

HINDUSTAN UNILEVER

Strong show despite GST headwind

India Equity Research | Consumer Goods

Hindustan Unilever (HUL) reported in-line Q1FY18 revenue growth of 4.9% YoY, while EBITDA (14.1% YoY) and PAT (14.9% YoY) growth surpassed estimates. Volumes remained flattish versus our 1-2% YoY dip estimate; this is commendable, especially in light of destocking by CSD as well as trade channel imbalance on GST rollout from July 2017. Benign raw material prices helped gross margin expand 91bps YoY and 104bps QoQ. This, coupled with cost rationalisation (ZBB strategy) and calibrated A&P spends, aided EBITDA margin jump 173bps. New launches in the natural space (launched skincare natural brand *Citra*) as well as pan-India roll out of Ayush have been successful. We envisage HUL to be key beneficiary of GST and recovery in the staples space. Maintain 'HOLD'.

Broad-based growth

Key highlights: (i) HUL's homecare segment grew 5.9% YoY on a high base of 6.8% YoY with margin also expanding 232bps YoY—highest in the past 7 quarters (premium brand *Surf* continued to outperform category growth); (ii) personal care grew at 3.5% YoY helped by spurt in relaunched *Fair & Lovely* and *Lever Ayush*, but mildly dragged by the oral care segment; (iii) refreshments continued double digit revenue growth—up 10.8% YoY aided by broad-based volume-led spurt; and (iv) foods continued to disappoint with 4.4% YoY growth, <5% growth for fifth consecutive quarter.

Q1FY18 conference call: Key takeaways

Rural growth has been a tad lower than urban growth. Rural markets continued to remain challenging. **Impact of lack of offtake in CSD channel on the quarter's sales was 2%.** HUL's growth in the personal care segment was in line with industry growth. Oral care's performance continued to remain subdued.

Outlook and valuations: Long-term positive; maintain 'HOLD'

We expect HUL to be key beneficiary of share gains helped by GST. **Increased launches in the natural space and higher GST rate for herbal products are likely to boost share gains.** At CMP, the stock is trading at 40.6x FY19E. On better-than-expected Q1FY18 numbers, we revise up FY18/19E EPS 2.6%/4.2%, respectively, and also our target multiple to 44x (earlier 40x) to arrive at revised TP of INR1,253 (INR1,106 earlier). We maintain 'HOLD/SP'.

EDELWEISS 4D RATINGS

| | |
|--------------------------------|-------------|
| Absolute Rating | HOLD |
| Rating Relative to Sector | Performer |
| Risk Rating Relative to Sector | Low |
| Sector Relative to Market | Underweight |

MARKET DATA (R: HLL.BO, B: HUVR IN)

| | |
|------------------------------|------------------|
| CMP | : INR 1,158 |
| Target Price | : INR 1,253 |
| 52-week range (INR) | : 1,190 / 782 |
| Share in issue (mn) | : 2,164.5 |
| M cap (INR bn/USD mn) | : 2,506 / 38,953 |
| Avg. Daily Vol.BSE/NSE('000) | : 1,349.8 |

SHARE HOLDING PATTERN (%)

| | Current | Q2FY17 | Q1FY17 |
|---|---------|--------|--------|
| Promoters * | 67.2 | 67.2 | 67.2 |
| MF's, FI's & BK's | 5.7 | 5.7 | 5.2 |
| FII's | 13.3 | 13.1 | 13.8 |
| Others | 13.9 | 13.9 | 13.8 |
| * Promoters pledged shares (% of share in issue) | : | NIL | |

PRICE PERFORMANCE (%)

| | Stock | Nifty | EW Consumer goods Index |
|-----------|-------|-------|-------------------------|
| 1 month | 6.0 | 2.5 | (1.4) |
| 3 months | 26.9 | 7.9 | 8.1 |
| 12 months | 25.6 | 15.5 | 16.3 |

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Financials

(INR mn)

| Year to March | Q1FY18 | Q1FY17 | % Chg | Q4FY17 | % Chg | FY17 | FY18E | FY19E |
|----------------------|--------|--------|-------|--------|-------|---------|---------|---------|
| Net revenues | 85,290 | 81,282 | 4.9 | 82,130 | 3.8 | 331,620 | 367,163 | 413,286 |
| EBITDA | 18,660 | 16,359 | 14.1 | 16,510 | 13.0 | 63,400 | 74,192 | 88,690 |
| Adjusted Profit | 12,960 | 11,280 | 14.9 | 11,180 | 15.9 | 42,650 | 51,695 | 61,660 |
| Adjusted Diluted EPS | 6.0 | 5.2 | 14.9 | 5.2 | 15.9 | 19.7 | 23.9 | 28.5 |
| Diluted P/E (x) | | | | | | 58.8 | 48.5 | 40.6 |
| EV/EBITDA (x) | | | | | | 38.7 | 33.1 | 27.6 |
| ROAE (%) | | | | | | 63.8 | 73.6 | 80.8 |

Table 1: Segmental growth and margins under IND AS

| | Q4FY16 | Q1FY17 | Q2FY17 | Q3FY17 | Q4FY17 | Q1FY18 |
|-----------------------------|--------|--------|--------|--------|--------|--------|
| % sales growth (YoY) | | | | | | |
| Home care | 4.3 | 6.8 | 3.2 | 1.0 | 7.4 | 5.9 |
| Personal care | 1.5 | 2.1 | (0.3) | (2.7) | 8.1 | 3.5 |
| Foods | 10.0 | 4.7 | 2.4 | 0.5 | 2.4 | 4.4 |
| Refreshment | 9.2 | 5.4 | 8.4 | 8.1 | 10.5 | 10.8 |
| Others | (6.1) | NM | (15.2) | (27.3) | (30.4) | (17.6) |
| EBIT margins (%) | | | | | | |
| Home care | 12.2 | 13.9 | 10.1 | 8.7 | 12.9 | 14.7 |
| Personal care | 25.7 | 26.2 | 22.9 | 23.1 | 24.1 | 24.7 |
| Foods | 13.5 | 6.4 | 4.9 | 9.4 | 9.5 | 14.4 |
| Refreshment | 16.9 | 16.1 | 14.8 | 14.7 | 16.8 | 18.9 |
| Others | 4.7 | (4.8) | 4.2 | (8.5) | (2.0) | (3.6) |

Source: Company

Table 2: Performance trend across categories at a glance (according to IGAAP segmental reporting)

| % sales growth (YoY) | Q1FY14 | Q2FY14 | Q3FY14 | Q4FY14 | Q1FY15 | Q2FY15 | Q3FY15 | Q4FY15 | Q1FY16 | Q2FY16 | Q3FY16 | Q4FY16 |
|--------------------------------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|
| Soaps and detergents | 7.7 | 6.4 | 7.1 | 9.6 | 12.9 | 11.1 | 6.0 | 5.0 | 0.2 | 1.6 | 0.8 | 2.1 |
| Personal products | 2.0 | 11.8 | 12.4 | 8.3 | 14.7 | 9.9 | 6.5 | 13.4 | 11.4 | 9.5 | 5.6 | 2.8 |
| Beverages | 15.8 | 16.1 | 7.2 | 7.5 | 10.5 | 7.5 | 8.2 | 12.3 | 9.4 | 6.1 | 7.0 | 6.1 |
| Packaged Food | 4.8 | 8.7 | 12.9 | 12.7 | 18.8 | 13.4 | 12.6 | 13.6 | 11.8 | 12.4 | 11.8 | 11.7 |
| Overall volume growth (% YoY) | 4.0 | 5.0 | 4.0 | 3.0 | 6.0 | 5.0 | 3.0 | 6.0 | 6.0 | 7.0 | 6.0 | 4.0 |
| % EBIT growth (YoY) | | | | | | | | | | | | |
| Soaps and detergents | 14.0 | 4.5 | 14.5 | 10.1 | 21.1 | 7.9 | 11.4 | 15.8 | 12.4 | (4.1) | 1.3 | 11.6 |
| Personal products | (1.6) | 5.3 | 13.9 | 5.1 | 27.4 | 17.4 | 3.3 | 26.0 | 19.5 | 17.2 | 9.9 | 9.2 |
| Beverages | 46.1 | 37.5 | (2.2) | 19.7 | (1.8) | 9.9 | 2.7 | 11.4 | 5.3 | (11.5) | 22.6 | 9.5 |
| EBIT margins (%) | | | | | | | | | | | | |
| Soaps and detergents | 12.9 | 14.0 | 13.3 | 12.1 | 13.8 | 13.6 | 14.0 | 13.3 | 15.5 | 12.8 | 14.0 | 14.5 |
| Personal products | 24.9 | 22.8 | 28.6 | 25.0 | 27.6 | 24.4 | 27.7 | 27.8 | 29.6 | 26.1 | 28.9 | 29.5 |
| Beverages | 18.3 | 17.0 | 16.2 | 18.8 | 16.3 | 17.3 | 15.3 | 18.6 | 15.7 | 14.5 | 17.6 | 19.2 |
| Packaged Food | 8.4 | 3.3 | (3.6) | 5.5 | 10.9 | 4.4 | (5.1) | 5.3 | 8.9 | 5.3 | 3.2 | 5.7 |

Source: Edelweiss research

HUL Q1FY18 conference call: Key takeaways

Overall:

- Under volatile conditions, domestic consumer business grew at 6% with underlying volume growth remaining flat. Price growth actions from previous quarters continued.
- During the quarter, trade sentiment remained cautious, particularly in the run up to GST implementation. Despite high promotional intensity, stock pipelines remained low and varied across categories, channels and geographies.
- Rural growth has been slightly lower than urban growth. Rural markets continued to remain challenging. In the near term, the company expects rural demand to improve gradually. Affordable housing will go up which is likely to improve rural wages and hence consumption.
- Top priority is to build trade stocks to normative levels over the next few months.

- HUL is already profit accretive to Unilever and hence first objective is to increase penetration and deliver growth.

Pricing

- Expects a stream of products where prices have been reduced. This will be advertised as well.
- There has been distinct change in price vis-à-vis volume owing to changing mix.

GST

- HUL's transition to GST has been swift and smooth with no disruption.
- Geographies with higher wholesale proportion will take time to recover—wholesalers and smaller retailers have been impacted.
- No change in stock holding at the distributor level.
- Wholesalers are still figuring out compliance and will take time to return to normal buying. A few wholesalers are still sitting on the fence.
- **GST-led pricing actions have already started to land:** Output tax rate has been reduced for detergent bars, skin cleansers, toothpastes and hair oil. Output tax rate has been increased for detergent powders, hair care, skin creams, colour cosmetics and instant coffee. HUL will pass on the net benefit to consumers, as applicable. Post the rate changes, the company confirmed that there have been net benefits.
- Cut off related compensation (for 9 odd days of stock held at stockist level) will not be material.
- Aim is to restore trade pipeline on priority as well as to step-up communication to trade and advisors.
- No offtake by CSD channel for the past 45 days. However, recently a few depots have started to pick up stock. Impact of CSD sales on this quarter's sales was 2%.
- HUL has increased margins at GT or MT level wherever costs have increased.

Home care: Broad-based growth driven by premiumisation

- Q1FY18 saw strong growth across mass & premium laundry. Surf, the largest brand, maintained its robust volume led growth momentum.
- Surf continued to drive premiumisation.
- In detergents, mass markets also grew. The company will however, continue to drive premiumisation.
- Upgradation from bars to powders is likely which has been pushed by differential GST rate. However, dosage control and washing machine penetration will also need to be seen and will help enhance growth. Bars within detergents is ~40%. This percentage has remained at this level for over 3-4 years now.
- However, the water business witnessed a muted quarter due to lower trade purchases and destocking before GST implementation. This business will come back once the trade channel restores.
- Margin track record of this category has been good and will continue to grow.

Personal care: Growth rebounds in personal wash and personal products

- Growth was impacted disproportionately by thinning of trade pipelines, particularly in CSD.
- Personal wash clocked broad-based growth across brands. HUL has been growing in tandem with market.
- Colour cosmetics delivered yet another quarter of robust growth.
- Fair & Lovely relaunch was well received.
- Oral care performance continued to remain subdued.
- After successful test market, the company has rolled out *Lever Ayush* nationally. It is an ayurvedic range of personal care products spanning 6 categories of skin care, soaps, hair care, hand wash, body lotions and oral care. Nation-wide primary shipments for Ayush have just started. Communication will commence after 2-3 weeks.
- HUL will incrementally focus on increasing its play in male grooming. Hence, more activities in male grooming segment are expected.

Foods & refreshments: Modest growth

- Refreshments witnessed broad-based volume-led growth. In tea, double digit growth was sustained by leveraging differentiated portfolios across different parts of India.
- Coffee, ice cream and frozen desserts also delivered a robust quarter.
- In foods, the focus continued to be on market development for the category with soups and jams driving category growth.
- Nothing much to read in improvement in foods margin.

Margin improvement sustained:

- A combination of benign raw material prices as well as reduction in promotion activity helped improve gross margin.
- Strong margin delivery aided by savings agenda. Thinking and delivering end to end savings of 6% of turnover.
- Input costs remained stable and expected to remain so in the foreseeable future as well.
- Implemented ZBB—facilitated 20bps savings in A&P. EBITDA margin improvement was helped by ZBB.
- Overall strong savings delivery continues.

Distribution reach:

- HUL will continue to drive direct distribution.

Capex & tax rate

- Factory at Assam is still ramping up.

Management comment

- In light of GST implementation, HUL worked closely with all key shareholders including industry associations, the government and trade partners to prepare for smooth transition. Both growth and margin improvement were delivered through a combination of sustained innovation, a comprehensive savings programme and relentless focus on execution in market place.

HUL's new brand *Citra* in India | Skin care brand for women with focus on Naturals

- *Citra* is a brand in countries like Indonesia, Thailand and the Middle East. It is a complete skincare product that provides overall natural beauty.
- It was launched first as a **Hand & Body Lotion brand**. But, in recent years has expanded its brand to other segments, such as, **Body Scrub, Facial Wash and Facial Moisturiser**.
- *Citra's target consumers are women aged in the 15 to 35 age group who* want to take care of their skin.
- *Citra Body Scrub* effectively eliminates impurities from the skin and releases dead skin cells that make the skin look clean and fresh.
- Unilever also opened launched *Aktivasi Rumah Cantik Citra* in Indonesia, which is a semi permanent spa house to enjoy the full range of *Citra* products.

In our view, this will further strengthen HUL's dominance in skin care and also ward off competition from herbal players like Patanjali, Dabur, Himalaya, etc. Brand launches in past few years like *Tresemme* have done well in India.

Outlook and valuations: Long-term positive; maintain 'HOLD'

We remain positive on HUL's ability to outpace market growth and its pricing power due to the company's distribution expansion, deepening direct reach and product innovation initiatives. Despite tough market conditions with GST rollout from July 2017, it efficiently managed volumes. Pricing growth has largely returned, which along with pick up in volumes will help boost overall growth to double digits. Also, GST will help create a level playing field, rendering a large organised player like HUL the biggest beneficiary. However, it will face some short-term pressure till the time trade channel imbalances are ironed out. Cost savings and mix improvement are bound to spur margins structurally—HUL's margin has improved in the past 6 consecutive years. Margin, going forward, is expected to further improve helped by cost saving initiatives such as zero-based budgeting, efficiency in ad spends, etc. Globally, Unilever is targeting ~200-300bps YoY improvement in overall margins led by costs savings initiatives; HUL is also likely to see some impact of the same.

HUL has taken cognisance of the rising potential in the natural space and labeled it a mega trend. Launch of the *Ayush* master brand in the mass segment across categories like toothpaste, facewash, shampoo, conditioner, etc., is envisaged to propel growth. However, Patanjali's aggression, especially in core segments of soaps & detergents, needs to be closely monitored. On account of better-than-expected Q1FY18 numbers, we revise up our EPS 2.6%/4.2% for FY18/19E, respectively, and also our target multiple to 44x (earlier 40x) to arrive at revised TP of INR1,253. We maintain 'HOLD/SP'.

Chart 1: Overall volume growth

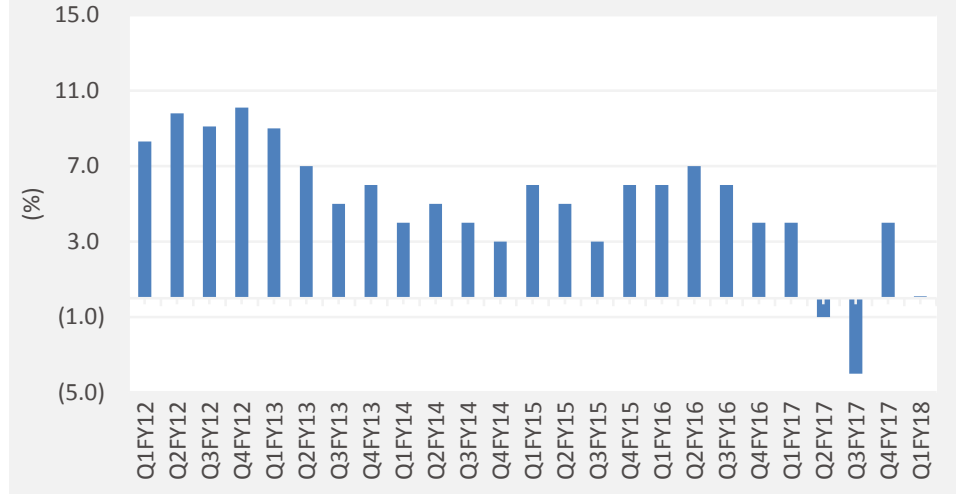


Chart 2: A&P spends

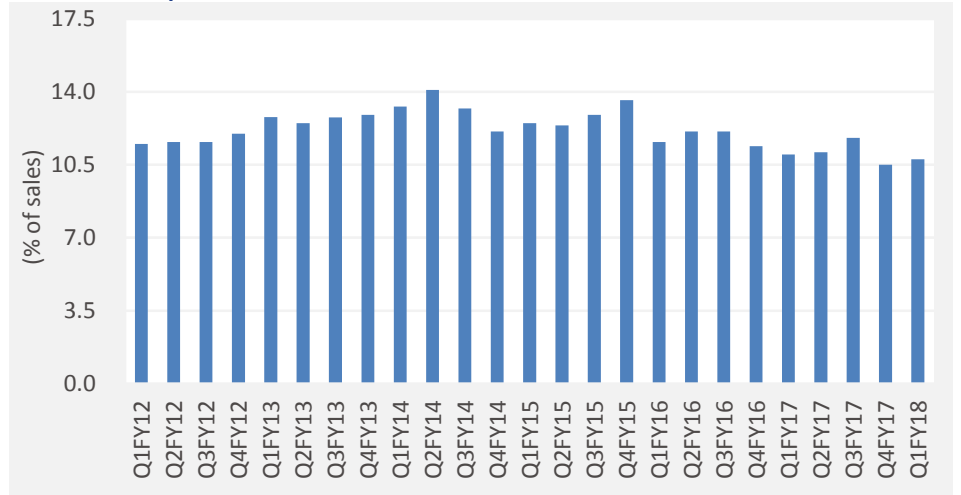
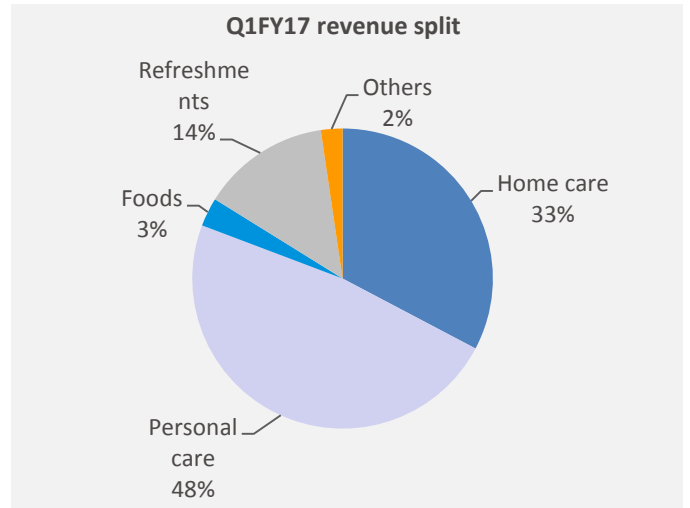
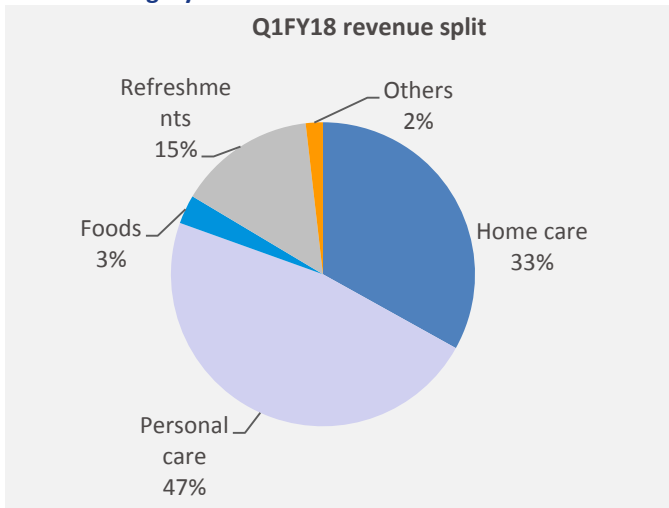
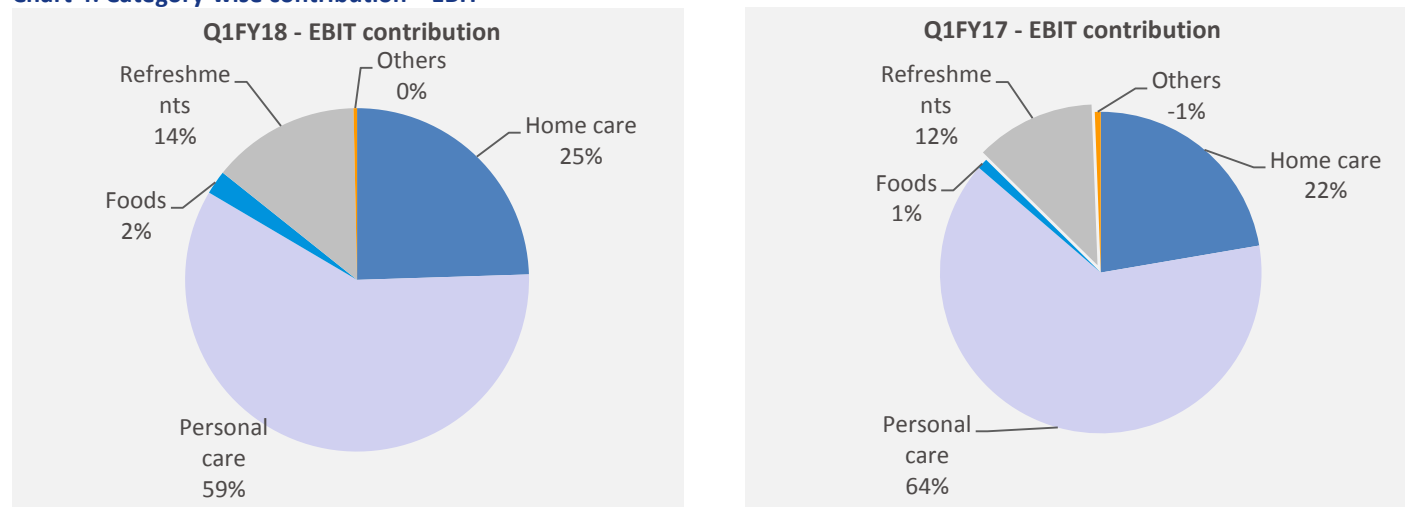


Chart 3: Category-wise contribution—Sales



Source: Company, Edelweiss research

Chart 4: Category-wise contribution—EBIT



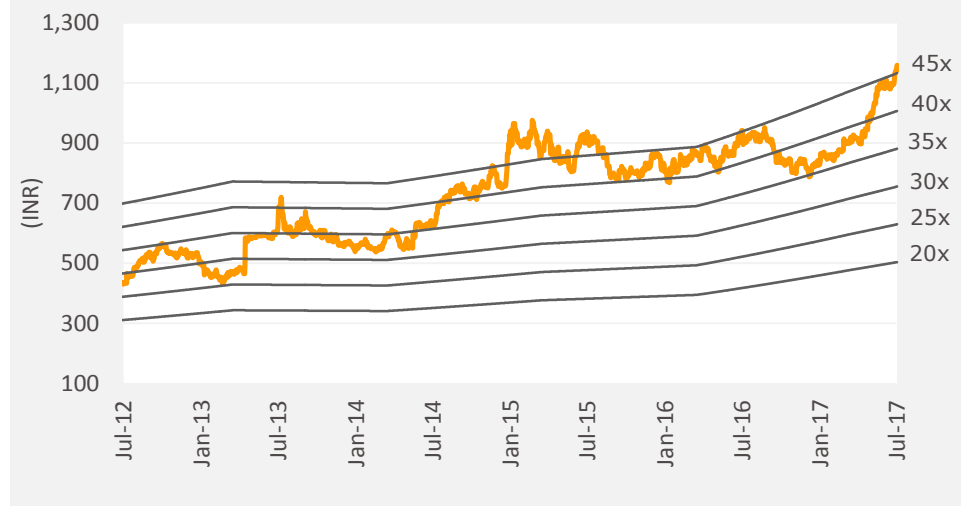
Source: Company, Edelweiss research

Table 3: Segmental performance

| Year to March - Revenues (INR mn) | Q1FY18 | Q1FY17 | YoY growth | Q4FY17 | QoQ growth |
|--|--------|--------|------------|--------|------------|
| Home care | 30,470 | 28,760 | 5.9 | 30,040 | 1.4 |
| Personal care | 43,680 | 42,220 | 3.5 | 40,750 | 7.2 |
| Foods | 2,840 | 2,720 | 4.4 | 2,950 | (3.7) |
| Refreshments | 13,460 | 12,150 | 10.8 | 13,000 | 3.5 |
| Others (includes exports, infant and feminine care etc) | 1,680 | 2,040 | (17.6) | 2,010 | (16.4) |
| Segment results (Profit/(Loss) before tax and interest) | | | | | |
| Home care | 4,480 | 3,560 | 25.8 | 3,890 | 15.2 |
| Personal care | 10,790 | 10,214 | 5.6 | 9,840 | 9.7 |
| Foods | 410 | 170 | 141.6 | 280 | 46.4 |
| Refreshments | 2,550 | 1,921 | 32.8 | 2,190 | 16.4 |
| Others (includes exports, infant and feminine care etc) | (60) | (95) | NA | (40) | NM |
| Segment margins | | | | | |
| Margin (%) | | | | | |
| Home care | 14.7 | 12.4 | 232 | 12.9 | 175 |
| Personal care | 24.7 | 24.2 | 51 | 24.1 | 56 |
| Foods | 14.4 | 6.2 | 820 | 9.5 | 495 |
| Refreshments | 18.9 | 15.8 | 314 | 16.8 | 210 |
| Others (includes exports, infant and feminine care etc) | (3.6) | (4.6) | NM | (2.0) | NM |

Source: Company, Edelweiss research

Chart 5: One year forward P/E chart



Source: Edelweiss research

Financial snapshot

(INR mn)

| Year to March | Q1FY18 | Q1FY17 | % change | Q4FY17 | % change | FY17 | FY18E | FY19E |
|-----------------------------|--------|--------|----------|--------|----------|---------|---------|---------|
| Net revenues | 85,290 | 81,282 | 4.9 | 82,130 | 3.8 | 331,620 | 367,163 | 413,286 |
| Cost of goods sold | 40,840 | 39,555 | 3.2 | 40,220 | 1.5 | 163,130 | 178,784 | 198,544 |
| Gross profit | 44,450 | 41,727 | 6.5 | 41,910 | 6.1 | 168,490 | 188,379 | 214,742 |
| Staff costs | 4,190 | 4,265 | (1.8) | 3,880 | 8.0 | 17,430 | 19,092 | 21,078 |
| Advt. sales & promotions | 9,050 | 8,798 | 2.9 | 8,530 | 6.1 | 35,420 | 38,185 | 42,569 |
| Other expenses | 12,550 | 12,306 | 2.0 | 12,990 | (3.4) | 52,240 | 56,910 | 62,406 |
| Total expenditure | 25,790 | 25,368 | 1.7 | 25,400 | 1.5 | 105,090 | 114,188 | 126,052 |
| EBITDA | 18,660 | 16,359 | 14.1 | 16,510 | 13.0 | 63,400 | 74,192 | 88,690 |
| Depreciation | 1,140 | 933 | 22.2 | 1,080 | 5.6 | 4,320 | 4,537 | 4,943 |
| EBIT | 17,520 | 15,426 | 13.6 | 15,430 | 13.5 | 59,080 | 69,654 | 83,747 |
| Other income | 1,130 | 1,076 | 5.0 | 830 | 36.1 | 3,690 | 5,060 | 5,299 |
| Interest | 60 | 60 | 0.8 | 60 | 0.0 | 350 | 150 | 120 |
| Add: Prior period items | | | | | | | | |
| Add: Exceptional items | (130) | 459 | NA | 650 | NA | 2,370 | - | - |
| Profit before tax | 18,590 | 16,442 | 13.1 | 16,200 | 14.8 | 62,420 | 74,564 | 88,925 |
| Provision for taxes | 5,630 | 5,162 | 9.1 | 5,020 | 12.2 | 19,770 | 22,742 | 27,122 |
| Minority interest | - | - | - | - | - | - | 127 | 143 |
| Associate profit share | | | | | | | | |
| Reported net profit | 12,830 | 11,739 | 9.3 | 11,830 | 8.5 | 45,020 | 51,695 | 61,660 |
| Adjusted Profit | 12,960 | 11,280 | 14.9 | 11,180 | 15.9 | 42,650 | 51,695 | 61,660 |
| Diluted shares (mn) | 2,164 | 2,164 | | 2,164 | | 2,164 | 2,164 | 2,164 |
| Adjusted Diluted EPS | 6.0 | 5.2 | 14.9 | 5.2 | 15.9 | 19.7 | 23.9 | 28.5 |
| Diluted P/E (x) | | | | | | 58.8 | 48.5 | 40.6 |
| EV/EBITDA (x) | | | | | | 38.7 | 33.1 | 27.6 |
| ROAE (%) | | | | | | 63.8 | 73.6 | 80.8 |
| As % of net revenues | | | | | | | | |
| COGS | 48.6 | 49.5 | | 49.7 | | 50.4 | 49.9 | 49.1 |
| Employee cost | 5.0 | 5.3 | | 4.8 | | 5.4 | 5.3 | 5.2 |
| Adv. & sales promotions | 10.8 | 11.0 | | 10.5 | | 10.9 | 10.6 | 10.5 |
| Other expenditure | 14.9 | 15.4 | | 16.0 | | 16.1 | 15.9 | 15.4 |
| EBITDA | 22.2 | 20.5 | | 20.4 | | 19.6 | 20.7 | 22.0 |
| EBIT | 20.9 | 19.3 | | 19.0 | | 18.3 | 19.4 | 20.7 |
| PBT | 22.1 | 20.6 | | 20.0 | | 19.3 | 20.8 | 22.0 |
| Reported net profit | 15.4 | 14.1 | | 13.8 | | 13.2 | 14.4 | 15.3 |
| Tax rate | 30.3 | 31.4 | | 31.0 | | 31.7 | 30.5 | 30.5 |

Company Description

HUL, the largest FMCG Company in India, was formed by merging three subsidiaries of Unilever in 1956. At present, Unilever Plc holds a 67.2% stake in the company. HUL's portfolio of products covers a wide spectrum including soaps, detergents, skin creams, shampoos, toothpastes, tea, coffee, packaged foods and branded atta.

Powerful brands and an enviable distribution network (direct coverage of 3.2mn outlets) are HUL's primary strengths. The company operates through segments—Home care, personal care, Refreshments, Foods and other operations.

Investment Theme

HUL is a play on consumption growth in India. The company has displayed its ability to effect price hikes and ability to grow ahead of market, which, combined with improved outlook for S&D and personal care, and strong growth in processed foods and beverages, boosts our positive outlook on the company. We like its revenue growth from a medium to long term perspective. Commodity price correction will aid gross margin expansion though we expect partial benefit to be passed on to customers through promotional offers/select price cuts. We expect higher investment in A&P to support brand equity and counter pick up in competitive intensity (especially from regional players). However with an anticipated recovery in urban demand and commodity correction to aid EBITDA margin expansion, we expect HUL to potentially benefit.

Key Risks

Depreciation in rupee impacts price of imported raw materials.

Ad spends likely to spike due to increased competition from regional players. Maintaining market share will also be a challenge for HUL.

The price war in HUL's popular segments with new entrants entering the fray could hit the company hard.

Financial Statements

Key Assumptions

| Year to March | FY16 | FY17 | FY18E | FY19E |
|------------------------------|-------|--------|-------|-------|
| Macro | | | | |
| GDP(Y-o-Y %) | 7.2 | 6.5 | 7.1 | 7.7 |
| Inflation (Avg) | 4.9 | 4.5 | 4.0 | 4.5 |
| Repo rate (exit rate) | 6.8 | 6.3 | 5.8 | 5.8 |
| USD/INR (Avg) | 65.0 | 67.5 | 66.0 | 66.0 |
| Company | | | | |
| Volume gr. (overall) | 6.0 | 1.0 | 5.0 | 7.0 |
| Pricing gr. (overall) | (1.9) | 2.2 | 5.6 | 5.7 |
| Growth in Soaps | (3.5) | (3.0) | 9.0 | 11.0 |
| Growth in Detergents | 3.9 | 3.0 | 8.0 | 12.0 |
| Growth in PP | 7.4 | 1.0 | 10.0 | 15.0 |
| Growth in beverages | 6.9 | 5.0 | 12.0 | 15.0 |
| Growth in packaged foods | 11.9 | 1.0 | 10.0 | 12.0 |
| EBITDA margin (%) | 19.1 | 19.6 | 20.7 | 22.0 |
| EBITDA margin assumpn | | | | |
| Oil fat resin % of COGS | 9.8 | 11.1 | 10.6 | 10.6 |
| Chem & perfume % of COGS | 30.2 | 32.9 | 31.0 | 31.2 |
| Tea & Grn leaf % of COGS | 10.1 | 9.7 | 8.9 | 9.0 |
| Selling & distribn costs | 15.2 | 15.8 | 15.5 | 15.1 |
| A&P as % of sales | 11.6 | 10.9 | 10.6 | 10.5 |
| Employee cost (% of rev) | 5.3 | 5.4 | 5.3 | 5.2 |
| Financial assumptions | | | | |
| Tax rate (%) | 31.0 | 31.7 | 30.5 | 30.5 |
| Capex (INR mn) | 7,060 | 15,000 | 7,410 | 7,000 |
| Debtor days | 13 | 13 | 14 | 14 |
| Inventory days | 64 | 59 | 61 | 63 |
| Payable days | 129 | 133 | 130 | 130 |
| Cash conversion cycle | (52) | (61) | (55) | (53) |
| Dep. (% gross block) | 6.3 | 6.4 | 5.8 | 5.8 |
| Yield on cash | 6.9 | 6.6 | 9.0 | 10.0 |

Income statement

(INR mn)

| Year to March | FY16 | FY17 | FY18E | FY19E |
|--------------------------|---------|---------|---------|---------|
| Net revenue | 314,610 | 323,670 | 358,577 | 404,014 |
| Other Operating Income | 7,250 | 7,950 | 8,586 | 9,273 |
| Total operating income | 321,860 | 331,620 | 367,163 | 413,286 |
| Materials costs | 158,670 | 163,130 | 178,784 | 198,544 |
| Gross profit | 163,190 | 168,490 | 188,379 | 214,742 |
| Employee costs | 16,800 | 17,430 | 19,092 | 21,078 |
| Other Expenses | 49,630 | 52,240 | 56,910 | 62,406 |
| Ad. & sales costs | 36,560 | 35,420 | 38,185 | 42,569 |
| EBITDA | 60,200 | 63,400 | 74,192 | 88,690 |
| Depreciation | 3,530 | 4,320 | 4,537 | 4,943 |
| EBIT | 56,670 | 59,080 | 69,654 | 83,747 |
| Add: Other income | 4,230 | 3,690 | 5,060 | 5,299 |
| Less: Interest Expense | 170 | 350 | 150 | 120 |
| Add: Exceptional items | (310) | 2,370 | - | - |
| Profit Before Tax | 60,730 | 62,420 | 74,564 | 88,925 |
| Less: Provision for Tax | 18,750 | 19,770 | 22,742 | 27,122 |
| Less: Minority Interest | 90 | - | 127 | 143 |
| Reported Profit | 41,580 | 45,020 | 51,695 | 61,660 |
| Exceptional Items | (310) | 2,370 | - | - |
| Adjusted Profit | 41,890 | 42,650 | 51,695 | 61,660 |
| Shares o/s (mn) | 2,164 | 2,164 | 2,164 | 2,164 |
| Adjusted Basic EPS | 19.4 | 19.7 | 23.9 | 28.5 |
| Diluted shares o/s (mn) | 2,165 | 2,165 | 2,165 | 2,165 |
| Adjusted Diluted EPS | 19.4 | 19.7 | 23.9 | 28.5 |
| Adjusted Cash EPS | 21.0 | 21.7 | 26.0 | 30.8 |
| Dividend per share (DPS) | 15.5 | 16.5 | 17.9 | 21.4 |
| Dividend Payout Ratio(%) | 96.6 | 95.0 | 89.6 | 89.6 |

Common size metrics

| Year to March | FY16 | FY17 | FY18E | FY19E |
|--------------------|------|------|-------|-------|
| Materials costs | 50.4 | 50.4 | 49.9 | 49.1 |
| Staff costs | 5.3 | 5.4 | 5.3 | 5.2 |
| Ad. & sales costs | 11.6 | 10.9 | 10.6 | 10.5 |
| Interest Expense | 0.1 | 0.1 | - | - |
| EBITDA margins | 19.1 | 19.6 | 20.7 | 22.0 |
| Net Profit margins | 13.3 | 13.2 | 14.5 | 15.3 |

Growth ratios (%)

| Year to March | FY16 | FY17 | FY18E | FY19E |
|-----------------|------|------|-------|-------|
| Revenues | 4.1 | 2.9 | 10.8 | 12.7 |
| EBITDA | 9.9 | 5.3 | 17.0 | 19.5 |
| Adjusted Profit | 13.7 | 1.8 | 21.2 | 19.3 |
| EPS | 13.7 | 1.8 | 21.2 | 19.3 |

| Balance sheet | | (INR mn) | | | |
|--------------------------|---------------|---------------|---------------|---------------|--|
| As on 31st March | FY16 | FY17 | FY18E | FY19E | |
| Share capital | 2,164 | 2,164 | 2,164 | 2,164 | |
| Reserves & Surplus | 63,570 | 65,280 | 70,680 | 77,120 | |
| Shareholders' funds | 65,734 | 67,444 | 72,844 | 79,285 | |
| Minority Interest | 200 | 220 | 347 | 490 | |
| Short term borrowings | 1,770 | 2,770 | 2,770 | 2,770 | |
| Total Borrowings | 1,770 | 2,770 | 2,770 | 2,770 | |
| Long Term Liabilities | 11,330 | 12,260 | 12,260 | 12,260 | |
| Def. Tax Liability (net) | (1,670) | (1,700) | (1,700) | (1,700) | |
| Sources of funds | 77,364 | 80,994 | 86,521 | 93,105 | |
| Gross Block | 59,730 | 74,730 | 81,730 | 88,730 | |
| Net Block | 31,650 | 39,680 | 42,143 | 44,199 | |
| Capital work in progress | 4,080 | 2,290 | 2,700 | 2,700 | |
| Intangible Assets | 930 | 4,510 | 4,510 | 4,510 | |
| Total Fixed Assets | 36,660 | 46,480 | 49,353 | 51,409 | |
| Non current investments | 320 | 60 | 60 | 60 | |
| Cash and Equivalents | 55,690 | 56,160 | 52,929 | 58,334 | |
| Inventories | 27,260 | 25,410 | 29,879 | 34,269 | |
| Sundry Debtors | 12,640 | 10,850 | 14,083 | 15,852 | |
| Loans & Advances | 3,860 | 4,590 | 4,590 | 4,590 | |
| Other Current Assets | 9,834 | 11,814 | 11,814 | 11,814 | |
| Current Assets (ex cash) | 53,594 | 52,664 | 60,366 | 66,526 | |
| Trade payable | 56,850 | 61,860 | 63,676 | 70,714 | |
| Other Current Liab | 12,050 | 12,510 | 12,510 | 12,510 | |
| Total Current Liab | 68,900 | 74,370 | 76,186 | 83,224 | |
| Net Curr Assets-ex cash | (15,306) | (21,706) | (15,820) | (16,699) | |
| Uses of funds | 77,364 | 80,994 | 86,521 | 93,105 | |
| BVPS (INR) | 30.4 | 31.2 | 33.7 | 36.6 | |

| Free cash flow | | (INR mn) | | | |
|-----------------------|---------------|---------------|---------------|---------------|--|
| Year to March | FY16 | FY17 | FY18E | FY19E | |
| Reported Profit | 41,580 | 45,020 | 51,695 | 61,660 | |
| Add: Depreciation | 3,530 | 4,320 | 4,537 | 4,943 | |
| Interest (Net of Tax) | 118 | 239 | 104 | 83 | |
| Others | (2,628) | (4,669) | 173 | 180 | |
| Less: Changes in WC | 120 | (8,650) | 5,886 | (879) | |
| Operating cash flow | 42,480 | 53,560 | 50,624 | 67,745 | |
| Less: Capex | 7,060 | 15,000 | 7,410 | 7,000 | |
| Free Cash Flow | 35,420 | 38,560 | 43,214 | 60,745 | |

Peer comparison valuation

| Name | Market cap (USD mn) | Diluted P/E (X) | | EV / EBITDA (X) | | ROAE (%) | |
|--------------------|------------------------|-----------------|-------|-----------------|-------|----------|-------|
| | | FY18E | FY19E | FY18E | FY19E | FY18E | FY19E |
| Hindustan Unilever | 38,953 | 48.5 | 40.6 | 33.1 | 27.6 | 73.6 | 80.8 |
| Colgate | 4,537 | 42.8 | 36.9 | 26.9 | 23.0 | 52.6 | 52.0 |
| Dabur | 8,211 | 36.5 | 31.2 | 31.2 | 26.3 | 27.5 | 27.7 |
| Godrej Consumer | 10,124 | 41.7 | 34.3 | 30.0 | 24.9 | 24.7 | 26.0 |
| ITC | 53,789 | 29.7 | 26.2 | 19.6 | 17.2 | 28.9 | 29.6 |
| Nestle Ltd | 10,269 | 51.2 | 39.6 | 28.2 | 22.1 | 39.4 | 41.9 |
| Median | - | 42.3 | 35.6 | 29.1 | 23.9 | 34.1 | 35.8 |
| AVERAGE | - | 41.7 | 34.8 | 28.2 | 23.5 | 41.1 | 43.0 |

Source: Edelweiss research

| Cash flow metrics | | FY16 | FY17 | FY18E | FY19E |
|---------------------|--|----------|----------|----------|----------|
| Year to March | | | | | |
| Operating cash flow | | 41,790 | 52,060 | 50,624 | 67,745 |
| Investing cash flow | | (2,820) | (11,730) | (7,410) | (7,000) |
| Financing cash flow | | (38,640) | (42,140) | (46,445) | (55,339) |
| Net cash Flow | | 330 | (1,810) | (3,231) | 5,406 |
| Capex | | (7,060) | (15,000) | (7,410) | (7,000) |
| Dividend paid | | (40,090) | (42,640) | (46,295) | (55,219) |

Profitability and efficiency ratios

| Year to March | FY16 | FY17 | FY18E | FY19E |
|-------------------------|-------|-------|-------|-------|
| ROAE (%) | 78.9 | 63.8 | 73.6 | 80.8 |
| ROACE (%) | 112.1 | 90.9 | 102.1 | 112.4 |
| Inventory Days | 63 | 59 | 61 | 63 |
| Debtors Days | 14 | 13 | 14 | 14 |
| Payable Days | 131 | 133 | 130 | 130 |
| Cash Conversion Cycle | (54) | (61) | (55) | (53) |
| Current Ratio | 1.6 | 1.5 | 1.5 | 1.5 |
| Adjusted Debt/Equity | - | - | - | - |
| Net Debt/Equity | (0.8) | (0.8) | (0.7) | (0.7) |
| Interest Coverage Ratio | 333.4 | 168.8 | 464.4 | 697.9 |

Operating ratios

| Year to March | FY16 | FY17 | FY18E | FY19E |
|----------------------|------|------|-------|-------|
| Total Asset Turnover | 4.9 | 4.1 | 4.3 | 4.5 |
| Fixed Asset Turnover | 10.4 | 8.4 | 7.9 | 8.5 |
| Equity Turnover | 5.9 | 4.8 | 5.1 | 5.3 |

Valuation parameters

| Year to March | FY16 | FY17 | FY18E | FY19E |
|-------------------------|------|------|-------|-------|
| Adj. Diluted EPS (INR) | 19.4 | 19.7 | 23.9 | 28.5 |
| Y-o-Y growth (%) | 13.7 | 1.8 | 21.2 | 19.3 |
| Adjusted Cash EPS (INR) | 21.0 | 21.7 | 26.0 | 30.8 |
| Diluted P/E (x) | 59.8 | 58.8 | 48.5 | 40.6 |
| P/B (x) | 38.1 | 37.2 | 34.4 | 31.6 |
| EV / Sales (x) | 7.8 | 7.6 | 6.8 | 6.1 |
| EV / EBITDA (x) | 40.7 | 38.7 | 33.1 | 27.6 |
| Dividend Yield (%) | 1.3 | 1.4 | 1.5 | 1.8 |

Additional Data

Directors Data

| | | | |
|--------------------|--|----------------------|---|
| Mr. Harish Manwani | Chairman | Mr. Sanjiv Mehta | Managing Director and Chief Executive Officer |
| Mr. P. B. Balaji | Executive Director, Finance & IT and Chief Financial Officer | Mr. Pradeep Banerjee | Executive Director, Supply Chain |
| Mr. Dev Bajpai | Executive Director, Legal & CS | Mr. A. Narayan | Independent Director |
| Mr. S. Ramadorai | Independent Director | Ms. Kalpana Morparia | Independent Director |
| Mr. O. P. Bhatt | Independent Director | Dr. Sanjiv Misra | Independent Director |

Auditors - BSR & Co. LLP

**as per last annual report*

Holding – Top10

| | Perc. Holding | | Perc. Holding |
|--------------------------------|---------------|---------------------------------|---------------|
| Life Insurance Corp Of India | 1.7 | Aberdeen Asset Managers | 1.3 |
| Blackrock Fund Advisors | 1.1 | Vanguard Group | 1.1 |
| Franklin Resources | 0.5 | Vontobel Asset Management | 0.4 |
| ICICI Prudential Asset Mgmt Co | 0.4 | Birla Sun Life Asset Management | 0.3 |
| Virtus Investment Partners | 0.3 | Schroders Plc | 0.3 |

**as per last available data*

Bulk Deals

| Data | Acquired / Seller | B/S | Qty Traded | Price |
|-------------------|-------------------|-----|------------|-------|
| No Data Available | | | | |

**in last one year*

Insider Trades

| Reporting Data | Acquired / Seller | B/S | Qty Traded |
|-------------------|-------------------|-----|------------|
| No Data Available | | | |

**in last one year*

| Company | Absolute reco | Relative reco | Relative risk | Company | Absolute reco | Relative reco | Relative Risk |
|-----------------|---------------|---------------|---------------|-------------------------------------|---------------|---------------|---------------|
| Asian Paints | BUY | SO | M | Bajaj Corp | HOLD | SU | H |
| Berger Paints | BUY | SO | L | Britannia Industries | BUY | SO | L |
| Colgate | HOLD | SP | M | Dabur | BUY | SO | M |
| Emami | BUY | SO | H | GlaxoSmithKline Consumer Healthcare | HOLD | SU | M |
| Godrej Consumer | BUY | SO | H | Hindustan Unilever | HOLD | SP | L |
| ITC | HOLD | SP | M | Marico | BUY | SO | M |
| Nestle Ltd | HOLD | SP | L | Pidilite Industries | BUY | SO | M |
| United Spirits | HOLD | SP | H | | | | |

ABSOLUTE RATING

| Ratings | Expected absolute returns over 12 months |
|---------|--|
| Buy | More than 15% |
| Hold | Between 15% and - 5% |
| Reduce | Less than -5% |

RELATIVE RETURNS RATING

| Ratings | Criteria |
|----------------------------|-------------------------------------|
| Sector Outperformer (SO) | Stock return > 1.25 x Sector return |
| Sector Performer (SP) | Stock return > 0.75 x Sector return |
| | Stock return < 1.25 x Sector return |
| Sector Underperformer (SU) | Stock return < 0.75 x Sector return |

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

| Ratings | Criteria |
|------------|---------------------------------------|
| Low (L) | Bottom 1/3rd percentile in the sector |
| Medium (M) | Middle 1/3rd percentile in the sector |
| High (H) | Top 1/3rd percentile in the sector |

Risk ratings are based on Edelweiss risk model

SECTOR RATING

| Ratings | Criteria |
|------------------|-------------------------------------|
| Overweight (OW) | Sector return > 1.25 x Nifty return |
| Equalweight (EW) | Sector return > 0.75 x Nifty return |
| | Sector return < 1.25 x Nifty return |
| Underweight (UW) | Sector return < 0.75 x Nifty return |

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Aditya Narain

Head of Research

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Coverage group(s) of stocks by primary analyst(s): Consumer Goods

Asian Paints, Bajaj Corp, Berger Paints, Britannia Industries, Colgate, Dabur, Godrej Consumer, Emami, Hindustan Unilever, ITC, Marico, Nestle Ltd, Pidilite Industries, GlaxoSmithKline Consumer Healthcare, United Spirits

Recent Research

| Date | Company | Title | Price (INR) | Recos |
|-----------|----------------|--|-------------|-------|
| 17-Jul-17 | ITC | Negative surprise on cess; Company Update | 325 | Hold |
| 14-Jul-17 | Consumer Goods | Food for thought: Prudent diversification; Sector Update | | |
| 13-Jul-17 | Bajaj Corp | Destocking pangs dent volumes; Outlook improving; Result Update | 410 | Hold |

Distribution of Ratings / Market Cap

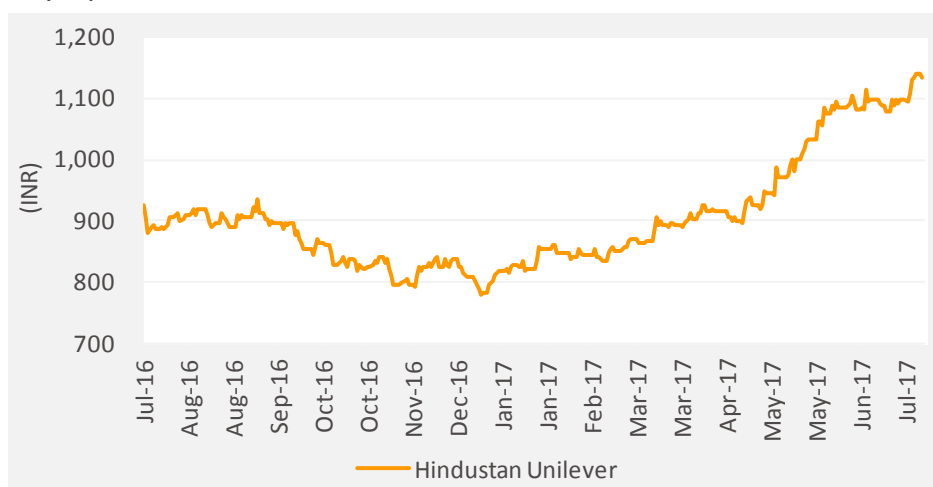
Edelweiss Research Coverage Universe

| | Buy | Hold | Reduce | Total |
|------------------------|--------|------------------------|--------|-------|
| Rating Distribution* | 161 | 67 | 11 | 240 |
| * 1stocks under review | | | | |
| | > 50bn | Between 10bn and 50 bn | < 10bn | |
| Market Cap (INR) | 156 | 62 | 11 | |

Rating Interpretation

| Rating | Expected to |
|--------|---|
| Buy | appreciate more than 15% over a 12-month period |
| Hold | appreciate up to 15% over a 12-month period |
| Reduce | depreciate more than 5% over a 12-month period |

One year price chart



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