Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Jyothy Labs Ltd

Falling crude prices augurs well for margins

Consumer Goods	Sharekhan code: JYOTHYLAB
Reco/View: Buy ↔	CMP: Rs. 186
Price Target: Rs. 240 ↔	

↑ 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		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 31.95

Updated Feb 08, 2023

High Risk

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

Source: Morningstar

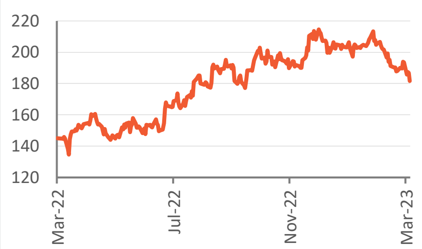
Company details

Market cap:	Rs. 6,819 cr
52-week high/low:	Rs. 223 / 134
NSE volume: (No of shares)	4.2 lakh
BSE code:	532926
NSE code:	JYOTHYLAB
Free float: (No of shares)	13.6 cr

Shareholding (%)

Promoters	62.9
FII	13.7
DII	17.1
Others	6.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-8.4	-10.4	2.2	27.9
Relative to Sensex	-3.0	-4.9	3.6	27.7

Sharekhan Research, Bloomberg

Summary

- We maintain our Buy recommendation on Jyothy Labs (JLL) with a PT of Rs. 240. The stock has corrected by 18% from its recent high and is trading at an attractive valuation of 22x/18x its FY2023E/24E earnings.
- Recent fall in crude prices augurs well for JLL from a profitability perspective as we expect gross margins to improve in the quarters ahead. Management expects margins to reach 15% over the next two years.
- With the expected harsh summer season, mosquito infestation might increase which will help recovery in JLL's household insecticide business. It will lead to an overall good recovery in volume growth.
- JLL remains one of the preferred picks in small to mid-cap FMCG space in view of its steady operating performance in a tough demand environment, good future growth prospects and discounted valuations to some of its close peers.

Jyothy Labs (JLL) has been a consistent performer in the consumer goods pack with double-digit revenue growth for eight consecutive quarters and sequential improvement in the OPM for past two quarters. Against the backdrop of a slowing demand environment, the company posted double-digit growth in categories such as fabric wash and dish wash led by market share gains. The company is in a relatively comfortable position as falling crude prices augurs well from a margin perspective while extreme summers might help in recovery in the sales of the household insecticide (HI) category in the coming quarters. The stock has corrected from its recent high providing a good opportunity to enter the good stock in the small-to-mid-cap FMCG space, which provides good earning visibility in the medium term.

- **OPM to recover to 15% by FY2025; falling crude prices will provide support to margins:** JLL's OPM reached 16%+ in FY2021 on the back of a decline in input prices and a better mix. However, the margins witnessed a drop from Q1FY2022 with OPM standing in the range of 10-12% due spike in the crude and other input cost along with rising freight cost. With crude prices witnessing some correction since Q2FY2023, the OPM sequentially improved to 13.8% in Q3. With the recent correction in the crude prices, OPM will further improve in the quarters ahead. We expect OPM to recover to 15%+ in FY2025.
- **Extreme summers might lift HI sales:** JLL's HI category saw a sharp decline of 30%+ in the revenues for 9MFY2023 as abnormal weather conditions affected the sales during the season and demand slowdown impacted performance during the off-season. The expectation of extreme summers might lead to high mosquito infestation resulting in higher demand for mosquito repellants in the coming quarters. Thus, after year of lull, we should expect a recovery in the sales of HI products in the coming quarters. This will also be supported by the deepening of penetration and high media spends in the near term. If HI sales recover, it will provide some boost to the sales volume of the company in FY2024.
- **New product launches and distribution expansion will support the overall growth:** A large focus remains on expanding the distribution of key brands in newer markets, improving the saliency of liquids in the HI category, and improving traction for lower unit packs in the dishwashing category to deliver consistent growth in the long run. The company currently sells its products through one million direct outlets and three million indirect outlets. It targets a consistent increase in the distribution reach in the coming years. Further, the company is planning to launch new products and take some of its recent launches to new markets in the coming years.

Our Call

View: Maintain Buy with an unchanged PT of Rs. 240: JLL posted relatively better broad-based performance in the past few quarters despite input price inflation and a slowdown in volume growth (especially in rural India). Product innovation and availability of relevant product assortment for general trade/e-commerce/modern trade and distribution expansion will help JLL to continue to gain market share in key categories. JLL's stock price has corrected by 18% in the recent past and is currently trading at discounted valuations of 22x/18x its FY2024E/FY2025E earnings compared to some of the large peers. Improving cash flows, focus on achieving double-digit volume growth, and attractive valuations make it a good mid-cap pick in the consumer goods space. We maintain our Buy recommendation on the stock with an unchanged price target (PT) of Rs. 240 over the next 12 months.

Key Risks

Any late recovery in the HI category or market share loss in some of the key categories would act as a key risk to our earnings estimates.

Valuation (Consolidated) Rs cr

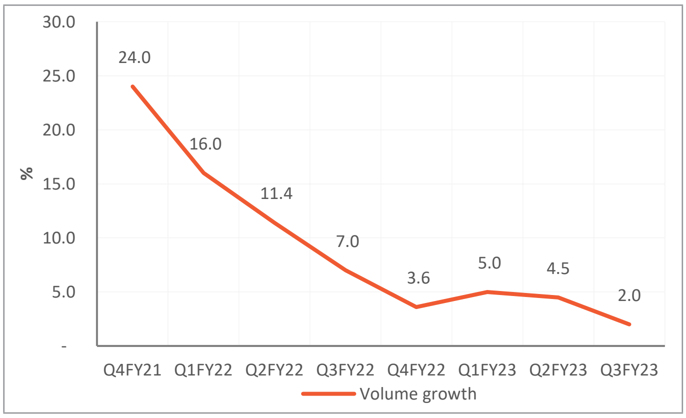
Particulars	FY21	FY22	FY23E	FY24E	FY25E
Revenues	1,909	2,196	2,472	2,821	3,233
OPM (%)	16.5	11.3	13.1	14.9	15.5
Adjusted PAT	208	159	226	307	372
% YoY growth	30.5	-23.5	42.0	36.1	21.0
Adjusted EPS (Rs.)	5.7	4.3	6.2	8.4	10.1
P/E (x)	32.8	42.9	30.2	22.2	18.4
P/B (x)	4.8	4.7	4.7	4.3	3.9
EV/EBIDTA (x)	21.7	27.2	21.1	16.1	13.2
RoNW (%)	15.7	11.1	15.5	20.2	22.4
RoCE (%)	14.2	10.7	14.6	18.5	20.6

Source: Company; Sharekhan estimates

Volume growth might recover in FY2024

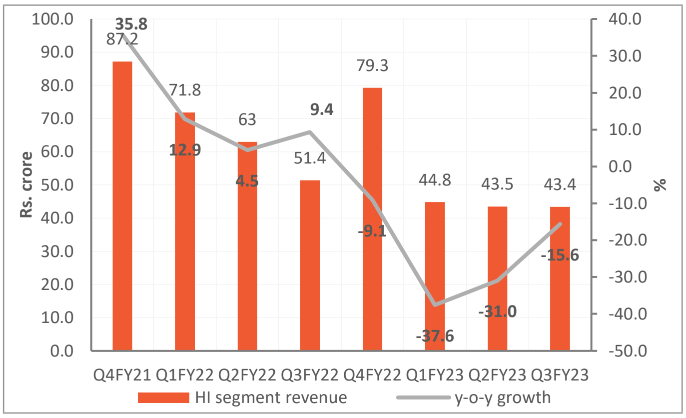
JLL registered revenue growth of 19% (ex-HI) with volume growth standing at mid-single digit. JLL's HI category saw a sharp decline of 30%+ in the revenues for 9MFY2023 as abnormal weather conditions affected the sales during the season and demand slowdown impacted performance during the off-season. The expectation of extreme summers might lead to high mosquito infestation resulting in higher demand for mosquito repellants in the coming quarters. Thus, recovery in the HI category would help in the overall improvement in the volume growth in the coming quarters. Management is quite confident of achieving volume-led revenue growth in FY2024.

Trend in quarterly volume growth



Source: Company, Sharekhan Research

HI category quarterly trend in revenue and y-o-y growth

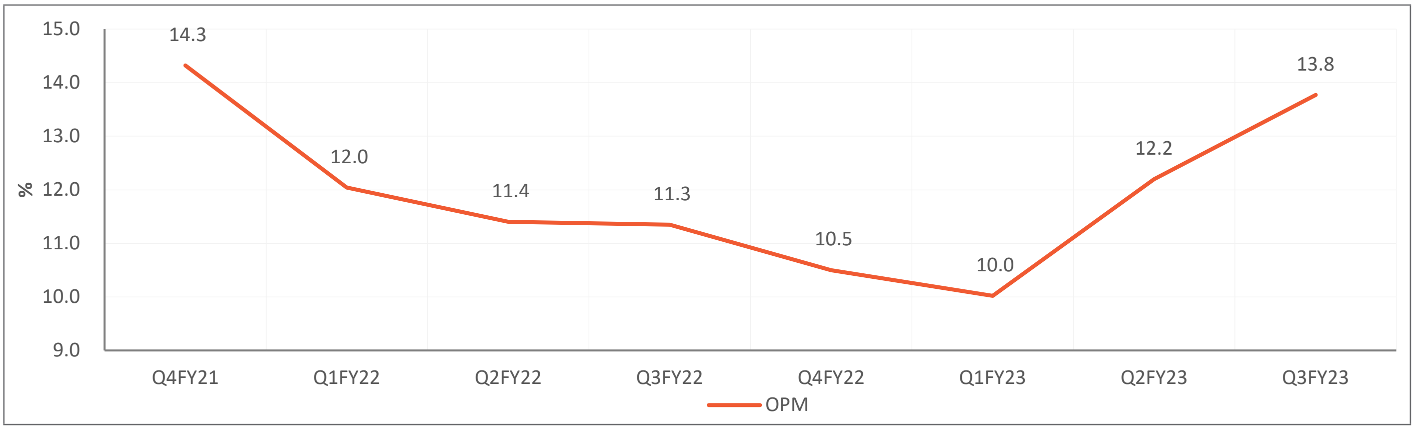


Source: Company, Sharekhan Research

OPM to recover to 15% by FY2025; falling crude prices will provide support to margins

JLL's OPM reached 16%+ in FY2021 on the back of a decline in input prices and a better mix. However, the margins witnessed a drop from Q1FY2022 with OPM standing in the range of 10-12% due spike in the crude and other input cost along with the freight cost. With crude prices witnessing some correction since Q2FY2023, the OPM sequentially improved to 13.8% in Q3. OPM is likely to further improve in the quarters ahead aided by recent correction in crude prices. We expect OPM to recover to 15%+ in FY2025.

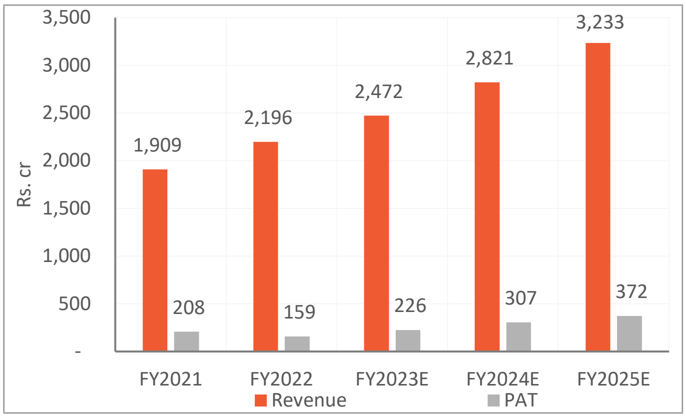
Quarterly trend in OPM



Source: Sharekhan Research

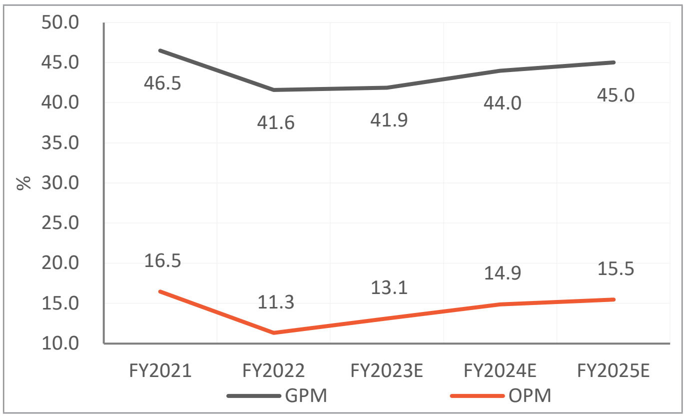
Financials in charts

Steady growth in revenue and PAT



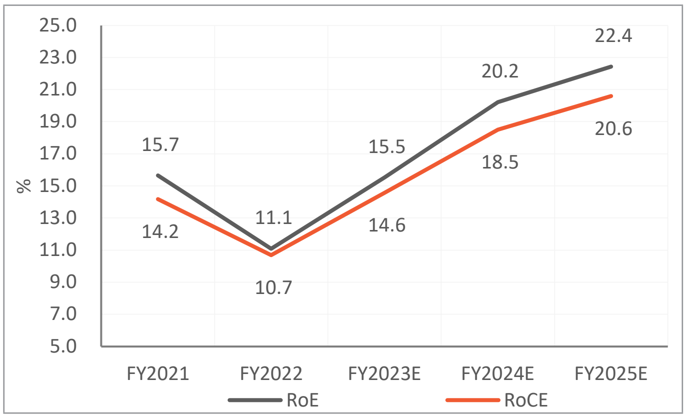
Source: Company, Sharekhan Research

Margins to improve from current level



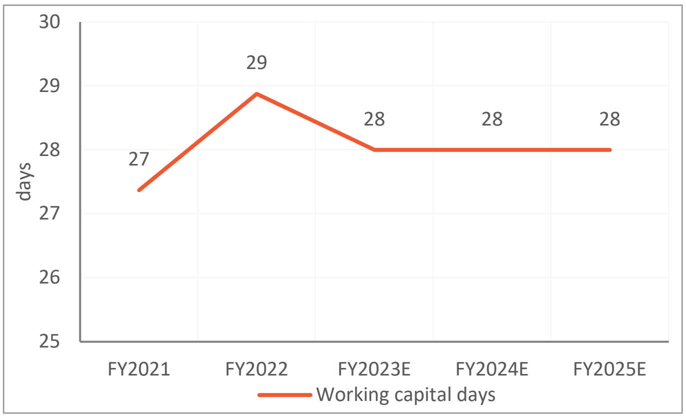
Source: Company, Sharekhan Research

Return ratios to rise sharply



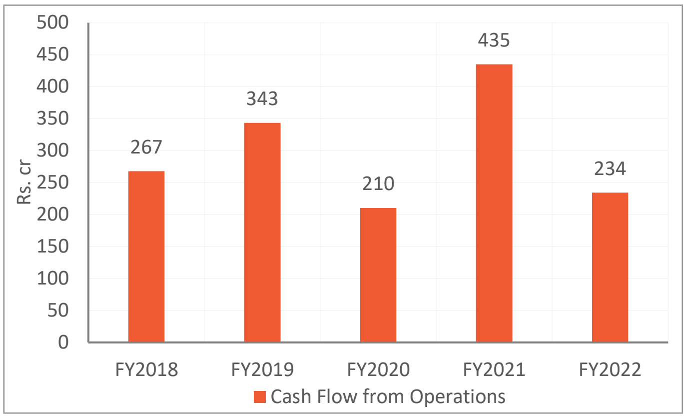
Source: Company, Sharekhan Research

Stable working capital days



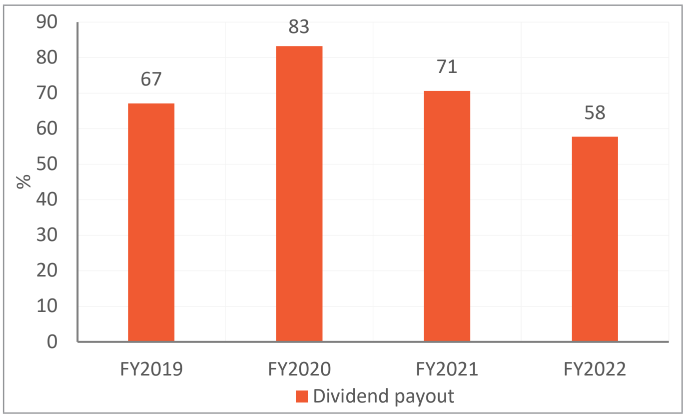
Source: Company, Sharekhan Research

Trend in operating cash flow generation



Source: Company, Sharekhan Research

Consistent dividend payout



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Rural recovery key for better growth ahead

A recovery in rural demand is key for consumer goods companies to post recovery in volume growth in the quarters ahead. Urban demand remained resilient with a good pick-up in modern trade, while the momentum in general trade continues to remain strong for the past 2-3 quarters. Out-of-home, packaged foods and edible oil categories witnessed good growth in recent times and will maintain momentum in the coming quarters. With the mercury rising in most parts of the country, demand for summer products is on the rise as trade channels are building up the inventory prior to the season. On the other hand, stable raw-material prices post the recent correction in some of the key inputs (including crude oil and vegetable oils) will help margins to consistently improve in the coming quarters. Overall, we expect Q4FY2023 to be better compared to Q3 and the momentum to improve at the start of the next fiscal.

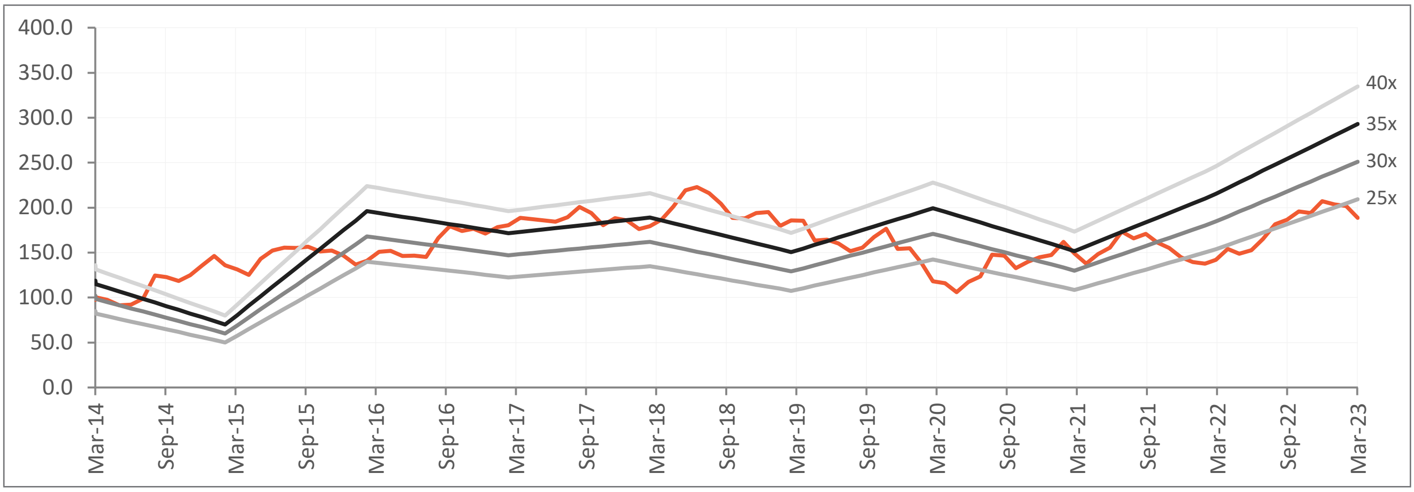
■ Company Outlook – Focus remains on achieving double-digit revenue growth

JLL posted resilient performance in 9MFY2023 with revenue growth in double digits and volume growth standing at a low single digit. The company is focusing on achieving volume-led, double-digit revenue growth in the medium to long term through driving category development, increased brand-building initiatives, digital technology driving sales efficiency in go-to-market initiatives, market share gains, distribution expansion, and improving penetration for key categories in rural and urban markets. With recent correction in key input prices, the company expects OPM to reach historical levels of 14-15% by the end of FY2023.

■ Valuation – Maintain Buy with an unchanged PT of Rs. 240

JLL posted relatively better broad-based performance in the past few quarters despite input price inflation and a slowdown in volume growth (especially in rural India). Product innovation and availability of relevant product assortment for general trade/e-commerce/modern trade and distribution expansion will help JLL to continue to gain market share in key categories. JLL's stock price has corrected by 18% in the recent past and is currently trading at discounted valuations of 22x/18x its FY2024E/FY2025E earnings compared to some of the large peers. Improving cash flows, focus on achieving double-digit volume growth, and attractive valuations make it a good mid-cap pick in the consumer goods space. We maintain our Buy recommendation on the stock with an unchanged price target (PT) of Rs. 240 over the next 12 months.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Godrej Consumer Products	54.0	53.9	42.8	39.5	39.9	32.1	17.3	16.0	18.7
HUL	65.0	60.2	50.8	45.5	42.0	35.7	24.1	25.9	30.1
Jyothy Labs	42.9	30.2	22.2	27.2	21.1	16.1	10.7	14.6	18.5

Source: Company, Sharekhan estimates

About company

JLL has evolved from being a promoter-driven, south-centric, single-product company to a professionally managed, multi-brand, multi-product company with pan-India operations and a turnover of over Rs. 2,000 crores. JLL is present in key categories such as fabric care, dish wash, HI, and personal care products. JLL's power brands include *Ujala, Henko, Exo, Maxo, Margo,* and *Pril*. The company's flagship brand, *Ujala* has remained at the top of the fabric whitener category since its launch, with an ~80% market share.

Investment theme

JLL has a leadership position in the fabric whitener category in India, whereas it ranks number two in the dish wash bar, liquid, and mosquito repellent coil categories. Going forward, long-term strategies undertaken to enhance growth include winning through innovations in the fabric wash category, leveraging rural penetration in the dish wash category, increasing footprint, and relevant extensions in the HI and personal care categories. A large presence in the essential and hygiene category will help JLL drive near-term growth in the pandemic situation. A resurgence in the HI category will help drive growth in the medium term.

Key Risks

- **Slowdown in demand:** A sustained slowdown in the HI category's growth would affect demand.
- **Higher input prices:** Sharp rise in key raw-material prices such as Brent crude oil would affect profitability and earnings growth.
- **Increased competition in highly penetrated categories:** Increased competition in highly penetrated categories such as fabric whiteners would threaten revenue growth.

Additional Data

Key management personnel

Ramakrishnan Lakshminarayanan	Chairman
Jyothy Ramachandran	Managing Director
Sanjay Agarwal	Chief Financial Officer
Shreyas Trivedi	Company Secretary

Source: Company Website

Top 9 shareholders

Sr. No.	Holder Name	Holding (%)
1	Franklin Resources	6.43
2	Nalanda India Equity Fund	6.02
3	ICICI Prudential AMC	3.84
4	Nippon Life India AMC	3.17
5	ICICI Lombard General Insurance Co Ltd	1.68
6	Pari Washington Company Pvt Ltd	1.67
7	abrdn plc	0.79
8	BlackRock Inc	0.60
9	Dimensional Fund Advisors	0.50

Source: Bloomberg (Old data)

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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Compliance Officer: Ms. Binkle Oza; Tel: 022-61169602; email id: complianceofficer@sharekhan.com;

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