

31 January 2018

Emami Ltd. – BUY

CMP : 1,114
Target Price : 1,392
Upside : 25%+
Stop Loss : 986 (closing basis)

Investment Thesis

Recently, the stock price of Emami Ltd. (Emami) corrected by ~19% from 52-week high of Rs.1,365 on account of the company reported lower than expected revenue in the recent quarters as the volume growth was adversely affected post demonetization.

Emami's revenue had grown at a CAGR of ~11.7% during FY12-17 largely aided by distribution expansion and its recent acquisitions. The company is confident of achieving double-digit revenue growth in the power brands for the next 3-4 years. Emami gets ~60% of its revenue from relatively under penetrated segments such as cooling oil, talcum powder, fairness cream, antiseptic cream and cold cream which secures a long term growth for the company, as there is still enough room left for the strong growth. Being an early entrant in these spaces, Emami commands the market leader position which translates into a higher growth. Generally, underpenetrated segment offers higher growth compared to the highly penetrated segment.

Emami's dependence on the rural channel is one of the highest among peers. As a result, Emami has reported sub-optimal growth during FY14-17, a period of rural slowdown. While drought had impacted rural demand in FY15 and FY16, demonetization washed away the benefits of a near normal monsoon in FY17. With another year of normal monsoon in FY18, rural growth has started exceeding urban growth for the first time in the last few years and players like Emami are poised to benefit from the recovery. With government initiatives like direct benefit transfer, Pahal, rural wage increases, hike in MSP, etc., will further aid growth in rural demand. Emami, with its larger rural portfolio appears well placed to gain growth momentum ahead of others as a result of the ongoing revival in rural demand going forward.

Financials

- During the past 5 years, revenue of Emami grew at a CAGR of 11.7% while PAT grew at a CAGR of 5.6% in the same period.

Consol. (Rs.Mn.)	FY15	FY16	FY17	FY18E	FY19E
Revenue	22,173	23,937	25,326	29,125	33,494
EBITDA	5,401	6,750	7,591	8,730	10,039
% growth	22.4	25.0	12.5	15.0	15.0
PAT	4,856	3,591	3,404	3,918	4,514
EPS (INR)	21.4	15.8	15.0	17.3	19.9
P/E (x)	53.4	72.2	76.2	66.2	57.4
RoE (%)	39.5%	25.6%	19.4%	20.3%	21.3%

- Emami has reported 4.2% YoY increase in revenue in Q3FY18 to Rs.7,566mn led by 6.0% YoY increase in volumes. Domestic revenues grew by 10% YoY (including GST/VAT) while revenues of international business division grew by 16% YoY during the quarter.

Stock Data

Market Cap (INR MN)	259,220
Market Cap (\$ MN)	4,075.80
Shares O/S (in MN)	227.0
Avg. Volume (3 month)	162,000
52-Week Range (Rs.)	1,365 / 981

Shareholding Pattern

Promoters	72.74%
FII's	13.77%
Institutions	5.01%
Others (incl. body corporate)	8.48%

Performance (%)	1M	6M	1Yr
Absolute	-14.5%	3.1%	12.8%
BSE FMCG	1.7%	7.5%	26.7%

Key Ratios

Div Yield	0.6%
TTM PE	81.6x
ROE	19.2%
TTM EPS (INR)	14.0/-

- Emami's EBITDA improved by 2.4% YoY in Q3FY18 to Rs.2,647mn. However, the EBITDA margin has declined by 62bps YoY to 35.0% in Q3FY18 due to 140bps increase in ad-spends even as raw material cost as a % of revenue decreased by 160bps in the quarter.
- PAT for the quarter for Emami grew by 9.6% YoY to Rs.1,472mn as tax out go and interest expenditure declined by 11.2% YoY and 27.4% YoY, respectively.

Key Business Highlights

- Emami is one of the leading and fastest growing personal and healthcare company in India, with an enviable portfolio of household brand names such as Boroplus, Navratna, Fair and Handsome, Zandu balm, Mentho Plus balm and Fast Relief.
- Emami has a portfolio of 4 focus brands namely Navratna, Zandu, Himani and Fair & Handsome that hold strong market leadership positions. Overall product portfolio comprises of 300 products which are primarily positioned as 'value for money'.
- With seven manufacturing locations in India and one in Bangladesh supported by a widespread distribution network, Emami is positioned to make its products available in every corner of the country.

Valuation

- Focus on the ayurvedic products is one of the key attributes of Emami as its margin being one of the best in the Industry and ~80% of Emami's products have ayurvedic base. Moreover, penetration level in most of these niche segments is low resulting in the strong revenue momentum for these segments thus offering operating leverage benefits. In Emami's portfolio, Zandu Healthcare products have highest gross margins in the range of 65-67%, which contributes ~5.6% of company's total sales, followed by Boroplus and Zandu Balm which has a gross margin of ~65%. We expect, with gain in market share of high yield product in the portfolio, the EBITDA margin will be over 30% during FY17-19E.
- Emami's marketing spend is one of the highest in the industry as it spends ~18.0% of its sales on advertisement and promotion. Aggressive marketing spend has helped Emami in gaining market share across its power brands. Emami has guided that it will continue to spend 17-18% of its sales in advertisement and sales promotions, which, we believe, will help Emami to keep the growth momentum.
- To enhance reach and market share, Emami plans to focus on increasing its direct retail reach and reduce the dependency on wholesale channel. In FY17, Emami has added ~85,000-90,000 retail outlets and currently, Emami has a direct reach to 0.7mn retail outlets and planning to increase 0.1mn retail outlets further in FY18E. This will gradually reduce dependence on wholesale channel, which got severely affected due to demonetization. Currently, 50-55% of Emami's domestic revenue comes from wholesale channel and management plans to reduce it to 40% over the next five years.
- With market leader position in some products, revival in rural demand, niche focus on the ayurvedic products, highest marketing spend and plans to increase the direct retail reach, we value Emami at 70.00x FY19E EPS of Rs.19.90 to arrive at target price of Rs.1,392.00, an upside of ~22%.

Risk & Concern

- Any delay in recovery in consumer demand post demonetization will negatively affect all consumer companies.
- Any sharp rise in cost of key inputs, like Mentha and Crude oil will negatively impact margin of Emami.
- Any seasonal fluctuations that might impact growth of brands such as Navratna and Boroplus will affect company's growth.

Graphs & Charts

Figure 1: Net Sales Trend

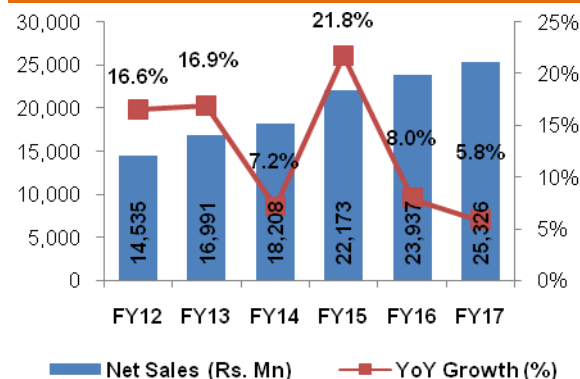


Figure 2: EBITDA & EBITDA Margin Trend

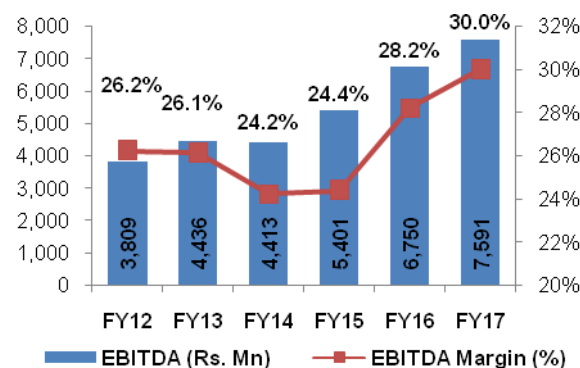


Figure 3: PAT Trend

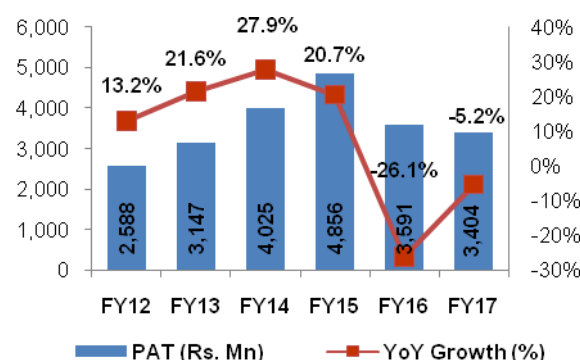
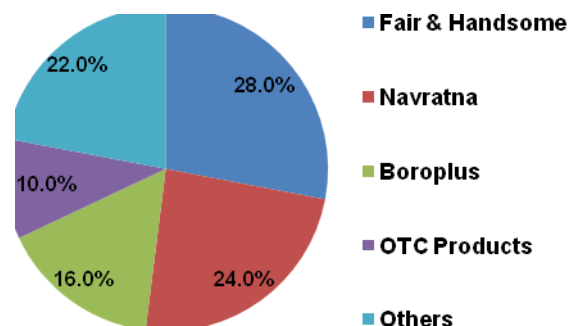


Figure 4: Brand-wise Revenue Share (FY17)



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