COMPANY UPDATE

# ITC

## Negative surprise on cess

India Equity Research| Consumer Goods

**In a negative surprise, the GST Council on Monday stepped in to check the windfall being reaped by cigarette manufacturers and increased effective tax under GST by ~10-11% which will result in MRP increase of ~8-9%. This with 6% hike in the Budget 2017-18 amounts to ~16-17% total hike in taxes for FY18. So, why was this unexpected? The Budget had sprung a positive surprise with mere 6% tax hike (lowest hike in past 6 years) coupled with relatively softer stance in earlier GST. In the past (FY13-16), when the hike in tax was ~18% on an average, ITC's volumes declined by ~20% over the period. Accordingly, we cut our cigarette volume estimates for FY18/19 to 5% / 2% YoY decline versus 5%/5% YoY growth, respectively. Ergo, we cut EPS estimates by 5.6%/8.2% YoY for FY18/19 respectively and cigarette business multiple to 27x (30x earlier). We downgrade to 'HOLD'.**

### Unexpected hike in new GST rates

**The government increased the fixed component of cess across all cigarette sizes (except for 84mm) by ~27%, which was unexpected. For 84mm cigarette, the government increased the ad valorem rate to 36% (5% earlier) - this along with 28% GST rate increased ad-valorem component to 64%.** 84mm cigarettes post this move should see maximum price hike which would likely impact volumes and margins. **Government's move to hike taxes to more than pre-GST levels brings to fore its negative stance on the sin sector**. Finance Minister mentioned in his speech that the government proposes to reverse the windfall gain being garnered by cigarette companies. **Even if this policy gets partially rolled back, uncertainty would still loom large over the taxation policy for cigarette companies.**

### Outlook and valuations: Uncertainty looms; downgrade to 'HOLD'

With per capita consumption 1/18th of China's, cigarette opportunity in India remains attractive over long term. Negative surprise on taxation front coupled with uncertainty will keep the stock under pressure. We value ITC on SoTP basis on FY19E and arrive at a target price of INR304. We downgrade to **'HOLD/SP'** from 'BUY/SO'.

### Financials (INR mn)

| Year to March | FY16 | FY17E | FY18E | FY19E |
|---|---|---|---|---|
| Net revenue | 388,042 | 423,600 | 457,266 | 512,295 |
| *Rev. growth (%)* | *1.0* | *9.2* | *7.9* | *12.0* |
| EBITDA | 144,509 | 154,359 | 166,288 | 187,245 |
| Adjusted Profit | 95,009 | 104,773 | 115,178 | 130,687 |
| Diluted equity shares (mn) | 12,108 | 12,040 | 12,040 | 12,040 |
| Adjusted diluted EPS (INR) | 7.8 | 8.7 | 9.6 | 10.9 |
| *EPS Growth (%)* | *(1.9)* | *10.9* | *9.9* | *13.5* |
| Diluted P/E (x) | 41.4 | 37.4 | 34.0 | 30.0 |
| EV/EBITDA (x) | 26.2 | 24.4 | 22.5 | 19.9 |
| ROAE (%) | 28.7 | 29.0 | 28.9 | 29.6 |

**EDELWEISS 4D RATINGS**

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

**MARKET DATA** *(R: ITC.BO, B: ITC IN)*

| | |
|---|---|
| CMP | : INR 325 |
| Target Price | : INR 304 |
| 52-week range (INR) | : 368 / 222 |
| Share in issue (mn) | : 12,152.2 |
| M cap (INR bn/USD mn) | : 3,951 / 61,466 |
| Avg. Daily Vol.BSE/NSE('000) | : 11,432.2 |

**SHARE HOLDING PATTERN (%)**

| | Current | Q3FY17 | Q2FY17 |
|---|---|---|---|
| Promoters * | - | - | - |
| MF's, FI's & BK's | 35.7 | 35.3 | 34.9 |
| FII's | 20.0 | 20.2 | 20.8 |
| Others | 44.2 | 44.4 | 44.2 |

** Promoters pledged shares (% of share in issue) : NIL*

**PRICE PERFORMANCE (%)**

| | Stock | Nifty | EW Consumer goods Index |
|---|---|---|---|
| 1 month | 6.0 | 3.4 | 5.0 |
| 3 months | 16.5 | 8.9 | 16.2 |
| 12 months | 30.6 | 16.5 | 23.9 |


**Abneesh Roy**
+91 22 6620 3141
abneesh.roy@edelweissfin.com

**Tanmay Sharma, CFA**
+91 22 4040 7586
tanmay.sharma@edelweissfin.com

**Alok Shah**
+91 22 6620 3040
alok.shah@edelweissfin.com


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**Table 1: Total cess under GST (new rates)**

| Segments | GST cess | NCCD | Total cess under GST with NCCD |
|---|---|---|---|
| Not exceeding 65mm | 5% plus INR2,076 per thousand sticks | 90 | 5% plus INR2,116 per thoudsand sticks |
| Exceeding 65mm but not 70mm | 5% plus INR2,747 per thousand sticks | 90 | 5% plus INR2,837 per thoudsand sticks |
| Exceeding 70mm but not 75mm | 5% plus INR3,668 per thousand sticks | 145 | 5% plus INR3,813 per thoudsand sticks |
| Others | 36% plus INR4,170 per thousand sticks | 235 | 36% plus INR4,405 per thoudsand sticks |

**Table 2: Total cess under GST as per the old rates**

| Segments | GST cess | NCCD | Total cess under GST with NCCD |
|---|---|---|---|
| Not exceeding 65mm | 5% plus INR1,591 per thousand sticks | 90 | 5% plus INR1,681 per thoudsand sticks |
| Exceeding 65mm but not 70mm | 5% plus INR2,126 per thousand sticks | 90 | 5% plus INR2,216 per thoudsand sticks |
| Exceeding 70mm but not 75mm | 5% plus INR2,876 per thousand sticks | 145 | 5% plus INR3,021 per thoudsand sticks |
| Others | 5% plus INR4,170 per thousand sticks | 235 | 5% plus INR4,405 per thoudsand sticks |

**Table 3: Hike in taxation over the years in cigarettes**

| Budget year | Excise Duty Hike (%) | Nature of excise hike in the Budget |
|---|---|---|
| FY18 | ~16-17% (6% in Budget and ~11% in GST) | Harsh |
| FY17 | 10% | Moderate |
| FY16 | 13% weighted average (25% on 64mm; 15% on other size) | Harsh |
| FY15 | 21% weighted average (11-72% range) | Harsh |
| FY14 | 18% (applicable on above 64mm size) | Harsh |
| FY13 | 20% | Harsh |
| FY12 | No change in duty | Soft |
| FY11 | 15% | Harsh |
| FY10 | No change in duty | Soft |
| FY09 | Increased tax on non filter cig by 200% | Moderate |
| FY08 | Specific rates of duty on cigarettes increased by 5% | Soft |
| FY07 | 5% | Soft |
| FY06 | 10% | Moderate |
| FY05 | No change in duty | Soft |
| FY04 | No change in duty | Soft |
| FY03 | No change in duty | Soft |
| FY02 | 15% | Harsh |
| FY01 | 5% | Soft |
| FY00 | No change in duty | Soft |

**Table 4: Likely increase in MRP and taxation for 64mm cigarettes under the new GST rates**

| 64mm excise rate per stick | PRE GST SCENARIO<br>INR1681 per 1000 sticks | OLD GST RATE<br>5% plus INR1681 per 1000 sticks | NEW GST RATE<br>5% plus INR2116 per 1000 sticks | Price increase / (decrease) |
|---|---|---|---|---|
| Factory costs (assumed per stick price) | 2.0 | 2.0 | 2.0 | |
| Plus: Excise (under Pre GST scenario) / GST (under GST scenario (28% plus cess per stick)) | 1.7 | 2.3 | 2.8 | |
| Total costs including excise | 3.7 | 4.3 | 4.8 | |
| Plus: Distrbutor commission @ 10% | 0.4 | 0.4 | 0.5 | |
| Total costs including distributor commission | 4.0 | 4.8 | 5.2 | |
| Plus: VAT @ 24% in pre GST scenario/ GST of 28% on value added | 1.0 | 0.1 | 0.1 | |
| **MRP** | **5.0** | **4.9** | **5.4** | **7.3** |
| **Tax per stick** | **2.6** | **2.5** | **2.9** | **9.6** |

*Source: Edelweiss research*

**Table 5: Likely increase in MRP and taxation for 69mm cigarettes under the new GST rates**

| 69mm excise rate per stick | PRE GST SCENARIO INR2216 per 1000 sticks | OLD GST RATE SCENARIO 5% plus INR2216 per 1000 sticks | NEW GST RATE SCENARIO 5% plus INR2837 per 1000 sticks | % increase / (decrease) |
|---|---|---|---|---|
| Factory costs (assumed per stick price) | 4.4 | 4.4 | 4.4 | |
| Plus: Excise (under Pre GST scenario) / GST (under GST scenario (28% plus cess per stick)) | 2.2 | 3.7 | 4.3 | |
| Total costs including excise | 6.6 | 8.0 | 8.7 | |
| Plus: Distrbutor commission @ 10% | 0.7 | 0.8 | 0.9 | |
| Total costs including distributor commission | 7.3 | 8.8 | 9.5 | |
| Plus: VAT @ 24% in pre GST scenario/ GST of 28% on value added | 1.7 | 0.2 | 0.2 | |
| **MRP** | **9.0** | **9.1** | **9.8** | **8.6** |
| **Tax per stick** | **4.0** | **3.9** | **4.5** | **14.3** |

*Source: Edelweiss research*

**Table 6: Likely increase in MRP and taxation for 74mm cigarettes under the new GST rates**

| 74mm excise rate per stick | PRE GST SCENARIO INR3021 per 1000 sticks | OLD GST RATE 5% plus INR3021 per 1000 sticks | NEW GST RATE 5% plus INR3813 per 1000 sticks | Price increase / (decrease) |
|---|---|---|---|---|
| Factory costs (assumed per stick price) | 3.6 | 3.6 | 3.6 | |
| Plus: Excise (under Pre GST scenario) / GST (under GST scenario (28% plus cess per stick)) | 3.0 | 4.2 | 5.0 | |
| Total costs including excise | 6.6 | 7.8 | 8.6 | |
| Plus: Distrbutor commission @ 10% | 0.7 | 0.8 | 0.9 | |
| Total costs including distributor commission | 7.3 | 8.6 | 9.4 | |
| Plus: VAT @ 24% in pre GST scenario/ GST of 28% on value added | 1.7 | 0.2 | 0.2 | |
| **MRP** | **9.0** | **8.8** | **9.7** | **7.4** |
| **Tax per stick** | **4.8** | **4.4** | **5.2** | **9.9** |

*Source: Edelweiss research*

**Table 7: Likely increase in MRP and taxation for 84mm cigarettes under the new GST rates**

| 84mm excise rate per stick | PRE GST SCENARIO INR4421 per 1000 sticks | OLD GST RATE 5% plus INR4405 per 1000 sticks | NEW GST RATE 36% plus INR4405 per | Price increase / (decrease) |
|---|---|---|---|---|
| Factory costs (assumed per stick price) | 5.8 | 5.8 | 5.8 | |
| Plus: Excise (under Pre GST scenario) / GST (under GST scenario (28% plus cess per stick)) | 4.4 | 6.3 | 8.1 | |
| Total costs including excise | 10.2 | 12.1 | 13.9 | |
| Plus: Distrbutor commission @ 10% | 1.0 | 1.2 | 1.4 | |
| Total costs including distributor commission | 11.2 | 13.3 | 15.3 | |
| Plus: VAT @ 24% in pre GST scenario/ GST of 28% on value added | 2.7 | 0.3 | 0.4 | |
| **MRP** | **13.9** | **13.6** | **15.6** | **12.5** |
| **Tax per stick** | **7.1** | **6.6** | **8.5** | **19.3** |

*Source: Edelweiss research*

## Outlook: Uncertainty looms; downgrade to 'HOLD'

The government's move to increase the overall taxation under the new GST rates has come as a surprise to all – against the benefit seen under the previous GST rates declared by the government. This alongwith the ~6% hike in budget results in an overall tax hike of ~16-17% for FY18 - ITC's cigarette volumes have come under tremendous pressure during the period from FY13 to FY16 when the government had increased the excise duty on cigarette by ~18% on an average (volumes were down by 20% during the said period). Government's statement highlighting the fact that it is not right that demerit goods should be benefitted due to decrease in taxation and the same has led to windfall gains – suggests a tough stance of the government on the sin sector. Also, with cigarette under GST, it remains a key source for the government to address any deficit it may have due to GST implementation and hence uncertainly looms in terms of taxation. We remain positive on ITC over long term as per capita consumption of cigarettes in India is 1/18th of China, while the proportion of legal cigarettes in overall tobacco consumption remains low at 11%.

We cut our volume assumptions for FY18E and FY19E to a decline of 5% YoY and 2% YoY respectively and hence cut our EPS estimates by 5.6%/8.2% YoY for FY18/19 respectively. We downgrade to **'HOLD/ Sector Performer'** from **'BUY/Sector outformer'**. We value ITC on SoTP basis on FY19E and arrive at a target price of INR304.

**Table 8: SOTP valuation**

| | | FY19E | Methodology | Target multiple | Per share contribution |
|---|---|---|---|---|---|
| Cigs | EPS | 8.3 | P/E | 27x | 223 |
| FMCG | Sales/Share | 10.0 | P/S | 4x | 40 |
| Hotels | EBITDA/Share | 0.4 | EV/EBITDA | 15x | 5 |
| Agri | EBITDA/Share | 1.0 | EV/EBITDA | 10x | 10 |
| Paper | EBITDA/Share | 1.2 | EV/EBITDA | 10x | 12 |
| Net cash | | | | | 13 |
| **Value of share** | | | | | **304** |

*Source: Edelweiss research*

**Change in Estimates**

| | FY18E | | | FY19E | | | |
|---|---|---|---|---|---|---|---|
| | New | Old | *% change* | New | Old | *% change* | Comments |
| Net Revenue | 457,266 | 473,288 | *(3.4)* | 512,295 | 543,443 | *(5.7)* | Cut in cigarette volume growth assumption |
| EBITDA | 166,288 | 175,289 | *(5.1)* | 187,246 | 204,884 | *(8.6)* | Decline in volumes and higher proportion of ad valorem duty in 84mm |
| *EBITDA Margin* | *36.1* | *36.7* | | *36.2* | *37.4* | | |
| Adjusted PAT | 115,178 | 122,000 | *(5.6)* | 130,687 | 142,323 | *(8.2)* | |
| *Net Profit Margin* | *25.0* | *25.6* | | *25.3* | *26.0* | | |
| Capex | 25,000 | 25,000 | *0.0* | 25,000 | 25,000 | *0.0* | |

## Company Description

ITC is one of the largest consumer companies in India with businesses spanning cigarettes, hotels, paper and agri-commodities. Its branded foods division with products such as staples, confectionery, noodle, snacks and biscuits is doing well and gaining strong market share across many categories. ITC has been successful in foods and constantly expanding its personal product portfolio (soaps, shampoos, deo, talc). Though the cigarettes division is still the major source of revenue, other businesses (agri, paper, hotel) have grown over the years. Recently ITC has entered the nicotine gum space with the launch of Kwiknic.

## Investment Theme

ITC has sustained its market leadership in the cigarettes space and delivered robust performance (both topline and profitability) amidst heavy taxation burden (three consecutive years of steep excise hike on cigarettes in Union Budget) and regulations with constant focus on innovation and distribution. The e-Choupal network established by ITC gives it a phenomenal sourcing edge, which has helped it transform into a consumer giant. ITC's FMCG business is likely to remain profitable in FY15 (turned profitable in FY14 with overall profit of INR220mn). Paper business helps address packaging needs of FMCG business with consistent quality and comparatively lower costs. Agri business has seen robust performance aided by tobacco leaf and traded commodities exports; provides strategic sourcing support to the company's cigarette and branded packaged foods businesses by ensuring high quality supplies. We expect ITC's cigarette EBIT growth to remain resilient and FMCG's profitability surge to sustain. With a new business-friendly government at the Centre, we expect hotel, paper and FMCG growth rates to improve over ensuing years.

## Key Risks

High incidence of taxation and strict regulatory norms on cigarette usage in public and packaging poses threat to cigarette volume growth.

Growing contraband market of cigarettes also poses significant threat for the cigarettes business.

Slowdown in macro-economic environment is a major threat to hotels business.

SUUTI stake sale is a likely overhang on the stock.

# 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 | 4.8 | 5.0 | 5.2 |
| Repo rate (exit rate) | 6.8 | 6.0 | 5.8 | 5.8 |
| USD/INR (Avg) | 65.0 | 67.5 | 69.0 | 69.0 |
| **Company** | | | | |
| **Revenue growth (Y-o-Y %)** | | | | |
| Cigs-Volume growth (dom) | (8.5) | 1.5 | (5.0) | (2.0) |
| Cigs-Price change (dom) | 15.9 | 3.5 | 10.0 | 8.0 |
| FMCG sales growth (dom) | 7.7 | 7.7 | 14.6 | 18.0 |
| Hotel sales growth (dom) | 8.5 | 4.0 | 12.0 | 14.0 |
| Agri sales growth (dom) | (22.6) | 11.0 | 14.0 | 16.0 |
| Paper sales growth (dom) | 5.9 | - | 6.0 | 10.0 |
| Overall growth (%) | 1.0 | 9.2 | 7.9 | 12.0 |
| Cig margin (dom) | 38.2 | 39.0 | 39.2 | 39.5 |
| FMCG margin (dom) | 0.6 | 0.4 | 3.0 | 4.0 |
| Hotel margin (dom) | 4.8 | 9.0 | 10.0 | 10.0 |
| Agri margin (dom) | 21.3 | 18.5 | 18.5 | 18.5 |
| Paper margin (dom) | 23.6 | 25.0 | 24.0 | 24.0 |
| **EBITDA margin assumpn** | | | | |
| COGS as % of sales | 34.6 | 37.5 | 37.6 | 37.5 |
| A&P as % of sales | 2.3 | 2.3 | 2.3 | 2.3 |
| Employee cost (% of rev) | 8.8 | 8.5 | 8.5 | 8.4 |
| **Financial assumptions** | | | | |
| Tax rate (%) | 36.1 | 34.6 | 34.5 | 34.0 |
| Capex (INR mn) | 10,529 | 17,849 | 25,000 | 25,000 |
| Debtor days | 18 | 18 | 18 | 18 |
| Inventory days | 239 | 230 | 230 | 230 |
| Payable days | 60 | 60 | 60 | 60 |
| Cash conversion cycle | 197 | 188 | 188 | 188 |
| Dep. (% gross block) | 4.6 | 4.5 | 4.6 | 4.6 |
| Dividend payout | 86.1 | 65.0 | 65.0 | 65.0 |
| Yield on cash | 10.6 | 10.9 | 13.0 | 13.0 |

**Income statement** (INR mn)

| Year to March | FY16 | FY17 | FY18E | FY19E |
|---|---|---|---|---|
| Gross revenues | 546,732 | 582,880 | 629,683 | 693,639 |
| Excise duties | 158,690 | 159,279 | 172,417 | 181,344 |
| Net revenue | 388,042 | 423,600 | 457,266 | 512,295 |
| Other Operating Income | 3,879 | 4,436 | 3,959 | 4,356 |
| Total operating income | 391,921 | 428,036 | 461,225 | 516,651 |
| Materials costs | 135,685 | 160,492 | 173,304 | 193,648 |
| Gross profit | 256,236 | 267,545 | 287,921 | 323,004 |
| Manufacturing expenses | 68,369 | 67,125 | 71,791 | 80,430 |
| Employee costs | 34,410 | 36,317 | 39,325 | 43,545 |
| Ad. & sales costs | 8,949 | 9,743 | 10,517 | 11,783 |
| EBITDA | 144,509 | 154,359 | 166,288 | 187,245 |
| Depreciation | 10,774 | 11,528 | 12,849 | 13,999 |
| EBIT | 133,735 | 142,832 | 153,440 | 173,247 |
| Add: Other income | 15,307.99 | 17,615.3 | 22,433.84 | 24,684.64 |
| Less: Interest Expense | 536 | 243 | 127 | 30 |
| Profit Before Tax | 148,507 | 160,204 | 175,746 | 197,901 |
| Less: Provision for Tax | 53,582 | 55,491 | 60,632 | 67,286 |
| Less: Minority Interest | (84) | (60) | (64) | (72) |
| Reported Profit | 95,009 | 104,773 | 115,178 | 130,687 |
| Adjusted Profit | 95,009 | 104,773 | 115,178 | 130,687 |
| Shares o /s (mn) | 12,040 | 12,040 | 12,040 | 12,040 |
| Adjusted Basic EPS | 7.9 | 8.7 | 9.6 | 10.9 |
| Diluted shares o/s (mn) | 12,108 | 12,040 | 12,040 | 12,040 |
| Adjusted Diluted EPS | 7.8 | 8.7 | 9.6 | 10.9 |
| Adjusted Cash EPS | 8.8 | 9.7 | 10.6 | 12.0 |
| Dividend per share (DPS) | 5.7 | 4.7 | 5.2 | 5.9 |
| Dividend Payout Ratio(%) | 86.1 | 65.0 | 65.0 | 65.0 |

**Common size metrics**

| Year to March | FY16 | FY17 | FY18E | FY19E |
|---|---|---|---|---|
| Materials costs | 34.6 | 37.5 | 37.6 | 37.5 |
| Staff costs | 8.8 | 8.5 | 8.5 | 8.4 |
| Ad. & sales costs | 2.3 | 2.3 | 2.3 | 2.3 |
| Other expenses | 17.4 | 15.7 | 15.6 | 15.6 |
| EBITDA margins | 36.9 | 36.1 | 36.1 | 36.2 |
| EBIT margins | 34.1 | 33.4 | 33.3 | 33.5 |
| Net Profit margins | 24.2 | 24.5 | 25.0 | 25.3 |

**Growth ratios (%)**

| Year to March | FY16 | FY17 | FY18E | FY19E |
|---|---|---|---|---|
| Revenues | 1.0 | 9.2 | 7.9 | 12.0 |
| EBITDA | 1.8 | 6.8 | 7.7 | 12.6 |
| PBT | 3.4 | 7.9 | 9.7 | 12.6 |
| Adjusted Profit | (1.7) | 10.3 | 9.9 | 13.5 |
| EPS | (1.9) | 10.9 | 9.9 | 13.5 |

| Balance sheet | | | | (INR mn) |
|---|---|---|---|---|
| **As on 31st March** | **FY16** | **FY17** | **FY18E** | **FY19E** |
| Share capital | 8,047 | 8,047 | 8,047 | 8,047 |
| Reserves & Surplus | 331,597 | 368,267 | 408,580 | 454,320 |
| Shareholders' funds | 339,644 | 376,315 | 416,627 | 462,367 |
| Minority Interest | 2,623 | 2,564 | 2,499 | 2,427 |
| Short term borrowings | 571 | 514 | 457 | 400 |
| Long term borrowings | 428 | 385 | 342 | 300 |
| Total Borrowings | 999 | 899 | 799 | 699 |
| Long Term Liabilities | 1,869 | 1,869 | 1,869 | 1,869 |
| Def. Tax Liability (net) | 18,205 | 18,205 | 18,205 | 18,205 |
| **Sources of funds** | **363,341** | **399,851** | **439,999** | **485,567** |
| Gross Block | 241,824 | 266,824 | 291,824 | 316,824 |
| Net Block | 147,567 | 161,039 | 173,190 | 184,191 |
| Capital work in progress | 31,151 | 24,000 | 24,000 | 24,000 |
| Intangible Assets | 6,400 | 6,400 | 6,400 | 6,400 |
| Total Fixed Assets | 185,119 | 191,440 | 203,591 | 214,592 |
| Non current investments | 45,565 | 45,565 | 45,565 | 45,565 |
| Cash and Equivalents | 136,186 | 157,457 | 177,826 | 200,204 |
| Inventories | 91,564 | 101,132 | 109,205 | 122,024 |
| Sundry Debtors | 19,198 | 20,890 | 22,550 | 25,264 |
| Loans & Advances | 28,987 | 28,987 | 28,987 | 28,987 |
| Other Current Assets | 5,602 | 5,602 | 5,602 | 5,602 |
| Current Assets (ex cash) | 145,351 | 156,610 | 166,344 | 181,877 |
| Trade payable | 24,042 | 26,382 | 28,488 | 31,832 |
| Other Current Liab | 124,838 | 124,838 | 124,838 | 124,838 |
| Total Current Liab | 148,880 | 151,220 | 153,326 | 156,670 |
| Net Curr Assets-ex cash | (3,528) | 5,391 | 13,018 | 25,207 |
| **Uses of funds** | **363,341** | **399,851** | **439,999** | **485,567** |
| BVPS (INR) | 28.1 | 31.3 | 34.6 | 38.4 |

| Free cash flow | | | | (INR mn) |
|---|---|---|---|---|
| **Year to March** | **FY16** | **FY17** | **FY18E** | **FY19E** |
| Reported Profit | 95,009 | 104,773 | 115,178 | 130,687 |
| Add: Depreciation | 10,774 | 11,528 | 12,849 | 13,999 |
| Interest (Net of Tax) | 343 | 159 | 83 | 20 |
| Others | (11,863) | 24 | (19) | (60) |
| Less: Changes in WC | 1,666 | 8,919 | 7,628 | 12,189 |
| Operating cash flow | 92,596 | 107,565 | 120,463 | 132,457 |
| Less: Capex | 10,529 | 17,849 | 25,000 | 25,000 |
| **Free Cash Flow** | **82,067** | **89,716** | **95,463** | **107,457** |

**Cash flow metrics**

| Year to March | FY16 | FY17 | FY18E | FY19E |
|---|---|---|---|---|
| Operating cash flow | 92,596 | 107,565 | 120,462 | 132,455 |
| Investing cash flow | (39,657) | (17,849) | (25,000) | (25,000) |
| Financing cash flow | (57,692) | (68,445) | (75,093) | (85,077) |
| Net cash Flow | (4,752) | 21,271 | 20,369 | 22,378 |
| Capex | (10,529) | (17,849) | (25,000) | (25,000) |
| Dividend paid | (51,327) | (68,102) | (74,866) | (84,947) |

**Profitability and efficiency ratios**

| Year to March | FY16 | FY17 | FY18E | FY19E |
|---|---|---|---|---|
| ROAE (%) | 28.7 | 29.0 | 28.9 | 29.6 |
| ROACE (%) | 44.8 | 44.4 | 44.0 | 44.7 |
| Inventory Days | 239 | 230 | 230 | 230 |
| Debtors Days | 18 | 18 | 18 | 18 |
| Payable Days | 60 | 60 | 60 | 60 |
| Cash Conversion Cycle | 197 | 188 | 188 | 188 |
| Current Ratio | 1.9 | 2.1 | 2.2 | 2.4 |
| Adjusted Debt/Equity | - | - | - | - |
| Interest Coverage Ratio | 249.5 | 587.8 | 1,204.4 | 5,780.3 |

**Operating ratios**

| Year to March | FY16 | FY17 | FY18E | FY19E |
|---|---|---|---|---|
| Total Asset Turnover | 1.1 | 1.1 | 1.1 | 1.1 |
| Fixed Asset Turnover | 2.6 | 2.7 | 2.7 | 2.8 |
| Equity Turnover | 1.2 | 1.2 | 1.2 | 1.2 |

**Valuation parameters**

| Year to March | FY16 | FY17 | FY18E | FY19E |
|---|---|---|---|---|
| Adj. Diluted EPS (INR) | 7.8 | 8.7 | 9.6 | 10.9 |
| *Y-o-Y growth (%)* | *(1.9)* | *10.9* | *9.9* | *13.5* |
| Adjusted Cash EPS (INR) | 8.8 | 9.7 | 10.6 | 12.0 |
| Diluted P/E (x) | 41.4 | 37.4 | 34.0 | 30.0 |
| P/B (x) | 11.6 | 10.4 | 9.4 | 8.5 |
| EV / Sales (x) | 9.7 | 8.8 | 8.1 | 7.2 |
| EV / EBITDA (x) | 26.2 | 24.4 | 22.5 | 19.9 |
| Dividend Yield (%) | 1.7 | 1.5 | 1.6 | 1.8 |

**Peer comparison valuation**

| | Market cap | Diluted P/E (X) | | EV / EBITDA (X) | | ROAE (%) | |
|---|---|---|---|---|---|---|---|
| **Name** | **(USD mn)** | **FY18E** | **FY19E** | **FY18E** | **FY19E** | **FY18E** | **FY19E** |
| ITC | 61,466 | 34.0 | 30.0 | 22.5 | 19.9 | 28.9 | 29.6 |
| Asian Paints | 16,780 | 46.2 | 37.3 | 29.0 | 23.2 | 33.0 | 34.5 |
| Hindustan Unilever | 38,789 | 49.7 | 41.7 | 34.5 | 28.7 | 106.5 | 113.0 |
| Marico | 6,567 | 44.5 | 38.9 | 30.1 | 26.1 | 38.1 | 37.1 |
| Nestle Ltd | 10,308 | 51.4 | 39.7 | 28.3 | 22.2 | 39.4 | 41.9 |
| United Spirits | 6,224 | 59.8 | 42.4 | 33.6 | 26.7 | 30.2 | 31.2 |

*Source: Edelweiss research*

# Additional Data

### Directors Data

| | | | |
|---|---|---|---|
| Yogesh Chander Deveshwar | Chairman | Nakul Anand | Executive Director |
| Sanjiv Puri | CEO & Executive Director | R Tandon | Executive Director |
| Zafir Alam | Non-Executive Director | Sunil Behari Mathur | Non-Executive Director |
| Pillappakkam Bahukutumbi Ramanujam | Non-Executive Director | Sahibzada Syed Habib-ur-Rehman | Non-Executive Director |
| Meera Shankar | Non-Executive Director | Suryakant Balkrishna Mainak | Non-Executive Director |
| S Banerjee | Non-Executive Director | Nirupama Rao | Non-Executive Director |
| A Duggal | Non-Executive Director | | |

Auditors - Deloitte Haskins & Sells, Kolkata

### Holding – Top10

| | Perc. Holding | | Perc. Holding |
|---|---|---|---|
| Tobacco manufacturer | 24.49 | Life insurance corp | 16.24 |
| Unit trust of india | 9.07 | Myddleton invest coy | 4 |
| General insurance co | 1.75 | New india assurance | 1.69 |
| Aberdeen | 1.48 | Oriental insurance c | 1.39 |
| Gic private limited | 1.27 | Rothmans intl enterp | 1.27 |

**in last one year*

### Bulk Deals

| Data | Acquired / Seller | B/S | Qty Traded | Price |
|---|---|---|---|---|
| 07 Feb 2017 | Lic A/C Lic Allocation Contra Fund | Buy | 80840763 | 275.85 |
| 07 Feb 2017 | Administrator Of The Specified Undertaking Of The Uti-1964 | Sell | 80840763 | 275.85 |
| 07 Feb 2017 | Administrator Of The Specified Undertaking Of The Unit Trus | Sell | 80840763 | 275.85 |
| 07 Feb 2017 | Uti Admnstr Of The Specified Undertaking Of Uti-Unit Schm 64 | Sell | 80840763 | 275.85 |
| 07 Feb 2017 | Life Insurance Corporation (Scheme 5) | Buy | 80840763 | 275.85 |
| 07 Feb 2017 | Life Insurance Corporation Of India Ltd | Buy | 80840763 | 275.85 |

**in last one year*

### Insider Trades

| Reporting Data | Acquired / Seller | B/S | Qty Traded |
|---|---|---|---|
| 19 May 2017 | Rajeev Pathak | Sell | 25000.00 |
| 19 May 2017 | D. M. Hazarika | Sell | 15000.00 |
| 04 May 2017 | G. Vijaya Kumar | Sell | 30000.00 |
| 03 May 2017 | Barun Kar | Sell | 17000.00 |
| 03 May 2017 | A. Madhusudhana Rao | Sell | 32345.00 |

**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 |

**Edelweiss Securities Limited,** Edelweiss House, off C.S.T. Road, Kalina, Mumbai – 400 098.
Board: (91-22) 4009 4400**,** Email*: research@edelweissfin.com*

Aditya Narain
Head of Research
aditya.narain@edelweissfin.com

ADITYA NARAIN

Digitally signed by ADITYA NARAIN
DN: c=IN, o=EDELWEISS SECURITIES LIMITED, ou=HEAD RESEARCH, cn=ADITYA NARAIN, serialNumber=e0576796072ad1a3266c27990f20bf0213f69235fc3f1bcd0fa1c30092792c20, postalCode=400005, 2.5.4.20=6b7d777d3c8c77e0e2c454e91543f9f4d9b8311cf0678cd975097fc645327865, st=Maharashtra
Date: 2017.07.18 11:00:40 +05'30'

***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 |
|---|---|---|---|---|
| 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 |
| 06-Jul-17 | **Consumer Goods** | Destocking to impact topline; *Quarterly Result Preview* | | |

**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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