

Institutional Equity Research

ITC

FMCG | India

1QFY18 Result Update | July 28, 2017

CMP* (Rs)	289
Upside/ (Downside) (%)	16
Bloomberg Ticker	ITC IN
Market Cap. (Rs bn)	3,511
Free Float (%)	68
Shares O/S (mn)	12,147

BUY 

Target Price: Rs336

Cigarettes do well before moving on to the GST regime

ITC has reported a decent set of numbers for 1QFY18. Although revenues fell by 0.8% YoY to Rs98.7bn, EBITDA increased by 7% YoY to Rs36.7bn (vs. our estimate of Rs37.3bn) and net profit surged by 7.4% YoY to Rs25.6bn (vs. our estimate of Rs26bn). Its core Cigarettes business marginally exceeded our estimates with 6.6% growth in segmental revenues and 9% growth in segmental EBIT.

ITC has been in focus over government's flip flop on GST rates on cigarettes. Now that the issue is settled and the GST rates would be 8-9% higher than the pre-GST indirect tax incidence on cigarettes business. ITC has undertaken a weighted average price increase of 6-7% across most of its key brands. Although this will have an adverse impact on volume growth, we expect the margins on cigarettes business to improve on the back of price hike. **Expecting 9.9% revenue and 12.4% earnings CAGR through FY17-19E, we maintain our BUY recommendation on the stock with a revised SOTP-based Target Price of Rs336, which implies an upside of 16% from the current levels.**

Decent Performance by Cigarette Biz

Cigarette volumes for the quarter grew by 1% YoY, while gross revenues surged by 6.6% YoY to Rs87.7bn. Segmental margins improved by 80bps YoY to 37.3%, which led to 9% YoY growth in segmental EBIT to Rs32.7bn. Non-cigarette FMCG business witnessed a decent 9% YoY growth in revenues in spite of inventory de-stocking prior to GST roll-out. The segment reported EBIT of Rs54mn in 1QY18 vs. loss of Rs45mn in the base quarter.

Subdued Growth in non-FMCG Biz

Growth in Paperboard and Agri business remained muted. Revenues from Paperboard business increased by just 2.8% YoY to Rs13.6bn owing to sluggish demand conditions in key target categories i.e. FMCG, Liquor and cigarettes and pipeline correction prior to GST roll-out. Revenues from Agri business declined by 1.2% YoY to Rs 27.6bn, primarily due to lower quality of tobacco output in AP and limited trading opportunities. Revenues from Hotels business grew by 6% YoY to Rs3bn on the back of increase in ARR and higher F&B sales. Thus, profit growth across all non-cigarette businesses remained muted.

Outlook & Valuation

Considering the increased cess on cigarettes, we have revised our revenue and earnings estimate downwards by 4.6% and 5.2%, respectively for FY19E. We expect ITC to report net sales of Rs436.9bn and Rs484.4bn and net profit of Rs115.4bn and Rs128.8bn in FY18E and FY19E, respectively. Based on expected EPS of Rs10.6, the stock currently trades at P/E multiples of 27.3x FY19E earnings. The stock has traded at an average 1-Yr forward PE multiple of 30x in past five years in spite of challenging regulatory environment, which provides cushion for the stock price, in our view. **We maintain our BUY recommendation on the stock with a revised SOTP-based Target Price of Rs336.**

Key Financials (Rs mn)	FY16	FY17	FY18E	FY19E
Sales	365,826	400,887	436,865	484,398
EBITDA	137,146	145,780	164,178	183,528
Net profit	93,283	102,009	115,352	128,781
EPS (Rs)	7.7	8.4	9.5	10.6
DPS (Rs)	8.5	4.8	6.0	8.0
P/E (x)	37.6	34.4	30.4	27.3
P/B (x)	8.4	7.7	7.3	7.1
EV/EBITDA (x)	24.2	22.6	19.9	17.8
ROE (%)	23.6	23.5	24.7	26.4
Dividend yield (%)	2.9	1.6	2.1	2.8

Source: Company, RSec Research

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	(4.4)	6.0	15.9
Relative to Nifty	(9.7)	(1.4)	0.5

Shareholding Pattern (%)	Mar'17	Jun'17
Promoter	-	-
Public	100	100

1 Year Stock Price Performance



Note: * CMP as on July 27, 2017

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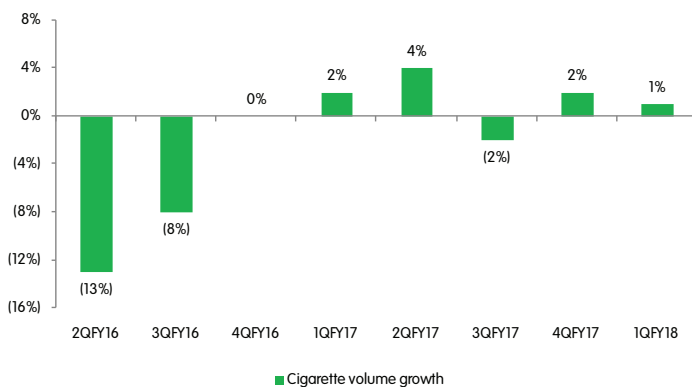
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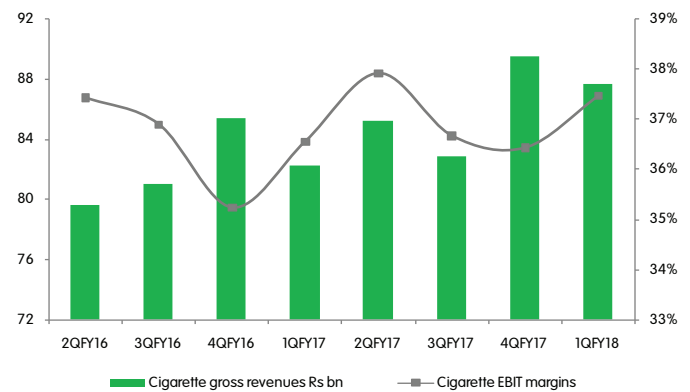
Target Price: Rs336

Risks to the view

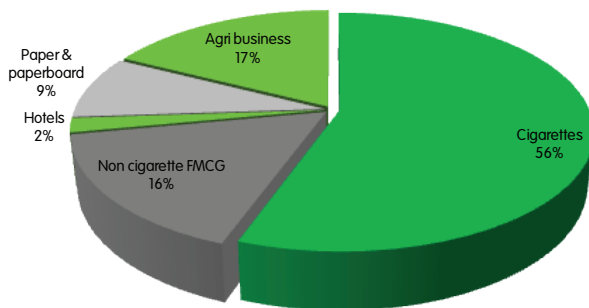
- ▶ Continued regulatory overhang on the cigarettes industry
- ▶ Increasing share of illegal cigarettes trade
- ▶ Poor demand environment that might impact growth of non-cigarette segments

Exhibit 1: Trend in Cigarette volume growth


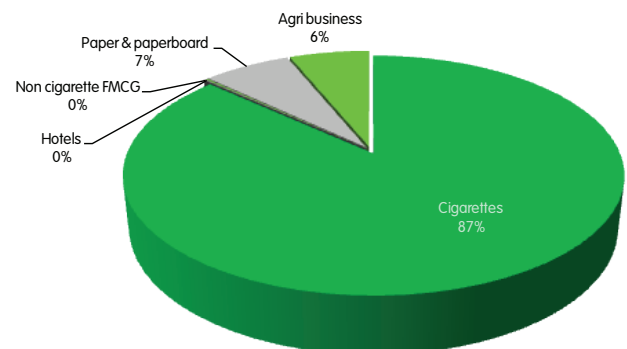
Source: Company, RSec Research

Exhibit 2: Performance of Cigarette division


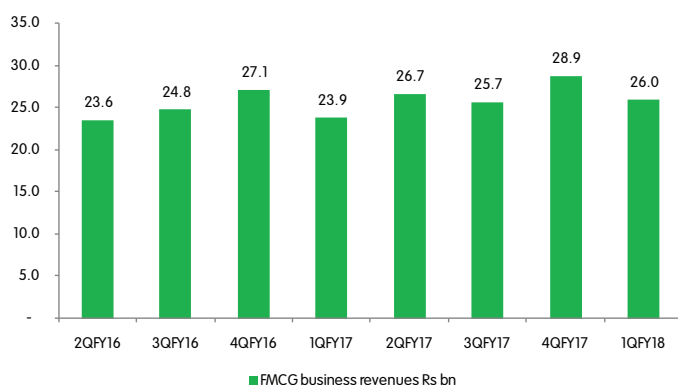
Source: Company, RSec Research

Exhibit 3: Share of revenues (1QFY18)


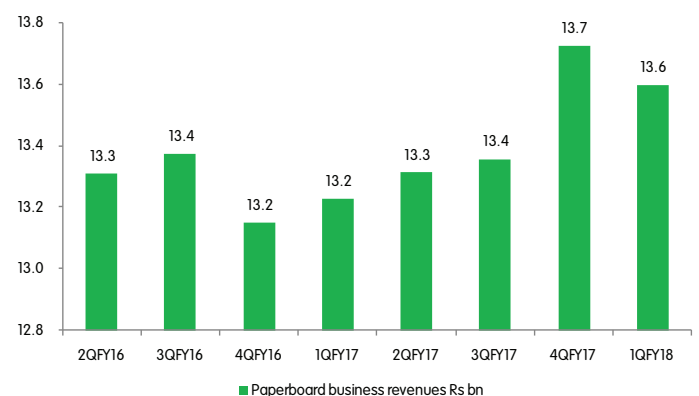
Source: Company, RSec Research

Exhibit 4: Share of EBIT (1QFY18)


Source: Company, RSec Research

Exhibit 5: Trend in quarterly FMCG revenues


Source: Company, RSec Research

Exhibit 6: Trend in paperboard business revenues


Source: Company, RSec Research

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Exhibit 7: Quarterly Performance

Y/E March (Rs mn)	1QFY18	1QFY17	% yoy	4QFY17	% qoq	FY17	FY16	% chg
Net Sales	98,765	99,577	(0.8)	111,255	(11.2)	400,887	365,827	9.6
Consumption of RM	38,360	42,456	(9.6)	46,828	(18.1)	159,763	134,500	18.8
(% of Sales)	38.8	42.6		42.1		39.9	36.8	
Staff Costs	6,746	7,003	(3.7)	5,714	18.1	24,443	23,316	4.8
(% of Sales)	6.8	7.0		5.1		6.1	6.4	
Other Expenses	16,976	15,819	7.3	19,960	(14.9)	70,900	70,865	0.1
(% of Sales)	17.2	15.9		17.9		17.7	19.4	
Total Expenditure	62,083	65,278	(4.9)	72,502	(14.4)	255,106	228,681	11.6
Operating Profit	36,682	34,299	6.9	38,754	(5.3)	145,780	137,146	6.3
OPM	37.1	34.4		34.8		36.4	37.5	
Depreciation	2,682	2,613	2.7	2,418	10.9	10,380	10,007	3.7
EBIT	34,000	31,686	7.3	36,336	(6.4)	135,400	127,139	6.5
Interest	104	101	2.8	(115)	(190.6)	230	491	(53.3)
Other Income	5,550	5,169	7.4	4,021	38.0	19,859	17,693	12.2
PBT	39,446	36,754	7.3	40,471	(2.5)	155,030	144,341	7.4
(% of Sales)	39.9	36.9		36.4		38.7	39.5	
Provision for Taxation	13,841	12,907	7.2	13,777	0.5	53,021	51,057	3.8
(% of PBT)	35.1	35.1		34.0		34.2	35.4	
PAT (recurring)	25,605	23,847	7.4	26,695	(4.1)	102,009	93,284	9.4
Extr. Income/(Expense)	-	-		-		-	-	
Reported PAT	25,605	23,847	7.4	26,695	(4.1)	102,009	93,284	9.4
PATM	25.9	23.9		24.0		25.4	25.5	
Equity shares (mn)	12,147	12,147		12,147		12,147	12,147	
EPS (Rs)	2.1	2.0	7.4	2.2	(4.1)	8.4	7.7	9.4

Source: Company, RSec Research

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Profit & Loss Statement

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Net Sales	365,826	400,887	436,865	484,398
Total operating income	365,826	400,887	436,865	484,398
% chg	1.4	9.6	9.0	10.9
Total Expenditure	228,681	255,106	272,686	300,870
Cost of Materials	134,500	159,763	174,101	193,044
Advertising Exp (Incl Promotion)	9,643	9,059	10,922	12,110
Personnel	23,316	24,443	27,376	30,661
Others	61,221	61,842	60,287	65,055
EBITDA	137,146	145,780	164,178	183,528
% chg	5.1	6.3	12.6	11.8
(% of Net Sales)	37.5	36.4	37.6	37.9
Depreciation& Amortisation	10,007	10,380	10,973	11,924
EBIT	127,139	135,400	153,206	171,603
% chg	5.2	6.5	13.2	12.0
(% of Net Sales)	34.8	33.8	35.1	35.4
Interest & other Charges	491	230	180	180
Other Income	17,693	19,859	21,750	23,700
(% of PBT)	12.3	12.8	12.4	12.1
Recurring PBT	144,340	155,030	174,776	195,123
% chg	3.1	7.4	12.7	11.6
PBT (reported)	144,340	155,030	174,776	195,123
Tax	51,057	53,021	59,424	66,342
(% of PBT)	35.4	34.2	34.0	34.0
PAT (recurring)	93,283	102,009	115,352	128,781
% chg	(2.9)	9.4	13.1	11.6
(% of Net Sales)	25.5	25.4	26.4	26.6
Basic EPS (Rs)	7.7	8.4	9.5	10.6
Fully Diluted EPS (Rs)	7.7	8.4	9.5	10.6
% chg	(2.9)	9.4	13.1	11.6

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Balance Sheet

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Share capital	8,047	12,147	12,147	12,147
Reserves	408,517	441,262	469,436	481,991
Networth	416,564	453,410	481,583	494,138
Borrowings	294	180	258	258
Defferred tax	18,674	18,717	19,243	19,906
Total liabilities	435,533	472,307	501,084	514,303
Gross block	150,361	169,413	181,413	193,413
Less: accumulated depreciation	9,944	20,154	31,126	43,051
Net block	140,417	149,259	150,287	150,362
Capital work in progress	23,884	34,913	32,413	29,913
Investments	133,245	185,853	210,853	235,853
Current assets	202,766	172,134	183,653	182,579
Inventories	85,198	78,640	85,697	95,022
Debtor	16,864	22,075	24,056	26,674
Cash	56,392	27,473	25,753	7,681
loans and advances	14,504	11,140	12,396	13,561
other current assets	29,809	32,807	35,751	39,641
Current liabilities	62,931	68,029	74,134	82,200
Provisions	1,849	1,824	1,988	2,204
Net current assets	137,986	102,281	107,531	98,174
Total assets	435,533	472,307	501,084	514,303

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Cash Flow Statement

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Net profits	93,283	102,009	115,352	128,781
Depreciation	10,007	10,380	10,973	11,924
Deferred tax	1,902	43	526	663
Change in working capital	(4,116)	6,786	(6,970)	(8,715)
Operating cash flow	101,077	119,218	119,880	132,654
Capital expenditure	(11,610)	(27,581)	(9,500)	(9,500)
Investments	(43,549)	(52,608)	(25,000)	(25,000)
Investing cash flow	(55,159)	(80,189)	(34,500)	(34,500)
Free cash	89,466	91,637	110,380	123,154
Dividend	(81,816)	(69,009)	(87,178)	(116,226)
Fresh equity issue	5,072	10,724	0	0
Debt	(93)	(114)	78	0
Financing cash flow	(76,837)	(58,400)	(87,100)	(116,226)
Others	24,583	(9,548)	0	0
Net change in cash	(6,336)	(28,919)	(1,720)	(18,072)
Opening cash	62,728	56,392	27,473	25,753
Closing cash	56,392	27,473	25,753	7,681

Key Ratios

Y/E March	FY16	FY17	FY18E	FY19E
Valuation Ratio (x)				
P/E (on FDEPS)	37.6	34.4	30.4	27.3
P/CEPS	33.3	31.2	27.7	24.8
P/BV	8.4	7.7	7.3	7.1
Dividend yield (%)	2.9	1.6	2.1	2.8
EV/Sales	9.1	8.2	7.5	6.7
EV/EBITDA	24.2	22.6	19.9	17.8
Per Share Data (Rs)				
EPS (Basic)	7.7	8.4	9.5	10.6
Core EPS	7.7	8.4	9.5	10.6
Cash EPS	8.7	9.3	10.4	11.6
DPS	8.5	4.8	6.0	8.0
Book Value	34.3	37.3	39.6	40.7
Returns (%)				
RoCE	23.7	23.5	24.7	26.4
RoE	23.6	23.5	24.7	26.4
Turnover ratios (x)				
Inventory / Sales (days)	136	113	115	115
Receivables (days)	17	20	20	20
Payables (days)	168	153	153	153
Working capital cycle (ex-cash) (days)	(15)	(20)	(18)	(17)

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Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

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