

Spirit call

United Spirits (USL) raised \$350 million (Rs 1,681.4 crore) through a qualified institutional placement recently. The liquor company issued about 18 million shares at a price of Rs 913.7 per share.

Higher debt burden has been eating into USL's profits for some time now. More so, after the company bought Scottish whiskey distiller Whyte & Mackay two years back. In FY2009, USL's debt-equity ratio stood at 3.4 with overall debt at Rs 7,360 crore.

Analysts expect the company to utilise about \$250 million of the \$350 million raised to repay debt. The company has already repaid \$300 million of debt in the last six months and the latest repayment would take the effective debt-equity ratio to 1.1 times and bring down the debt level to Rs 5,200 crore.

Over the past week, USL's stock has outperformed broader indices, gaining 10.4% to Rs 1,011.25 per share as compared with a 1.7% gain in the BSE Sensex. De-leveraging the balance sheet augurs well, as interest costs would reduce substantially.

In the last one year, USL's margins were adversely impacted on account of rising prices of molasses (raw material for alcohol and ethanol).

Going by the unfavourable demand-supply gap in the sugar industry, molasses prices could increase further going forward, to the detriment of companies such as USL, though the sharp decline in demand for ethanol for industrial purposes could check a runaway rise.

At the current market price, the USL stock trades at 28 times its estimated earnings for 2010.

"With underlying volume growth at 13%-plus, likely easing of molasses prices from here, and healthier balance sheet, we maintain our Outperformer call with a price target of Rs 1,142," Nikhil Vora, Bhushan Gajaria and Swati Nangalia of IDFC-SSKI India Research wrote in a note to clients on October 16.

Positively, USL enjoys over 50% market share in Indian made foreign liquor, which has seen a compounded annual growth rate of 12% in the last four years. Competition in the space is expected to be low given the strong entry barriers.

In view of all this, investors could consider the stock on declines.

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Relative showing

Base: Jul 1, 2009 = 100

