	91.8	91.6
RM as % of Net sales	87.3	88.5	74.1	65.7	77.7	77.4	77.1
Finished Goods purchased	129	45	855	1280	0	0	0
% of Net Sales	2.6	0.7	10.2	13.6	0.0	0.0	0.0
Employee expenses	46	56	68	78	94	112	129
% of Net Sales	0.9	0.9	0.8	0.8	1.0	1.0	1.0
Power & Fuel	33	40	49	57	61	75	100
% of Net Sales	0.7	0.7	0.6	0.6	0.7	0.70	0.8
Selling & Distribution exp.	60	93	265	280	290	318	376
% of Net Sales	1.2	1.5	3.2	3.0	3.1	3.0	3.0
Administrative expenses	16	22	41	39	36	45	53
% of Net Sales	0.3	0.4	0.5	0.4	0.4	0.4	0.4
Other expenses	34	41	88	161	172	194	227
% of Net Sales	0.7	0.7	1.1	1.7	1.9	1.8	1.8
Operating income	316	394	810	1340	1428	1671	1971
Operating Margin (%)	6.3	6.5	9.7	14.2	15.3	15.6	15.8
Other Operating income (Wind farm)	0	0	63	147	365	443	612
EBITDA	**316**	**394**	**873**	**1487**	**1793**	**2114**	**2584**
EBITDA Margin (%)	6.3	6.5	10.4	15.8	19.2	19.7	20.7
Depreciation	17	21	40	93	151	186	246
Other income	2	2	0	2	2	2	2
EBIT	**301**	**375**	**833**	**1397**	**1644**	**1930**	**2340**
Interest paid	172	144	291	373	562	667	781
Pre-tax profit (before non-recurring items)	128	231	541	1023	1082	1263	1558
Pre-tax profit (after non-recurring items)	128	231	541	1023	1082	1263	1558
Tax (current + deferred)	41	73	163	363	388	455	561
Net profit	**87**	**158**	**379**	**660**	**694**	**809**	**997**
PAT Margin (%)	1.7	2.6	4.5	7.0	7.4	7.5	8.0

Balance Sheet

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Current assets	3,300	4,275	6,866	8,714	10,249	11,909	13,945
Investments	0	1	2	6	12	23	30
Net fixed assets	354	687	1,578	3,070	4,044	4,451	5,243
Total assets	**3,654**	**4,963**	**8,446**	**11,790**	**14,304**	**16,382**	**19,217**
Current liabilities	794	1,114	1,424	495	437	475	514
Total Debt	2,385	2,874	5,123	7,533	8,283	8,889	10,417
- Short term	2,212	2,728	4,546	6,615	6,783	7,089	7,917
- Long term	174	146	577	918	1,500	1,800	2,500
Other non-current liabilities	0	0	230	503	795	1,136	1,556
Total liabilities	**3,179**	**3,988**	**6,777**	**8,530**	**9,514**	**10,499**	**12,487**
Share capital(*)	233	696	734	788	848	875	875
Reserves & surplus	245	280	936	2,471	3,942	5,008	5,855
- Retained Earnings	188	171	474	1,033	1,598	2,256	3,104
Less: Misc. expenditure	(2)	(1)	(1)	0	0	0	0
Shareholders' funds	475	974	1,670	3,259	4,790	5,883	6,730
Total equity & liabilities	**3,654**	**4,963**	**8,446**	**11,790**	**14,304**	**16,382**	**19,217**
Capital employed	**2,861**	**3,848**	**7,023**	**11,294**	**13,868**	**15,908**	**18,704**

*Includes Preference Share Capital of Rs. 97.8 mn (FY03) and Rs. 400 mn (FY04 onwards).

Cash Flow Statement

(Rs. mn)	FY03	FY04	FY05	FY06	FY07E	FY08E	FY09E
Pre-tax profit	128	231	541	1,023	1,082	1,263	1,558
Depreciation	17	21	40	92	151	186	245
Chg in working capital	(648)	(637)	(2,304)	(2,874)	(1,563)	(1,636)	(1,980)
Total tax paid	(43)	(80)	90	(46)	(89)	(104)	(139)
Cash flow from oper. (a)	**(545)**	**(466)**	**(1,633)**	**(1,804)**	**(420)**	**(290)**	**(316)**
Capital expenditure	(66)	(354)	(932)	(1,584)	(1,124)	(593)	(1,037)
Chg in investments	3	(1)	(1)	(4)	(6)	(11)	(8)
Other investing activities	(0)	(148)	0	(0)	0	0	(0)
Cash flow from inv. (b)	**(63)**	**(503)**	**(933)**	**(1,588)**	**(1,130)**	**(604)**	**(1,044)**
Free cash flow (a+b)	**(608)**	**(968)**	**(2,567)**	**(3,391)**	**(1,551)**	**(894)**	**(1,360)**
Equity raised/(repaid)	99	464	501	1,031	966	435	0
Debt raised/(repaid)	519	489	2,249	2,410	751	606	1,528
Dividend (incl. tax)	(8)	(9)	(27)	(158)	(18)	(129)	(150)
Other financing activities	15	52	(109)	0	0	0	0
Cash flow from fin. (c)	**624**	**996**	**2,614**	**3,282**	**1,698**	**912**	**1,378**
Net chg in cash (a+b+c)	**16**	**27**	**47**	**(109)**	**148**	**17**	**18**

REI Agro

Income Statement

Yr. ended 31 Mar. (Rs. mn)	FY06	FY07E	FY08E	FY09E
Net sales	9,440	9,315	10,713	12,476
Growth (%)	12.6	(1.3)	15.0	16.5
Operating expenses	(8,100)	(7,887)	(9,041)	(10,504)
Operating profit	1,340	1,428	1,671	1,971
Other operating income	147	365	443	612
EBITDA	**1,487**	**1,793**	**2,114**	**2,584**
Growth (%)	70.4	20.6	17.9	22.2
Depreciation	(93)	(151)	(186)	(246)
Other income	2	2	2	2
EBIT	**1,397**	**1,644**	**1,930**	**2,340**
Interest paid	(373)	(562)	(667)	(781)
Pre-tax profit	1,023	1,082	1,263	1,558
(before non-recurring items)				
Pre-tax profit	1,023	1,082	1,263	1,558
(after non-recurring items)				
Tax (current + deferred)	(363)	(388)	(455)	(561)
Net profit	**660**	**694**	**809**	**997**
Adjusted net profit	660	694	809	997
Growth (%)	74.4	5.1	16.5	23.4
Net income	**660**	**694**	**809**	**997**

Balance Sheet

Yr. ended 31 Mar. (Rs. mn)	FY06	FY07E	FY08E	FY09E
Current assets	8,714	10,249	11,909	13,945
Investments	6	12	23	30
Net fixed assets	3,070	4,044	4,451	5,243
Total assets	**11,790**	**14,304**	**16,382**	**19,217**
Current liabilities	495	437	475	514
Total Debt	7,533	8,283	8,889	10,417
Other non-current liabilities	503	795	1,136	1,556
Total liabilities	8,530	9,514	10,499	12,487
Share capital	788	848	875	875
Reserves & surplus	2,471	3,942	5,008	5,855
Shareholders' funds	3,259	4,790	5,883	6,730
Total equity & liabilities	**11,790**	**14,304**	**16,382**	**19,217**
Capital employed	**11,294**	**13,868**	**15,908**	**18,704**

Cash Flow Statement

Yr. ended 31 Mar. (Rs. mn)	FY06	FY07E	FY08E	FY09E
Pre-tax profit	1,023	1,082	1,263	1,558
Depreciation	92	151	186	245
Chg in working capital	(2,874)	(1,563)	(1,636)	(1,980)
Total tax paid	(46)	(89)	(104)	(139)
Cash flow from oper. (a)	**(1,804)**	**(420)**	**(290)**	**(316)**
Capital expenditure	(1,584)	(1,124)	(593)	(1,037)
Chg in investments	(4)	(6)	(11)	(8)
Cash flow from inv. (b)	**(1,588)**	**(1,130)**	**(604)**	**(1,044)**
Free cash flow (a+b)	**(3,391)**	**(1,551)**	**(894)**	**(1,360)**
Equity raised/(repaid)	1,031	966	435	
Debt raised/(repaid)	2,410	751	606	1,528
Dividend (incl. tax)	(158)	(18)	(129)	(150)
Cash flow from fin. (c)	3,282	1,698	912	1,378
Net chg in cash (a+b+c)	(109)	148	17	18

Key Ratios

Yr. ended 31 Mar. (%)	FY06	FY07E	FY08E	FY09E
EPS (Rs.)	17.0	15.5	17.0	21.0
EPS growth	50.3	(9.0)	9.9	23.4
EBITDA margin	15.5	18.5	19.0	19.7
EBIT margin	14.6	17.0	17.3	17.9
ROCE	15.3	13.1	13.0	13.5
Net debt/Equity	229.8	168.9	147.5	151.4

Valuations

Yr. ended 31 Mar. (x)	FY06	FY07E	FY08E	FY09E
PER	11.4	12.5	11.3	9.2
PCE	10.0	10.2	9.2	7.4
Price/Book	2.3	1.8	1.6	1.4
Yield (%)	1.2	1.3	1.4	1.4
EV/Net sales	1.7	1.8	1.6	1.5
EV/EBITDA	10.9	9.3	8.2	7.3

Du Pont Analysis – ROE

Yr. ended 31 Mar (x)	FY06	FY07E	FY08E	FY09E
Net margin (%)	7.0	7.4	7.5	8.0
Asset turnover	0.9	0.7	0.7	0.7
Leverage factor	4.1	3.2	2.9	2.8
Return on equity (%)	26.8	17.2	15.2	15.8

Share Data

Mkt. Cap.	Rs. 0.97 bn (US$ 22 mn)
Price	Rs. 44
BSE Sensex	12886
Reuters	LTOL.BO
Bloomberg	LTO IN
52-week High/Low	Rs. 63/35
Issued Shares	22.3 mn

Shareholding Pattern (%)

Promoters	64
Public & Others	36

LT Overseas

Not Rated

Aiming to enter "Big league"

Incorporated in 1990 as LT Overseas Private Limited (LT), the company became public limited company in 1994. It is primarily in the business of milling, processing and marketing of branded and non-branded basmati rice as well as manufacturing of food products. It has recently raised fund from the public through an initial public offer of 7 mn shares (inclusive 390,000 shares reserved for employees) of Rs. 10 each at a premium of Rs. 46.

Year to March	FY03	FY04	FY05	FY06	CAGR (%)
P&L Data (Rs. mn)					**FY03-06**
Net Sales	2,826	3,615	3,609	4,008	12.3
Operating Profit	181	176	216	281	15.9
Net Profit	48	54	50	111	32.0
Margins (%)					
EBITDA	6.4	4.9	6.0	7.0	–
Net Profit	1.7	1.5	1.4	2.5	–
Balance Sheet (Rs. mn)					
Total Assets	2,388	2,624	2,901	3,145	9.6
Shareholders' Funds	389	427	463	549	12.2
Per Share Data (Rs.)					
EPS	7.0	7.6	6.9	6.7	(1.6)
CEPS	14.0	16.1	15.8	10.4	(9.4)
Dividend	0	0	0	18.1	–
Return (%)					
RoE	13.1	12.9	11.2	20.1	–
RoCE	11.3	10.0	8.8	9.9	–

- Brands like **'Daawat'** and **'Heritage'** have a strong recognition in Indian and international markets.
- LT recently raised capital through an IPO for expanding its capacity by 6 TPH for parboiling rice makes the total capacity by 36.5 TPH (inclusive of leased capacity of 3.5 TPH).
- AC Nielson ORG-MARG survey assessed a 22% volume share for LT and a 17.5% market share for their Daawat brand for CY05.
- At the current market price of Rs. 44, the stock trades at 6.5x FY06 EPS of Rs. 6.7.

Investment arguments

- **Global rice food company**

Targeting the potential in international market

The company through its continuous efforts is trying to emerge as a global rice food company on the back of its strengths and a diversified business mix, suitable for achieving such goal. The company has strong raw material sourcing ability through relationship and rapport developed with farmers over the years, production of quality output at minimum cost through use of latest technology, presence in 35 countries through its products and a distribution network of 100 distributors in India. As the world is moving towards convenience foods, there is a growing acceptance of ready-to-cook and ready-to-eat meals which will further the purpose of the company.

- **Brand recognition**

Daawat – largest selling brand of the company

The company has over the years established its brand in the rice industry and has 19 brands under its umbrella with the major being **'Daawat'** and **'Heritage'**. The company is also in the process of registering another 30 brands, the applications of which are pending at various levels. The brands of the company are registered in almost 40 countries. As per AC Nielsen ORG MARG survey 2005, **'Daawat'** has been among the top three basmati rice brands in India.

- **Scale of operation**

The size of the company helps it in procuring raw materials at economical prices which is fed to its vast distribution network. The scale of operation also helps the company to cater to customers with large requirements. The size of operation has provided the company to achieve economies of scale which in turn has helped in pricing its product at competitive rates. The company has been ranked as one of the top three players in the domestic basmati rice market with a market share of around 22% as per AC Nielsen ORG MARG survey for 2005.

- **Product portfolio**

Comprehensive product porfolio

The company's product portfolio consists of almost all types of rice such as brown rice, white rice, steamed rice, parboiled rice, organic rice, quick cooking rice, value-added rice and flavoured rice in ready-to-cook segment. **'Daawat'** is the largest selling brand of the company and has sub-brands to cater various classes of customers.

- **Strategic alliance**

The company has strategic alliance with Tata Chemicals for contract farming of basmati paddy to have access to better quality of rice and optimise the procurement process. It also has entered into strategic alliance with **Phoenix Agri Silica Corporation** to provide it the raw material in the form of by-product husk ash which is obtained while processing of rice. This plant would be producing silica for the cement industry.

- **Group companies/firms**

The company by merging its group companies and firms under single entity can have more economies of scale. This would lead to tough competition to its competitors. The company might achieve higher growth rate both in topline as well as bottomline as compared to others by adopting such activity.

Investment concerns

Possibility of conflict of interest

- Non-completion of the expansion programme may have a negative impact on the bottomline as the capacities will not be utilised to the maximum level.
- Subsidiaries/group companies/firms in similar business may be treated as a concern, as they may create conflict of interests. The details of such group companies/firms are:

Associate enterprises (Rs. mn)

Name of the concern	Business activity	Location	Share capital	LT Overseas holding (%)	Turnover	PAT
Nature Bio Foods Limited	Organic Agro Products	New Delhi	0.5	99.9	0.0	(0.0)
LT International Limited	Merchant Exporters & Traders	New Delhi	20.0	90.0	96.9	0.0
Sona Global Limited	General Trading	Dubai	12.2	100.0	0.0	(0.2)
Nice International FZE(~)	General Trading	Dubai	12.2	100.0	0.0	(0.7)
Raghunath Agro Industries(*)	Rice milling & processing (@)	Amritsar	38.5	–	496.0	1.3
Daawat Foods Private Limited(#)	Food Products processing & Trading	New Delhi	10.0	–	0.0	(0.0)
R S Rice & General Mills(*)	Rice milling & processing (@)	Amritsar	1.1	–	0.7	0.1

Note: (~) Wholly owned subsidiary of Sona Global Limited.

(*) Firm (1st column is partner's capital).

(#) Group company.

(@) Capacity of 24,000 tonnes each.

Business overview

Key milestones

Company history

Year	Events
1990-91	Incorporation of company as private limited.
1993-94	Conversion of private limited company into public limited.
1994-95	Setting up of 1st own milling capacity of 4 TPH.
1995-96	Registration of Daawat brand in USA.
1998-99	Business of LCTRRM taken over with capacity of 6TPH.
1999-00	Star trading house recognition granted by GOI.Registration as well as launch of Daawat brand in Mauritius, Saudi Arabia and New Zealand.
2000-01	Processing facility with a capacity of TPH at Bahalgarh made operational. Registration as well as launch of Daawat brand in Australia.
2001-02	Registration as well as launch of Daawat brand in Canada.
2002-03	Capacity expansion at Bahalgarh by 6 TPH making the total capacity of the company 16 TPH.
2004-05	Further capacity expansion at Bahalgarh by 2 TPH making the total capacity of the company 18 TPH.
2006-07	Silos complex made operational. Further capacity expansion at Bahalgarh by 9 TPH making the total capacity of the company 27 TPH.

Management

Vijay Kumar Arora, the Promoter Director of the company holds the position of Chairman-cum-Managing Director. His key areas of responsibility are international marketing, strategic planning, finance and business development. He is presently the Vice President of All India Rice Exporters Associations.

Ashwani Arora, the Promoter Director holds the position of whole-time Director with key areas of responsibility such as marketing and brand promotion in the domestic market.

Surinder Arora, the Promoter of the company has been serving as Director since 2000. Since he has a vast experience in procurement, production and plant operations his key areas of responsibility are the same.

Equity history (Nos. mn)

Duration	Issued capital	Increase	Face value (Rs.)	Particulars
1990-92 (Nos.)	20.0	–	100.0	Subscriber to MOA
1992-93 (Nos.)	45,781	45,761	100.0	Further allotment
1993-94	1.1	0.6	10.0	FV reduced to Rs. 10/share, Bonus in the ratio of 9:10, further allotment
1994-98	2.3	2.2	10.0	Bonus in the ratio of 2:3, Right issue
1999-05	7.2	4.9	10.0	Shares issued under ESOP
2006-07	22.3	15.0	10.0	Bonus issue in the ratio of 1:1, Pre-IPO placements, IPO issue

Processing facilities

Rice: The company has a combined capacity of 30.5 TPH processing of paddy at three processing facilities located one each in Bahalgarh and Sonepat in Haryana and one in Amritsar, Punjab. The 1st facility has a capacity of 27 TPH whereas the latter two have a combined capacity of 3.5 TPH on lease from group companies.

Processed food: The company has taken on lease a food processing plant.

Capacity utilisation (Actual and proposed)

Capacity (MT)	FY04	FY05	FY06	FY07E	FY08E	FY09E
Installed	157,680	175,200	158,712	230,940	293,670	319,714
Actual	114,606	143,523	127,327	–	–	–
Expected	–	–	–	202,400	232,760	267,674
Utilisation (%)	72.7	81.9	80.2	87.0	79.0	84.0

Source: Company prospectus

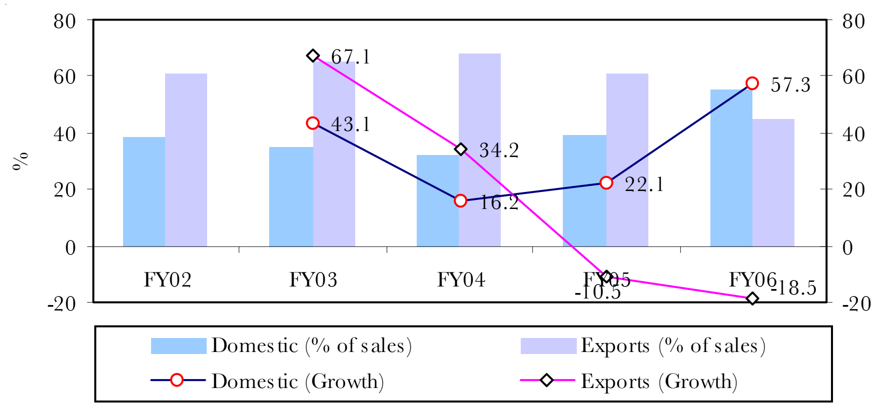
Products portfolio

LT's product portfolio consists of almost all types of rice such as brown rice, white rice, steamed rice, parboiled rice, organic rice, quick cooking rice, value-added rice and flavoured rice in ready-to-cook segment. The sub-brands of 'Daawat' are classified into three classes i.e. for retail customers, for institutional segment, for economy segment.

Revenue mix

LT deals in two types of products i.e. own manufactured and traded products. These generated 93% and 7% to the total revenues of the company in FY06. The company has decreased its revenues from traded goods by 65% form Rs. 730 mn in FY05 to Rs. 263 mn in FY06. Export contributes 45% of the total revenue which is decreased by 26% as compared to FY05, due to the concentrating on the domestic market.

Geographical break-up



Source: Company

Distribution network

Global distribution network

The company has its presence in almost all major basmati consuming regions with strong distribution network of more than 100 distributors. The distributors provide the company with valuable feedback obtained by interacting with the customers, to increase the quality and quantity of its output. There are exclusive arrangements with most of the distributors in the domestic market.

The company's products are presently available in 35 countries including USA, Canada, UK and the European Union with the help of its distribution network including both exclusive and non-exclusive arrangements. Some of the countries where the company has exclusive arrangements with its distributors are North America, South America and European region. It has plans to increase its presence in the overseas market by entering in Far East, Africa and Middle East.

Capex

Sourcing and deployment of funds

The company has planned to incur a capex of Rs. 317.2 mn. The company has during the year raised fund for capex requirement, through pre-IPO placements and an IPO, amounting to Rs. 53.5 mn and Rs. 394 mn, respectively. The capacity expansion at this facility will be of 6 TPH making the total capacity to be 36.5 TPH. (Inclusive of leased capacity of 3.5 TPH.)

Details of cost of expansion programme (Rs. mn)

Project	Civil ands other work	Plant and Machinery	Total	Expected completion
Expansion, automation and modernisation at Sonepat (Haryana)				
- New parboiled rice (sella) processing and milling capacity	12.0	58.2	70.2	Sep. '07
- New milling line for producing value-added products		41.0	41.0	Jul. '06*
- Balancing equipments and automation of existing facility		31.3	31.3	Sep. '06*
- Increasing storage capacity				
+ Silo grain storage		98.4	98.4	Jun. '07
+ New white rice storage	5.8	15.3	21.1	Jun. '07
+ Open Bardana shed	4.7		4.7	Jul. '07
Generating power for captive consumption		**50.5**	**50.5**	**Jul. '07**
Total	**22.5**	**294.7**	**317.2**	

B&K's view

The company is trying to develop its decling export market with parboiled rice. Now LT is focusing on its own manufactured products and reducing its focus on traded goods. But the company is facing the heat of this competition in basmati rice segment from its peer group.

At the current market price of Rs. 44, the stock trades at 6.5x FY06 EPS of Rs. 6.7.

LT Overseas

Income Statement

Yr. ended 31 Mar. (Rs. mn)	FY03	FY04	FY05	FY06
Net sales	2,826	3,615	3,609	4,008
Growth (%)	57.8	27.9	-0.2	11.0
Operating expenses	(2,646)	(3,439)	(3,393)	(3,727)
Operating profit	181	176	216	281
EBITDA	**181**	**176**	**216**	**281**
Growth (%)	4.9	(2.8)	23.0	30.1
EBITDA Margins(%)	6.4	4.9	6.0	7.0
Depreciation	(48)	(58)	(64)	(57)
Other income	67	88	52	38
EBIT	**199**	**205**	**204**	**262**
Interest paid	(140)	(143)	(139)	(144)
Pre-tax profit	60	62	65	118
(before non-recurring items)				
Non-recurring items		1		10
Pre-tax profit	60	63	65	128
(after non-recurring items)				
Tax (current + deferred)	(11)	(9)	(15)	(16)
Net profit	**48**	**54**	**50**	**111**
Adjusted net profit	48	53	50	102
Growth (%)	33.0	8.9	(5.7)	104.7
PAT Margins (%)	1.7	1.5	1.4	2.5
Net income	**48**	**54**	**50**	**111**

Balance Sheet

Yr. ended 31 Mar. (Rs. mn)	FY03	FY04	FY05	FY06
Current assets	1,990	2,236	2,508	2,549
Investments	6	9	12	76
Net fixed assets	392	379	380	520
Total assets	**2,388**	**2,624**	**2,901**	**3,145**
Current liabilities	413	499	412	328
Total Debt	1,566	1,673	1,998	2,236
Other non-current liabilities	20	25	28	32
Total liabilities	1,998	2,198	2,437	2,596
Share capital	69	69	69	72
Reserves & surplus	332	386	436	532
Less: Misc. expenditure	(11)	(28)	(41)	(55)
Shareholders' funds	**389**	**427**	**463**	**549**
Total equity & liabilities	**2,388**	**2,624**	**2,901**	**3,145**

Cash Flow Statement

Yr. ended 31 Mar. (Rs. mn)	FY03	FY04	FY05	FY06
Pre-tax profit	60	63	65	128
Depreciation	44	57	57	0
Chg in working capital	(307)	(119)	(386)	(89)
Total tax paid	9	(4.0)	(13)	(12)
Cash flow from oper. (a)	**(194)**	**(2)**	**(277)**	**26**
Capital expenditure	(130)	(45)	(58)	(140)
Chg in investments	2	(3)	(4)	(63)
Other investing activities	(48)	(54)	(50)	(91)
Cash flow from inv. (b)	**(176)**	**(101)**	**(111)**	**(294)**
Free cash flow (a+b)	(371)	(103)	(388)	(268)
Equity raised/(repaid)	42	37	37	86
Debt raised/(repaid)	350	107	325	238
Dividend (incl. tax)				(21)
Cash flow from fin. (c)	**392**	**144**	**362**	**303**
Net chg in cash (a+b+c)	**21**	**41**	**(26)**	**35**

Key Ratios

Yr. ended 31 Mar. (%)	FY03	FY04	FY05	FY06
EPS (Rs.)	7.0	7.6	6.9	6.7
EPS growth	33.0	8.9	(10.1)	(2.8)
EBITDA margin	6.4	4.9	6.0	7.0
EBIT margin	7.1	5.7	5.6	6.5
ROCE	11.3	10.0	8.8	9.9
Net debt/Equity	391.7	372.9	419.1	390.5

Valuations

Yr. ended 31 Mar. (x)	FY03	FY04	FY05	FY06
PER	6.2	5.7	6.4	6.6
PCE	3.1	2.7	2.8	4.2
Price/Book	0.8	0.7	0.7	1.2
Yield (%)				2.7
EV/Net sales	0.7	0.5	0.6	0.6
EV/EBITDA	10.2	10.9	10.5	8.8

Du Pont Analysis – ROE

Yr. ended 31 Mar. (x)	FY03	FY04	FY05	FY06
Net margin (%)	1.7	1.5	1.4	2.5
Asset turnover	1.3	1.4	1.3	1.3
Leverage factor	5.8	6.1	6.2	6.0
Return on equity (%)	13.1	12.9	11.2	20.1

Lakshmi Energy and Foods **Not Rated**

Share Data

Mkt. Cap.	Rs. 9.2 bn (US$ 209 mn)
Price	Rs. 161
BSE Sensex	12886
Reuters	LAKO.BO
Bloomberg	LKEF IN
Daily Volume	US$ 0.1 mn (Rs. 4.4 mn)
52-week High/Low	Rs. 232/131
Issued Shares	57.1 mn

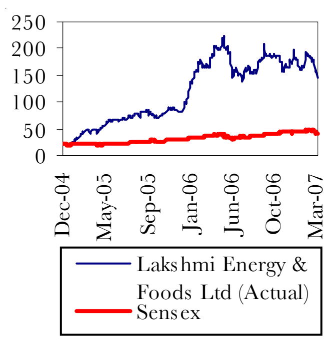
Performance (%)

	1m	3m	12m
Absolute	(22)	(11)	(18)
Relative	(13)	(5)	(32)

Shareholding Pattern (%)

Promoters	39
FIIs	40
Public & Others	21

Relative Performance



Capitalising through by-products

Incorporated in July 1990, Lakshmi Energy and Foods Limited (LEAF), formerly known as Lakshmi Overseas Industries, is a leading processor of non-basmati rice. LEAF is slated to have an integrated processing plant for paddy along with the value-added products such as rice bran oil, cattle feed and a power plant; generating electricity up to 30 MW. To diversify its business mix, the company is also planning to set up a 300 TPD wheat flour mill at its existing plant location.

Year to March	FY03	FY04	FY05	FY06	CAGR (%)
P&L Data (Rs. mn)					**FY03-06**
Net Sales	1,251	2,251	4,077	5,584	64.7
Operating Profit	49	62	325	738	147.1
Net Profit	1	89	180	420	715.2
Margins (%)					
EBITDA	3.9	2.7	8.0	13.2	–
Net Profit	0.1	4.1	4.4	7.5	–
Balance Sheet (Rs. mn)					
Total Assets	1,477	1,397	2,050	3,360	31.5
Shareholders' Funds	792	822	999	1,632	27.2
Per Share Data (Rs.)					
EPS	0.0	1.9	3.4	7.7	688.8
CEPS	0.4	2.3	4.0	8.6	167.3
Dividend	0	0	3	4	–
Return (%)					
RoE	0.1	11.3	19.8	32.0	–
RoCE	4.2	9.8	22.8	31.5	–

(*The EPS is calculated on the post- split equity base of 57.2 mn shares).

- LEAF has first mover advantage since it had entered into non-basmati rice segment as an organised player, which was dominated mainly by unorganised players. The non-basmati rice market is largely a fragmented market even today.
- The company is also concentrating on processing of the by-products obtained from non-basmati rice processing, to improve its margins. LEAF is steadily increasing the capacity of power to 105 MW within next two-three years.
- Realisation from non-basmati rice processing is low, as it depends upon government policies in regards to minimum support price and levy rates to procure paddy and to sell it to Food Corporation of India.
- At the current market price of Rs. 161, the stock trades at 21.7x FY06 diluted EPS of Rs. 7.4 (post-stock split in the ratio of 5:1 in December 2006).

Investment arguments

- **Largest processor of non-basmati rise**

Leader in non-basmati rice

Among the major organised players in the industry, LEAF is the leader in non-basmati rice processing. The company is scaling its capacity from 2,100 TPD (87.5 TPH) to 3,300 TPD (137.5 TPH) by December 2006 and also ramping up additional 800 TPD, to scrap and replace the old plant gradually. The imported machines from Japan, Germany, Denmark and USA for its expanded capacities will definitely improve the head rice recovery rate going forward. The company is also planning to have a greenfield project for rice processing having a capacity of 1 mn tonnes (expected to be completed by FY09 at Moga in Punjab).

- **Adding value to by-products**

LEAF has the advantage of further processing by-products i.e. husk, bran and nakku obtained from rice processing. These are processed for the following purposes:

Power from husk

Biomass power plant: Husk is a major byproduct in processing of paddy with an output of around 20%. LEAF will use the same to generate power**,** which in return will contribute to the company margin. The first phase of power generation will start with a capacity of 30 MW at Khamanon. Out of the 30 MW, 15 MW will be operational in the 4th quarter of FY07 and the remaining 15 MW will be operational in the 2nd quarter FY08. The company would further install two more power plants of 30 MW each in next two years and will be followed by one in the 3rd year with a capacity of 15 MW. In total the power plant will generate 105 MW of electricity within the next three-four years. The company has signed the agreement with Punjab State Electricity Board (PSEB) to sell power from cogeneration units at Rs. 3.48/unit as per the promotion policy of the Ministry of Non-conventional Energy Sources (MNES).

Oil from bran

Oil: Rice bran oil can be produced from bran, whose demand is increasing by 5 lacs tonnes per annum due to increase in population and rise in the disposable incomes. Presently, there is a demand-supply mismatch of round 50 lacs tonnes in the domestic market, the demand and supply are 115 lac and 65 lac tonnes, respectively. The company has a capacity of 200 TPD (2,500 TPH) which is expected to increase to 400 TPD by January 2007. The refinery capacity is also expected to increase from 30 tonnes (375 TPH) to 60 tonnes.

The company is using de-oiled cakes to produce **cattle feed**. It currently has a production capacity of 130 TPD which is expected to increase to 300 TPD by May 2007.

These value-added products will definitely help in realising better margins for the company in years to come.

- **Wheat flour mill**

LEAF is expanding its portfolio from just a non-basmati rice processor by adding wheat flour mill to its product profile, in Khamano plant. The facility is having a capacity of 300 TPD is expected to contribute Rs. 500 mn in the topline for FY08.

- **Well-defined margins**

Buying and selling to FCI

LEAF procures its raw material i.e. paddy from FCI at minimum support price (MSP) fixed by the government. The average procurement cost (inclusive of 4% market fees, 4% VAT, 2.5% commission paid to agents, 1% brokerage, 1% labour charges, 4% freight cost ant cost of gunny bag), is higher than MSP.

And in turn sells its production to FCI at levy rate. LEAF sells 75% of its products to FCI, which is located at a distance of 1 km from the company's plant and balance 25% is sold in the open market through the traders.

- **Location advantage**

Pre-fixed prices reduces the risk

LEAF processing facility is located in Punjab, which is said to be the largest surplus producer of rice in India. The government procures over 95% of rice produced in the state at the pre fixed prices both for the paddy as well as rice ,thus, removing any price risk for the processors. For FY07, LEAF is procuring paddy and selling the final output at around Rs. 6, 500/MT and Rs. 11, 840/MT, respectively.

- **Expansion benefits**

  o **Incentives from government for Biomass Power Plant:** LEAF is implementing all its expansion projects in the state of Punjab. State government and Central government have granted the company various incentives for all its power expansion programmes.

  It has been granted **single window clearance** by empowered government committee due to the company's entry into non-conventional power. The company would also be granted 100% tax exemption and depreciation benefits for its Biomass power plant and will get the waiver of 4% market fee once the plant becomes operational.

Single window clearence from State and Central Goverments

  o **Power to earn carbon credits:** Its power plant will be eligible for carbon credits under the **Kyoto Protocol** and is eligible to en-cash these within a period of 10 years. There is a huge demand for credits from the European market. LEAF power plant with a capacity of 30 MW is expected to fetch CER's of around 140,000 units/annum. Currently, the price floating in the market for these credits is 10 Euro per credit. The company has appointed **Ernst & Young (E&Y)** as the advisors for credit's earnings.

Potential source for cash flows

- **Companies under promoter control**

Ganeshay Overseas Industries Limited (Ganeshay) is an associate company, with a capacity of 25 TPH for paddy processing which is expected to increase to 50 TPH. It has a turnover of Rs. 371 mn and has reported a PAT of Rs. 21 mn in FY06. LEAF is planning to merge Ganeshay to achieve economies of scale and consolidation of similar businesses under single company. LEAF is also planning to incorporate a wholly owned subsidiary with the object of conducting other related business activities.

Investment concerns

Support price

LEAF margin is mainly dependent upon the MSP for procurement of paddy and levy prices for rice, fixed by the government. It sells almost 75% of its processed rice to the FCI which in turn sells it to common public at large.

Competition

As the non-basmati market is mainly unorganised, many large players are looking towards it as an opportunity to enter. This could be a threat for LEAF resulting in reduction in its margins as well as its market share in this segment.

Business overview

Management

Mr. Balbir Singh Uppal, Chairman is a Promoter Director of the company. He holds the position of MD of the company since inception. His experience in the food grain processing industry is almost more than 20 years.

Mr. Janak Raj Singh Uppal is the Executive Director of the company and has extensive experience in the grain processing industry.

Equity history (Nos. mn)

Stock-split in the ratio of 1:5

Duration	Issued capital	Increase	Face value (Rs.)	Particulars
1993-94	2.0	–	10.0	
94-00	4.4	2.3	10.0	Public Issue in 1995
00-03	8.6	4.2	10.0	Bonus Issue in 2000 in the ratio of 1:1 Reduction of 0.2 mn shares
03-04	9.9	1.3	10.0	Preferential Issue
04-05	10.4	0.5	10.0	Preferential Issue
05-06	10.9	0.5	10.0	Preferential Issue
06-07	11.4	0.5	10.0	Conversion of warrants
	57.1	–	2.0	Stock-split in the ratio of 1:5

Product portfolio

Value-added products complementing the product portfolio

Rice	Oils	De-oiled cakes	Others
Paddy	Rice Bran Oil	Rice Bran DOC	Cattle Feed
Rice	Cotton Seed Oil		Damaged Wheat
Nakku	Mustard Oil		Paddy Husk
	Sunflower Oil		Bardana
			Gold
			Rice Bran
			Khudi Phak

Different classes under its products

Category	Brand	Products
Rice	Lakshmi Foods	Non-basmati Rice
Refined Oils	Gold Crown	Rice Bran, Sunflower, Mustard, Cottonseed and Soya Oil Punjab, Delhi
Cattle Feed	Hira Moti	

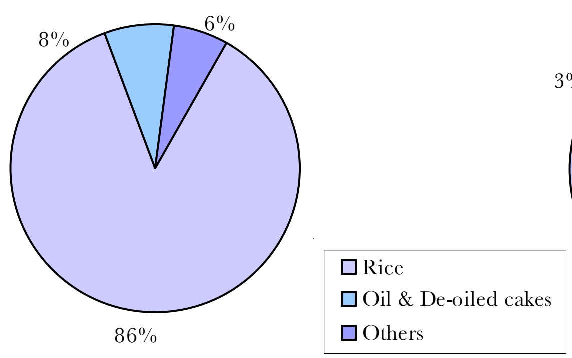
Revenue break-up

LEAF revenue contribution is mainly from non-basmati rice (including parboiled rice) sales in the domestic market. The proportion of revenues from raw non-basmati rice and parboiled non-basmati rice is in the ratio of 90:10, respectively. The net sales have increased by 37% to Rs. 5.6 bn (FY06) from Rs. 4.1 bn (FY05).

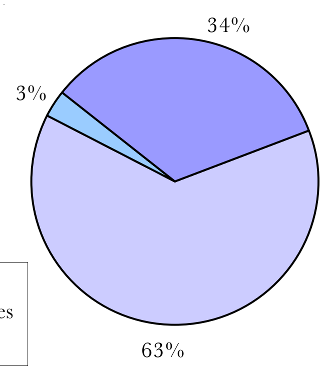
- **Rice:** Contribution of rice in total revenue has increased to 86% (Rs. 4.9 bn in FY06) from 63% (Rs. 2.6 bn in FY05) mainly due to increase in capacity utilisation from 65 TPH to 105 TPH.
- **Value-added products:** De-oiled cakes (DOC) and oils sales are the value-added products contributing around 8% in the total revenue, the revenues from such products has increased by 236% to Rs. 458.4 mn (FY06) from Rs. 136 mn (FY05).
- **Others:** Revenue contribution from others in FY06 was around 6% amounting to Rs. 250 mn a decline of 82% from previous year which was around Rs. 1,369 mn. The main reason for such decline was on account of sales of damaged wheat which was Rs. 203 mn in FY06 comparatively lower by Rs. 1,058 mn in FY05.

Revenue mix

FY06



FY05



Source: Company

Capex and its funding

Particulars	Capex (Rs. mn)	Completion	Old capacity	New capacity	Source of funding
Biomass power plant	1, 100	Mar. '07	Nil	105 MW	Power Finance Corporation
Rice	1, 000	Dec. '06	2,100 TPD	3, 300 TPD	Punjab National Bank and Syndicate Bank
Wheat	220	Jul. '07	Nil	300 MT	
Bran oil	100	Jan. '07	200 TPD	400 TPD	
Cattle feed	50	May '07	130 TPD	300 TPD	

Financial highlights (9 Monthly)

(Rs. mn)	3QFY06	3QFY07	YoY (%)	9MFY06	9MFY07	YoY (%)
Net Sales	**1565**	**1820**	**16.3**	**4124**	**4913**	**19.1**
EBITDA	**213**	**335**	**57.2**	**486**	**837**	**72.1**
EBITDA Margins (%)	13.6	17.5	–	11.8	16.2	–
Other Income	2	3	22.4	8	5	(27.2)
Interest	(18)	(12)	(36.3)	(36)	(30)	(17.9)
Depreciation	(8)	(12)	63.2	(22)	(34)	54.8
PBT	189	314	65.7	435	778	78.8
Tax	(38)	(31)	(17.1)	(89)	(78)	(12.2)
Adjusted PAT	**151**	**282**	**86.4**	**347**	**700**	**102.1**
PAT Margins (%)	9.7	14.8	–	8.4	13.5	–
EPS (Rs.)	3	5	–	6	12	–

B&K's view

LEAF has achieved significant presence in non-basmati rice which is largely an unorganised segment (95%) in rice industry. With its further impetus on using its residual products (like Husk and Bran) for power generation and edible oil, the company expects to add revenue at an expected growth rate of 25% for the next two years. The company also foresees improvement in margins, as a result of low operational cost on this portion of revenue.

The company has split its share of face value Rs. 10 each into 5 equity shares with a face value of Rs. 2 each with effect from 18th December 2006. The number of outstanding shares as on date is 57.2 mn shares.

At the current market price of Rs. 161, the stock trades at 21.7x FY06 diluted EPS of Rs. 7.4 (on account of stock split).

Lakshmi Energy and Foods

Income Statement

Yr. ended 31 Mar. (Rs. mn)	FY03	FY04	FY05	FY06
Net sales	1,251	2,251	4,077	5,584
Growth (%)	2.0	80.0	81.1	37.0
Operating expenses	(1,202)	(2,189)	(3,753)	(4,846)
Operating profit	49	62	325	738
EBITDA	**49**	**62**	**325**	**738**
Growth (%)	(21.8)	25.9	427.2	127.3
Depreciation	(19)	(20)	(27)	(49)
Other income	30	87	42	8
EBIT	**60**	**128**	**340**	**696**
Interest paid	(59)	(28)	(50)	(59)
Pre-tax profit	1	100	290	637
(before non-recurring items)				
Non-recurring items	0	(2)		
Pre-tax profit	1	98	290	637
(after non-recurring items)				
Tax (current + deferred)	0	(9)	(110)	(216)
Net profit	**1**	**89**	**180**	**420**
Adjusted net profit	1	92	180	420
Growth (%)	3,205.8	13,463.1	97.2	133.0
Net income	**1**	**89**	**180**	**420**

Balance Sheet

Yr. ended 31 Mar. (Rs. mn)	FY03	FY04	FY05	FY06
Current assets	974	913	1,532	2,523
Investments	1	1	2	5
Net fixed assets	502	484	516	832
Total assets	**1,477**	**1,397**	**2,050**	**3,360**
Current liabilities	132	127	345	637
Total Debt	552	446	682	997
Other non-current liabilities		2	24	94
Total liabilities	685	576	1,051	1,728
Share capital	86	99	104	179
Reserves & surplus	707	723	895	1,453
Less: Misc. expenditure	(1)			
Shareholders' funds	**792**	**822**	**999**	**1,632**
Total equity & liabilities	**1,477**	**1,397**	**2,050**	**3,360**

Cash Flow Statement

Yr. ended 31 Mar. (Rs. mn)	FY03	FY04	FY05	FY06
Pre-tax profit	1	98	290	637
Depreciation	54	56	63	85
Chg in working capital	121	49	(400)	(746)
Total tax paid	0	2	(30)	(78)
Cash flow from oper. (a)	**177**	**205**	**(77)**	**(103)**
Capital expenditure	(17)	(38)	(95)	(401)
Chg in investments	1	0	(1)	(3)
Other investing activities	6	(28)	0	(1)
Cash flow from inv. (b)	**(10)**	**(66)**	**(96)**	**(405)**
Free cash flow (a+b)	167	139	(173)	(507)
Equity raised/(repaid)	1	16	67	273
Debt raised/(repaid)	(125)	(106)	236	315
Dividend (incl. tax)	(6)	(12)	(30)	(28)
Other financing activities	(36)	(36)	(36)	(36)
Cash flow from fina. (c)	**(167)**	**(138)**	**236**	**524**
Net chg in cash (a+b+c)	**0**	**1**	**63**	**17**

Key Ratios

Yr. ended 31 Mar (%)	FY03	FY04	FY05	FY06
EPS (Rs.)	0.0	1.9	3.4	7.7
EPS growth	3,205.8	11,748.9	86.3	122.4
EBITDA margin	3.9	2.7	8.0	13.2
EBIT margin	4.8	5.7	8.3	12.5
ROCE	4.2	9.8	22.8	31.5
Net debt/Equity	68.9	53.4	61.1	55.7

Valuations

Yr. ended 31 Mar. (x)	FY03	FY04	FY05	FY06
PER	9,091.3	76.7	41.2	18.5
PCE	316.9	62.8	35.8	16.6
Price/Book	7.7	8.5	7.4	4.8
Yield (%)	0.1	0.2	0.4	0.3
EV/Net sales	6.9	3.8	2.1	1.6
EV/EBITDA	177.1	138.9	26.9	12.2

Du Pont Analysis – ROE

Yr. ended 31 Mar. (x)	FY03	FY04	FY05	FY06
Net margin (%)	0.1	4.1	4.4	7.5
Asset turnover	0.8	1.6	2.4	2.1
Leverage factor	1.9	1.8	1.9	2.1
Return on equity (%)	0.1	11.3	19.8	32.0

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Analyst Certification

We, Rohit Anand & Rishab Bothra, hereby certify that the views expressed in this report accurately reflect our personal views about the subject securities and issuers. We also certify that no part of our compensation was, is, or will be, directly or indirectly, related to the specific recommendation or view expressed in this report.

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