Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

ITC Ltd

Building a sustainable growth path

Consumer Goods	Sharekhan code: ITC
Reco/View: Buy ↔	CMP: **Rs. 228** — Price Target: **Rs. 280** ↔

↑ Upgrade ↔ Maintain ↓ Downgrade

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

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS	Neutral	↔	Neutral
RQ	Positive	↔	Positive
RV	Positive	↔	Positive

ESG Disclosure Score NEW

ESG RISK RATING 27.3

Updated Nov 08, 2021

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

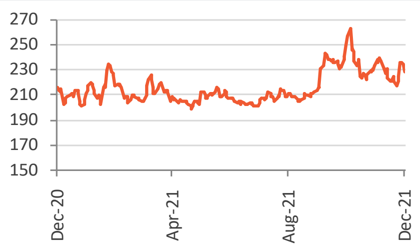
Company details

Market cap:	Rs. 281,273 cr
52-week high/low:	Rs. 265 / 197
NSE volume: (No of shares)	231.7 lakh
BSE code:	500875
NSE code:	ITC
Free float: (No of shares)	1232.0 cr

Shareholding (%)

Promoters	0.0
FII	11.8
DII	43.7
Others	44.6

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-4.0	5.8	10.4	5.9
Relative to Sensex	0.3	6.9	0.3	-19.8

Sharekhan Research, Bloomberg

Summary

- ITC eyes double-digit revenue growth and higher PAT growth in the medium term with sustained margin expansion riding on six core growth strategies of leveraging on institutional strengths, innovation, digitalisation, cost optimisation, sustainability and creating a strong talent base.
- Capex of Rs. 10,000 crore has been lined up over three years of which 35-40% will be ploughed into the FMCG business. Hotel business would stay asset-light and ITC would raise investments on digitalisation and inorganic initiatives in medium term.
- Management is committed to restructure hotel business after an overall recovery while it will evaluate unlocking value in the infotech and FMCG business once it attains scale. However there is not stated timeline for same. With strong cash flow generation, ITC's dividend payout would stay at 80-85%.
- Stock continues to trade at a discounted valuation of 16.3x/14.6x its FY2023/24E EPS. We maintain our Buy on the stock with an unchanged price target of Rs. 280.

In its first-ever investor meet, ITC's management stated that its focusing on improving growth prospects all its businesses through core business strategies and equally committed towards enhancing shareholder value by restructuring business and maintaining higher dividend payouts. ITC is focusing on achieving double-digit revenue growth with sustained margin expansion through six core strategies of developing a consumer centric organisation, identifying new vectors of growth in each business, innovation, cost optimisation, sustainability and creating a strong talent base. ITC's cumulative free cash flows have stood at ~Rs. 74000 crore over the last decade. It will continue to pay dividends at the rate of 80-85% in the medium term after investing towards growth prospects of key businesses.

- **Strategising to deliver double-digit earnings growth:** ITC's revenue and PAT grew at 2.6x and 3.7x over FY2010-20 (Non cigarette businesses revenues and PBIT cumulatively grew by 20x and 18x over the same period). ITC is focusing on growing its cigarette business by maximising cigarette potential within tobacco basket, non-cigarette FMCG by strengthening the core portfolio and entering into new categories through innovation, hotel business through asset-light model, Paperboard, paper & packaging by developing sustainable packing solutions and agri-products business by climbing the value chain. Management is confident of achieving double-digit revenue and PAT growth in the medium term.
- **Cigarette sales volume back to pre-COVID level; hotel business recovering well:** ITC's cigarette sales volume is back to pre-COVID levels led by improved mobility post easing of lockdown norms, quick restoring of inventory and stable pricing environment. Management expects ITC revenue growth to be volume led in the stable pricing environment with focus on gaining share from illicit cigarettes. Hotel business has recovered strong with occupancies back to pre-covid levels while average room rentals recovered to 75% of pre-covid level. Despite raw material inflation, non-cigarette FMCG business will focusing on maintaining margins through cost efficiencies, judicious price hikes and better mix.
- **Strong cash flows; dividend pay-out to remain at 80-85%:** ITC's cumulative free cash flow for last decade stood at Rs. 74000 crore on back of strong cash generation ability in core cigarette business. The company's non-cigarette FMCG business is largely on cash and carry business with limited debtors on books while inventory levels high due to stocking up agri commodities such as wheat for non-cigarette FMCG business. The company is focusing on smart buying with the help of digital analytics and input optimisation to efficiently manage inventory in long run. The company has planned for capital expenditure of Rs. 10,000 crore in the next three years. Dividend payout would remain at 80-85% in the medium term.

Our Call

View – Retain Buy with an unchanged PT of Rs. 280: ITC's management has enhanced focus and redefined growth strategies for all its business vertical to improve its growth prospects in medium to long term. The company has sustained ESG rating of AA by MSCI-ECG highest amongst global tobacco companies. The management is committed towards restructuring of hotel business post overall recovery in the hotel industry, while it will evaluate unlocking value in the Infotech and FMCG business once it attains scale. However, there is no stated time-line for restructuring programme. The stock is currently trading at 16.3x and 14.6x its FY2023 and FY2024 EPS, which is at stark discount to some of the large consumer goods stock. We maintain our Buy recommendation on the stock with an unchanged price target of Rs. 280.

Key Risks

Any increase in taxes on cigarettes or government implementing policies to curb tobacco products consumption or any disruption in consumer demand due to frequent lockdowns would act as key risk to our earnings estimates.

Valuation (standalone) Rs cr

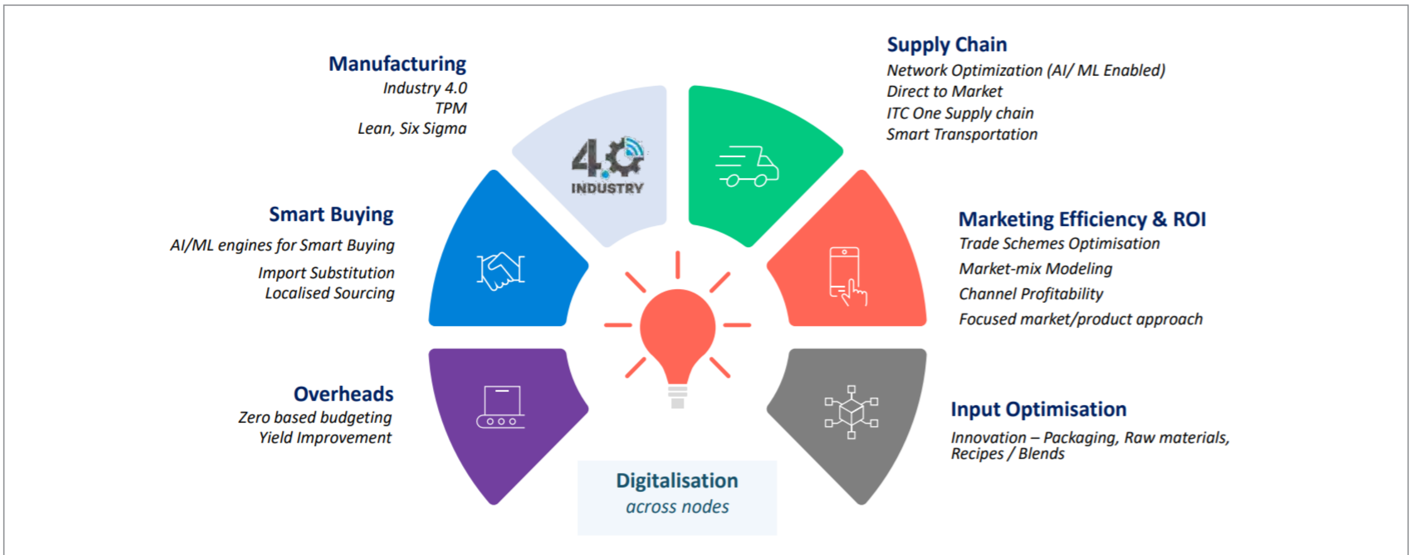
Particulars	FY21	FY22E	FY23E	FY24E
Revenues	48,525	53,756	59,351	65,763
OPM (%)	32.0	34.5	36.5	37.0
Adjusted PAT	13,032	14,371	17,052	19,058
Adjusted EPS (Rs.)	10.7	11.8	14.0	15.6
P/E (x)	21.4	19.4	16.3	14.6
P/B (x)	4.8	4.7	4.5	4.3
EV/EBIDTA (x)	16.5	13.6	11.6	10.2
RoNW (%)	21.2	24.2	28.0	29.9
RoCE (%)	21.5	26.9	31.1	33.6

Source: Company; Sharekhan estimates

Six core strategies to achieve sustainable earning growth in the medium term

ITC's revenue and PAT grew at 2.6x and 3.7x over FY2010-20 (Non cigarette businesses revenues and PBIT cumulatively grew by 20x and 18x over the same period). ITC is focusing on sustainable earnings growth on back of six core strategies of developing consumer-centric organisation, identifying new vectors of growth in each business, innovation, cost optimisation, sustainability and creating a strong talent base. It is focusing on growing its cigarettes business by maximising the potential of cigarettes within the tobacco basket, non-cigarette FMCG by strengthening the core portfolio and entering into new categories through innovation, hotel business through the asset-light model, Paperboard, paper & packaging by developing sustainable packing solutions and agri-business by climbing the value chain. The company is focusing on driving cost agility and productivity through manufacturing and supply chain efficiency, smart buying, market efficiency, input optimisation and zero-based budgeting. Management is targeting to achieve double digit revenue and earnings growth with sustained margin expansion in the medium term.

Driving cost agility & Productivity

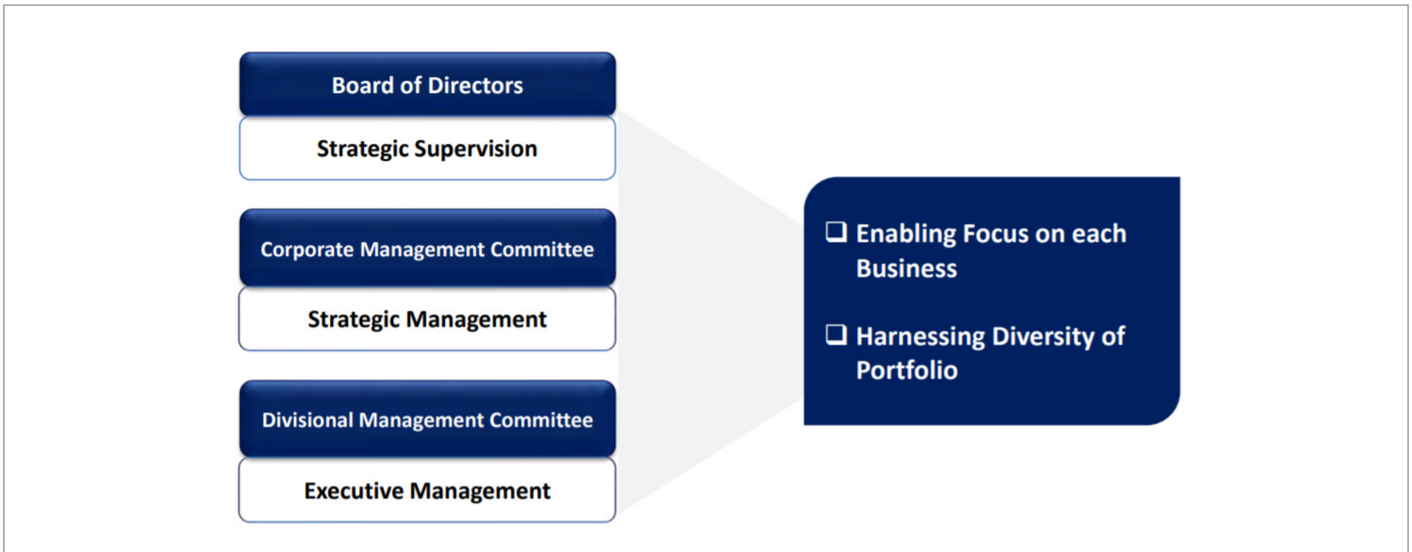


Source: Company presentation

Strategy of organisation

ITC has developed 3-tier governance structure, which will enable it to focus on each business. This approach allows Businesses, through their management committees, to focus, develop and execute business plans relevant to their product-market spaces while leveraging the institutional strength of the company.

3-tiered governance structure

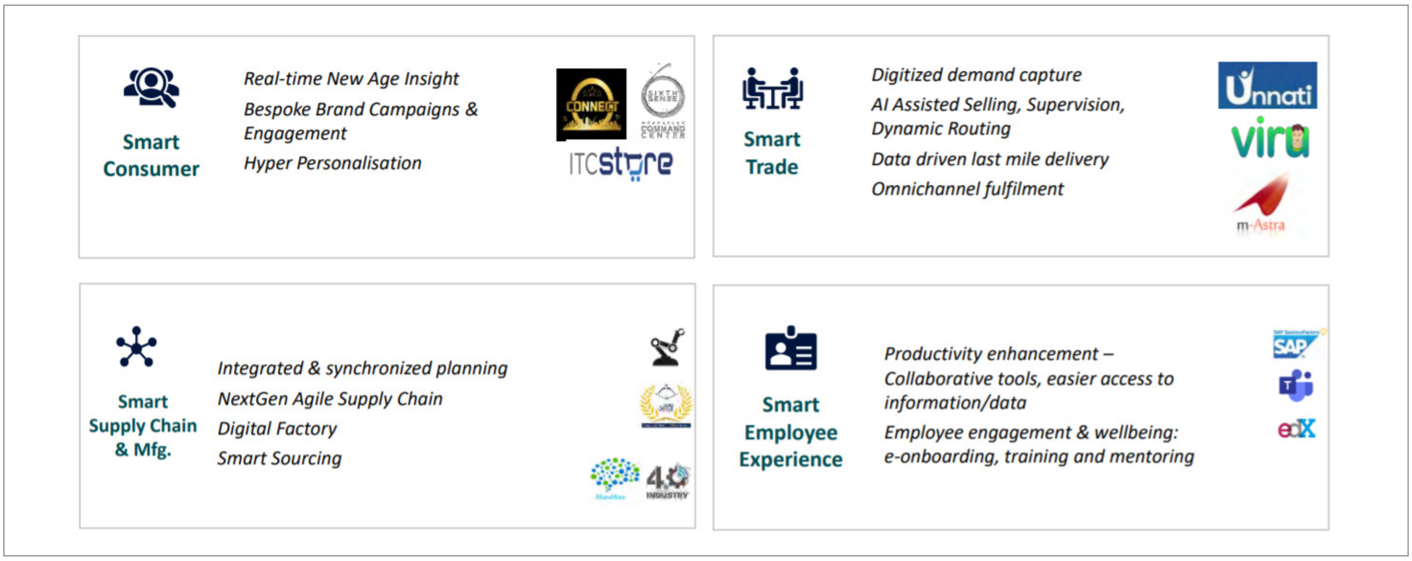


Source: Company presentation

Digital @ITC

Accelerated digital transformation is integral to ITC's future-ready strategy and is increasingly being harnessed to enhance the competitive advantage. Digital technologies are being increasingly deployed across the ecosystem spanning consumer experience, smart and agile manufacturing & supply chain operations, employee experience and intelligent insights platforms. Foundational initiatives such as the DigiNext / Young Digital Leaders Forum and 6th Sense have been implemented towards steering your Company through its digital journey and fostering a data-driven and digital first culture across the organisation.

Building a dynamic 'Future-tech' enterprise



Source: Company presentation

Capex plan of Rs 10,000 crore over the next three years

The company has planned for capital expenditure of Rs. 10,000 crore over the next three years (~Rs. 3,000 crore per annum). Around 35-40% of the capex will be allocated towards non-cigarette FMCG business. With demand improving and business scaling up, the company would invest in adding more production lines at various facilities. Further it would be investing 25-30% of planned capex to augment the paperboard and packaging capacity to maintain the higher capacity utilisation. With focus on asset light model, the company would be allocating ~10% of total capex for hotel business. It expects the capex for hotel business to reduce substantially over the medium term. Further, the company is also focusing on developing digital infrastructure and improving growth prospects of export business in medium to long term. It is also looking at inorganic initiatives (especially in FMCG and IT business) to fast scale up the key business verticals.

Strong cash generation ability; higher dividend payout and prudent capital allocation would sustain

ITC has strong cash generation ability on back of high cash generated by its core cigarette business. It has generated cumulative free cash flow (FCF) of over ~Rs. 74,000 crore in the last ten years. The company had invested large part of these cash flows in improving growth prospects of non-cigarette FMCG business. Further the strong cash flow is also utilised in health dividend payout which stood at 102% in FY2021 (dividend yield of 4.4%). With prudent capital allocation and strengthening of working capital management, the company expects cash flows to remain high in the medium term. Hence, targets to maintain dividend payout at 80-85% in the medium term.

Cigarette business – stable tax policy would help in driving steady growth

With strong portfolio of brands (straddling the pyramid) and wide distribution network (available in 7.1 million outlets) ITC is market leader in the domestic cigarette business. The company is focusing on maximising potential of cigarettes within the tobacco basket (with legal cigarettes constituting ~8% of tobacco consumption in India), countering illicit trade and reinforcing market standing. In the event of high growth in taxes of cigarette, the cigarette sales volumes have moderately grown as consumers shift to illicit cigarettes and other forms tobacco products. However, in the stable tax environment in the recent past, volume growth was good (except for pandemic affected year of FY2021). ITC cigarette sales volume has recovered to pre-COVID levels in Q3FY2022 with improved mobility, stable pricing environment and fast restoring of inventory. The management expects ITC revenue growth to be volume led in the stable pricing environment with focus on gaining share from illicit cigarettes. However, in the event of significant increase in the tax rate, the revenue growth would largely be a price led growth. The company has proposed for reasonable tax hike in the upcoming budget which will help in maintaining the steady volume growth momentum in the medium term.

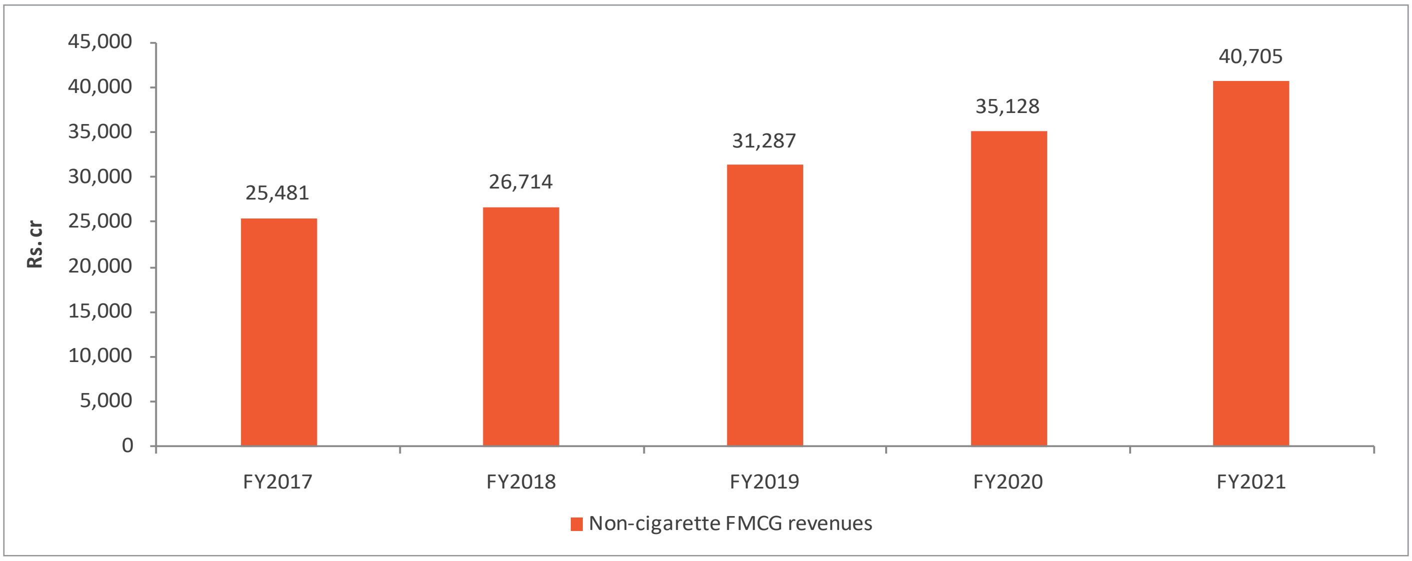
Hotel business – Eyeing growth through asset-light model

The company is focusing on fuelling growth in hotel business through asset-light model. The company expects managed rooms to constitute to around 43% (2.1x over the next five years) in FY2026 from 25% in FY2021. With easing of lockdowns and improvement in overall mobility, the hotel business has recovered faster in Q2FY2022. Management expects performance to be much better in Q3 with occupancies recovering to pre-COVID level while average room rentals (ARRs) recovering to 75% of pre-COVID levels. Domestic leisure travel is growing much faster while business travel has recovered to 50% of pre-COVID level. With outbound travel likely to take a step back, the domestic tourism is likely to propel the growth for domestic hotel industry in the medium term.

FMCG (Non cigarette) – focus on scaling up the business by strengthening the core

ITC's non-cigarette FMCG business revenues posted a 9% CAGR over FY2015-FY2021 (to Rs. 14,728.1 crore in FY2021). The company's current product portfolio comprises of 25 recognised brands and caters to Rs. 22,000 crore of consumer annual spends, providing a number of opportunities to grow in the coming years. ITC remains focused on rapidly scaling up the FMCG businesses anchored on strong growth platforms and a future-ready portfolio. It focuses on building brands with a purpose and aims to achieve growth by driving its digital engagement and multi-channel go-to-market capability. The growth platforms of the company include fortifying the core - Strengthen its market standing in the existing core operating categories, in many of which it is already a leading player. Aashirvaad is No. 1 in Branded Atta, Bingo! is No. 1 in Bridges segment of Snack Foods (No.2 overall in Snacks & Potato Chips), Sunfeast is No. 1 in the Cream Biscuits segment, Yippee! is No. 2 in Noodles, Engage is No. 2 in Deodorants among others; addressing adjacencies leveraging mother brands - Address adjacent growth opportunities by leveraging the 25 powerful mother brands it has established over the years. Recent examples of such brand extensions include Aashirvaad into dairy, ready meals, salt and spices; Sunfeast into dairy beverages and cakes; Bingo! to namkeen; ITC Master Chef's expansion to frozen snacks and cooking pastes; Savlon's entry in surface & cloth disinfectant sprays, sanitisers, masks etc; building categories of the future - Continue to make strategic investments in building the 'new core' by scaling up nascent categories such as Dairy (Aashirvaad Svasti), Beverages (B Natural), Chocolates (Fabelle, Candyman Fantastik), Coffee (Sunbean), Home Care (Nimyle, Nimwash, Nimeasy) and Skin Care (Dermafique, Charmis). Overall, the non-cigarette FMCG business revenue is expected to post a CAGR of 15-16% over FY2021-FY2024.

Non-cigarette FMCG revenues growing steadily



Source: Company; Sharekhan Research

The company's multi-channel distribution has grown over the years with increased penetration and accessibility and strengthening of the core channels. ITC's total reach stands at over 6.6 million outlets having grown at 1.2x since 2016 while the direct reach is at over 2.5 million outlets having grown 1.4x since 2016. The company's market coverage and number of stockists have grown by 4.5x and 6x, respectively since 2016. The company has also expanded its e-commerce channel with current salience at 7% and H1FY2022 growth at 3x compared to H1FY2020. The company is also exploring new routes to market with on-the go, direct marketing, QSR and strategic partnerships.

Branded packaged Foods - Strong foundation for rapid & sustainable growth; both in scale & profitability

ITC foods business is one of India's largest and fastest-growing businesses with net revenue having growing by 4.2x in the last 10 years and reporting 16% CAGR over the same period. ITC is present in 20 food categories with four ITC food brands (Aashirvaad, Sunfeast, Bingo, Yippee) among the top 20 trusted food brands in India. ITC food brands are available in over 56 lakh (>50%) stores across the country with one in two Indian households using the company's products. Aashirvaad Atta which is the No. 1 branded Atta in the country grew by 5.1x and reported 18% CAGR over FY2011-21 which is 2.1x of branded Atta. Aashirvaad has been the market leader for 15 consecutive years and is among the top 50 most trusted brands in India. The category has benefited from the shift from loose to packaged, and unbranded to branded products. Atta is still only 15% branded providing huge opportunity for growth. ITC's communication for Aashirvaad Atta is different in North and South with North requiring conversion of wheat and loose atta buyers while south requiring increase in usage occasions. Sunfeast which is No. 1 in the Cream Biscuits segment grew by 4.4x and reported 16% CAGR over FY2011-21 and has 26% share of premium biscuits segment. Bingo! which is No. 1 in Bridges segment of Snack Foods (No.2 overall in Snacks & Potato Chips) grew by 9.1x and reported 25% CAGR over FY2011-21. Yippee noodles which is India's second-largest instant noodles brand grew by 34.2x and reported 42% CAGR over FY2011-21 which is 5.3x of its leading peer. Yippee noodles has leadership position in Andhra Pradesh, Odisha and Kerala. ITC is expanding its global footprint with 2x growth in export revenue since FY2018 and addition of eight countries in FY2021 (total reach in 58 countries). ITC with its deep understanding of regional tastes and preferences has created region specific products with the help of region specific procurement and region specific blend. In its staples portfolio, it has developed different blends for different regions/recipes for Atta and spices based on consumer preferences. It leverages its cross category competencies and synergises its institutional strengths to deliver efficiency. With branded packaged F&B share currently at 15%, there is huge headroom for growth in the segment driven by consumers seeking safe and trusted products, rising disposable income, growth of e-commerce and D2C, attractive PLI in the foods sector coupled with very low per capita expenditure vs other countries.

ITC's strategy for growth involves consumer centric innovation, strengthening the core and premiumisation. ITC's innovations are based on consumer insights with data from multiple sources which helps the company in addressing the consumer needs. The company brings in new brand experiences by delighting customers with first to market products (Dark Fantasy: Chocolate filled cookies, Bingo! Mad Angles: Unique to market triangles; Sunbean: Beaten Caffe, Squeeze-It bottle for Ghee) while catering to long-term consumer trends of health (Aashirvaad Salt Proactive: Better Heart health; B Natural: Immunity Focus) and indulgence (Sunfeast Dark Fantasy: Premium chocolate biscuit experience; Fabelle: Premium chocolate bar experience) by offering convenience and accessibility via multiple touchpoints (Partnering with airlines, Amway, Inox & Dominos; Available through vending machines & Swiggy, Home Carts for Frozen). To strengthen its core, the company aims to address the key consumer needs by launching new ranges (expanding into categories of Salt, Spices, breakfast solutions) / value added products within existing ranges (Atta with Multigrains: High fibre atta for better digestion); by leveraging power brands to adjacent categories (product portfolio expansion in Dairy – Dahi, Lassi, Panner, Mishti Doi); by addressing emerging consumption moments (B Natural: Harnessing goodness of fruit & fibre) and by extending into newer/alternate channels (Institutional Partnership, modern trade & e-commerce). ITC aims to drive profitability through smart manufacturing (Integrated Consumer Manufacturing & Logistics Facilities (ICML) across 9 food categories); agile cost management (increased manpower productivity by 1.4x versus FY2019, improved energy efficiency by 1.2x versus FY2019); mix premiumisation; value accretive acquisition (Acquired Sunrise - No.1 brand in WB in spices – which offers great range of blends with high quality differentiated & regional products and healthy profitability & return).

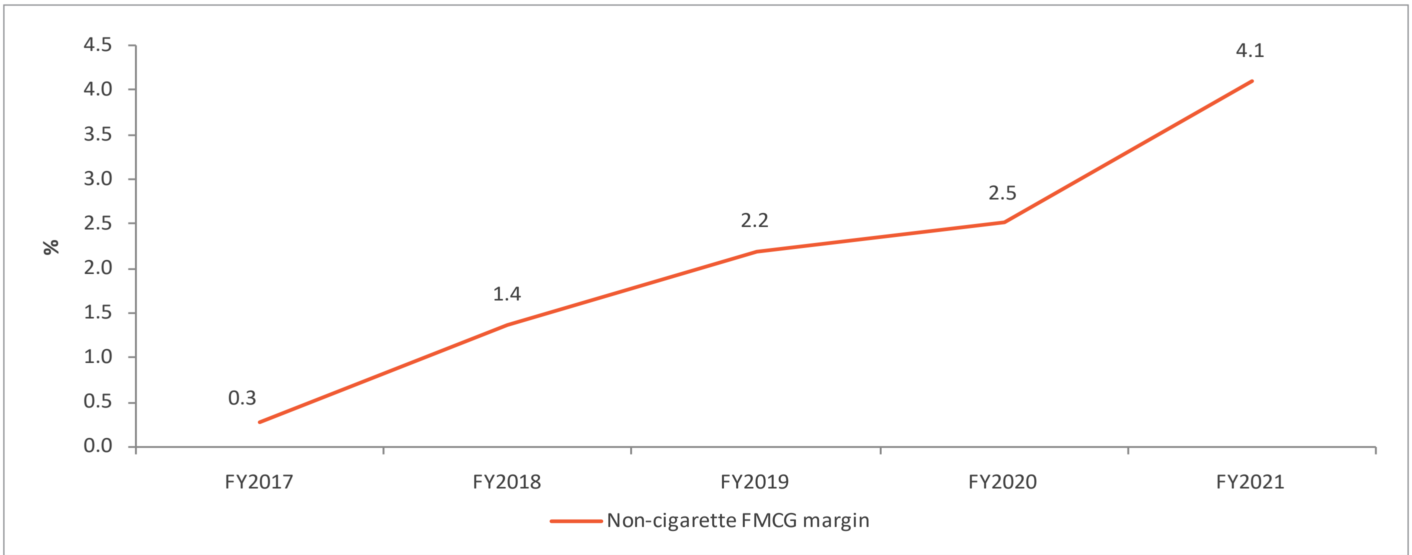
Personal care products - Well positioned to seize emerging opportunities: Drive scale and Profitability

ITC's personal care products business which comprises of four segments – Personal wash, health & hygiene, fragrances and home care – grew at 19% CAGR over FY2017-21. Strategic levers of the personal care business include building power brands with purpose, first in category innovations, drive growth in focus category and value accretive acquisitions. ITC's Savlon brand is promoted with the proposition of building a healthier India, Vivel for empowerment by breaking stereotypes and promoting gender equality. The company has leadership positions in many upcoming categories including No. 2 position in deodorants (12% penetration), No. 2 position in bodywash (3% penetration), No. 1 position in disinfectant spray (2% penetration). First in category innovation by ITC include Engage: pocket fragrance, Savlon: clothes disinfectant spray, Fiama: gel bathing bars. ITC aims to drive growth in focus category by innovating to upgrade from soaps to liquids through market development (Building category relevance) and price democratization (Price per wash similar to soap). ITCs value accretive acquisitions in the personal care business include Savlon and Nimyle. Both the brands have reported strong growth since acquisition with Savlon having grown by 14x since 2015 and Nimyle having grown by 5x since 2018.

Non-FMCG margins expanded by 590 bps over FY2018-FY2021; Scope for further margin expansion

Non-cigarette FMCG business' OPM expanded by 590 bps to 8.9% over the past four years. The company is focusing on scaling in contribution of high-margin products, premiumisation through new launches, and supply and operational efficiencies to improve business margins ahead. Categories such as Bingo, Noodles, and Biscuits have higher margins compared to categories such as Atta in foods. Further, through inorganic initiatives, the company added margin-accretive brands such as Sunrise, B-Naturals, and Savlon in its portfolio, which have strong growth prospects in the medium to long term. Focus would be increasing the presence of these brands in key markets, leveraging on its strong distribution reach. Further, the company is focusing on distribution and supply chain efficiencies such as reducing distance-to-market, direct shipments by eliminating multiple handlings, smart buying through real-time price discovery, and packaging innovations to add-on incrementally to margins in the near to medium term. Thus, we expect FMCG margins to further scale-up by 300-400 bps in 3-4 years. Any significant increase in raw-material prices or slowdown in the high-margin category's growth would act as key risk to margin expansion.

Significant margin expansion of non-cigarette FMCG business



Source: Company; Sharekhan Research

ITC Infotech - Delivering Business-friendly Solutions

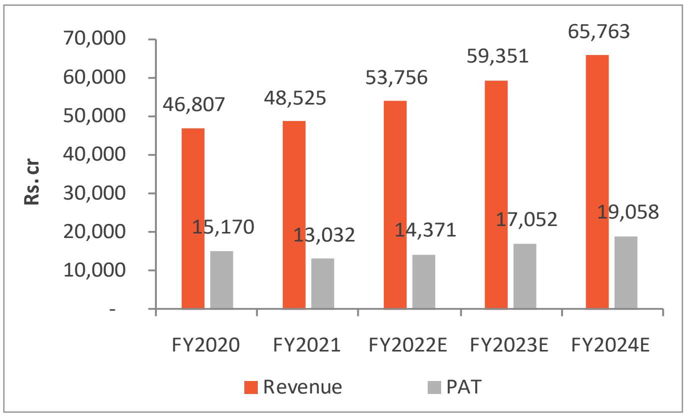
ITC Infotech, a wholly-owned subsidiary of ITC Limited, is a leading global technology services and solutions provider delivering business friendly solutions to clients across 29 countries, including 60+ Fortune listed clients. It serves industries such as Banking, Financial Services, Consumer Packaged Goods, Manufacturing, Travel, Hospitality and Healthcare. The company's strategic pillars include customer-centricity, employee centricity and operational excellence. ITC Infotech's revenue has grown from Rs. 2,007 crore in FY2019 to Rs. 2,454 crore in FY2021 reporting a CAGR of 10.6%. The company's EBITDA margin has expanded from 8% in FY2019 to 25.2% in FY2021. The company is scouting for inorganic initiatives for fast scale-up of Infotech business in the medium term. The company is likely to unlock value for the shareholder by listing the Infotech business. However, the timeline for same has not been disclosed by the company.

Sustainability initiatives

ITC with its robust sustainability strategies in place is the only company in the world to be carbon positive for 16 years, water positive for 19 years and solid waste recycling positive for 14 years. ITC currently supports sustainable livelihoods for six million people with an aim to support 10 million livelihoods in the future. ITC's initiatives in agriculture include e-Choupal: Empowering four million farmers and Baareh Mahine Hariyali: Leveraging technology & innovation to enhance productivity & incomes. At present, 41.3% of ITC's total energy comes from renewable sources which the company aims to increase to 50% in the coming period. Thirty three buildings of the company have achieved Platinum certification from USGBC-LEED/IGBC. With respect to biodiversity conservation, the company has undertaken green cover improvement by up to 110%, tree species by 150% and bird species by 225%. Towards a circular economy, the company has reduced waste to landfill from 80% to 20% and introduced a green temple programme, which is adopted in 226 temples. ITC has achieved top notch ESG credentials including AA rating by MSCI-ESG every year since 2018, inclusion in the Dow Jones Sustainability Emerging Markets Index, rated at the 'Leadership Level' by CDP with scores of 'A-' for both climate change and water security.

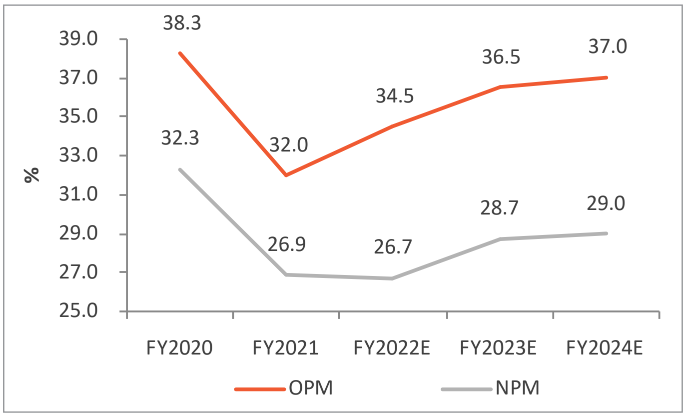
Financials in charts

Revenue and PAT to grow steadily



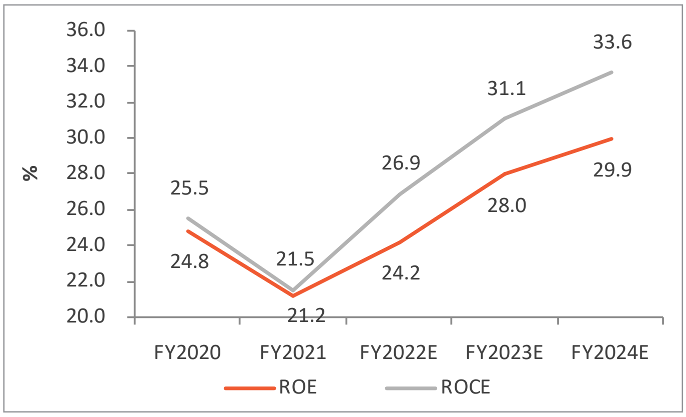
Source: Company, Sharekhan Research

Margins to rise from current level



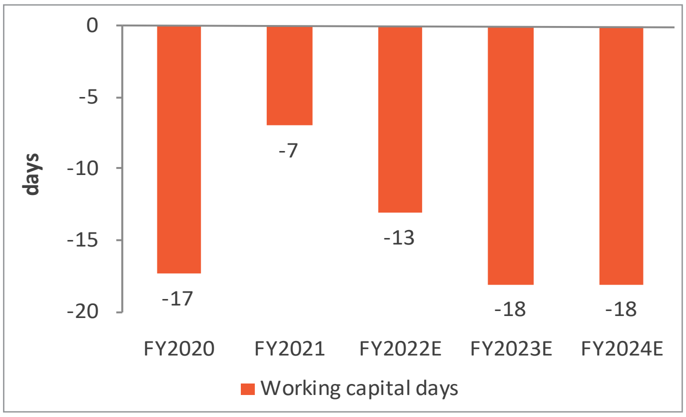
Source: Company, Sharekhan Research

Return ratios to improve significantly



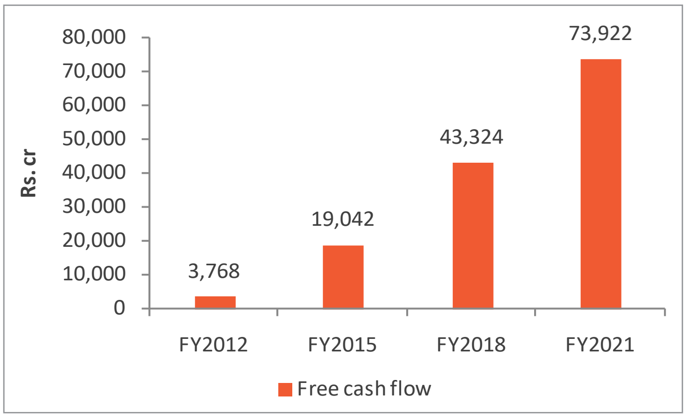
Source: Company, Sharekhan Research

Working capital days to reduce



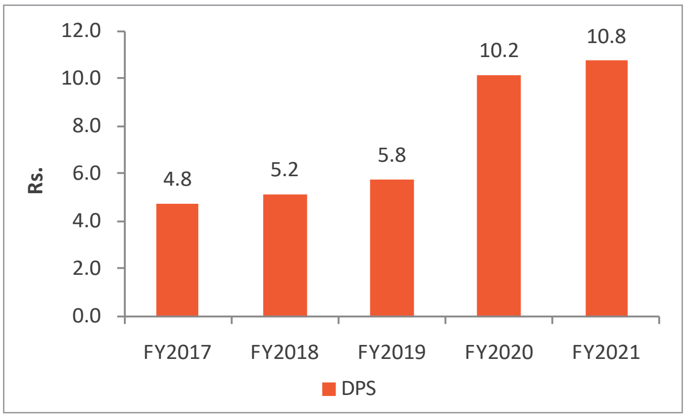
Source: Company, Sharekhan Research

Trend of free cash flow generation



Source: Company, Sharekhan Research

Dividend per share increasing over the years



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Cigarette remains a regulatory risk, FMCG long's-term growth prospects intact

The domestic cigarettes industry is affected by a sustained increase in taxes and regulatory regime along with a sharp increase in illegal trade in recent years, especially at the premium end, which continue to pose significant challenges to the legal cigarette industry in the country. Though cigarette was skipped from increased taxes in Union Budget, there is sustained risk of regulatory hurdles implemented to curb tobacco products consumption. On the other hand, outlook for the FMCG industry in India is positive as lower capita consumption, emergence of new categories, and improving demographics provide enough scope for FCMG companies to achieve sustainable revenue growth in the medium to long run.

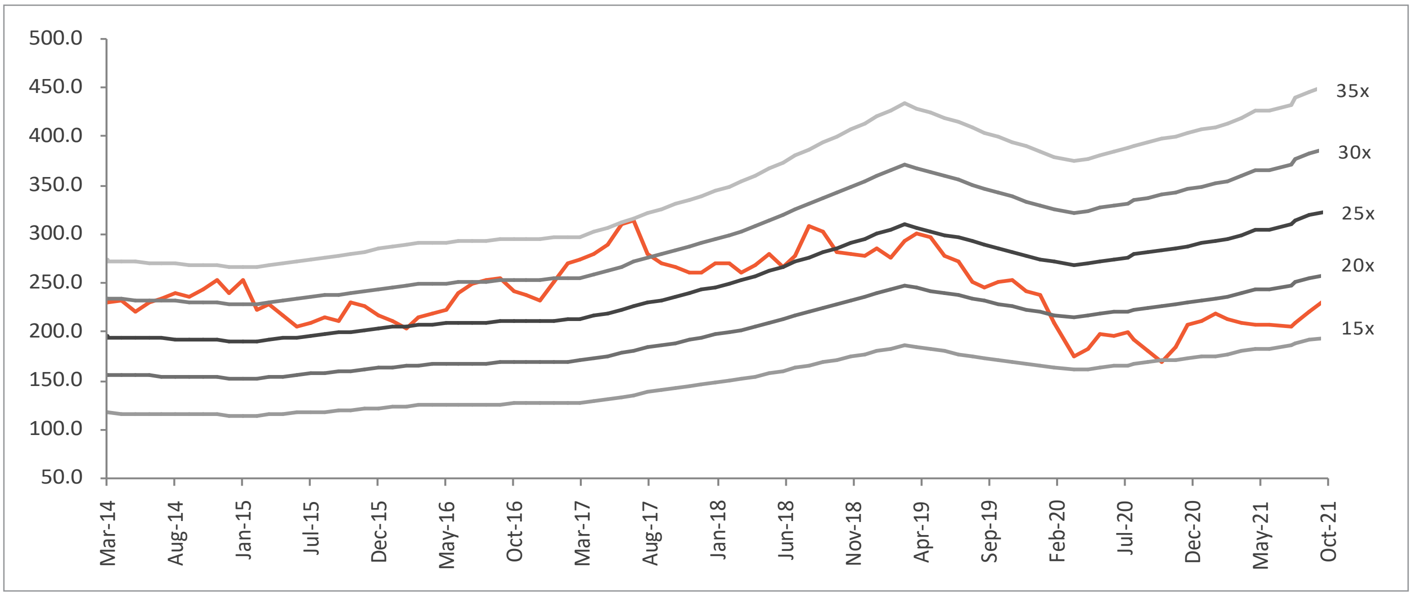
■ Company outlook - Cigarette business to regain normalcy; FMCG margins to scale up

Q1FY2022 performance was strong because of low base. Cigarette business sales volume improved from mid-week of June 2021 with most regaining normalcy (except for Kerala, Odisha, and North East). We expect cigarette sales volume to sequentially improve with easing of restrictions and no price hikes expected in the immediate term due to no hike in tax rate of cigarettes in Union Budget. Resilient demand in the domestic market, scale-up in sales of new product launches, and improved penetration would help non-FMCG business revenue to grow in double digits in the coming quarters. Business margin expansion would sustain, with scale-up in revenue of products/categories and better revenue mix.

■ Valuation - Retain Buy with an unchanged PT of Rs. 280:

ITC's management has enhanced focus and redefined growth strategies for all its business verticals to improve its growth prospects in medium to long term. The company has sustained ESG rating of AA by MSCI-ECG highest amongst global tobacco companies. The management is committed towards restructuring of hotel business post overall recovery in the hotel industry, while it will evaluate unlocking value in the Infotech business once it attains certain scale. However, there is no stated time-line for restructuring programme. The stock is currently trading at 16.3x and 14.6x its FY2023E and FY2024E EPS, which is at stark discount to some of the large consumer goods stock. We maintain our Buy recommendation on the stock with an unchanged price target of Rs. 280.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Company	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Hindustan Unilever	66.9	59.3	48.3	47.6	42.0	34.8	36.5	25.2	31.1
ITC	21.4	19.4	16.3	16.5	13.6	11.6	21.5	26.9	31.1

Source: Company, Sharekhan estimates

About company

ITC is one of the largest diversified players in India present in businesses such as cigarettes, FMCG, hotels, and paper. The company is the market leader in the domestic cigarette and PPP segments. The company is also the second-largest hotel chain by revenue and profitability, with a strong room inventory. The company has a strong distribution reach of more than 2 million, which it is utilising to scale-up its consumer goods business and de-risk its business model. ITC's revenue and PAT grew by 3.0x and 3.8x, respectively, over FY2009-FY2020.

Investment theme

ITC is focusing on de-risking its business model by reducing dependence on its core cigarette business (affected by regulatory and tax hurdles for the past few years) by scaling up the fast-growing consumer goods and hotel businesses. The company has quickly rebound from disruption caused by the lockdown and key businesses are operating at normal levels. Though FY2021/FY2022 is expected to be impacted by supply disruption; strong recovery is anticipated in FY2023. Further, scale up in the performance of the non-cigarette FMCG business and margin improvement would be triggers for the stock in the medium to long term. Moreover, strong cash flows and cheery dividend payout make it a good bet in the current uncertain environment.

Key Risks

- Significant rise in taxes on cigarettes or government actions to curb tobacco and tobacco consumption would act as a key risk to the cigarette business.
- Sustained consumption slowdown would affect the growth rate of categories such as consumer goods and hotels in the near term.

Additional Data

Key management personnel

Sanjiv Puri	Chairman and Managing Director
Supratim Dutta	Executive Director and Chief Financial Officer
Nakul Anand	Executive Director
Sumant Bhargavan	Executive Director
Rajiv Tandon	Executive Director
Rajendra Kumar Singhi	Executive Vice President & Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	British American Tobacco PLC	29.4
2	Life Insurance Corp of India	16.2
3	Unit Trust of India	7.9
4	SBI Funds Management Pvt. Ltd.	2.82
5	Capital Group Companies	2.47
6	QIB Insurance Company	2.36
7	ICICI Prudential Asset Management	2.05
8	General Insurance Corp. of India	1.76
9	HDFC Asset Management Co. Ltd.	1.68
10	New India Assurance Co. Ltd.	1.49

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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