Sharekhan
by BNP PARIBAS

Hindustan Unilever Limited

Recent correction a good entry point

Sector: Consumer Goods

Company Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 2,088**	
Price Target: **Rs. 2,305**	↔

↑ Upgrade ↔ No change ↓ Downgrade

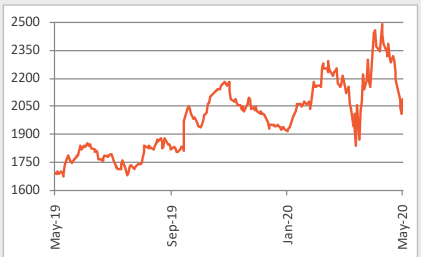
Company details

Market cap:	Rs. 490,569 cr
52-week high/low:	Rs. 2614/1660
NSE volume: (No of shares)	16.6 lakh
BSE code:	500696
NSE code:	HINDUNILVR
Sharekhan code:	HINDUNILVR
Free float: (No of shares)	89.5 cr

Shareholding (%)

Promoters	61.9
FII	12.0
DII	6.3
Others	19.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-15.1	-3.3	0.1	23.9
Relative to Sensex	-20.9	19.5	21.6	40.2

Sharekhan Research, Bloomberg

The GSK Group sold a 5.7% stake (13.37 crore shares) in Hindustan Unilever Limited (HUL) through multiple block deals in the open market at an average price of Rs. 1,902 per share. The stock has corrected by ~16% from its high and its currently trading at 48.1x its FY2022E earnings. GSK Group selling the stake has reduced supply overhang on the stock and the current valuations factors in a sluggish Q4 due to supply disruption caused by the nation-wide lockdown in the fag-end of the quarter. We expect supply disruption to sustain in the coming months till the time the nation recovers from the pandemic situation. Thus, H1FY2021 would see HUL's sales significantly lower than H1FY2020. However, if the pandemic situation is under control by June/July, we expect recovery in demand to begin from H2FY2020. With half of the portfolio catering to essential categories, the strong direct distribution reach of almost three million retail outlets and new product launches (especially in the hygiene space) would help HUL to see faster recovery post normalisation of business environment. The merger of GSK Consumer Healthcare (GSK Consumer) will make HUL one of the strongest players in domestic processed foods space (~50% of overall FMCG market in India and growing at good pace) and would lead to earnings accretion of 4-8% over FY2021-22.

Innovation remains core of growth strategy; GSK Consumer merger will enhance future earnings growth: Innovation has always remained the core of HUL's growth strategy and will continue to drive growth for the company in the near term. After the lockdown ends, demand for hygiene products is expected to increase. In view of this, HUL has launched products such as Lifebuoy germ skill spray, Domex germ removal wipes and Domex disinfectant spray, etc. Further, recent acquisitions will expand the company's portfolio and will be a key revenue driver in the long run. The penetration level for health food drinks (HFD) in India is just 24% (14% in rural India), which provides a huge scope for HUL in long run. The acquisition of V Wash gives the company an entry into the currently underpenetrated and rapidly growing female intimate hygiene segment, the penetration of which is currently 8-10% in India. This will be well-supported by a strong distribution reach and adequate media spends.

Our Call

Valuation- Retain Buy with price target of Rs. 2,305: HUL is currently operating at 70-80% capacity in most of its manufacturing facilities and focusing on supplying whatever its manufacturing through various distribution models. Though FY2021 is expected to affected by spread of COVID-19, HUL's long-term growth prospects are intact and we expect a strong recovery in FY2022 (if pandemic situation is under control by H1FY2021). The stock has already corrected by ~16% from its recent high and trading at 48.1x its FY2022E EPS, which is at discount to its last three years average multiple of 55x. Thus, the recent correction provides a good entry opportunity in quality large consumer goods stock such as HUL from a long-term perspective. We maintain our Buy recommendation on the stock with unchanged price target of Rs. 2,305.

Key Risks

If the global pandemic takes time to normalise, it will continue to impact on HUL's earnings in the near term.

Valuation Rs cr

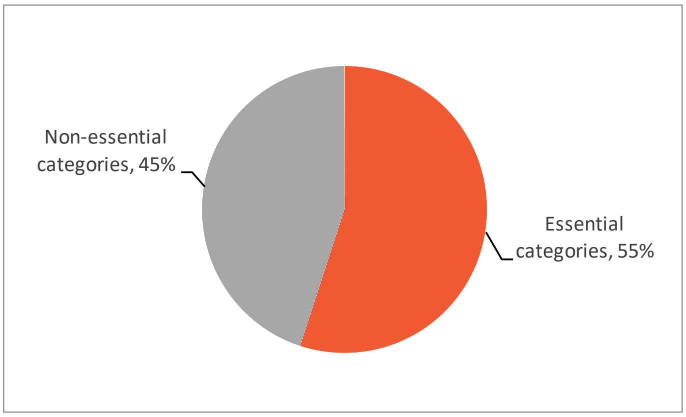
Particulars	FY18	FY19	FY20	FY21E*	FY22E*
Revenue	35,218	38,224	38,785	41,044	48,323
OPM (%)	20.7	22.6	24.8	25.2	27.0
Adjusted PAT	5,287	6,199	6,886	7,627	10,209
Adjusted EPS (Rs.)	24.5	28.7	31.9	32.5	43.5
P/E (x)	85.3	72.7	65.5	64.3	48.1
P/B (x)	63.7	58.9	56.2	10.3	9.9
EV/EBIDTA (x)	61.1	51.5	46.4	51.4	40.8
RoNW (%)	77.9	84.2	87.8	27.4	21.0
RoCE (%)	104.2	113.2	105.2	35.9	27.9

Source: Company; Sharekhan estimates
** FY2021 and FY2022 earnings estimates include the merger of GSK Consumer*

Focus on essentials to help in posting good recovery in H2FY2020

Essential categories (including homecare, personal wash and hygiene products) fetch 50-55% of HUL's overall revenues. HUL has been focusing on manufacturing essential category products in the near term due to high demand, while discretionary categories remain affected amid the pandemic. The management is also focusing on value products and smaller SKUs in premium category products in view of downtrading. Innovative delivery models such as partnering with last-mile delivery apps such as Swiggy and Dunzo will help the company.

Contribution to domestic revenue

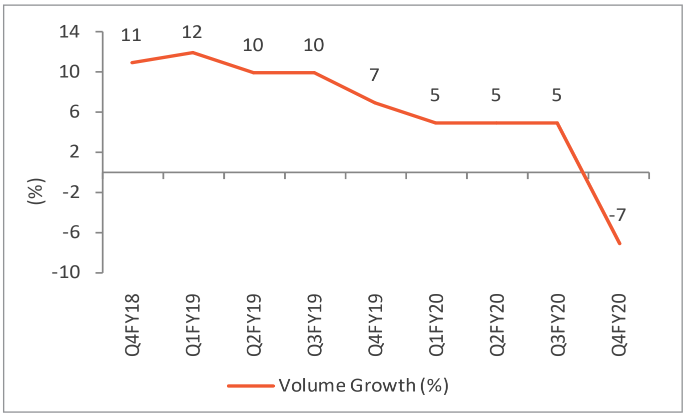


Source: Company, Sharekhan Research

GSK Consumer merger will improve the growth prospects in long run: GSK Consumer has a very strong portfolio of brands in the health food drinks (HFD) category. The penetration level for GSK Consumer's brands stands at 24% (14% in rural geographies), which will provide a massive opportunity and lot of synergistic benefits for HUL. The company plans to leverage category leaders, Horlicks and Boost, and focus would be to grow brands with the help of HUL's extensive distribution channels. It is also an opportunity for HUL to drive premiumisation as the premium portfolio of Horlicks is 22%. The merger is in-line with the company's strategy of building a sustainable and profitable foods and refreshment business in India by leveraging the mega-trend of health and wellness. The management is confident of achieving double-digit revenue growth see margins expand by 800-1,000 bps in the medium term. Further the acquisition of V-Wash gives the company an entry into the currently underpenetrated and rapidly growing female intimate hygiene segment, the penetration of which is currently 8-10% in India. The brand has a leadership position and fits well into the white spaces in the beauty and personal care business.

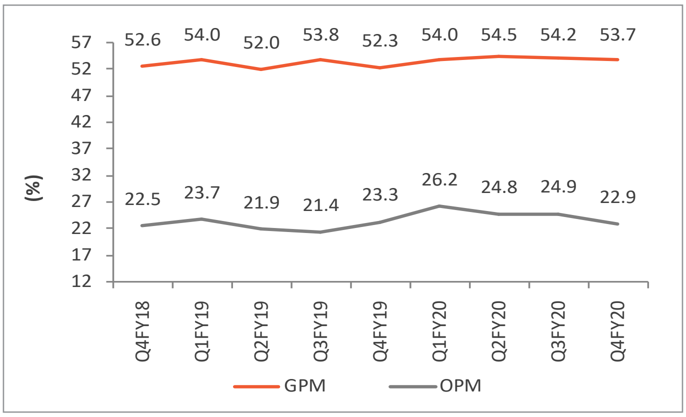
Financials in charts

Volumes declined by 7% in Q4FY2020



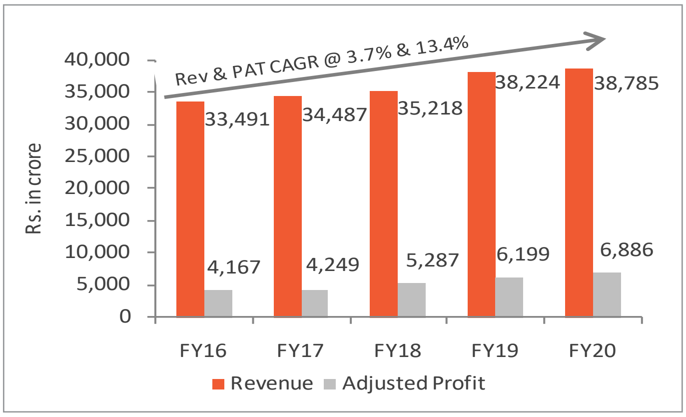
Source: Company, Sharekhan Research

GPM improved y-o-y in Q4, OPM saw slight dip



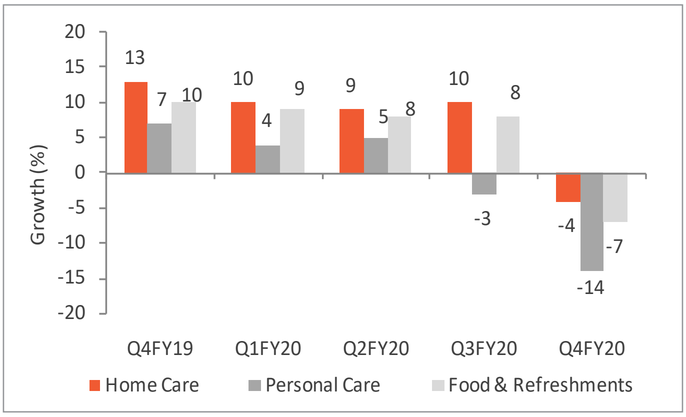
Source: Company, Sharekhan Research

Revenue & PAT CAGR of 3.7% & 13.4% over FY16-20



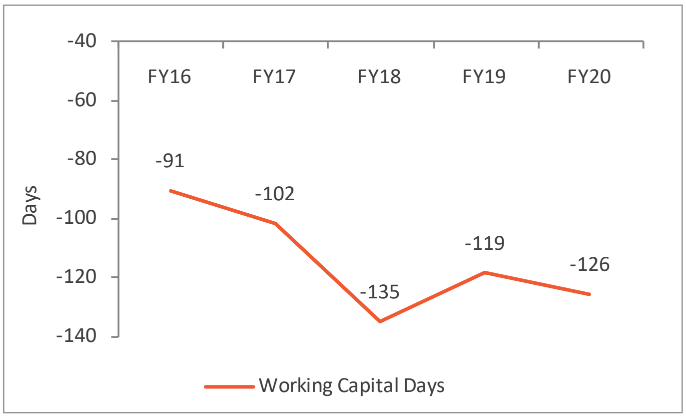
Source: Company, Sharekhan Research

Key categories impacted by lockdown



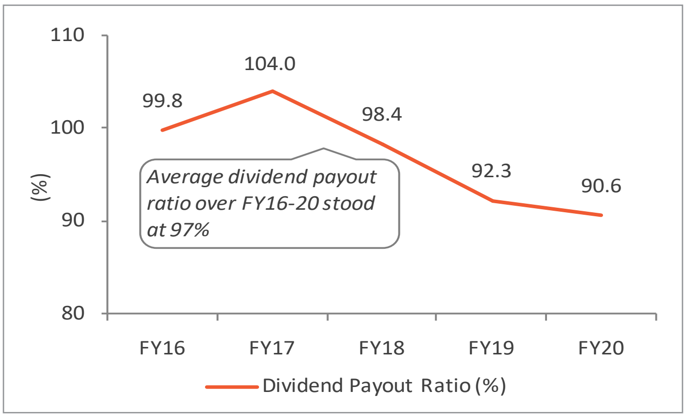
Source: Company, Sharekhan Research

Working Capital remained negative



Source: Company, Sharekhan Research

Strong dividend payout maintained



Source: Company, Sharekhan Research

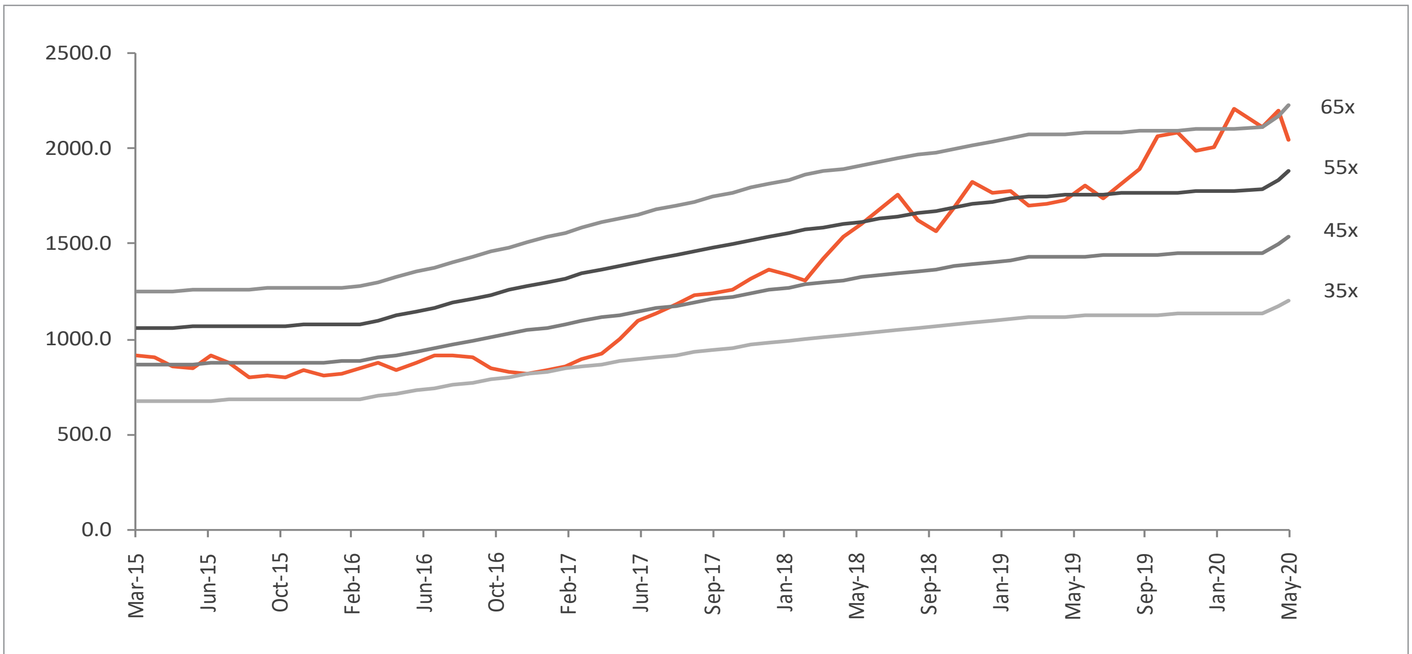
Outlook

Recovery expected post normalisation of the pandemic situation: Q4FY2020 performance was affected by disruption in supply chain at the fag-end of the quarter due to a nationwide lockdown. With the lockdown continuing in April-May, supply disruption is expected to continue though production of essential products has scaled up to 70-80% in many facilities. Thus, Q1FY2021 is expected to be another disappointing quarter with significant loss in revenue and profitability. If the pandemic situation gets under control by June-July, we expect sales to normalise from Q3FY2021 (largely in essential categories). Discretionary categories (such as skin care and hair care) will take some time to regain momentum. We expect performance to fully recover in FY2022. On the other hand, stringent cost-cutting measures and reduction of advertisement spends would provide some support to OPM in the near term.

Valuation

Retain Buy with price target of Rs. 2,305: HUL is currently operating at 70-80% capacity in most of its manufacturing facilities and focusing on supplying whatever its manufacturing through various distribution models. Though FY2021 is expected to affected by spread of COVID-19, HUL's long-term growth prospects are intact and we expect a strong recovery in FY2022 (if pandemic situation is under control by H1FY2021). The stock has already corrected by ~16% from its recent high and trading at 48.1x its FY2022E EPS, which is at discount to its last three years average multiple of 55x. Thus, the recent correction provides a good entry opportunity in quality large consumer goods stock such as HUL from a long-term perspective. We maintain our Buy recommendation on the stock with unchanged price target of Rs. 2,305.

One year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E
Nestle India*	87.1	76.9	62.9	59.5	53.7	44.8	96.9	138.2	126.2
ITC	13.2	12.6	11.2	9.0	8.5	7.5	27.5	28.1	30.7
HUL	65.5	64.3	48.1	46.4	51.4	40.8	105.2	35.9	27.9

Source: Company, Sharekhan estimates
**Values for Nestle India are for CY2019, CY2020E and CY2021E*

About company

HUL is India's largest FMCG company with a strong presence in the homecare and beauty and personal care categories. The company is a subsidiary of Unilever Plc (that holds a 67% stake in HUL), the world's largest consumer goods company present across 190 countries. With over 40 brands spanning 12 distinct categories such as personal wash, fabric wash, skin care, hair care, oral care, deodorants, colour cosmetics, beverages, ice creams, frozen desserts and water purifiers, HUL is part of the everyday life of millions of consumers across India. The company's portfolio includes leading brands such as Lux, Lifebuoy, Surf Excel, Rin, Wheel, Fair & Lovely, Pond's, Vaseline, Lakmé, Dove, Clinic Plus, Sunsilk and Axe. HUL reported revenue of Rs. 38,224 crore and OPM of 22.6% in FY2019.

Investment theme

HUL has a leadership position in highly penetrated categories such as soaps, detergents and shampoos in India. Sustaining product innovation, entering into new categories, premiumisation and increased distribution network remain some of the key revenue drivers for the company. The recent acquisition of GSK Consumer will make HUL a formidable play in the HFD segment and will enhance the growth prospects of its relatively small food business. A strong financial background, robust cash generation ability and leadership position in some key categories give HUL an edge over other companies and, hence, justify the stock's premium valuation.

Key Risks

- **Slowdown in the demand environment:** Any slowdown in demand (especially in rural India) would affect sales of key categories, resulting in moderation of sales volume growth.
- **Increased input prices:** Palm oil and crude derivatives such as linear alkyl benzene are some of the key raw materials used by HUL. Any significant increase in the prices of some of these raw materials would affect profitability and earnings growth.
- **Increased competition in highly penetrated categories:** Increased competition in highly penetrated categories such as soaps and detergents would act as a threat to revenue growth.

Additional Data

Key management personnel

Sanjiv Mehta	Chairman and Managing Director
Srinivas Pathak	Executive Director, Finance & IT and CFO
Pradeep Bannerjee	Executive Director, Supply Chain
Dev Bajpai	Executive Director, Legal and Corporate Affairs and Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Vanguard Group Inc	1.2
2	BlackRock Inc	1.1
3	Nomura Holdings Inc	0.7
4	SBI Funds Management Pvt Ltd	0.7
5	ICICI Prudential Life Insurance Co Ltd	0.4
6	Standard Life Aberdeen PLC	0.4
7	ICICI Prudential Asset Management Co Ltd	0.3
8	J P Morgan Chase & Co	0.3
9	UTI Asset Management Co Ltd	0.3
10	Government Pension Investment Fund	0.2

Source: Bloomberg, **Shareholding as on 17th March, 2020*

Sharekhan

by BNP PARIBAS

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Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;