Marico Limited

Core products regained volume growth in Q2

Consumer Goods	Sharekhan code: MARICO	Result Update

Summary

- Q2FY2021 performance was largely in line with expectations as revenues grew by ~9% while OPM improved marginally by 26 bps to 19.6% (as gross margins slumped by 163 bps).
- Domestic sales volumes grew by 11% in Q2FY2021 (as against a 14% decline in volumes in Q1FY2021), led by a 10% volume growth in Parachute rigid packs, 4% volume growth in value-added hair oils (VAHO) portfolio and a 20% volume growth in Saffola edible oil.
- Parachute rigid packs to maintain 5-7% volume growth, while Saffola edible oil would achieve low-teens volume growth in the near to medium term. Though higher copra prices would impact gross margins in the near term, operating efficiencies would help mitigate impact on OPM.
- We have broadly maintained our earnings estimates for FY2021/22/23E. We retain a Buy on the stock with an unchanged price target of Rs. 420.

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 363**	
Price Target: **Rs. 420**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

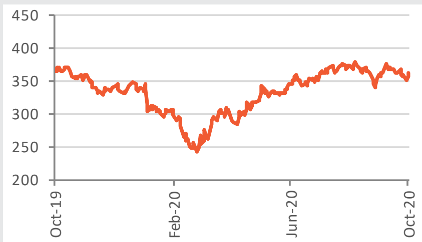
Company details

Market cap:	Rs. 46,885 cr
52-week high/low:	Rs. 392 / 234
NSE volume: (No of shares)	31.7 lakh
BSE code:	531642
NSE code:	MARICO
Free float: (No of shares)	52.2 cr

Shareholding (%)

Promoters	59.6
FII	24.1
DII	11.1
Others	5.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	0.7	0.3	25.1	-0.9
Relative to Sensex	-4.4	-3.4	0.8	-1.1

Sharekhan Research, Bloomberg

Marico's consolidated revenues grew by ~9% in Q2FY2021 driven by an 11% volume growth in the domestic business and 7% constant currency growth in the international business. With improving consumer sentiments and supply chain operations reaching near pre-COVID levels, 95% of the company's product portfolio returned to the growth track y-o-y. Traditional channels continued to outperform with rural growth standing ahead of urban growth. The core portfolio comprising Parachute rigid packs, Saffola edible oil and value-added hair oils (VAHO) registered a volume growth of 10%, 20% and 4%, respectively, during the quarter. VAHO posted strong recovery q-o-q with the middle and bottom-of-pyramid portfolio registering healthy traction. The foods portfolio continues to gain traction and grew by of 55% in value terms. The business is likely to contribute Rs. 200-250 crore in FY2021 (and Rs. 500 crore in FY2022). Globally, Bangladesh registered a constant currency growth of 16% while South Africa posted strong recovery on a sequential basis. Consolidated gross margins decreased by 163 bps to 48% mainly on account of higher copra prices. However, lower advertising spends and efficiencies helped OPM improve by ~26 bps to 19.6%. With a good recovery in the volume growth of core categories, strong traction to the new launches (especially in food category) and steady growth in the international business, Marico is expected to post 10-13% revenue growth over the next two years. Though rising input prices would put stress on margins, stringent cost-saving measures and prudent ad-spends would help in the mitigating the impact at OPM level. Thus, we expect OPM to sustain at ~20% in the near term and would gradually improve with stabilisation in the key input prices.

Key positives

- Domestic business volume growth recovered to 11% as against ours as well as the street's expectation of 7-8%.
- Newly-launched Saffola honey garnered market share of 8% in the modern trade channels within 3 months of launch.
- Rationalising SKUs helped reduce inventory days by 8 days to 58 days and a lower modern trade/CSD contribution helped shorten debtor days by 11 days to 26 days.

Key negatives

- Increase in copra prices led to 163 bps decline in gross margins to 48%.

Our Call

View - Retain Buy with an unchanged PT of Rs. 420: We have broadly maintained our earnings estimates for FY2021/22/23. Gaining market share from a shift to branded products in core categories, expanding into hygiene and foods category through relevant launches, expanding the reach in the rural market and scaling-up of international business (especially in Bangladesh and MENA) will be medium-term growth drivers. We expect revenue and earnings to clock a CAGR of 8.3% and 13.6% over FY2020-23. The stock is currently trading at 34.2x and 29.9x its FY2022E and FY2023E EPS, respectively, which is at a discount to some of the large-cap FMCG stocks. We maintain our Buy recommendation on the stock with an unchanged price target of Rs. 420.

Key Risks

Any slowdown in the demand of key categories or sustained surged in the key input prices would act as a key risk to revenue growth and earnings estimates in the near term.

Valuations (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	7,334	7,315	7,505	8,501	9,382
OPM (%)	17.3	19.9	20.3	21.5	22.0
Adjusted PAT	939	1,069	1,114	1,369	1,568
Adjusted EPS (Rs.)	7.3	8.3	8.6	10.6	12.2
P/E (x)	49.9	43.8	42.0	34.2	29.9
P/B (x)	15.6	15.5	13.2	10.8	8.8
EV/EBIDTA (x)	36.3	31.8	30.2	24.7	21.4
RoNW (%)	33.9	35.5	33.9	34.7	32.4
RoCE (%)	40.6	41.3	40.9	44.2	41.6

Source: Company; Sharekhan estimates

Domestic volumes grew by 11%; higher input prices affected margins: Consolidated revenue grew by 8.7% y-o-y to Rs. 1,989 crore driven by domestic volume growth of 11%. The India business grew by 8% y-o-y, reporting revenue of Rs. 1,508 crore as lockdown restrictions were eased in most parts of the country and supply chains normalised. The international business grew by 7% y-o-y in constant currency terms. Rise in input prices of certain key inputs such as copra and other edible oils resulted in consolidated gross margins contracting by 163 bps to 48%. Despite this, rationalised advertisement spends in discretionary categories and aggressive cost control, resulted in consolidated OPM to expand by 26 bps to 19.6%. OPM of the India business was slightly lower at 20.7% in Q2FY2021 as against 21% in Q2FY2020, as the company undertook cost-saving initiatives to counter input cost headwinds. Consolidated operating profit grew by 10.2% y-o-y to Rs. 389 crore. In spite of lower other income, a fall in interest and depreciation charges helped before tax (PBT) to grow by 10.3% y-o-y to Rs. 375 crore, whereas lower tax incidence led adjusted PAT to grow by 16.2% y-o-y to Rs. 294 crore in Q2FY2021 from Rs. 253 crore in Q2FY2020. There was a post-tax exceptional item of Rs. 21 crore pertaining to partial rationalisation of capacities in one of the units resulting in impairment of fixed assets and inventory. Thus, reported PAT came in at Rs. 273 crore, growing by 8% y-o-y. Excluding the impact of this one-off, like-to-like PAT growth stood at 15% at Rs. 285 crore.

Strong quarter for Saffola led by in-home consumption trend; VAHO and Parachute bounce back to positive growth trajectory:

- **Coconut Oil – Parachute Rigid packs recover; clock 10% volume growth:** Parachute rigid pack sales grew by 10% in volume terms and 8% in value terms, driven by shift to trusted brands and its strong leadership position. The brand reinforced its hygienic processing and safety credentials in the minds of consumers with the launch of the “Untouched by hand” campaign. The focus would be on availing value preposition to consumers in an uncertain environment. The company will take judicious pricing decisions to maintain a balance between volumes and margins. Rural penetration for Parachute stands at ~46%, driven by a shift towards branded products from local/unbranded products. Marico intends to expand its direct distribution, especially in rural geographies. The company expects 5-7% volume CAGR in Parachute Rigid packs in the medium term.
- **Saffola continued its robust growth momentum:** Sales volume of Saffola refined edible oil grew by 20% in Q2FY2021, driven by in-home consumption trend and an increase in household penetration. 62% of the volume growth came from enhanced penetration. Higher salience was witnessed in e-commerce channels. Saffola continues to do well in modern trade, however, CSD channel remains affected. Since people are searching for healthier brands, the retention rate in Saffola has gone up leading to market share gains. The company leveraged digital media through targeted campaigns in the lockdown to engage with consumers. Marico continued its media investments behind the brand. The company expects double-digit growth in FY2021, led by increased in-house consumption, stronger brand equity, and higher demand for healthy products. As consumption will normalise, the company expects to sustain high single-digit volume growth over the medium term.
- **VAHO bounced back strongly:** The VAHO segment stood almost flat in value terms, while sales volumes grew by 4% in Q2FY2021 after a sharp decline of 30% in Q1, largely driven by healthy growth in the bottom of the pyramid/value products. The premium segment remained subdued and CSD volumes declined in double digit. Excluding CSD, VAHO volumes grew by 7%. Nihar Shanti Amla Badam led the recovery in VAHO, while among the newer introductions, Parachute Advansed Aloe Vera Enriched Coconut Hair Oil witnessed increased traction. The company will continue to invest in TV and print media to further strengthen its brand image and drive penetration of larger packs. Expanding its presence in the non-sticky hair oil space, Nihar Naturals Almond was launched in select states. The company aims to revive growth in the VAHO segment in the medium term by adopting a three-pronged strategy of aggressive participation at the bottom of the pyramid, accelerating growth in the mid-segment through pricing, and brand renovation and gaining market share in premium segments, where penetration is low, through innovations and brand-building.
- **Other discretionary categories barring foods stayed subdued; good traction for hygiene products:** The foods category’s revenue grew by 55% y-o-y, driven by strong ~45% growth in Saffola Oats franchise. 60% of the growth came from increased household penetration. Saffola Honey is scaling up across channels and has gained an 8% market share in modern trade within three months of launch. In response to heightened immunity boosting needs of consumers, the company has launched Kadha Mix & Golden Turmeric Milk Mix under Saffola ImmuniVeda in select modern trade and e-Commerce channels. The company also forayed into the chyawanprash category with the launch of Saffola Arogyam Chyawan Amrut. Premium hair nourishment,

male grooming, and premium skin care categories recorded improved sequentially after a tough Q1, however, they continue to decline on a y-o-y basis. The company had forayed into the hygiene segment with the launch of Mediker hand sanitiser and Veggie Clean in April, which are gaining good traction. The company also launched Revive laundry sanitiser. Given the shift in consumer behaviour during this crisis, the company will prioritise investments in foods and hygiene categories over premium personal care categories in the near term.

Good growth in Bangladesh and South Africa; Southeast Asia and MENA markets continue to remain soft

International business revenue grew by 12% y-o-y (7% growth in constant currency [CC] terms) mainly driven by 16% revenue growth in Bangladesh and South Africa each. Growth in Bangladesh was largely led by the non-coconut oil portfolio (contributes 35% to revenue), which grew by 31% in CC terms Q2FY2021, while Parachute coconut oil grew by 8%. Marico launched Just for Baby Skin Cream and Saffola Honey in Bangladesh. Strong growth in South Africa was driven by robust growth in the health care and hair care portfolios. Southeast Asia reported a revenue decline of 4% in CC terms due to a 6% decline in Vietnam as the home and personal care segment slowed down. The MENA region witnessed a 6% decline in revenue in CC terms due to continued volatile macro-economic environment coupled with COVID-19 related restrictions and supply disruptions. OPM of the international business expanded to 23.1% in Q2FY2021 from 21.5% in Q2FY2020 on account of tight cost management across all geographies. The company aims at reporting an organic broad-based double-digit CC growth over the medium term.

Key conference call highlights

- About 95% of the portfolio has returned to positive growth trajectory across categories. Saffola continues to do well driven by heightened penetration whereas the VAHO segment and Parachute recovered sequentially after a sharp decline in Q1, driven by shift towards trusted brands and higher demand for value-for-money products. The company has maintained its target of 8-10% volume growth in the medium term.
- Traditional trade and e-Commerce channels registered healthy growth whereas CSD channel continued to decline. E-Commerce channel grew by 39% y-o-y and its contribution improved to 8% of total revenue. Modern trade channel is expected to improve sequentially. Rural growth stood ahead of urban growth, with rural volumes growing by 22%. Secondary sales were ahead of primary sales, as the company maintained lower inventory levels with distributors to maintain higher return profile for them and to keep the supply chain more agile. Marico sells its products through 5.1 million retail outlets and its direct distribution reach currently stands at 1 million outlets and the company intends to expand it in the coming years.
- The foods business is expected to touch revenue of Rs. 450-500 crore by FY2022 driven by strong growth in Saffola oats and good traction to Saffola honey. The hygiene portfolio contributed 1.5% to the total revenue in H1FY2021, though the company has witnessed normalising of the accelerated demand in this category. Marico expects the portfolio to report revenue of Rs. 80-100 crore going ahead. Margins of food products are higher than that of edible oils; and thus, they are expected to perform better than the edible oil portfolio.
- In terms of the international business, Bangladesh continued to register strong growth, driven by non-coconut hair oil portfolio; and growth momentum is expected to sustain. Vietnam is recovering faster. The company plans to diversify the portfolio in Vietnam (as it did in Bangladesh) and expects to see results from Q4FY2021. South Africa reported strong growth and the company intends to continue focusing on ethnic hair care and health care portfolio over the medium term. MENA region is expected to remain soft and will take some time to recover.
- Copra prices and other edible oils such as rice bran oil prices had increased during the quarter. However, some softening has been witnessed in input costs over the past 10 days. The company expects the input prices to remain on the higher side only till November/December and expects the prices to remain soft in Q4FY2021. Thus, the company does not want to take any pricing actions for this short period and will absorb the rise in input costs. Efficient cost management will help Marico tackle the input cost pressure and the company intends to focus on maximising volumes. Conservative ad-spends and cost saving initiatives would aid in structural cost savings of over ~Rs. 150 crore, which would help consolidated OPM to stay ahead of 20% in the near to medium term.
- Marico has planned to expand its digital brands such as Beardo by creating/acquiring more such brands over a period of 3-4 years to fill in the gaps. It will continue to invest in its digital capability.

Results (Consolidated) Rs cr

Particulars	Q4FY20	Q4FY19	YoY %	Q3FY20	QoQ %
Net sales	1989.0	1829.0	8.7	1925.0	3.3
Expenditure	1600.0	1476.0	8.4	1458.0	9.7
Operating profit	389.0	353.0	10.2	467.0	-16.7
Other income	27.0	35.0	-22.9	19.0	42.1
Interest expenses	8.0	13.0	-38.5	9.0	-11.1
Depreciation	33.0	35.0	-5.7	34.0	-2.9
PBT	375.0	340.0	10.3	443.0	-15.3
Tax	81.0	88.0	-8.0	104.2	-22.3
PAT (before MI)	294.0	252.0	16.7	338.8	-13.2
Minority Interest (MI)	0.0	1.0	-	-2.0	
Adjusted PAT (After MI)	294.0	253.0	16.2	336.8	-12.7
Extraordinary items	21.0	0.0	-	-51.2	-
Reported PAT	273.0	253.0	7.9	388.0	-29.6
Adjusted EPS	2.3	2.0	16.2	2.6	-12.7
			bps		**bps**
GPM (%)	48.0	49.6	-163	48.6	-61
OPM (%)	19.6	19.3	26	24.3	-470

Source: Company; Sharekhan Research

Results (Standalone) Rs cr

Particulars	Q4FY20	Q4FY19	YoY %	Q3FY20	QoQ %
Net Sales	1550.0	1454.0	6.6	1516.0	2.2
Operating profit	279.0	262.0	6.5	332.0	-16.0
Adjusted PAT	339.4	259.0	31.0	255.0	33.1
GPM(%)	43.3	45.9	-258	44.1	-84
OPM(%)	18.0	18.0	-2	21.9	-390

Source: Company; Sharekhan Research

Value and Volume growth of key categories

Categories	Q2FY21		Revenue share in FY20 (%)
	Value growth	Volume growth	
Parachute Coconut Oil (Rigid packs)	8%	10%	38%
Value Added Hair Oils	-1%	4%	24%
Saffola (Refined Edible Oil)	16%	20%	20%

Source: Company

Outlook and Valuation

■ **Sector Outlook - Supply chain back to normal; foods gaining strong traction; hair care on recovery mode**

Consumer goods companies saw a strong revival in Q2FY2021 with production and supply recovering to 100% of pre-COVID levels. A strong pick-up in rural demand, general trade normalising and higher sales through online channels aided most consumer goods companies to recover to pre-COVID levels in most categories. Hair-care products are re-gaining momentum (especially at the bottom-of-the pyramid). Consumers shifting from loose to branded hair oil would help large companies gain market share. 1) Sustained demand for branded foods, hygiene and HI products; 2) pick-up in rural demand; 3) new launches and 4) focus on expansion of distribution reach are some of the near-term growth catalysts. Prices of most of the key inputs (barring palm oil, raw tea and coffee) have remained benign. This along with cost-saving initiatives would help consumer goods companies to post better margins in the coming quarters.

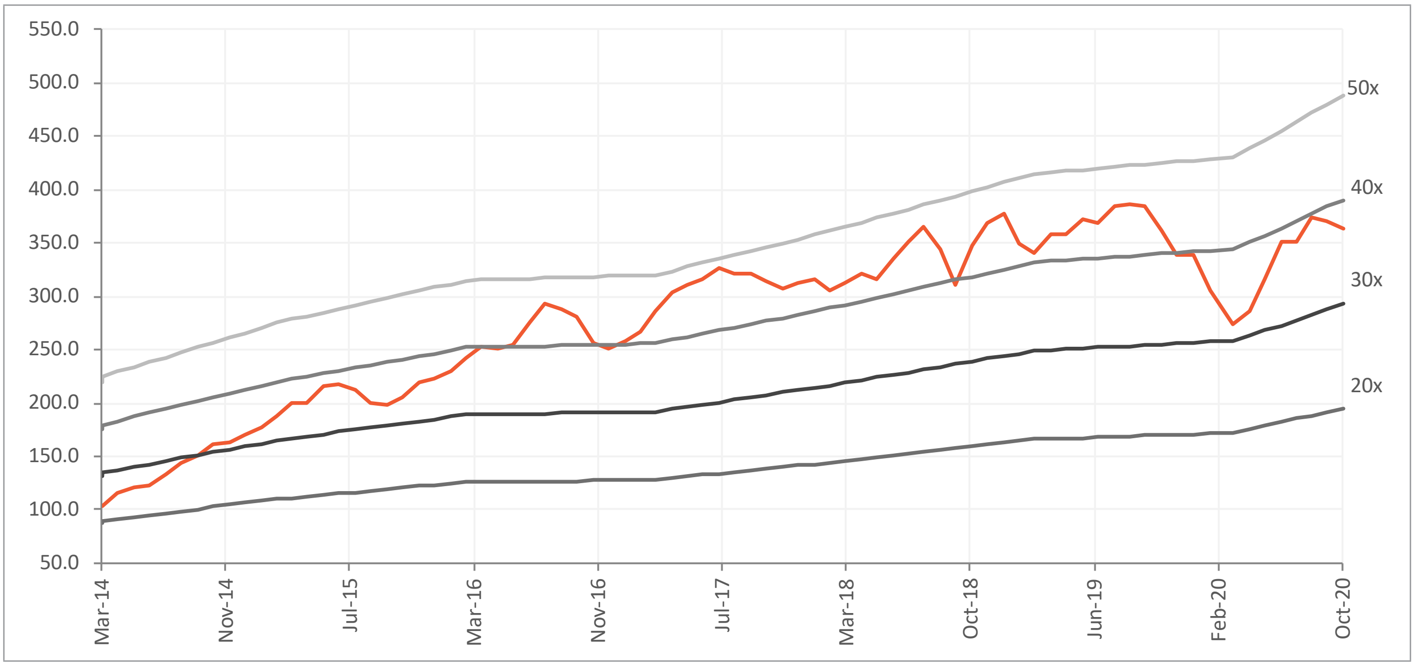
■ **Company outlook - 95% of portfolio back to growth trajectory**

With a recovery in the sales volume of core domestic portfolio, Marico posted 11% volume growth in the domestic business. The company expects Parachute rigid packs to achieve volume growth of 5-7%; Saffola edible oil to achieve volume growth of 12-14% and VAHO to post a sequential recovery in volume growth in the near term. On the international front, Bangladesh continues to perform well, Vietnam has recovered and MENA region is getting out of tough times. On the margin front, the management is confident of achieving OPM of ~20%+ at consolidated level. New launches, scale-up of male grooming and hair nourishment, market share gains from conversion of loose to branded oils, double-digit growth in VAHO (focus on premium end), higher contribution from hygiene portfolio and higher sales target in foods portfolio are some of the medium-term revenue drivers for Marico. Improvement in revenue mix along with cost-saving initiatives would help the company to achieve gradual improvement in margins.

■ **Valuation - Retain Buy with unchanged price target of Rs.420**

We have broadly maintained our earnings estimates for FY2021/22/23. Gaining market share from a shift to branded products in core categories, expanding into hygiene and foods category through relevant launches, expanding the reach in the rural market and scaling-up of international business (especially in Bangladesh and MENA) will be medium-term growth drivers. We expect revenue and earnings to clock a CAGR of 8.3% and 13.6% over FY2020-23. The stock is currently trading at 34.2x and 29.9x its FY2022E and FY2023E EPS, respectively, which is at a discount to some of the large-cap FMCG stocks. We maintain our Buy recommendation on the stock with an unchanged price target of Rs. 420.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer valuation

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E
Dabur	59.8	55.1	43.3	50.1	44.7	34.8	27.0	26.7	30.0
Hindustan Unilever	67.3	59.7	47.3	47.7	42.0	35.6	105.2	39.1	28.5
Marico	43.8	42.0	34.2	31.8	30.2	24.7	41.3	40.9	44.2

Source: Company, Sharekhan estimates

About company

Marico is one of India's leading consumer products companies in the domestic hair and wellness market with a turnover of over Rs. 7,000 crore. Marico is present in the categories of hair care, skin care, edible oils, health foods, and male grooming, with a vast portfolio of brands such as Parachute, Saffola, Hair & Care, Nihar, Livon, Kaya Youth, and Coco Soul. The company is currently present in 25 countries across emerging markets of Asia and Africa, including Middle East, Bangladesh, Vietnam, Egypt, and South Africa, which constitute 22% of the total revenue. The company has a retail reach of 4.9 million outlets in the domestic market.

Investment theme

Marico is a leading player in the domestic hair and wellness market with a leadership position in categories such as branded hair oil (~62% market share), value-added hair oil (~36% market share), and branded edible oil (~77% market share). The company has a three-pronged strategy of driving growth through key categories, innovations/entrance into niche category and scale up its presence in international geographies. In recent times, the company has entered into niche categories such as male grooming, premium hair nourishment, and healthy foods, which will not only improve the revenue growth trajectory but would help in boosting margins in the long run due to their premium nature. Consistent innovations, a wide distribution network, and expansion in new-age channels such as modern trade and e-commerce would be key platforms to achieve good growth in the near term.

Key Risks

- Demand slowdown: Slowdown in key product categories would affect overall demand and revenue growth.
- Higher input prices: A significant increase in prices of key raw materials such as copra (~40% of input costs) would affect profitability and earnings growth.
- Increased competition in highly penetrated categories: Increased competition in highly penetrated categories such as VAHO and edible oils would threaten revenue growth.

Additional Data

Key management personnel

Harsh Mariwala	Chairman
Saugata Gupta	Managing Director and CEO
Vivek Karve	Chief Financial Officer
Hemangi Ghag	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	First State Investment ICVC	5.3
2	First State Global Umbrella Fund	4.0
3	Life Insurance Corporation of India	3.7
4	Blackrock Inc	1.3
5	Vanguard Group Inc	1.3
6	Arisaig India Fund Limited	1.3
7	Mitsubishi UFJ Financial Group Inc	0.6
8	Aditya Birla Sunlife Asset Management	0.6
9	UTI Asset Management Co Ltd	0.6
10	Bajaj Allianz Life Insurance Co Ltd	0.4

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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