Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Hindustan Unilever Ltd

Mixed Q2; volume growth to gradually pick up

Consumer Goods	Sharekhan code: HINDUNILVR

Reco/View: Buy	↔	CMP: Rs. 2,548	Price Target: Rs. 2,910	↓

↑ 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 Updated Aug 08, 2023	23.4

Medium Risk

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

Source: Morningstar

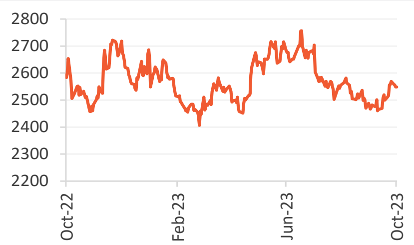
Company details

Market cap:	Rs. 5,98,641 cr
52-week high/low:	Rs. 2,769 / 2,393
NSE volume: (No of shares)	14.6 lakh
BSE code:	500696
NSE code:	HINDUNILVR
Free float: (No of shares)	89.5 cr

Shareholding (%)

Promoters	61.9
FII	15.1
DII	11.6
Others	11.46

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	2.4	-2.2	2.2	-1.4
Relative to Sensex	5.3	-0.6	-7.8	-12.4

Sharekhan Research, Bloomberg

Summary

- HUL's Q2FY24 numbers were mixed with revenues and PAT (excluding one-offs) growing by 3% and 7%, y-o-y respectively. OPM improved by 91 bps to 23.8% driving better PAT growth. Volume growth at 2% was a slight miss on expectation.
- Moderation in inflation, stability in price cuts in key product categories and festive season will help in gradual pick in volume growth. Urban demand remains steady while rural demand is witnessing a slow recovery.
- Lower input prices would keep gross margin healthy. A large part of savings will be invested in higher ad spends given increased competitive intensity. Impact of global uncertainly needs to be monitored in the near term.
- Stock has underperformed for the past one year and trades at 55x/48x its FY2024E/FY2025E earnings. We retain Buy with a revised price target of Rs. 2,910.

HUL delivered mixed performance in Q2FY2024, with slight miss on volume growth (reported 2% y-o-y volume growth against expectation of 3-4%), while decline in input prices led to sharp 692 bps y-o-y expansion in the gross margin. Revenue grew by 3.6% y-o-y to Rs. 15,276 crore in Q2FY2024 (excluding tax credit grew by 2.6%). Gross margins improved by 692 bps y-o-y to 52.7% aided by softening of key input costs, while despite higher advertisement spends (increased by 420 bps) OPM rose by 129 bps y-o-y at 24.2% (excluding tax credit came at 23.8%). Adjusted PAT grew by 12% y-o-y to Rs. 2,672 crore and excluding one-off tax credit grew by 7% y-o-y to Rs. 2,533 crore. For H1FY2024, revenues grew by 5% y-o-y; OPM improved by 89 bps y-o-y to 23.7% and adjusted PAT grew by 11.5% y-o-y to Rs. 5,221 crore.

Key positives

- Home care and beauty segments registered mid-single digit volume growth.
- Over 75% of portfolio continued to gain volume market share.
- Gross margins improved by 692 bps y-o-y to 52.7% aided by softening of key input costs.

Key negatives

- Food & refreshments segment saw a mid-single digit decline in sales volumes and a 112 bps y-o-y decline in PBIT margin.

Management Commentary

- Rural volumes grew by 8% in Q2FY24 versus a 9% decline in Q2FY23. Moderating inflation and an expected rise in rural incomes due to an increase in government spending on infrastructure might lead to gradual recovery in rural demand.
- Urban demand remained steady with good traction to large packs especially in the modern trade. With price cuts largely done in the portfolio and improved demand during festive season might lead to better growth in Q3FY2024.
- Higher competition in mass categories (such as tea and detergent bars) might lead to downtrading in certain categories, which will be offset by consistent growth in the premium categories.
- Lower input prices will help gross margins stay high. Large part of raw material cost savings will be utilised for competitive advertisement and media spends in the coming quarters.
- Growing the core through product superiority, market development & premiumisation, portfolio transformation and winning the channel of future will help to achieve consistent growth in the long run.

Revision in estimates – We have broadly maintained our earnings estimates for FY2024 while reduced it for FY2025 by 3% to factor in little lower realisation growth in home care and BPC category due to recent price cuts in the portfolio.

Our Call

View - Maintain Buy with a revised PT of Rs. 2,910: HUL posted muted performance in H1FY2024 on the backdrop of weak rural demand. Moderating inflation and price cuts in portfolio should help volumes to gradually pick up in the coming quarters ahead. Leadership position in a few high-penetrated categories, thrust on innovation and market development to remain competitive will help to achieve consistent growth in the long run. HUL has underperformed the broader indices for last one year and is currently trading at 55x and 48x its FY2024E and FY2025E earnings, respectively. Any substantial recovery in the domestic volume growth with rural demand picking up while premiumization and market development strategy would help drive consistent profitable growth in the coming quarters might act as key trigger for the stock. We maintain our Buy recommendation on the stock with a revised PT of Rs. 2,910.

Key Risks

Sustained slowdown in rural demand or persistent volatility in key input prices from current levels would act as a key risk to our earnings in the near term.

Valuation (standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
Revenue	51,193	59,144	62,696	71,393
OPM (%)	24.4	23.0	24.0	24.2
Adjusted PAT	8,845	10,024	10,896	12,438
Adjusted EPS (Rs.)	37.6	42.7	46.4	52.9
P/E (x)	67.7	59.7	55.0	48.1
P/B (x)	12.3	11.9	11.6	10.9
EV/EBIDTA (x)	47.4	43.5	39.4	34.0
RoNW (%)	18.4	20.3	21.4	23.4
RoCE (%)	23.6	25.6	28.0	31.1

Source: Company; Sharekhan estimates

Mixed Q2; volume growth stood at 2%

Revenues grew by 3.6% y-o-y to Rs. 15,276 crore in Q2FY2024 (excluding tax credit – Rs. 15,134.5 crore; y-o-y growth of 2.6%) as against our and average street expectation of Rs. 15,317-15,483 crore. Domestic sales volume grew by 2% y-o-y slightly lower than our as well as street expectation of a 3-4% volume growth. Rural demand remained subdued, while urban and modern trade led growth in Q2FY2024. Homecare segment revenue grew by 3.3% y-o-y, beauty & personal care segment revenue grew by 4.5% y-o-y and foods segment registered a growth of 2.6% y-o-y. Homecare and beauty segments saw a mid-single digit volume growth while foods & refreshments segment saw mid-single digit decline in sales volumes. Gross margins improved by 692 bps y-o-y to 52.7% aided by softening of key input costs, while despite higher advertisement spends (up 420 bps y-o-y) OPM was higher by 129 bps y-o-y at 24.2% (excluding tax credit came at 23.8%). OPM (excluding tax credit) came largely in line with our and street average expectation of 23.5-23.7%. Operating profit grew by 9.4% y-o-y to Rs. 3,694 crore (excluding tax credit grew by 6.7%). In line with operating profit growth, adjusted PAT grew by 12% y-o-y to Rs. 2,672 crore and excluding one-off tax credit grew by 7% y-o-y to Rs. 2,533 crore, in line with our expectation of Rs. 2,539 crore and lower than street average expectation of Rs. 2,628 crore. In H1FY2024, revenues grew by 4.8% y-o-y to Rs. 30,424 crore, OPM came in higher by 89 bps y-o-y to 23.7% and adjusted PAT rose by 10.4% y-o-y to Rs. 5,171 crore. The company declared an interim dividend of Rs. 18 per share for FY2024.

Home Care (HC) – Mid-single digit volume growth; margins higher y-o-y

The HC segment grew by 3.3% y-o-y to Rs. 5,312 crore, with volume growth in mid single-digit. Fabric wash had mid-single digit volume growth with the premium portfolio continuing to outperform, while household care volumes grew in high single digit led by dishwash. Premium brands such as Surf and Comfort registered double digit volume growth during the quarter. Further price reductions were taken in both fabric wash and household care. Brand and marketing investments were stepped-up to protect the company's competitive position. During the quarter, Vim Pure range with plant-based actives and Comfort Intense Fabric Conditioner were launched. PBIT margin of the HC segment increased by 145 bps y-o-y to 18.7%.

Beauty and personal care (BPC) – Volume-led growth; margins improved y-o-y

The segment reported 4.5% y-o-y growth to Rs. 5,809 crore driven by mid single-digit volume growth. The skin cleansing category revenue declined as further price reductions taken in soaps offset low-single digit volume growth. Lux and Hamam continued to outperform. Skincare and colour cosmetics grew in double-digit led by outperformance in Ponds and Vaseline coupled with focused interventions in new demand spaces and channels of the future. Hair care delivered high-single digit growth with Clinic Plus and Indulekha continuing to outperform. Oral care grew in mid-single digit led by Closeup. Key launches in this quarter include new range of Vaseline moisturizers, Lakme serums and cosmetics, Pond's serum, Indulekha Anti-Dandruff Oil and Shampoo. PBIT margins of the BPC segment expanded by 211 bps y-o-y to 27.2%.

Foods and Refreshments (F&R) – Pricing-led growth; margins lower y-o-y

The F&R segment delivered 2.6% y-o-y revenue growth to Rs. 3,851 crore, with mid-single digit decline in volume. Tea delivered a modest growth as the category continued to witness consumers downgrading. Coffee grew in double-digits. Health food drinks (HFD) delivered mid-single digit price led growth driven by activations and innovations. Foods and ice cream both grew in mid-single digit on a high base. Foods solutions, mayonnaise and peanut butter continued to clock strong growths. During the quarter, Horlicks Strength Plus, Slow Churn Ice Cream and new blends of Lipton Green Tea were launched. PBIT margin of F&R segment fell by 112 bps y-o-y to 18.7%.

HFD category – focus remains on improving penetration

HUL's focus remains on improving category penetration through low pack categories to attract more customers in the tier 2 and 3 markets and addition of new products backed by science catering to specific need of consumers to recruit new customers in the urban market. The company has seen an improvement in market share in the overall HFD category. Category consumption is impacted by significant inflation in milk prices. However, the same is expected to moderate in the coming quarters. Despite input cost inflation and slowdown in consumption, HFD category overall margins remained in-line with the margins when acquired by HUL. The company is confident of long term growth prospects of the category.

Results (Standalone) Rs cr

Particulars	Q2FY24	Q2FY23	y-o-y (%)	Q1FY24	q-o-q (%)
Net revenue	**15,276.0**	**14,751.0**	**3.6**	**15,148.0**	**0.8**
Total Raw Material	7,221.0	7,994.0	-9.7	7,588.0	-4.8
Employee Expenses	708.0	709.0	-0.1	651.0	8.8
Advertising and promotions	1,720.0	1,041.0	65.2	1,481.0	16.1
Other Expenses	1,933.0	1,630.0	18.6	1,907.0	1.4
Total expenditure	11,582.0	11,374.0	1.8	11,627.0	-0.4
Operating Profit	**3,694.0**	**3,377.0**	**9.4**	**3,521.0**	**4.9**
Other income	283.0	115.0	-	185.0	53.0
EBITDA	3,977.0	3,492.0	13.9	3,706.0	7.3
Interest	72.0	25.0	-	47.0	53.2
PBDT	3,905.0	3,467.0	12.6	3,659.0	6.7
Depreciation	269.0	248.0	8.5	257.0	4.7
PBT	**3,636.0**	**3,219.0**	**13.0**	**3,402.0**	**6.9**
Tax	914.0	833.0	9.7	903.0	1.2
Adjusted PAT	**2,672.0**	**2,386.0**	**12.0**	**2,499.0**	**6.9**
Extra-ordinary items	-44.7	-230.0	-	27.0	-
Reported PAT	**2,716.7**	**2,616.0**	**3.8**	**2,472.0**	**9.9**
Adjusted EPS (Rs.)	11.4	10.2	12.0	10.6	6.9
			bps		**Bps**
GPM (%)	52.7	45.8	692	49.9	282
OPM (%)	24.2	22.9	129	23.2	94
NPM (%)	17.5	16.2	132	16.5	100
Tax rate (%)	25.1	25.9	-74	26.5	-141

Source: Company, Sharekhan Research

Result snapshot (excluding one-off) Rs cr

Particulars	Q2FY24	Q2FY23	y-o-y (%)	Q1FY24	q-o-q (%)
Net Revenues	15134.5	14751.0	2.6	15148.0	-0.1
Total Expenditure	11532.5	11374.0	1.4	11627.0	-0.8
Operating Profit	3602.0	3377.0	6.7	3521.0	2.3
Adjusted PAT	2553.0	2386.0	7.0	2499.0	2.2
OPM (%)	23.8	22.9	91	23.2	56

Source: Company, Sharekhan Research

Segmental performance Rs cr

Particulars	Q2FY24	Q2FY23	y-o-y (%)	Q1FY24	q-o-q (%)
Revenue					
Home Care	5,312.0	5,143.0	3.3	5,425.0	-2.1
Beauty & Personal Care	5,809.0	5,561.0	4.5	5,601.0	3.7
Food & Refreshments	3,851.0	3,755.0	2.6	3,797.0	1.4
Others	304.0	292.0	4.1	325.0	-6.5
Total	**15,276**	**14,751**	**3.6**	**15,148**	**0.8**
PBIT margins (%)					
Home Care	18.7	17.3	145	18.3	46
Beauty & Personal Care	27.2	25.1	211	26.3	94
Food & Refreshments	18.7	19.8	-112	17.9	76
Total	**21.6**	**20.5**	**104**	**20.8**	**82**

Source: Company, Sharekhan Research

Outlook and Valuation

Sector view - Rural recovery on cards; margin improvement to sustain

With food inflation easing and expected stable kharif crop, managements of most consumer goods companies are confident of witnessing a pick-up in rural demand in H2FY2024. This will also be supported by the upcoming festive season and higher government spending prior to the general elections. Overall, we expect a gradual improvement in volume growth of consumer goods companies in the quarters ahead. Crude oil prices moved up from its low but continue to remain in a comfortable zone. Other input prices are yet to see a significant jump and will provide lesser stress on the profitability in the near term. Thus, we expect gross margin expansion to sustain in the quarters ahead. Despite higher media spends, OPM is expected to remain elevated y-o-y in the near term. Most of the consumer goods companies are optimistic about medium-term growth outlook aided by low penetration in most categories, emerging distribution channels, and improving per-capita income.

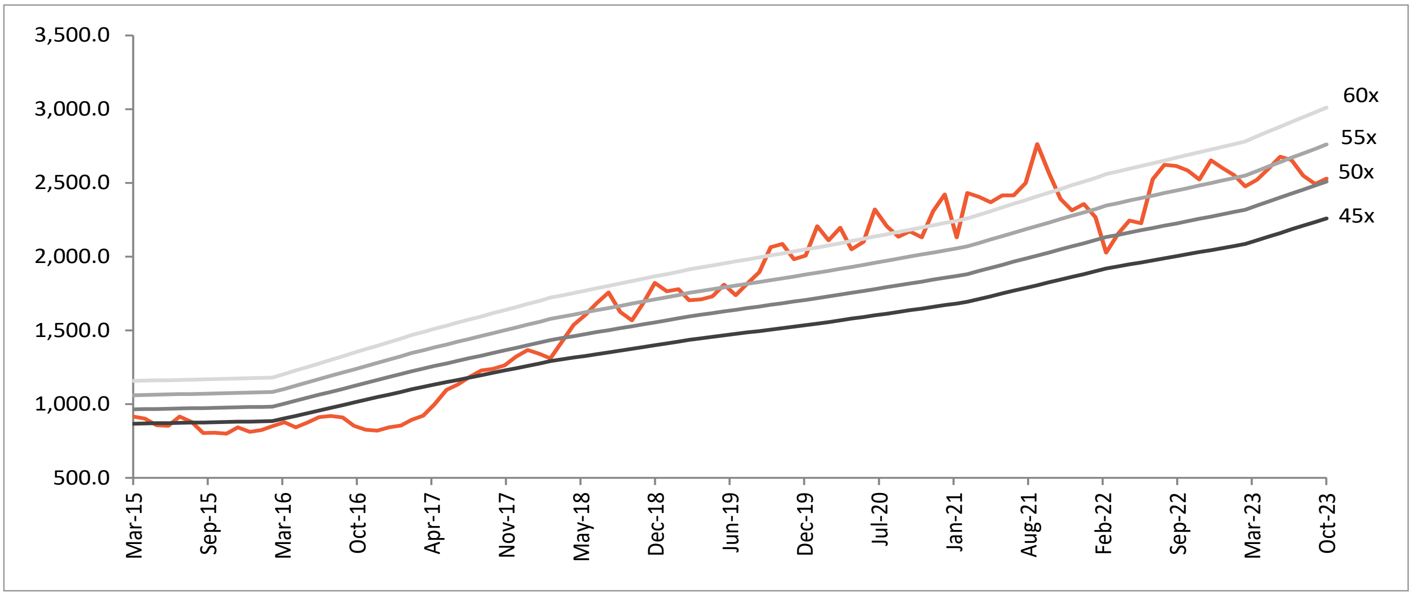
Company outlook - Focus remains on achieving competitive volume growth

HUL posted mixed performance in Q2FY2024 with a slight miss on volumes, while gross margins saw sharp jump due to decline in the input prices. The company is well poised to achieve good growth in the coming years with a leadership position in over 85% of the portfolio and a presence in more than 8 million stores. Recovery in rural demand, improvement in demand for out-of-home categories with better mobility, addition of relevant products in the portfolio and sustained improvement in the penetration of key categories remain key growth drivers in the near term. We expect revenue growth in FY2024 will largely be a volume-led growth with input price inflation receding for past few months. A better product mix with a recovery in discretionary categories, calibrated price hikes and operational efficiencies and integration benefits would help margins to improve in the coming years. However, the recent hike in royalty charges and continued focus on A&P spends will moderate margin expansion.

Valuation - Maintain Buy with a revised PT of Rs. 2,910

HUL posted muted performance in H1FY2024 on the backdrop of weak rural demand. Moderating inflation and price cuts in portfolio should help volumes to gradually pick up in the coming quarters ahead. Leadership position in a few high-penetrated categories, thrust on innovation and market development to remain competitive will help to achieve consistent growth in the long run. HUL has underperformed the broader indices for last one year and is currently trading at 55x and 48x its FY2024E and FY2025E earnings, respectively. Any substantial recovery in the domestic volume growth with rural demand picking up while premiumization and market development strategy would help drive consistent profitable growth in the coming quarters might act as key trigger for the stock. We maintain our Buy recommendation on the stock with a revised PT of Rs. 2,910.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Companies	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E
Nestle India*	97.3	77.0	66.5	62.5	52.1	44.9	129.2	135.5	138.9
ITC	29.3	25.7	22.7	22.8	19.7	17.2	32.7	35.1	37.1
Godrej Consumer Products	57.7	46.6	38.5	39.2	34.0	28.9	15.2	15.4	16.6
HUL	59.7	55.0	48.1	43.5	39.4	34.0	25.6	28.0	31.1

Source: Company, Sharekhan estimates; *Values for Nestle India are for CY22, CY23E and CY24E

About company

HUL is India's largest FMCG company with presence of more than 90 years. The company is a subsidiary of Unilever Plc (that holds a 62% stake in HUL), the world's largest consumer goods company present across 190 countries. It has a strong portfolio in the homecare and beauty and personal care categories. With over 50 brands spanning 16 distinct categories such as personal wash, fabric wash, skin care, hair care, oral care, deodorants, colour cosmetics, beverages, ice creams, frozen desserts, and water purifiers, HUL is part of the everyday life of millions of consumers across India. The company's portfolio includes leading brands such as Lux, Lifebuoy, Surf Excel, Rin, Wheel, Fair & Lovely, Pond's, Vaseline, Lakmé, Dove, Clinic Plus, Sunsilk, and Axe. Out of the company's portfolio of over 50 brands, 19 brands have a turnover exceeding Rs. 1,000 crore per annum (FY23).

Investment theme

HUL has a leadership position in highly penetrated categories such as soaps, detergents, and shampoos in India. The company maintained its leadership position in more than 85% of business (FY23). Sustaining product innovation, entering new categories, premiumisation, and increasing distribution network remain some of the company's key revenue drivers. A strong financial background, robust cash-generation ability, and leadership position in some of the key categories give HUL an edge over other companies and, hence, justify the stock's premium valuation. With strategies in place, we expect the company to clock 10%/11% revenue/PAT CAGR over FY2023-25E.

Key Risks

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

Additional Data

Key management personnel

Nitin Paranjpe	Chairman
Rohit Jawa	Chief Executive Officer & Managing Director
Ritesh Tiwari	Executive Director, Finance & IT and Chief Financial Officer
Dev Bajpai	Executive Director, Legal & Corporate Affairs & Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	3.69
2	SBI Funds Management	1.62
3	Vanguard Group Inc	1.56
4	Blackrock Inc	1.48
5	Republic of Singapore	1.04
6	JP Morgan and Chase	0.61
7	ICICI Prudential AMC	0.59
8	ICICI Prudential Life Insurance Co.	0.49
9	UTI Asset Management Co Ltd	0.46
10	Norges Bank	0.34

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

Sharekhan

by BNP PARIBAS

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Other registrations of Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669.

Compliance Officer: Ms. Binkle Oza; Tel: 022-62263303; email id: complianceofficer@sharekhan.com

For any complaints/grievance, email us at igc@sharekhan.com or you may even call Customer Service desk on - 022 - 41523200/022 - 69920600