

Better execution yields better Q1FY24 results; maintain BUY

Consumer Goods ▶ Result Update ▶ August 15, 2023

TARGET PRICE (Rs): 535

We hold a positive stance on ITC, heartened by its improved management execution, ahead-of-time investment in businesses, and leadership position in most segments. Overall revenue fell 8% in Q1, while growing 11% adjusted for Agri revenue; Cigarettes net sales grew 11% (volume growth estimate: ~8%) and Other FMCG sales growth was a healthy 16%. Cigarettes EBIT grew 11% YoY (as it navigates margin pressure well), with EBIT margin at 74.2%, up by ~20bps YoY. Other FMCG EBITDA margin stands at 11%, up by 375bps YoY (PLI benefit: 30-40bps). We see double-digit EBIT growth for Cigarettes and healthy EBITDA expansion for the Other FMCG segment, going forward. We uprear our earnings estimates for Cigarettes by 3%, on better pricing power/margins; this hoists our SOTP-based Jun-24E TP to Rs535/share (vs Rs525 earlier).

ITC: Financial Snapshot (Consolidated)

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Revenue	5,63,413	6,60,023	7,28,852	7,98,339	8,77,309
EBITDA	1,89,337	2,39,035	2,62,503	2,97,773	3,26,741
Adj. PAT	1,50,578	1,86,394	2,03,546	2,26,211	2,51,063
Adj. EPS (Rs)	12.2	15.0	16.3	18.0	19.9
EBITDA margin (%)	33.6	36.2	36.0	37.3	37.2
EBITDA growth (%)	22.0	26.2	9.8	13.4	9.7
Adj. EPS growth (%)	15.4	22.7	8.6	10.6	10.4
RoE (%)	25.3	29.2	30.2	32.1	32.9
RoIC (%)	47.7	56.5	58.5	63.3	65.6
P/E (x)	36.8	30.0	27.6	24.9	22.6
EV/EBITDA (x)	27.7	21.9	20.1	17.7	16.1
P/B (x)	9.1	8.3	8.3	7.7	7.1
FCFF yield (%)	2.5	3.0	3.1	3.5	3.8

Source: Company, Emkay Research

Cigarettes volume likely grew ~8%; EBIT growth sustained double-digit level

ITC's cigarettes gross sales grew 13% YoY, while net sales growth stood at 10.9%. We now estimate cigarettes vol. growth at ~8% YoY (marginally better than our expectation of 7%). The company saw decent performance in differentiated variants launched recently. With the 3% price and mix growth, we see accelerated premiumization in the portfolio. As per our checks, the company now has ~70% share in the capsule segment. Cigarettes EBIT grew 11% YoY, aided by EBIT margin expansion of ~20bps YoY to 74.2%. With high single-digit net sales growth, we see 10% EBIT CAGR over FY23-26E.

Non-Cigarettes performance subdued, on a high Agri base; Paper: weak show

Non-Cigarettes revenue fell 8% YoY, hit by the 27% decline in Agri revenue. Adjusted for Wheat exports in the base, non-Cigarettes revenue grew 17% YoY with 31% growth in Agri. Overall, non-Cigarettes business EBIT grew 15% YoY, aided by 200bps expansion in EBIT margin to 10.2%. Other FMCG business maintained its strong run, with 16% YoY revenue growth. Other FMCG EBITDA grew 64% YoY, with 325bps expansion in segment EBITDA margin to 11% (PLI benefit: 30-40bps). The Paper business put up a muted show, with 6.5% revenue decline (weak demand and low-priced supplies from China) and 23% EBIT decline (EBIT margin down by 475bps YoY to 22.3%). Hotels revenue grew 8% on a high base; EBIT grew 17% with EBIT margin at 22% (+165bps YoY). ITC Infotech revenue grew 12% YoY to Rs8.4bn, with OPM at 13.6% (down 220bps YoY).

Better execution to aid earnings and valuation; maintain BUY

We believe the stock re-rating has been a factor of healthy EBIT growth in Cigarettes and strong recovery in the non-Cigarettes business. On a normalized base, we perceive that better execution would help the company outgrow the industry and drive profitability in its businesses. The Board of Directors has approved the Hotel demerger, with share entitlement ratio of 10:1 for the demerged entity, wherein for every 10 shares of ITC, shareholders will get one share of the new entity. We see this as a positive move for keeping the share price considerable; maintain BUY.

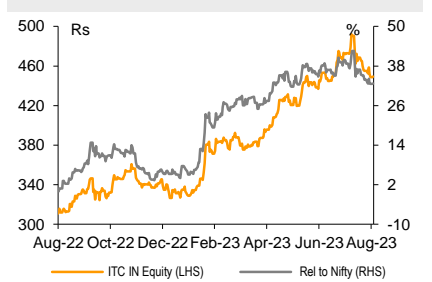
Target Price – 12M	Jun-24
Change in TP (%)	NA
Current Reco.	BUY
Previous Reco.	BUY
Upside/(Downside) (%)	19.1
CMP (14-Aug-23) (Rs)	449.2

Stock Data	Ticker
52-week High (Rs)	500
52-week Low (Rs)	307
Shares outstanding (mn)	12,464.8
Market-cap (Rs bn)	5,599
Market-cap (USD mn)	67,497
Net-debt, FY24E (Rs mn)	0
ADTV-3M (mn shares)	12
ADTV-3M (Rs mn)	5,394.4
ADTV-3M (USD mn)	65.0
Free float (%)	-
Nifty-50	19,435
INR/USD	83.0
Shareholding, Jun-23	
Promoters (%)	-
FPIs/MFs (%)	43.6/41.9

Price Performance

(%)	1M	3M	12M
Absolute	(5.0)	7.5	46.5
Rel. to Nifty	(4.4)	1.3	33.4

1-Year share price trend (Rs)



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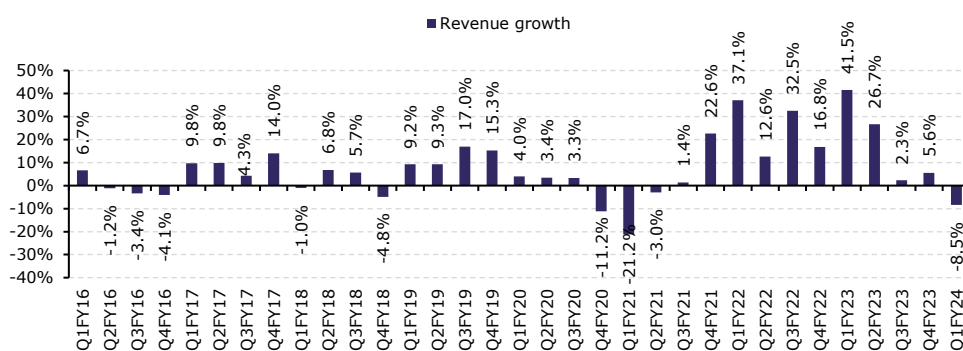
Quarterly performance

Exhibit 1: Assessing ITC's Q1FY24 show

(Rs mn)	1QFY24	1QFY23	YoY (%)	4QFY23	QoQ (%)
Total income	158,282	172,897	(8.5)	163,980	(3.5)
Cost of goods	64,155	84,768	(24.3)	67,941	(5.6)
Employee expenses	9,038	8,621	4.8	8,940	1.1
Other expenses	22,588	23,032	(1.9)	25,005	(9.7)
EBITDA	62,501	56,475	10.7	62,094	0.7
EBITDA margin (%)	39.5	32.7	680bps	37.9	160bps
Depreciation	4,025	4,115	(2.2)	4,219	(4.6)
EBIT	58,476	52,360	11.7	57,875	1.0
EBIT margin (%)	36.9	30.3		35.3	
Interest cost	107	91	17.4	118	(9.4)
Other income	7,087	3,127	126.7	7,463	(5.0)
PBT	65,456	55,396	18.2	65,219	0.4
Tax	16,429	13,702		15,079	8.9
Tax rate (%)	25.1	24.7		22.9	
PAT	49,027	41,694	17.6	50,140	(2.2)
Non-recurring items	0	0		729	
Adj Profit	49,027	41,694	17.6	50,140	(2.2)
Net profit margin (%)	31.0	24.1		30.6	
EPS (Rs)	3.9	3.4	16.6	4.0	(2.3)

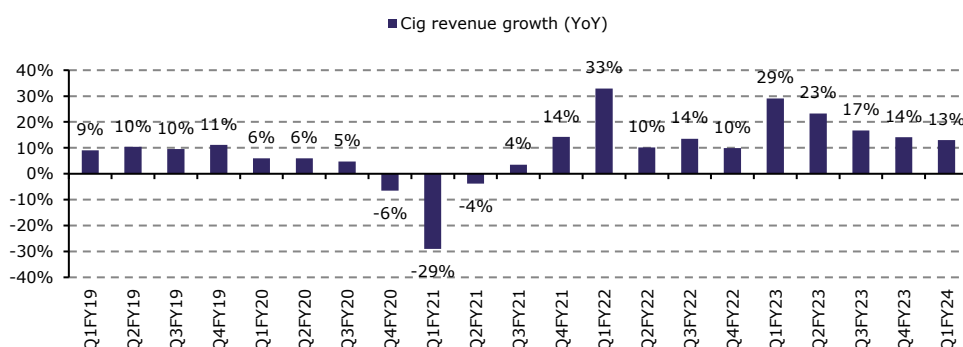
Source: Company, Emkay Research

Exhibit 2: Revenue growth trend



Source: Company, Emkay Research

Exhibit 3: Cigarettes – Revenue growth



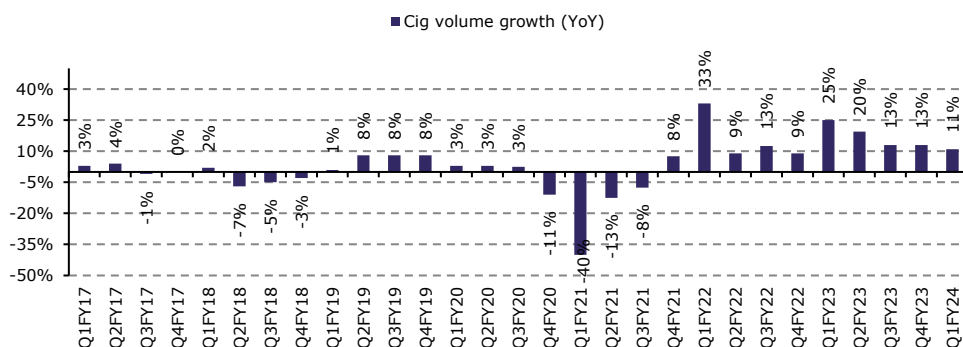
Source: Company, Emkay Research

Exhibit 4: Cigarettes business – Per-stick analysis

(Rs)	1QFY24	1QFY23	YoY
MRP sales	8.23	7.99	3%
Retailers margin	0.75	0.73	3%
Actual price to retailer	7.48	7.26	3%
Distributor margin	0.17	0.16	3%
GST	0.02	0.01	12%
Cess	0.05	0.05	3%
Actual price to distributor	7.25	7.04	3%
GST	0.91	0.87	5%
Cess	3.09	3.07	1%
Gross realization to company	3.25	3.10	5%
Excise duty	0.00	0.00	-1%
NCCD	0.51	0.44	16%
Net realization to company	2.73	2.66	3%
Cost of goods sold	0.26	0.26	0%
Gross profit	2.47	2.40	3%
Overheads	0.44	0.43	3%
Ebit	2.03	1.97	3%
Ebit margin on gross sales	62.4%	63.4%	-101bps
Ebit margin on net sales	74.2%	74.0%	17bps
Excise duty	0.52	0.45	16%
GST	4.06	4.00	2%
Total tax	4.58	4.44	3%

Source: Company, Emkay Research

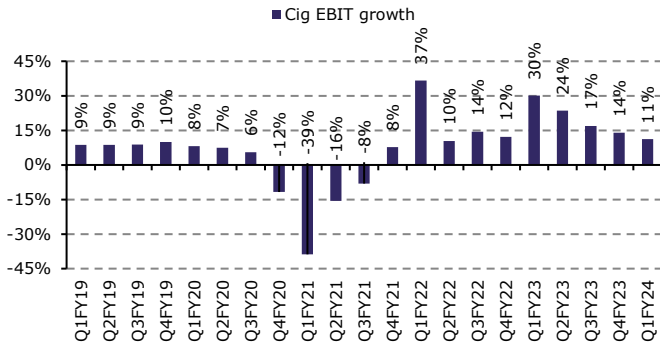
Net sales grew 10.9% with an estimated ~8% volume growth. The company has effected price hike in parts of the portfolio

Exhibit 5: Cigarettes – Volume growth

Source: Company, Emkay Research

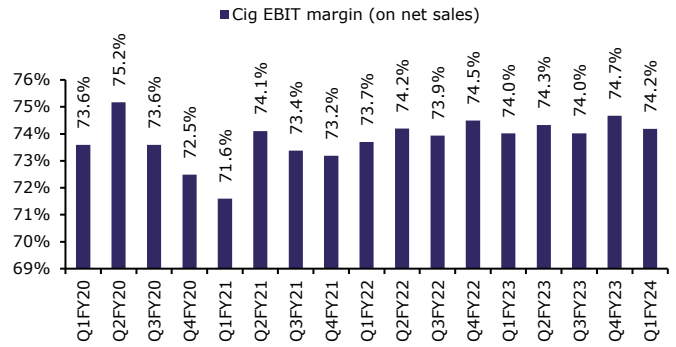
In the Capsule segment, the company has ~70% market share. In overall Cigarettes volume, we estimate capsule contribution to be ~17%

Exhibit 6: Cigarettes – EBIT growth



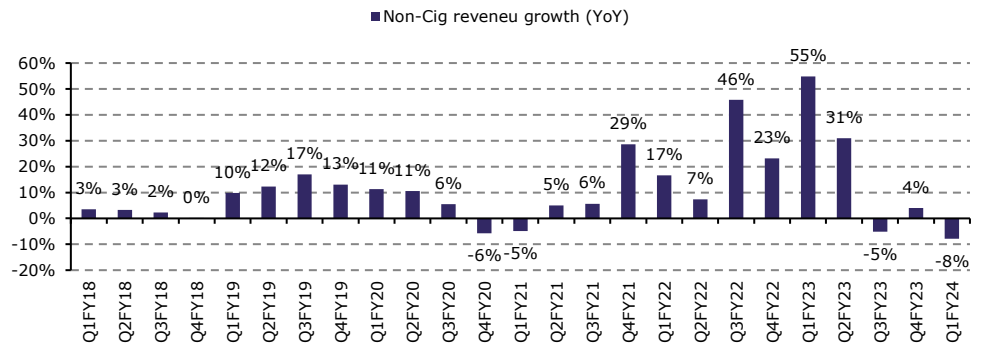
Source: Company, Emkay Research

Exhibit 7: Cigarette – EBIT margin (on net sales)



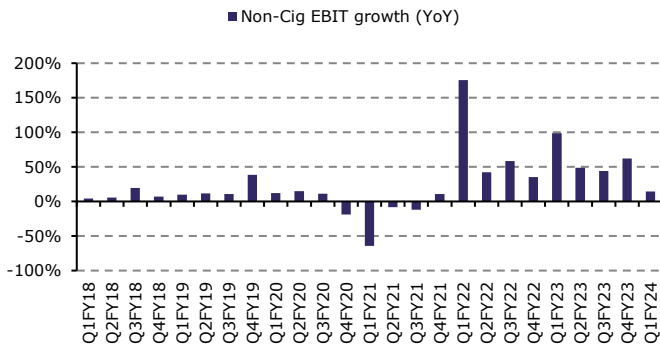
Source: Company, Emkay Research

Exhibit 8: Non-cigarettes business – Revenue growth



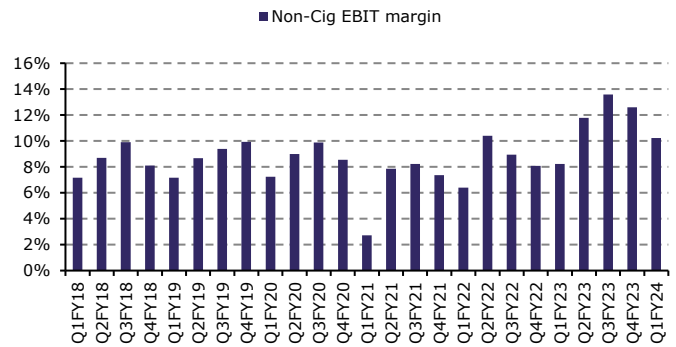
Source: Company, Emkay Research

Exhibit 9: Non-cigarettes – EBIT growth



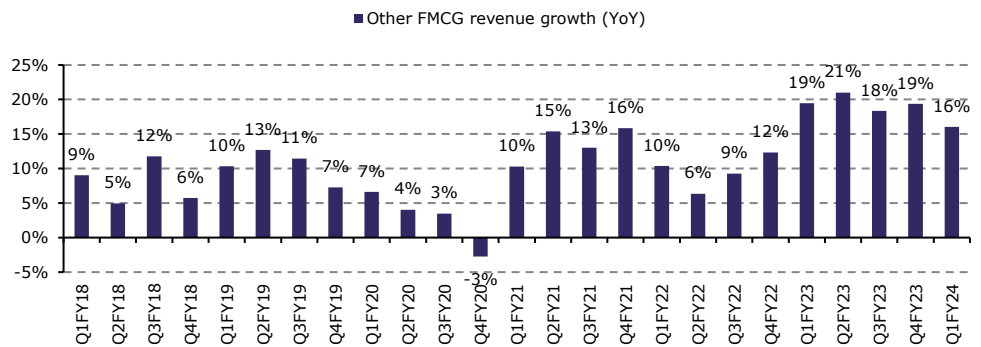
Source: Company, Emkay Research

Exhibit 10: Non-cigarettes – EBIT margin



Source: Company, Emkay Research

Exhibit 11: Other FMCG – Revenue growth

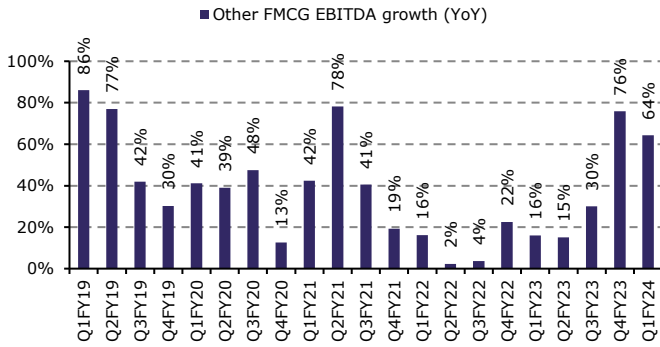


Source: Company, Emkay Research

The company saw surge in competitive intensity in the biscuits and beverages segments, at the local level

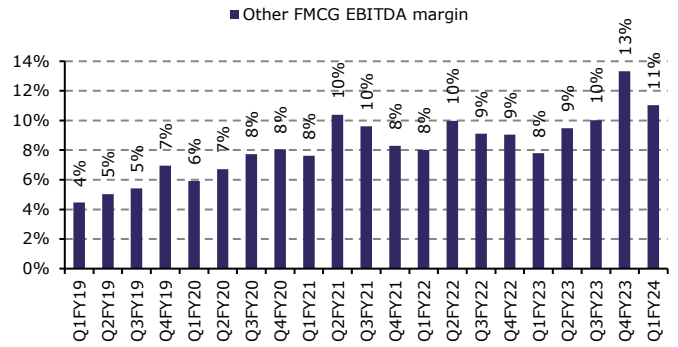
Stationary continues to clock healthy growth; we estimate revenue contribution at ~10% in Q1FY24

Exhibit 12: Other FMCG – EBITDA growth



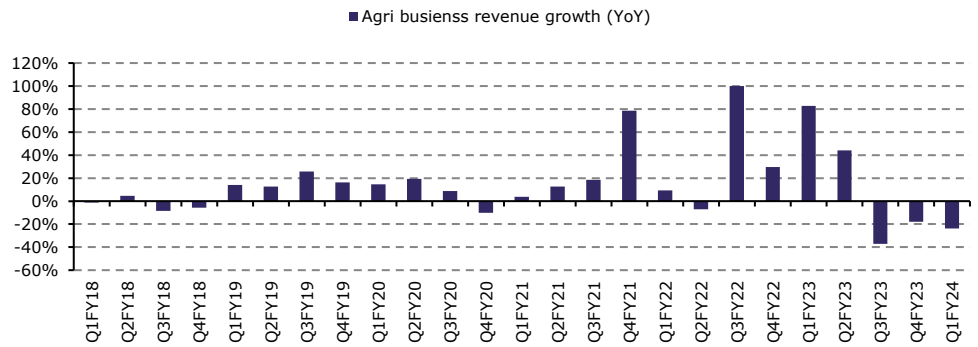
Source: Company, Emkay Research

Exhibit 13: Other FMCG – EBITDA margin



Source: Company, Emkay Research

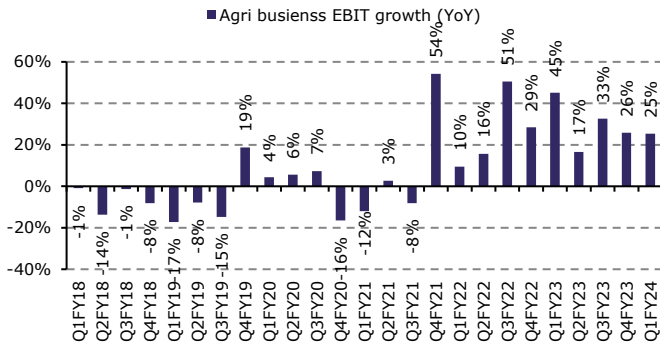
Exhibit 14: Agri-business – Revenue growth trend



Source: Company, Emkay Research

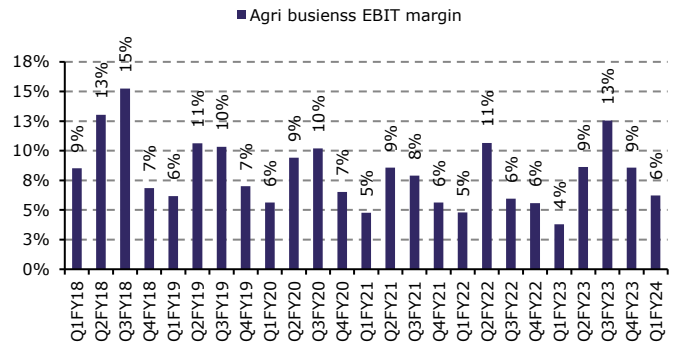
Strong growth in value-added Agri products; leveraging strong customer relations and agile execution as well as new state-of-the-art value-added Spices processing facility in Guntur. Robust growth in Leaf Tobacco revenue and margins

Exhibit 15: Agri business – EBIT growth



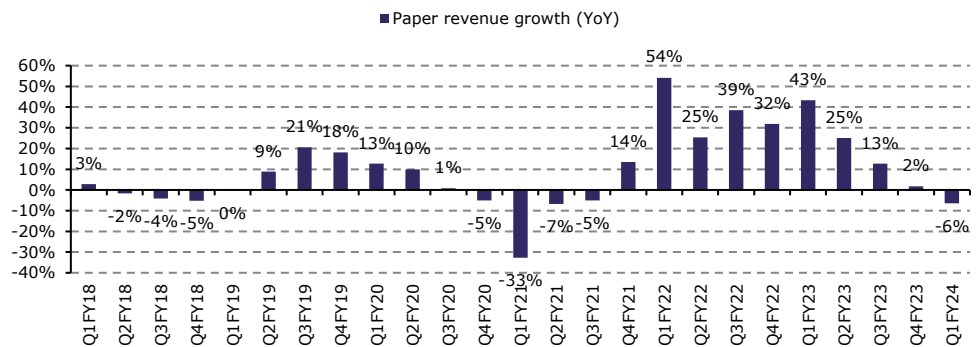
Source: Company, Emkay Research

Exhibit 16: Agri business – EBIT margin



Source: Company, Emkay Research

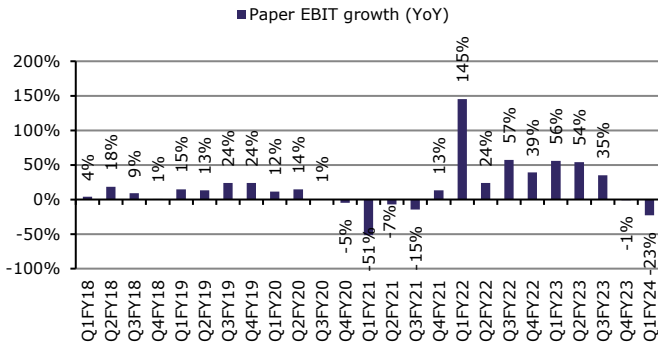
Exhibit 17: Paper business – Revenue growth



Source: Company, Emkay Research

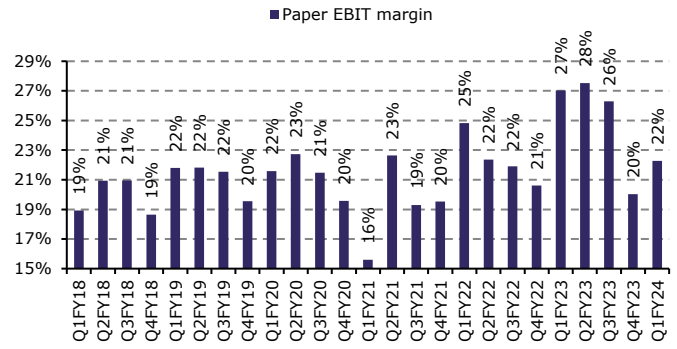
Subdued demand conditions, low-priced Chinese supplies in global markets, steep decline in global pulp prices on a high base, and relatively muted customer offtake in domestic markets (destocking) weighed on Q1FY24 performance

Exhibit 18: Paper business – EBIT growth



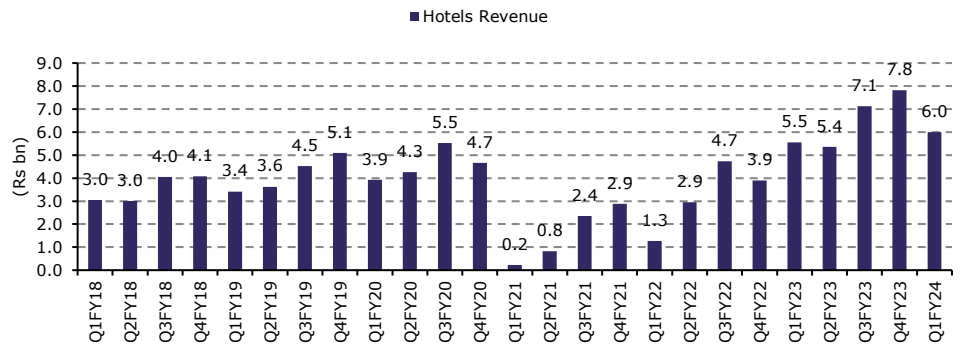
Source: Company, Emkay Research

Exhibit 19: Paper business – EBIT margin



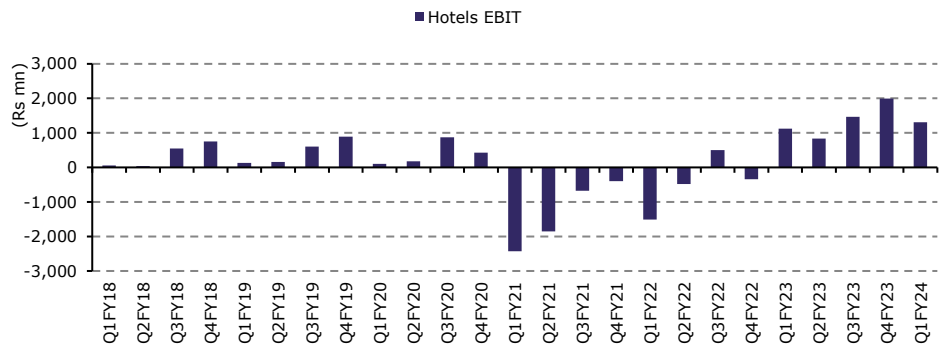
Source: Company, Emkay Research

Exhibit 20: Hotels business – Revenue trend



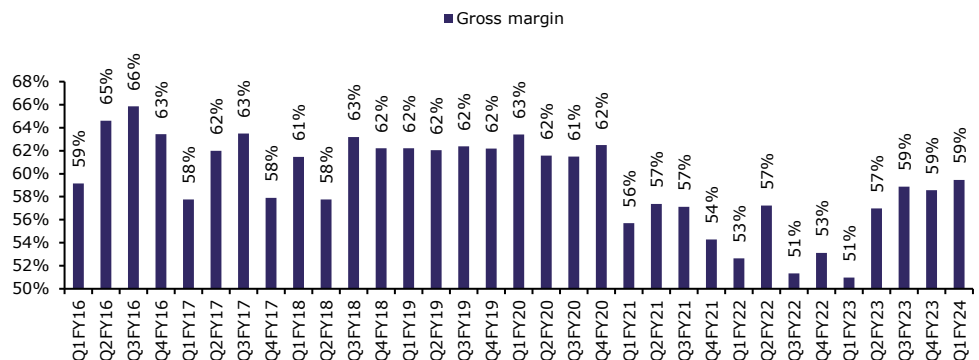
Source: Company, Emkay Research

Exhibit 21: Hotel business – EBIT trend



Source: Company, Emkay Research

Exhibit 22: Overall gross margin trend

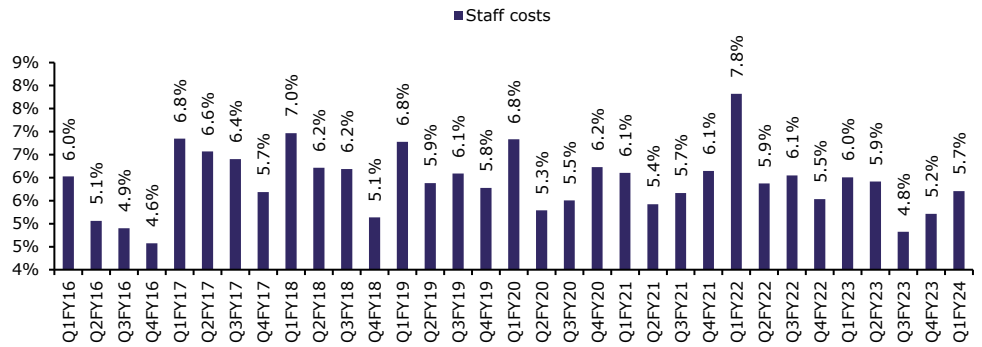


Source: Company, Emkay Research

Occupancy moderated on a high base due to relatively fewer wedding dates during the quarter and pre-planned renovations. Six new hotels were added to the ITC Hotels Group during the quarter

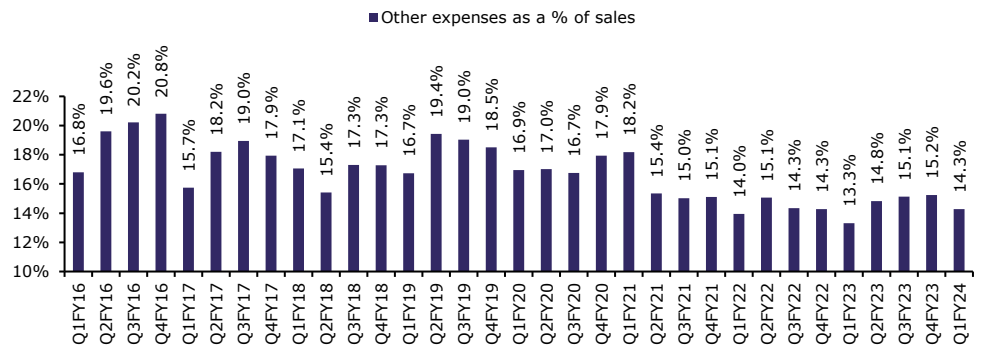
Hotels EBIT margin expansion in Q1FY24 was driven by higher RevPAR, curated packages, the finest F&B offerings and strategic cost management initiatives

Exhibit 23: Staff cost, as a % of sales



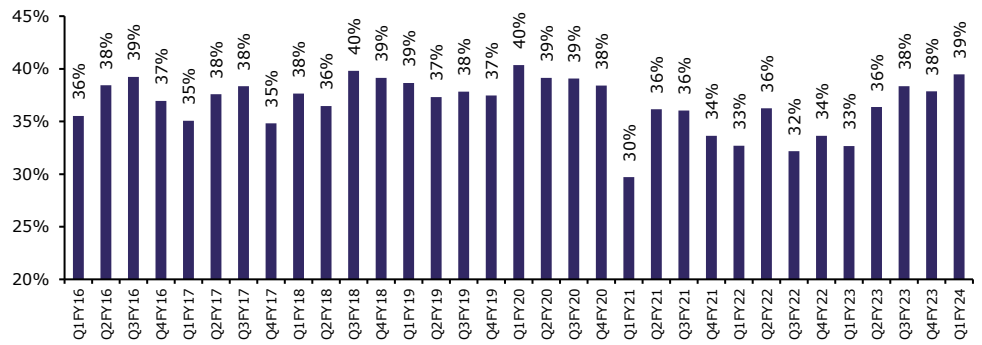
Source: Company, Emkay Research

Exhibit 24: Other expense, as a % of sales



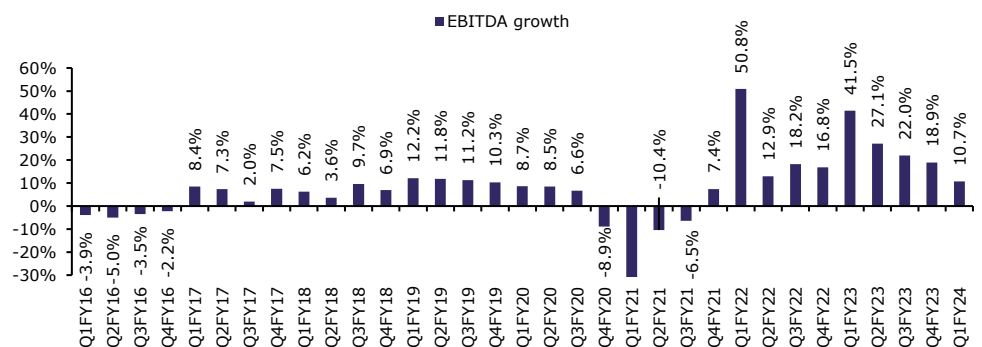
Source: Company, Emkay Research

Exhibit 25: EBITDA margin trends

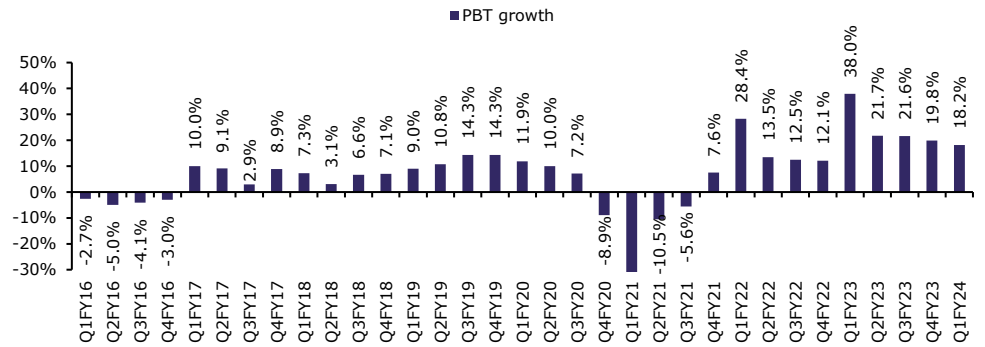


Source: Company, Emkay Research

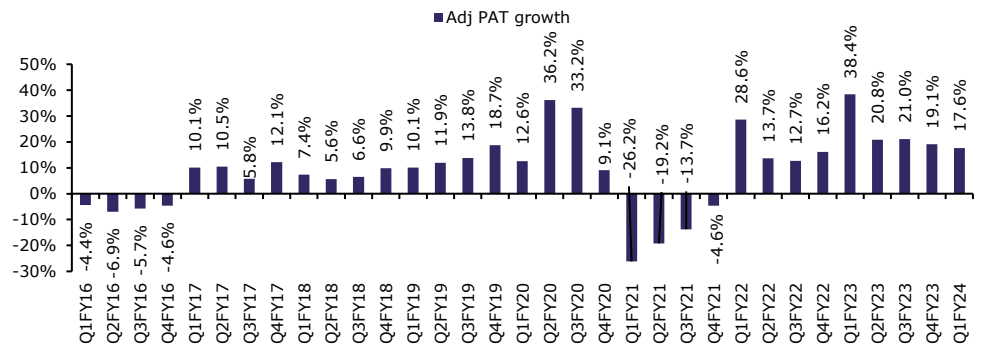
Exhibit 26: EBITDA growth trends, YoY



Source: Company, Emkay Research

Exhibit 27: Profit before tax growth, YoY

Source: Company, Emkay Research

Exhibit 28: Adjusted profit after tax growth, YoY

Source: Company, Emkay Research

Valuations to follow execution

Exhibit 29: ITC's SoTP-based target price

Segment	Valuation methodology	Units	Jun-25E	Multiple (x)	Value
Cigarettes	PER	EPS (Rs)	12.68	23.0	292
Other FMCG	EV/Sales	Sales (Rs mn)	250,176	6.0	120
Agri	EV/Sales	Sales (Rs mn)	231,528	2.5	46
Paper	EV/EBITDA	EBITDA (Rs mn)	26,488	10.0	21
Hotels	EV/EBITDA	EBITDA (Rs mn)	11,364	20.0	18
ITC Infotech	PER	EPS (Rs)	0.50	20.0	10
Net cash		Actual (Rs mn)		1.0	27
Fair value					534
Target price (Rs/share)					535

Source: Emkay Research

Exhibit 30: Changes to our estimates

(Rs mn)	New estimates			Old estimates			Changes to estimate		
	FY24	FY25	FY26	FY24	FY25	FY26	FY24	FY25	FY26
Sales	728,852	798,339	877,309	731,215	802,146	880,527	0%	0%	0%
EBITDA	262,503	297,773	326,741	259,700	293,848	322,683	1%	1%	1%
EBITDA margin	31.1%	31.2%	31.8%	37.1%	37.6%	37.3%			
Adj PAT	203,546	226,211	251,063	201,452	223,194	247,708	1%	1%	1%
EPS (Rs)	16.29	18.01	19.89	16.13	17.77	19.62	1%	1%	1%

Source: Company, Emkay Research

Hotels demerger to be effected in 15 months

The Board of Directors has approved the scheme of demerger, with share entitlement ratio of 10:1. In the new entity, the ITC shareholder will get one share for every 10 shares held. Management noted that as 100% of the ultimate economic beneficial interest of the Hotels Business will remain with ITC shareholders (60% directly, 40% through ITC), there is no need for determining fair valuation of the relevant companies.

We see this is as an apt move by the company, wherein liquidity in the stock will be balanced. Simply put: we expect the hotels business fair value to have been reassessed, but if we consider our business value of Rs225bn as fair, per-share value for Hotels in SOTP is Rs18. In case the company had decided entitlement at 1:1, traded value for Hotels would have been Rs11 (like a penny stock). With approved shareholder entitlement ratio of 10:1, Hotels would trade at Rs108, based on our ascribed value for the Hotels business.

Exhibit 31: Share allotment for the new entity

Share Entitlement Ratio: For every 10 shares held in ITC, ITC shareholders to get 1 share of ITC Hotels		
Particulars	Reference	Value
Total no. of equity shares of ITC Hotels (pre demerger)	A	83 cr.
Equity stake of ITC in ITC Hotels (post demerger)	B	40%
Total no. of equity shares of ITC Hotels (post demerger)	C = (A/B)	208 cr.
No. of equity shares of ITC Hotels to be issued to ITC's shareholders	D = C - A	125 cr.
Total no. of equity shares of ITC	E	1246.5 cr.
Number of ITC shares against which 1 share of ITC Hotels will be issued (rounded off)	E/D	10

Note: Above Share Entitlement Ratio has been recommended by an independent Registered Valuer

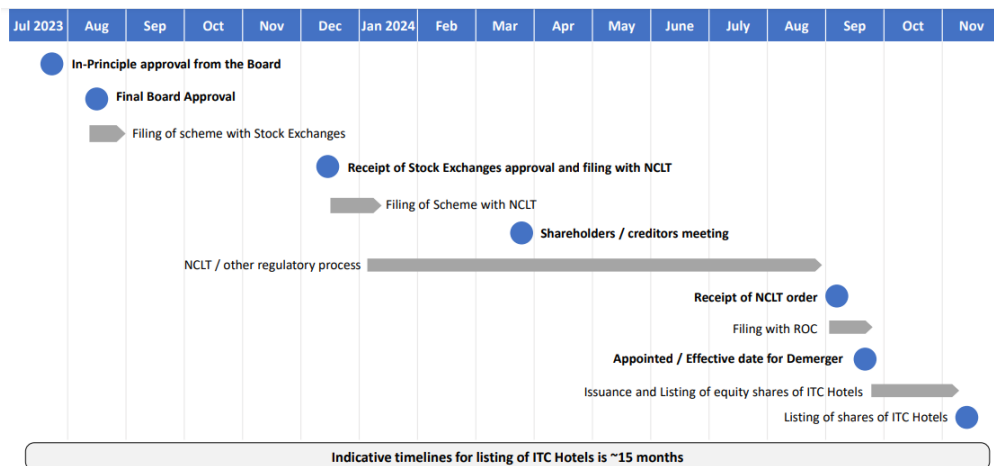
Source: Company

Exhibit 32: Assessing value of Hotels share, based on different share entitlement ratios on our SOTP-based business value estimates

	Business value	Scenario 1	Scenario 2
Hotels business value (Rs mn)	225,000		
Share entitlement ratio		1:1	10:1
Total shares to issue (mn)	12,465	12,465	1,247
Shares with ITC (mn; for 40% stake)		8,310	831
Total share of demerged entity (mn)		20,775	2,078
Per share value of Hotels (Rs)		11	108

Source: Emkay Research

Exhibit 33: Indicative time line for the Hotels demerger



Source: Company

ITC: Consolidated Financials and Valuations

Profit & Loss

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Revenue	5,63,413	6,60,023	7,28,852	7,98,339	8,77,309
Revenue growth (%)	23.9	17.1	10.4	9.5	9.9
EBITDA	1,89,337	2,39,035	2,62,503	2,97,773	3,26,741
EBITDA growth (%)	22.0	26.2	9.8	13.4	9.7
Depreciation & Amortization	16,522	16,627	17,364	17,564	17,867
EBIT	1,72,815	2,22,407	2,45,139	2,80,209	3,08,874
EBIT growth (%)	23.8	28.7	10.2	14.3	10.2
Other operating income	6,445	7,704	7,668	8,176	8,994
Other income	25,900	24,376	27,806	23,529	28,680
Financial expense	420	418	460	506	556
PBT	1,98,295	2,46,365	2,72,485	3,03,232	3,36,998
Extraordinary items	0	0	0	0	0
Taxes	47,717	59,971	68,939	77,021	85,934
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
Reported PAT	1,50,578	1,87,123	2,03,546	2,26,211	2,51,063
PAT growth (%)	15.5	24.3	8.8	11.1	11.0
Adjusted PAT	1,50,578	1,86,394	2,03,546	2,26,211	2,51,063
Diluted EPS (Rs)	12.2	15.0	16.3	18.0	19.9
Diluted EPS growth (%)	15.4	22.7	8.6	10.6	10.4
DPS (Rs)	11.0	15.5	14.0	15.0	16.5
Dividend payout (%)	90.0	102.9	85.9	83.3	83.0
EBITDA margin (%)	33.6	36.2	36.0	37.3	37.2
EBIT margin (%)	30.7	33.7	33.6	35.1	35.2
Effective tax rate (%)	24.1	24.3	25.3	25.4	25.5
NOPLAT (pre-IndAS)	1,31,230	1,68,268	1,83,119	2,09,036	2,30,111
Shares outstanding (mn)	12,323.3	12,428.0	12,493.0	12,558.0	12,623.0

Source: Company, Emkay Research

Cash flows

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
PBT	1,98,295	2,46,365	2,72,485	3,03,232	3,36,998
Others (non-cash items)	0	0	0	0	0
Taxes paid	(45,100)	(58,006)	(68,939)	(77,021)	(85,934)
Change in NWC	1,841	(4,441)	(2,467)	(7,964)	(9,344)
Operating cash flow	1,48,078	1,79,117	1,91,097	2,12,789	2,31,463
Capital expenditure	(16,748)	(18,095)	(24,000)	(28,000)	(28,000)
Acquisition of business	0	0	0	0	0
Interest & dividend income	18,204	17,732	27,806	23,529	28,680
Investing cash flow	(15,171)	(51,594)	3,806	(34,471)	(29,320)
Equity raised/(repaid)	2,919	24,774	65	65	65
Debt raised/(repaid)	(4)	(7)	105	0	0
Payment of lease liabilities	590	0	0	0	0
Interest paid	(421)	(400)	(460)	(506)	(556)
Dividend paid (incl tax)	(1,35,471)	(1,51,504)	(1,92,634)	(1,74,902)	(1,88,370)
Others	(393)	(166)	0	0	0
Financing cash flow	(1,33,370)	(1,27,304)	(1,92,924)	(1,75,343)	(1,88,861)
Net chg in Cash	(463)	219	1,978	2,975	13,281
OCF	1,48,078	1,79,117	1,91,097	2,12,789	2,31,463
Adj. OCF (w/o NWC chg.)	1,46,237	1,83,558	1,95,538	2,20,753	2,40,807
FCFF	1,31,330	1,61,022	1,67,097	1,84,789	2,03,463
FCFE	1,49,115	1,78,336	1,94,443	2,07,812	2,31,586
OCF/EBITDA (%)	78.2	74.9	72.8	71.5	70.8
FCFE/PAT (%)	99.0	95.7	95.5	91.9	92.2
FCFF/NOPLAT (%)	100.1	95.7	91.3	88.4	88.4

Source: Company, Emkay Research

Balance Sheet

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	12,323	12,428	12,493	12,558	12,623
Reserves & Surplus	6,01,672	6,63,510	6,74,422	7,25,731	7,88,424
Net worth	6,13,996	6,75,938	6,86,915	7,38,289	8,01,047
Minority interests	0	0	0	0	0
Deferred tax liability (net)	16,671	16,211	17,508	18,909	20,422
Total debt	3,112	3,247	3,511	3,679	3,856
Total liabilities & equity	6,33,779	6,95,396	7,07,935	7,60,877	8,25,325
Net tangible fixed assets	2,37,701	2,34,582	2,45,218	2,55,654	2,65,787
Net intangible assets	0	0	0	0	0
Net ROU assets	9,772	10,260	10,774	11,312	11,878
Capital WIP	24,662	16,966	12,966	12,966	12,966
Goodwill	0	0	0	0	0
Investments [JV/Associates]	21,936	23,936	23,936	23,936	23,936
Cash & equivalents	2,89,666	3,41,583	3,43,561	3,76,536	4,19,817
Current assets (ex-cash)	1,82,455	1,98,392	2,19,041	2,38,409	2,60,220
Current Liab. & Prov.	1,17,146	1,27,221	1,43,947	1,53,783	1,64,560
NWC (ex-cash)	65,309	71,170	75,094	84,627	95,660
Total assets	6,33,779	6,95,396	7,07,935	7,60,877	8,25,325
Net debt	(2,89,621)	(3,41,550)	(3,43,411)	(3,76,386)	(4,19,667)
Capital employed	6,23,584	6,85,023	6,97,414	7,50,189	8,14,460
Invested capital	2,90,386	3,05,752	3,20,312	3,40,280	3,61,447
BVPS (Rs)	49.2	53.8	54.4	58.2	62.9
Net Debt/Equity (x)	(0.5)	(0.5)	(0.5)	(0.5)	(0.5)
Net Debt/EBITDA (x)	(1.5)	(1.4)	(1.3)	(1.3)	(1.3)
Interest coverage (x)	0.0	0.0	0.0	0.0	0.0
RoCE (%)	32.5	37.7	39.5	42.0	43.1

Source: Company, Emkay Research

Valuations and key Ratios

Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	36.8	30.0	27.6	24.9	22.6
P/CE (x)	33.4	27.7	25.6	23.3	21.2
P/B (x)	9.1	8.3	8.3	7.7	7.1
EV/Sales (x)	9.4	8.0	7.3	6.7	6.0
EV/EBITDA (x)	27.7	21.9	20.1	17.7	16.1
EV/EBIT(x)	30.6	23.7	21.7	18.9	17.1
EV/IC (x)	18.2	17.3	16.6	15.6	14.6
FCFF yield (%)	2.5	3.0	3.1	3.5	3.8
FCFE yield (%)	2.7	3.2	3.4	3.7	4.1
Dividend yield (%)	2.4	3.5	3.1	3.3	3.7
DuPont-RoE split					
Net profit margin (%)	26.7	28.2	27.9	28.3	28.6
Total asset turnover (x)	0.9	1.0	1.1	1.1	1.1
Assets/Equity (x)	1.0	1.0	1.0	1.0	1.0
RoE (%)	25.3	29.2	30.2	32.1	32.9
DuPont-RoIC					
NOPLAT margin (%)	23.3	25.5	25.1	26.2	26.2
IC turnover (x)	2.0	2.2	2.3	2.4	2.5
RoIC (%)	47.7	56.5	58.5	63.3	65.6
Operating metrics					
Core NWC days	11.1	10.7	9.0	7.1	7.1
Total NWC days	42.3	39.4	37.6	38.7	39.8
Fixed asset turnover	1.5	1.6	1.7	1.7	1.8
Opex-to-revenue (%)	19.8	20.0	20.4	19.9	19.7

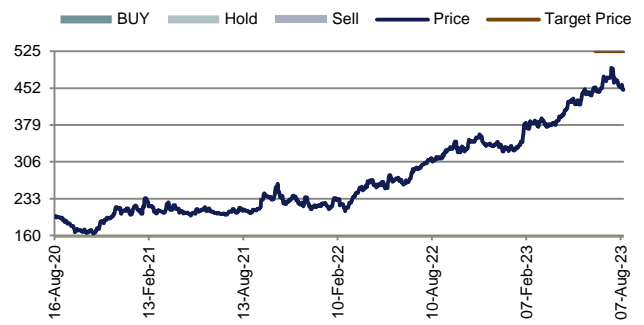
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	CMP (INR)	TP (INR)	Rating	Analyst
28-Jul-23	468	525	Buy	Nitin Gupta
24-Jul-23	471	525	Buy	Nitin Gupta
15-Jul-23	473	525	Buy	Nitin Gupta
19-Jun-23	454	525	Buy	Nitin Gupta

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Bloomberg, Company, Emkay Research

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