

ITC Limited (ITC)

₹ 204

WHAT'S CHANGED...

PRICE TARGET	Unchanged
EPS (FY12E)	Changed from ₹ 7.3 to ₹ 8.0
EPS (FY13E)	Changed from ₹ 8.4 to ₹ 9.2
RATING	Unchanged

Moderate volume growth, rise in other income...

ITC posted strong results with ~22.5% growth in earnings in Q3FY12. Net sales witnesses 13.6% growth YoY to ₹ 6195.4 crore led by ~11% growth in cigarettes and 24.5% growth in the FMCG business. Cigarettes and FMCG constitutes ~74% of the total sales. EBITDA margins expanded by 200 bps to 38.4% compared to 36.4% in Q3FY11. Other income increased by 47.7% to ₹ 285.1 crore mainly on account of treasury income. Strong EBITDA growth and higher other income resulted in a 22.5% increase in net profit to ₹ 1701.0 crore.

Segmental results

Cigarette revenues grew 11% to ₹ 5809 crore on the back of strong volume growth of ~5% and ~5.7% price led growth. The steep price hike of ~10% in most categories resulted in volume growth moderating from ~7% in H1FY12 to ~5% in Q3FY12. We believe ITC will witness volume growth of ~5% in Q4FY12 and FY13. The FMCG business witnessed 24.5% growth in sales led by almost ~15-17% volume growth in the food segment of the FMCG business. The hotel business witnessed 2.5% growth in sales led by marginal improvement in average room rates (ARR).

Valuation

Currently, the stock is trading at 25x its FY12E EPS of ₹ 8.0 and 21x its FY13E EPS of ₹ 9.4. We believe a continuous reduction in FMCG losses and sustained growth in the cigarettes business (mainly led by price hikes) would continue to drive bottomline growth and expand overall margins in FY13E. However, due to moderate volume growth in cigarettes, we are changing multiples for the cigarettes business from 26x P/E to 25x P/E. Simultaneously, the risk of a steep increase in excise duty would remain an overhang on the stock till the 2012 Budget. We have valued the stock on an SOTP basis and arrived at a fair value of ₹ 230.

Exhibit 1: Financial Performance

(₹ Crore)	Q3FY12	Q3FY12E	Q3FY11	Q2FY12	QoQ (Chg %)	YoY (Chg %)
Net Sales	6195.4	6058.0	5453.5	5974.2	3.7	13.6
EBITDA	2381.1	2194.8	2029.3	2219.0	7.3	17.3
EBITDA Margin (%)	38.4	36.2	36.4	37.1	129 bps	201 bps
Depreciation	173.6	169.8	168.1	170.1	2.0	3.3
Interest	16.0	13.2	23.0	14.2	12.6	-30.4
Other Income	285.1	134.3	193.0	180.8	57.7	47.7
Reported PAT	1701.0	1444.3	1389.1	1514.3	12.3	22.5
EPS (₹)	2.1	1.8	1.6	1.7	24.3	33.0

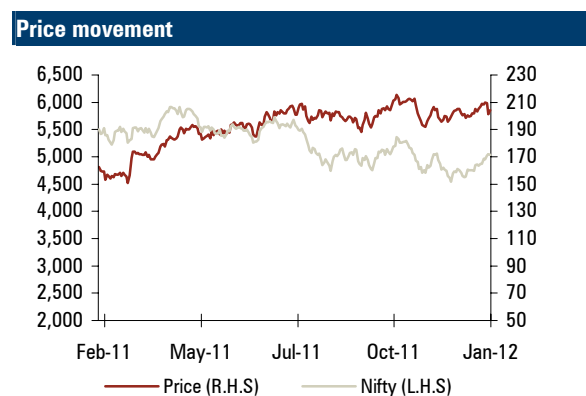
Source: Company, ICICIdirect.com Research

Rating matrix	
Rating	: Buy
Target	: ₹ 230
Target Period	: 12-15 months
Potential Upside	: 13%

Key Financials				
₹ Crore	FY11	FY12E	FY13E	FY14E
Net Sales	21,168	24,279.8	28,250.3	32,435.5
EBITDA	34.7	36.6	38.0	38.1
Net Profit	4,987.6	6,203.4	7,269.8	8,377.5
EPS (Rs)	6.4	8.0	9.4	10.8

Valuation summary				
	FY11	FY12E	FY13E	FY14E
P/E	31.2	25.1	21.4	18.6
Target P/E	35.8	28.7	24.5	21.3
Dividend yield	2.2	2.6	3.0	3.0
Price/Sales	7.3	6.4	5.5	4.8
RoNW	31.3	35.5	37.5	37.5
RoE	31.3	35.5	37.5	37.5
RoNW	31.3	35.5	37.5	37.5

Stock data	
Bloomberg/Reuters Code	ITC.BO / ITC.NS
Sensex	16,913.0
Average volumes	618,169.0
Market Cap (Rs crore)	155,536.7
52 week H/L	216 / 201
Equity Capital (Rs crore)	779.6
Promoter's Stake (%)	-
FII Holding (%)	16.3
DII Holding (%)	34.8



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Revising estimates

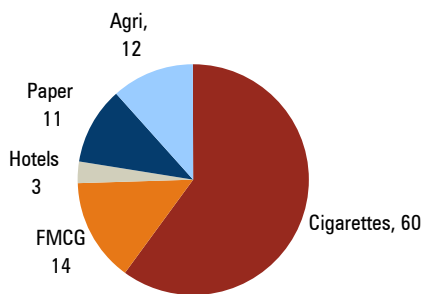
In light of the price hikes in cigarettes, reduction in losses in the FMCG business and higher other income, we believe the company would post higher earnings for FY12 and FY13. Hence, we are revising our estimates for FY12 and FY13.

Exhibit 2: Revising Estimates

Particulars	FY12E			FY13E		
	Old	New	% Change	Old	New	% Change
Revenue	23,928.5	24279.8	1.5	27,702.9	28250.3	2.0
EBITDA	8,643.0	9007.2	4.2	10,015.2	10902.7	8.9
EBITDA Margi	36.1	37.1	98 bps	36.2	38.6	244 bps
PAT	5769.8	6203.4	7.5	6665.1	7269.8	9.1
EPS	7.3	8.0	10.3	8.4	9.4	11.9

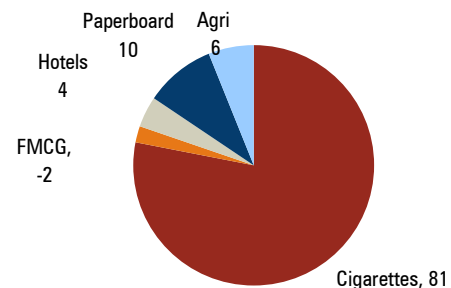
Source: Company, ICICIdirect.com Research

Exhibit 3: ITC's revenues contribution (%)



Source: Company, ICICIdirect.com, Research

Exhibit 4: ITC's EBIT contribution (%)

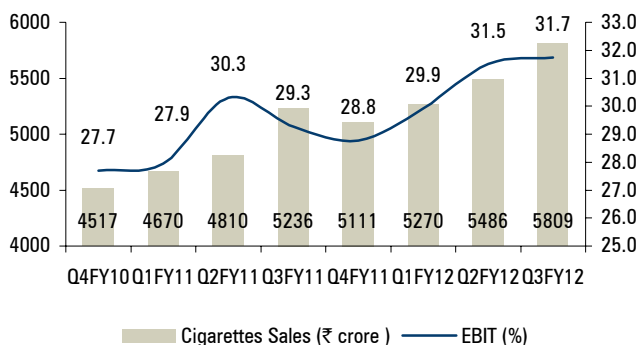


Source: Company, ICICIdirect.com, Research

Moderation in volume growth

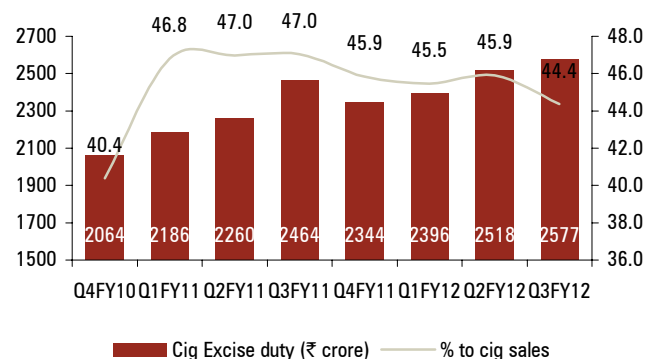
The company posted ~5% volume growth in cigarettes compared to 7%+ growth in the first half of FY12. The moderation in volumes has been on account of steep price hikes taken by the company in August 2011. We expect the cigarettes volume growth to remain at ~5% in FY13 and growth in the cigarettes business would be more from the price hikes in future.

Exhibit 5: Cigarette sales and EBIT trend



Source: Company, ICICIdirect.com Research

Exhibit 6: Excise duty on cigarettes and percentage to cigarette sales



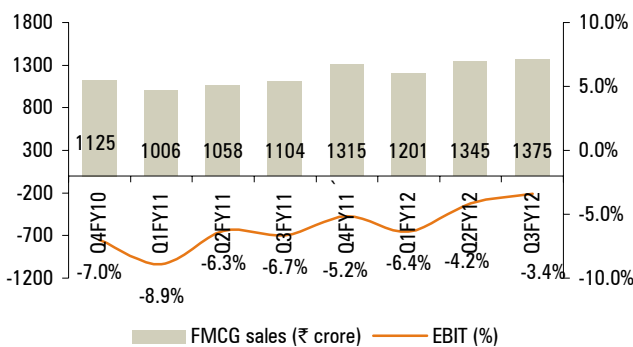
Source: Company, ICICIdirect.com Research

Reduction in FMCG losses, hotels business margins improving

FMCG losses for the company are coming down on a continuous basis and margins have improved from negative ~9% in Q1FY11 to negative ~3.4 in Q3FY12. The food segment of the FMCG business has broken even. The company has adopted a strategy of continuous spend on personal care brands and is increasing the penetration of Fiama, Vivel and other brands in the personal care segment.

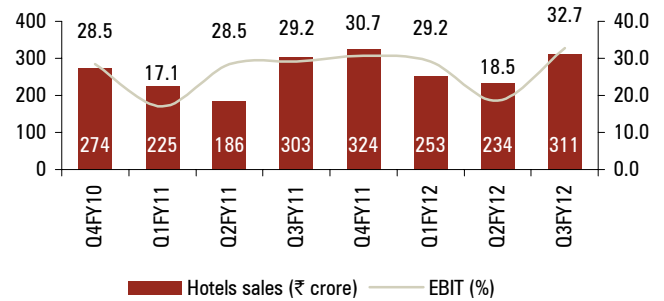
The hotels business witnessed a moderate 2.5% YoY growth. The occupancy remains between ~65% and 68%, whereas the average room rate for the company improved marginally to ₹ 8300. The company would be adding 600 rooms in Chennai in Q1FY13, which should start contributing to the topline from Q2FY13.

Exhibit 7: FMCG sales and EBIT margins trend



Source: Company, ICICIdirect.com Research

Exhibit 8: Hotels sales and EBIT trend

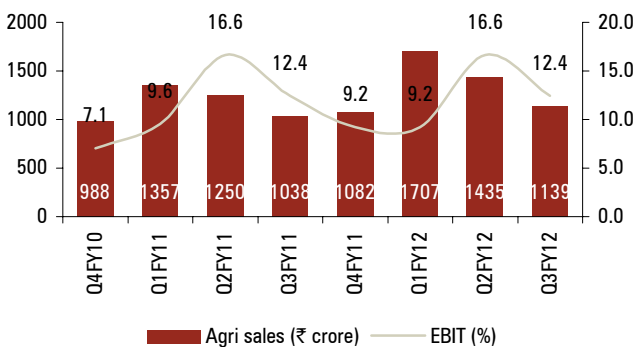


Source: Company, ICICIdirect.com Research

Strong volume growth in agri and paper business

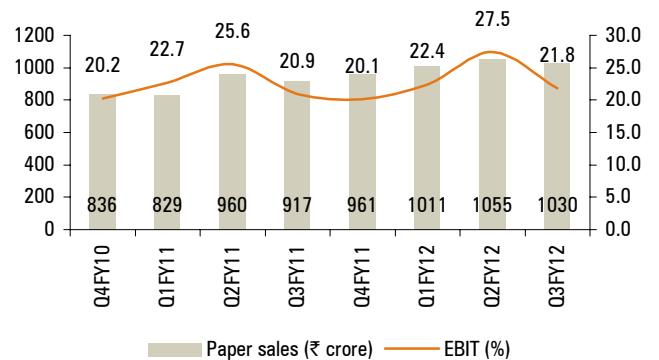
The company has witnessed 9.8% and 12.3% growth in the agri and paper business mainly driven by volumes. Margins in the agri segment remain similar to the previous quarter and improved marginally in the paper business.

Exhibit 9: Agri sales and EBIT trend



Source: Company, ICICIdirect.com Research

Exhibit 10: Paper sales and EBIT trend

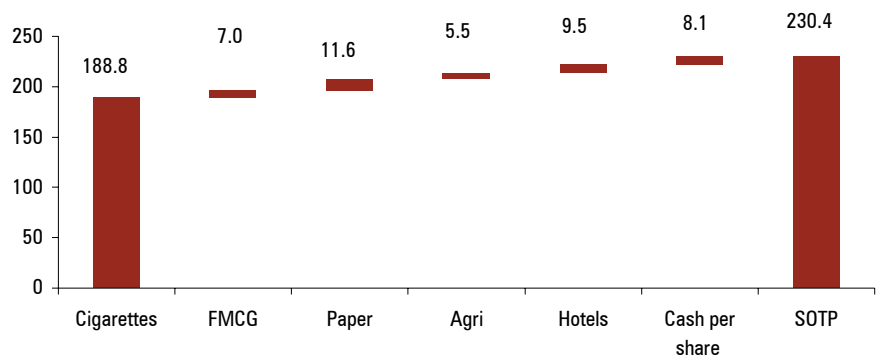


Source: Company, ICICI direct.com Research

Valuation

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Exhibit 11: SOTP valuation (₹ per share)



Source: Company, ICICIdirect.com Research

Financial summary

Profit and loss statement

	(₹ Crore)			
(Year-end March)	FY11	FY12E	FY13E	FY14E
Total operating Income	21,468.3	24,594.6	28,713.4	32,435.5
Growth (%)	16.7	14.6	16.7	13.0
Raw Material Expenses	8,126.5	9,152.7	10,253.8	10862.7
Employee Expenses	1,159.4	1,283.4	1,723.3	2140.7
Marketing Expenses	765.5	423.4	988.8	1297.4
Administrative Expenses	1,569.3	833.3	2,005.8	2400.2
Other expenses	2,393.4	3,894.6	2,839.2	3697.6
Total Operating Expenditure	14,014.1	15,587.4	17,810.8	20,398.7
EBITDA	7,454.1	9,007.2	10,902.7	12,542.4
Growth (%)	18.1	20.8	21.0	15.0
Depreciation	656.0	675.8	734.6	809.6
Interest	48.1	59.8	42.7	42.8
Other Income	518.2	789.5	543.6	593.6
PBT	7,268.2	9,061.2	10,668.9	12283.7
Others				
Total Tax	2,280.6	2,857.8	3,399.1	3906.2
PAT	4,987.6	6,203.4	7,269.8	8,377.5
Growth (%)	22.8	24.4	17.2	15.2
EPS (₹)	6.4	8.0	9.4	10.8

Source: Company, ICICIdirect.com Research

Balance sheet

	(₹ Crore)			
(Year-end March)	FY11	FY12E	FY13E	FY14E
Liabilities				
Equity Capital	773.8	779.6	779.6	779.6
Reserve and Surplus	15179.5	16695.1	18601.0	21569.5
Total Shareholders funds	15953.3	17474.7	19380.7	22349.2
Total Debt	99.2	99.2	69.2	79.2
Deferred Tax Liability	801.9	751.9	711.9	691.9
Minority Interest / Others				
Total Liabilities	16854.3	18325.8	20161.7	23120.2
Assets				
Gross Block	12,765.8	14,265.8	15,965.8	17765.82
Less: Acc Depreciation	4,416.3	5,092.0	5,826.7	6,636.2
Net Block	8,349.6	9,173.8	10,139.2	11,129.6
Capital WIP	1,333.4	1,433.4	1,533.4	1,533.4
Total Fixed Assets	9,683.0	10,607.2	11,672.6	12,663.0
Investments	5,554.7	5,754.7	5,974.7	6,224.7
Inventory	5,267.5	6,706.1	7,225.6	8,770.0
Debtors	907.6	1,263.9	1,548.0	1,777.3
Loans and Advances	1,418.1	1,495.5	1,894.6	1,997.7
Other Current Assets	347.5	380.9	410.1	433.2
Cash	2,238.8	1,974.9	2,609.6	4,083.4
Total Current Assets	10,179.5	11,821.3	13,687.8	12,832.0
Creditors	4457.9	4457.9	5294.0	6753.7
Provisions	4,104.8	4,669.7	5,294.0	6,078.3
Total Current Liabilities	8,562.8	9,858.3	11,176.3	12,832.0
Net Current Assets	1,616.7	1,963.0	2,511.5	4,229.6
Others Assets	0.0	1.0	3.0	3.0
Application of Funds	16,854.4	18,325.8	20,161.7	23,120.3

Source: Company, ICICIdirect.com Research

Cash flow statement

	(₹ Crore)			
(Year-end March)	FY11	FY12E	FY13E	FY14E
Profit after Tax	4,987.6	6,203.4	7,269.8	8,377.5
Add: Depreciation	656.0	675.8	734.6	809.6
(Inc)/dec in Current Assets	-939.1	-1,905.6	-1,231.9	-1,900.0
Inc/(dec) in CL and Provisions	513.7	1,295.5	1,318.0	1,655.7
Others				
CF from operating activities	5,218.2	6,269.1	8,090.6	8,942.8
(Inc)/dec in Investments	-2,889.1	172.2	-200.0	-220.0
(Inc)/dec in Fixed Assets	-1,357.0	-1,166.8	-1,650.0	-1,840.0
Others	0.0	0.0	-1.0	-2.0
CF from investing activities	-994.6	-1,851.0	-2,062.0	-2,070.0
Issue/(Buy back) of Equity	392.0	5.8	0.0	0.0
Inc/(dec) in loan funds	-69.8	-8.5	0.0	-30.0
Dividend paid & dividend tax	-4,001.5	-4,687.8	-5,363.9	-5,409.0
Inc/(dec) in Sec. premium	511.8	0.0	0.0	0.0
Others	-1.1	0.0	0.0	0.0
CF from financing activities	-3,107.2	-4,682.0	-5,393.9	-5,399.0
Net Cash flow	1,116.4	-263.9	634.7	1,473.8
Opening Cash	1,122.4	2,238.8	1,974.9	2,609.6
Closing Cash	2,238.8	1,974.9	2,609.6	4,083.4

Source: Company, ICICIdirect.com Research

Key ratios

(Year-end March)	FY11	FY12E	FY13E	FY14E
Per share data (₹)				
EPS	6.4	8.0	9.4	10.8
Cash EPS	7.3	8.9	10.3	11.9
BV	20.6	22.6	25.0	28.9
DPS	4.4	5.2	6.0	6.0
Cash Per Share	2.9	2.6	3.4	5.3
Operating Ratios (%)				
EBITDA Margin	34.7	36.6	38.0	38.1
PBT / Total Operating income	34.3	37.3	37.8	37.9
PAT Margin	23.2	25.2	25.3	25.4
Inventory days	4.3	4.1	4.1	4.1
Debtor days	23.3	19.2	18.3	18.3
Creditor days	5.2	4.7	4.7	4.8
Return Ratios (%)				
RoE	31.3	35.5	37.5	37.5
RoCE	42.3	47.4	52.3	52.3
RoIC	31.9	34.9	39.5	42.0
Valuation Ratios (x)				
P/E	31.2	25.1	21.4	18.6
EV / EBITDA	20.0	16.6	13.7	11.7
EV / Net Sales	7.1	6.2	5.3	4.5
Market Cap / Sales	7.3	6.4	5.5	4.8
Price to Book Value	9.7	8.9	8.0	7.0
Solvency Ratios				
Debt/EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	1.2	1.2	1.2	1.3
Quick Ratio	0.9	1.0	1.0	1.0

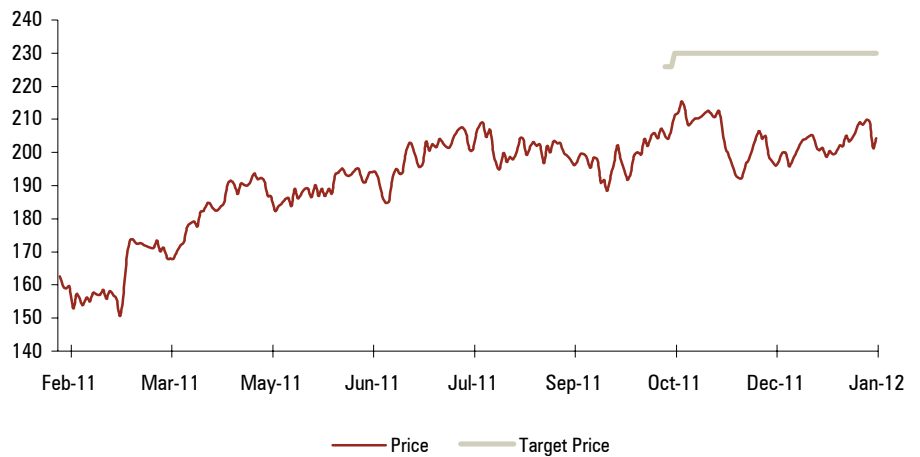
Source: Company, ICICIdirect.com Research

ICICIdirect.com Coverage Universe

					Sales (₹ crore)	EPS (₹)	PE (x)	EV/E (x)	RoNW (%)	RoCE (%)
Asian Paints										
Idirect Code	ASIPAI	CMP	2827	FY11	7706.2	87.9	32.2	22.8	57.6	54.5
		Target	3390	FY12E	9111.1	100.0	28.3	20.7	49.3	49.4
MCap	29898.3	Upside	20%	FY13E	10011.7	127.6	22.2	16.4	51.2	49.5
Dabur India										
Idirect Code	DABIND	CMP	95	FY11	4077.4	3.3	29.1	21.1	48.9	41.1
		Target	120	FY12E	5076.1	3.7	25.5	19.3	38.9	32.2
MCap	17180.7	Upside	27%	FY13E	5895.4	4.7	20.1	16.0	35.5	32.0
ITC										
Idirect Code	ITC	CMP	204	FY11	21167.6	6.4	31.7	20.0	31.3	42.3
		Target	230	FY12E	24279.8	8.0	25.4	16.6	35.5	47.4
MCap	164048.7	Upside	13%	FY13E	28250.3	9.4	21.7	13.7	37.5	52.3
Jyothy Laboratories										
Idirect Code	JYOLAB	CMP	173	FY11	599.8	6.8	25.3	11.7	12.3	9.6
		Target	136	FY12E	600.1	-0.1	NA	37.6	8.6	1.9
MCap	1145.0	Upside	-21%	FY13E	632.0	1.2	148.7	24.0	8.9	3.6
Kansai Nerolac										
Idirect Code	GOONER	CMP	868	FY11	2138.7	41.6	20.9	16.2	22.5	24.1
		Target	1048	FY12E	2580.9	42.3	20.5	12.9	20.2	25.1
MCap	4677.8	Upside	21%	FY13E	2891.7	48.3	18.0	11.4	18.5	23.2
Marico										
Idirect Code	MARIN	CMP	150	FY11	3128.3	4.7	32.2	23.9	36.5	29.1
		Target	165	FY12E	4035.6	5.2	29.1	20.4	30.0	24.8
MCap	9218.4	Upside	10%	FY13E	4729.8	6.6	22.7	16.2	29.5	28.8

Source: Company, ICICIdirect.com Research

Exhibit 12: Recommendation History



Source: Company, ICICIdirect.com Research

Exhibit 13: Recent releases

Date	Event	CMP	Target Price	Rating
20-Oct-11	Initiating Coverage	205	226	Buy
25-Oct-11	Q2FY12 Result Update	210	230	Buy

Source: Company, ICICIdirect.com Research

RATING RATIONALE

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Strong Buy: > 15%/20% for large caps / midcaps, respectively, with high conviction;

Buy: > 10%/15% for large caps / midcaps, respectively;

Hold: Up to +/-10%;

Sell: -10% or more;

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