

09 January, 2012

SECTOR REPORT

FMCG SECTOR

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Selective Picks



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Executive Summary

Selective Picks

- India's past 5 years average GDP growth was at ~8.6% which was way ahead of ~5.5% GDP growth in the last 5 decades. India's key states Maharashtra, UP, AP, TN, West Bengal and Gujarat have contributed well towards India's robust growth. These 6 states contribute >50% to the Indian GDP and grew by >13% in the past 5 years.
- Urban India growth is marked by rise in urban population mix which stands at 30% as compared to 18% in 1960. Besides, there is a significant expansion in upper urban income mix to 36% in 2010 from 17% in 2002. Such favourable transformation is supporting FMCG companies from premiumisation perspective.
- Rural market is being driven by growth in non-agriculture income, better MSP rates, higher education and the Government's emphasis on rural development programmes. Large rural population provides consistent volume growth for FMCG companies.
- FMCG categories, with low per capita and low penetration level i.e. skin care, shampoo, oral care, deodorant and packaged juices are the opportunities for FMCG companies. While categories like soaps and detergents which have high penetration level can also show healthy growth due to their low per capita consumption.
- International business is an opportunity for the long term growth potential for domestic FMCG companies. Entrance into new geographies provides growth scope for the established brands/power brands. However, we expect initial cost would impact the profitability of domestic players in the near term.
- We evaluate the competitive strength of FMCG companies based on our 'RIVER' analysis through which HUL, Nestle, Dabur and ITC are the foremost rankers.

Sector Valuation

FMCG sector, in the current global financial turmoil, converted into a preferable bet for the investors which resulted in 35% outperformance of BSE FMCG over BSE-Sensex in the past 12 months. FMCG sector trades at ~27x P/E on 12-month forward earnings which is ~13% higher than its past 5 years median P/E. FMCG sector valuations are at 118% premium over BSE-Sensex (above +2 standard deviation) as compared to the 5 year average premium of 70%. FMCG valuations are very expensive and we believe going forward growth in net earnings would play a key role in the stocks' performance.

At the current juncture, we prefer stocks on their relative traits where earnings growth and valuations both are at attractive level.

Recommendation

We initiate coverage on ITC (BUY) and HUL (REDUCE) while update on Nestle India (SELL), Dabur (ACCUMULATE), Colgate (REDUCE), Marico (REDUCE) and Jyothy Labs (BUY).

Sector Summary *

KEY FINANCIALS

| Company | Mcap (Rs bn) | Reco | Net Sales (Rs mn) | | EPS (Rs) | | P/E (x) | | TP (Rs) | Potential Upside |
|-------------|--------------|------------|-------------------|---------|----------|-------|---------|-------|---------|------------------|
| | | | FY13E | FY14E | FY13E | FY14E | FY13E | FY14E | | |
| ITC | 1,563 | BUY | 309,394 | 355,647 | 9.4 | 10.9 | 21.5 | 18.6 | 233 | 15.3% |
| HUL | 857 | REDUCE | 261,492 | 298,550 | 13.5 | 15.7 | 29.3 | 25.2 | 371 | (6.5)% |
| Nestle # | 399 | SELL | 94,350 | 117,129 | 118.3 | 146.3 | 35.0 | 28.3 | 3,618 | (12.7)% |
| Dabur | 172 | ACCUMULATE | 59,628 | 69,055 | 4.6 | 5.5 | 21.7 | 18.0 | 109 | 10.1% |
| Colgate | 133 | REDUCE | 31,276 | 36,130 | 38.6 | 44.7 | 25.4 | 22.0 | 937 | (4.5)% |
| Marico | 93 | REDUCE | 45,905 | 53,600 | 6.3 | 7.9 | 24.1 | 19.1 | 144 | (4.6)% |
| Jyothy Labs | 13 | BUY | 13,754 | 15,678 | 12.4 | 15.0 | 12.9 | 10.6 | 212 | 32.5% |

* All stocks prices based on 6th January 2012 closing # Dec. ending company

ITC (CMP Rs202, TP Rs233, Reco- BUY with an upside of 15%)**Investment Rationale**

- ITC's cigarette dominance would persist on the back of extensive cigarette portfolio, large distribution network, consumers' stickiness towards its brands and appropriate backward integration. We expect ITC's strong pricing power would help it in maintaining the healthy growth.
- We believe ITC's cigarette business growth would drive the overall profitability. Better cigarette revenue mix, higher operational efficiency and cigarette pricing power would expand PBIT/stick to 103paise by FY14E from 71paise in FY11.
- We expect ITC's non cigarette business to show 17% CAGR during FY11-14E as compared to 13% CAGR during FY08-11E. FMCG business has grown 15x in the past 8 years through consistent entrance into new segments and aggressive marketing strategy. We expect FMCG business to clock 20% CAGR during FY11-14E owing to better foothold of the existing portfolio and consistent investment in innovation. Paperboard and Agribusiness would maintain their robust growth and we expect 16% and 13% CAGR during FY11-14E respectively. We expect non cigarette business to contribute 21% of ITC's total PBIT in FY14E as compared to 19% in FY11.

VALUATIONS AND RECOMMENDATION

We value ITC using DCF methodology and arrive at a target price of Rs233. We believe relative valuation is not feasible as there is no appropriate comparable for ITC. The stock has 15% upside potential hence we initiate ITC with 'BUY' rating. ITC has high dependence on cigarette business hence any significant change in the govt. regulation on cigarette can lead to change in our estimates.

HUL (CMP Rs397, TP Rs371, Reco- REDUCE with a downside of 6%)**Investment Rationale**

- The higher involvement of top management at the field level, setting up of aggressive sales targets and expansion in distribution network are the indicators for business development going forward. We expect it would help in delivering better revenue going forward which HUL was missing in previous several years. However, as HUL has already reduced A&P (% of sales) spending during H1FY12 further control is limited. A&P (% of sales) spending substantially declined during H1FY12 to 11.5% v/s 14% in FY11. We expect sales and net earnings to show 14.1% and 16.6% CAGR during FY11-14E as compared to 12.4% and 7% during FY08-11 respectively.
- As per our 'RIVER' analysis, skin care has the highest ranking in terms of competitive positioning among HUL's other categories. We believe skin care contributes 38% and 50% of sales and profitability of Personal Care business.
- The performance of 'Soaps and Detergent' segment in the past 3 quarters was very encouraging. The segment has not only shown better volume growth but simultaneously improved the profitability profile too. HUL in FY11 reported lowest PBIT margin of 9.5% which we believe was largely due to down trading in the detergent products. We expect segment profitability would improve from FY11 level however, achieving historical mid teen margin seems difficult due to high competition from P&G, Rohit Surfactant (Ghari), Godrej Consumers, Wipro, Reckitt Benkiser and ITC which would limit the profitability upside for the segment.

VALUATIONS AND RECOMMENDATION

We value HUL at P/E of 28x (12-month forward earnings) which is ~10% premium to the FMCG sector valuations and ~8% higher than its past three years median P/E. We arrive at a target price of Rs371 which is 6% down from the CMP. Hence, we initiate HUL with a 'REDUCE' rating.

Nestle India (CMP Rs4,143, TP Rs3,618, Reco- SELL with a downside of 13%)**Investment Rationale**

- Nestle India (Nestle) underperformed BSE FMCG by 7% during last 6 months but its valuations are still very expensive. Nestle's valuations premium has come down to 31% from 45% during this time. Considering pressure on Nestle's EBITDA margin, reduction in return ratios and improvement in performance of peers, we argue that Nestle's P/E premium should reduce further.
- Nestle reported 9% volume growth during 9MCY11 which is the slowest growth in the past 5 years. Milk Product & Nutrition, Prepared Dishes and Chocolates registered slower volume growth of 4%, 15% and 1% while Beverages registered volume contraction during 9MCY11. Rising competition and sharp price hike on all the key brands were the key reason for slower volume growth performance.
- We believe Nestle's EBITDA margin would be lower by 90bps during CY10-13E on account of limited scope of further price hike and higher marketing spending for retaining leadership position.

VALUATIONS AND RECOMMENDATION

Nestle's monopoly in Maggi noodles would be difficult to maintain for long time post the entrance of big players. Competition is rising in almost all the categories while Nestle is expanding capacities which would force the company to maintain volume market share. Therefore, we expect pressure on pricing power of key brands. Nestle trades at a ~31% premium to the FMCG sector and we argue that this premium would narrow. We peg 30x P/E multiple on 12-months forward earnings and revise our TP to Rs3,618 (Rs3,578 earlier). We maintain 'SELL' rating on the stock.

Dabur (CMP Rs99, TP Rs109, Reco- ACCUMULATE with an upside of 10%)**Investment Rationale**

- Dabur India's (Dabur) rural segment is facing slowdown which impacted its H1FY12 performance. Consolidated net sales has shown robust 31% growth led by its recent acquisitions (Hobi Kozmetic and Namaste Group), excluding the same, sales grew at a slower pace of 13% during H1FY12. Hair oil and food categories were the exception and clocked strong growth of 21% and 30% during H1FY12 while skin care, health supplement, oral care and home care displayed muted growth of 7%, 4%, 9% and 10% growth respectively during H1FY12. We have not witnessed the recovery of shampoo business during H1FY12 which posted 24% YoY decline due to sharp price cut by its peers.
- Dabur's international business (excluding recent acquisitions) displayed 18% growth in H1FY12 which was also lower as compared to the past three years' >25% history. GCC, Egypt and Nigeria continue to perform well and registered 27%, 27% and 36% growth during H1FY12 respectively.
- We expect EBITDA margin during FY12-14E would be lower than FY10-11 as we believe higher contribution of low margin acquisitions. Hobi Kozmetic and Namaste Group fetch low profitability profile which would change the overall profitability profile of the company. We expect Hobi and Namaste would combined contribute 13% and 10% of consolidated sales and EBITDA of FY14.

VALUATIONS AND RECOMMENDATION

Dabur's strong presence in the domestic market through its robust portfolio and regular entrance in geographies enabled it to maintain its high growth momentum. We retain our 25x multiple on 12-month forward earnings and derive TP of Rs109 (earlier Rs107). We maintain our 'ACCUMULATE' rating on the stock.

Colgate (CMP Rs981 TP Rs937, Reco- REDUCE with a downside of 4%)**Investment Rationale**

- In our sector thesis we mentioned that oral care is one of the personal categories which has low weightage in the monthly household budget therefore its price sensitivity is low. We witnessed this in the Colgate's H1FY12 performance in which volume growth was maintained despite taking price hike on most of the brands.
- We believe oral care market is set for premiumisation which would lead to better price growth for Colgate in FY13 and FY14.
- Colgate is the only company in FMCG space that increased its A&P spendt in H1FY12 while most of the other players were protecting profitability through lower A&P spends. Colgate's aggression was to expand its market share as well as to promote sensitive oral care segment. We believe Colgate would continue to spend high on A&P in FY13 and FY14 to maintain its double digit volume growth.
- We increase our target multiple from 24x to 25x on 12-month forward earnings as Colgate's aggressive marketing efforts would further strengthen its position in the oral care industry.

VALUATIONS AND RECOMMENDATION

We expect volume growth to sustain owing to Colgate's regular product launches, higher rural focus and continued dental awareness programmes. We increase our target multiple from 24x to 25x on 12-month forward earnings and arrive at a TP of Rs937 (earlier Rs878). We upgrade our recommendation to 'REDUCE' from 'SELL'.

Marico (CMP Rs151, TP Rs144, Reco- REDUCE with a downside 5%)**Investment Rationale**

- Marico's 29% sales growth in H1FY12 is not sustainable in our opinion. Marico has already taken sharp price hike on Parachute which limits the scope of further price hike. Parachute volume growth at ~17% during H1FY12 was ahead of our expectation and we expect it to taper down.
- We believe softening of input prices would be set off by higher A&P spend. New product launches and requirement of higher marketing efforts in the international business would force Marico to escalate A&P (% of sales) spending by 200-250bps going forward from 9.7% in H1FY12.
- Slower growth in depreciation and interest cost would translate ~19% EBITDA CAGR into ~22% net earnings CAGR during FY11-14E.

VALUATIONS AND RECOMMENDATION

On account of limited product portfolio, higher exposure to commodity prices and moderate scope for further price hike on key brands, we maintain Marico's P/E discount over FMCG sector. We retain our 24x multiple on 12-month forward earnings and raise TP to Rs144 (earlier Rs141). We maintain our 'REDUCE' rating on the stock.

Jyothy Labs (CMP Rs160, TP Rs212, Reco- BUY with an upside of 33%)**Investment Rationale**

- We believe Jyothy's standalone low EBITDA margin in H1FY12 is not sustainable going forward. Ujala Supreme contributes >70% of the standalone EBITDA and post the stability in the sales distribution we expect better business from this front. Ujala Supreme sales in H1FY12 was down by ~10% which why overall profitability was under pressure. We don't see reasons for pressure on its consumer demand.
- Improvement in Henkel's profitability since acquisition has been encouraging. However, the key challenge will be to harness the synergy by improving the sales of Henkel brands. Other thing to watch out for will be monetization of idle assets available with Henkel which will help the company in reducing the interest burden.
- We remain positive on the long term growth potential of the combined business. The combined entity represents several synergies i.e. better revenue mix, optimum rural/urban ratio and cost saving on distribution. Jyothy now has multiple drivers to run the business and better execution can reduce timing of turnaround in Henkel India.

VALUATIONS AND RECOMMENDATION

Jyothy's slack performance in the past three quarters has resulted into 40% decline in the stock price in the past 12 months. We believe investor's visibility in the business would be clearer with each quarter's better performance. We maintain 16x multiple to Jyothy's FY13 earnings and add Rs12/share NPV on tax saving of Rs1.2bn at 12% discount rate. We maintain our 'BUY' recommendation with TP of Rs212.

Exhibit 1 - Financial Summary

| (Rs mn) | Sales | | | Sales CAGR | EBITDA Margin | | | EBITDA CAGR | Adjusted PAT | | | EPS (Rs) | | | EPS CAGR |
|-----------------|---------|---------|---------|------------|---------------|-------|-------|-------------|--------------|----------|--------|----------|-------|-------|----------|
| | FY12E | FY13E | FY14E | | FY11-14E | FY12E | FY13E | | FY14E | FY11-14E | FY12E | FY13E | FY14E | FY12E | |
| Companies | | | | | | | | | | | | | | | |
| ITC | 267,694 | 309,394 | 355,647 | 16.7% | 34.2% | 34.5% | 34.5% | 18.1% | 61,963 | 72,800 | 84,095 | 8.0 | 9.4 | 10.9 | 19.1% |
| HUL | 229,960 | 261,492 | 298,550 | 14.1% | 14.2% | 14.5% | 14.7% | 17.4% | 25,225 | 29,229 | 33,987 | 11.7 | 13.5 | 15.7 | 16.6% |
| Nestle # | 76,556 | 94,350 | 117,129 | 23.0% | 19.8% | 19.5% | 19.2% | 21.1% | 9,648 | 11,405 | 14,102 | 100.1 | 118.3 | 146.3 | 19.7% |
| Dabur | 51,672 | 59,628 | 69,055 | 18.8% | 17.0% | 17.3% | 17.6% | 17.0% | 6,507 | 7,935 | 9,560 | 3.7 | 4.6 | 5.5 | 18.7% |
| Colgate | 26,739 | 31,276 | 36,130 | 16.3% | 21.9% | 22.5% | 22.7% | 16.5% | 4,449 | 5,244 | 6,072 | 32.7 | 38.6 | 44.7 | 14.5% |
| Marico | 39,243 | 45,905 | 53,600 | 19.4% | 12.2% | 12.5% | 12.9% | 18.8% | 3,108 | 3,853 | 4,863 | 5.1 | 6.3 | 7.9 | 21.9% |
| Jyothy Labs | 11,675 | 13,754 | 15,678 | 36.0% | 9.7% | 12.9% | 12.8% | 39.7% | 452 | 1,000 | 1,212 | 5.6 | 12.4 | 15.0 | 20.5% |
| GCPL* | 45,720 | 55,298 | 64,165 | 20.5% | 17.9% | 18.3% | 18.6% | 16.8% | 5,781 | 7,159 | 8,828 | 17.7 | 22.0 | 27.3 | 22.3% |
| GSK Consumers* | 27,098 | 31,933 | 36,721 | 16.6% | 17.0% | 17.5% | 18.3% | 10.7% | 3,619 | 4,350 | 5,116 | 86.0 | 102.5 | 120.0 | 19.5% |
| Emami Ltd* | 15,210 | 18,071 | 21,526 | 17.4% | 19.6% | 20.3% | 21.1% | 12.9% | 2,702 | 3,251 | 3,905 | 17.9 | 21.5 | 25.8 | 20.2% |
| Britannia Ind.* | 53,367 | 63,473 | 74,274 | 17.1% | 5.8% | 6.2% | 6.5% | 17.0% | 1,906 | 2,423 | 3,260 | 16.0 | 20.3 | 27.3 | 39.3% |

Source: PINC Research, Company * Bloomberg Consensus # Dec. ending company

Exhibit 2 - Valuation Summary

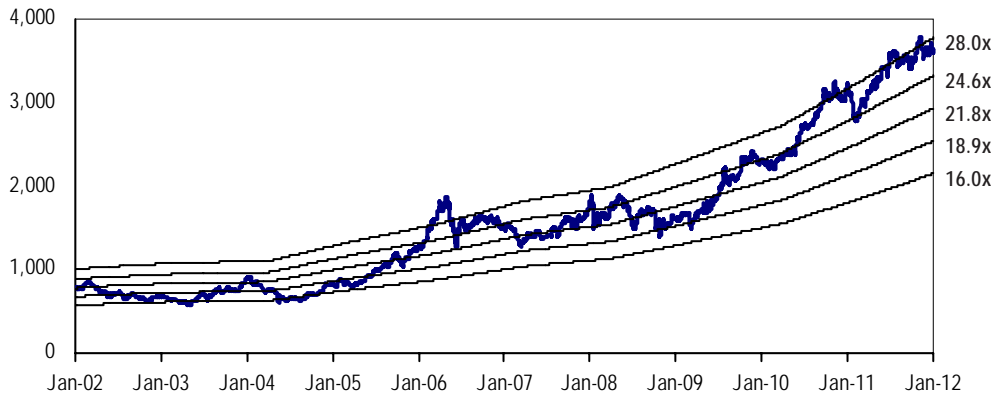
| Companies | Mkt. Cap (Rs bn) | CMP (Rs) | Reco | TP (Rs) | O/S Shares (mn) | EV/Sales (x) | | | EV/EBITDA (x) | | | P/E (x) | | | ROE | | |
|-----------------|------------------|----------|------------|---------|-----------------|--------------|-------|-------|---------------|-------|-------|---------|-------|-------|--------|--------|-------|
| | | | | | | FY12E | FY13E | FY14E | FY12E | FY13E | FY14E | FY12E | FY13E | FY14E | FY12E | FY13E | FY14E |
| ITC | 1,563 | 202 | BUY | 233 | 7,738 | 5.6 | 4.7 | 4.0 | 16.2 | 13.6 | 11.6 | 25.2 | 21.5 | 18.6 | 31.4% | 30.8% | 30.0% |
| HUL | 857 | 397 | REDUCE | 371 | 2,160 | 3.6 | 3.1 | 2.7 | 25.1 | 21.3 | 18.2 | 34.0 | 29.3 | 25.2 | 75.4% | 73.0% | 73.3% |
| Nestle # | 399 | 4,143 | SELL | 3,618 | 96 | 5.2 | 4.3 | 3.4 | 26.5 | 21.9 | 17.8 | 41.4 | 35.0 | 28.3 | 80.3% | 70.8% | 66.6% |
| Dabur | 172 | 99 | ACCUMULATE | 109 | 1,741 | 3.3 | 2.9 | 2.4 | 19.7 | 16.5 | 13.7 | 26.5 | 21.7 | 18.0 | 35.4% | 32.7% | 30.1% |
| Colgate | 133 | 981 | REDUCE | 937 | 136 | 4.8 | 4.0 | 3.5 | 21.8 | 18.0 | 15.2 | 30.0 | 25.4 | 22.0 | 103.2% | 102.8% | 97.3% |
| Marico | 93 | 151 | REDUCE | 144 | 614 | 2.5 | 2.0 | 1.7 | 20.1 | 16.3 | 13.1 | 29.8 | 24.1 | 19.1 | 26.7% | 26.2% | 26.2% |
| Jyothy Labs | 13 | 160 | BUY | 212 | 81 | 1.5 | 1.2 | 1.0 | 15.7 | 9.5 | 8.0 | 28.6 | 12.9 | 10.6 | 8.5% | 16.9% | 17.9% |
| GCPL* | 126 | 384 | na | na | 327 | 3.2 | 2.7 | 2.3 | 18.1 | 14.7 | 12.4 | 21.7 | 17.5 | 14.1 | 25.1% | 23.7% | 22.6% |
| GSK Consumers* | 105 | 2,491 | na | na | 42 | 3.5 | 3.0 | 2.6 | 20.5 | 16.9 | 14.1 | 29.0 | 24.3 | 20.8 | 32.1% | 32.0% | 31.2% |
| Emami Ltd* | 50 | 330 | na | na | 151 | 3.6 | 3.0 | 2.5 | 18.2 | 14.8 | 11.9 | 18.4 | 15.3 | 12.8 | 25.4% | 23.4% | 21.9% |
| Britannia Ind.* | 53 | 441 | na | na | 119 | 1.1 | 0.9 | 0.8 | 19.2 | 15.2 | 12.5 | 27.6 | 21.7 | 16.2 | 36.9% | 31.9% | 30.1% |

Source: PINC Research, Company * Bloomberg Consensus # Dec. ending company

SECTOR VALUATION

Exhibit 3 - FMCG Sector Rolling P/E

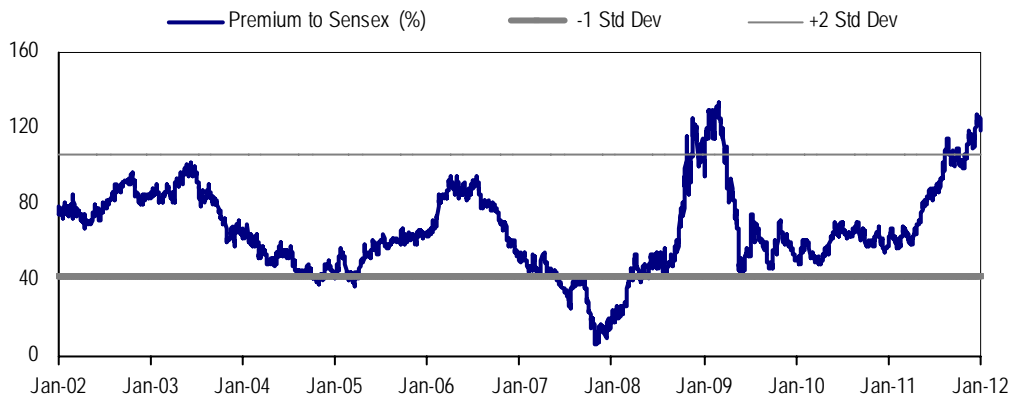
FMCG sector is trading at ~27x P/E (12-month forward earnings) which is the highest in the past 5 years...



Source: PINC Research, Bloomberg

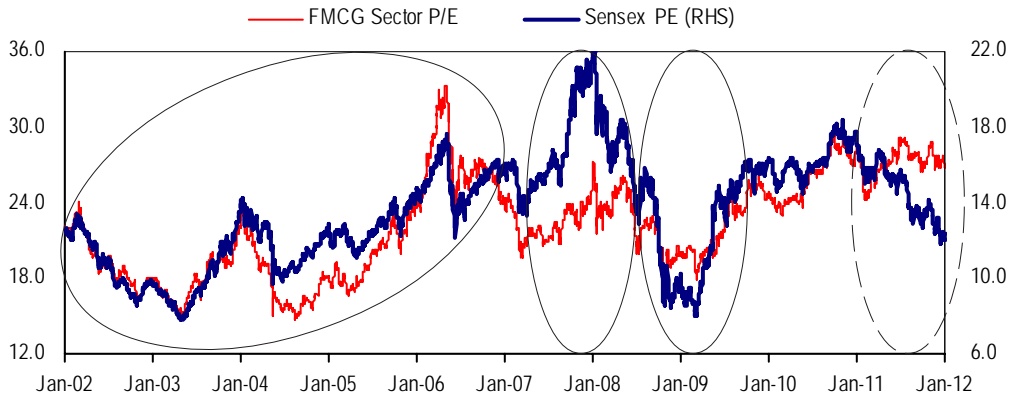
Exhibit 4 - FMCG Sector P/E Premium over BSE Sensex

FMCG sector P/E is at ~118% premium to the Sensex P/E, this is close to the +2 standard deviation of the past 10 years...



Source: PINC Research, Bloomberg

Exhibit 5 - FMCG and BSE Sensex Valuation



Source: PINC Research, Bloomberg

PHASE-WISE FMCG SECTOR VALUATION

2001 to 2006

During this phase, valuations of both FMCG sector and Sensex moved in line and the average FMCG premium over Sensex was at ~70%.

2007

FMCG sector underperformed to the Sensex during 2007 and that reduced the FMCG valuations premium to an average level of ~36%. This premium was lowest in the past 10 years.

2008

Global financial crisis impacted the whole world economy during this period. India's stock market also tempered down and valuations corrected significantly. FMCG sector valuations also corrected however, relative caution was there and valuation fall was lower than the Sensex. FMCG valuations premium slightly expanded to ~56% as compared to 36% in 2007.

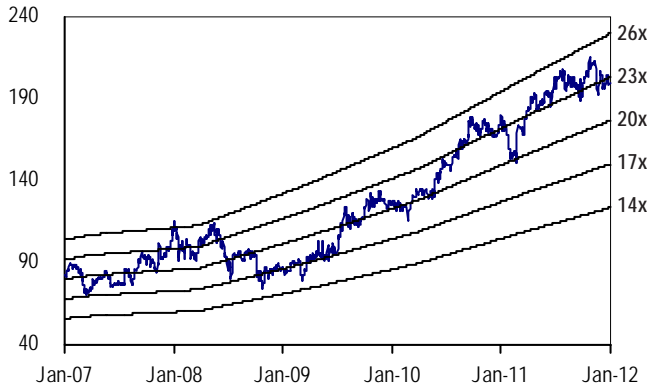
2009 and 2010

During these two years, valuations of both FMCG sector and Sensex moved in line and the average FMCG premium over Sensex was at ~65%.

2011

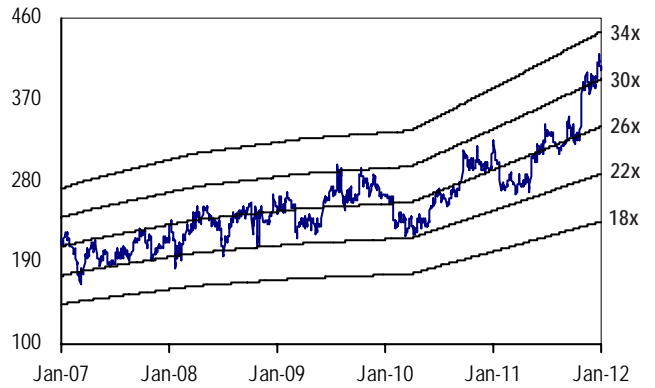
This is a unique situation wherein FMCG sector and Sensex valuations moved in opposite direction and resulted into a high valuation premium for the FMCG sector. Investors' strong preference to the FMCG sector and substantial decline in other sector's valuation has created this situation. FMCG sector trades at ~27x P/E on 12-month forward earnings which is ~13% higher than its past 5 years median P/E. FMCG sector valuations are at 118% premium over BSE-Sensex (above +2 standard deviation) as compared to 5 year average premium of 70%. We believe FMCG valuations are very expensive and going forward growth in net earnings would play a key role in stocks' performance.

Exhibit 6 - ITC 1-Year forward P/E Band



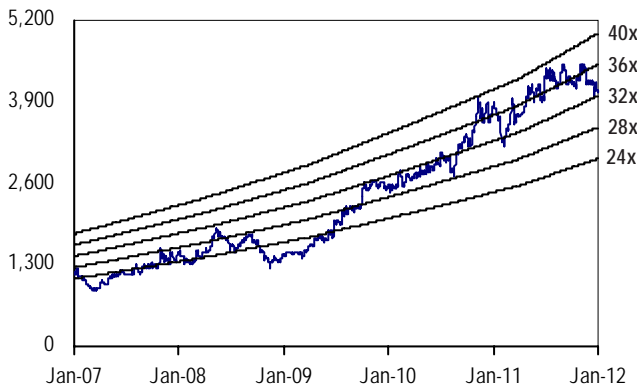
Source: PINC Research, Bloomberg

Exhibit 7 - HUL 1-Year forward P/E Band



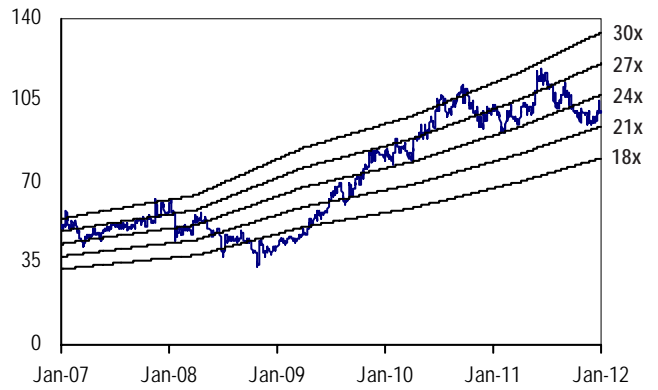
Source: PINC Research, Bloomberg

Exhibit 8 - Nestle India 1-Year forward P/E Band



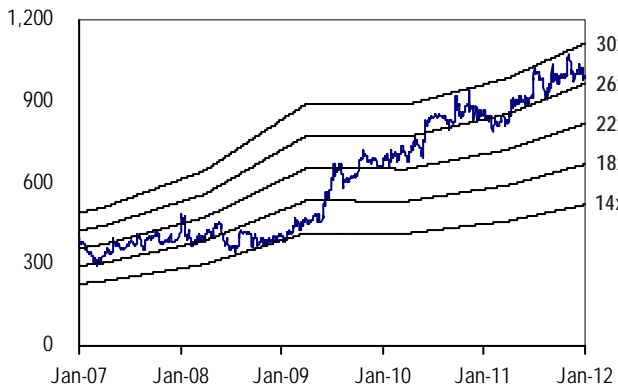
Source: PINC Research, Bloomberg

Exhibit 9 - Dabur 1-Year forward P/E Band



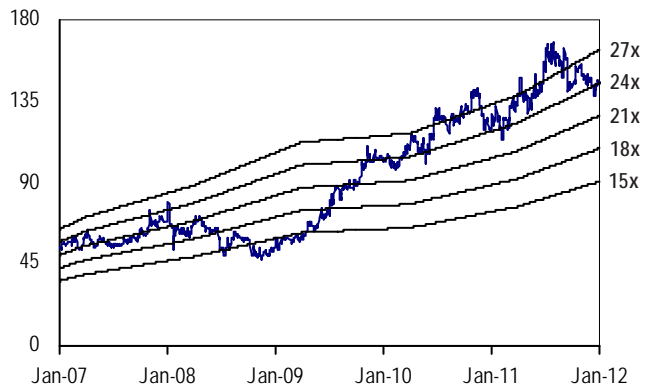
Source: PINC Research, Bloomberg

Exhibit 10 - Colgate Rolling 1-Year forward P/E Band



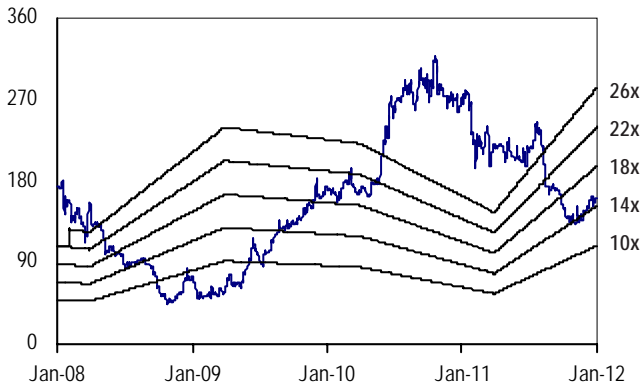
Source: PINC Research, Bloomberg

Exhibit 11 - Marico Rolling 1-Year forward P/E Band



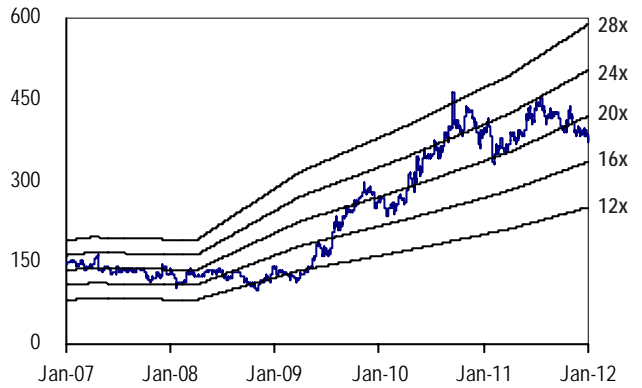
Source: PINC Research, Bloomberg

Exhibit 12 - Jyothy Labs 1-Year forward P/E Band



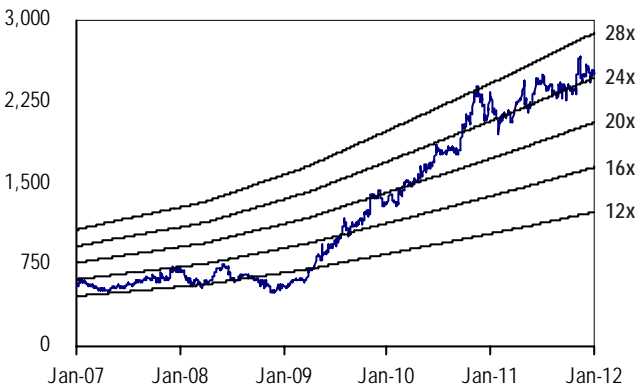
Source: PINC Research, Bloomberg

Exhibit 13 - Godrej Cons. 1-Year forward P/E Band



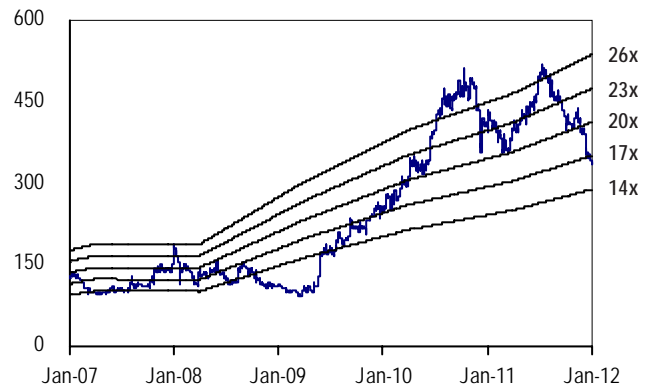
Source: PINC Research, Bloomberg

Exhibit 14 - GSK Consumer 1-Year forward P/E Band



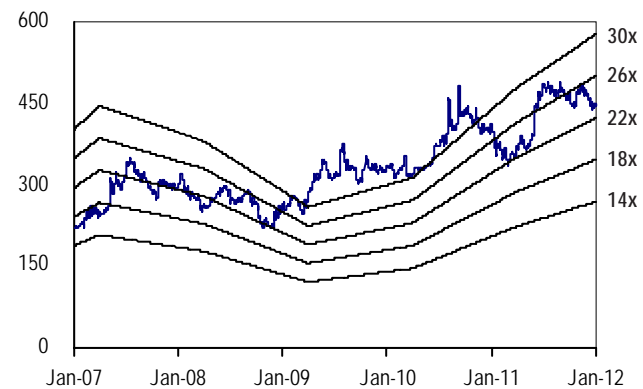
Source: PINC Research, Bloomberg

Exhibit 15 - Emami 1-Year forward P/E Band



Source: PINC Research, Bloomberg

Exhibit 16 - Britannia 1-Year forward P/E Band



Source: PINC Research, Bloomberg

SECTOR DESCRIPTION

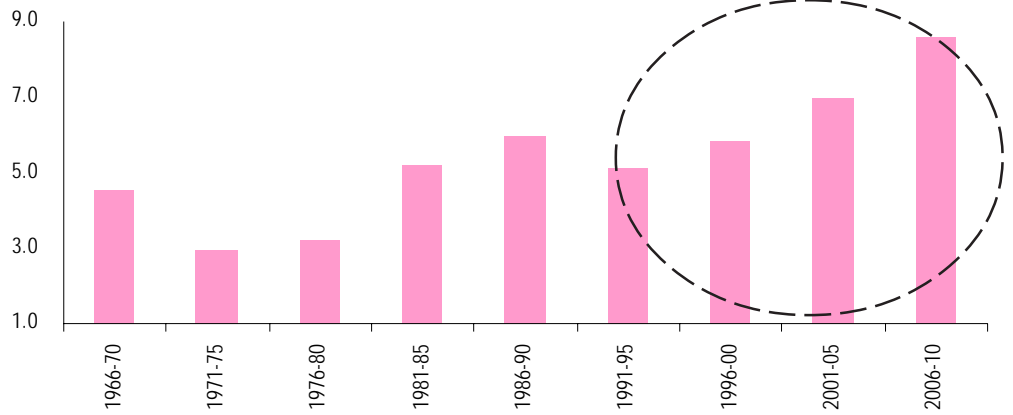
Domestic Market - growth sustainable for long period

India's last 5 years were very significant as the GDP growth achieved highest levels of the last 5 decades. Last 5 years' average GDP growth was at ~8.6% as compared to ~5.5% GDP growth in the last 5 decades.

We observed that India's key states Maharashtra, UP, AP, TN, West Bengal and Gujarat have contributed well towards India's robust growth. These 6 states contribute more than 50% of the Indian GDP and grew by >13% in the past 5 years.

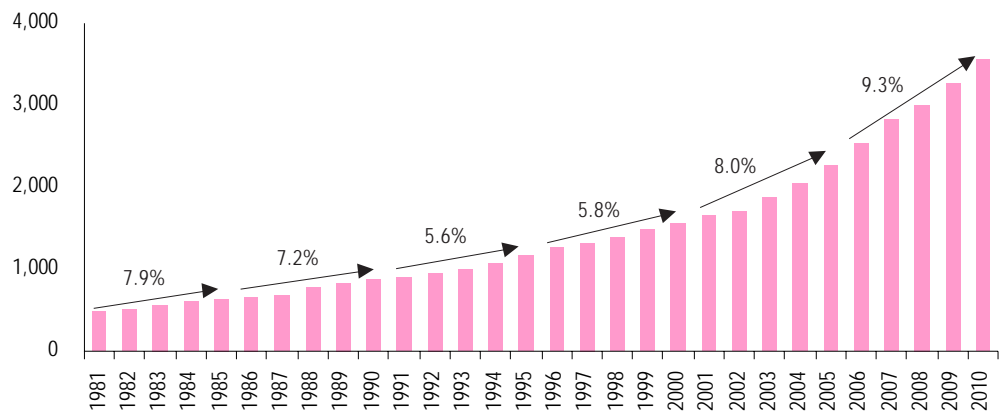
The strong growth across states had helped FMCG companies to deliver >15% growth in the past 5 years. We are positive on the sustainability of strong domestic FMCG growth for long period on account of rise in urban and rural disposable income, credit easing and low per capita consumption & lower penetration level of several categories.

Exhibit 17 - Average GDP growth in past 5 years was highest in past 5 decade



Source: PINC Research, World Bank Data

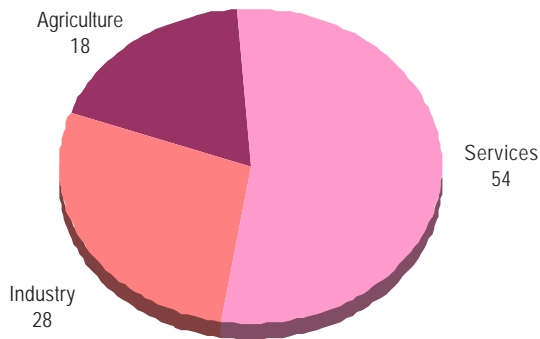
Exhibit 18 - Per Capita GDP - PPP (current international US\$)



Source: PINC Research, World Bank Data

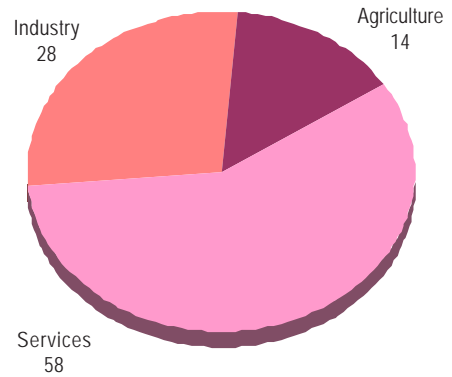
Agriculture provides >50% of the employment although its contribution to the GDP is mere ~14%.

Exhibit 19 - GDP Mix in 2005-06 (%)



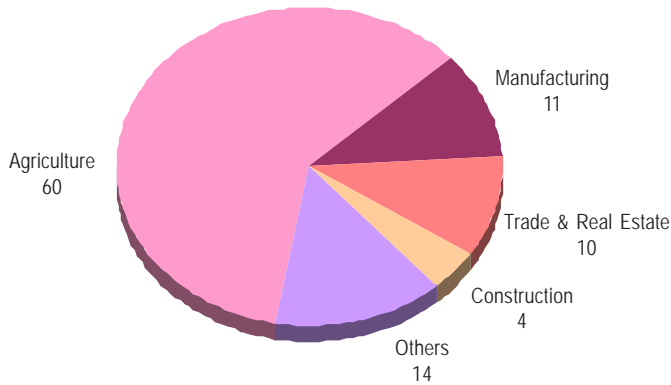
Source: CSO Note: At constant (2004-05) Prices

Exhibit 20 - GDP Mix in 2010-11 (RE) (%)



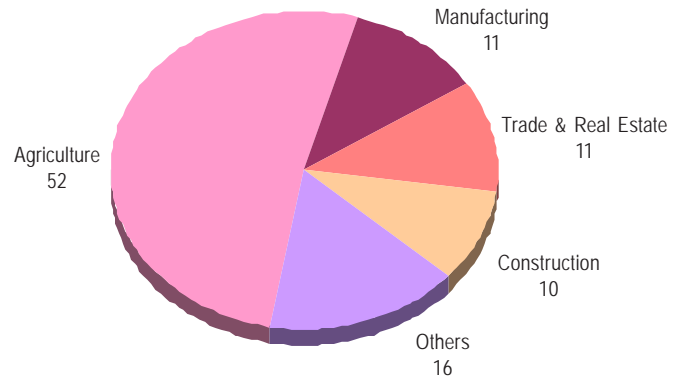
Source: CSO Note: At constant (2004-05) Prices

Exhibit 21 - Sectoral Employment Mix in 2000 (%)



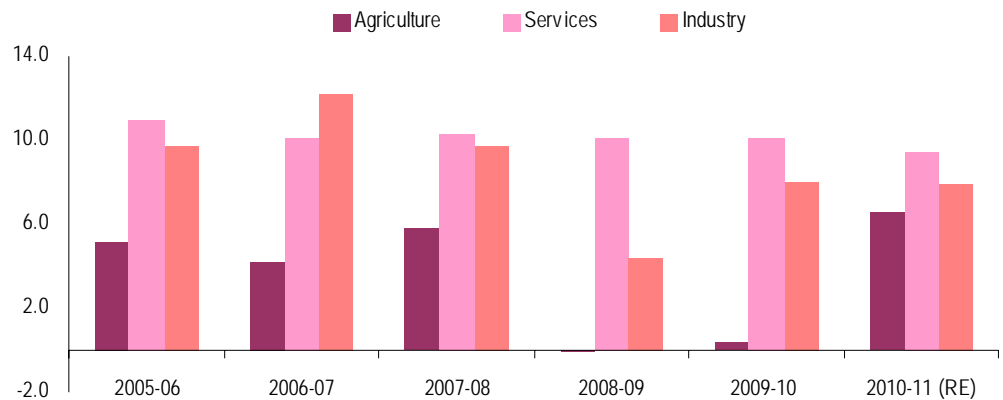
Source: CSO

Exhibit 22 - Sectoral Employment Mix in 2010 (%)



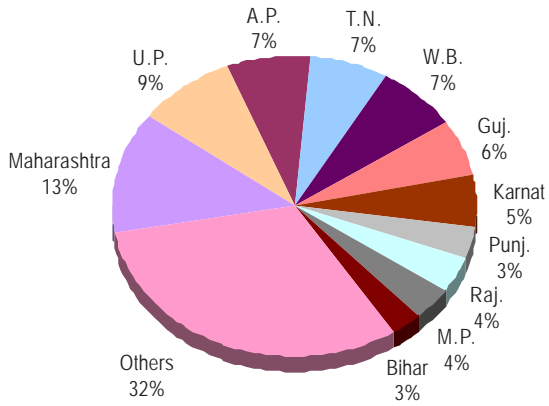
Source: CSO

Exhibit 23 - GDP Growth at Constant (2004-05) Prices



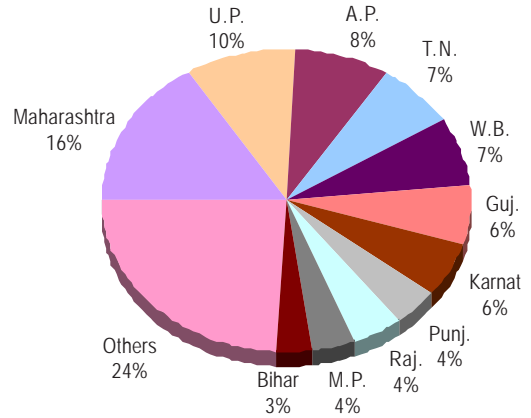
Source: CSO

Exhibit 24 - Mix of Net State Domestic Product (2005)



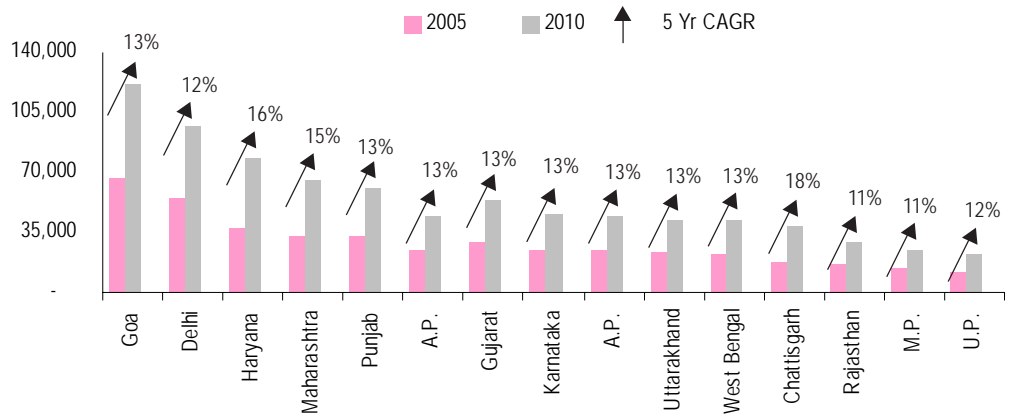
Source: PINC Research, Economic Survey 2011

Exhibit 25 - Mix of Net State Domestic Product (2010)



Source: PINC Research, Economic Survey 2011

Exhibit 26 - Per Capita Net State Domestic Product At Current Prices (Rs)



Source: PINC Research, Economic Survey 2011

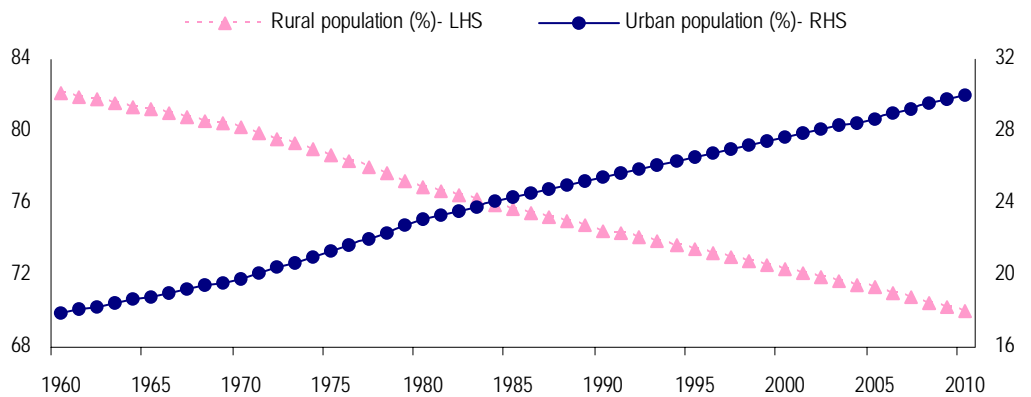
Urban India and FMCG - growth through premiumisation

Higher urban population mix supporting demand

Rising urban population is supporting urban demand for FMCG companies. Urban population mix was 18% in 1960 which increased to 28% in 2000 and then reached to 30% in 2010. The shift in the urban: rural mix has positively changed the dynamics for FMCG companies.

Apart from change in population mix, the urban income distribution has also favourably changed over a period of time. Upper class in the urban income group has increased to ~36% as compared to 17% and 7% in 2002 and 1996 respectively.

Exhibit 27 - Change in Rural: Urban Mix (%)

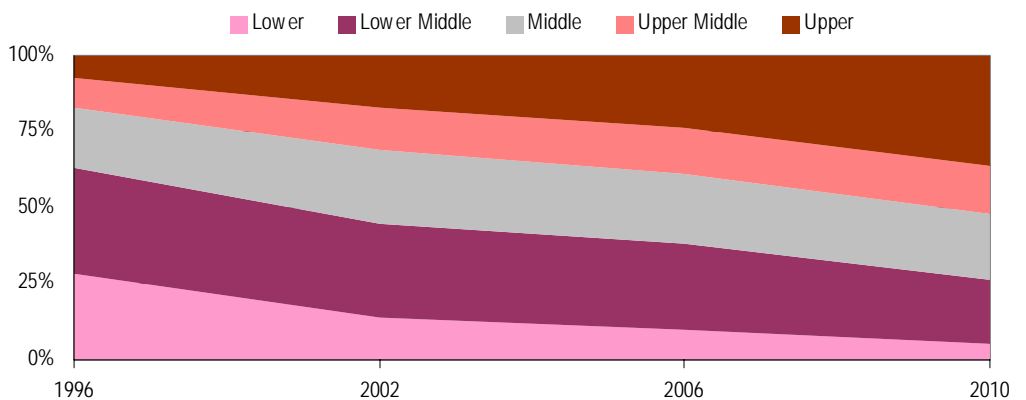


Source: PINC Research, World Bank

Growth through premiumisation

Rise in urban population couple with improvement in urban income mix is positive for FMCG companies. Urban market has higher appetite for premiumisation. Apart from the better value growth in the urban market, FMCG companies also enjoy launching innovative premium products.

Exhibit 28 - Urban Income Distribution (%)



Upper class contributes >36% as compared to ~17% in 2002 and ~7% in 1996...

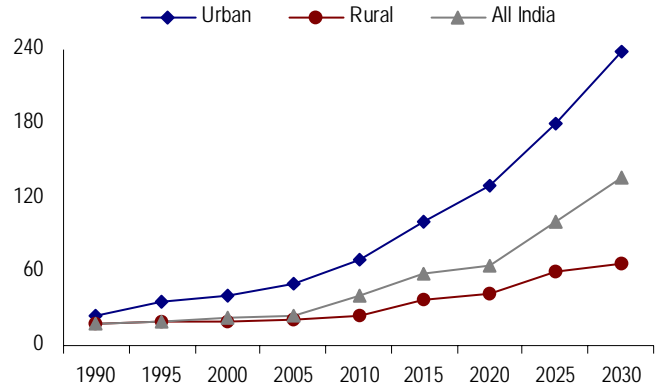
Source: PINC Research, NCAER

Exhibit 29 - Higher Urbanisation is Expected



Source: McKinsey Global Institute Analysis

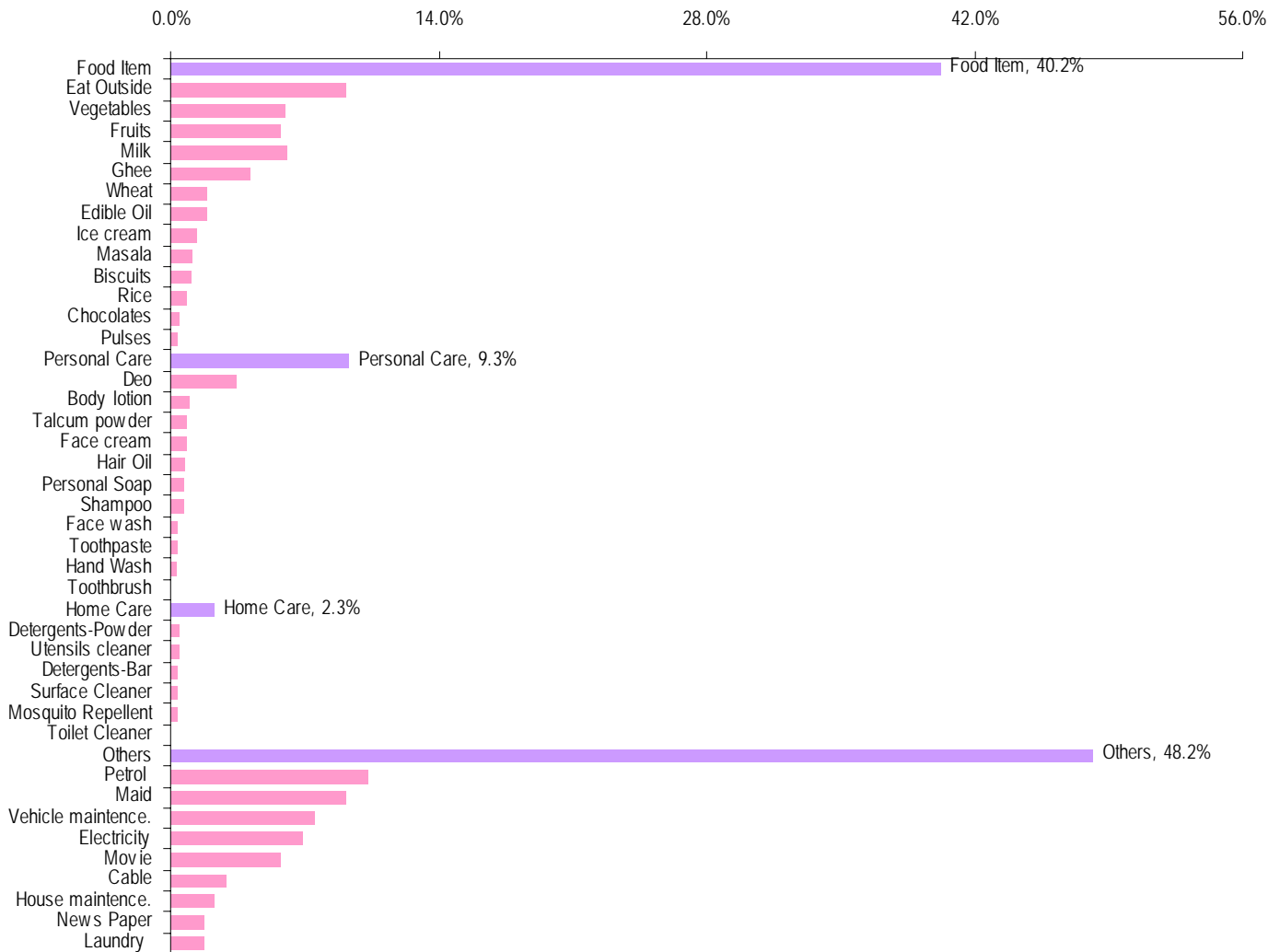
Exhibit 30 - Per Capita Disposable Income (Rs 000)



Source: McKinsey Global Institute Analysis

Spending Pattern - Optimism for Personal Care

Exhibit 31 - Typical Urban Middle Class Monthly Spending Mix



Source: PINC Research

We analysed few urban middle class families to understand the broader mix of monthly spending. In this analysis, we exclude spending on apparels as we found spending on apparels has wide variation even among the same income and age group. We also exclude items like rents and EMIs for our analysis as these do not serve our purpose for this analysis.

Through this analysis, we want to emphasise the broader spending pattern of the consumers rather than the close pattern. We found, although personal care and home care products are expensive but their weightage in the monthly spending is very low. Therefore, we expect substantial scope of value growth for the personal care segment. Home care is dominated by the unorganised players therefore shift from unbranded to branded products would create growth potential for FMCG companies.

Consumer, for the personal care products, needs quality and the 'value for money' concept is relatively less applicable for it. FMCG companies can tap this opportunity through regularly launching innovative and better products. We assumed that personal care mix should be higher for upper class while lower class will spend more on the food items. Our focus was on the middle class, as it covers the largest consumer base for FMCG companies.

Rural India and FMCG - price sensitivity is high

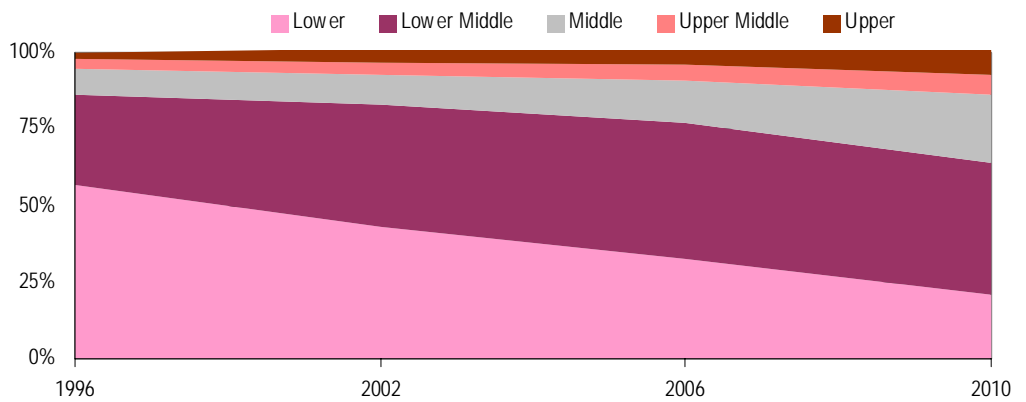
Improvement in rural income mix

The rapid changes in the rural India have improved the ways of generating income. With a huge population base the improvement in the rural income has opened several gates for the FMCG companies. In the last 5 years, rural India has outperformed the overall FMCG growth and providing significant volume growth to the FMCG companies. During the same period, Rural market displayed ~15% growth compared to ~12% growth in the urban market.

We observed a sharp change in the rural income mix in the past 15 years. Lower class had >50% share of the rural India in 1996 which has lowered down to ~21% in 2010. High income growth has shifted lower class people into lower middle class and middle class. This resulted into 1,400bps and 1,300bps expansion in lower middle class and middle class mix in the past 15 years.

Higher rural income has improved the middle class mix to ~22% in 2010 from ~10% in 2002...

Exhibit 32 - Rural Income Distribution



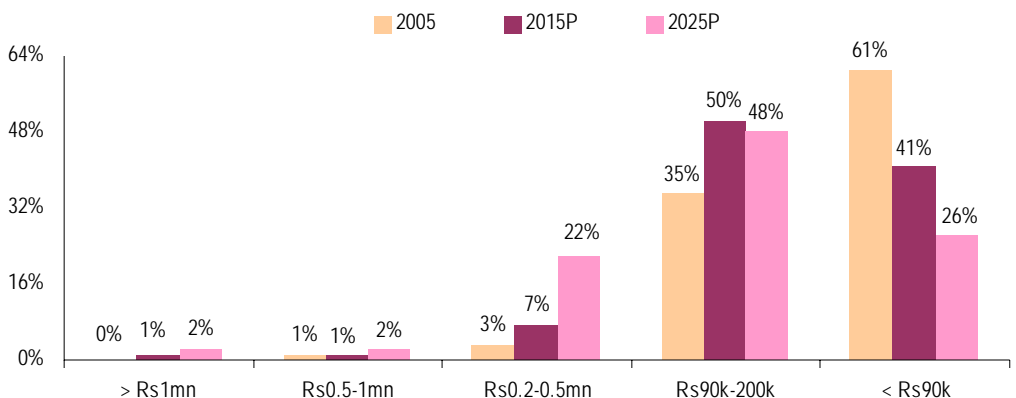
Source: PINC Research, NCAER

Promising rural income level

The dynamics for rural India has changed favourably for FMCG companies and will benefit for long period. As per the 'CII and Euromonitor' (source: Businessworld Marketing Whitebook 2011-12), ~50% of the rural population will come under Rs90k-200k annual income range by 2015 which was at ~35% in 2005. This rise in annual income will favourably improve the lower middle class and middle class mix going forward. The change in the rural income mix will help FMCG companies in maintaining the volume growth for long period.

~50% of the rural population will come under Rs90k-200k range by 2015...

Exhibit 33 - Promising Annual Rural Income Levels



Source: PINC Research, Businessworld Marketing Whitebook 2011-12

Govt. spending continue to support rural reforms

Rural India's face change was also because of government's initiative to spend through many rural development schemes. In the last four years, government spending in these schemes has increased by more than 3x. These initiatives have several direct and indirect benefits for the rural development. Bharat Nirman, NREGA and Sarva Shiksha Abhiyan are the key schemes for these spending. We believe the buoyancy in the rural economy is sustainable.

Govt. spending for rural reforms has increased by 3x in the last four years...

Benefits of these schemes will come gradually and will be effective for long period...

| Exhibit 34 - Rural Reforms Through Higher Spending in Major Govt. Schemes | | | | | |
|--|----------------|----------------|----------------|----------------|-----------------|
| Budget Allocation to Major Schemes (Rs bn) | 2007-08 | 2008-09 | 2009-10 | 2010-11 | 2011-12* |
| Bharat Nirman | - | 313 | 454 | 480 | 580 |
| Mahatma Gandhi NREGS | 120 | 160 | 391 | 401 | 400 |
| Pradhan Mantri Gram Sadak Yojana (PMGSY) | 65 | 75 | 120 | 120 | 200 |
| Indira Awaas Yojana (Rural Housing) | 40 | 54 | 88 | 100 | 100 |
| Sarva Shiksha Abhiyan (SSA) | 107 | 131 | 131 | 150 | 210 |
| National Rural Health Mission (NRHM) | 110 | 119 | 139 | 154 | 178 |
| Highways | 117 | 107 | 116 | 167 | 133 |
| NHDP / NHA | 65 | 70 | 86 | 95 | 103 |
| National Programme of Mid Day Meals in Schools | 73 | 80 | 80 | 94 | 104 |
| Integrated Child Development Services | - | 63 | 67 | 87 | 103 |
| National Rural Drinking Water Programme | 65 | 73 | 80 | 90 | 94 |
| IIFCL Cum. Disbursement target | - | - | 90 | 200 | 250 |
| Swaranjayanti Gram Swarozgar Yojana | 18 | 22 | 24 | 30 | 29 |
| Rural Sanitation | 11 | 12 | 12 | 16 | 17 |
| Integrated Watershed Management Programme | 11 | 18 | 19 | 25 | 25 |
| For Health Sector | - | 37 | 44 | 56 | 57 |
| Rashtriya Krishi Vikas Yojana | - | - | - | - | 78 |
| Total Outlay | 802 | 1,334 | 1,941 | 2,265 | 2,661 |
| YoY Gr% | | 66% | 46% | 17% | 17% |
| Credit support to farmers | 0 | 2,870 | 3,250 | 3,750 | 4,750 |
| Interest Subvention to farmers | 0 | 0 | 1% | 2% | 3% |

Source: PINC Research, Union Budget 2011, * Budget estimates

MSP growth and higher crop yield boost the farm income

Robust MSP growth and higher crop yield in the past 5 years were the key reasons for the change in rural income distribution. MSP growth during the past 5 years (2006-11) for Wheat, Paddy, Cotton, Maize and Arhar were 11%, 13%, 11%, 13% and 18% respectively compared to 1%, 2%, 2%, 4% and 3% during 2000-05.

MSP rates for Kharif crop for 2011-12 was slightly lower than the past 5 years CAGR. However, MSP rates for the Rabi crop for 2011-12 is encouraging as MSP rates for most of the crops are ahead of the past 5 year CAGR.

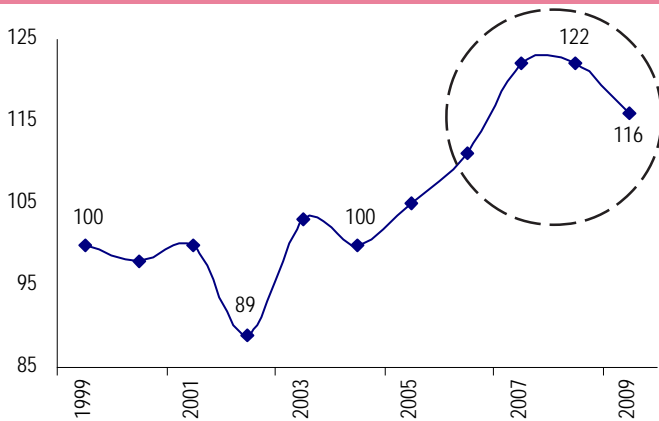
Robust MSP growth in the past 5 years raised the rural income significantly...

Strong growth in Rabi crops for 2011-12...

| Exhibit 35 - Strong MSP Rates Boost the Farm Income | | | | |
|--|---------|---------|--------------|--------------|
| (Rs/quintal) | 2011-12 | YoY Gr. | CAGR 2000-05 | CAGR 2006-11 |
| Kharif Crops | | | | |
| Paddy (Grade A) | 1,110 | 8% | 2% | 13% |
| Jowar (Hybrid) | 980 | 11% | 3% | 13% |
| Bajra | 980 | 11% | 3% | 13% |
| Maize | 980 | 11% | 4% | 13% |
| Ragi | 1,050 | 9% | 3% | 14% |
| Arhar (Tur) | 3,200 | 7% | 3% | 18% |
| Moong | 3,500 | 10% | 5% | 18% |
| Urad | 3,300 | 14% | 5% | 17% |
| Cotton (H-4) | 3,300 | 10% | 2% | 11% |
| Groundnut in shell | 2,700 | 17% | 4% | 12% |
| Sunflower seed | 2,800 | 19% | 5% | 13% |
| Soybean (Yellow) | 1,690 | 17% | 3% | 11% |
| Sesamum | 3,400 | 17% | 4% | 17% |
| Niger seed | 2,900 | 18% | 0% | 19% |
| Rabi Crops | | | | |
| Wheat | 1,285 | 15% | 1% | 11% |
| Barley | 980 | 26% | 2% | 12% |
| Gram | 2,800 | 33% | 5% | 14% |
| Masur (Lentil) | 2,800 | 24% | 3% | 13% |
| Rapeseed/Mustard | 2,500 | 35% | 7% | 8% |
| Safflower | 2,500 | 39% | 5% | 10% |
| Toria | 2,425 | 40% | 8% | 0% |
| Other Crops | | | | |
| Copra (Ball) | 4,775 | 2% | 2% | 4% |
| Dehusked coconut | 1,200 | 0% | na | na |
| Jute | 1,600 | 0% | 3% | 10% |
| Sugarcane | 139 | 29% | 6% | 12% |

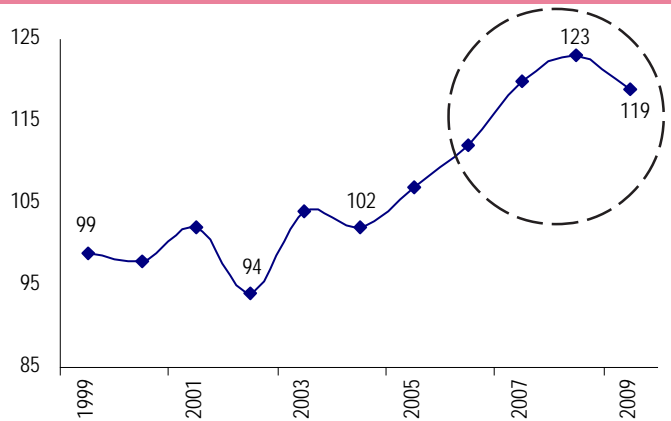
Source: PINC Research, Press Information Bureau

Exhibit 36 - Crop Production Index (1999 as base)



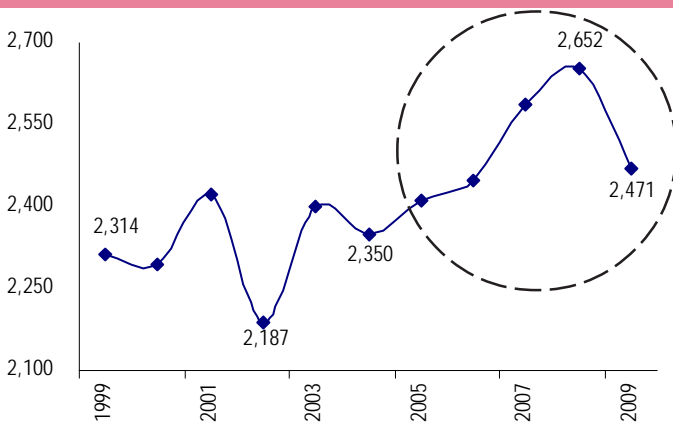
Source: PINC Research, World Bank

Exhibit 37 - Food Production Index (1999 as base)



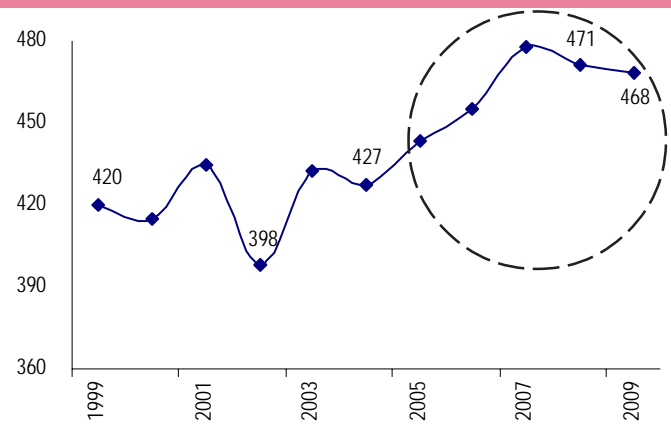
Source: PINC Research, World Bank

Exhibit 38 - Cereal Yield (Kg/hectare)



Source: PINC Research, World Bank

Exhibit 39 - Agric. value added per worker



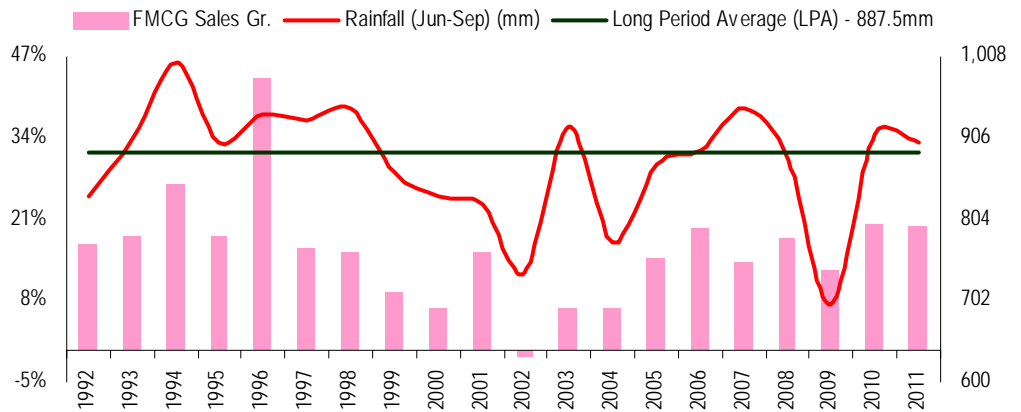
Source: PINC Research, World Bank Note: Constant 2000 US\$

Low Dependence on Monsoon

Monsoon is one of the key indicators for farm income but better irrigation facilities, higher MSP rates and higher farming related educational programme has reduced the overdependence on Monsoon. Rural income is now less dependent on farming owing to generation of non-agriculture income sources and migration from rural to urban areas.

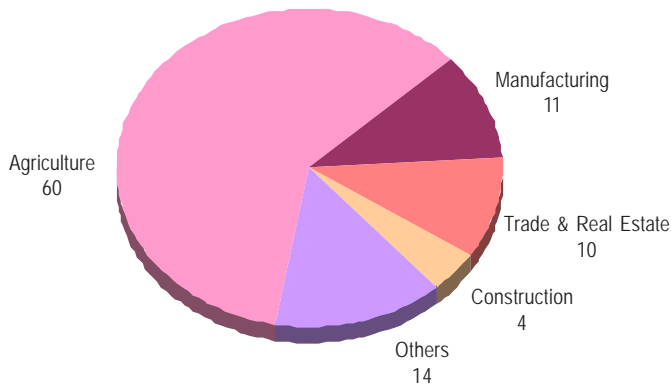
India's dependence on Agriculture has been reducing gradually over the last several years. Agriculture's contribution in GDP and Employment generation has declined to 14% and 52% as compared to 18% and 60% around 7-8 years back.

Exhibit 40 - Dependence on Monsoon has Reduced



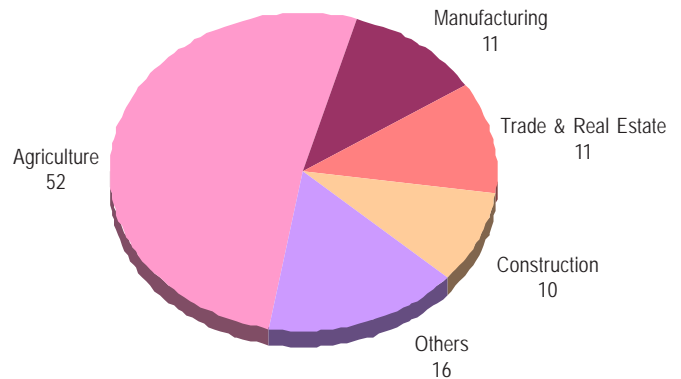
Source: PINC Research, IMD

Exhibit 41 - Sectoral Employment Mix in 2000 (%)



Source: CSO

Exhibit 42 - Sectoral Employment Mix in 2010 (%)



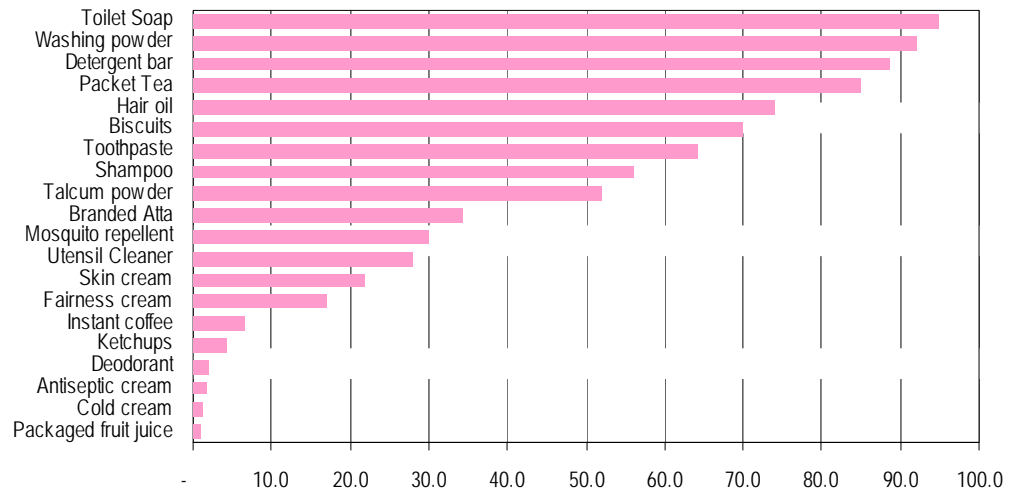
Source: CSO

Opportunities in Low Penetration and Low Per Capita Consumption Categories

We see immense opportunities in several categories on account of low penetration level and low per capita consumption. Our observation suggests, despite having high penetration level, categories like detergent soap, personal soap and washing powder have low per capita consumption therefore change in the consumption pattern will drive these categories.

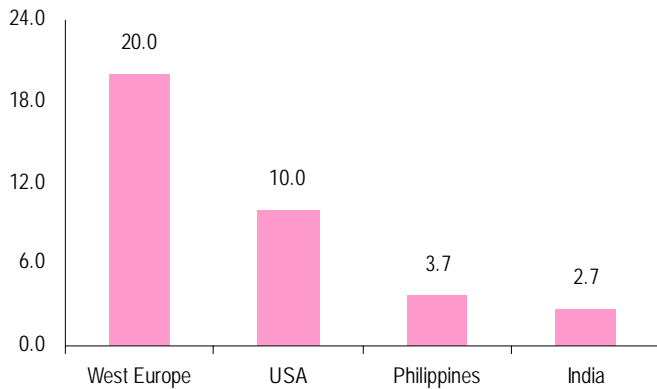
Apart from this, we found categories like oral care, shampoo, skin cream, deodorant and packaged juice etc where penetration level and per capita consumption both is low. Therefore, these categories have enormous opportunity to grow through addition in consumer base as well as change in the consumption pattern.

Exhibit 43 - Penetration level of key categories (%)



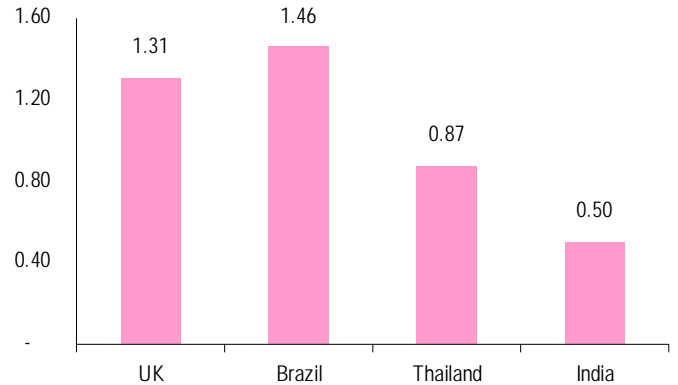
Source: PINC Research, Emami Annual Report 2011, Industry data

Exhibit 44 - Detergent per capita consumption (kg)



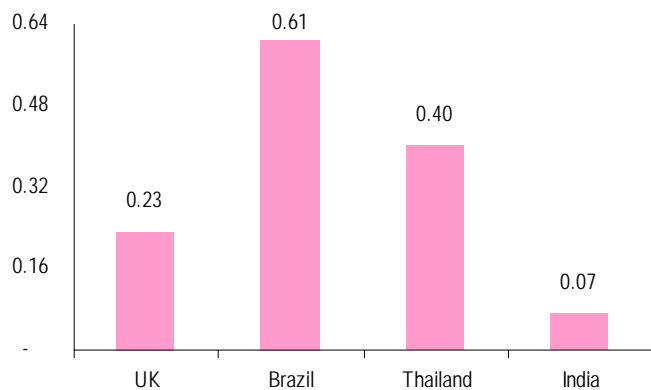
Source: PINC Research, IBEF

Exhibit 45 - Personal wash per capita consumption(kg)



Source: PINC Research, IBEF

Exhibit 46 - Toothpaste per capita consumption (kg)



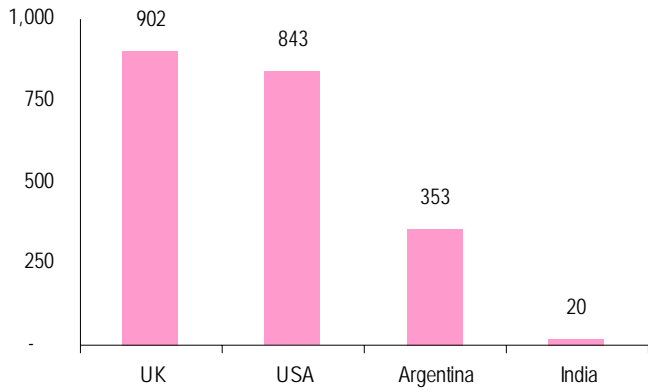
Source: PINC Research, IBEF

Exhibit 47 - Tea per capita consumption (kg)



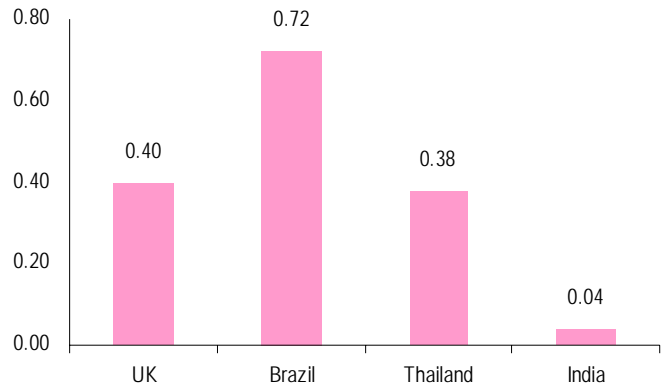
Source: PINC Research, IBEF

Exhibit 48 - Skin care per capita consumption (Rs)



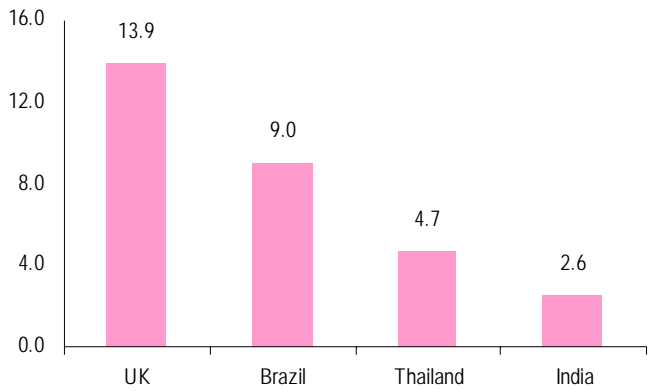
Source: PINC Research, IBEF

Exhibit 49 - Shampoo per capita consumption (Kg)



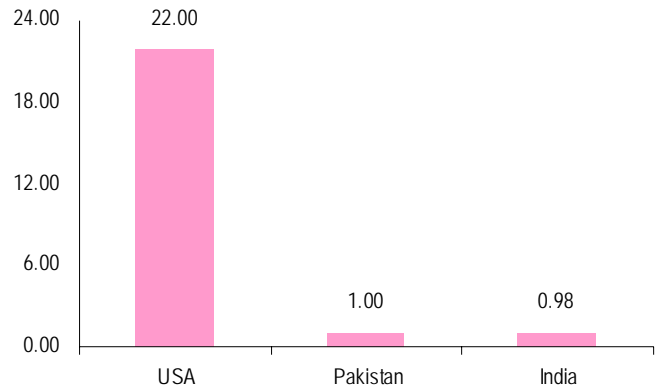
Source: PINC Research, IBEF

Exhibit 50 - Fabric wash per capita consumption (Kg)



Source: PINC Research, IBEF

Exhibit 51 - Ice cream per capita consumption (litre)



Source: PINC Research, IBEF

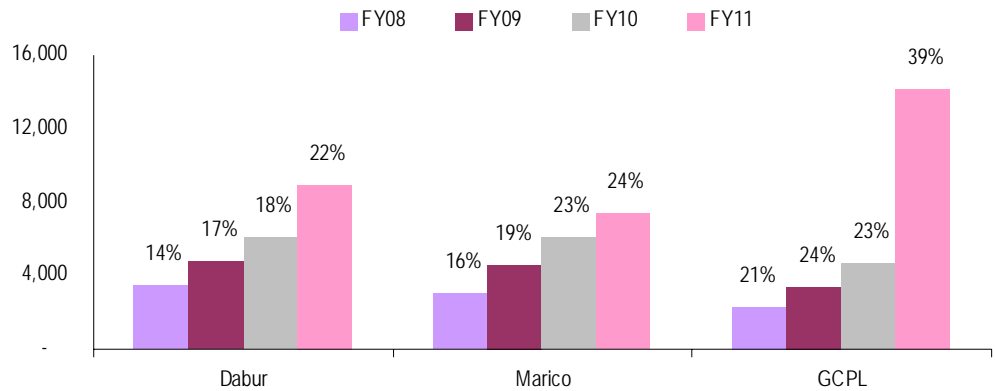
Overseas Market - Opportunities galore; near term margin pressure

Most of the domestic FMCG companies are enhancing their presence in the overseas market. We observed several acquisitions as well as capacity installation in the overseas market in the past three years. We see overseas market as an opportunity for long term however higher spending on brand building would exert pressure on EBITDA margin in the near term.

Reducing exposure of domestic competition

Most of the domestic FMCG companies are facing challenges through rising competition in the domestic market. Hence, entering into the overseas market provides newer opportunities for growth and provides diversification benefits to these companies.

Exhibit 52 - Overseas Sales (Rs mn) and Contribution in Total Sales (%)



Source: PINC Research, Bloomberg

Better opportunities for power brands

Most power brands facing volume pressure in the domestic market and overseas market can provide big opportunity for these brands. As these brands have already cleared all the testing levels now the incremental efforts would only be to market it well to the new consumers. This can change the life cycle of the brand which either is in stagnant or declining phases.

"Parachute is 2nd most trusted brand in Bangladesh across categories"

Acquisitions at low valuation

High valuations of domestic FMCG companies led to an opportunity to acquire in the overseas market. There are several markets which are not expensive as compared to Indian market although have similarity in the growth outlook.

Exhibit 53 - Few Strategic Deals in Overseas and India

| Company | Acquired Company | Date of acquisition | Geography | Valuations (Acq. Cost/Sales) |
|-------------------|--------------------------------------|---------------------|----------------|------------------------------|
| Overseas | | | | |
| Dabur | Hobi | Oct-10 | Turkey | -2.6 |
| Dabur | Namaste Lab | Jan-11 | US | -1.2 |
| GCPL | Megasari | May-10 | Indonesia | -2.2 |
| GCPL | Tura | Mar-10 | Nigeria | -3.3 |
| GCPL | Issue | May-10 | Latin America | -1.5 |
| GCPL | Keyline Brands Ltd | Oct-05 | UK | -0.7 |
| Wipro | Yardley, Business | Nov-09 | London | -1.9 |
| Wipro | Unza | 2007 | Singapore | -1.5 |
| Marico | Derma Rx Asia Pacific Pte Ltd | May-10 | Singapore | -1.0 |
| Marico | Ingwe Brand | Aug-10 | South Africa | -1.0 |
| Marico | Code 10 brand from Colgate-Palmolive | Jan-10 | Malaysia | -1.0 |
| Marico | ICP | Feb-11 | Vietnam | -1.4 |
| Marico | Fiancee | Sep-06 | Egypt | -1.8 |
| India | | | | |
| Reckitt Benckiser | Paras Pharma | Apr-11 | Gujarat, India | -8.1 |
| Dabur | FEM Care Pharma Ltd | Nov-08 | Mumbai, India | -3.0 |
| Dabur | Balsara India Group Companies | Jan-05 | India | -0.7 |

Source: PINC Research, Company

Near term margin pressure expected

Most of the companies are in a mode to spend high on marketing expenses in the overseas market. These are new markets which require necessary investment on brand building. We believe this will provide long term benefits. Dabur and Marico have already expressed their intent and guided EBITDA margin pressure in the overseas market.

Who will win the game?

We believe companies with higher current in their RIVER (Range, Innovation, Value weightage, Engage and Reach) will lead the game.

Range- We believe the range of any brand in terms of coverage of price points and wide variety should be considered as a key trait. We have observed that many companies has benefited with this strategy specially launching at low price point. It not only provides high volume growth but it also helps in improving the margins (not in every case but largely).

Innovation- Innovation is the key for any industry and FMCG industry is not exception of that. Although, the innovations what we want to mention here are the consistent improvement in usability, product extension, packaging and quality.

Value Weightage- The large part of Indian consumers' buying was depending on 'value for money' concept. However, we have observed gradual change in that concept. Now consumers have changed their buying process post the success of plastic money and modern trade. Consumer buys through a mathematical matrix that calculates each item's weightage in the monthly expense. The importance of brand plays a key role in choosing products. So in the urban market companies should focus more on the variety and quality.

Engage - There was a time when consumers used to stick with one brand for whole life and that case was largely with soaps, oral care, skin care and hair care categories. Our observation states that consumers' brand loyalty has been reducing over a period of time and consistent change in brands have been noticed. Now it is difficult for a consumer to stick with one brand for whole life.

In our opinion, companies should aggressively look at the change in customer profile and should try to give the required product to fulfill the new demand. So the consumer can be engaged with the company; if not with the brand through improvement in features, packing, quality and better schemes.

Reach- It is a proven fact that long term survival of any brand depends on its reach to the customers. Good companies consistently develop their distribution channel and always wait for the opportunities to come to challenge the competitor.

Consumers' buying pattern shifting towards a concept of weightage in the monthly budget...

Tries to engage with the company; if not with the brand...

Exhibit 54 - FMCG Competitiveness through RIVER Analysis

| Companies | Range | Innovation | Value Weightage | Engage | Reach | Total |
|-------------|-------|------------|-----------------|--------|-------|-------|
| HUL | +++ | +++ | +++ | +++ | +++ | 15+ |
| ITC | ++ | ++ | +++ | ++ | +++ | 12+ |
| GCPL | +++ | ++ | ++ | ++ | ++ | 11+ |
| Nestle | +++ | ++ | +++ | ++ | +++ | 13+ |
| Dabur | ++ | ++ | +++ | ++ | +++ | 12+ |
| Colgate | +++ | ++ | ++ | ++ | +++ | 12+ |
| Marico | ++ | ++ | ++ | ++ | ++ | 10+ |
| Britannia | ++ | ++ | +++ | ++ | ++ | 11+ |
| Emami | ++ | ++ | ++ | ++ | ++ | 10+ |
| Jyothy Labs | ++ | ++ | ++ | ++ | ++ | 10+ |

Source: PINC Research

Note: (+) Points are based on competitive edge and ranges between 1-3 where 3 is for the most competitive

Significance of Power Brands - over dependence is risky

The over dependence on a brand or few brands can create trouble for the company in the long term. Here, we mention comparative analysis of dependence of power brands.

We classified the companies based on their profitability dependence on power brands.

High Dependence : Nestle, Marico and Jyothy Labs

Medium Dependence : Emami and Colgate

Low Dependence : HUL and Dabur

However, risk exposure would be higher for those companies where volume growth of power brand is slowing down. Parachute and Ujala Supreme is already growing at single digit and expectation is further muted for volume growth. We believe this can create high risk scenario for these two companies. However, post acquisition of Henkel India we expect next two years' scenario would be very different for Jyothy Labs and dependence on Ujala Supreme will reduce substantially. Nestle is also highly dependent on Maggi brand while high volume growth expectation reduces the risk exposure. Although we expect going forward Maggi's price power will reduce on account of higher competitive intensity.

Exhibit 55 - Company Dependence on Power Brand

| Player | Brand | Brand Size (Rs bn) | Sales Dependence | EBITDA dependence | Last 1 yr Gr. | Last 3 yr Gr. | Mkt Share | Mkt Gr. |
|-------------|----------------------|--------------------|------------------|-------------------|---------------|---------------|-----------|---------|
| HUL | Wheel | ~20 | 9% | -5% | ~10% | ~15% | ~15% | ~8% |
| HUL | Lux | ~13 | 7% | -5% | ~5% | ~10% | ~15% | ~11% |
| HUL | Lifebuoy | ~12 | 6% | -4% | ~5% | ~10% | ~14% | ~11% |
| HUL | Fair & Lovely | ~13 | 7% | -8% | ~15% | ~16% | ~40% | ~20% |
| Nestle | Maggi | ~15 | 25% | -35% | ~25% | ~25% | ~88% | ~30% |
| Dabur | Dabur Chyawanprash | ~3 | 6% | -9% | ~20% | ~14% | ~65% | ~16% |
| Dabur | Babool | ~2 | 6% | -5% | ~12% | ~12% | ~7% | ~13% |
| Dabur | Dabur Amla | ~2 | 5% | -4% | ~17% | ~16% | na | na |
| Dabur | Vatika | ~3 | 8% | ~7% | ~13% | ~10% | na | na |
| Dabur | Real Fruit Juice | ~3 | 8% | -8% | ~30% | ~20% | ~60% | ~25% |
| Colgate | Colgate Dental Cream | ~9 | 44% | -18% | ~5% | ~5% | ~25% | ~13% |
| Marico | Parachute | ~9 | 28% | -47% | ~23% | ~9% | ~45% | ~15% |
| Jyothy Labs | Ujala Supreme | ~2 | 22% | -55% | ~15% | ~16% | ~72% | ~15% |
| Emami | Navratna oil | ~3 | 27% | } -75% | ~20% | ~15% | ~49% | ~15% |
| Emami | Zandu Balm | ~4 | 28% | | ~22% | ~20% | ~57% | ~18% |
| Emami | Boroplus | ~2 | 17% | | ~9% | ~14% | ~75% | ~12% |

Source: PINC Research, Company

Packaging norms would increase price sensitivity

As per the notification issued by 'Packaged Commodity Rules, 2011', several FMCG products would have to follow stipulated pack size from July'12. We mention below list of the products and the stipulated quantity which are covered in the notification. Most of the FMCG companies are not in favour and at least don't want low price point (Rs1, Rs2, Rs5, Rs10 and Rs20) to be part of this rule. Here we mention our take on this new rule and its possible impact on the FMCG companies.

Our Take

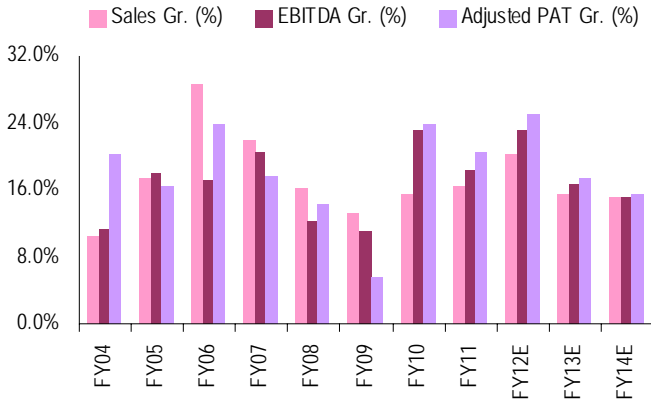
- It would largely impact the modern trade market where consumers get an opportunity to compare products. Modern trade market is <10% of the total FMCG market so the impact should be restricted to that level only.
- FMCG companies with higher focus on popular segment (mass segment) would have to be more cautious for frequent price change. Popular segment is price sensitive and also faces competition from unbranded products too. Soaps, Detergents, Biscuits, Chocolates and Snacks are among the price sensitive products therefore HUL, P&G, ITC, Nestle and Britannia would be more vigilant for price hike.
- In high inflationary scenario, FMCG companies frequently reduce grammage and increase MRP to pass on the input burden to the consumers. Post the implementation of this new rule, price increase would remain only alternative to protect profitability. Typically price change is more visible than reducing the grammage so volume would be more sensitive for any change.

Exhibit 56 - List of the products under notification

| S.N. | Category | Quantities in which to be packed |
|------|--|--|
| 1 | Baby Food | 100g, 200g, 300g, 400g, 500g, 600g, 700 g, 800 g, 900g, 1 kg, 2kg, 5 kg and 10 kg. |
| 2 | Weaning Food | 100g, 200g, 300g, 400g, 500g, 600g, 700g, 800g, 900g, 1 kg, 2kg, 5 kg and 10 kg. |
| 3 | Biscuits | 25g, 50g, 75g, 100g, 150g, 200g, 250g, 300g and thereafter in multiples of 100g up to 1 kg. |
| 4 | Bread including brown bread but excluding bun. | 100g and there after in of multiples 100g. |
| 5 | Un-canned packages of butter and margarine | 25 g, 50 g, 100 g, 200 g, 500 g, 1 kg, 2 kg, 5 kg, and thereafter in multiples of 5 kg |
| 6 | Cereals and Pulses | 100g, 200g, 500g, 1 kg, 2 kg, 5 kg and thereafter multiples of 5 kg |
| 7 | Coffee | 25g, 50g, 100g, 200g, 250g, 500g, 1kg and thereafter in multiples of 1kg. |
| 8 | Tea | 25g, 50g, 100g, 125g 250g, 500g, 1kg and thereafter in multiples of 1kg. |
| 9 | Materials which may be constituted or reconstituted as beverages. | 25 g, 50 g, 100 g, 200 g, 500 g, 1 kg and thereafter in multiples of 1kg. |
| 10 | Edible Oils, Vanaspati, Ghee, Butter oil | 50 g, 100 g, 200 g, 500 g, 1 kg, 2 kg, 3 kg, 5 kg and thereafter in multiples of 5 kg If net quantity is declared by volume the same number in milliliters or liters, as the case may be. If the net quantity is declared by volume, then the equivalent quantity in terms of mass to be declared in brackets in same size of letters/numerals |
| 11 | Milk Powder. | Below 50g no restriction, 50 g, 100g, 200g, 500 g, 1 kg and thereafter in multiples of 500 g. |
| 12 | Non-soapy detergents (powder) | Below 50 g no restriction, 50g, 100g, 200g, 500g, 700g, 1kg, 1.5 kg, 2 kg and thereafter, in multiples of 1 kg |
| 13 | Rice(powdered),Flour, Atta, Rawa and Suji | 100g, 200g, 500g, 1kg, 2kg, 5 kg and thereafter in multiples of 5 kg |
| 14 | Salt | Below 50g in multiples of 10g, 50g, 100g, 200g, 500g, 750g, 1 kg, 2 kg, 5 kg and thereafter in multiples of 5kg |
| 15 | Soaps | |
| | (a) Laundry Soap | 50g, 75g, 100g, and thereafter in multiples of 50g. |
| | (b) Non-soapy detergent cakes/bars | 50g, 75g, 100g, 125g, 150g, 200g, 250g, 300g and thereafter in multiples of 100g |
| | (c) Toilet Soap including all kinds of bath soap (cakes). | 25g, 50g, 75g, 100g, 125g, 150g and thereafter in multiples of 50g. |
| 16 | Aerated soft drinks, non-alcoholic beverages | 65 ml (fruit based drinks only), 100 ml, 125ml(fruit based drinks only), 150 ml, 200 ml, 250 ml, 300 ml, 330ml(in cans only), 500ml, 750 ml, 1 litre, 1.5 litre, 2 litre, 3 litre, 4 litre and 5 litre. |
| 17 | Mineral water and drinking water | 100 ml, 150 ml, 200 ml, 250 ml, 300 ml, 500 ml, 750 ml, 1 litre, 1.5 litre, 2 litre, 3 litre, 4 litre and 5 litre. |
| 18 | Cement in bags | 1 kg, 2 kg, 5 kg, 10 kg, 20 kg, 25 kg, 40 kg (for White cement only) and 50 kg. |
| 19 | Paint varnish etc. | |
| | (a) Paint (other than paste paint or solid paint) varnish, varnish stains, enamels | 50 ml, 100 ml, 200 ml, 500 ml, 1 litre, 2 litre, 3 litre, 4 litre, 5 litre and thereafter in multiples of 5 litre. |
| | (b) Paste paint and solid paint | 500g, 1 kg, 1.5 kg, 2 kg, 3 kg, 5 kg, 7kg and thereafter multiple of 5kg. |
| | (c) Base paint: | 450 ml, 500 ml, 900 ml, 925 ml, 950 ml, 975 ml, 1 litre, 3.6 litre, 3.7 litre, 3.8 litre, 3.9 litre and 4 litre and no restriction above 4 litre. |

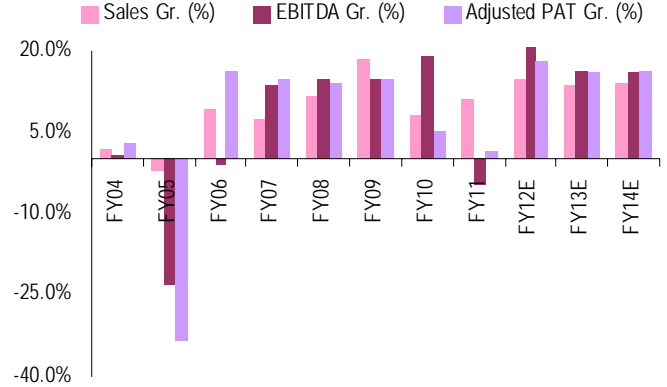
Business Trend

Exhibit 57 - ITC Business Performance



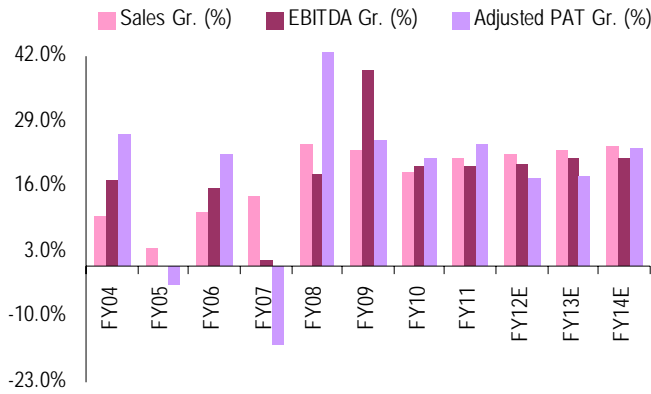
Source: PINC Research, Company

Exhibit 58 - HUL Business Performance



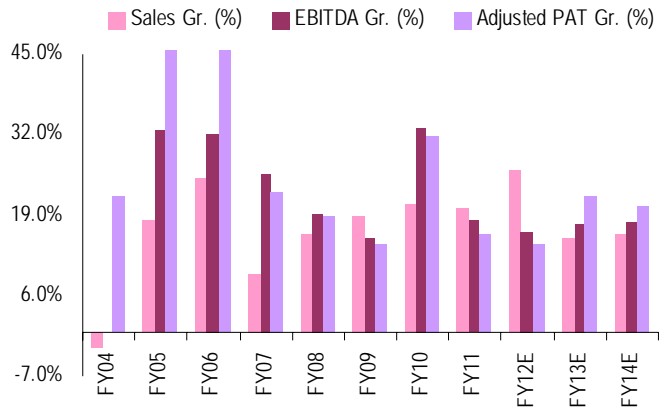
Source: PINC Research, Company

Exhibit 59 - Nestle India Business Performance



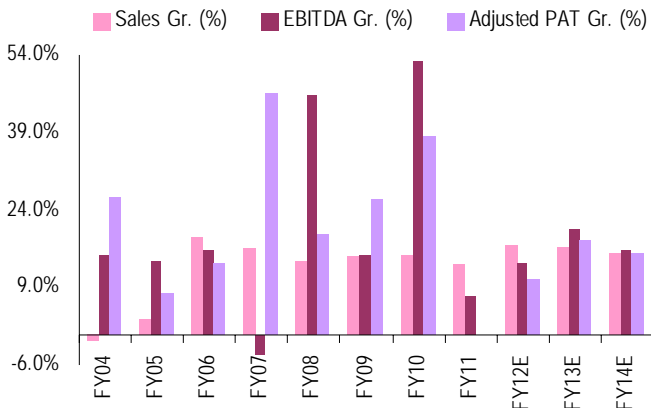
Source: PINC Research, Company

Exhibit 60 - Dabur Business Performance



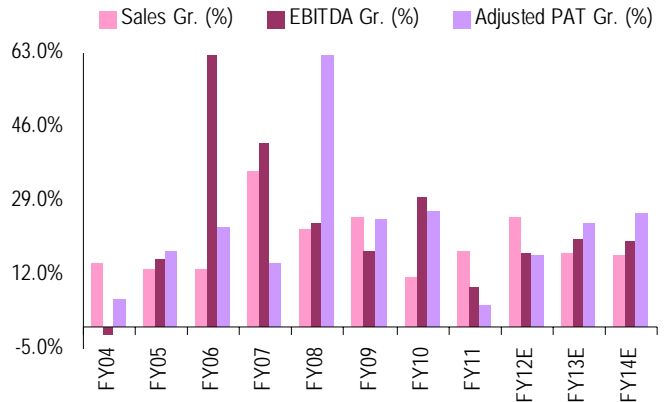
Source: PINC Research, Company

Exhibit 61 - Colgate Business Performance



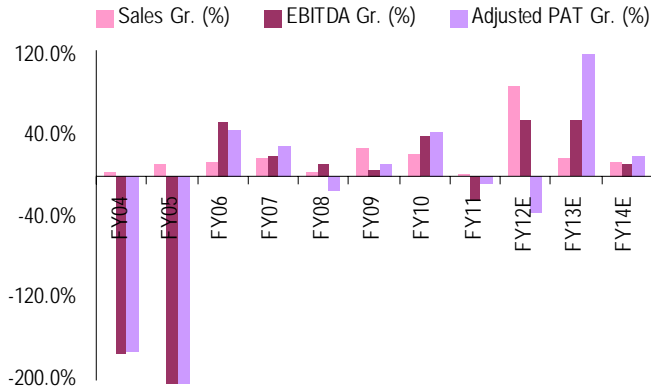
Source: PINC Research, Company

Exhibit 62 - Marico Business Performance



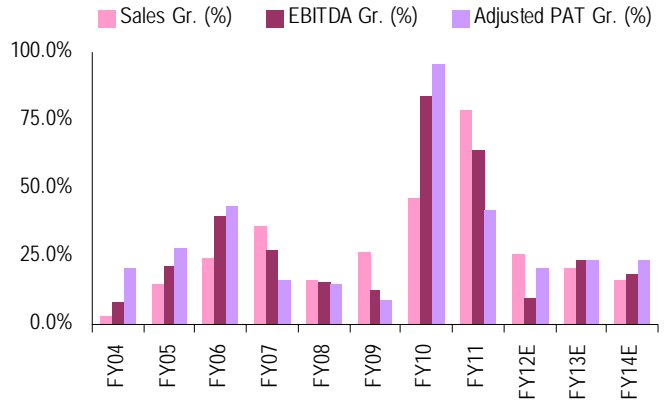
Source: PINC Research, Company

Exhibit 63 - Jyothy Labs Business Performance



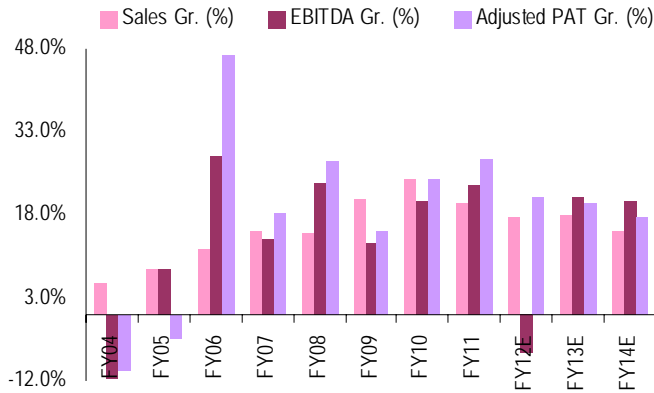
Source: PINC Research, Company

Exhibit 64 - GCPL Business Performance



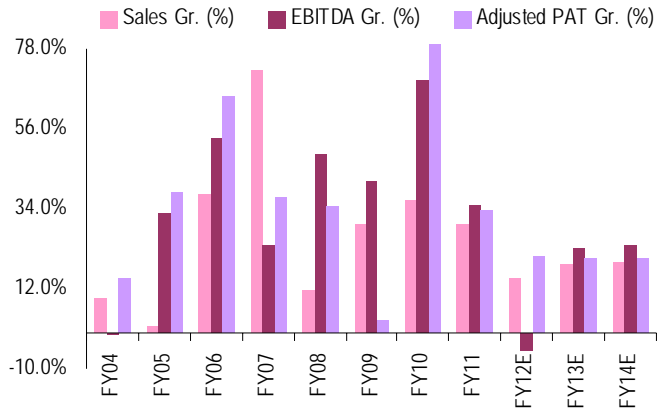
PINC Research, Bloomberg Consensus

Exhibit 65 - GSK Consumers Business Performance



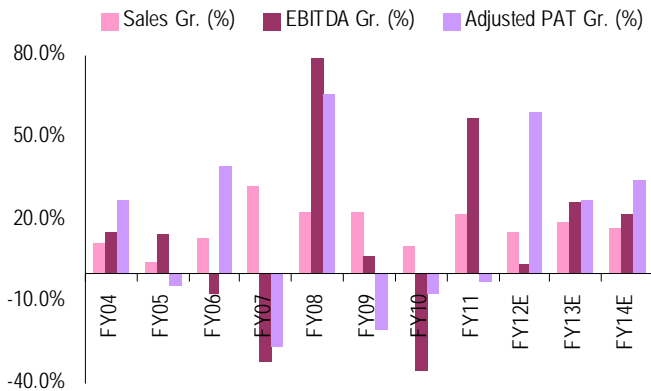
PINC Research, Bloomberg Consensus

Exhibit 66 - Emami Business Performance



PINC Research, Bloomberg Consensus

Exhibit 67 - Britannia Business Performance



PINC Research, Bloomberg Consensus

Cost Structure

| Exhibit 68 - EBITDA Margin Comparison | | | | | | | | | |
|---------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
| ITC | 35.7% | 35.9% | 36.1% | 32.9% | 32.5% | 31.4% | 30.7% | 32.8% | 33.3% |
| HUL | 19.3% | 19.1% | 15.0% | 13.6% | 14.4% | 14.8% | 14.3% | 15.7% | 13.5% |
| Nestle India | 19.7% | 21.0% | 20.2% | 21.1% | 18.7% | 17.8% | 20.1% | 20.3% | 20.1% |
| Dabur | 12.2% | 12.5% | 14.1% | 14.9% | 17.1% | 17.5% | 17.0% | 18.7% | 18.4% |
| Colgate | 13.4% | 15.6% | 17.4% | 17.0% | 14.0% | 18.0% | 18.0% | 23.8% | 22.5% |
| Marico | 9.8% | 8.4% | 8.5% | 12.2% | 12.8% | 12.9% | 12.1% | 14.1% | 13.1% |
| Jyothy Labs | 8.1% | -5.7% | 11.1% | 14.9% | 15.0% | 16.3% | 13.6% | 15.6% | 11.8% |
| GCPL | 17.2% | 18.1% | 19.1% | 21.5% | 20.1% | 20.0% | 17.7% | 22.2% | 20.5% |
| GSK Consumers | 22.5% | 18.9% | 18.8% | 21.6% | 21.4% | 23.0% | 21.5% | 20.8% | 21.4% |
| Emami Ltd | 13.1% | 12.0% | 15.7% | 17.4% | 12.6% | 16.8% | 18.4% | 22.8% | 23.8% |
| Britannia Industries | 14.2% | 14.8% | 16.2% | 13.3% | 6.8% | 9.9% | 8.6% | 5.0% | 6.5% |
| Total | 22.1% | 22.2% | 21.5% | 20.8% | 20.6% | 20.8% | 19.8% | 21.8% | 21.2% |

Source: PINC Research, Company

Gainer : Dabur, Colgate, Marico, GCPL, Emami
Looser : HUL, Britannia Industries
Maintain : Nestle India, GSK Consumers

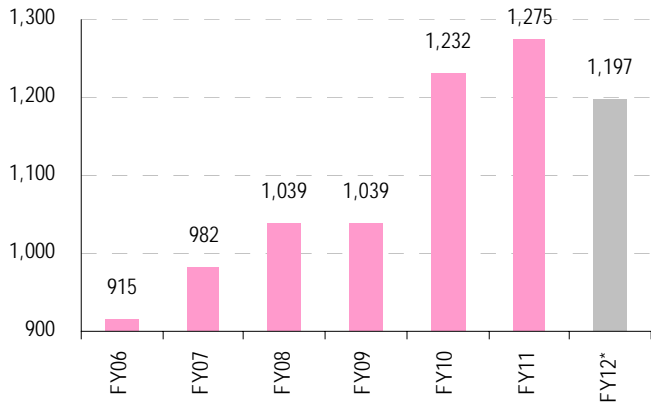
| Exhibit 69 - RM Dependence | | | | | | | | | |
|----------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
| ITC | 36.7% | 34.3% | 34.2% | 39.0% | 39.8% | 40.5% | 35.7% | 36.4% | 36.4% |
| HUL | 52.1% | 52.3% | 54.2% | 54.9% | 53.0% | 52.5% | 52.7% | 50.0% | 51.1% |
| Nestle India | 43.2% | 44.6% | 46.4% | 45.0% | 46.9% | 48.0% | 48.7% | 47.6% | 48.8% |
| Dabur | 44.4% | 45.9% | 44.0% | 43.2% | 47.4% | 47.0% | 48.8% | 45.5% | 46.5% |
| Colgate | 48.6% | 51.1% | 50.1% | 44.1% | 43.3% | 41.8% | 42.4% | 38.5% | 38.2% |
| Marico | 64.1% | 64.1% | 61.4% | 52.6% | 51.6% | 51.5% | 53.8% | 47.4% | 51.7% |
| Jyothy Labs | 50.6% | 54.0% | 50.9% | 46.5% | 51.8% | 48.5% | 54.8% | 53.1% | 51.9% |
| GCPL | 46.8% | 48.0% | 48.9% | 46.7% | 48.6% | 46.9% | 55.1% | 46.3% | 48.0% |
| GSK Consumers | 23.7% | 25.2% | 26.7% | 22.2% | 24.7% | 25.1% | 27.6% | 28.3% | 29.1% |
| Emami Ltd | 60.3% | 63.4% | 57.5% | 58.2% | 43.6% | 35.6% | 35.7% | 37.2% | 39.6% |
| Britannia Industries | 42.4% | 42.0% | 58.8% | 58.7% | 64.2% | 61.0% | 61.9% | 63.9% | 65.7% |

Source: PINC Research, Company

- Britannia is having high RM dependence & any fluctuation in the same impacts it the most. Wheat and Sugar are the key commodities for Britannia. Increase in excise duty along with rise in competition has enlarged the RM dependence from FY05 onwards.
- HUL has substantially reduced (by >250bps in the past 9 years) its dependence on raw material through higher contribution of its high margin Personal care business. However 160bps rise in packaging cost has limited the overall benefit to ~90bps.

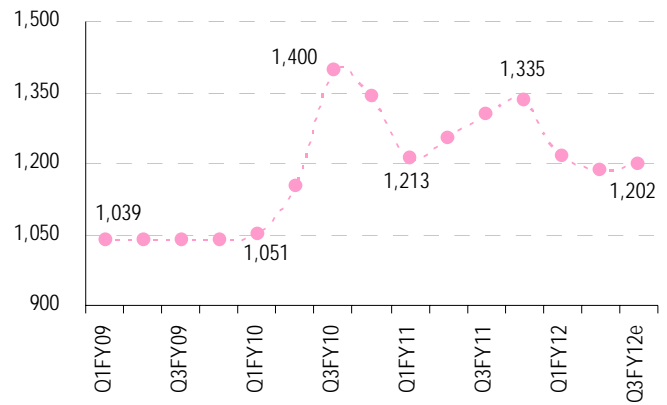
Key RM Trend

Exhibit 70 - Yearly Avg. Wheat Prices (Rs/quintal)



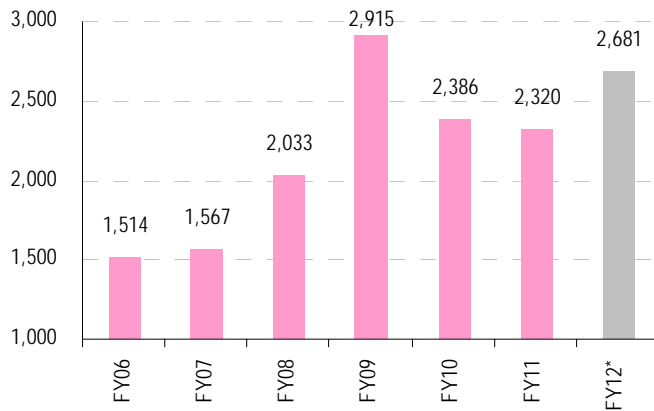
Source: PINC Research, Bloomberg *Till date

Exhibit 71 - Quarterly Avg. Wheat Prices (Rs/quintal)



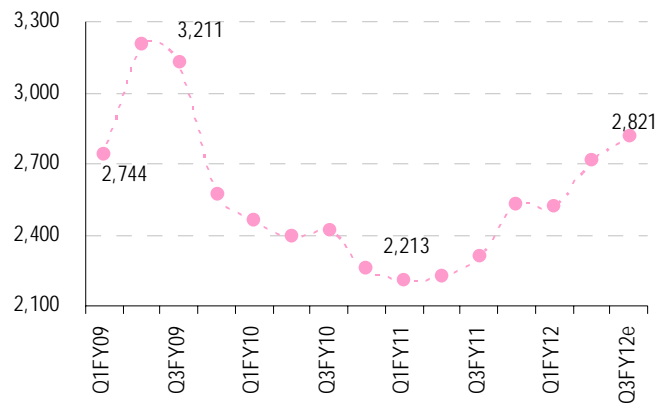
Source: PINC Research, Bloomberg *Till date

Exhibit 72 - Yearly Avg. Safflower Prices (Rs/quintal)



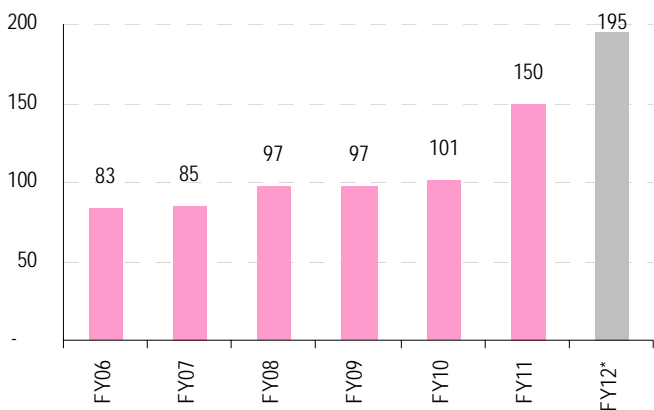
Source: PINC Research, Bloomberg *Till date

Exhibit 73 - Quarterly Avg. Safflower Prices (Rs/quintal)



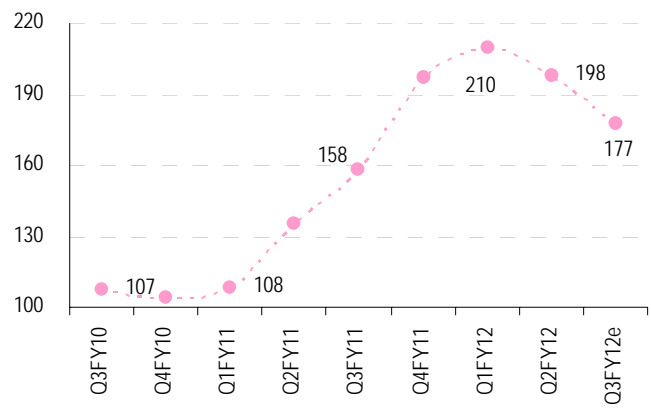
Source: PINC Research, Bloomberg *Till date

Exhibit 74 - Yearly Avg. Coffee Index (USD)



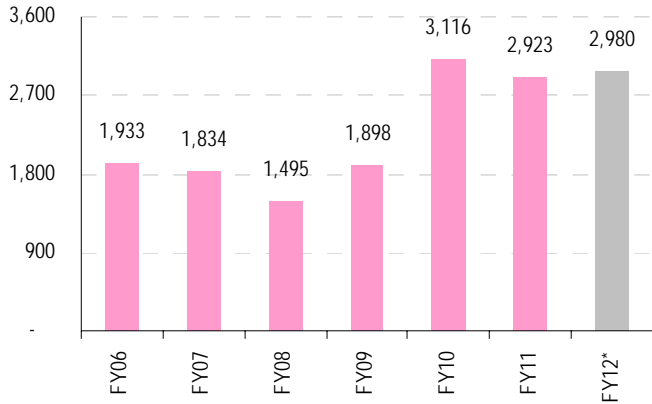
Source: PINC Research, Bloomberg *Till date

Exhibit 75 - Quarterly Avg. Coffee Index (USD)



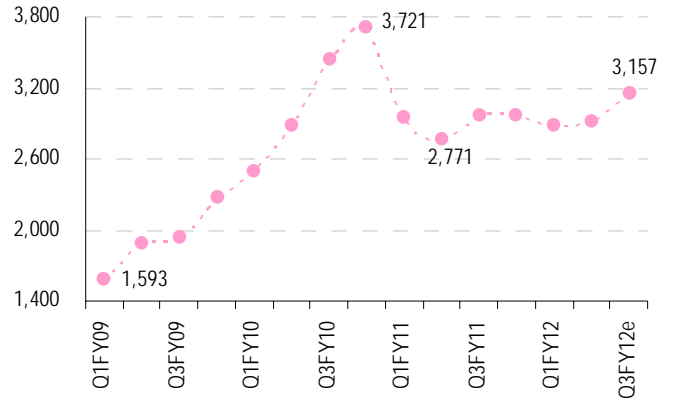
Source: PINC Research, Bloomberg *Till date

Exhibit 76 - Yearly Avg. Sugar Prices (Rs/quintal)



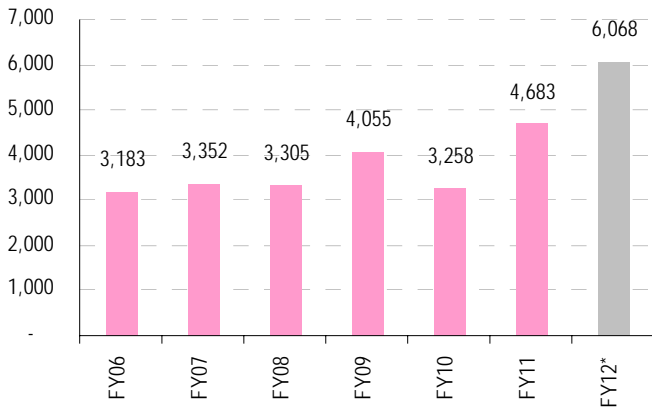
Source: PINC Research, Bloomberg *Till date

Exhibit 77 - Quarterly Avg. Sugar Prices (Rs/quintal)



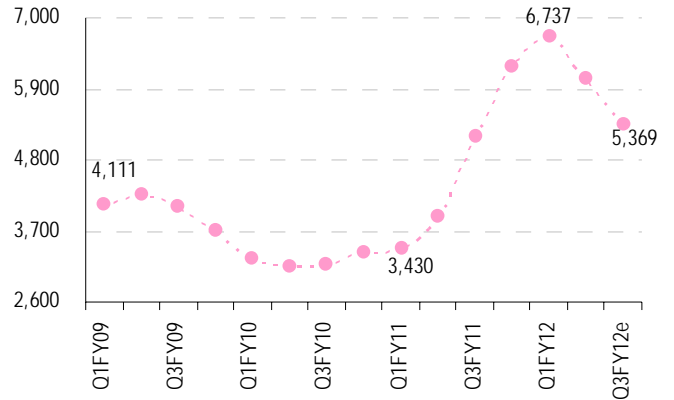
Source: PINC Research, Bloomberg *Till date

Exhibit 78 - Yearly Avg. Copra Prices (Rs/quintal)



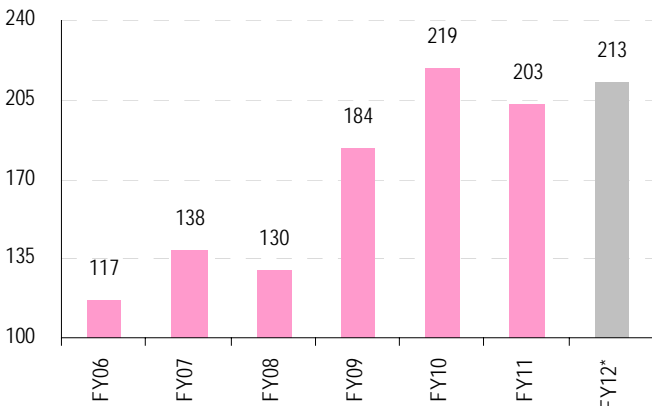
Source: PINC Research, Bloomberg *Till date

Exhibit 79 - Quarterly Avg. Copra Prices (Rs/quintal)



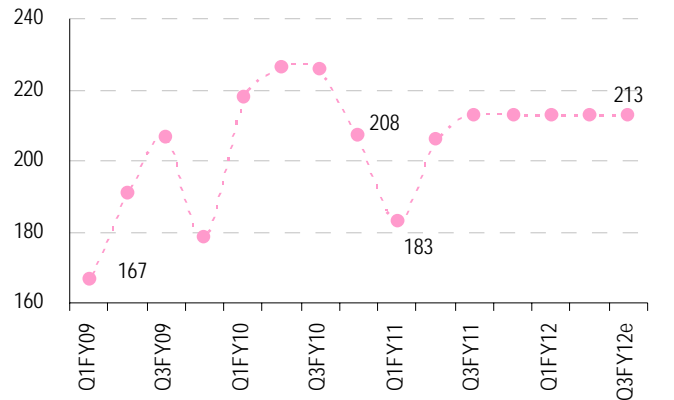
Source: PINC Research, Bloomberg *Till date

Exhibit 80 - Yearly Avg. Tea Prices (Rs/quintal)



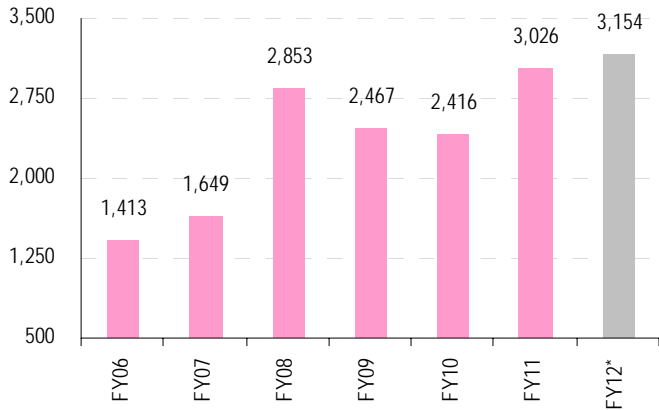
Source: PINC Research, Bloomberg *Till date

Exhibit 81 - Quarterly Avg. Tea Prices (Rs/quintal)



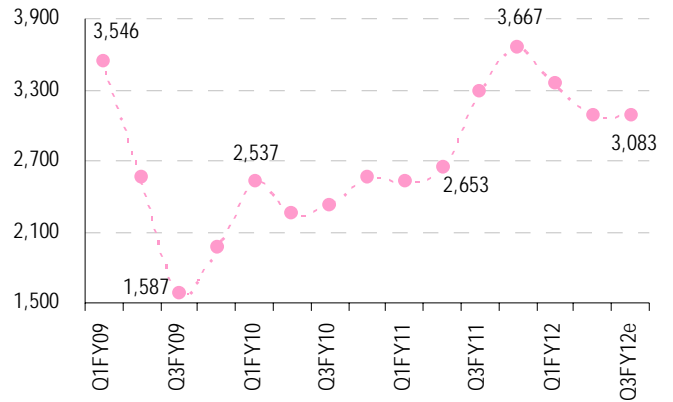
Source: PINC Research, Bloomberg *Till date

Exhibit 82 - Yearly Avg. Palm oil Prices (MYR/mt)



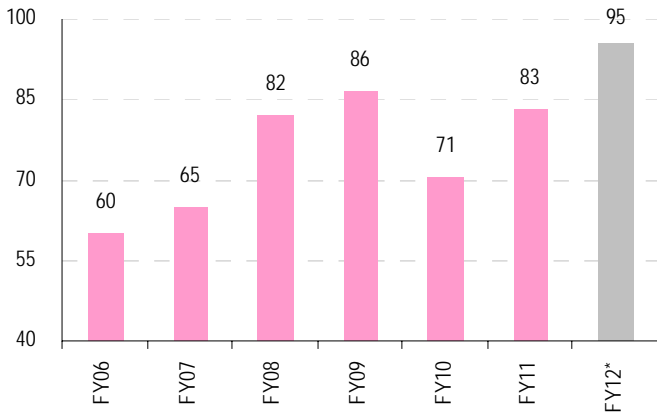
Source: PINC Research, Bloomberg *Till date

Exhibit 83 - Quarterly Avg. Palm oil Prices (MYR/mt)



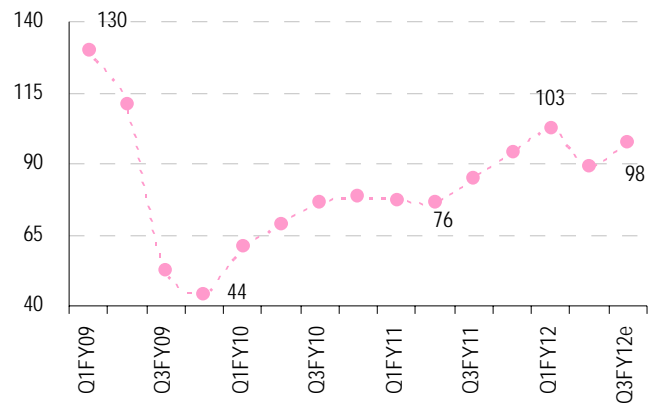
Source: PINC Research, Bloomberg *Till date

Exhibit 84 - Yearly Avg. Crude (USD/barrel)



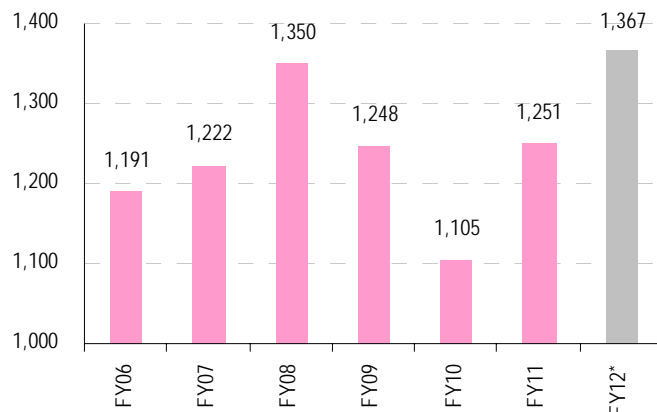
Source: PINC Research, Bloomberg *Till date

Exhibit 85 - Quarterly Avg. Crude (USD/barrel)



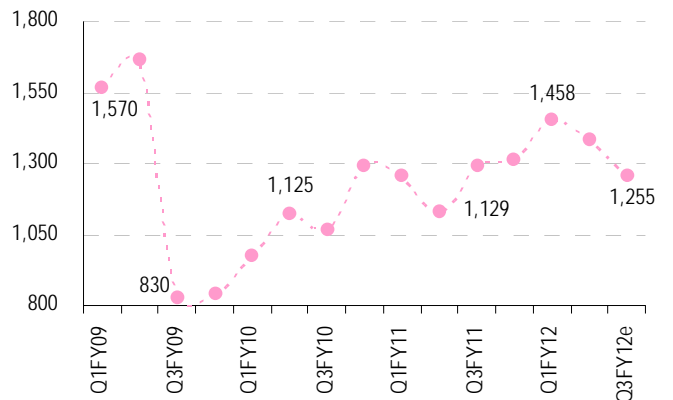
Source: PINC Research, Bloomberg *Till date

Exhibit 86 - Yearly Avg. HDPE (USD/mt)



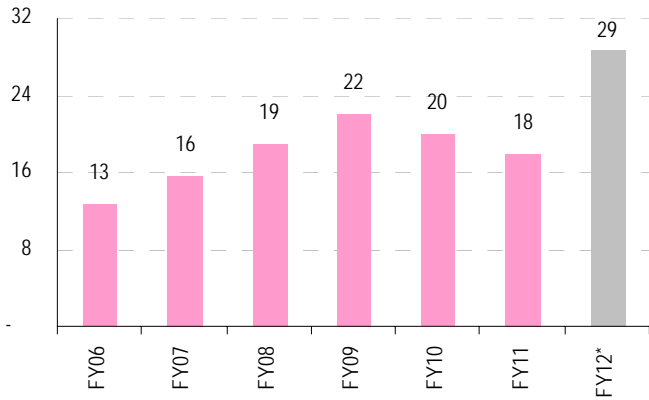
Source: PINC Research, Bloomberg *Till date

Exhibit 87 - Quarterly Avg. HDPE (USD/mt)



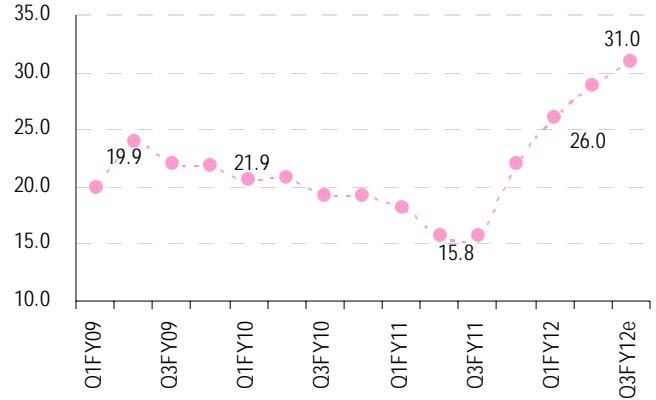
Source: PINC Research, Bloomberg *Till date

Exhibit 88 - Yearly Avg. Soda Ash (Rs/kg)



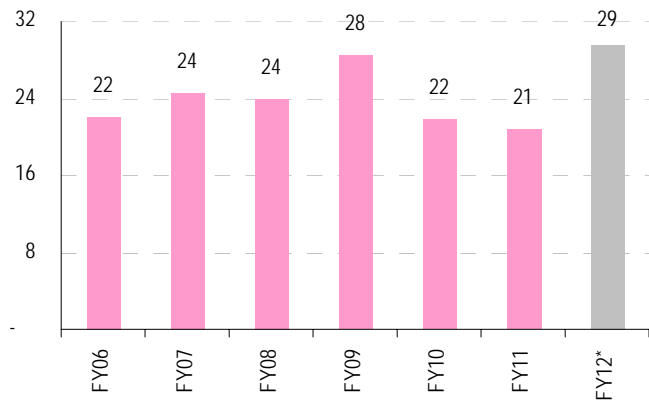
Source: PINC Research, Bloomberg *Till date

Exhibit 89 - Quarterly Avg. Soda Ash (Rs/kg)



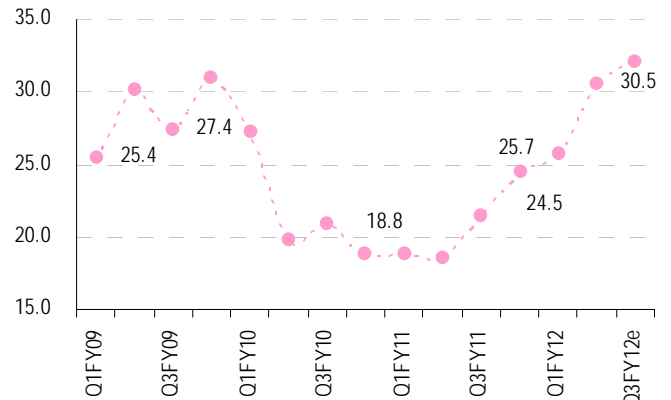
Source: PINC Research, Bloomberg *Till date

Exhibit 90 - Yearly Avg. Caustic Soda (Rs/kg)



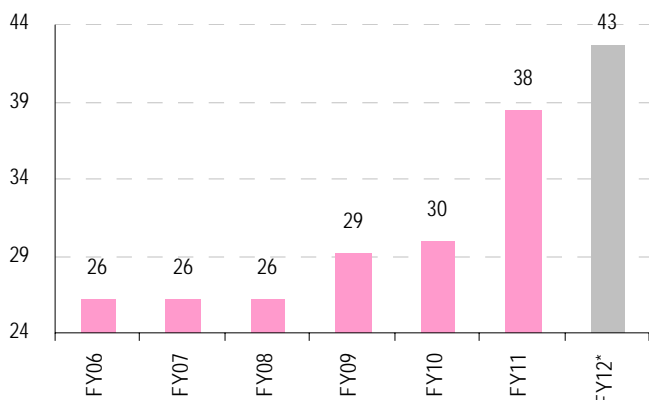
Source: PINC Research, Bloomberg *Till date

Exhibit 91 - Quarterly Avg. Caustic Soda (Rs/kg)



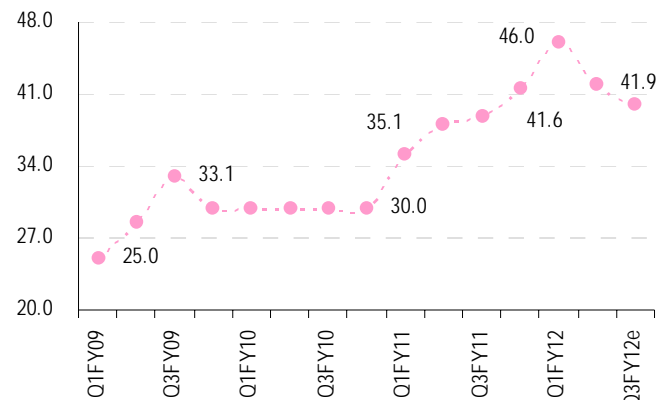
Source: PINC Research, Bloomberg *Till date

Exhibit 92 - Yearly Avg. Sorbitol (Rs/kg)



Source: PINC Research, Bloomberg *Till date

Exhibit 93 - Quarterly Avg. Sorbitol (Rs/kg)



Source: PINC Research, Bloomberg *Till date

Exhibit 94 - Staff Cost (% of sales)

| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|----------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| ITC | 7.1% | 7.8% | 7.3% | 7.0% | 6.9% | 7.3% | 8.0% | 7.7% | 7.8% |
| HUL | 6.3% | 6.3% | 6.7% | 6.3% | 6.2% | 5.7% | 6.1% | 6.4% | 5.1% |
| Nestle India | 7.3% | 7.2% | 7.2% | 7.2% | 7.5% | 7.5% | 7.1% | 8.4% | 6.9% |
| Dabur | 7.6% | 6.8% | 6.7% | 7.3% | 7.5% | 8.0% | 7.7% | 7.9% | 7.3% |
| Colgate | 7.7% | 7.4% | 7.8% | 8.5% | 12.8% | 7.8% | 8.2% | 7.9% | 8.5% |
| Marico | 4.5% | 5.2% | 5.1% | 6.8% | 5.8% | 6.7% | 6.9% | 7.3% | 7.4% |
| Jyothy Labs | 6.8% | 9.0% | 10.7% | 11.5% | 11.7% | 13.5% | 13.1% | 12.6% | 13.2% |
| GCPL | 5.0% | 4.8% | 5.4% | 6.8% | 5.7% | 6.6% | 6.2% | 7.4% | 7.8% |
| GSK Consumers | 12.9% | 12.2% | 12.0% | 11.9% | 11.8% | 11.8% | 10.8% | 10.1% | 9.6% |
| Emami Ltd | 4.8% | 5.3% | 5.6% | 4.9% | 4.4% | 5.7% | 6.4% | 6.4% | 5.6% |
| Britannia Industries | 6.4% | 6.3% | 4.5% | 4.0% | 3.5% | 4.5% | 4.6% | 4.4% | 3.9% |

Source: PINC Research, Company

High Pay : Jyothy Labs, GSK Consumers

Low Pay : Britannia, HUL

Average Pay : ITC, Nestle India, Dabur, Colgate, Marico, GCPL

Exhibit 95 - Advertisement and Sales Promotion (% of sales)

| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|----------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| ITC | 3.8% | 4.1% | 2.9% | 2.3% | 2.5% | 2.8% | 3.2% | 2.8% | 2.9% |
| HUL | 8.4% | 7.2% | 8.1% | 8.8% | 10.2% | 10.3% | 10.4% | 13.4% | 14.0% |
| Nestle India | 7.7% | 6.3% | 5.4% | 5.5% | 5.3% | 4.9% | 4.5% | 5.2% | 4.8% |
| Dabur | 13.0% | 13.5% | 13.6% | 11.8% | 12.5% | 12.5% | 12.2% | 14.5% | 13.1% |
| Colgate | 19.4% | 15.7% | 14.2% | 17.3% | 15.6% | 16.9% | 15.6% | 14.8% | 15.3% |
| Marico | 8.3% | 8.5% | 9.6% | 12.1% | 13.6% | 12.8% | 10.2% | 13.2% | 11.1% |
| Jyothy Labs | 22.7% | 27.0% | 11.7% | 9.5% | 9.4% | 8.0% | 5.1% | 6.4% | 9.0% |
| GCPL | 7.9% | 7.0% | 11.0% | 10.3% | 11.4% | 11.9% | 9.9% | 9.9% | 11.2% |
| GSK Consumers | 11.4% | 12.3% | 11.8% | 13.1% | 12.9% | 12.9% | 12.6% | 15.7% | 16.1% |
| Emami Ltd | 5.0% | 1.7% | 1.3% | 2.4% | 20.3% | 18.0% | 19.2% | 19.0% | 17.4% |
| Britannia Industries | 7.3% | 8.0% | 6.7% | 6.3% | 6.1% | 6.6% | 6.9% | 8.0% | 7.3% |

Source: PINC Research, Company

High Spending : HUL, Colgate, Dabur and Emami

Low Spending : ITC, Nestle,

Average Spending : Marico, Jyothy Labs, GCPL, Britannia Industries

- ITC's A&P spending mainly occurs on its FMCG business which includes branded packaged foods, personal care, education & stationary and life style retailing. Therefore A&P spending ratio in total sales is very low otherwise for FMCG business ITC's A&P spending is competitive enough.
- Nestle India doesn't spend on infant foods business and we believe spending on milk products also entail low A&P spending. Nestle's large part of the expense happens on Noodles, Chocolates and Beverages in the same order. Excluding Infant foods and Milk business, Nestle's A&P spending is in the range of 8-9% which comes in the average spending category. With rising competition in almost all the categories, we expect higher A&P spending going forward.

Exhibit 96 - Distribution Expense (% of sales)

| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|----------------------|------|------|------|------|------|------|------|------|------|
| ITC | 2.8% | 2.9% | 3.3% | 3.5% | 3.7% | 3.8% | 4.1% | 3.4% | 3.4% |
| HUL | 4.1% | 4.4% | 4.9% | 5.0% | 5.3% | 5.2% | 5.5% | 4.8% | 5.3% |
| Nestle India | 5.1% | 4.9% | 4.9% | 4.8% | 4.7% | 4.6% | 4.7% | 4.7% | 5.0% |
| Dabur | 2.8% | 2.7% | 2.9% | 3.4% | 3.5% | 2.8% | 2.1% | 1.8% | 2.4% |
| Colgate | 1.7% | 1.7% | 1.7% | 2.2% | 2.2% | 2.3% | 2.5% | 2.5% | 3.1% |
| Marico | 4.0% | 3.9% | 3.8% | 3.8% | 3.7% | 4.1% | 3.9% | 3.9% | 4.2% |
| Jyothy Labs | 1.3% | 1.8% | 1.4% | 1.9% | 2.2% | 2.9% | 2.6% | 2.5% | 2.9% |
| GCPL | 9.1% | 8.4% | 4.7% | 5.0% | 3.4% | 3.0% | 2.6% | 2.5% | 2.6% |
| GSK Consumers | 5.1% | 4.1% | 4.6% | 4.7% | 5.2% | 5.2% | 5.1% | 4.7% | 4.9% |
| Emami Ltd | 2.9% | 3.3% | 3.5% | 2.7% | 2.6% | 2.6% | 2.5% | 2.2% | 2.7% |
| Britannia Industries | 3.1% | 3.7% | 3.8% | 6.0% | 7.4% | 6.8% | 6.9% | 6.7% | 6.5% |

Source: PINC Research, Company

High Expense : Britannia Industries, HUL
 Low Expense : Dabur, GCPL, Jyothy Labs, Emami
 Average Expense : Nestle, Marico, Colgate, GSK Consumers, ITC

Exhibit 97 - Other Income (% of PBT)

| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|----------------------|-------|--------|-------|-------|-------|-------|-------|-------|-------|
| ITC | 9.5% | 10.4% | 19.9% | 9.9% | 9.3% | 12.8% | 10.6% | 10.4% | 10.7% |
| HUL | 13.0% | 15.9% | 12.8% | 9.8% | 10.4% | 11.1% | 9.1% | 3.0% | 9.6% |
| Nestle India | 5.3% | 5.5% | 3.6% | 5.6% | 6.4% | 13.3% | 4.2% | 3.0% | 3.2% |
| Dabur | 3.1% | 4.6% | 3.3% | 3.7% | 6.1% | 5.6% | 7.3% | 5.5% | 6.6% |
| Colgate | 24.9% | 19.7% | 19.2% | 13.6% | 15.5% | 13.9% | 16.0% | 9.0% | 8.2% |
| Marico | 18.8% | 6.8% | 7.8% | 9.6% | 18.3% | 9.8% | 5.3% | 6.1% | 7.4% |
| Jyothy Labs | 14.4% | -28.9% | 15.4% | 19.9% | 19.5% | 21.1% | 14.3% | 17.4% | 29.2% |
| GCPL | 2.9% | 3.0% | 7.5% | 6.9% | 7.1% | 2.4% | 19.1% | 10.5% | 16.0% |
| GSK Consumers | 39.0% | 46.0% | 36.7% | 26.8% | 17.2% | 14.2% | 19.8% | 12.2% | 13.2% |
| Emami Ltd | 1.6% | 6.7% | 6.0% | 11.3% | 24.1% | 21.5% | 22.9% | 20.4% | 1.5% |
| Britannia Industries | 35.7% | 44.3% | 52.8% | 19.5% | 30.3% | 25.1% | 42.2% | 53.6% | 34.7% |

Source: PINC Research, Company

High Share : Britannia Industries, Jyothy Labs, GCPL, GSK Consumers
 Low Share : Nestle India, Emami Ltd
 Average Share : ITC, HUL, Colgate, Marico, Dabur

Exhibit 98 - Dividend Payout Ratio (%)

| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|----------------------|-------|-------|-------|-------|-------|--------|-------|-------|-------|
| ITC | 27.6% | 30.6% | 41.0% | 42.6% | 42.4% | 41.9% | 42.0% | 92.8% | 69.5% |
| HUL | 73.1% | 93.6% | 96.7% | 81.0% | 87.2% | 113.8% | 65.6% | 67.6% | 66.1% |
| Nestle India | 83.7% | 73.6% | 93.6% | 77.9% | 75.1% | 73.8% | 75.8% | 71.1% | 57.1% |
| Dabur | 47.2% | 54.4% | 46.7% | 44.8% | 44.5% | 39.7% | 40.6% | 35.4% | 30.6% |
| Colgate | 67.8% | 75.6% | 81.8% | 77.0% | 66.5% | 76.3% | 69.8% | 67.3% | 67.6% |
| Marico | 26.8% | 45.4% | 44.5% | 41.9% | 41.3% | 24.9% | 20.0% | 15.9% | 15.2% |
| Jyothy Labs | 7.9% | na | 8.1% | 22.9% | 17.5% | 32.3% | 37.8% | 39.1% | 58.6% |
| GCPL | 77.4% | 86.1% | 78.9% | 66.1% | 61.0% | 58.3% | 59.4% | 37.2% | 34.0% |
| GSK Consumers | 37.4% | 39.0% | 43.4% | 31.3% | 33.1% | 31.0% | 33.7% | 32.1% | 70.5% |
| Emami Ltd | 7.6% | 7.9% | 20.8% | 25.2% | 37.4% | 31.3% | 37.0% | 27.1% | 20.3% |
| Britannia Industries | 25.3% | 22.9% | 22.5% | 24.5% | 34.1% | 24.2% | 63.1% | 57.9% | 57.8% |

Source: PINC Research, Company

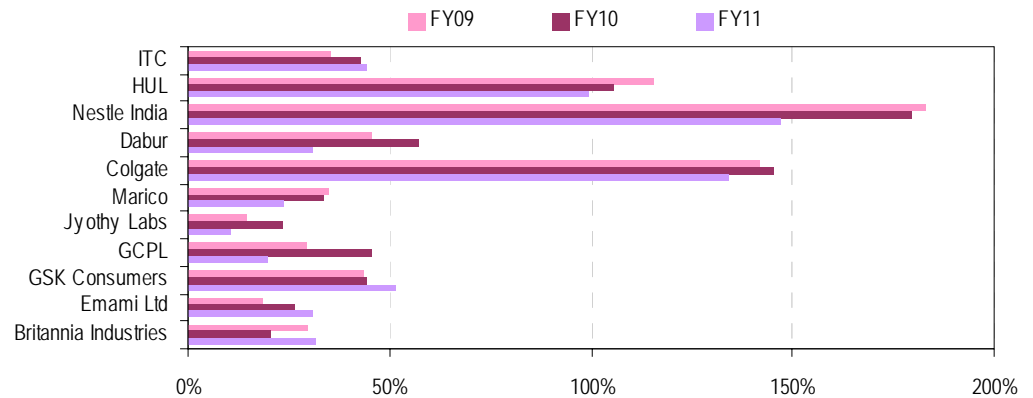
High Paying : ITC, HUL, Colgate, GSK Consumers
 Low Paying : Marico, Emami, Dabur, GCPL
 Average Paying : Nestle India, Jyothy Labs, Britannia

Exhibit 99 - Effective Tax Rate (%)

| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|----------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| ITC | 34.3% | 31.6% | 27.6% | 30.7% | 31.4% | 32.0% | 32.6% | 32.9% | 31.8% |
| HUL | 22.7% | 21.2% | 22.0% | 16.7% | 17.9% | 19.0% | 17.8% | 22.6% | 21.6% |
| Nestle India | 35.7% | 34.1% | 34.8% | 34.0% | 34.4% | 34.0% | 30.7% | 28.6% | 28.5% |
| Dabur | 12.8% | 12.0% | 10.8% | 12.3% | 11.7% | 13.2% | 12.1% | 16.7% | 19.6% |
| Colgate | 40.3% | 28.7% | 36.4% | 26.8% | 20.6% | 20.7% | 16.0% | 12.7% | 22.6% |
| Marico | 12.2% | 9.7% | 5.6% | 11.3% | 24.8% | 17.5% | 17.8% | 21.6% | 22.6% |
| Jyothy Labs | 16.7% | 16.8% | 21.2% | 18.7% | 12.5% | 25.0% | 22.4% | 22.5% | 19.0% |
| GCPL | 24.4% | 20.6% | 11.5% | 8.5% | 10.7% | 14.2% | 15.2% | 18.9% | 20.1% |
| GSK Consumers | 32.9% | 22.2% | 36.8% | 34.0% | 33.4% | 33.6% | 33.7% | 34.4% | 33.6% |
| Emami Ltd | 13.3% | 12.6% | 6.5% | 1.9% | 11.4% | 11.9% | 13.3% | 17.2% | 17.0% |
| Britannia Industries | 33% | 36% | 32% | 27% | 10% | 19% | 27% | 27% | 27% |

Source: PINC Research, Company

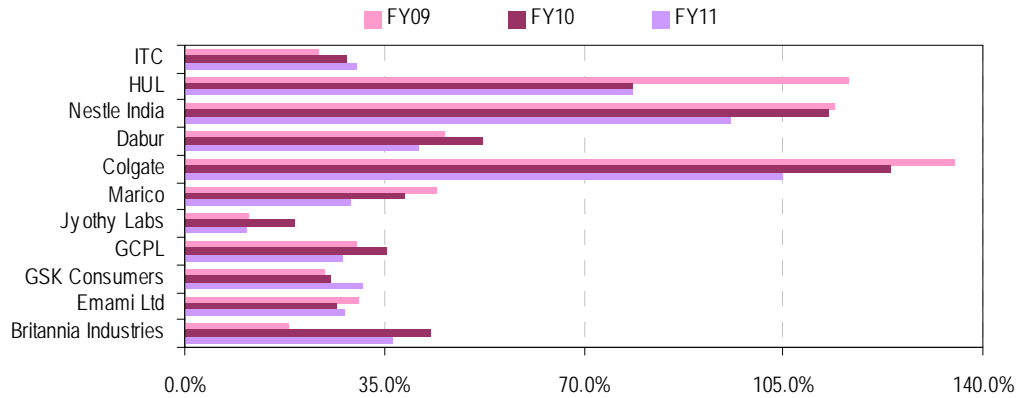
Exhibit 100 - ROCE (%)



Source: PINC Research, Company

Improved : ITC, GSK Consumers, Emami
 Decline : Nestle India, Jyothy Labs, Dabur, Marico, GCPL
 Maintained : HUL, Colgate, Britannia

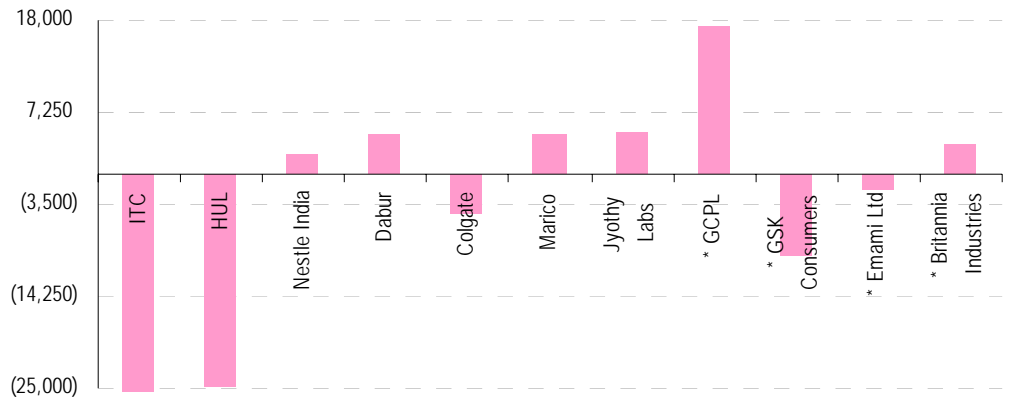
Exhibit 101 - ROE



Source: PINC Research, Company

- Improved : ITC, Britannia
- Decline : HUL, Nestle India, Jyothy Labs, Marico, Colgate
- Maintained : Dabur, GCPL, GSK Consumers, Emami

Exhibit 102 - Net Debt Position (FY12E)



Source: PINC Research, Company * Bloomberg Consensus

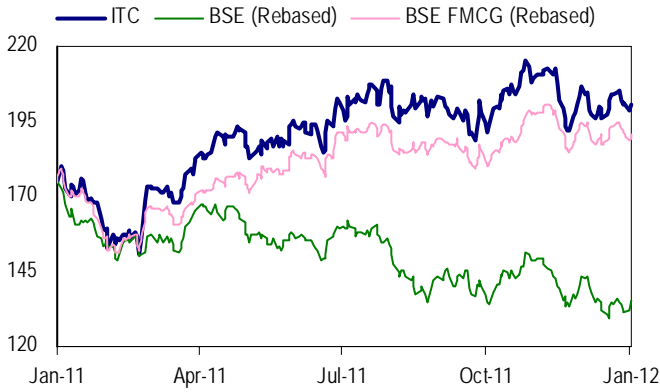
Exhibit 103 - Cash Flow From Operations

| Companies | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|----------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| ITC | 18,459 | 19,984 | 15,872 | 20,966 | 22,476 | 30,067 | 35,335 | 44,433 | 54,536 |
| HUL | 16,196 | 15,742 | 12,265 | 20,094 | 16,714 | 17,289 | 20,541 | 34,797 | 19,102 |
| Nestle India | 3,355 | 3,588 | 3,652 | 4,031 | 4,186 | 5,192 | 7,236 | 9,280 | 10,368 |
| Dabur | 1,472 | 0 | 2,157 | 2,187 | 2,098 | 3,821 | 3,222 | 4,989 | 5,011 |
| Colgate | 1,657 | 801 | 1,212 | 1,878 | 1,577 | 2,914 | 3,497 | 4,040 | 3,855 |
| Marico | 646 | 797 | 402 | 1,648 | 1,924 | 1,429 | 1,847 | 2,021 | 3,134 |
| Jyothy Labs | (272) | 26 | 390 | 512 | 324 | 566 | 299 | 503 | (55) |
| GCPL | 707 | 843 | 898 | 1,427 | 1,204 | 1,622 | 1,433 | 3,385 | 2,061 |
| GSK Consumers | 1,523 | 1,455 | 1,291 | 985 | 1,386 | 1,881 | 1,347 | 4,000 | 3,262 |
| Emami Ltd | 308 | 186 | 317 | 513 | 494 | 224 | 2,542 | 1,462 | 1,265 |
| Britannia Industries | 571 | 738 | 689 | 1,506 | 1,308 | 691 | 2,503 | 2,377 | 2,761 |

Source: PINC Research, Company

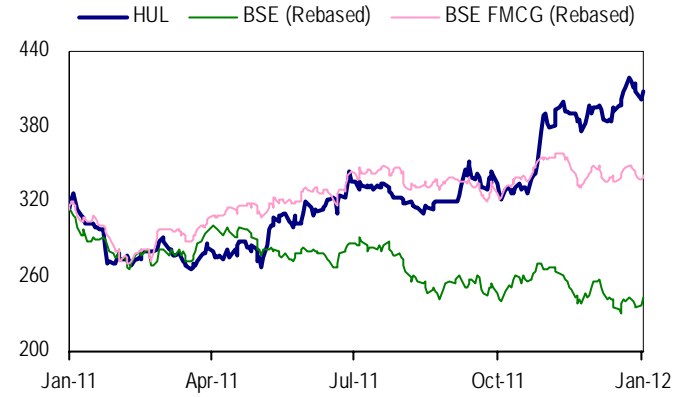
Past One Year Performance

Exhibit 104 - ITC Stock Performance



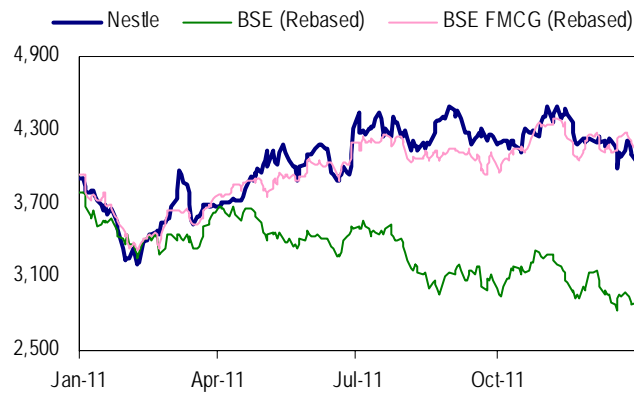
Source: Bloomberg

Exhibit 105 - HUL Stock Performance



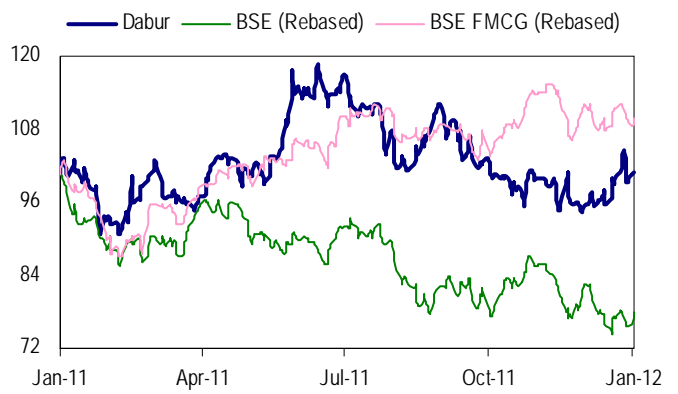
Source: Bloomberg

Exhibit 106 - Nestle India Stock Performance



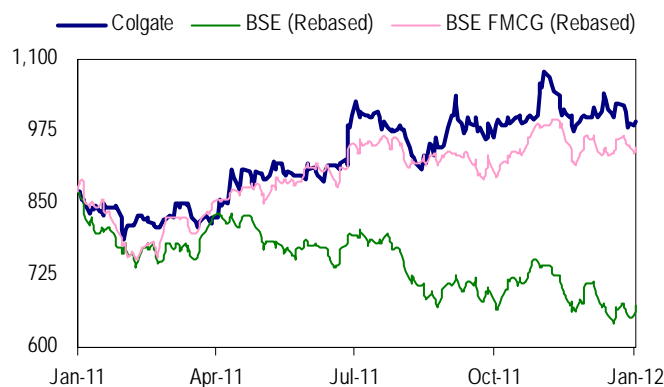
Source: Bloomberg

Exhibit 107 - Dabur Stock Performance



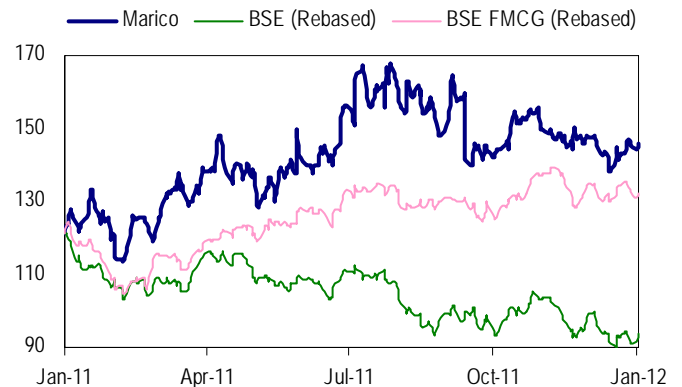
Source: Bloomberg

Exhibit 108 - Colgate Stock Performance



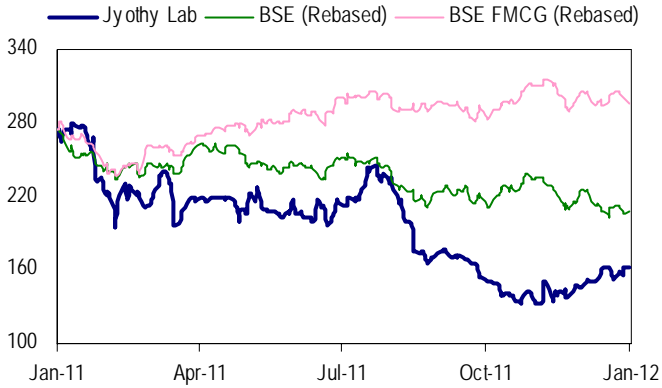
Source: Bloomberg

Exhibit 109 - Marico Stock Performance



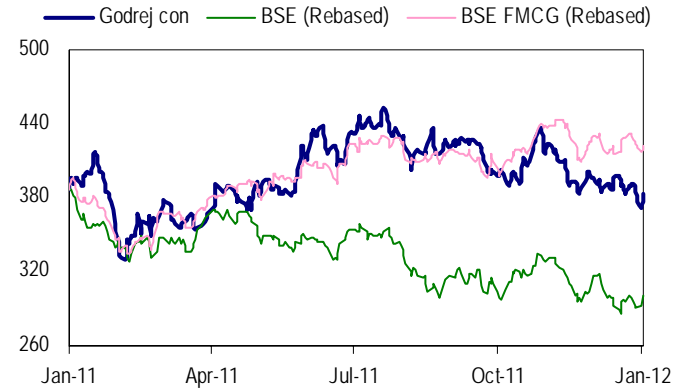
Source: Bloomberg

Exhibit 110 - Jyothy Labs Stock Performance



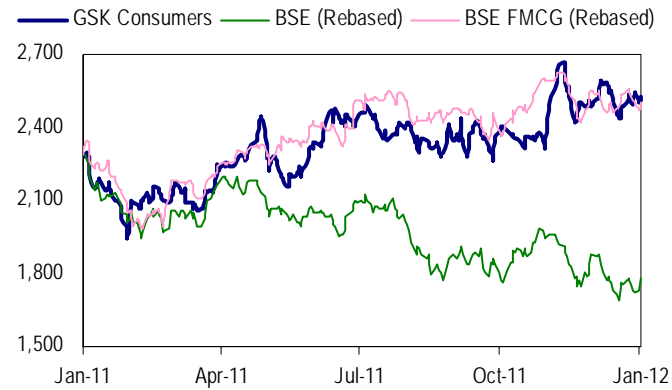
Source: Bloomberg

Exhibit 111 - Godrej Consumers Stock Performance



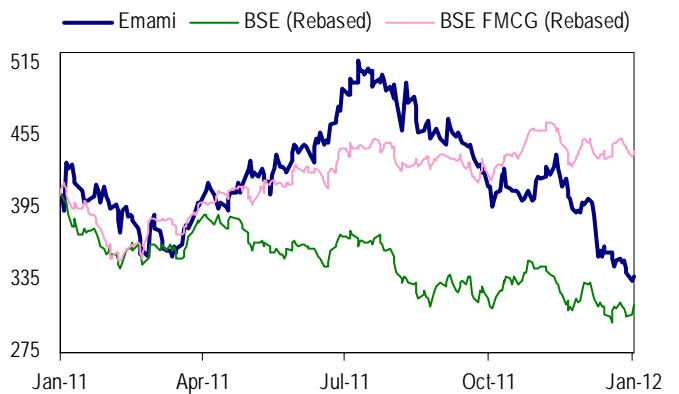
Source: Bloomberg

Exhibit 112 - GSK Consumers Stock Performance



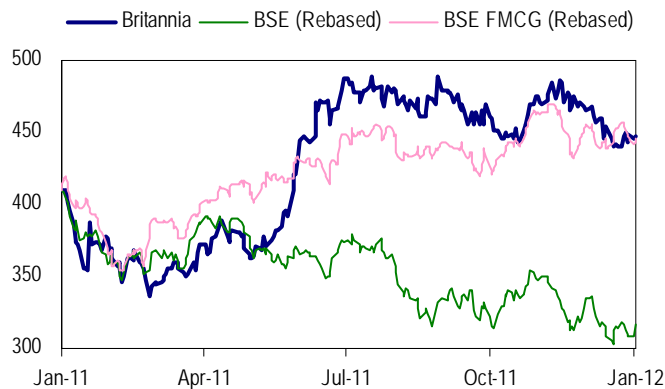
Source: Bloomberg

Exhibit 113- Emami Stock Performance



Source: Bloomberg

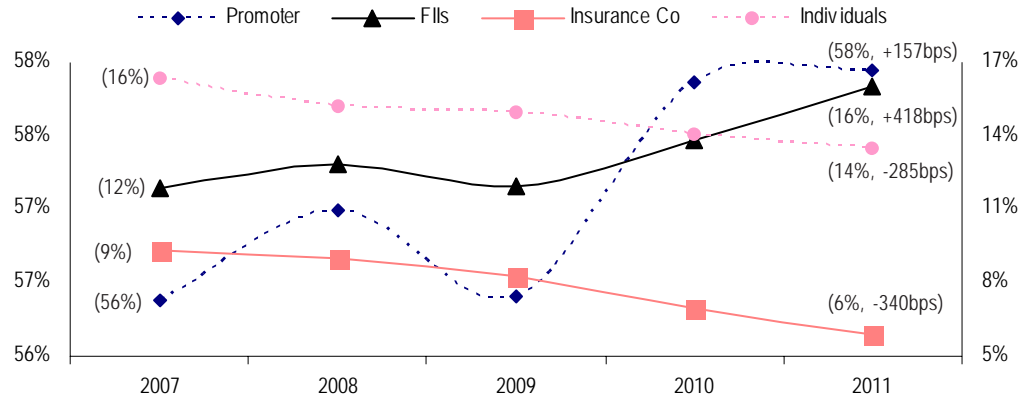
Exhibit 114 - Britannia Stock Performance



Source: Bloomberg

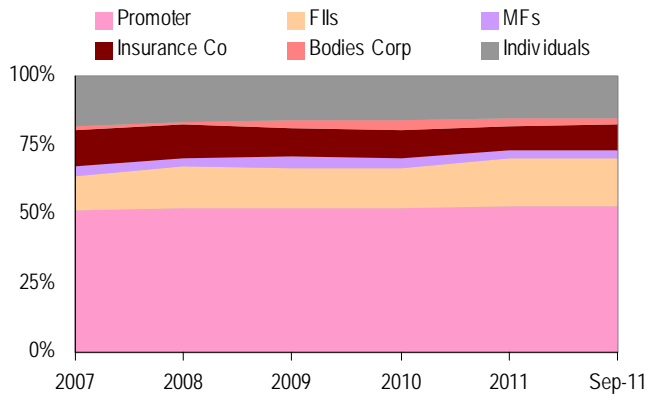
Shareholding Pattern - Higher FII Holdings

Exhibit 115 - Sector Weighted Shareholding Pattern (%) Ex-ITC



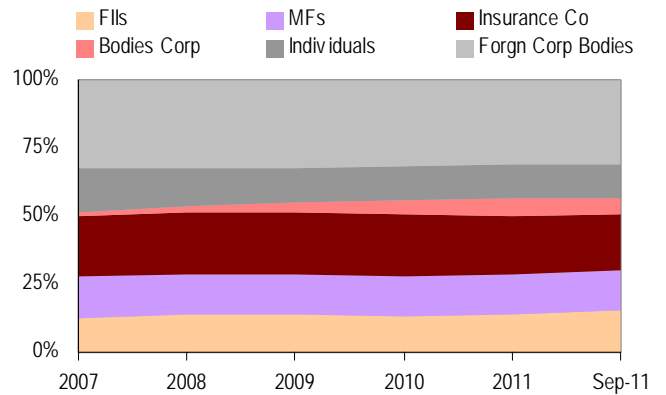
Source: PINC Research

Exhibit 116 - HUL Shareholding Pattern (%)



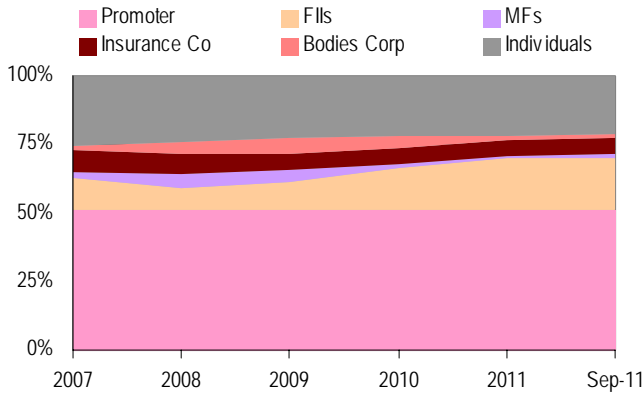
Source: PINC Research

Exhibit 117 - ITC Shareholding Pattern (%)



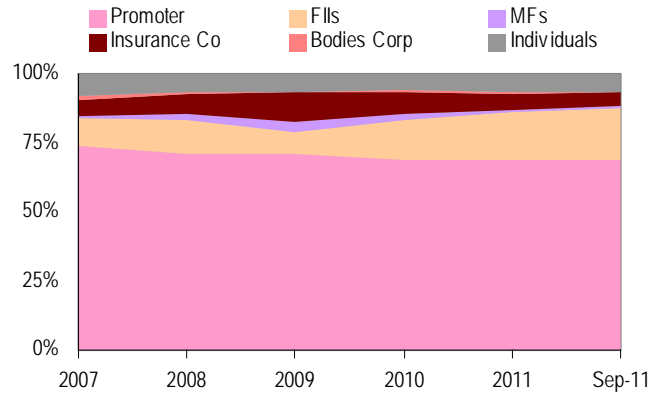
Source: PINC Research

Exhibit 118 - Colgate Shareholding Pattern (%)



Source: PINC Research

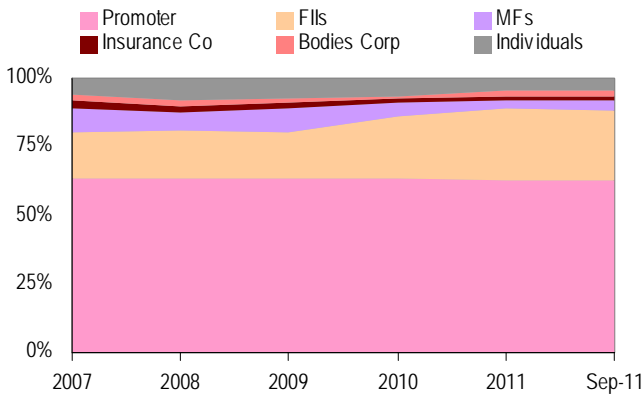
Exhibit 119- Dabur Shareholding Pattern (%)



Source: PINC Research

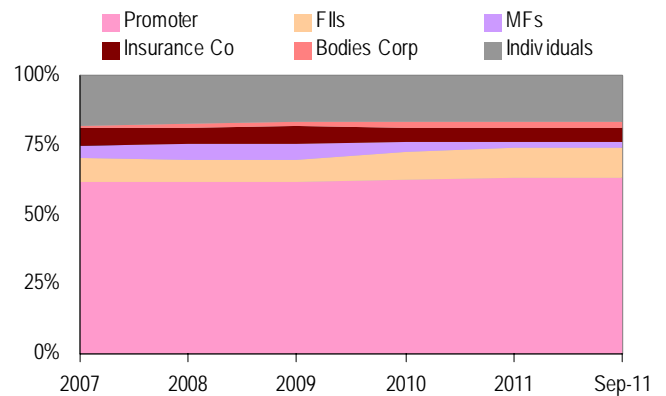
- Marico's FIs stake has increased to 26% in Mar-11 from 17% in Mar-09; this resulted into lower stake with small shareholders.

Exhibit 120 - Marico Shareholding Pattern (%)



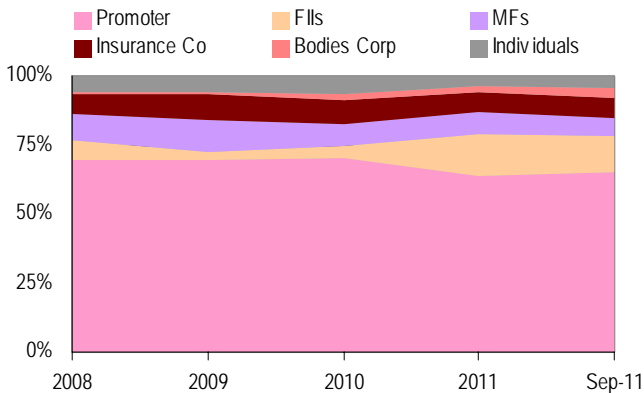
Source: PINC Research

Exhibit 121 - Nestle Shareholding Pattern (%)



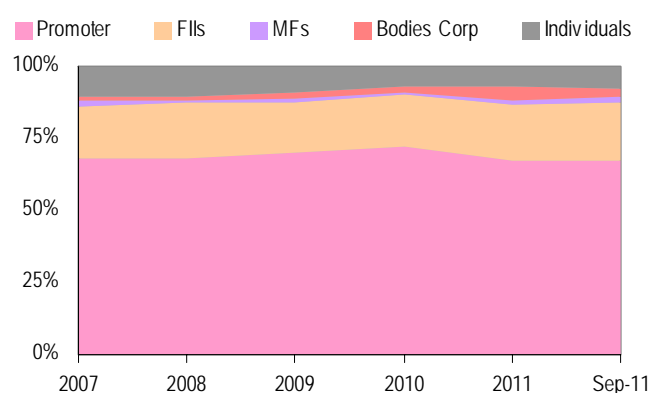
Source: PINC Research

Exhibit 122 - Jyothy Shareholding Pattern (%)



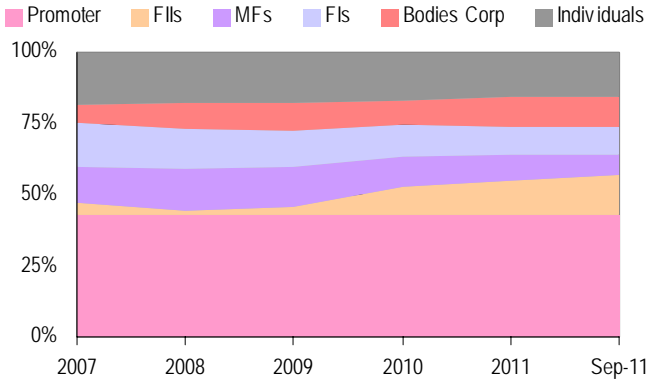
Source: PINC Research

Exhibit 123 - Godrej Cons. Shareholding Pattern (%)



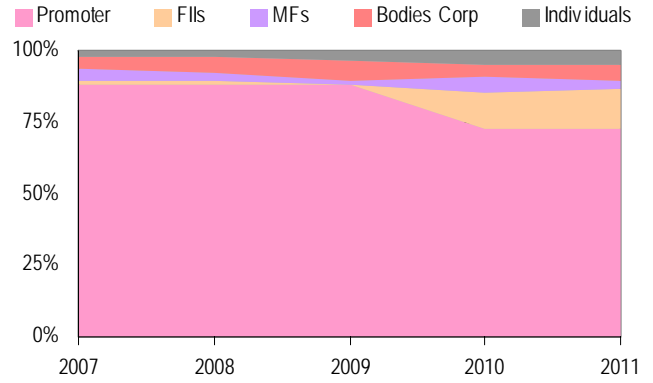
Source: PINC Research

Exhibit 124 - GSK Cons.Shareholding Pattern (%)



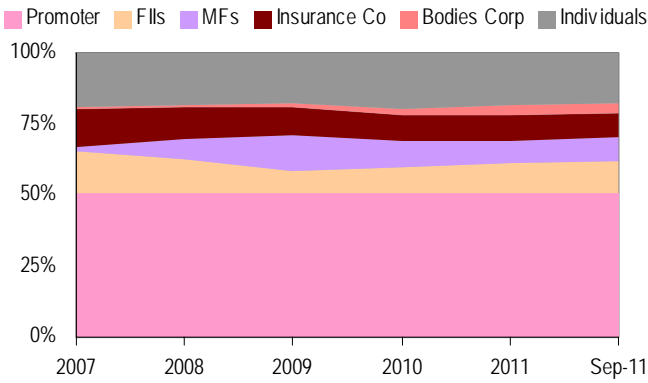
Source: PINC Research

Exhibit 125 - Emami Shareholding Pattern (%)



Source: PINC Research

Exhibit 126 - Britannia Shareholding Pattern (%)



Source: PINC Research

COMPANIES

- ITC
- HUL
- Nestle India
- Dabur India
- Colgate-Palmolive (India)
- Marico
- Jyothy Labs

Initiating Coverage
 Sector: FMCG
 BSE Sensex: 15,868

ITC

 BUY
 CMP Rs202
 TP Rs233

09 January 2012

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 naveent@pinc.co.in

Cigarette still profitability lighter

ITC is a diversified conglomerate with a presence in cigarette, FMCG, hotel, paperboard and agribusiness. Despite its presence in various business segments, cigarette still draws a major part of profitability with +80% share in PBIT. We expect cigarette segment gross sales to show ~13% CAGR during FY11-14E driven by ~3% and ~10% CAGR in volume and price. Besides, superior performance of non cigarette business would help in achieving ~17% CAGR in net sales for ITC during FY11-14E. ITC's profitability should remain strong on the assumption of expansion of PBIT/cigarette, profitable conversion of FMCG business and retention of profitability by other segments. We expect net earnings to deliver ~19% CAGR during FY11-14E.

Cigarette dominance to persist

Compared to the other FMCG segment, cigarette has relatively low competitive pressure and ITC has retained its leadership position due to its extensive cigarette offering, large distribution and consumers' stickiness towards ITC brands. We expect ITC's strong pricing power would help in maintaining the healthy growth.

Superior performance of non cigarette business

FMCG business has grown 15x in past 8 years through consistent entry into new segments backed by aggressive marketing strategy of ITC. We expect segment to clock 20% CAGR during FY11-14E owing to better foothold of the existing portfolio and consistent investment in innovation. Paperboard and Agribusiness would maintain their robust growth and we expect 16% and 13% CAGR during FY11-14E respectively.

Profitability would remain high

ITC's profitability would remain strong on the assumption of expansion of PBIT/cigarette to 103paise in FY14E compared to 71paise in FY11, profitable conversion of FMCG business and retention of profitability by other segments.

VALUATIONS AND RECOMMENDATION

We value ITC using DCF methodology and arrive at a target price of Rs233. We believe relative valuation is not feasible as there is no appropriate comparable for ITC. The stock has 15% upside potential hence we initiate ITC with 'BUY' rating. As ITC has high dependence on cigarette business hence any significant change in the govt. regulation on cigarette can lead to change in our estimates.

KEY FINANCIALS (CONSOLIDATED)

| | (Rs mn) | | | | |
|-----------------|---------|---------|---------|---------|---------|
| | FY10 | FY11 | FY12E | FY13E | FY14E |
| Net Sales | 191,359 | 222,737 | 267,694 | 309,394 | 355,647 |
| YoY Gr. (%) | 15.6 | 16.4 | 20.2 | 15.6 | 14.9 |
| Op. Profits | 62,730 | 74,208 | 91,485 | 106,812 | 122,803 |
| OPM (%) | 32.8 | 33.3 | 34.2 | 34.5 | 34.5 |
| Adj. Net Profit | 41,123 | 49,558 | 61,963 | 72,800 | 84,095 |
| YoY Gr. (%) | 23.8 | 20.5 | 25.0 | 17.5 | 15.5 |

KEY RATIOS

| | | | | | |
|---------------|------|------|------|------|------|
| Dil EPS (Rs) | 5.3 | 6.4 | 8.0 | 9.4 | 10.9 |
| ROCE (%) | 42.7 | 44.4 | 45.6 | 44.5 | 43.0 |
| RONW (%) | 28.4 | 30.1 | 31.4 | 30.8 | 30.0 |
| P/E (x) | 38.0 | 31.5 | 25.2 | 21.5 | 18.6 |
| EV/Sales (x) | 7.8 | 6.7 | 5.6 | 4.7 | 4.0 |
| EV/EBITDA (x) | 23.9 | 20.1 | 16.2 | 13.6 | 11.6 |

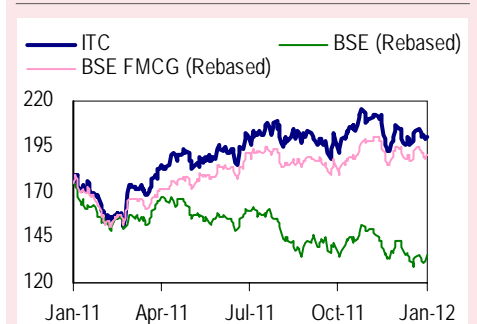
STOCK DATA

| | |
|----------------------------|-----------|
| Market cap | Rs1,563bn |
| Book Value per share | Rs21 |
| Shares O/S (F.V. Rs1) | 7,738mn |
| Free Float | 100% |
| Avg Trade Value (6 months) | Rs1,574mn |
| 52 week High/Low | 216/150 |
| Bloomberg Code | ITCIN |
| Reuters Code | ITC.BO |

PERFORMANCE (%)

| | 1M | 3M | 12M |
|----------|-------|-----|------|
| Absolute | (2.1) | 2.9 | 11.7 |
| Relative | 3.7 | 2.5 | 42.2 |

RELATIVE PERFORMANCE



INVESTMENT ARGUMENT

Cigarette growth to drive the overall profitability

In the last Union Budget there were no changes in the central excise duty structure which led to the expectation of higher volume growth for FY12. However, during the past 6 months, most of the states increased state VAT rate which forced ITC to increase cigarette prices on key brands. We anticipate moderate cigarette volume growth of 6% for FY12 which would help in expanding gross sales by ~16% during FY12. Further, better revenue mix and strong pricing power would help ITC to sustain this high growth in cigarette; we foresee ~13% gross sales CAGR during FY11-14E.

Better revenue mix, higher operational efficiency and significant cigarette price rise enabled ITC to expand PBIT per cigarette (stick) to 71paise in FY11 from 30paise in FY03. We expect profitability to remain high on account of focus on operational efficiency and pricing power due to low competitive intensity leading to expansion in PBIT/stick to 103paise by FY14E.

Exhibit 1 - Cigarette Profitability to Improve Further

| | FY07 | FY08 | FY09 | FY10 | FY11 | FY12E | FY13E | FY14E |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|
| Cig Volume Gr. (%) | 7.1% | -0.7% | -2.9% | 7.2% | -2.8% | 6.1% | 3.0% | 1.0% |
| Cig Gross Price Gr. (%) | 5.8% | 8.5% | 12.6% | 6.7% | 18.0% | 8.9% | 10.0% | 9.9% |
| Cig Gross Sales Gr. (%) | 13.3% | 7.7% | 9.3% | 14.4% | 14.7% | 15.5% | 13.3% | 11.0% |
| Cig Net Sales Gr. (%) | 16.1% | 12.6% | 13.9% | 21.0% | 15.8% | 21.7% | 14.4% | 13.0% |
| Cig PBIT (Rs/stick) | 0.39 | 0.45 | 0.53 | 0.59 | 0.71 | 0.82 | 0.91 | 1.03 |
| Cig PBIT Gr.(%) | 17.1% | 14.6% | 15.1% | 18.0% | 16.8% | 23.1% | 14.8% | 13.8% |
| ITC EBIT Gr. (%) | 19.3% | 13.0% | 9.6% | 23.9% | 20.2% | 22.5% | 16.8% | 16.0% |

Source: PINC Research, Company

Exhibit 2 - ITC's Business Mix

| Segments | Net Sales Mix (%) | | | Sales CAGR (%) | | PBIT Margin (%) | | | PBIT Mix (%) | | | PBIT CAGR (%) | |
|--------------------------------|-------------------|-------|-------|----------------|----------|-----------------|-------|-------|--------------|-------|-------|---------------|----------|
| | FY08 | FY11 | FY14E | FY08-11 | FY11-14E | FY08 | FY11 | FY14E | FY08 | FY11 | FY14E | FY08-11 | FY11-14E |
| Cigarettes | 47.8% | 50.1% | 49.6% | 17.9% | 17.4% | 54.8% | 54.5% | 55.8% | 83.3% | 81.0% | 78.4% | 16.5% | 17.0% |
| FMCG | 18.7% | 21.9% | 24.0% | 16.7% | 16.1% | -10.5% | -6.7% | 1.0% | -6.0% | -4.2% | 0.7% | na | na |
| Hotels | 7.3% | 4.7% | 4.2% | 20.9% | 20.2% | 40.6% | 26.6% | 27.0% | 9.4% | 3.7% | 3.2% | -13.3% | 12.5% |
| Agribusiness | 17.5% | 13.1% | 12.1% | -0.5% | 12.3% | 3.3% | 11.9% | 12.0% | 3.0% | 8.0% | 6.8% | 62.9% | 12.4% |
| Paperboards, Paper & Packaging | 8.7% | 10.2% | 10.1% | 4.5% | 13.3% | 21.0% | 23.4% | 24.0% | 10.4% | 11.5% | 10.8% | 21.6% | 16.0% |

Source: PINC Research, Company

Low peer threat

Compared to the other FMCG segments, cigarette has relatively very low competitive pressure which has helped ITC to retain its leadership position in the market. Despite its premium pricing, ITC has succeeded in expanding volume and value market share by 500bps and 400bps to 75% and 83% respectively in the past 10 years. We expect ITC's cigarette dominance will remain high owing to its extensive cigarette offering, large distribution, consumers' stickiness towards brands and appropriate backward integration. The low profitability profile of other cigarette players will also restrict them to challenge ITC's leadership.

Exhibit 3 - Cigarette Gross Price (company level) Comparison (Rs/cig)

| Company | FY01 | FY02 | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|---------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| ITC | 1.15 | 1.32 | 1.38 | 1.41 | 1.43 | 1.49 | 1.58 | 1.71 | 1.93 | 2.06 | 2.43 |
| YoY Gr (%) | | 14% | 5% | 2% | 1% | 4% | 6% | 8% | 13% | 7% | 18% |
| Godfrey Phillips India | 0.87 | 1.01 | 0.96 | 0.93 | 0.98 | 1.04 | 1.09 | 1.15 | 1.42 | 1.42 | 1.56 |
| YoY Gr (%) | | 17% | -5% | -3% | 6% | 6% | 5% | 6% | 23% | 0% | 9% |
| VST Industries | 0.61 | 0.72 | 0.72 | 0.71 | 0.70 | 0.76 | 0.77 | 0.80 | 1.24 | 1.28 | 1.51 |
| YoY Gr (%) | | 18% | 0% | -1% | -2% | 8% | 2% | 4% | 54% | 3% | 18% |
| GTC Industries | 0.52 | 0.50 | 0.46 | 0.45 | 0.43 | 0.42 | 0.45 | 0.46 | 0.77 | 0.68 | 0.73 |
| YoY Gr (%) | | -4% | -8% | -2% | -3% | -4% | 8% | 4% | 65% | -11% | 7% |
| Sector Realisation | 1.00 | 1.15 | 1.19 | 1.21 | 1.23 | 1.30 | 1.38 | 1.49 | 1.79 | 1.89 | 2.19 |
| YoY Gr (%) | | 15% | 3% | 2% | 1% | 6% | 6% | 8% | 20% | 6% | 16% |

Source: PINC Research, Company

Pictorial warnings – negligible impact in the near term

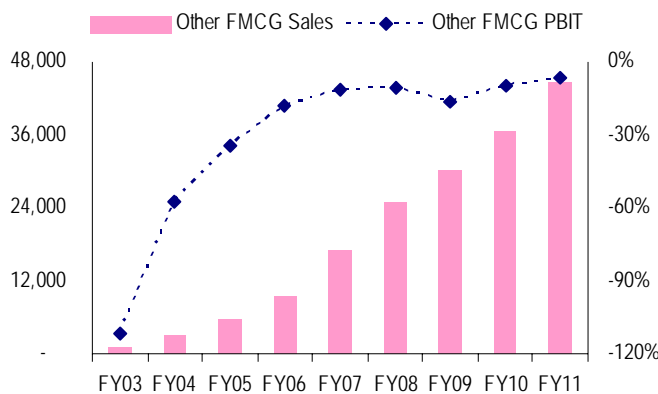
Cigarette pack is required to display a new set of pictorial warning from 1st Dec’11 and the new pictures are expected to be more gory and effective. However, we believe there would be no immediate impact on the cigarette consumption. The impact on the existing users would be insignificant due to their habits however we think it can restrict growth on the new users.

FMCG business gaining traction

Strong cash flows from cigarette business resulted into better appetite for the FMCG business. ITC has swallowed Rs21bn operational loss to achieve 15x sales growth to Rs45bn in the past 8 years. No other FMCG player has that strong profitable segment which can help them in expanding into other segments. ITC consistently entered into new segments and has now become a critical player in the FMCG market too.

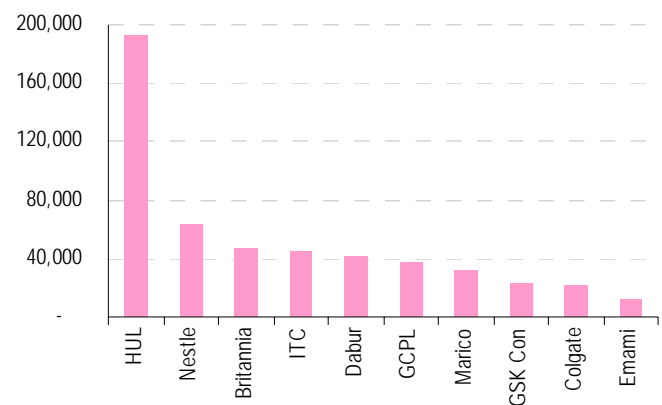
We are encouraged by 240bps decline in PBIT loss (% of sales) during H1FY12 to ~5% of sales, particularly when input prices are facing high inflation. Retention of high sales growth along with reduction in operational losses is remarkable in our opinion. We believe ‘Branded Packaged Food’ and ‘Stationary’ businesses are profitable while losses in ‘Lifestyle Retailing’ and ‘Personal Care’ businesses are impacting the overall profitability of the segment. On account of softening of input prices and better growth in the profitable businesses, we expect FMCG segment would further reduce the losses and should achieve breakeven in FY13.

Exhibit 4 - Strong Performance of FMCG Segment



Source: PINC Research, Company

Exhibit 5 - Significant Presence in FMCG Market



Source: PINC Research, Company

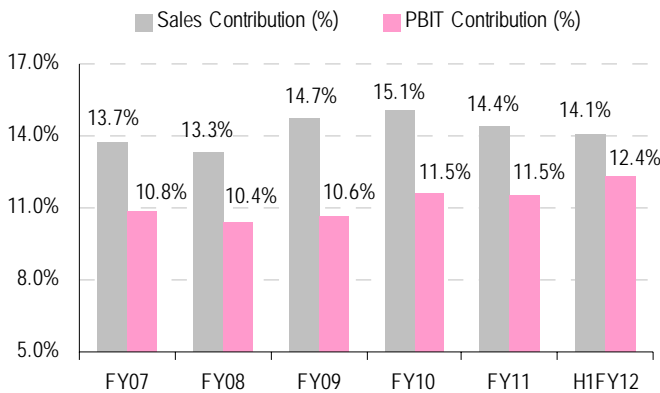
Better contribution from Paper and Agribusiness

ITC's paperboard business is a backward integration of cigarette business while agribusiness is largely a cross selling of unmanufactured tobacco. ITC's 95% inter segment sales comes from these two segments.

ITC improved agribusiness profitability through develop strong network with farmers. Through 'e-Choupal' ITC is now connected with more than 4mn farmers in 40,000 villages in 10 states. Further development of 'e-Choupal' and other agri initiatives would expand the agribusiness.

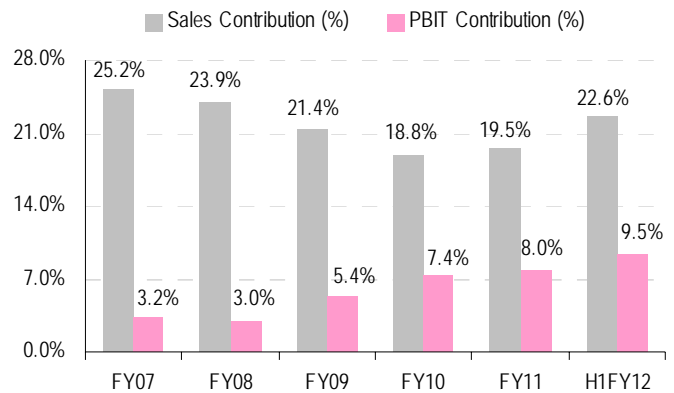
ITC's paper business performance also improved through focusing on the value-added products. We expect higher contribution from the value-added products would further improve the margin profile of the business.

Exhibit 6 - Paperboard Contribution in Sales & PBIT



Source: PINC Research, Company

Exhibit 7 - Agribusiness Contribution in Sales & PBIT



Source: PINC Research, Company

VALUATIONS AND RECOMMENDATION

We value ITC using DCF methodology and arrive at a target price of Rs233. We believe relative valuation is not feasible as there is no appropriate comparable for ITC.

Cigarette business is not comparable with domestic as well as global players. ITC dominate with 83% market share in the domestic cigarette market and its business model is far superior which is appropriately backward integrated. Therefore, apart from the disparity in sales, ITC's profitability is also not comparable with other domestic players.

Exhibit 8 - Domestic Cigarette Player Comparison

| | ITC | Godfrey Phillips | VST Industries |
|--------------------------|---------|------------------|----------------|
| Net Sales (Rs mn) - FY11 | 105,737 | 16,025 | 5,784 |
| EBITDA Margin (%) - FY11 | 54.5 | 18.3 | 23.7 |
| Market Cap (Rs bn) | 1,577 | 26 | 17 |

Source: PINC Research

We also compare ITC with global players but we found that the comparison with global players is also not appropriate. Global players are facing volume pressure and their profitability is also lower than ITC.

Exhibit 9 - Global Cigarette Comparison

| | Mkt Cap (USD mn) | Revenue Gr. | | | EBITDA Margin | | | Net Income Gr. | | | ROE (%) | | | P/E (x) | | | EV/EBITDA (x) | | |
|------------------------------|---------------------|-------------|-------|-------|---------------|-------|-------|----------------|-------|-------|---------|-------|-------|---------|-------|-------|---------------|-------|-------|
| | | 2010 | 2011E | 2012E | 2010 | 2011E | 2012E | 2010 | 2011E | 2012E | 2010 | 2011E | 2012E | 2,010 | 2011E | 2012E | 2,010 | 2011E | 2012E |
| PHILIP MORRIS INTERNATIONAL | 136,371 | 10% | 12% | 2% | 45% | 47% | 48% | 12% | 19% | 4% | 146.0 | 267.0 | 489.0 | 20.0 | 16.2 | 15.0 | 12.5 | 10.5 | 10.2 |
| BRITISH AMERICAN TOBACCO PLC | 92,709 | 13% | 1% | 4% | 37% | 39% | 40% | 22% | 8% | 8% | 42.0 | 40.5 | 41.6 | 17.5 | 15.7 | 14.3 | 12.7 | 11.5 | 10.8 |
| ALTRIA GROUP INC | 61,117 | 1% | 0% | 1% | 40% | 42% | 43% | 8% | 6% | 6% | 88.0 | 89.0 | 101.0 | 15.6 | 14.6 | 13.6 | 10.5 | 10.1 | 9.6 |
| JAPAN TOBACCO INC | 46,945 | 15% | -62% | 2% | 9% | 25% | 26% | 28% | 55% | 19% | 9.6 | 14.3 | 16.6 | 21.0 | 16.6 | 13.7 | 7.8 | 7.4 | 6.8 |
| IMPERIAL TOBACCO GROUP PLC | 37,621 | -2% | -1% | 4% | 42% | 43% | 43% | 5% | 4% | 6% | 24.7 | 25.0 | 25.9 | 13.0 | 11.8 | 10.9 | 10.2 | 9.6 | 9.2 |
| REYNOLDS AMERICAN INC | 24,307 | 3% | 0% | 1% | 31% | 34% | 35% | 4% | 14% | 5% | 20.4 | 23.6 | 26.1 | 16.6 | 15.1 | 14.0 | 9.7 | 9.0 | 8.5 |
| GUDANG GARAM TBK PT | 12,907 | 25% | 7% | 11% | 17% | 19% | 19% | 41% | 17% | 15% | 19.8 | 22.0 | 22.0 | 28.9 | 23.0 | 20.0 | 19.0 | 15.6 | 13.7 |

Source: Bloomberg, PINC Research

Our DCF methodology assumes 18% and 15% FCF growth during first and second 5 years post FY14. Our strong cash flow assumption is based on ITC's robust past performance and low peer threat on its high margin cigarette business. Based on our assumptions, we derive a DCF value of Rs233/share in which terminal value accounts for 52%.

Exhibit 10 - DCF Sensitivity

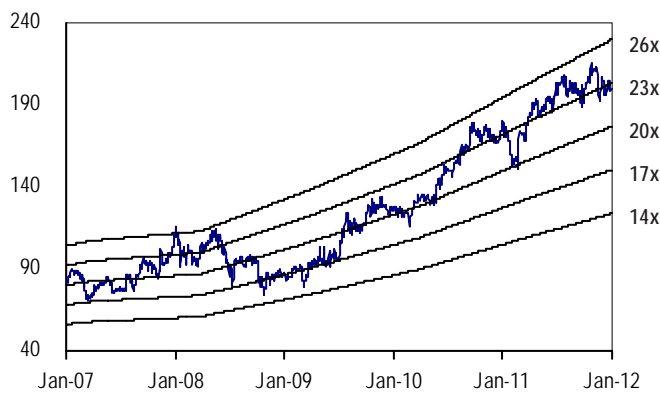
| Terminal Growth Rate | | Cost of Equity | | | | |
|----------------------|------|----------------|-------|---------|-------|-------|
| | | 11.0% | 11.5% | 12.0% | 12.5% | 13.0% |
| | 2.0% | 253 | 236 | 220 | 206 | 193 |
| | 2.5% | 262 | 243 | 226 | 211 | 198 |
| | 3.0% | 272 | 251 | (233) | 217 | 203 |
| | 3.5% | 283 | 261 | 241 | 224 | 209 |
| | 4.0% | 295 | 271 | 250 | 231 | 215 |

Source: PINC Research

ITC's past 5 years history suggest that the stock was on an average trades at 22x 12-month forward earnings. Our DCF based target price is valued at 25x 12-month forward earning which is 14% premium over past 5 year average P/E. At our target multiple, ITC's P/E discount over FMCG sector P/E is at 9% as compared to past 5 years' average discount of 12%. At our valuation, ITC still maintain its valuation discount over sector which is largely because of high government regulation in ITC's cigarette business.

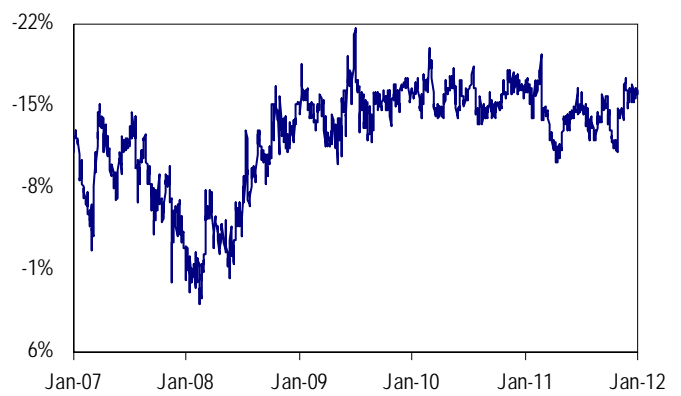
We believe our valuations are well justified given low peer threat in the cigarette business and expectation of superior performance of its non-cigarette business. The stock has 15% upside potential at our TP of Rs233, hence we initiate ITC with 'BUY' rating.

Exhibit 11 - ITC P/E Band



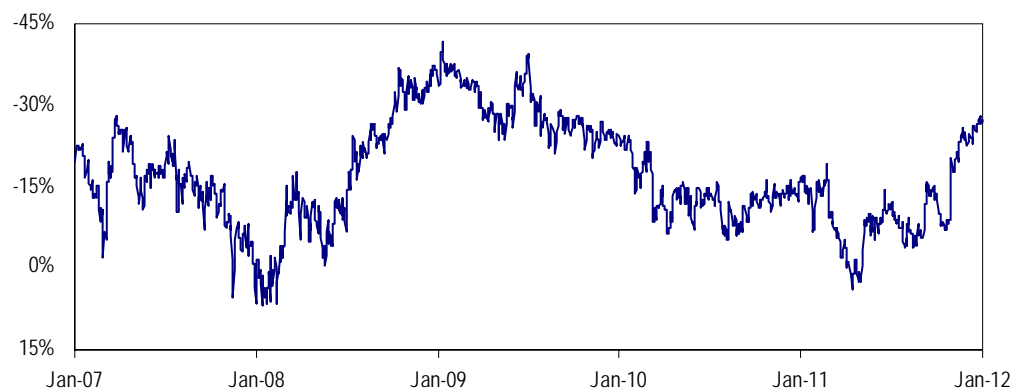
Source: PINC Research, Bloomberg

Exhibit 12 - ITC Valuations Discount v/s FMCG Sector



Source: PINC Research, Bloomberg

Exhibit 13 - ITC Valuations Discount v/s HUL



Source: PINC Research, Bloomberg

Cigarette Business - dominance to continue

ITC has a strong hold in the cigarette segment with brands like Gold Flake, Classic, Wills, India Kings, Lucky Strike, 555, Players, Insignia, Navy Cut, Scissors, Bristol and B&H. The wide range of products and strong distribution channel has led ITC to garner ~75% and ~83% volume and value market share in the cigarette industry. We expect ITC to deliver ~3% and ~10% CAGR in volume and price respectively during FY11-14E.

Exhibit 14 - Cigarette Performance

| Particulars | FY02 | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------|--------|--------|--------|--------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Gross Sales (Rs mn) | 80,136 | 87,568 | 92,236 | 99,964 | 113,229 | 128,244 | 138,155 | 151,009 | 172,779 | 198,212 | 229,004 | 259,503 | 288,101 |
| YoY Gr. (%) | 4.4% | 9.3% | 5.3% | 8.4% | 13.3% | 13.3% | 7.7% | 9.3% | 14.4% | 14.7% | 15.5% | 13.3% | 11.0% |
| Volume (mn no) | 60,865 | 63,415 | 65,387 | 69,998 | 75,894 | 81,265 | 80,723 | 78,370 | 84,040 | 81,723 | 86,708 | 89,309 | 90,202 |
| YoY Gr. (%) | -8.4% | 4.2% | 3.1% | 7.1% | 8.4% | 7.1% | -0.7% | -2.9% | 7.2% | -2.8% | 6.1% | 3.0% | 1.0% |
| Gross Price (Rs/cig) | 1.32 | 1.38 | 1.41 | 1.43 | 1.49 | 1.58 | 1.71 | 1.93 | 2.06 | 2.43 | 2.64 | 2.91 | 3.19 |
| YoY Gr. (%) | 14.0% | 4.9% | 2.2% | 1.2% | 4.5% | 5.8% | 8.5% | 12.6% | 6.7% | 18.0% | 8.9% | 10.0% | 9.9% |
| PBIT (Rs mn) | 16,931 | 19,235 | 20,333 | 22,888 | 27,088 | 31,722 | 36,340 | 41,838 | 49,381 | 57,668 | 70,985 | 81,494 | 92,749 |
| YoY Gr. (%) | | 13.6% | 5.7% | 12.6% | 18.3% | 17.1% | 14.6% | 15.1% | 18.0% | 16.8% | 23.1% | 14.8% | 13.8% |
| PBIT/Cig | 0.28 | 0.30 | 0.31 | 0.33 | 0.36 | 0.39 | 0.45 | 0.53 | 0.59 | 0.71 | 0.82 | 0.91 | 1.03 |
| YoY Gr. (%) | | 9.0% | 2.5% | 5.2% | 9.2% | 9.4% | 15.3% | 18.6% | 10.1% | 20.1% | 16.0% | 11.5% | 12.7% |

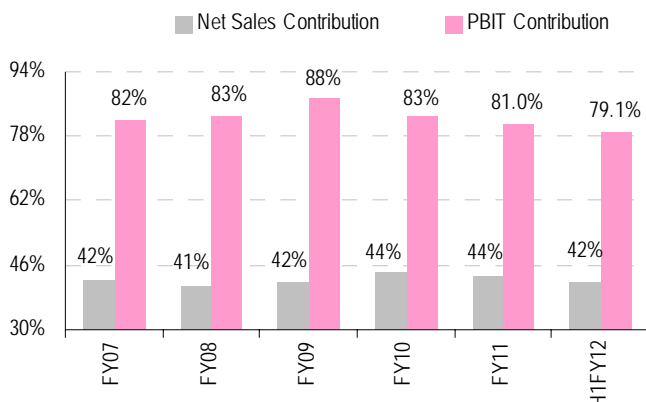
Source: Bloomberg, PINC Research

ITC reported strong 11.8% CAGR in gross sales during FY06-11 which was substantially ahead of 8.1% CAGR during FY01-06. Cigarette volume grew by mere 1.5% during the past 5 years and that suggested that realisation growth played a big role in the sales growth. ITC achieved better realisation growth through conscious price hike and achievement of better product mix. The swing in the consumers' buying power in the past 5 years has also helped ITC to pass on extra cost burden.

Still a key profitable segment

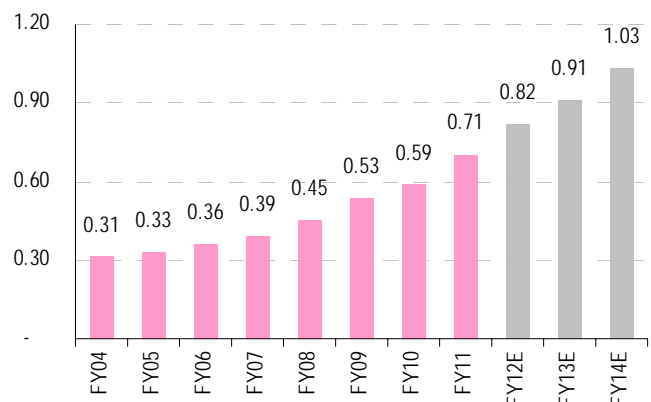
Although cigarette contributes 44% of the total net sales of ITC, its contribution in the profitability is significantly higher at >80% of the total PBIT. Better raw material sourcing, appropriate backward integration, better revenue mix and substantial cigarette price growth has enabled ITC to improve the PBIT/cig.

Exhibit 15 - Cigarette Contribution in Sales and PBIT



Source: PINC Research, Company

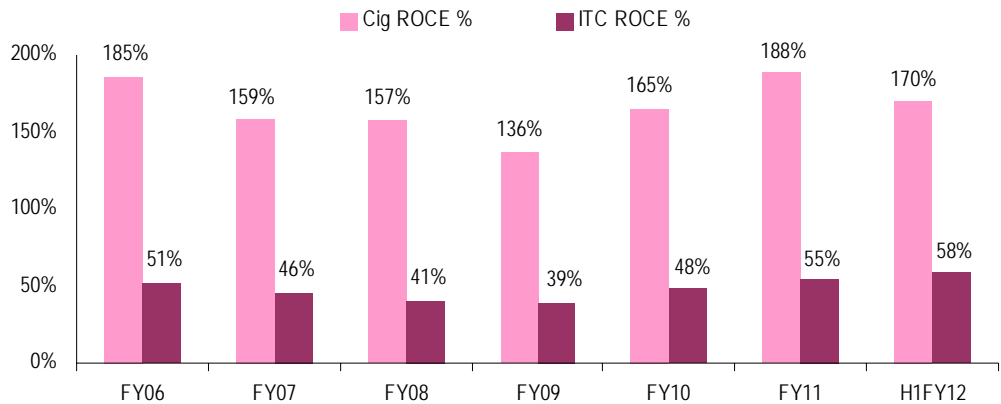
Exhibit 16 - PBIT/Cigarette (Rs/stick)



Source: PINC Research, Company

Exhibit 17 - Wide difference between Cigarette and ITC's ROCE (%)

Loss in FMCG segment and single digit ROCE of Hotel business wiped off the benefits of strong cigarette ROCE ...



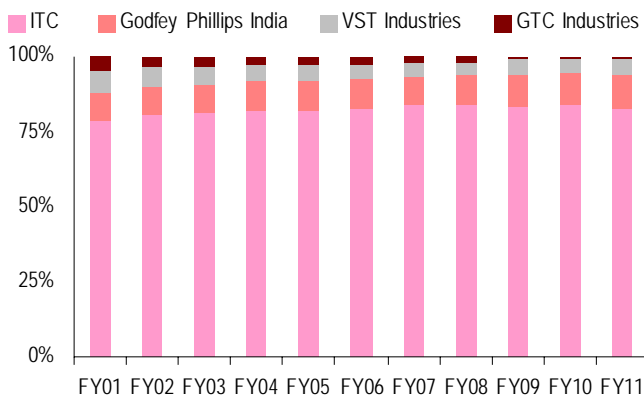
Source: PINC Research, Company

ITC's strong positioning in the cigarette market

ITC is an undisputed leader in the cigarette market with 75% and 83% volume and value market share respectively. Despite ITC's premium pricing over the other cigarette brands, strong distribution and better product offering enabled ITC to expand volume market share by 500bps in the past decade.

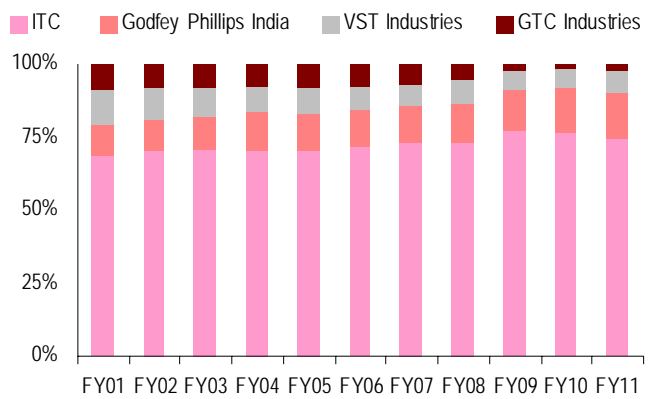
We believe ITC would be able to retain its cigarette market share owing to extensive product offering, strong distribution network, appropriate backward integration and superior profitability. Which is why, apart from couple of years like FY11 most of the time ITC expanded in volume and value market share.

Exhibit 18 - Cigarette Value Market Share (%)



Source: PINC Research, Company

Exhibit 19 - Cigarette Volume Market Share (%)



Source: PINC Research, Company

Exhibit 20 - Cigarette Gross Price (company level) Comparison (Rs/cig)

| Company | FY01 | FY02 | FY03 | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|------------------------|------|------|------|------|------|------|------|------|------|------|------|
| ITC | 1.15 | 1.32 | 1.38 | 1.41 | 1.43 | 1.49 | 1.58 | 1.71 | 1.93 | 2.06 | 2.43 |
| YoY Gr (%) | | 14% | 5% | 2% | 1% | 4% | 6% | 8% | 13% | 7% | 18% |
| Godfrey Phillips India | 0.87 | 1.01 | 0.96 | 0.93 | 0.98 | 1.04 | 1.09 | 1.15 | 1.42 | 1.42 | 1.56 |
| YoY Gr (%) | | 17% | -5% | -3% | 6% | 6% | 5% | 6% | 23% | 0% | 9% |
| VST Industries | 0.61 | 0.72 | 0.72 | 0.71 | 0.70 | 0.76 | 0.77 | 0.80 | 1.24 | 1.28 | 1.51 |
| YoY Gr (%) | | 18% | 0% | -1% | -2% | 8% | 2% | 4% | 54% | 3% | 18% |
| GTC Industries | 0.52 | 0.50 | 0.46 | 0.45 | 0.43 | 0.42 | 0.45 | 0.46 | 0.77 | 0.68 | 0.73 |
| YoY Gr (%) | | -4% | -8% | -2% | -3% | -4% | 8% | 4% | 65% | -11% | 7% |
| Sector Realisation | 1.00 | 1.15 | 1.19 | 1.21 | 1.23 | 1.30 | 1.38 | 1.49 | 1.79 | 1.89 | 2.19 |
| YoY Gr (%) | | 15% | 3% | 2% | 1% | 6% | 6% | 8% | 20% | 6% | 16% |

Source: PINC Research, Company

Better raw material sourcing, appropriate backward integration and substantial price premium has enabled ITC to engender strong profitability among cigarette peers.

Tobacco cost comparison

| Particulars (Rs/kg) | FY09 | FY10 | FY11 |
|---------------------|------|------|------|
| ITC | 76 | 104 | 110 |
| Godfrey Phillips | 85 | 118 | 126 |
| VST Industries | 81 | 110 | 104 |

Source: PINC Research, Company

Cigarette EBITDA Margin Comparison

| Companies | FY09 | FY10 | FY11 |
|------------------|------|------|------|
| ITC | 55% | 54% | 55% |
| Godfrey Phillips | 15% | 12% | 18% |
| VST Industries | 18% | 15% | 24% |

Source: PINC Research, Company

Exhibit 21 - Mkt Share of Top 10 Cig Brands in India - Retail Volume

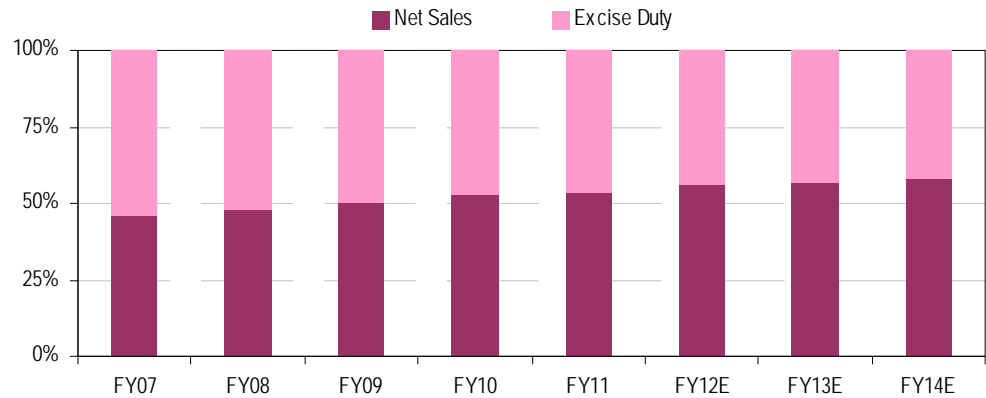
| Brand | Company | Mkt Share (%) |
|-------------|------------------------|---------------|
| Gold Flake | ITC Group | 31.2% |
| Wills | ITC Group | 18.2% |
| Scissors | ITC Group | 8.4% |
| Four Square | Godfrey Phillips India | 7.9% |
| Capstan | ITC Group | 7.4% |
| Bristol | ITC Group | 6.9% |
| Charminar | VST Industries | 4.0% |
| Red & White | Godfrey Phillips India | 3.0% |
| Charms | VST Industries | 3.0% |
| Cavenders | Godfrey Phillips India | 2.5% |

Source: PINC Research, Industry data for 2009

Low dependence on tobacco prices

Tobacco by weight contributes ~75% of a cigarette however in value terms it is insignificant at <7% of net cigarette realisation. Our analysis suggests that tobacco, cigarette paper and filter rods accounts <10% of net cigarette realisation. Therefore, raw material has low sensitivity on cigarette profitability. As taxes constitute large part of the cigarette prices its sensitivity over cigarette profitability is high.

Exhibit 22 - Gross Sales Breakup



Source: PINC Research, Company

FDI ban is relief for the domestic manufacturers

In 2010, Indian government has banned fresh FDI in the cigarette manufacturing and this has shut the doors on foreign companies such as Japan Tobacco, BAT and Altria group. It is positive for ITC as it restricts the possibility of rise in the competition.

In addition, Indian government is also looking into a proposal to ban FDI in the wholesale marketing arms of the foreign cigarette companies.

Following, Japan Tobacco Inc (JT) is closing its joint venture (JT International Indian Pvt Ltd.) from India by 31st Dec, 2011 and has surrendered its license to the Indian government. Its sales was insignificant and was selling close to 300mn sticks per year which is <0.5% of the Indian market.

Higher involvement of Health Ministry

The tobacco related death in India is among the highest in the world and accounts ~16% of total world wide deaths. Higher consumption of bidi and chewing tobacco are the key reasons for such high death toll. India’s Health Ministry is being cautious in the recent time and trying control tobacco consumption through rise in taxes, nationwide ban on smoking in public places and implementation of more gory and effective pictures on cigarette pack. However, we believe these actions are still not very effective and not serving the purpose. Health Ministry’s higher involvement and strong actions is always a threat for the cigarette sector.

In addition, a panel of experts also recommended a sharp 26% tax rise on bidis to 33% while suggested 15% tax rise on cigarette to 58%.

Winter season to lead near term growth

We expect H2FY12 to be strong in terms of sales as well as profitability. We noticed that during winter season, cigarette sales and PBIT creates a significant difference between the first half and second half year performance. Recent cigarette price rise along with seasonal volume advantage should translate into strong cigarette profitability in H2FY12.

Exhibit 23 - Cigarette Sales and PBIT Difference between H1 and H2 of the Fiscal Year

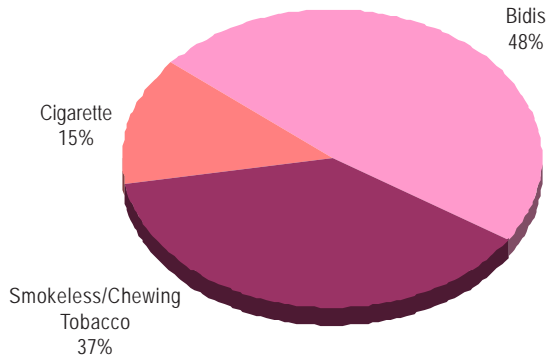
| | H1FY06 | H2FY06 | H1FY07 | H2FY07 | H1FY08 | H2FY08 | H1FY09 | H2FY09 | H1FY10 | H2FY10 | H1FY11 | H2FY11 |
|-------------------------------|--------|---------|--------|---------|--------|--------|--------|--------|--------|--------|--------|--------|
| Gross Sales Contribution (%) | 49.1% | 50.9% | 48.8% | 51.2% | 48.6% | 51.4% | 48.1% | 51.9% | 48.3% | 51.7% | 47.8% | 52.2% |
| PBIT Contribution (%) | 50.9% | 49.1% | 50.5% | 49.5% | 49.6% | 50.4% | 47.0% | 53.0% | 48.1% | 51.9% | 47.9% | 52.1% |
| Sales contribution diff (bps) | | 173bps | | 243bps | | 289bps | | 388bps | | 345bps | | 437bps |
| PBIT contribution diff (bps) | | -171bps | | -102bps | | 78bps | | 591bps | | 373bps | | 417bps |

Source: PINC Research, Company

Other Tobacco Products

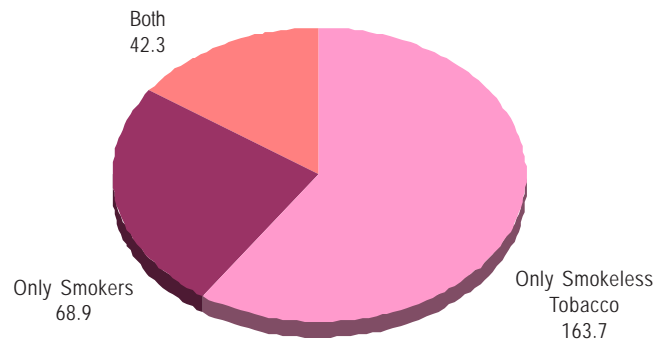
Other tobacco products like Bidi and chewing tobacco contributes ~85% of the total tobacco consumption with bidi forming 48% of the total consumption. Wide difference between cigarette and bidi taxes resulted into substantial price gap. Although, bidi forming largest share in the tobacco consumption; its share in the excise revenue is mere 5-7%.

Exhibit 24 - Tobacco consumption Pattern (%)



Source: Industry

Exhibit 25 - Tobacco Users in India (mn)



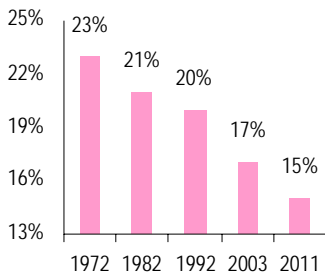
Source: Press Information Bureau, GOI

Exhibit 26 - Wide Difference in Bidi and Cigarette Excise Duty Structure

| Excise Duty Rate (Rs/1000 sticks) | 1997-98 | 1998-99 | 1999-00 | 2000-01 | 2001-02 | 2002-03 | 2003-04 | 2004-05 | 2005-06 | 2006-07 | 2007-08 | 2008-09 | 2009-10 | 2010-11 | 2011-12 |
|-----------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Bidi | | | | | | | | | | | | | | | |
| Handmade | 7 | 7 | 7 | 8 | 9 | 9 | 9 | 9 | 9 | 12 | 14 | 12 | 12 | 12 | 12 |
| Machine-made | 16 | 16 | 16 | 17 | 19 | 19 | 19 | 19 | 19 | 22 | 26 | 30 | 30 | 30 | 30 |
| Cigarette | | | | | | | | | | | | | | | |
| Non-filiter <60mm | 90 | 100 | 110 | 115 | 135 | 135 | 135 | 135 | 150 | 160 | 168 | 819 | 819 | 819 | 669 |
| Non-filiter >60mm | 350 | 370 | 370 | 390 | 450 | 450 | 450 | 450 | 495 | 520 | 546 | 1,323 | 1,323 | 1,323 | 1,473 |
| Filter <70mm | 500 | 550 | 550 | 580 | 670 | 670 | 670 | 670 | 740 | 780 | 819 | 819 | 819 | 969 | 969 |
| Filter >70-75mm | 820 | 900 | 900 | 945 | 1,090 | 1,090 | 1,090 | 1,090 | 1,200 | 1,260 | 1,323 | 1,323 | 1,323 | 1,473 | 1,473 |
| Filter >75-85mm | 1100 | 1,200 | 1,200 | 1,260 | 1,450 | 1,450 | 1,450 | 1,450 | 1,595 | 1,675 | 1,759 | 1,759 | 1,759 | 1,959 | 1,959 |
| Filter >85mm | 1350 | 1,470 | 1,470 | 1,545 | 1,780 | 1,780 | 1,780 | 1,780 | 1,960 | 2,060 | 2,163 | 2,163 | 2,163 | 2,363 | 2,363 |

Source: PINC Research, CBEC

Tobacco Consumption by Cigarette



Source: PINC Research, Company

Bidi: Cigarette Ratio=8:1

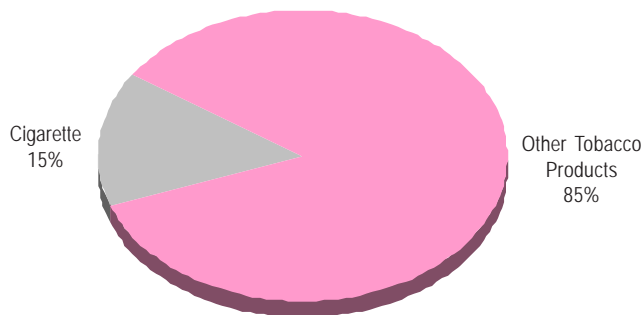
Tax rise on other tobacco products is positive

The differential tax treatment for cigarette and other tobacco products has always posed a challenge for the cigarette industry. It led to a fall in cigarette’s share in the total tobacco consumption from about 25% in the 1970s to about 15% currently. Other tobacco products are more harmful than cigarette although tax levy on these are significantly low.

Recently some of the states have included other tobacco products under schedule ‘D’ and imposed the VAT rate similar to cigarette item during their recent budget. Besides, a panel of experts also recommended sharp 26% tax rise on Bidis to 33% while on cigarette they suggested 15% tax rise to 58%.

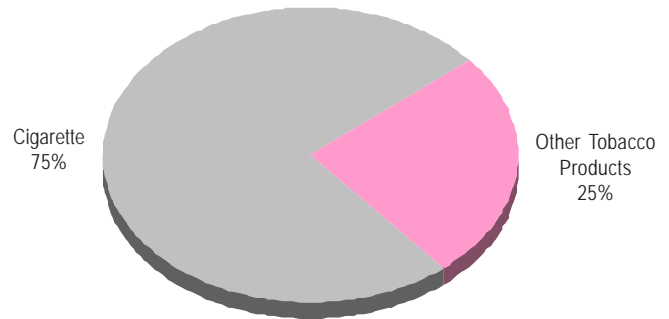
We believe rise in taxes on other tobacco products would not materially change in the consumption mix as cigarette and other products have significant price difference. However, we expect tax revenue mix would be more balanced and subsequently reduce the pressure on cigarette.

Exhibit 27 - Tobacco Consumption Share (%)



Source: Company

Exhibit 28 - Tobacco Tax Revenue Share (%)

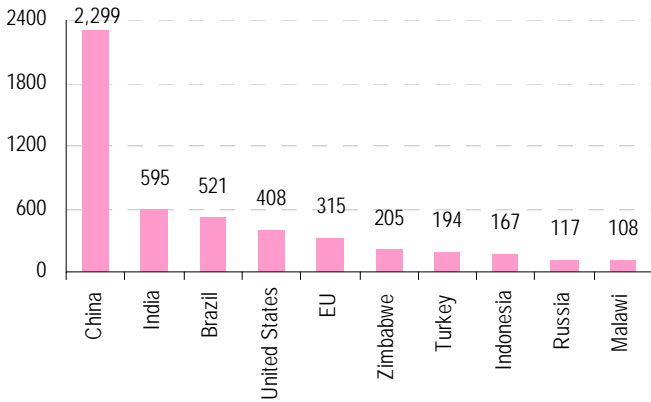


Source: Company

How Indian cigarette market is different than the global market

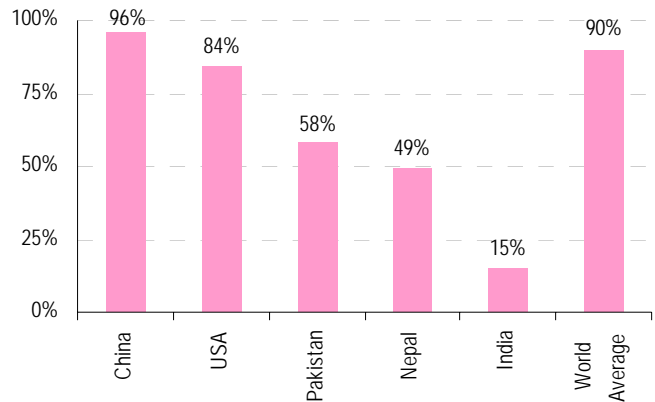
- Indian cigarette market is widely different than the world market. India is among the lead player in terms of tobacco production and consumption while its cigarette share in the world market is <2%. In India, Cigarette accounts mere ~15% of the tobacco consumption as compared to the world average of ~90%. Large part of the difference is on account of high tax differential between cigarette and other tobacco products i.e. Bidi and chewing tobacco.

Exhibit 29 - Tobacco Production (000 tons)



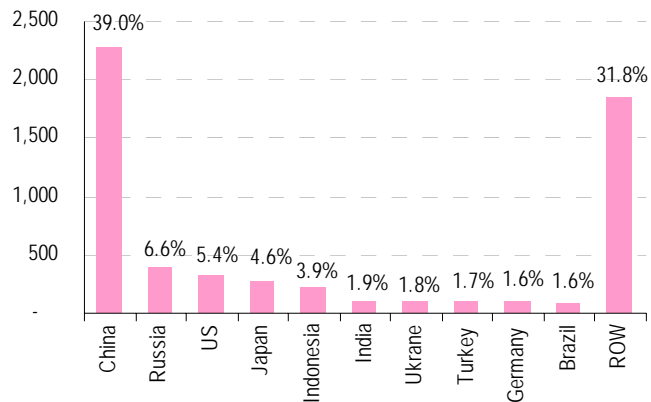
Source: PINC Research, Industry

Exhibit 30 - Cigarette's Share in Tobacco Consumption



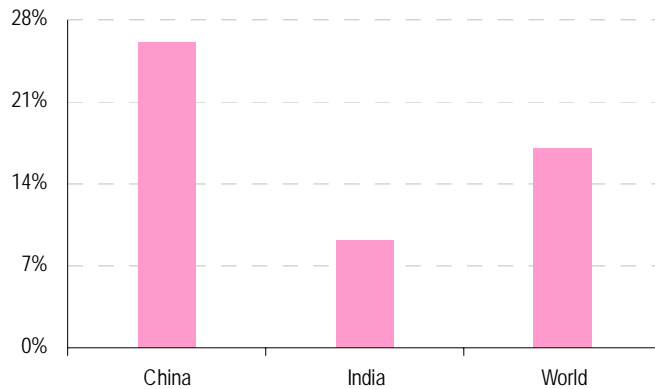
Source: PINC Research, Industry

Exhibit 31 - Global Cigarette Volume Share (%)



Source: PINC Research, Industry

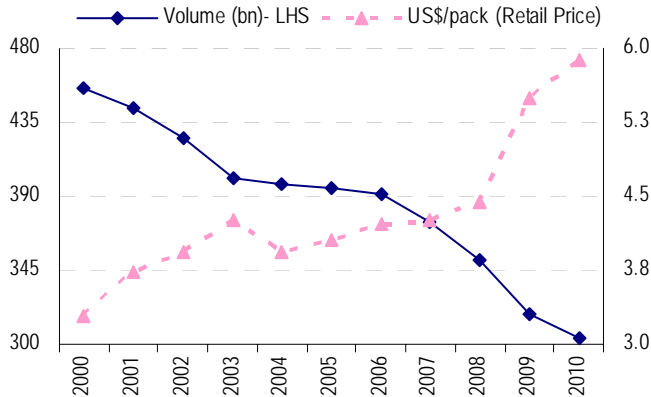
Exhibit 32 - Smokers as % of Population



Source: PINC Research, Industry

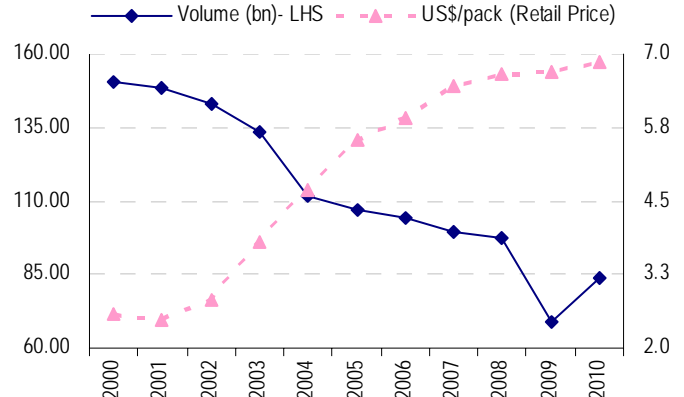
- Globally, several developed markets are reporting volume decline owing to consistent cigarette price rise, higher taxes and government's health awareness programme. US and Germany have witnessed substantial decline in cigarette volume in the past decade due to steady price rise in cigarettes. Japanese market is also facing severe pressure due to recent 40% rise in taxes during 2010 and as per BAT presentation, the Japanese market can show 17% volume decline in 2011.
- Indian cigarette market is different than other nations as cigarette contributes mere 15% of the total tobacco consumption compared to world average of 90%. Cigarette grew by slower volume as compared to other tobacco products due to consistent rise in taxes on cigarette. Taxes already contributes 50% of the cigarette price therefore to control the cigarette consumption further tax upside is limited. Other tobacco products are more dangerous for health and taxes still not a portion of price. Therefore tax rise probability is higher with other tobacco products than cigarette.

Exhibit 33 - US Cigarette Market



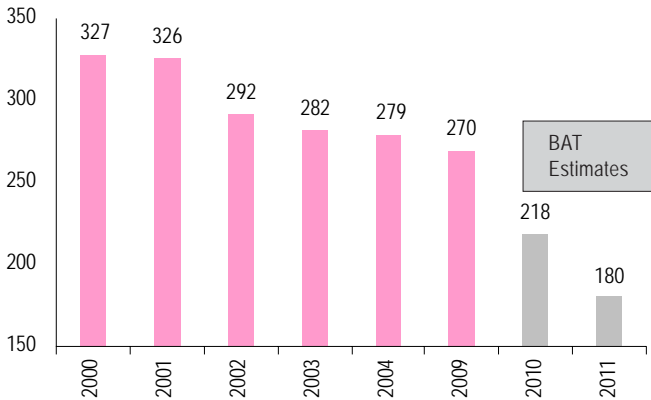
Source: Tobacco Merchants Association

Exhibit 34 - Germany Cigarette Market



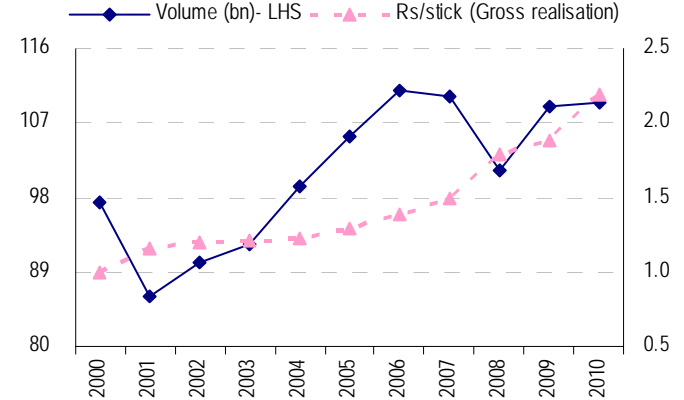
Source: Tobacco Merchants Association

Exhibit 35 - Japan Cigarette Volume (bn)



Source: Tobacco Merchants Association, Industry

Exhibit 36 - India Cigarette Market



Source: PINC Research

- Illicit market is high in the low or middle income countries that accounts for ~78% of the total cigarette consumption and <80% of the global illicit market. Smuggling impacts government tax revenue and increase death toll as low price cigarette has higher share in smuggling. Illicit is a big challenge all over the world as it accounts for ~12% of the global consumption. India is also among the largest smuggling countries and ~15% of the consumption is illegal.

Exhibit 37 - World Illicit Trade

| World Bank Income Group | Illicit Cig Mkt (Bn Cig) | Illicit Cig Contribution | (% of Cig Consumption) | Total Cig Consumption (bn Cig) | Cig Consumption Share |
|---------------------------------|--------------------------|--------------------------|------------------------|--------------------------------|-----------------------|
| High Income Countries | 124 | 19% | 10% | 1,265 | 22% |
| Low and Middle Income Countries | 533 | 81% | 12% | 4,405 | 78% |
| Total Illicit Market | 657 | | 12% | 5,670 | |

Source: PINC Research, World Lung Foundation 2007

Exhibit 38 - Top Countries for Illicit Consumption

| Countries | Illicit Trade (Bn Cig) | % of Consumption | World Bank Income Group |
|--------------------|------------------------|------------------|-------------------------|
| China | 214 | ~9% | Low or Middle |
| Russian Federation | 76 | ~23% | Low or Middle |
| United States | 62 | ~20% | High |
| EU | 58 | ~13% | High |
| Brazil | 38 | ~35% | Low or Middle |
| Philippines | 19 | ~19% | Low or Middle |
| India | 18 | ~15% | Low or Middle |
| Indonesia | 14 | ~6% | Low or Middle |
| Pakistan | 13 | ~17% | Low or Middle |
| Turkey | 12 | ~11% | Low or Middle |

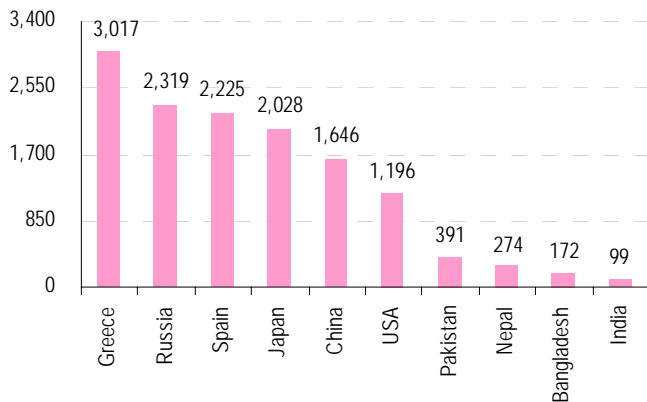
Source: PINC Research, World Lung Foundation 2007

What do we expect?

What makes us to assume that absolute cigarette consumption in India would grow or maintain its current level in the medium term?

- Most of the nations have witnessed absolute decline in the cigarette consumption while we believe Indian cigarette market would continue to grow or maintain its current consumption level in the medium term. India's per capita cigarette consumption per year is among the lowest in the world. Here, we don't argue for any dramatic change in the per capita consumption pattern as the cigarette market is set since so many years. However, there is a definite scope of improvement and slight improvement in the per capita consumption would be favourable for the Indian cigarette market.

Exhibit 39 - Number of Cigarettes Per Adult Per Year

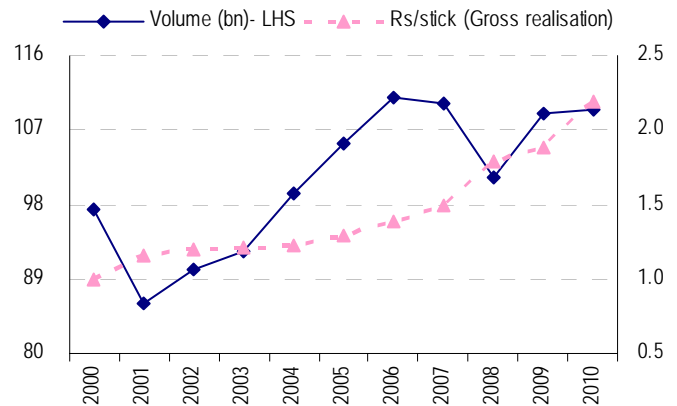


Source: WHO

We expect higher probability of tax rise on other tobacco products...

Higher youth income has relevance for the cigarette demand...

Exhibit 40 - Indian Cigarette Market



Source: PINC Research, Company, Industry

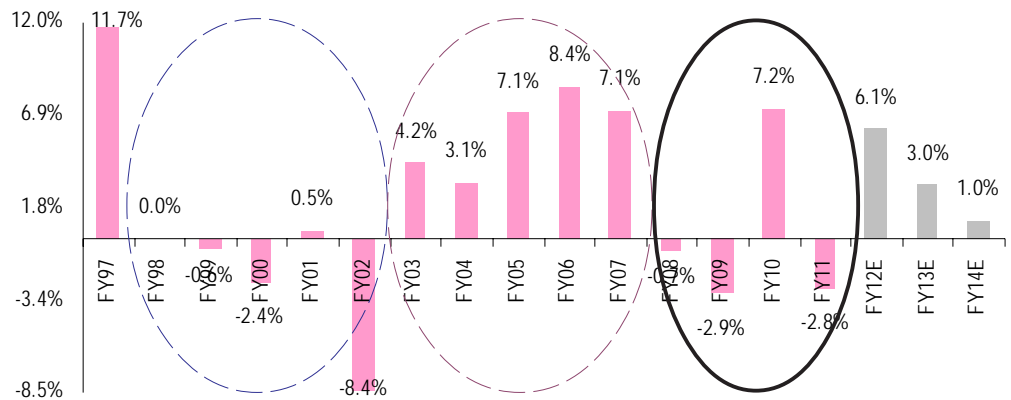
- Although, cigarette share in the Indian tobacco consumption has consistently reduced and reached to 15%; absolute cigarette consumption has improved albeit at a slower pace. The wide difference between prices of cigarette and other tobacco products resulted into higher demand for other tobacco products. Cigarette share in world tobacco consumption is ~90% which means our tobacco consumption pattern is almost opposite as compared to other countries. We don't expect any drastic change in the consumption pattern however, as other tobacco products have a lion's share in the total tobacco consumption we see higher probability of tax rise on other tobacco products. This would reduce the imbalance between tobacco consumption and tax mix and would subsequently reduce the tax pressure on cigarette.
- The rapid change in the youth culture is also positive for the cigarette industry. There is a visible sign of rise in the youth income and higher consumption of cigarette. We believe growth in the new cigarette users would be supported by rising youth income, higher female involvement, adoption of modern culture and increase in the urban population.

Cigarette prices and volume growth have high correlation...

What is our assumption for ITC's cigarette revenue?

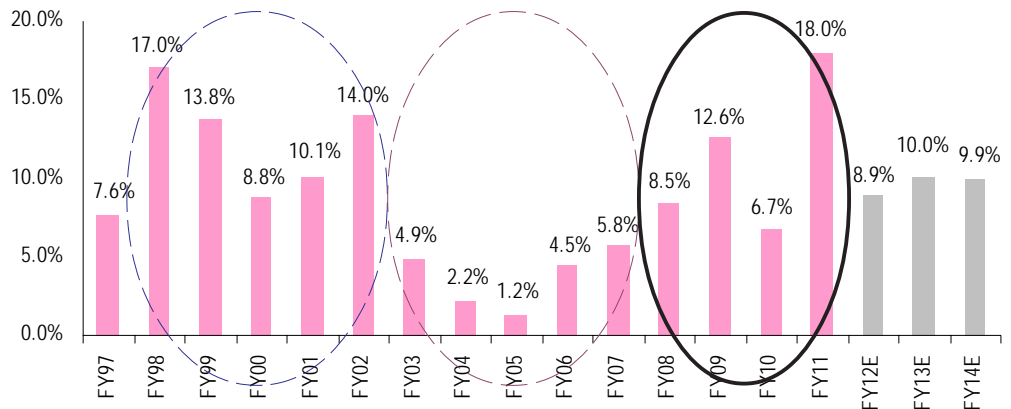
- ITC's history suggests that cigarette volume and price have high correlation. We analysed past 15 years' performance and classified period into three phases. Phase A, during FY1998-2002, was extremely high price rise period in which ITC's gross cigarette price increased by ~13% owing to ~6.3% average excise duty hike, it led to the volume decline of >2%. Phase B, during FY2003-2007, was just opposite to Phase A where the whole cigarette growth was volume driven. ITC's gross cigarette price grew by ~3.7% while volume increased by >6%. Phase C, during FY2008-2011, was mainly driven by price increase. Sharp rise in excise duty in FY11 led to the jump in cigarette prices and resulted into volume decline of ~3% during FY11. Phase C displayed +11% CAGR in gross price while volumes were flat.
- We expect volume growth of 6.1% in FY12 owing to no change in the excise duty structure and low cigarette base in FY11. However, we expect excise duty hike in FY13 and FY14 to the tune of ~7% which would force ITC to raise cigarette prices. We expect ~9.5% gross price CAGR during FY11-14E, while expect moderate volume CAGR of 3.3%.

Exhibit 41 - ITC Cigarette Volume Growth



Source: PINC Research, Company

Exhibit 42 - ITC Cigarette Price Growth



Source: PINC Research, Company

Exhibit 43 - ITC Volume and Price Scenario

| | Duration | Volume CAGR | Price CAGR | Avg. Excise Rise |
|---------|-----------|-------------|------------|------------------|
| Phase A | 1997-2002 | -2.2% | 12.7% | 6.3% |
| Phase B | 2002-2007 | 6.0% | 3.7% | 3.7% |
| Phase C | 2007-2011 | 0.1% | 11.3% | 4.7% |
| Phase D | 2011-2014 | 3.3% | 9.5% | 4.1% |

Source: PINC Research, Company

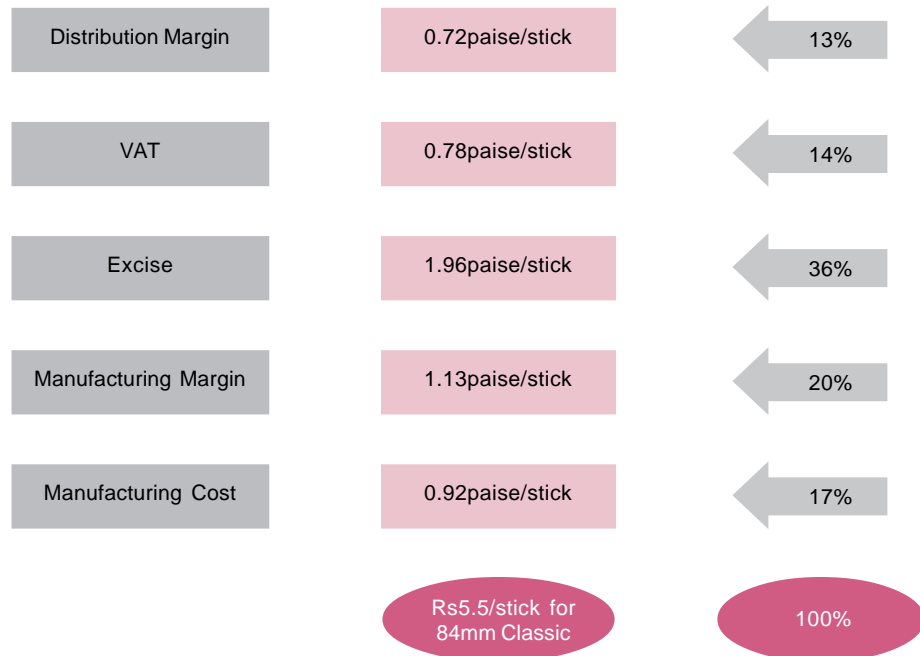
Our Breakup of Cigarette MRP

We expect revenue mix would be favourable for King size cigarette...

Our analysis suggests that large part of the cigarette volumes is accounted by the regular size (69mm). We believe regular size contributed 75% of the total cigarette volumes while large size (74mm) and King size accounted 12% and 13% respectively in FY11. In our opinion, volume mix has favorably skewed towards the King size over a period of time. We assume the cigarette mix would further shift towards the King size.

As most of the key states have recently taken substantial hike in VAT rate, we expect chance of further hike is limited. We maintain our weighted average VAT rate of 19.42% for FY12-14.

Exhibit 44 - Govt. Accounts Largest Share of Cigarette



Source: PINC Research

Exhibit 45- Our Assumption for all the Components of MRP

| Particulars | FY11P | | | FY12E | | | FY13E | | | FY14E | | |
|---|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| | 84mm | 74mm | 69mm | 84mm | 74mm | 69mm | 84mm | 74mm | 69mm | 84mm | 74mm | 69mm |
| Cig Avg MRP (Rs/stick) | 4.57 | 3.70 | 2.94 | 5.13 | 4.20 | 3.28 | 5.55 | 4.62 | 3.55 | 6.04 | 5.03 | 3.88 |
| Retailer/Distributor Margin (Rs/stick) | 0.60 | 0.48 | 0.38 | 0.67 | 0.55 | 0.43 | 0.72 | 0.60 | 0.46 | 0.79 | 0.66 | 0.51 |
| Retailer/Distributor's price (Rs/stick) | 3.97 | 3.21 | 2.56 | 4.46 | 3.65 | 2.85 | 4.83 | 4.02 | 3.09 | 5.25 | 4.38 | 3.38 |
| VAT Rate | 14.93% | 14.93% | 14.93% | 19.42% | 19.42% | 19.42% | 19.42% | 19.42% | 19.42% | 19.42% | 19.42% | 19.42% |
| VAT (Rs/stick) | 0.52 | 0.42 | 0.33 | 0.72 | 0.59 | 0.46 | 0.78 | 0.65 | 0.50 | 0.85 | 0.71 | 0.55 |
| Gross price for ITC (Rs/stick) | 3.46 | 2.80 | 2.23 | 3.73 | 3.06 | 2.38 | 4.04 | 3.36 | 2.59 | 4.40 | 3.67 | 2.83 |
| Excise (Rs/stick) | 1.96 | 1.47 | 0.97 | 1.96 | 1.47 | 0.97 | 2.10 | 1.58 | 1.03 | 2.22 | 1.67 | 1.09 |
| Net Price (Rs/stick) | 1.50 | 1.32 | 1.26 | 1.77 | 1.59 | 1.42 | 1.95 | 1.79 | 1.56 | 2.17 | 1.99 | 1.74 |
| Volume Mix | 13% | 12% | 75% | 14% | 12% | 74% | 15% | 12% | 73% | 17% | 12% | 71% |
| Cig Volume (mn no) | 10,624 | 9,807 | 61,292 | 12,139 | 10,405 | 64,164 | 13,396 | 10,717 | 65,196 | 15,334 | 10,824 | 64,044 |
| Weighted Avg. Net Sale Price | | | 1.30 | | | 1.49 | | | 1.65 | | | 1.84 |

Source: PINC Research

What is the profitability outlook?

Better revenue mix, higher operational efficiency and significant cigarette price rise enabled ITC to expand PBIT per cigarette (stick) to 71paise in FY11 from 30paise in FY03. We expect profitability to remain high on account of focus on operational efficiency and retaining of pricing power due to low competitive intensity. This should further expand PBIT/stick to 103paise by FY14E.

Exhibit 46 - Cigarette Profitability Breakup

| Cig Breakup (%) | FY07 | FY08 | FY09 | FY10 | FY11 | FY12E | FY13E | FY14E |
|-----------------------|-------|-------|-------|-------|-------|-------|-------|-------|
| Gross Price/cig | 1.58 | 1.71 | 1.93 | 2.06 | 2.43 | 2.64 | 2.91 | 3.19 |
| YoY Gr% | 5.8% | 8.5% | 12.6% | 6.7% | 18.0% | 8.9% | 10.0% | 9.9% |
| Excise duty/cig | 0.85 | 0.89 | 0.96 | 0.97 | 1.13 | 1.16 | 1.26 | 1.35 |
| Net cig price/stick | 0.72 | 0.82 | 0.96 | 1.09 | 1.29 | 1.48 | 1.65 | 1.84 |
| YoY Gr% | 8.5% | 13.3% | 17.3% | 12.8% | 19.1% | 14.7% | 11.1% | 11.9% |
| RM/cig | 0.09 | 0.10 | 0.15 | 0.22 | 0.23 | 0.26 | 0.29 | 0.33 |
| YoY Gr% | 9.6% | 14.0% | 43.8% | 46.5% | 4.3% | 14.9% | 11.6% | 12.7% |
| Gross Profit/cig | 0.63 | 0.72 | 0.82 | 0.87 | 1.07 | 1.22 | 1.36 | 1.52 |
| YoY Gr% | 8.3% | 13.2% | 13.5% | 6.7% | 22.8% | 14.7% | 11.0% | 11.7% |
| Gross Profit Margin % | 88% | 88% | 85% | 80% | 83% | 83% | 82% | 82% |
| Other Exp/Cig | 0.23 | 0.25 | 0.26 | 0.26 | 0.34 | 0.38 | 0.43 | 0.47 |
| YoY Gr% | 7.5% | 8.9% | 3.8% | 0.3% | 29.0% | 14.0% | 11.0% | 11.0% |
| EBITDA/Cig | 0.40 | 0.47 | 0.55 | 0.61 | 0.73 | 0.84 | 0.93 | 1.04 |
| YoY Gr% | 8.8% | 15.7% | 18.7% | 9.7% | 20.1% | 15.0% | 10.9% | 12.0% |
| EBITDA Margin % | 55.8% | 57.0% | 57.6% | 56.1% | 56.5% | 56.7% | 56.6% | 56.7% |
| Depreciation/cig | 0.01 | 0.02 | 0.02 | 0.02 | 0.03 | 0.03 | 0.03 | 0.03 |
| PBIT/cig (Rs) | 0.39 | 0.45 | 0.53 | 0.59 | 0.71 | 0.82 | 0.91 | 1.03 |
| YoY Gr% | 9.4% | 15.3% | 18.6% | 10.1% | 20.1% | 16.0% | 11.5% | 12.7% |

Source: PINC Research, Company

Better revenue mix would help in maintaining higher net price growth v/s gross price growth...

FMCG Business - encouraging performance

Although FMCG business contributes only ~19% of the total sales, it has a significant presence among the leading FMCG players. The business has developed multifold in the past 8 years and higher focus and better revenue mix has improved the operational performance too.

No 1 in branded packaged Atta among domestic players...

No 3 in Biscuits ...

No 2 in Noodles All India (Urban)...

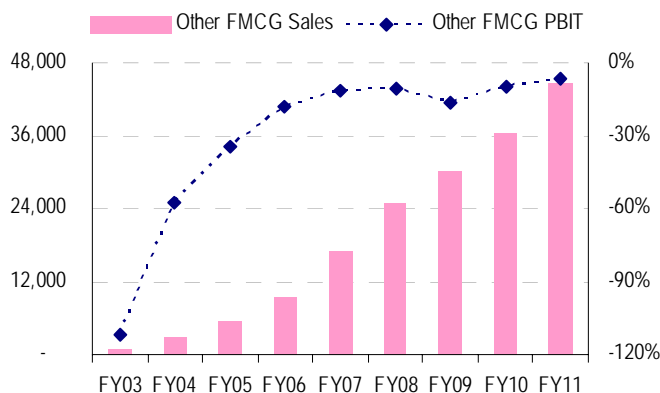
Exhibit 47 - FMCG Sales Breakup (%)

| Segments | Brands | Sales Mix (FY11) |
|------------------------|--|------------------|
| Branded Packaged Foods | Aashirvaad Atta | ~21.6% |
| | Sunfeast Biscuits | ~21.6% |
| | Minto, Candyman | ~3.1% |
| | Bingo | ~14.1% |
| | Yippee Noodles | ~2.2% |
| Matches | Ship, Houselite | ~5.5% |
| Others | Wills Lifestyle, John Players | ~8.1% |
| | Education and Stationary - Classmate, PaperKraft, Colour Crew | ~13.0% |
| | Incense Sticks - Mangaldeep | ~3.7% |
| | Personal care products - Essenza Di Wills, Fiama Di Wills, Vivel Di Wills, Superia | ~7.1% |

Source: PINC Research

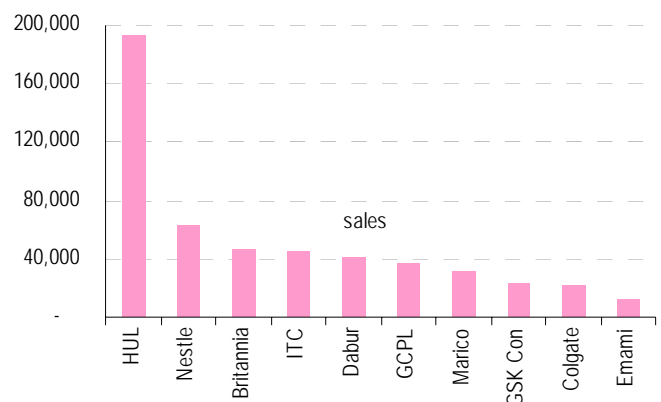
In our opinion, 'Branded Packaged Food' and 'Stationary' businesses are profitable while 'Lifestyle Retailing' and 'Personal Care' businesses are loss making thus impacting the overall profitability of the segment. The segment has consistently reduced the losses at PBIT level. We are encouraged by 240bps decline in PBIT loss (% of sales) during H1FY12 to ~5% of sales, particularly when input prices are facing high inflation. On account of softening of input prices and better growth in the profitable businesses, we expect FMCG segment to further reduce the losses and achieve breakeven in FY13.

Exhibit 48 - Strong Performance of FMCG Segment



Source: PINC Research, Company

Exhibit 49 - Significant Presence in FMCG Market



Source: PINC Research, Company

Branded Packaged Foods

| (Rs mn) | FY04 | FY11 |
|---------|-------|--------|
| Sales | 1,365 | 28,937 |

Source: PINC Research, Company

Branded Packaged Foods - matured category

ITC's branded food business is dominated by Aashirvaad and Sunfeast brand. Aggressive vertical and horizontal expansion has enabled ITC to achieve ~Rs29bn business in 7 years from mere Rs1.4bn in FY04. Aashirvaad atta and Sunfeast biscuits combined contributes ~67% of the total branded packaged food business. Aashirvaad is a matured brand and besides packaged wheat flour, ITC also uses this brand for salt, instant mix and organic spices.

Sunfeast was a game changer in the biscuit category. Through aggressive marketing, attractive pricing and regular launches, ITC poised a major challenge to incumbent big competitors like Britannia and Parle. Sunfeast covers almost whole category of biscuits from Glucose to Milky, Marie, Cream, Salted, Cookies and Dark Chocolates. Therefore, Sunfeast has been able to achieve 12% market share in a very competitive category.

Bingo has also become one of the key brands for ITC in the packaged food category. In short period of four years, ITC has positioned its Bingo brand well in snacks category and obtained >Rs6bn of sales.

Exhibit 50 - Food Business History

| Brands | Category | Launch | History |
|-------------------|---------------|--------|--|
| Kitchens of India | Ready to Eat | 2,001 | Through launch of "Dal Bukhara" |
| | | 2,004 | Launch of several non-veg cooking pastes |
| | | 2,010 | Launch of Masala mix- Paneer Makhani, Vegetable Biryani Mix, Chicken curry mix, Butter chicken mix and Hyderabad Biryani Mix |
| Aashirvaad | Staples | 2,002 | Introduce packaged wheat flour |
| | | 2004 | Launch of Aashirvaad Salt |
| | | 2,006 | Launch of instant mix- Rice, Idli, Rava Idli, Rice Dosa, Gulab Jamun and Khaman Dhokla |
| | | 2,007 | Launch of organic spices- chili, turmeric and coriander powders |
| Mint-O | Confectionery | 2002 | Through acquisition of Mint-O from Candico |
| | | 2004 | Extension of Mint-O to Mint-O Fresh |
| Candyman | Confectionery | 2003 | |
| Sunfeast | Biscuit | 2003 | Launch biscuits with entrance in glucose and cream segment |
| | | 2005 | Enter into instant pasta category through launch of "Pasta Treat" |
| | | 2010 | Entrance into noodles segment through launch of Sunfeast Yippee Noodles |
| Bingo | Snack Foods | 2007 | Potato chips and finger snacks |

Source: PINC Research, Company

Exhibit 51 - Positioning of Food Business

| Products | Mkt Share (%) | Peers |
|-------------------------|---------------------------------------|--|
| Aashirvaad | 50% in the branded flour market | Annapurna (HUL), Pillsbury (General Mills) and Shakti Bhog (Shakti Bhog Foods) |
| Confectionery | 10% in sugar based confectionery | Perfetti, Wrigley |
| Sunfeast Biscuits | 12% | Parle, Britannia |
| Sunfeast Yippee Noodles | No 2 position with ~7-8% market share | Nestle, Top Ramen, HUL, GSK Consumers |
| Bingo | 8% | PepsiCo |

Source: PINC Research, Company

Outlook: Our understanding is that, ITC has given enough focus to settle these brands in the market. Aashirvaad and Sunfeast are the matured brands and the positioning of Bingo is also well recognized. Going forward this business requires less investment which would help in expanding profitability.

Personal care products - promising category

ITC entered into personal care category in 2005 and today it has presence into Soap, Hair Care, Bath Care, Fairness cream, Deo and Perfumes. ITC covers these categories through four brands i.e. Essenza Di Wills, Fiama Di Wills, Vivel and Superia that caters super premium, premium, mid market and entry level respectively.

Exhibit 52 - Positioning of Personal Care Products

| Brands | Class | Products |
|------------------|-----------------|---|
| Superia | Popular Segment | Soaps and Shampoo |
| Vivel | Mid Market | Soaps and Shampoo, Fairness Cream |
| Fiama Di Wills | Premium | Shampoo, Soaps, Shower Gel, Conditioner |
| Essenza Di Wills | Super Premium | Perfume, Deo |

Source: PINC Research, Company

Outlook: Our understanding is that positioning of these four brands is not communicated well to consumers. Some of these products and price points overlap to each other and brand recognition is not very clear. Personal care is a very competitive category and MNCs dominant the market. ITC would have to invest high on product development and marketing of these products to achieve some significant market share. Therefore we expect profitability would be under pressure going forward.

Lifestyle retailing– More for Brand Equity Perspective

ITC’s lifestyle retailing business is positioned well in the >Rs100bn branded apparel market. ITC run this business with ‘Wills Lifestyle’ and ‘John Players’ brands catering to premium and popular segments in the branded apparel market respectively.

ITC forayed into the youth fashion segment through the launch of ‘John Players’ in 2002. ‘John Players’ is competing with ‘Peter England’ in the mass market range. We believe lifestyle retailing contributes ~8% of ITC’s net sales and share large portion of FMCG losses.

Exhibit 53 - Reach of 'Wills Lifestyle' Brand

| Wills Lifestyle | FY09 | FY10 | FY11 |
|------------------|------|------|------|
| Exclusive Stores | 50 | 56 | 73 |
| Shop-in-Shops | 150 | 150 | 150 |
| Cities | 30 | 30 | 40 |

Source: PINC Research, Company

Exhibit 54 - Reach of 'John Players' Brand

| John Players | FY09 | FY10 | FY11 |
|--------------------|-------|-------|-------|
| Flagship Stores | 200 | 225 | 280 |
| Multibrand Outlets | 1,300 | 1,200 | 1,100 |

Source: PINC Research, Company

Education and Stationery – robust growth

ITC started education and stationery business in 2002 with premium 'Paperkraft' brand and in 2003 it expanded into the popular segment with 'Classmate' brand.

'Paperkraft' portfolio comprises premium business paper, paper stationery, markers and highlighters. The brand is mainly focused on executive class.

'Classmate' range has over 300 variants of notebook, graph, drawing books, practical notebook, reminder pads and more. 'Classmate' is the dominant brand in writing material segment (~Rs40bn market) with ~12% market share (in 2010) which is followed by 'Navneet' at ~6%.

Stationery product market is >Rs100bn market in India of which notebook accounts for 40%. The market is dominated by the unorganised players which accounts ~75% of the total market. ITC operates this business through >900 distributors and its products are available at >70,000 outlets.

We believe education and stationery business comprises 13% of total net sales. It has displayed robust growth in the past and we are witnessing greater shift towards branded stationery which augurs well for ITC. We have positive bias for the business in terms of sales and profitability.

Hotel Business Performance

| (In Rs mn) | FY08 | FY11 |
|------------|--------|--------|
| Sales | 10,121 | 10,008 |
| PBIT | 4,108 | 2,666 |

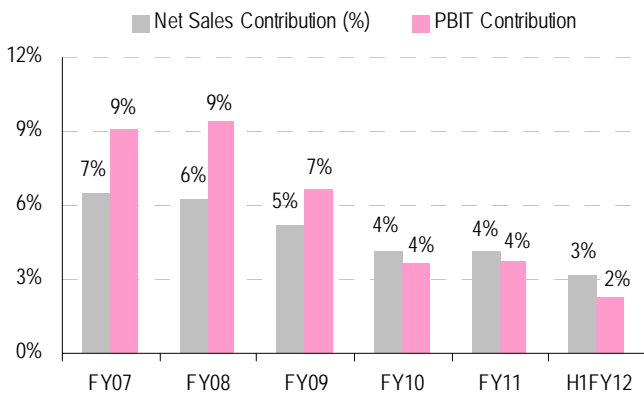
Source: PINC Research, Company

Hotels - sowing money to reap long term benefits

ITC operates +100 Hotels in 90 locations in India through its four brands i.e. ITC Hotels, WelcomHotel, Fortune and WelcomHeritage which covers mix of luxury, heritage and mid segment.

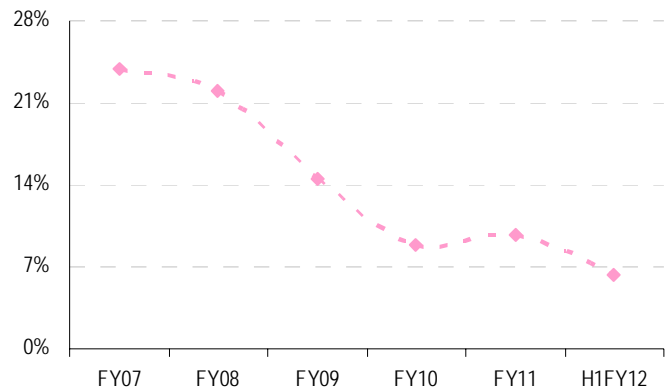
Hotel business has high dependence on foreign visitors therefore slowdown in the developed countries impacted ITC's performance during FY09 and FY10. The business improved in FY11 although sales and profitability could not achieve FY08 level. We don't expect any significant change in Hotel contribution in sales and PBIT in near term.

Exhibit 55 - Hotels Contribution in Sales and PBIT



Source: Company

Exhibit 56 - ROCE Under Pressure



Source: Company

ITC plans to invest ~Rs15-18bn over the next three years for expansion of hotel business. We believe in the near term it will further increase pressure on return ratio however long term potential of this business is immense. India is one of the favourite destinations for tourists and premium category hotels are in short supply. ITC's hotel expansion is to tap those opportunities.

5 Star category accounts for ~25% of total rooms in India ...

Exhibit 57 - ITC's Hotel Mix

| No of Hotels | Category | Owned/Lease | Rooms Managed | Total |
|--------------|----------------------|--------------|---------------|--------------|
| 15 | 5 Star Deluxe | 2,732 | 705 | 3,437 |
| 38 | Fortune- Mid Segment | | 3,088 | 3,088 |
| 53 | Heritage | | 1,335 | 1,335 |
| 106 | Total | 2,732 | 5,128 | 7,860 |

Source: PINC Research, Company

Exhibit 58 - Hotels Peer Comparison

| Particulars | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|--------------------------|--------------|--------------|---------------|---------------|--------------|---------------|
| Sales (Rs mn) | | | | | | |
| Indian Hotel | 19,554 | 27,035 | 30,306 | 27,993 | 26,467 | 29,618 |
| EH | 9,719 | 11,659 | 13,090 | 12,150 | 10,477 | 12,969 |
| ITC | 7,779 | 9,787 | 10,935 | 10,146 | 9,049 | 10,680 |
| Hotel Leela | 3,734 | 4,973 | 5,891 | 5,821 | 4,784 | 5,534 |
| Mahindra Holiday | 1,568 | 2,413 | 3,772 | 4,421 | 5,213 | 5,464 |
| EBITDA (Rs mn) | | | | | | |
| Indian Hotel | 6,258 | 9,168 | 9,475 | 6,159 | 5,221 | 5,449 |
| EH | 4,170 | 4,781 | 5,189 | 4,467 | 3,034 | 3,042 |
| ITC | 3,204 | 4,156 | 4,784 | 3,873 | 2,982 | 3,555 |
| Hotel Leela | 1,817 | 2,610 | 3,040 | 2,851 | 1,535 | 1,826 |
| Mahindra Holiday | 439 | 793 | 1,440 | 1,521 | 2,007 | 1,717 |
| EBITDA Margin (%) | | | | | | |
| Indian Hotel | 32.0% | 33.9% | 31.3% | 22.0% | 19.7% | 18.4% |
| EH | 42.9% | 41.0% | 39.6% | 36.8% | 29.0% | 23.5% |
| ITC | 41.2% | 42.5% | 43.8% | 38.2% | 33.0% | 33.3% |
| Hotel Leela | 48.6% | 52.5% | 51.6% | 49.0% | 32.1% | 33.0% |
| Mahindra Holiday | 28.0% | 32.9% | 38.2% | 34.4% | 38.5% | 31.4% |

Critical player in the Hotel industry...

ITC leads in profitability front...

Source: PINC Research, Capitaline

Exhibit 59 - Foreign Tourist Arrivals (FTAs) in World and India

| Year | World Number (In mn) | YoY Gr. (%) | India Number (In mn) | YoY Gr. (%) | Percentage of India | Rank of India |
|------|----------------------|-------------|----------------------|-------------|---------------------|---------------|
| 1997 | 593.0 | 4.2 | 2.4 | 3.8 | 0.40 | - |
| 1998 | 611.0 | 3.0 | 2.4 | (0.7) | 0.39 | 47th |
| 1999 | 633.8 | 3.7 | 2.5 | 5.2 | 0.39 | 46th |
| 2000 | 683.3 | 7.8 | 2.7 | 6.7 | 0.39 | 50th |
| 2001 | 683.4 | 0.2 | 2.5 | (4.2) | 0.37 | 51st |
| 2002 | 703.2 | 2.9 | 2.4 | (6.0) | 0.34 | 54th |
| 2003 | 691.0 | (1.7) | 2.7 | 14.3 | 0.39 | 51st |
| 2004 | 762.0 | 10.3 | 3.5 | 26.8 | 0.45 | 44th |
| 2005 | 798.0 | 5.4 | 3.9 | 13.3 | 0.49 | 43rd |
| 2006 | 846.0 | 5.3 | 4.5 | 13.5 | 0.53 | 44th |
| 2007 | 894.0 | 5.7 | 5.1 | 14.3 | 0.57 | 41st |
| 2008 | 917.0 | 2.6 | 5.3 | 4.0 | 0.58 | 42nd |
| 2009 | 882.0 | (3.8) | 5.2 | (2.2) | 0.59 | 42nd |
| 2010 | 940.0 | 6.6 | 5.8 | 11.8 | 0.61 | 40th |

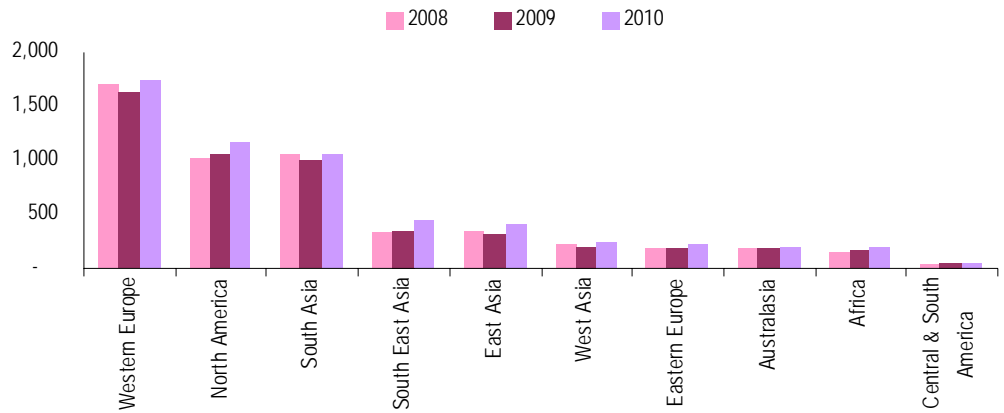
Foreign arrivals into India 5.8mn v/s 59.7mn in USA and 52.7mn in China...

Tourism contributes 6.2% of India's GDP...

Source: PINC Research, Ministry of Tourism

Exhibit 60 - Region-wise FTAs in India

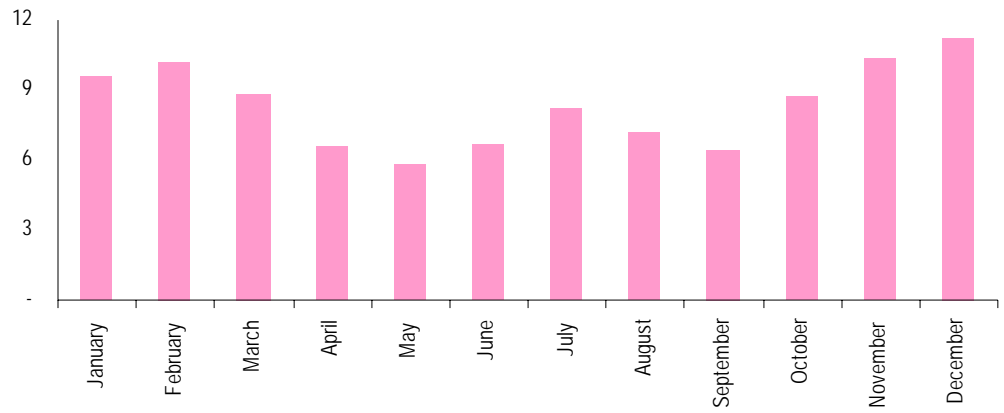
Europeans are the largest FTAs in India...



Source: PINC Research, Ministry of Tourism

Exhibit 61 - Average Month-wise FTAs Share in India

On an average >60% FTAs in second half of every financial year...



Source: PINC Research, Ministry of Tourism

Better performance of Paperboard and Agribusiness

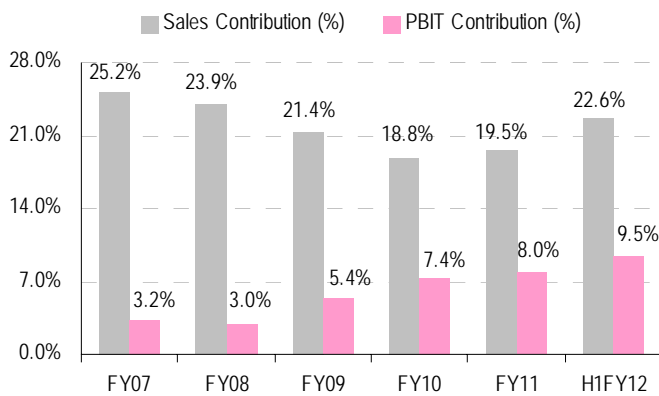
A significant portion of ITC’s Paperboard and Agribusiness segments support the cigarette and FMCG businesses. Large part of the inter segment revenue is contributed by these two segments. Both segment increased their contribution in sales and profitability and to some extent set off the muted Hotel performance in the past few years.

Agribusiness is largely trading business and it accounts ~60% of ITC’s total exports. Un-manufactured leaf tobacco is the largest product (~47% of total agribusiness) for the segment and fetches high margins. ITC also trades Soya in extraction, oil and seed form and these three combined contribute ~26% of agribusiness. Other key commodities for agribusiness are Coffee, Fruit pulp, Spices, Rice, Chillies, and Wheat etc.

Like any other commodity business, agribusiness is prone to high volatility. However, over a period of time ITC has been able to develop strong network with farmers which provides extensive backward linkages to agribusiness and has reduced volatility. ITC’s ‘e-Choupal’ model created a significant two-way multi-dimensional channel between farmers and ITC. Through ‘e-Choupal’ ITC is now connected with more than 4mn farmers in 40,000 villages in 10 states.

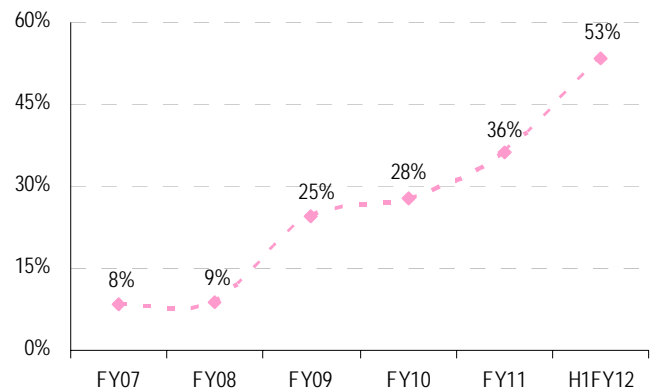
The profitability of agribusiness has improved substantially in the past 5 years. PBIT margin expanded to 12% in FY11 as compared to 4% in FY07. We expect agribusiness to maintain its growth as well as profitability momentum. Further development of ‘e-Choupal’ and other agri initiatives would help in expanding business.

Exhibit 62 - Agribusiness Contribution in Sales & PBIT



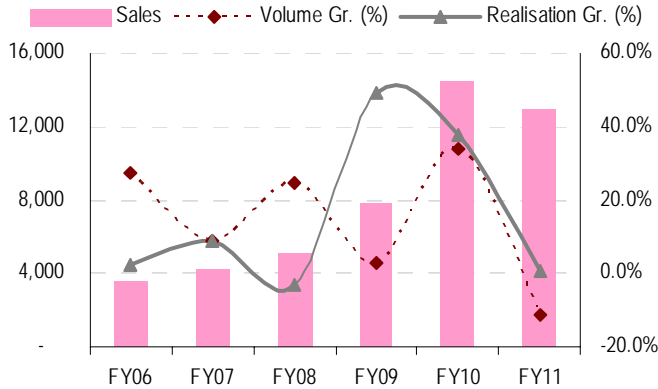
Source: PINC Research, Company

Exhibit 63 - Agribusiness ROCE (%)



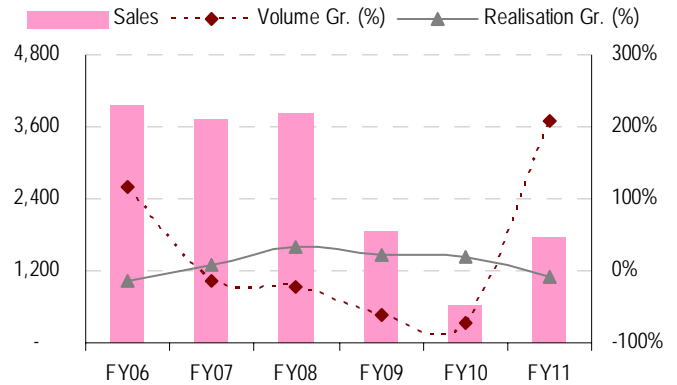
Source: PINC Research, Company

Exhibit 64 - Unmanufactured Tobacco Business



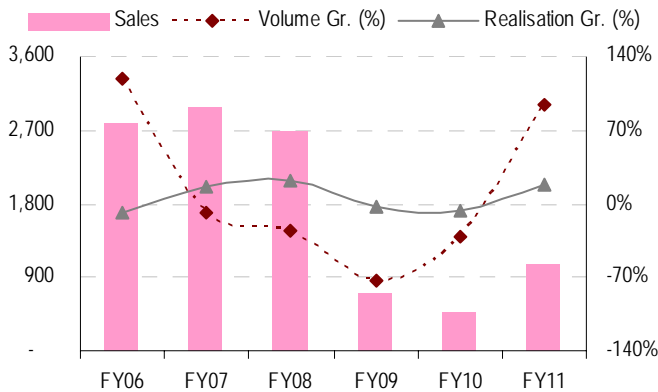
Source: PINC Research, Company

Exhibit 65 - Soya Extraction Business



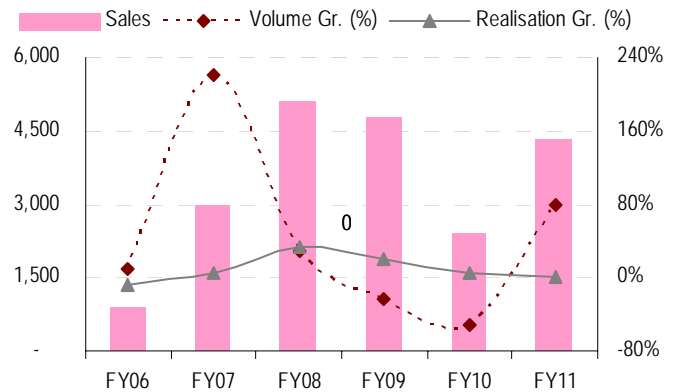
Source: PINC Research, Company

Exhibit 66 - Soya Oil Business



Source: PINC Research, Company

Exhibit 67 - Soya Seed Business



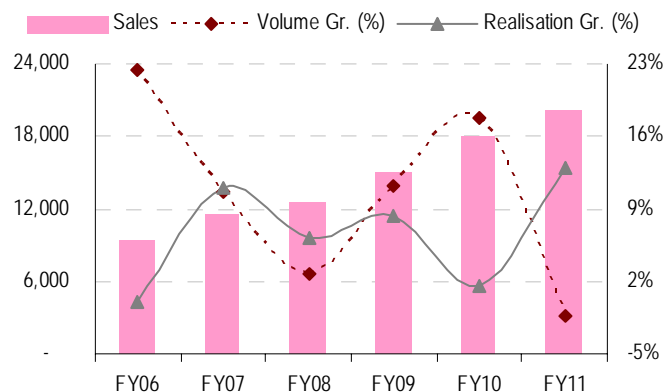
Source: PINC Research, Company

ITC's 'Paperboard, Paper and Packaging' business caters to packaging, graphic, communication, writing, printing and specialty paper requirement. Paper and paperboard business contributes >85% of the segment and it had a 17% CAGR in the past 3 years. This business was also a strategic move for backward integration of the cigarette business. A big portion (~38% of the total gross sales) of this business is being consumed internally.

ITC is now focusing more on the value-added products where ITC is already leader in the market. Value-added coated board growing at 15% and the outlook of the business is strong. The company recently indicated on robust demand from the retail segment for supplying of scratch card. To fulfill the upcoming demand for the value added products, ITC is expanding capacities.

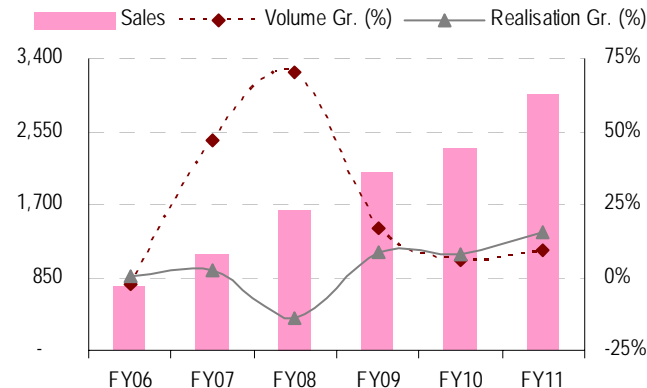
ITC maintained profitability of this business and PBIT margin has been moved between 20%-25% in the past 5 years. We expect higher contribution from the value-added products which would further improve the margin profile of this business.

Exhibit 68 - Paper and Paperboard Business



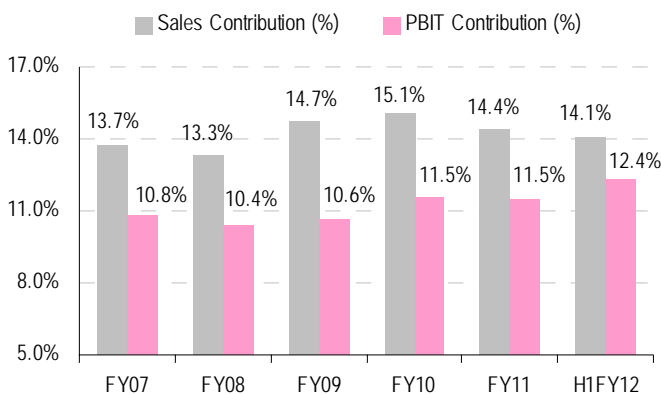
Source: PINC Research, Company

Exhibit 69 - Printing/Packaging Business



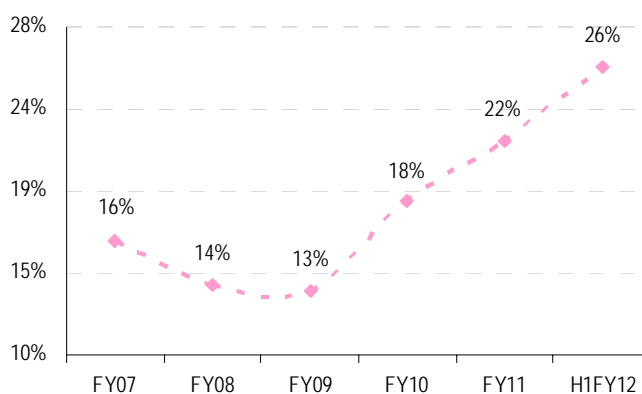
Source: PINC Research, Company

Exhibit 70 - Paperboard Contribution in Sales & PBIT



Source: PINC Research, Company

Exhibit 71 - Paperboard ROCE (%)



Source: PINC Research, Company

India's paperboard per capita consumption is mere 9kg compared to global average of 55kg ...

ITC has 26% market share in domestic paperboard market...

ITC leads in profitability front...

Exhibit 72 - Paper Business Peer Comparison

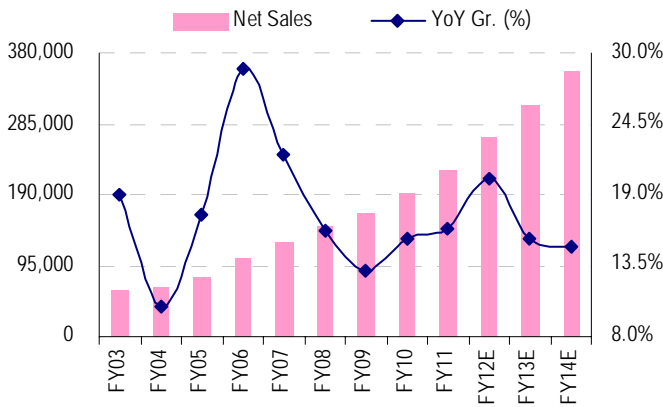
| | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
|----------------------------------|--------|--------|--------|--------|--------|--------|
| Sales (Rs mn) | | | | | | |
| Ballarpur | 18,003 | 22,038 | 24,247 | 26,512 | 33,826 | 39,275 |
| ITC | 19,097 | 21,001 | 23,643 | 28,220 | 32,336 | 36,669 |
| Andhra Paper/International Paper | 4,458 | 4,868 | 5,784 | 6,279 | 6,493 | 7,818 |
| Century Textile | 4,581 | 5,417 | 8,150 | 8,593 | 8,806 | 10,109 |
| EBITDA (Rs mn) | | | | | | |
| Ballarpur | 4,865 | 5,715 | 6,974 | 6,396 | 7,944 | 8,581 |
| ITC | 4,653 | 5,386 | 5,888 | 7,009 | 9,010 | 10,506 |
| Andhra Paper/International Paper | 629 | 554 | 671 | 1,151 | 1,443 | 1,471 |
| Century Textile | 1,273 | 1,456 | 1,826 | 1,518 | 268 | 913 |
| EBITDA Margin (%) | | | | | | |
| Ballarpur | 27% | 26% | 29% | 24% | 23% | 22% |
| ITC | 24% | 26% | 25% | 25% | 28% | 29% |
| Andhra Paper/International Paper | 14% | 11% | 12% | 18% | 22% | 19% |
| Century Textile | 28% | 27% | 22% | 18% | 3% | 9% |

Source: PINC Research, Capitaline

Financial Analysis

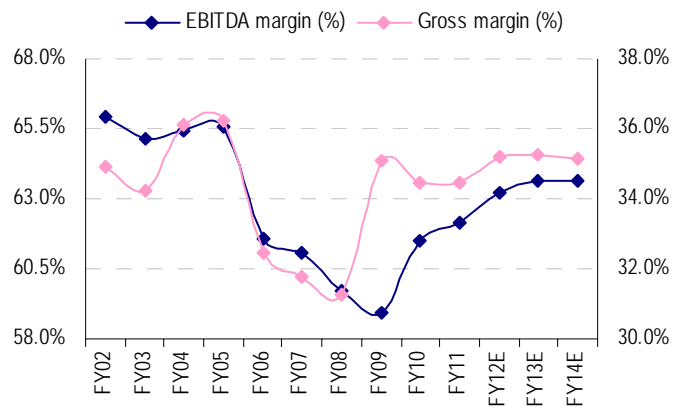
- We expect cigarette and non cigarette net sales CAGR of 16% and 16.9% respectively during FY11-14E.
- Due to strong profitability in cigarette business, ITC's profitability profile is far better and secure as compared to other FMCG players. The lowest EBITDA margin in past 10 years was at 31% which is even superior to highest margin of any FMCG player.

Exhibit 73 - Expectation of Healthy Sales Growth



Source: PINC Research, Company

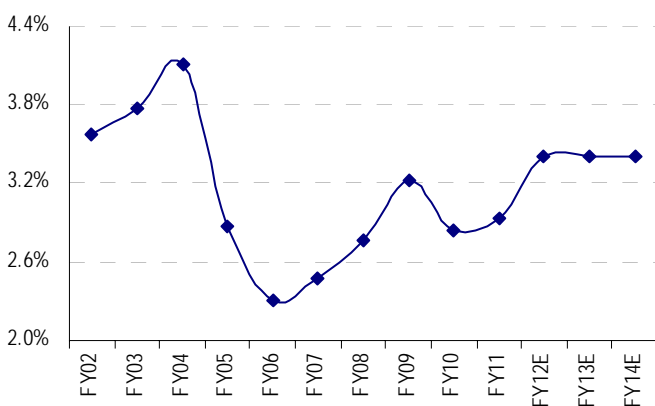
Exhibit 74 - Strong Operational Margin



Source: PINC Research, Company

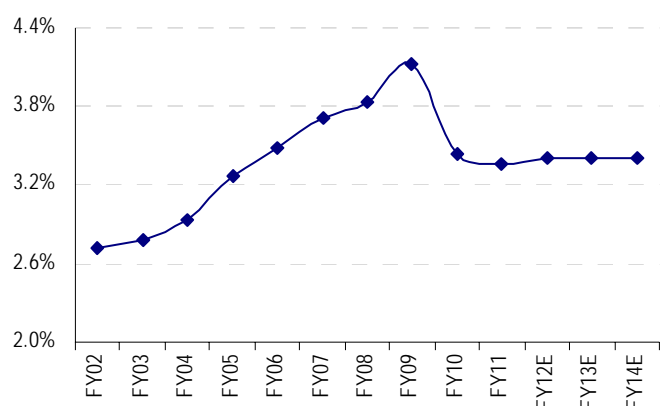
- ITC's spending on advertisement (% of sales) is much lower than other FMCG companies as cigarette, paper and agribusiness doesn't require advertisement. ITC's large part of A&P spending occurs on its FMCG business which includes branded packaged foods, personal care, education & stationary and life style retailing. We believe ITC is competitive on A&P spending on FMCG business.

Exhibit 75 - Advertisements Expense (% of net sales)



Source: PINC Research, Company

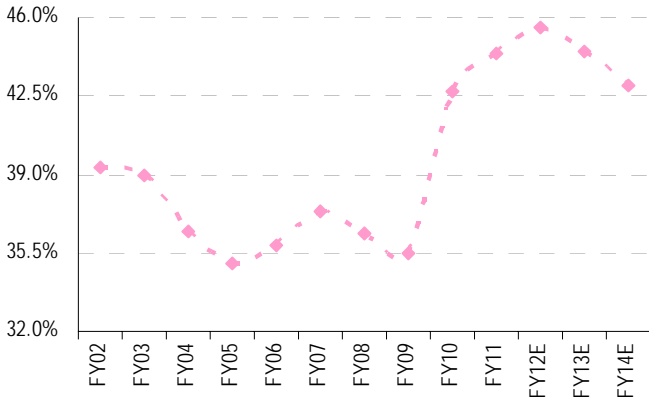
Exhibit 76 - Distribution Expense (% of net sales)



Source: PINC Research, Company

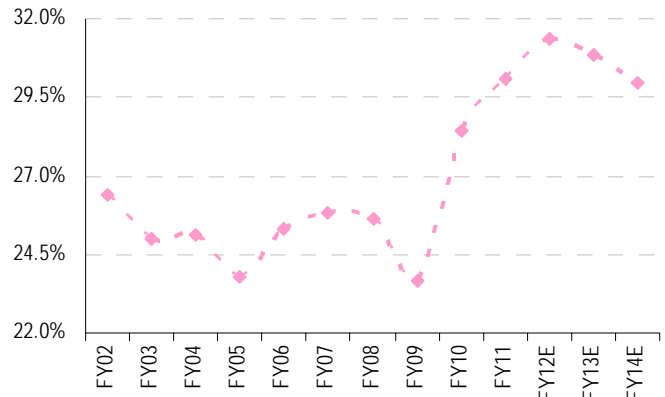
- Historically, cigarette business ROCE and ROE ranges in 140-160% v/s depressed return profile of non cigarette business which ranges between 8-14%. We expect overall return profile to be maintained going forward owing to requirement of high investment in the non cigarette businesses.

Exhibit 77 - ROCE Movement



Source: PINC Research, Company

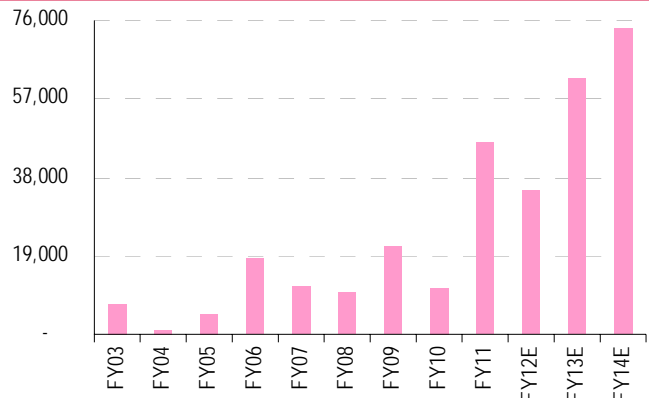
Exhibit 78 - ROE Movement



Source: PINC Research, Company

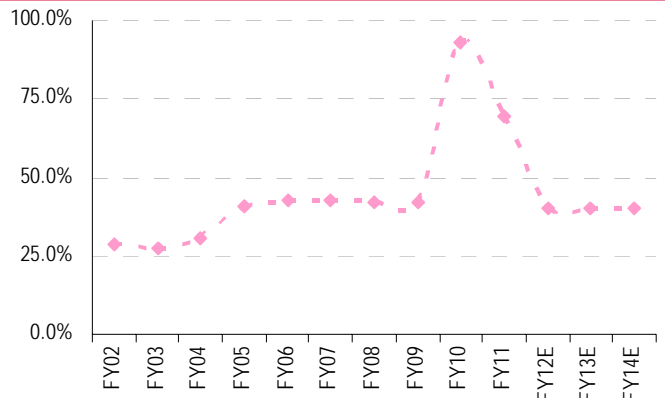
- ITC has been maintaining a dividend payout ratio of 40% except for FY10 and FY11 when it distributed special dividend. We expect ITC would maintain 40% dividend payout ratio going forward as the company plans for high capex.

Exhibit 79 - Strong FCF to Continue (Rs mn)



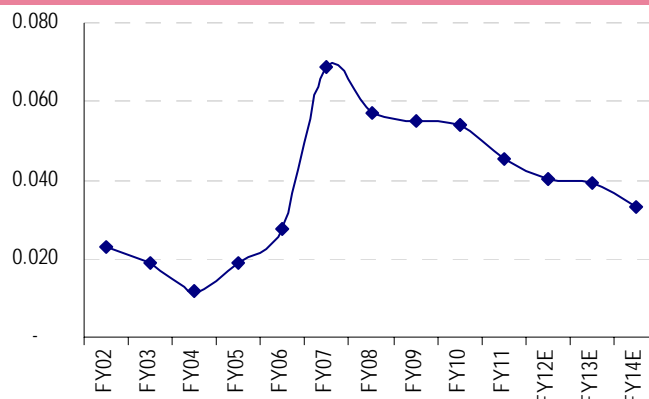
Source: PINC Research, Company

Exhibit 80 - Special Dividend Changed the Trajectory



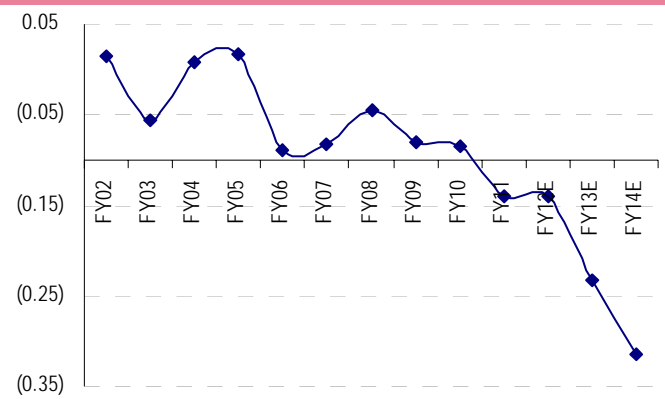
Source: PINC Research, Company

Exhibit 81 - Capex/Cigarette (Rs/stick)



Source: PINC Research, Company

Exhibit 82 - Net Debt/Equity Ratio



Source: PINC Research, Company

Company Background

ITC was incorporated in 1910 under the name of 'Imperial Tobacco Company of India Limited' which was later renamed to 'India Tobacco Company Limited' in 1970, 'I.T.C. Limited' in 1974 and finally named to 'ITC Limited' in 2001. ITC is one of the largest Indian conglomerates with presence in cigarette, FMCG, hotel, paperboard and agribusiness.

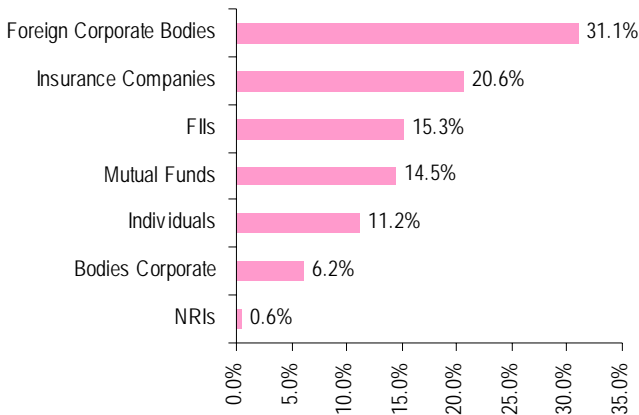
Exhibit 83 - ITC's Business History

| Year | Details |
|------|---|
| 1910 | Incorporated and run cigarette and leaf tobacco business |
| 1925 | ITC's first diversification of cigarette business was packaging and printing business which was started in 1925. It was strategic backward integration for ITC's cigarette business. |
| 1975 | Then ITC waited 50 years to enter into Hotel business with the acquisition of a hotel in Chennai. |
| 1979 | ITC entered into paperboard business through 'ITC Bhadrachalam Paperboard Limited' which amalgamated into ITC in 2002. |
| 1985 | ITC set up Surya Tobacco Co. in Nepal as an Indo-Nepal and British joint venture. In 2002, Surya Tobacco became a subsidiary of ITC Limited and its name was changed to Surya Nepal Private Limited (Surya Nepal) |
| 1990 | ITC acquired Tribeni Tissues Limited, a Specialty paper manufacturing company and a major supplier of tissue paper to the cigarette industry. Tribeni Tissues Division was merged with the Bhadrachalam Paperboards Division to form the Paperboards & Specialty Papers Division in 2002. |
| 1990 | To leverage agri-sourcing competency, ITC set up the Agri Business Division for export of agri-commodities. The Division is today one of India's largest exporters. |
| 2000 | Forayed into Education and Stationery business. |
| 2000 | ITD made a presence into Lifestyle Retailing business |
| 2000 | ITC spun off its IT business into a wholly owned subsidiary ITC Infotech India Ltd |
| 2001 | ITC foray into food business through launch of 'Kitchens of India' |
| 2002 | Commence Confectionery business |
| 2002 | Launch of Aashirvaad Atta |
| 2003 | Foray into biscuit business through 'Sunfeast' brand |
| 2003 | Commenced business of marketing of Agarbattis, having Spriha and Mangaldeep brands |
| 2005 | Introduced Essenza Di Wills, an exclusive range of fine fragrances and bath & body care products for men and women |
| 2007 | Entered into branded snacks category through launch of 'Bingo' |
| 2007 | Launch of 'Fiama Di Wills', a premium range of Shampoos, Shower Gels and Soaps |
| 2007 | Superia' range of Soaps and Shampoos in the mass-market segment |
| 2008 | Vivel range of shampoos |
| 2010 | Entrance into noodles segment through launch of Sunfeast Yippee Noodles |

Source: Company, PINC Research

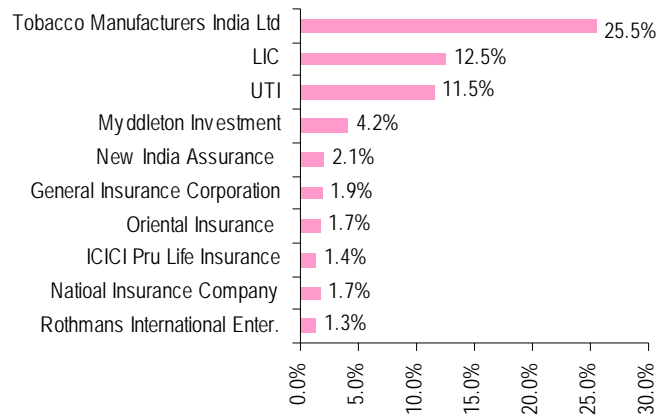
ITC has 100% free float as there is no promoter holding in the company. BAT is the largest shareholder with 31% indirect holding through its affiliates 'Tobacco Manufacturers India Ltd', 'Myddleton Investment Company Ltd' and 'Rothmans International Enterprises Ltd'. Insurance companies hold 20.6% with largest stake being held by LIC at 12.5%.

Exhibit 84 - Shareholding Pattern (%)



Source: PINC Research, BSE Sep'2011 Shareholdings

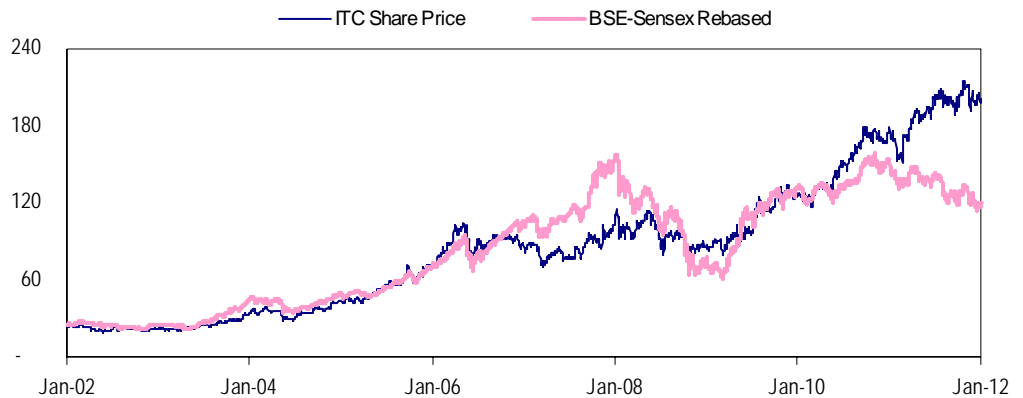
Exhibit 85 - Holding More Than 1% of the Total Shares



Source: PINC Research, BSE Sep'2011 Shareholdings

Over the last 10 year, ITC's stock has consistently outperformed benchmark BSE Sensex. During this time, BSE Sensex grew by 5x while ITC grew by >8x. Even in the last one year, ITC's has outperformed BSE Sensex by >30%.

Exhibit 86 - ITC's Share Price History v/s BSE-SENSEX Rebased



Source: PINC Research, Bloomberg

Exhibit 87 - ITC's Bonus History

| YEAR | BONUS |
|------|---|
| 1978 | One share for every five shares held |
| 1980 | One share for every five shares held |
| 1989 | One share for every one share held |
| 1991 | Three shares for every five shares held |
| 1994 | One share for every one share held |
| 2005 | One share for every two shares held |
| 2010 | One share for every one share held |

Source: PINC Research, Company

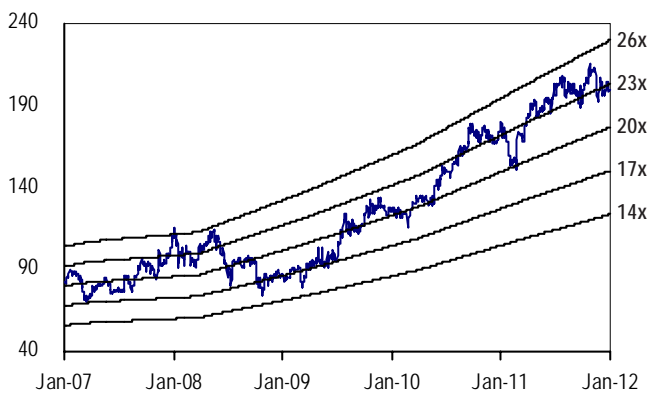
| Income Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|------------------------|---------|---------|---------|---------|---------|
| Gross Sales | 276,234 | 320,782 | 370,942 | 425,066 | 481,264 |
| Net sales | 191,359 | 222,737 | 267,694 | 309,394 | 355,647 |
| Growth (%) | 15.6 | 16.4 | 20.2 | 15.6 | 14.9 |
| EBITDA | 62,730 | 74,208 | 91,485 | 106,812 | 122,803 |
| Growth (%) | 23.3 | 18.3 | 23.3 | 16.8 | 15.0 |
| Depreciation | 6,439 | 6,990 | 7,489 | 8,110 | 8,800 |
| Other Income | 6,440 | 7,951 | 8,881 | 10,264 | 11,566 |
| EBIT | 62,731 | 75,169 | 92,877 | 108,966 | 125,569 |
| Interest Paid | 918 | 818 | 865 | 865 | 865 |
| PBT (before E/o items) | 61,813 | 74,351 | 92,011 | 108,101 | 124,703 |
| Tax Provision | 20,350 | 23,655 | 29,444 | 34,592 | 39,905 |
| Minority Interest | 488 | 611 | 705 | 814 | 814 |
| E/o income/(loss) | (86) | 624 | - | - | - |
| Reported PAT | 41,037 | 50,182 | 61,963 | 72,800 | 84,095 |
| Adjusted PAT | 41,123 | 49,558 | 61,963 | 72,800 | 84,095 |
| Growth (%) | 23.8 | 20.5 | 25.0 | 17.5 | 15.5 |
| Diluted EPS (Rs) | 5.3 | 6.4 | 8.0 | 9.4 | 10.9 |
| Diluted EPS Growth (%) | 22.4 | 20.5 | 25.0 | 17.5 | 15.5 |

| Cash Flow Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|----------|----------|----------|----------|----------|
| Pre-tax profit | 62,457 | 74,349 | 92,011 | 108,101 | 124,703 |
| Depreciation | 6,439 | 6,991 | 7,489 | 8,110 | 8,800 |
| Total Tax Paid | (20,712) | (22,784) | (29,252) | (34,386) | (39,682) |
| Chg in working capital | (882) | 119 | (17,153) | 916 | (303) |
| Other operating activities | (2,870) | (4,139) | 966 | 971 | 977 |
| Cash flow from oper (a) | 44,433 | 54,536 | 54,061 | 83,713 | 94,495 |
| Capital Expenditure | (12,463) | (14,207) | (18,700) | (18,100) | (17,100) |
| Chg in investments | (24,805) | 2,784 | (600) | (3,550) | (3,550) |
| Other investing activities | 3,804 | 3,261 | - | - | - |
| Cash flow from inv.(b) | (33,464) | (8,162) | (19,300) | (21,650) | (20,650) |
| Free cash flow (a+b) | 10,969 | 46,374 | 34,761 | 62,063 | 73,845 |
| Equity raised/(repaid) | 7,207 | 9,038 | - | - | - |
| Debt raised/(repaid) | (759) | 135 | - | - | - |
| Interest paid | (343) | (167) | (865) | (865) | (865) |
| Dividend (incl. Tax) | (14,486) | (38,662) | (24,785) | (29,120) | (33,638) |
| Other financing activities | (2,320) | (6,142) | (4,337) | (5,096) | (5,887) |
| Cash flow from fin. (c) | (10,701) | (35,797) | (29,988) | (35,082) | (40,390) |
| Net chg in cash (a+b+c) | 269 | 10,577 | 4,773 | 26,981 | 33,454 |

| Balance Sheet | FY10 | FY11 | FY12E | FY13E | FY14E |
|--------------------------|---------|---------|---------|---------|---------|
| Equity Share Capital | 3,818 | 7,738 | 7,738 | 7,738 | 7,738 |
| Reserves & surplus | 140,764 | 156,882 | 189,723 | 228,307 | 272,878 |
| Shareholders' funds | 144,582 | 164,621 | 197,461 | 236,045 | 280,616 |
| Minorities interests | 1,263 | 1,408 | 2,114 | 2,928 | 3,742 |
| Total Debt | 1,108 | 1,246 | 1,246 | 1,246 | 1,246 |
| Capital Employed | 146,953 | 167,274 | 200,820 | 240,218 | 285,603 |
| Net fixed assets | 97,974 | 105,117 | 116,328 | 126,317 | 134,617 |
| Cash & Cash Eq. | 13,485 | 24,269 | 29,043 | 56,024 | 89,479 |
| Net Other current assets | (6,694) | (2,812) | 14,342 | 13,425 | 13,729 |
| Investments | 50,003 | 48,677 | 49,277 | 52,827 | 56,377 |
| Net Deferred tax Assets | (7,805) | (7,981) | (8,172) | (8,378) | (8,601) |
| Total Assets | 146,966 | 167,273 | 200,820 | 240,218 | 285,603 |

| Key Ratios | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|--------|-------|-------|-------|-------|
| OPM (%) | 32.8 | 33.3 | 34.2 | 34.5 | 34.5 |
| Net Margin (%) | 21.5 | 22.2 | 23.1 | 23.5 | 23.6 |
| Div. Yield (%) | 2.4 | 2.2 | 1.6 | 1.9 | 2.2 |
| Net debt/Equity (x) | (0.1) | (0.1) | (0.1) | (0.2) | (0.3) |
| Net Working Capital (days) | (12.8) | (4.6) | 19.6 | 15.8 | 14.1 |
| ROCE (%) | 42.7 | 44.4 | 45.6 | 44.5 | 43.0 |
| RoE (%) | 28.4 | 30.1 | 31.4 | 30.8 | 30.0 |
| EV/Net Sales (x) | 7.8 | 6.7 | 5.6 | 4.7 | 4.0 |
| EV/EBITDA (x) | 23.9 | 20.1 | 16.2 | 13.6 | 11.6 |
| PER (x) | 38.0 | 31.5 | 25.2 | 21.5 | 18.6 |
| PCE (x) | 32.9 | 27.6 | 22.5 | 19.3 | 16.8 |
| Price/Book (x) | 10.8 | 9.5 | 7.9 | 6.6 | 5.6 |

1-Year forward P/E Band



| Assumptions | FY11 | FY12E | FY13E | FY14E |
|-------------------------|-------|-------|-------|-------|
| Cig Volume Gr. (%) | -2.8% | 6.1% | 3.0% | 1.0% |
| Cig Gross Price Gr. (%) | 18.0% | 8.9% | 10.0% | 9.9% |
| Cig Gross Sales Gr. (%) | 14.7% | 15.5% | 13.3% | 11.0% |
| Cig Net Sales Gr. (%) | 15.8% | 21.7% | 14.4% | 13.0% |
| Cig Excise Gr. (%) | 13.5% | 8.5% | 11.9% | 8.4% |
| Cig VAT Rate (%) | 14.9% | 19.4% | 19.4% | 19.4% |
| Cig PBIT (Rs/stick) | 0.71 | 0.82 | 0.91 | 1.03 |
| Cig PBIT Gr.(%) | 16.8% | 23.1% | 14.8% | 13.8% |
| FMCG Gr. (%) | 24.1% | 20.0% | 20.9% | 20.4% |
| Agribusiness Gr. (%) | 20.5% | 12.9% | 13.3% | 14.0% |
| Paper Business Gr. (%) | 12.4% | 16.1% | 16.3% | 16.4% |
| Hotel Gr. (%) | 17.3% | 10.6% | 14.2% | 12.7% |

Initiating Coverage
 Sector: FMCG
 BSE Sensex: 15,868

HUL

 BUY
 CMP Rs392
 TP Rs371

09 January 2012

Sign of improvement, Valuations stretched

Hindustan Unilever Ltd (HUL) is the largest FMCG player with the strong presence in Soaps, Detergents, Skin care, Oral care, Hair Care, Staple foods and Beverage businesses. As per our 'RIVER' analysis, we expect Personal Care segment would continue to dominate the overall profitability of HUL and would help in delivering 16.6% CAGR in net earnings during FY11-14E.

Business visibility improved, profitability scope is limited

The higher involvement of top management at the field level, setting up aggressive sales targets and expansion of distribution network are the indicators for business development. We expect it would help in delivering better revenue going forward which HUL was missing in previous several years. However, as HUL has already reduced A&P (% of sales) spending during H1FY12 to 11.5% from 14% in FY11, we believe to improve the profitability further A&P control is limited. We expect sales and net earnings to show 14.1% and 16.6% CGAR during FY11-14E as compared to 12.4% and 7% during FY08-11 respectively.

Personal care would continue to lead

Personal care accounts for 30% and 53% of sales and PBIT respectively for HUL. In our opinion, skin care is the largest contributor of personal care business and contributes ~50% of personal care EBITDA. Strong growth in skin care would adjust the profitability pressure in other categories like shampoo and oral care and would help in maintaining the profitability profile of the personal care segment.

'Soaps and Detergent' profitability upside is limited

The performance of 'Soaps and Detergent' segment in the past 3 quarters was very encouraging. The segment has not only shown better volume growth but simultaneously improved the profitability profile too. HUL in FY11 reported lowest PBIT margin of 9.5% which we believe was largely due to down trading in the detergent products. We expect segment profitability would improve from FY11 level however, achieving historical mid teen margin seems difficult due to high competition from P&G, Rohit Surfactant (Ghari), Godrej Consumers, Wipro, Reckitt Benkiser and ITC which would limit the profitability upside for the segment.

VALUATIONS AND RECOMMENDATION

We value HUL at P/E of 28x (12-month forward earnings) which is ~10% premium to the FMCG sector valuations and ~8% higher than its past three years median P/E. We arrive at a target price of Rs371 which is 6% down from the CMP. Hence, we initiate HUL with a 'REDUCE' rating.

KEY FINANCIALS (CONSOLIDATED)

| | (Rs mn) | | | | |
|---------------------|---------|---------|---------|---------|---------|
| | FY10 | FY11 | FY12E | FY13E | FY14E |
| Net Sales | 180,256 | 200,185 | 229,960 | 261,492 | 298,550 |
| YoY Gr. (%) | 8.3 | 11.1 | 14.9 | 13.7 | 14.2 |
| Op. Profits | 28,374 | 27,045 | 32,676 | 37,980 | 43,996 |
| OPM (%) | 15.7 | 13.5 | 14.2 | 14.5 | 14.7 |
| Adjusted Net Profit | 20,974 | 21,336 | 25,225 | 29,229 | 33,987 |
| YoY Gr. (%) | 5.3 | 1.7 | 18.2 | 15.9 | 16.3 |

KEY RATIOS

| | | | | | |
|---------------|-------|------|------|------|------|
| Dil EPS (Rs) | 9.6 | 9.9 | 11.7 | 13.5 | 15.7 |
| ROCE (%) | 105.5 | 99.2 | 96.8 | 93.9 | 93.8 |
| RONW (%) | 78.6 | 78.7 | 75.4 | 73.0 | 73.3 |
| P/E (x) | 41.3 | 40.2 | 34.0 | 29.3 | 25.2 |
| EV/Sales (x) | 4.6 | 4.1 | 3.6 | 3.1 | 2.7 |
| EV/EBITDA (x) | 29.4 | 30.6 | 25.1 | 21.3 | 18.2 |

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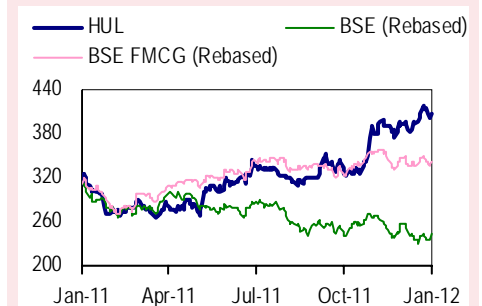
STOCK DATA

| | |
|----------------------------|-----------|
| Market cap | Rs857bn |
| Book Value per share | Rs13 |
| Shares O/S (F.V. Rs1) | 2,160mn |
| Free Float | 48% |
| Avg Trade Value (6 months) | Rs1,061mn |
| 52 week High/Low | 420/265 |
| Bloomberg Code | HUVR IN |
| Reuters Code | HLL.BO |

PERFORMANCE (%)

| | 1M | 3M | 12M |
|----------|-----|------|------|
| Absolute | 3.3 | 25.0 | 27.1 |
| Relative | 9.2 | 24.5 | 63.5 |

RELATIVE PERFORMANCE



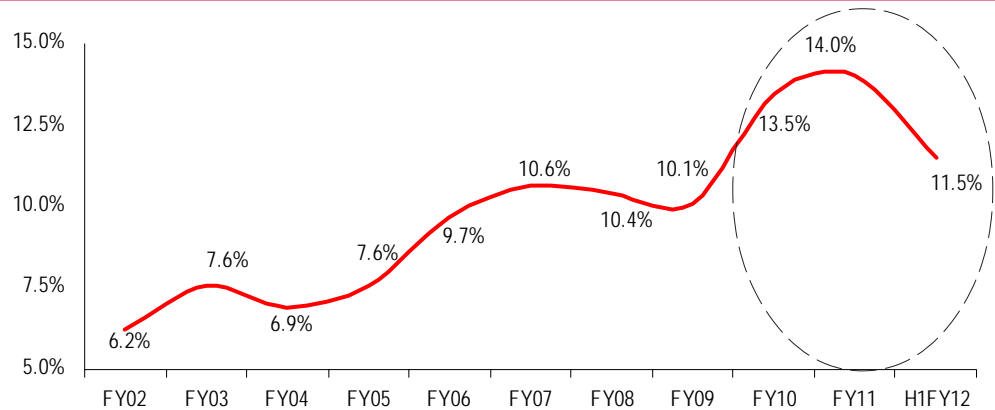
INVESTMENT ARGUMENT

Business visibility improved, profitability scope is limited

In last one year, we have noticed that Unilever Plc, parent of HUL, is focusing more in the Emerging market and India is one of the target markets. As a result, we have been witnessing aggression in the HUL's top management. The higher involvement of top management at the field level, setting up aggressive sales targets and expansion in distribution network are the indicators for business improvement going forward.

Higher management focus would increase the business growth but we believe further control on discretionary spending is limited. HUL has already reduced A&P (% of sales) spending substantially during H1FY12 to 11.5% v/s 14% in FY11; therefore to improve the profitability further scope of control on discretionary spending is limited. We expect 14.1% and 16.6% sales and net earnings CGAR during FY11-14E as compared to 12.4% and 7.1% during FY08-11 respectively.

Exhibit 1 - Further Scope of Reduction in A&P (% of sales) Spending is Limited



Source: PINC Research, Company

Power brands' presence in several categories

HUL has rationally reduced power brands' dependence on one category through frequent launches of these brands in other categories. It not only reduced the brands' dependence on one category but also expanded HUL's brands in one particular category. For example, Dove was known as a skin cleansing brand but today it has strong presence in categories like shampoo, body lotion, deodorant and conditioner. In the same manner Lux, Sunsilk, Liril, Pond's, Pears, Vaseline and Lakme expanded their presence in other categories too.

Through this, HUL improved its competitiveness in each of the categories. HUL has created alternative brands for each of the categories that engage customers with the company; if not with one brand.

Exhibit 2 - Brand Extension

| Brand | Presence |
|--------------|--|
| Dove | Shampoo, Soap, Body Lotion, Deodorant, Conditioner |
| Vaseline | Petroleum Jelly, Lip care, Body Lotion |
| Pears | Soap, Face wash, Hand wash |
| Pond's | Skin Care, Talc, Face wash |
| Liril | Soap, Talc |
| Lux | Soap, Shampoo |
| Sunsilk | Shampoo, Conditioner |
| Rexona | Soap, Deodorant |
| Lakme | Skin Care, Color Cosmetics |

Source: PINC Research, Company

“RIVER” Analysis

Despite the fact that HUL had maintained leadership position in most of the categories, the concern factor is losing volume and value market share. We think companies with higher current in their River (**R**ange, **I**nnovation, **V**alue weightage, **E**ngage and **R**each) will lead the game.

HUL's products available at several price points...

Range – We believe brand's range (coverage of price points and wide variety) should be considered as a key trait. HUL's leadership in soaps, detergent, skin care, shampoo market is owing to strong range of its products. In each of the category HUL has 2-3 brands with each brand having +10 variations; so this provides large option for customers.

Innovation- Innovation is the key for any industry and FMCG industry is not an exception. Although, the innovations what we want to mention here are the consistent improvement in look, packaging, usability and quality.

Innovation is the key to success...

We have observed couple of innovation in soaps industry that consumers adopted well.

- Typical square size of soap has changed to oval and round shapes.
- Purpose of soaps has shifted from typical germs care (like Lifebuoy, Cinthol and Dettol) to skincare (Like Dove, Pears and FairGlow) and fragrance (like Liril, Lux and Breeze).
- Liquid form of soap is again a good innovation but consumer acceptability is still lower as it is not well marketed by the manufacturers. We believe this innovation has good potential as it reduces the waste and improves the consumer ease.

Consumers buying through a concept of value weightage in the monthly budget...

Value weightage – The large part of consumers' buying was depending on 'value for money' concept. However, we have observed slight change in consumer's buying post the success of plastic money and modern trade. Now consumer buys through a mathematical matrix that calculates each item's weight in the monthly expense. Due to the low weightage in the monthly budget consumer shifts towards the better price product. The importance of brand plays a key role in choosing products. HUL through higher focus on branding created wide range of brands in home care and personal care that provides high value proposition for its consumers.

Tries to engage with the company; if not with the brand...

Engage – There was a time when consumers were used to stick with one brand for lifetime and that case was largely with soaps, oral care and hair care categories. Our observation states that consumers brand loyalty has been reducing over period of time and consistent change in brands have been witnessed. Now it is difficult for a consumer to stick with one brand for whole life.

However, in our opinion, variety in the product portfolio can engage consumer to buy through the same company if not the brand. The same consumer can buy low price Lifebuoy at certain age and with the rise in income and change in the life style can move towards expensive soaps like Dove and Liril.

So in our opinion, companies should aggressively look at the change in consumers' profile and should try to give the required product to fulfill the new demand. So the consumer can be engaged with the company; if not with the brand through improvement in features, packing, quality and better schemes.

Reach- It is a proven fact that long term survival of any brand depends on its reach to the customers. Good companies consistently develop their distribution channel and always wait for opportunities to come to beat the competitor. HUL has lost market share in soap category and we believe it is largely on account of better reach of its competitors. Wipro is strong in the Southern India while Godrej consumers (GCPL) in the North India. Strong regional hold of Wipro and GCPL has resulted in ~600bps and ~200bps expansion in value market share in the past 5 years.

Strong regional hold of Wipro and GCPL resulted in ~600bps and ~200bps market share expansion in the past 5 years...

Exhibit 3 - RIVER Analysis on HUL's Categories

| RIVER Analysis | R | I | V | E | R | Total |
|----------------|----|---|----|---|---|-------|
| Soaps | 10 | 8 | 10 | 8 | 8 | 44 |
| Detergent | 9 | 8 | 8 | 8 | 8 | 41 |
| Skin Care | 10 | 9 | 9 | 9 | 9 | 46 |
| Oral Care | 8 | 7 | 8 | 7 | 7 | 37 |
| Hair Care | 9 | 8 | 8 | 8 | 8 | 41 |
| Deodorant | 7 | 7 | 7 | 7 | 7 | 35 |
| Staple Food | 6 | 6 | 6 | 5 | 5 | 28 |
| Beverages | 8 | 8 | 8 | 8 | 7 | 39 |

Source: PINC Research

Note: Points are based on competitive edge and ranges between 0-10 where 10 is for the most competitive

Personal care continue to dominate profitability

We believe personal care category would continue to lead HUL on profitability front. In our opinion, skin care is the largest contributor of personal care business and contributes ~50% of personal care EBITDA. Skin care is the most promising categories in the personal care space which has immense growth potential through the favourable demographic change in consumers.

Although several domestic and MNCs are expanding personal care capacities in India, we believe it would rather help the category growth. Skin care market is still under developed market and competition would increase consumers' consciousness towards the beauty products.

HUL's large product portfolio in each of the categories would make the company more competitive. Strong growth in skin care would adjust the profitability pressure in other categories like shampoo and oral care and would help in maintaining the profitability profile of the personal care segment.

Exhibit 4 - Sales and EBITDA Mix Estimates of Personal Care Category

| Categories | Sales Mix (%) | EBITDA Mix (%) |
|-----------------|---------------|----------------|
| Skin Care | 38% | 50% |
| Shampoo | 26% | 18% |
| Oral Care | 17% | 12% |
| Color Cosmetics | 8% | 10% |
| Deodorant | 4% | 7% |
| Others | 6% | 7% |

Source: PINC Research

Exhibit 5 - HUL's Business Mix

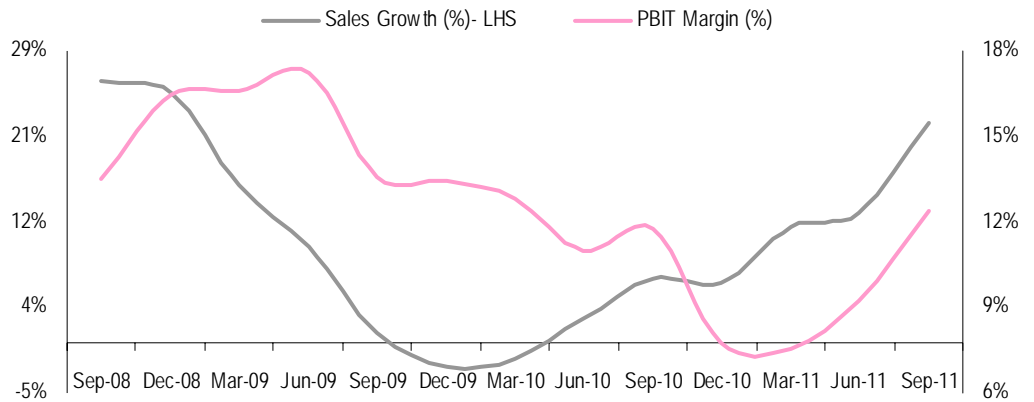
| Segments | Sales Mix | | | Sales CAGR | | PBIT Margin | | | PBIT Mix | | |
|----------------------|-----------|-------|-------|------------|----------|-------------|-------|-------|----------|-------|-------|
| | FY08 | FY11 | FY14E | FY08-11 | FY11-14E | FY08 | FY11 | FY14E | FY08 | FY11 | FY14E |
| Soaps and Detergents | 45.5% | 43.9% | 42.4% | 10.3% | 12.3% | 15.3% | 9.5% | 11.0% | 43.7% | 30.3% | 31.9% |
| Personal Products | 26.2% | 29.4% | 31.0% | 15.4% | 15.7% | 27.8% | 25.0% | 25.0% | 45.8% | 53.3% | 53.0% |
| Beverages | 10.9% | 11.7% | 11.2% | 13.8% | 11.8% | 14.9% | 15.3% | 15.0% | 10.3% | 13.0% | 11.4% |
| Foods | 3.8% | 4.5% | 5.1% | 17.1% | 18.4% | 2.8% | 1.4% | 1.5% | 0.7% | 0.5% | 0.5% |
| Ice Creams | 1.1% | 1.4% | 1.5% | 17.7% | 15.8% | 7.7% | 7.1% | 7.5% | 0.6% | 0.7% | 0.7% |
| Exports | 10.2% | 5.9% | 5.0% | -6.1% | 7.9% | 3.3% | 7.8% | 7.0% | 2.1% | 3.3% | 2.4% |
| Others | 2.2% | 3.3% | 3.8% | 25.8% | 19.8% | -22.2% | -4.5% | 0.0% | -3.1% | -1.1% | 0.0% |

Source: PINC Research, Company

‘Soaps and Detergent’ profitability upside is limited

The performance of ‘Soaps and Detergent’ segment in the past 3 quarters was very encouraging. The segment has not only shown better volume growth but simultaneously improved the profitability profile too. HUL in FY11 reported lowest PBIT margin of 9.5% which we believe was largely due to the down trading in the detergent products. We expect segment profitability would improve from FY11 level however, achieving historical mid teen margin seems difficult due to higher competition from P&G, Rohit Surfactant (Ghari), Godrej Consumers, Wipro, Reckitt Benkiser and ITC which would limit the profitability upside for the segment.

Exhibit 6 - Soaps and Detergent Sales Growth and PBIT margin

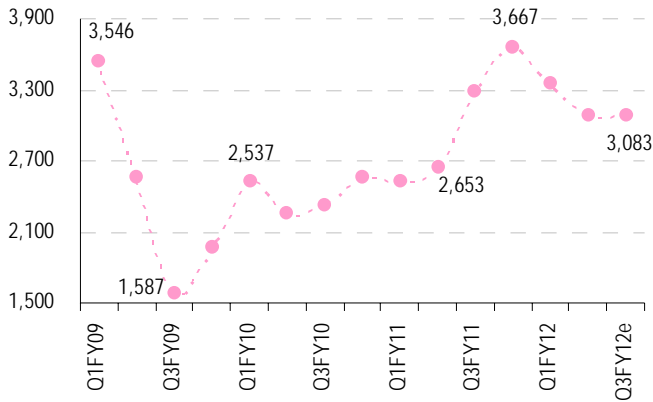


Source: PINC Research, Company

Softening of key commodities

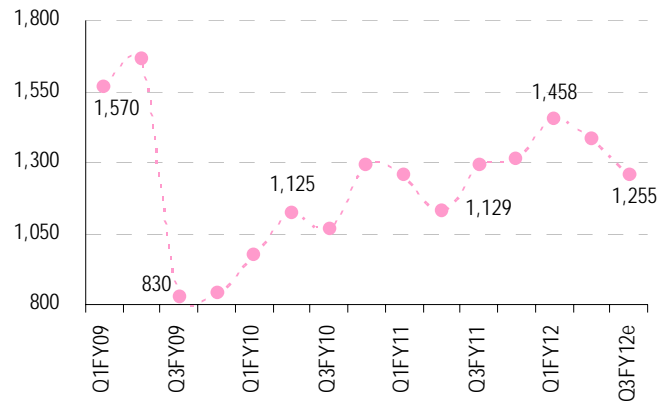
We observed prices of key commodities are softening and supporting our profitability assumption. We expect HUL's raw material cost would grow at a slower pace of ~13% during FY13E and FY14E as compared to >20% growth in FY12E. Packaging cost is also a critical cost component as it accounts ~10% of total expenses. Most of the packaging cost is based on crude related derivatives therefore Crude and HDPE prices have significant dependence. We expect packaging cost to grow by ~10% during FY13E and FY14E as compared to >20% growth in FY12E.

Exhibit 7 - Palm Oil Prices (MYR/mt)



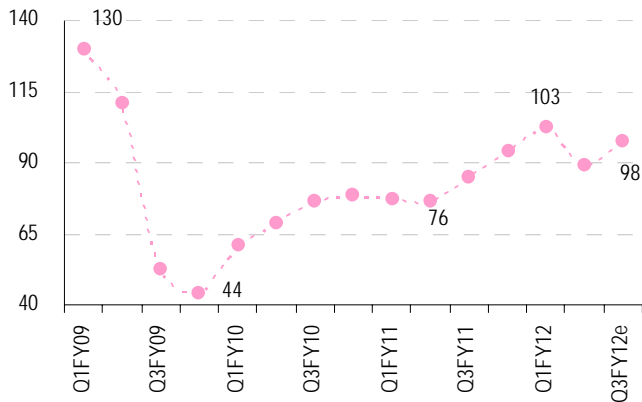
Source: PINC Research, Bloomberg

Exhibit 8 - HDPE Prices (USD/mt)



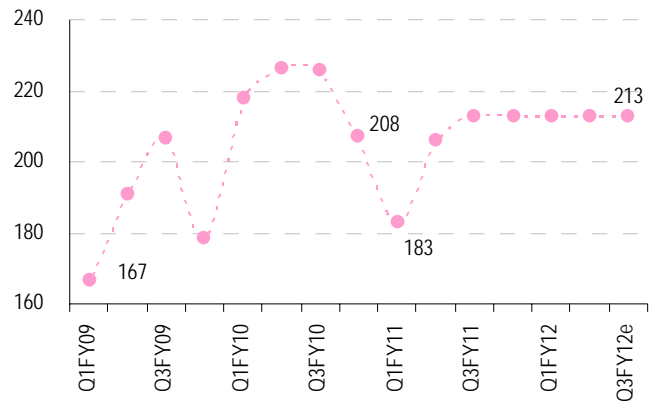
Source: PINC Research, Bloomberg

Exhibit 9 - Crude Oil Prices (USD/Barrel)



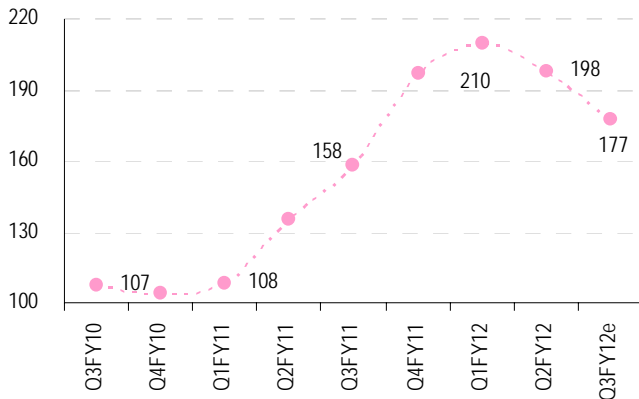
Source: PINC Research, Bloomberg

Exhibit 10 - Tea Prices (Rs/Quintal)



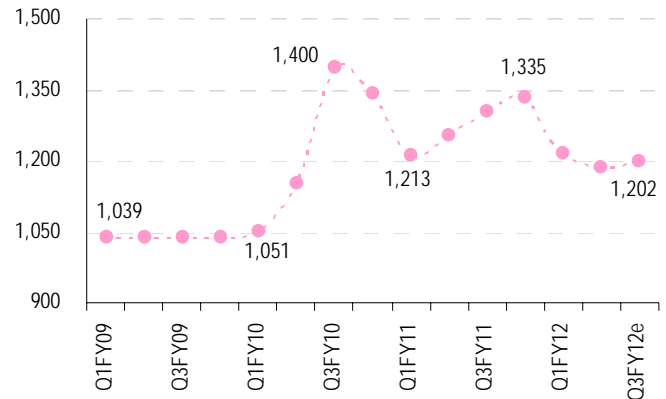
Source: PINC Research, Bloomberg

Exhibit 11 - Coffee Index (USD)



Source: PINC Research, Bloomberg

Exhibit 12 - Wheat Prices Index (Rs/Quintal)



Source: PINC Research, Bloomberg

Re-rating is over

HUL's past 40% stock run up in 300 days was largely on account of re-rating of the stock. We analysed Bloomberg's consensus earnings and found that earning up-gradation was miniscule as compared to the stock run up. In the past 300 days, stock moved up by 40% while consensus earnings increased by only ~4% and ~5% for FY12E and FY13E respectively.

Exhibit 13 - Re-rating of the Stock

| Days | HUL Stock Run Up | Consensus Earning Upgrade | |
|-----------|------------------|---------------------------|-------|
| | | FY12E | FY13E |
| 300 Days | 39.9% | 3.9% | 5.3% |
| 200 Days | 27.9% | 4.0% | 6.7% |
| 150 Days | 17.1% | 4.7% | 6.7% |
| 120 Days | 22.5% | 4.4% | 5.7% |
| 100 Days | 20.6% | 4.2% | 5.6% |
| 90 Days | 9.5% | 4.5% | 5.8% |
| 75 Days | 12.3% | 4.8% | 6.3% |
| 60 Days | 16.5% | 5.2% | 6.7% |
| 50 Days | 14.6% | 5.2% | 6.3% |
| 40 Days | 1.0% | 2.5% | 3.7% |
| 30 Days | -2.4% | 0.7% | 1.4% |
| 20 Days | 0.6% | 0.1% | 0.2% |
| 10 Days | -2.2% | 0.1% | 0.2% |
| 5 Days | -1.8% | 0.0% | 0.0% |
| 1 Day Ago | 0.7% | 0.0% | 0.0% |

Source: PINC Research, Bloomberg

VALUATIONS AND RECOMMENDATION

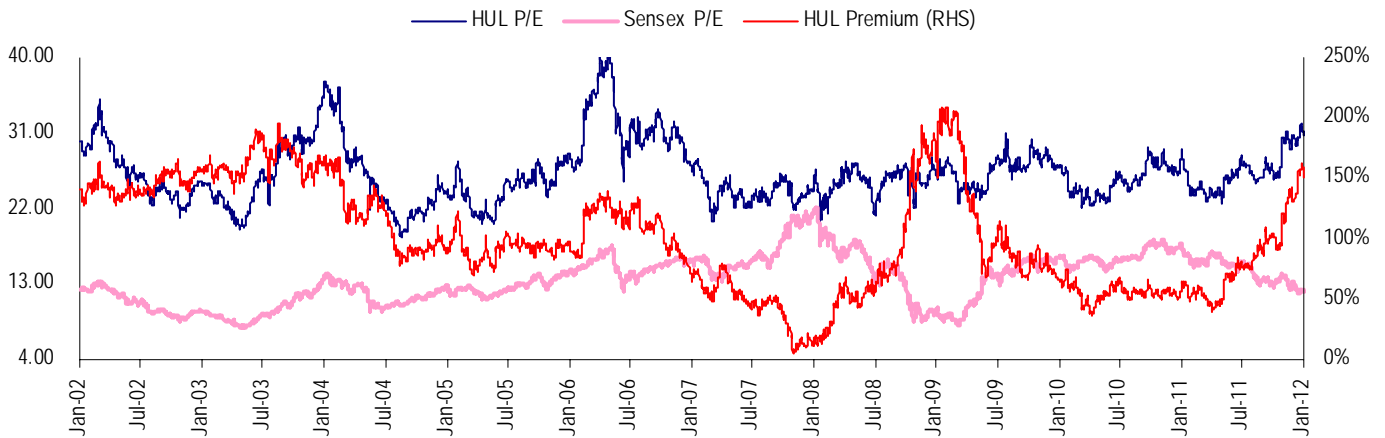
We believe higher management focus; strong growth potential of personal care segment and softening of raw material prices would provide necessary growth momentum in sales and profitability during FY11-14E. We expect HUL to deliver 14.4% and 16.9% CAGR in net sales and adjusted PAT respectively during FY11-14E.

HUL underperformed the BSE Sensex in the past several years and that trajectory changed in the current fiscal. The stock outperformed the BSE Sensex by 47% in the current fiscal (till date) and changed the stock’s return profile.

HUL traded at past 3 year and 5 year median P/E (at 12-month forward earnings) of 26x and 25x respectively. Recent 40% stock run made the valuations expensive, stock currently trades at 30x P/E of 12-month forward earnings.

We believe management’s higher focus vis-à-vis better operational performance in the past 3 quarters has improved the visibility in the business. Therefore, we also value HUL at high multiple of 28x (12-month forward earnings) which is ~10% premium to the FMCG sector valuations and ~8% higher than its past three years median P/E. We arrive at a target price of Rs371 which is 6% down from CMP. Hence, we initiate HUL with a ‘REDUCE’ rating.

Exhibit 14 - HUL Stock Performance



Source: PINC Research, Bloomberg

Soaps and Detergents

Soaps and Detergent is the largest contributor of HUL sales and accounts for ~45% of total sales. HUL holds extensive soaps and detergent portfolio with a mix of premium, economy and popular segments.

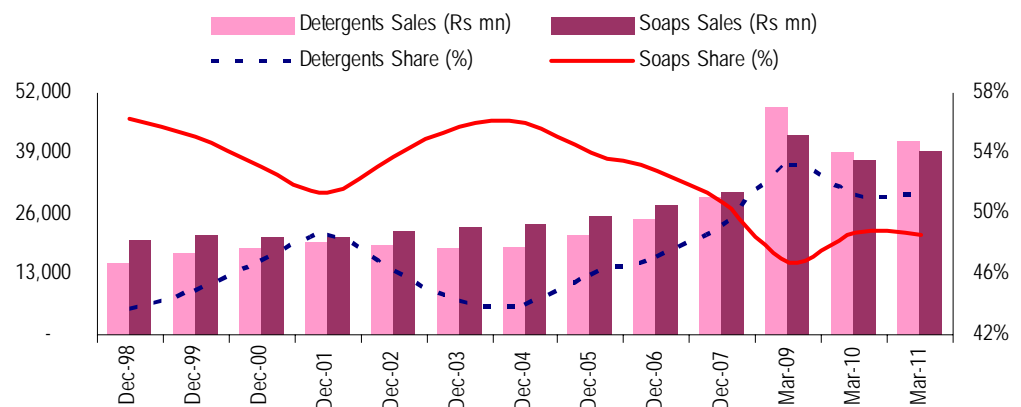
Exhibit 15 - Soaps and Detergent Product Portfolio

| Soaps Portfolio | Class | Detergent Powder Portfolio | Class | Detergent Bar Portfolio | Class |
|-----------------|-----------------|----------------------------|-----------------|-------------------------|-----------------|
| Dove | Premium | Surf Excel Blue | Premium | Surf Excel | Premium |
| Liril | Premium | Surf Excel Quick Wash | Premium | Rin | Economy |
| Pears | Premium | Rin | Economy | Wheel | Popular Segment |
| Lux | Economy | Active Wheel | Popular Segment | | |
| Hamam | Economy | Active Wheel Gold | Popular Segment | | |
| Rexona | Economy | | | | |
| Lifebuoy | Popular Segment | | | | |
| Breeze | Popular Segment | | | | |

Source: PINC Research, Company

Exhibit 16 - Soaps and Detergents Performance

Detergent mix improved consistently and now surpassed the share of soaps in 'Soaps and Detergent' segment...



Source: PINC Research, Company

Despite having lion's market share in the soaps and detergents business, profitability has been reducing consistently. Rise in competition vis-à-vis weakening price power on key products resulted into substantial change in sales and PBIT mix. Segment contribution for sales and PBIT were at 45% and 30% in FY11 as compared to 39% and 52% in FY02.

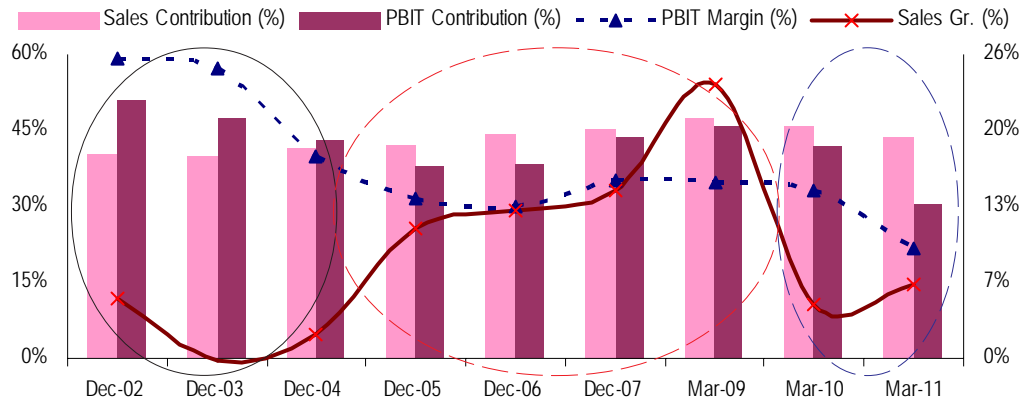
We classified HUL's last 10 years performance into three phases i.e. Phase A; Phase B and Phase C.

Phase A, during 2002-04, was more of slow sales growth and high profitability scenario. During this time competition was relatively low therefore HUL's profitability was at its peak.

Phase B, during 2005-09, was a scenario of high sales growth with a moderate profitability as compared to the Phase A.

Phase C, during 2010-11, was difficult time for the segment. HUL clocked slowest sales growth along with the lowest PBIT margin. High competitive intensity along with inflationary pressure on input prices impacted the performance.

Exhibit 17 - Substantial Decline in Profitability of Soaps & Detergents Segment

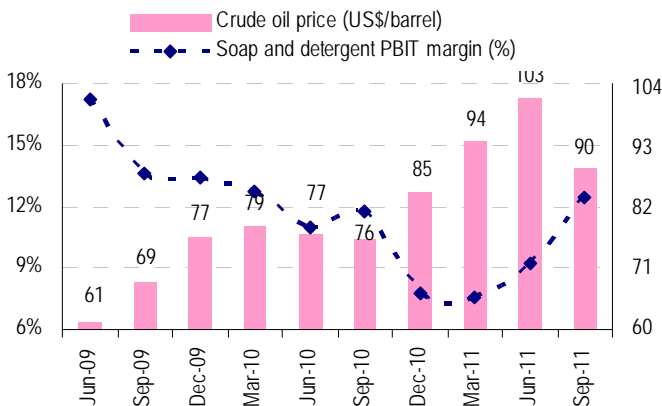


Source: PINC Research, Company

What is profitability outlook for 'Soaps and Detergent' segment

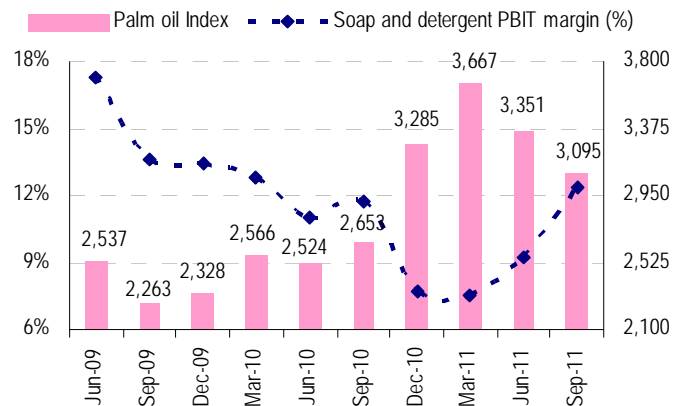
The performance of 'Soaps and Detergent' segment in the past 3 quarters was very encouraging. The segment has not only shown better volume growth but simultaneously improved the profitability profile too. HUL, in FY11, reported lowest PBIT margin of 9.5% which we believe was largely due to the down trading in the detergent products. We expect segment profitability would improve from FY11 level however achieving historical mid teen margin seems difficult due to higher competitive intensity from P&G, Rohit Surfactant (Ghari), Godrej Consumers, Wipro, Reckitt Benkiser and ITC that would limit the profitability upside for the segment.

Exhibit 18 - Impact of Crude Oil Price



Source: PINC Research, Bloomberg

Exhibit 19 - Impact of Palm Oil Price

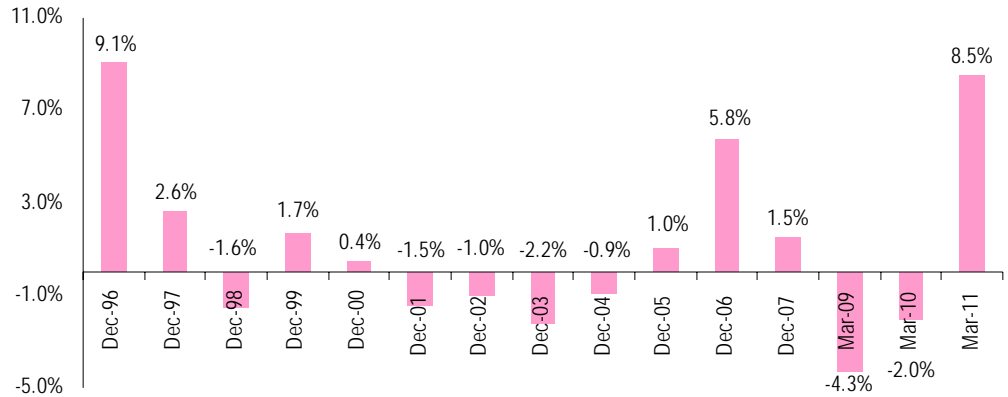


Source: PINC Research, Bloomberg

Soaps - a value driven business

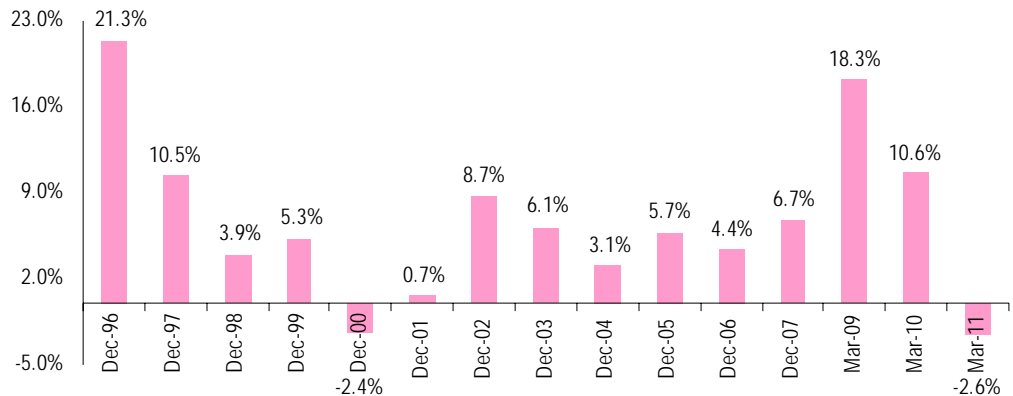
We analysed HUL's long history and found that the volume growth was never a driver for soaps business. Consistent price hike coupled with better revenue mix resulted in better realisation growth. Realisation growth shared >90% of the average soap sales growth in the past 10 years.

Exhibit 20 - Soaps Volume Growth (%)



Source: PINC Research, Company

Exhibit 21 - Soaps Realisation Growth (%)

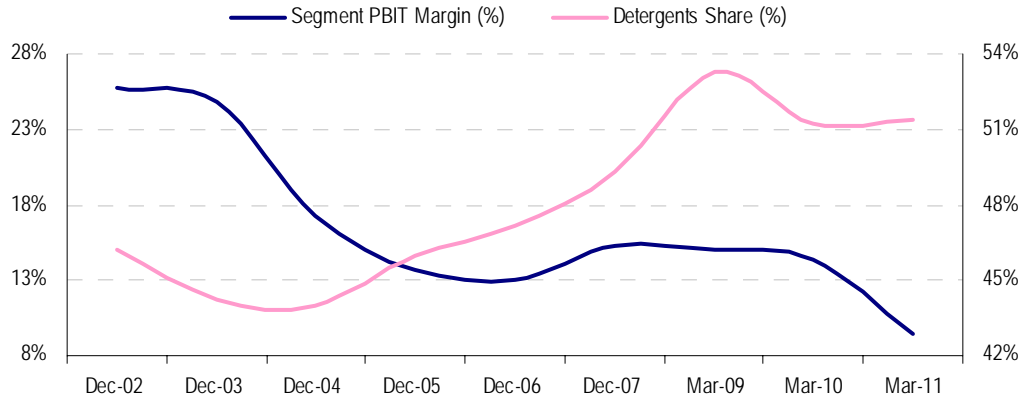


Source: PINC Research, Company

Soaps provides better operational margin than detergents

Our understanding is that soaps provides better operational margin than detergents. We observed that the contribution from the soaps has started falling since FY04 and at the same time PBIT margin of 'soaps and detergents' segment has also reduced. In the past three years, detergents share surpassed the soaps' contribution and resulted into substantial decline in 'soaps and detergent' PBIT margin.

Exhibit 22 - Profitability Decline on Change in Revenue mix

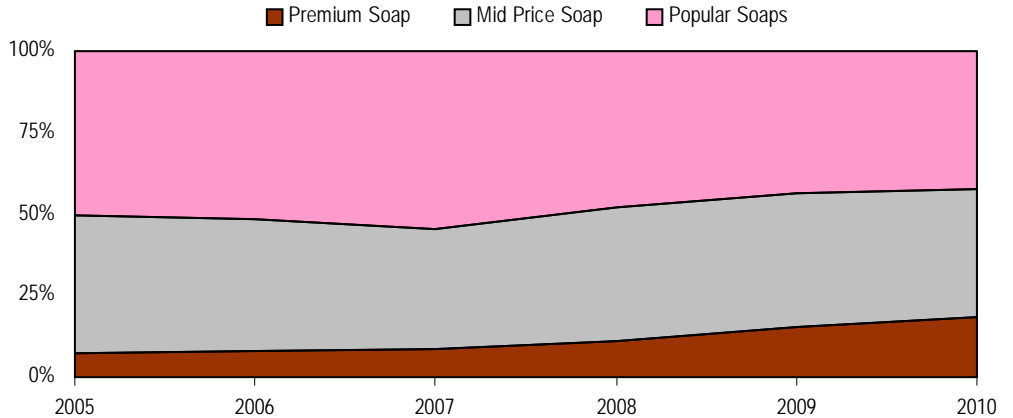


Source: PINC Research, Company

Improving sales mix for premium soaps

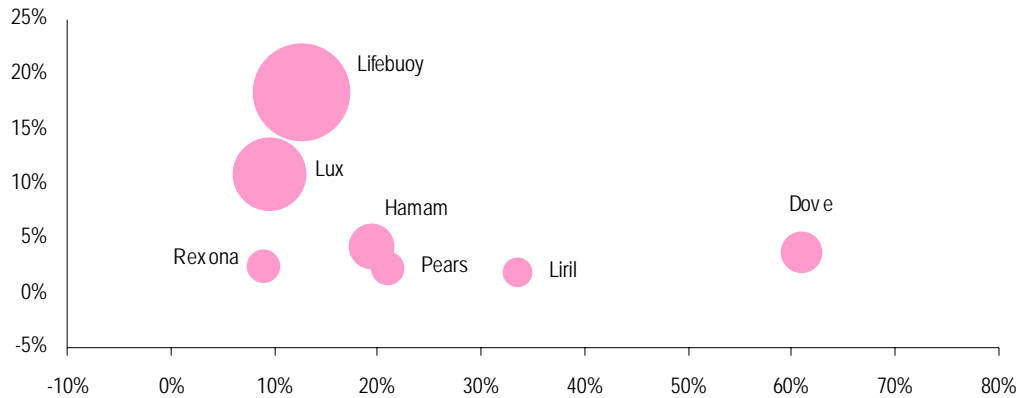
We believe HUL's premium category (Dove, Liril and Pears) soaps consists <20% of the total soaps sales but the segment is growing faster than the Economy (Lux, Hamam and Rexona) and popular categories (Lifebuoy and Breeze). HUL's higher marketing spend, consistent new launches vis-à-vis improvement in consumer demand for premium soaps were the key reasons for robust sales growth of premium soaps.

Exhibit 23 - Soap Mix (%)



Source: PINC Research, Company

Exhibit 24 - Key soap brands' sales (Rs mn), sales growth (%) & market share (%)



Source: PINC Research, Company, Industry

Note: X Axis-Estimated sales CAGR (%), Y Axis-Estimated market share in FY11 (%), Size of bubble- Estimated sales (Rs mn) in FY11

HUL's positioning in the soaps market

HUL's dominance in the soaps market is due to its long existence and large soap portfolio with a presence in all price groups. HUL is a market leader with ~45% market share but its market share has substantially reduced in the past 5 years. Godrej consumers, Wipro and Reckitt Benckiser are giving tough competition. These three players combined holds ~30% market share.

Consumers' shift towards the expensive soaps is driving the Soap industry...

Soaps industry has been facing volume pressure and in the last 5 years the volumes grew merely by ~2%. We believe higher penetration level (+90%); better alternates for face wash and limited growth in consumption (like through twice bath) were the key reasons for slower volume growth.

The soap market grew by ~10% during past 5 years in which value growth was ~8%. We believe value growth has happened on account of consistent price hike and consumers' shift towards the expensive soaps. While we believe the later part is more prominent in the overall value growth this will be the key for upcoming growth in the soap market.

Exhibit 25 - Soaps Peer Comparison

| Key players | Brands | Sales (Rs mn) FY11/CY10 | Sales CAGR (last 5 years) | Volume CAGR (last 5 years) | Value Mkt. Share | Mkt. Share Ch. (last 5 years) |
|-------------------|---|-------------------------|---------------------------|----------------------------|------------------|-------------------------------|
| HUL | Lux, Lifebuoy, Liril, Hamam, Breeze, Pears, Dove, Rexona | 39 | 9% | 2% | 45% | -940bps |
| Wipro | Santoor, Shikakai and Chandrika | 8 | 21% | 13% | 10% | 281bps |
| Reckitt Benckiser | Dettol | 8 | 26% | 22% | 10% | 405bps |
| Godrej Consumers | Cinthol, Godrej No 1, FairGlow | 8 | 15% | 8% | 9% | 53bps |
| Nirma | Nirma, Nima | 4 | -1% | -8% | 5% | -489bps |
| Henkel India | Margo | 1 | 1% | -1% | 1% | -65bps |
| Others | Johnson's baby soap, Himalaya, Neem, Park Avenue, Mysore Sandalwood, Dyna, Venus, Jeeva, etc. | 17 | 23% | | 30% | |
| Total | | 87 | 13% | | | |

Source: PINC Research, Company, Industry

Exhibit 26 - Soap Peer Price Comparison

| Products | Unit | MRP/unit | Category | Company |
|--------------|------|----------|----------|---------------------|
| Dove | gm | 0.51 | Premium | HUL |
| Yardely | gm | 0.45 | Premium | Wipro |
| Denim | gm | 0.44 | Premium | United Distribution |
| Pears | gm | 0.38 | Premium | HUL |
| Fiama | gm | 0.33 | Premium | ITC |
| Liril | gm | 0.32 | Premium | HUL |
| Savlon | gm | 0.32 | Premium | J&J |
| Dettol | gm | 0.26 | Economy | RB |
| Medimix | gm | 0.24 | Economy | Cholayil Pvt Ltd |
| Chandrika | gm | 0.23 | Economy | Wipro |
| Cinthol | gm | 0.23 | Economy | Godrej |
| Camay | gm | 0.22 | Economy | P&G |
| Hamam | gm | 0.21 | Economy | HUL |
| Lux | gm | 0.21 | Economy | HUL |
| Rexona | gm | 0.21 | Economy | HUL |
| Santoor | gm | 0.19 | Economy | Wipro |
| Godrej No. 1 | gm | 0.18 | Economy | Godrej |
| Lifebuoy | gm | 0.14 | Popular | HUL |
| Jo | gm | 0.14 | Popular | VVF Ltd |
| Breeze | gm | 0.11 | Popular | HUL |

Limited competition through branded soaps...

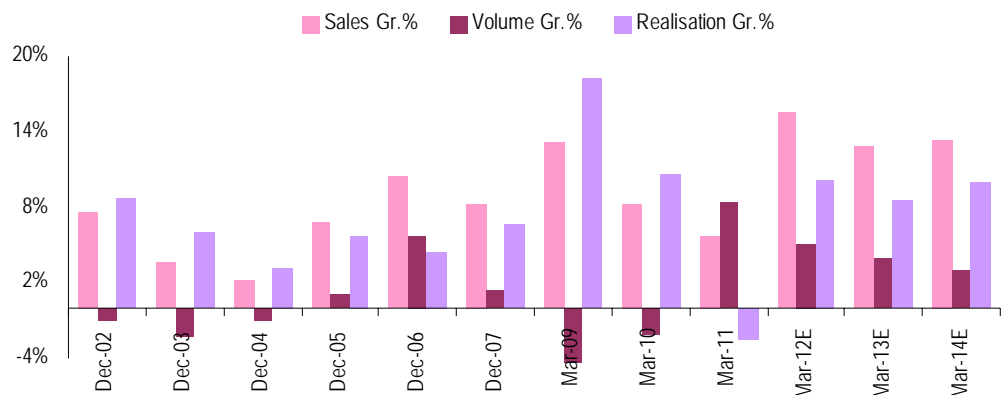
Source: PINC Research, Retail Market Dec'2011

What do we expect?

We expect premium soap segment (Dove, Liril and Pears) will continue to deliver higher growth compared to the overall soap segment growth. Dove has emerged as a separate category for skin conscious consumers. We expect Dove will continue to deliver higher double digit growth. Liril is reenergised with recent new variants and should continue to grow fast. Pears has changed its 'winters only' image to 'pure for skin' image and getting demand for whole year.

We anticipate favourable revenue mix (higher growth in the premium soap segment) would support in maintaining healthy growth in soap sales. However, aggressive competition from Wipro, Godrej Consumers, Reckitt Benckiser and ITC would restrict the growth potential. We expect HUL to clock ~13.7% CAGR in Soap sales during FY11-14E.

Exhibit 27 - Soaps Growth Breakup

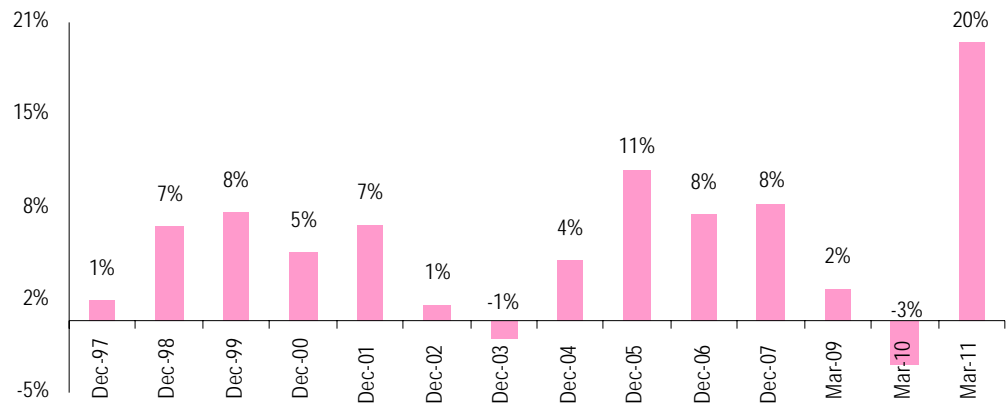


Source: PINC Research, Company * Growth is adjusted for the change in financial year

Detergents - persistence of high competitiveness

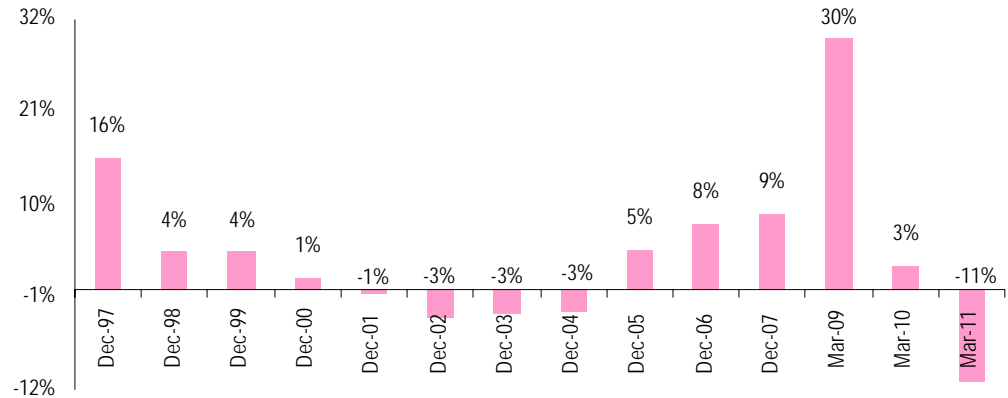
HUL operates its detergent business through Surf Excel, Rin and Wheel brand which caters to premium, economy and popular segments. It is largely volume driven business and popular segment (Wheel brand) covers half of the total detergent business.

Exhibit 28 - Detergent Volume Growth (%)



Source: PINC Research, Company

Exhibit 29 - Detergent Realisation Growth (%)



Source: PINC Research, Company

Detergent is like a commodity business

Detergent business is more of a commodity business, regional brands and household prepared detergent soaps also hold significant share in the detergent market. Detergent is one of those products which come into necessity product and very much available in households though the consumption level can be widely different among the households. We believe overall detergent volume market is growing at a very slow pace which is why the industry is very price sensitive. The growth for the branded detergent player would come through higher consumption and shift from unbranded product to branded products.

HUL's positioning in the detergent market

We have observed variability in the detergent business on account of rise in competitive intensity. Price war among the rivals has wiped off the price premium of this business. We believe HUL sacrificed profitability and managed market share at ~35%.

Nirma lost market share by ~750bps in past 5 years due to lack of focus in the business. HUL could not avail this opportunity while players like Rohit Surfactant (brand Ghari) and P&G expanded market share by ~650bps and ~150bps respectively during the past 5 years. Nirma basically caters to low price detergent segment that matches with Ghari's price point. Therefore, Ghari's aggressive efforts resulted into 25% sales CAGR during FY06-11.

Exhibit 30 - Detergent Peer Comparison

| Key players | Brands | Sales (Rs bn) FY11/CY10 | Sales CAGR% (last 5 years) | Volume CAGR% (last 5 years) | Value Mkt Share % | Value Mkt Share Change (last 5 years) |
|------------------|-------------------------|-------------------------|----------------------------|-----------------------------|-------------------|---------------------------------------|
| HUL | Surf Excel, Rin, Wheel | 42 | 14% | 7% | 37% | -330bps |
| Rohit Surfactant | Ghari | 21 | 25% | 16% | 19% | 570bps |
| P&G | Tide, Ariel | 12 | 18% | 17% | 11% | 79bps |
| Nirma | Nirma | 12 | 2% | -6% | 11% | -958bps |
| Henkel | Henko, Mr. White, Check | 2 | 9% | -4% | 2% | -71bps |
| Others | | 23 | 26% | | | |
| Total | | 112 | 16% | | | |

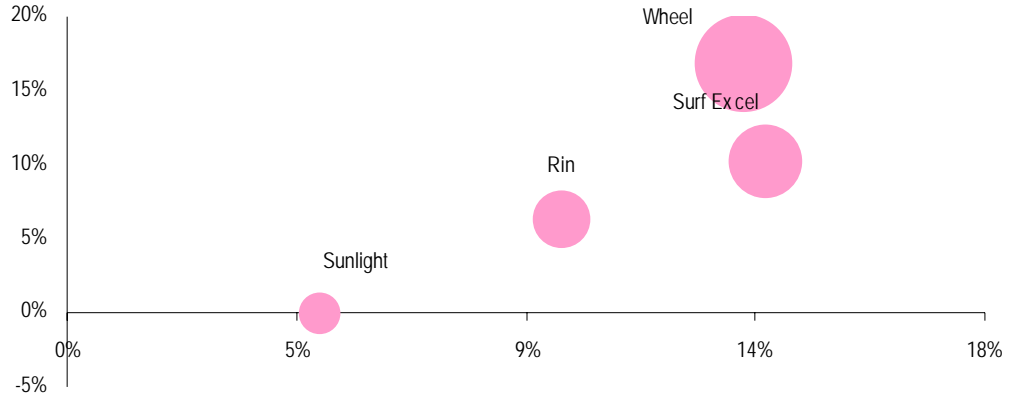
Source: PINC Research, Company, Industry

Exhibit 31 - Detergent Powder Peer Price Comparison

| Products | Unit | MRP/unit | Category | Company |
|----------------------------|------|----------|----------|------------------|
| Henko Matic | gm | 0.20 | Premium | Henkel India |
| Ariel Oxy Blue Ultra Matic | gm | 0.19 | Premium | P&G |
| Surf Excel Quick wash | gm | 0.16 | Premium | HUL |
| Ariel Oxy Blue | gm | 0.16 | Premium | P&G |
| Henko Champion | gm | 0.16 | Premium | Henkel India |
| Henko Stain Champion | gm | 0.13 | Economy | Henkel India |
| Surf Excel Blue | gm | 0.13 | Economy | HUL |
| Tide Plus | gm | 0.12 | Economy | P&G |
| Henko | gm | 0.12 | Economy | Henkel India |
| Expert | gm | 0.12 | Economy | Spencer's |
| Techno Bright | gm | 0.11 | Economy | Jyothy Labs |
| Tide | gm | 0.08 | Economy | P&G |
| Rin Jasmine | gm | 0.07 | Economy | HUL |
| Rin | gm | 0.07 | Economy | HUL |
| Mr. White | gm | 0.06 | Economy | Henkel India |
| Ghari | gm | 0.06 | Popular | Rohit Surfactant |
| Active Wheel Gold | gm | 0.04 | Popular | HUL |
| Ghari | gm | 0.04 | Popular | Rohit Surfactant |
| Active Wheel | gm | 0.03 | Popular | HUL |
| Check | gm | 0.02 | Popular | Henkel India |

Source: PINC Research, Retail Market Dec'2011

Exhibit 32 - Key detergent brands' sales (Rs mn), sales growth (%) & market share (%)

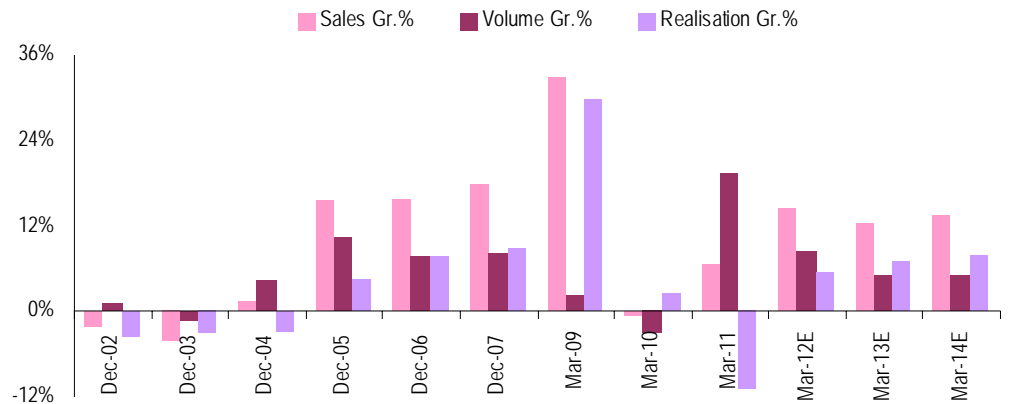


Source: PINC Research, Company, Industry
 Note: X Axis-Sales CAGR (%) during FY08-11e, Y Axis-Market share in FY11e (%), Size of bubble- Sales (Rs mn) in FY11e

What do we expect?

We believe popular segment played a key role for the strong volume growth in FY11 and H1FY12. As we already stated that the volume growth for the branded products would come through higher detergent consumption and shift from unbranded product to branded products. The consumption shift is very gradual process and we don't expect any sudden change in that proposition. A shift from unbranded products to branded products is also not low hanging fruit as there is a wide price difference between these two. Therefore, we believe branded detergent market would remain competitive and price sensitivity would be higher for the category. We have already witnessed price war between HUL and P&G therefore we are not very optimistic for the segment. We expect HUL to clock 13.3% CAGR in detergent sales during FY11-14E.

Exhibit 33 - Soaps Growth Breakup



Source: PINC Research, Company * Growth is adjusted for the change in financial year

Change in the mix

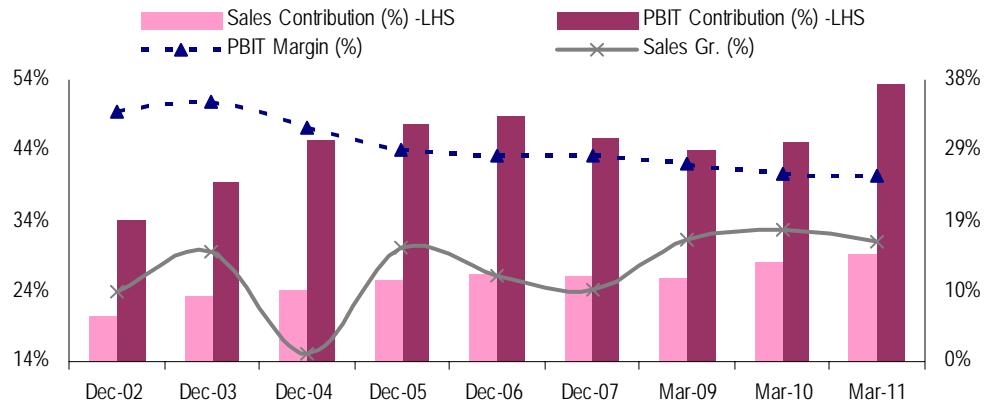
| | Dec-02 | Mar-11 |
|------------------------------|--------|--------|
| Soaps & Detergent | | |
| % of Sales | 40% | 44% |
| % of PBIT | 51% | 30% |
| Personal Care | | |
| % of Sales | 21% | 29% |
| % of PBIT | 34% | 53% |

Source: PINC Research, Company

Personal Care- profitability centre

HUL holds large product portfolio under personal care segment and covers skin care, oral care, hair care and deodorant categories. Personal care is the key profitability centre of HUL and contributes ~29% of sales and ~53% of PBIT. The profitability improvement in personal care has set off the lackluster performance of 'soap and detergent' segment in the past 10 years.

Exhibit 34 - Personal Care - Profitability Centre



Source: PINC Research, Company

Our understanding is that skin care is the largest contributor to the personal care segment with >35% contribution followed by shampoo and toothpaste.

Exhibit 35 - Personal Care Portfolio

| Skin Care | Class | Shampoo | Class | Oral Care | Class |
|------------------|--------------|----------------|--------------|------------------|--------------|
| Pond's | Premium | Dove | Premium | Pepsodent | Premium |
| Lakme | Premium | Clear | Premium | Close-up | Economy |
| Pears | Premium | Sunsilk | Economy | | |
| Fair & Lovely | Economy | Lux | Economy | | |
| Vaseline | Popular | Clinic Plus | Popular | | |

Source: PINC Research, Company

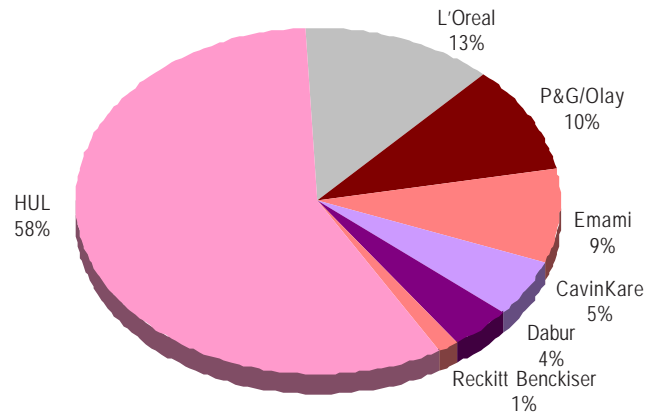
Skin care – money maker

We believe skin care is the largest contributor in sales and EBITDA among personal care segment with ~38% and ~50% share respectively. HUL is the market leader with >50% market share through brands like Pond’s, Pears, Lakme, Fair & Lovely and Vaseline. Fair & Lovely is the key brand for HUL for skin care and is equally recognised in the rural and urban market.

HUL’s positioning in skin care

Skin care is >Rs36bn market with fairness cream forming a dominant part. In India, skin care market is still resembled by the fairness cream market. HUL with an extensive product portfolio has the largest market share. This is the fastest and most profitable category in the personal care segment which is why many FMCG players entered in this category in past couple of years.

Exhibit 36 - Skin Care Share (%)



Source: PINC Research, Company

Fairness cream is the largest contributor in the skin care market in which HUL dominates with >65% market share. HUL has strong fairness cream portfolio under Pond’s, Lakme, Dove and Fair & Lovely brands.

Exhibit 37 - Fairness Cream Peer Comparison

| Fairness Cream (Day cream) | Unit | Qty | MRP | MRP/unit | Company |
|--|------|-----|-----|----------|-------------------|
| Olay Total Effects (Day cream) | gm | 20 | 349 | 17.45 | L'Oreal |
| Neutrogena Fairness Cream (SPF 20) | gm | 50 | 299 | 5.98 | Johnson & Johnson |
| Neutrogena Fairness Lotion | ml | 50 | 250 | 5.00 | Johnson & Johnson |
| Pond's Gold Radiance (Day Cream) | ml | 50 | 799 | 15.98 | HUL |
| Pond's Daily Whitening Cream (Green Flavour) | gm | 50 | 249 | 4.98 | HUL |
| Lakme Perfect Radiance (Fairness Cream) | gm | 50 | 175 | 3.50 | HUL |
| Pond's Lightning Cream | gm | 50 | 150 | 3.00 | HUL |
| Fair & Lovely Forever Glow | gm | 50 | 99 | 1.98 | HUL |
| Fair & Lovely Ayurvedic Balance Cream | gm | 50 | 76 | 1.52 | HUL |
| Fair & Lovely Winter Fairness Cream | gm | 50 | 76 | 1.52 | HUL |
| Fair & Lovely Multi Vitamin Cream | gm | 80 | 114 | 1.43 | HUL |
| Nivea Cream | ml | 60 | 70 | 1.17 | Beiersdorf AG |
| Nivea Soft Cream | ml | 200 | 210 | 1.05 | Beiersdorf AG |
| Nivea Cream | ml | 200 | 160 | 0.80 | Beiersdorf AG |

Source: PINC Research, Retail Market Dec'2011

Exhibit 38 - Body Lotion Peer Comparison

| Brands | Unit | MRP/unit | Category | Company |
|-----------------------|------|----------|----------|---------------------|
| Lakme | ml | 1.10 | Premium | HUL |
| Nivea Lotion | ml | 0.66 | Premium | Beiersdorf AG |
| Garnier | ml | 0.62 | Premium | L'Oreal |
| Dove | ml | 0.60 | Premium | HUL |
| Vaseline | ml | 0.55 | Economy | HUL |
| Himalaya | ml | 0.55 | Economy | Himalaya Healthcare |
| Parachute Advance | ml | 0.49 | Economy | Marico |
| Pond's Triple Vitamin | ml | 0.40 | Economy | HUL |

Source: PINC Research, Retail Market Dec'2011

Challenging Environment

HUL is facing a strong competition from L'Oreal, Johnson & Johnson, P&G and Beiersdorf AG (Nivea) in other skin care categories like Cleansers, Anti Aging, Sun Protection and Moisturiser. These are promising categories and outpacing the overall skin care growth.

P&G and L'Oreal intend to expand capacities in India and have expressed intention to tap opportunities in the skin care market. P&G and L'Oreal plan to invest ~Rs4bn and ~Rs5bn in the next couple of years. Both companies expect their skin care business growth in tune of >20% in medium term. We mention below the positioning of HUL's products in other skin care categories.

Exhibit 39 - Cleansers Peer Comparison

| Cleansers/Face wash/Scrub/cleanser | Unit | Qty | MRP | MRP/unit | Company |
|--------------------------------------|------|-----|-----|----------|-------------------|
| Olay Cleansing | gm | 50 | 99 | 1.98 | L'Oreal |
| Olay Natural White Foaming Cleansing | gm | 50 | 99 | 1.98 | L'Oreal |
| Neutrogena Deep Clean Scrub | gm | 100 | 240 | 2.40 | Johnson & Johnson |
| Neutrogena Scrub | ml | 125 | 225 | 1.80 | Johnson & Johnson |
| Neutrogena Fairness Cleanser | gm | 100 | 180 | 1.80 | Johnson & Johnson |
| Neutrogena Deep Clean Cleaner | ml | 200 | 350 | 1.75 | Johnson & Johnson |
| Neutrogena Foaming Cleanser | gm | 100 | 170 | 1.70 | Johnson & Johnson |
| Pond's White Beauty Facial Foam | gm | 100 | 105 | 1.05 | HUL |
| Lakme Deep Pour Cleanser | ml | 120 | 99 | 0.83 | HUL |
| Pond's Daily Face Wash | gm | 100 | 65 | 0.65 | HUL |

Source: PINC Research, Retail Market Dec'2011

Exhibit 40 - Moisturiser Peer Comparison

| Moisturiser | Unit | Qty | MRP | MRP/unit | Company |
|---|------|-----|-----|----------|-------------------|
| Olay Moisturising Cream | gm | 100 | 399 | 3.99 | L'Oreal |
| Garnier Daily Moisturiser | gm | 40 | 140 | 3.50 | L'Oreal |
| Garnier Essential Care Daily Moisturiser Cream | gm | 40 | 115 | 2.88 | L'Oreal |
| Olay Moisturiser Lotion | ml | 150 | 399 | 2.66 | L'Oreal |
| Neutrogena Hand Cream | gm | 56 | 240 | 4.29 | Johnson & Johnson |
| Neutrogena Ultra Shield Body Moisturiser (SPF 30) | gm | 141 | 600 | 4.26 | Johnson & Johnson |
| Neutrogena Moisturiser | ml | 115 | 299 | 2.60 | Johnson & Johnson |
| Neutrogena Body Emulsion Daily Relief Lotion | ml | 155 | 250 | 1.61 | Johnson & Johnson |
| Neutrogena Body Moisturiser Dry Skin | ml | 250 | 300 | 1.20 | Johnson & Johnson |
| Lakme Perfect Radiance Lotion | ml | 30 | 225 | 7.50 | HUL |
| Lakme Deep Pour Moisturiser | ml | 55 | 75 | 1.36 | HUL |

Source: PINC Research, Retail Market Dec'2011

Exhibit 41 - Anti Aging Cream Peer Comparison

| Anti Aging | Unit | Qty | MRP | MRP/unit | Company |
|---|------|-----|-----|----------|-------------------|
| Olay Anti Aging Serum | ml | 50 | 700 | 14.00 | L'Oreal |
| Garnier Anti Dark Circle (Roll on) | ml | 15 | 199 | 13.27 | L'Oreal |
| Garnier Age Lift (Roll on) | ml | 50 | 399 | 7.98 | L'Oreal |
| Garnier Wrinkle Lift Anti Aging | gm | 40 | 235 | 5.88 | L'Oreal |
| Neutrogena Eye | ml | 14 | 549 | 39.21 | Johnson & Johnson |
| Neutrogena Rapid Wrinkle Repair | ml | 29 | 799 | 27.55 | Johnson & Johnson |
| Pond's Age Miracle Serum | ml | 30 | 695 | 23.17 | HUL |
| Pond's Flawless Under Age | ml | 15 | 249 | 16.60 | HUL |
| Pond's Age Miracle Anti Aging Moisturiser | ml | 30 | 215 | 7.17 | HUL |
| Pond's Age Miracle (Day Cream) | gm | 50 | 349 | 6.98 | HUL |
| Fair & Lovely Anti Marks | gm | 50 | 90 | 1.80 | HUL |
| Nivea Sparkling Glow Age Control | ml | 50 | 329 | 6.58 | Beiersdorf AG |

Source: PINC Research, Retail Market Dec'2011

Exhibit 42 - Sun Protection Solution Peer Comparison

| Sun Protection | Unit | Qty | MRP | MRP/unit | Company |
|---------------------------------------|------|-----|-----|----------|---------|
| Olay UV Blocker | ml | 50 | 299 | 5.98 | L'Oreal |
| Garnier Sun Control Daily Moisturiser | ml | 50 | 130 | 2.60 | L'Oreal |
| Pond's UV Cream | ml | 50 | 299 | 5.98 | HUL |
| Lakme Sun Expert Gel | gm | 50 | 145 | 2.90 | HUL |
| Lakme Sun Expert Skin Lightning Mask | gm | 50 | 150 | 3.00 | HUL |

Source: PINC Research, Retail Market Dec'2011

What do we expect?

We believe skin care market is still dominated by the fairness cream and most of other categories are at the nascent stage. We expect skin care market has immense potential to develop owing to the change in the consumer's life style, rise in disposable income and higher consciousness towards the beauty products. Besides, men's skin care market has grown at double pace compared to the women's skin care market. Although it forms only ~10% of the overall skin care market share but growth opportunity is very promising.

HUL has developed four strong brands (Pond's, Lakme, Dove and Fair & Lovely) in skin care which would help the company to compete well. Our take is that skin care industry is still evolving and each player will get opportunity to expand. The segment is very profitable and dominated by the MNC players which typically work on high profitable model. We expect HUL to maintain its high growth momentum with strong profitability.

Shampoo – “Dove” flies

HUL has large product portfolio for its shampoo business with Dove, Clear, Sunsilk, Lux and Clinic Plus brands. Shampoo is second largest category in HUL's personal care business and we expect that it contributes ~25% of the segment.

HUL's positioning in Shampoo category

HUL enjoys leadership position with ~45% market share followed by P&G, CavinKare and Dabur. The price war between HUL and P&G has changed the dynamics of shampoo business that resulted into low profitability of this business.

Exhibit 43 - Shampoo Peer Comparison

| Key players | Brands | Sales (Rs bn) FY11/CY10 | Sales CAGR (last 5 years) | Value Mkt Share |
|--------------|--|-------------------------|---------------------------|-----------------|
| HUL | Dove, Clear, Sunsilk, Lux, Clinic Plus | 15 | 13% | 45% |
| P&G | Pantene, Head & Shoulders, Rejoice | 7 | 16% | 21% |
| CavinKare | Chik, Meera | 4 | na | 11% |
| Dabur | Vatika | 2 | 23% | 4% |
| Others | | 6 | 18% | |
| Total | | 34 | 14% | |

Source: PINC Research, Company, Industry

Clinic Plus is the largest selling shampoo...

Exhibit 44 - Shampoo Peer Price Comparison

| Shampoo | Unit | MRP/unit | Category | Company |
|-------------------------|------|----------|----------|---------------------|
| Vatika Anti Dandruff | ml | 0.60 | Premium | Dabur India |
| Garnier Fortifying | ml | 0.59 | Premium | L'Oreal |
| Garnier Damaged Care | ml | 0.59 | Premium | L'Oreal |
| Fiama Di Wills | ml | 0.58 | Premium | ITC |
| Head & Shoulder | ml | 0.56 | Economy | P&G |
| Dove | ml | 0.56 | Economy | HUL |
| Clear (Anti Dandruff) | ml | 0.56 | Economy | HUL |
| Clear Menthol | ml | 0.56 | Economy | HUL |
| L'Oreal Total Repair | ml | 0.55 | Economy | L'Oreal |
| L'Oreal Nutri Gloss | ml | 0.55 | Economy | L'Oreal |
| Pantene | ml | 0.52 | Economy | P&G |
| L'Oreal Smooth Intense | ml | 0.50 | Economy | L'Oreal |
| Himalaya | ml | 0.50 | Economy | Himalaya Healthcare |
| L'Oreal Color Protect | ml | 0.50 | Economy | L'Oreal |
| Vatika Sun Protect | ml | 0.50 | Economy | Dabur India |
| Sunsilk Hair Fall | ml | 0.46 | Popular | HUL |
| Vivel | ml | 0.45 | Popular | ITC |
| Clinic Plus | ml | 0.41 | Popular | HUL |
| Nyle | ml | 0.35 | Popular | CavinKare |
| Vatika Smooth and Silky | ml | 0.33 | Popular | Dabur India |

Source: PINC Research, Retail Market Dec'2011

What do we expect?

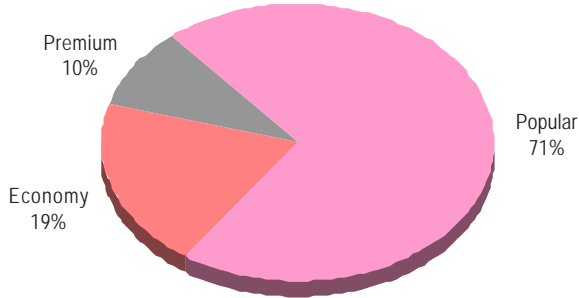
We believe HUL's shampoo business is still dominated by Clinic Plus which caters to popular segment. Clinic Plus brand is very well established in both rural and urban markets. Recent sharp price cut on Clinic Plus franchise has impacted several other shampoo players which are largely into rural market. Dabur was among the one who faced strong heat from such an action.

However, HUL's shampoo business would be supported by strong positioning of Dove franchise. Dove, since its launch in hair care range in 2007, has created a new category in the shampoo space. We believe higher marketing spend and strong consumer acceptance would maintain high growth rate for Dove in the coming years. We expect HUL would show ~15% CAGR in shampoo business during FY11-14E.

Oral care– scope of price growth

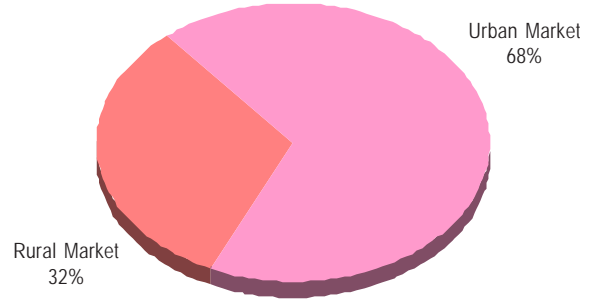
In the oral care market, HUL has a presence only in the toothpaste market. Toothpaste is also key category for HUL’s personal care segment and we believe it contributes ~15% of the segment. HUL holds Pepsodent and Closeup brands that cater to expensive and economy segment in the toothpaste market respectively.

Exhibit 45 - Toothpaste Segment Breakup



Source: PINC Research, Company, Industry

Exhibit 46 - Toothpaste Market Mix



Source: PINC Research, Company, Industry

HUL’s positioning in Oral care

Oral care market is dominated by top 3 players i.e. Colgate Palmolive India (Colgate), HUL and Dabur with combined contribution of >80% of the total oral care market. HUL is the number 2 player with >25% market share in the toothpaste market which is fairly dominated by Colgate Palmolive India (Colgate) with >50% market share.

Exhibit 47 - Toothpaste Peer Comparison

| Key players | Brands | Sales (Rs bn) FY11/CY10 | Sales CAGR% (last 5 years) | Value Mkt Share % |
|---------------|---------------------------|-------------------------|----------------------------|-------------------|
| Colgate | Colgate | 18 | 14% | 51% |
| HUL | Pepsodent, Closeup | 9 | 12% | 27% |
| Dabur | Dabur Red, Babool, Meswak | 4 | 13% | 13% |
| Amar Remedies | Amar, Smiles | 3 | 27% | 9% |
| Total | | 35 | 14% | |

Source: PINC Research, Company, Industry

Exhibit 48 - Toothpaste Peer Price Comparison

| Oral Care | Unit | MRP/unit | Category | Company |
|------------------------------|------|----------|----------|---------------------|
| Colgate Sensitive Pro Relief | gm | 1.50 | Premium | Colgate Palmolive |
| Sensodyne | gm | 1.13 | Premium | GSK Asia |
| Colgate Sensitive Original | gm | 1.00 | Premium | Colgate Palmolive |
| Colgate Total | gm | 0.55 | Economy | Colgate Palmolive |
| Pepsodent Gum Care | gm | 0.45 | Economy | HUL |
| Colgate Max White | gm | 0.43 | Economy | Colgate Palmolive |
| Close up Fire Freeze | gm | 0.43 | Economy | HUL |
| Close up Menthol | gm | 0.43 | Economy | HUL |
| Colgate Max Fresh | gm | 0.41 | Economy | Colgate Palmolive |
| Pepsodent Centre Fresh | gm | 0.41 | Economy | HUL |
| Pepsodent Whitening | gm | 0.41 | Economy | HUL |
| Close up Lemon Mint | gm | 0.41 | Economy | HUL |
| Close up Pepper Mint | gm | 0.40 | Economy | HUL |
| Close up Red Hot | gm | 0.40 | Economy | HUL |
| Himalaya | gm | 0.40 | Economy | Himalaya Healthcare |
| Pepsodent Germi Check 2in1 | gm | 0.39 | Economy | HUL |
| Close up Milk Calcium | gm | 0.39 | Economy | HUL |
| Colgate Active Salt | gm | 0.35 | Economy | Colgate Palmolive |
| Meswak | gm | 0.33 | Popular | Dabur India |
| Dabur Red | gm | 0.32 | Popular | Dabur India |
| Colgate Dental Cream | gm | 0.31 | Popular | Colgate Palmolive |
| Pepsodent Germi Check Magnet | gm | 0.30 | Popular | HUL |
| Colgate Herbal | gm | 0.29 | Popular | Colgate Palmolive |
| Neem | gm | 0.26 | Popular | Natural & Nature |
| Babool | gm | 0.18 | Popular | Dabur India |
| Colgate Cibaca | gm | 0.18 | Popular | Colgate Palmolive |
| Promise | gm | 0.17 | Popular | Dabur India |

HUL has no presence in the premium market...

We believe large part of HUL's toothpaste sales comes from the economy segment...

Source: PINC Research, Retail Market Dec'2011

What do we expect?

Historically, large part of the toothpaste market growth was based on the volume growth. We expect 9-10% toothpaste volume growth is sustainable in the medium term as India's oral care market is still under developed. Our per capita toothpaste consumption is lowest among the peer nations. However in the toothpaste market, most of the recent launches were in the premium segment and we believe that oral care market is now set for the value growth too. Toothpaste cost is insignificant in the monthly household expense therefore consumer market has appetite for price increase on the existing products as well as additional launches in the premium products. Our belief is that going forward toothpaste market would grow through a healthy mix of price and volume.

For HUL, we believe its large part of toothpaste sales comes from the 'Economy segment' as it has no presence in the 'Premium segment' while 'Popular segment' is largely dominated by Colgate Palmolive (Colgate) and Dabur India. Pepsodent and Close-up brands are well settled in the urban and modern trade market and HUL can enter into other oral care products like mouthwash where Colgate is a leader. Colgate will remain a big threat for HUL. Colgate is not only the market leader but also very aggressive in the field level therefore snatching market share from Colgate is a difficult task. Overall our take is that HUL will continue to grow slower than its peers and should clock 11% CAGR in toothpaste business during FY11-14E.

What do we expect for Personal care segment?

We believe personal care category would continue to lead HUL on profitability front. In our opinion, skin care is the largest contributor of personal care business and contributes ~50% of personal care EBITDA. Skin care is the most promising categories in the personal care space where we expect growth potential is immense. India’s favourable demographic change would be beneficial more for skin care market.

Exhibit 49 - Sales and EBITDA Mix Estimates of Personal Care Category

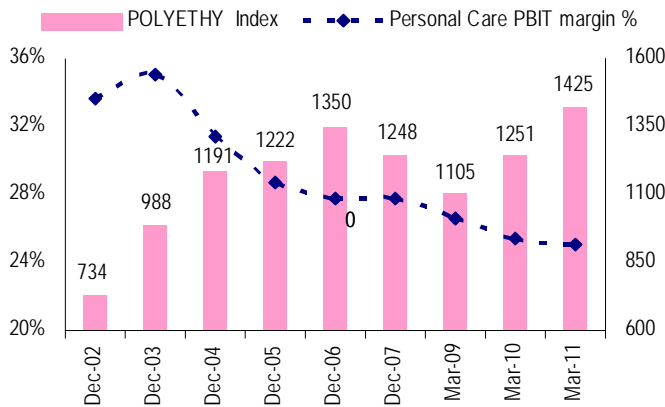
| Categories | Sales Mix (%) | EBITDA Mix (%) |
|-----------------|---------------|----------------|
| Skin Care | 38% | 50% |
| Shampoo | 26% | 18% |
| Oral Care | 17% | 12% |
| Color Cosmetics | 8% | 10% |
| Deodorant | 4% | 7% |
| Others | 6% | 7% |

Source: PINC Research

Although several domestic and MNCs are expanding personal care capacities in India, we believe it would rather help the category growth. Skin care market is still under developed market and competition would increase consumers’ consciousness towards the beauty products.

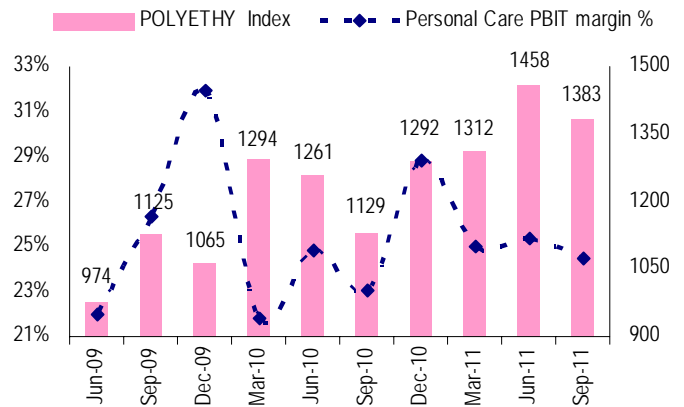
HUL’s large product portfolio in each of the categories would make the company more competitive. Strong growth in skin care would adjust the profitability pressure in other categories like shampoo and oral care and would help in maintaining the profitability profile of the personal care segment.

Exhibit 50 - Packaging Impact on PBIT Margin (Yr)



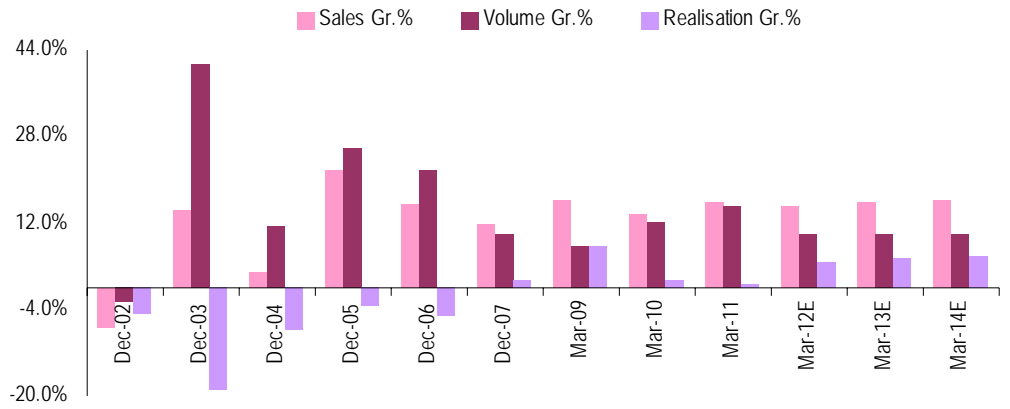
Source: PINC Research, Bloomberg

Exhibit 51 - Packaging Impact on PBIT Margin (Qt)



Source: PINC Research, Bloomberg

Exhibit 52 - Personal Care Expected Growth



Source: PINC Research, Company * Growth is adjusted for the change in financial year

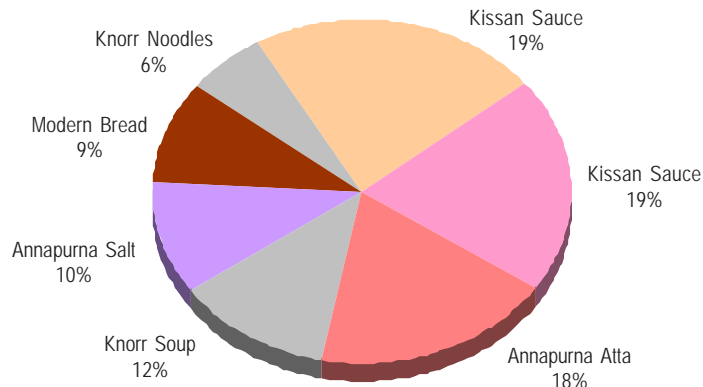
Foods Business-profitability is a concern

HUL operates Food business under Kissan, Annapurna, Knorr and Modern brands. Kissan is one of the oldest brands in India and the brand covers Jam, Tomato Ketchup and Squash products for HUL. Annapurna brand covers packaged Atta and Salt while Knorr brand envelop Soups and Noodles.

Branded staple foods which include Annapurna Atta, Salt and Modern bread could not positioned well in the market. These three brands faced stiff competition from the branded and unbranded products. ITC's Aashirvaad Atta has always been a big hurdle in the urban market (especially modern trade) for HUL's Annapurna. While Tata's Salt is fairly a leader in the urban and rural market and impacted Annapurna Salt. Although Modern bread is well known brand in modern trade but it could not compete with the regional players.

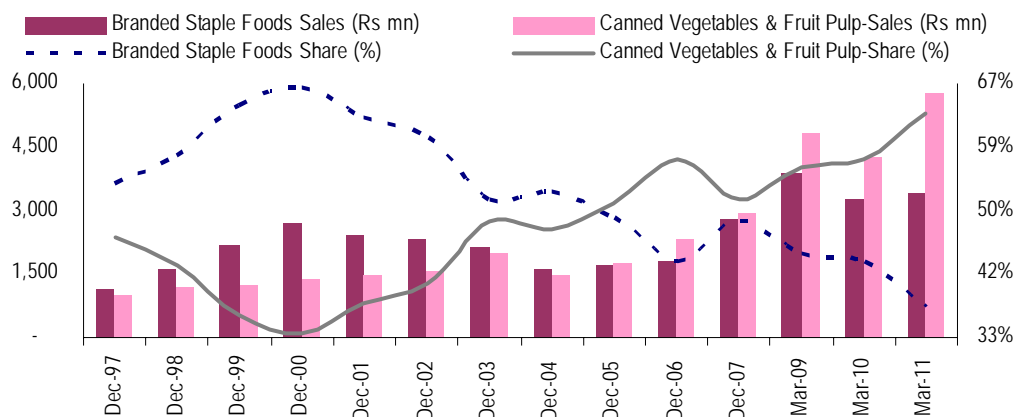
Canned vegetable and fruit pulp segment is dominated by Kissan and Knorr brand. HUL is the leader in the branded market for Jam, Sauce and Soup. Kissan brand is positioned well in the urban and rural market while Knorr soup and noodles are relatively urban market products with its large acceptance in the modern trade.

Exhibit 53 - Food Business Mix



Source: PINC Research, Company

Exhibit 54 - Food Business Mix

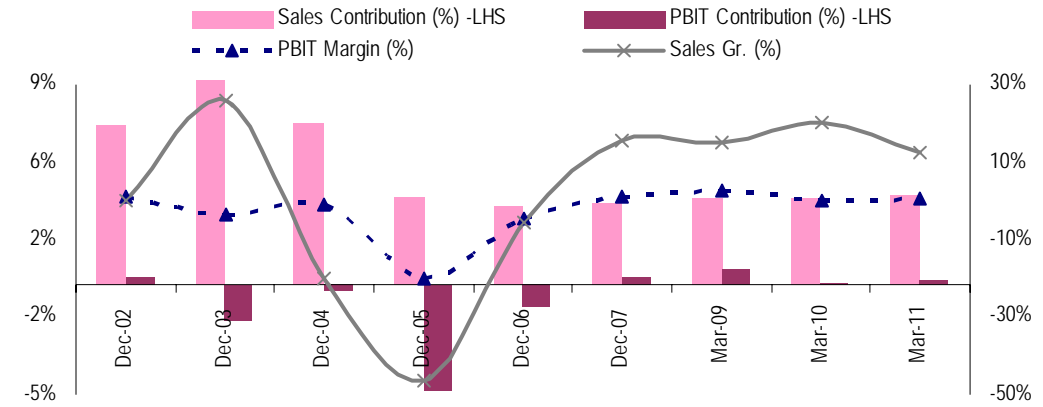


Source: PINC Research, Company

Concern over profitability remains

Profitability of the food business has always been a concern for HUL. We are not very optimistic for HUL's food business as most of the products are into those categories where unorganised players have strong dominance. We don't expect any significant contribution in the sales and profitability in the next three years.

Exhibit 55 - Food Business Performance

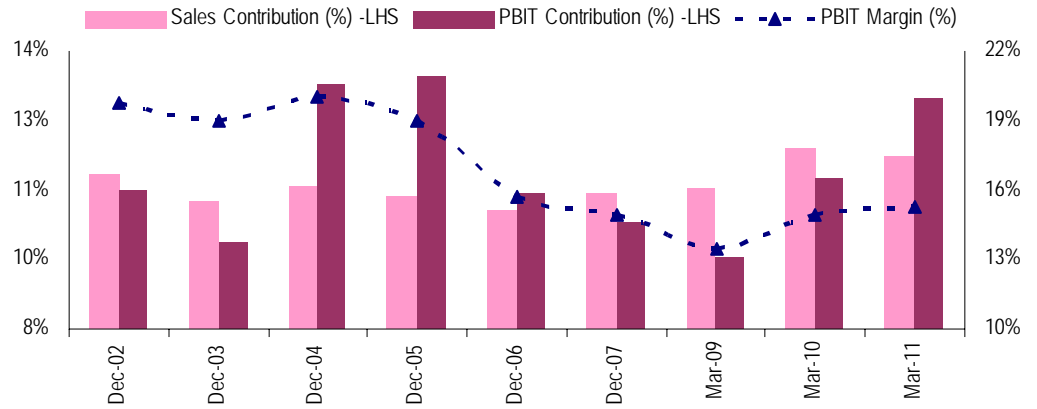


Source: PINC Research, Company

Beverages

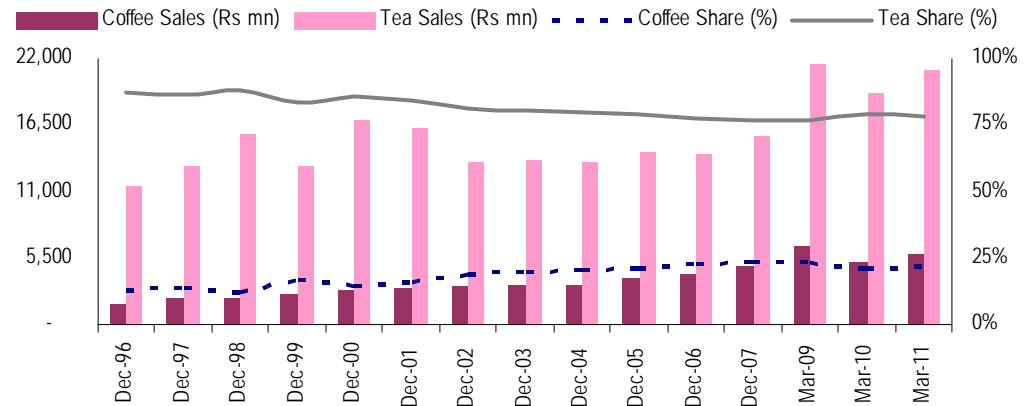
Beverage business contributes 12% and 14% of sales and PBIT for HUL respectively. Tea business dominates HUL's beverage business and contributes >80% of the total sales. In tea business HUL owns Taj Mahal, Lipton, Brooke Bond Red Label and Taaza brands while coffee business operates through 'Bru' brand.

Exhibit 56 - Beverage Business Performance



Source: PINC Research, Company

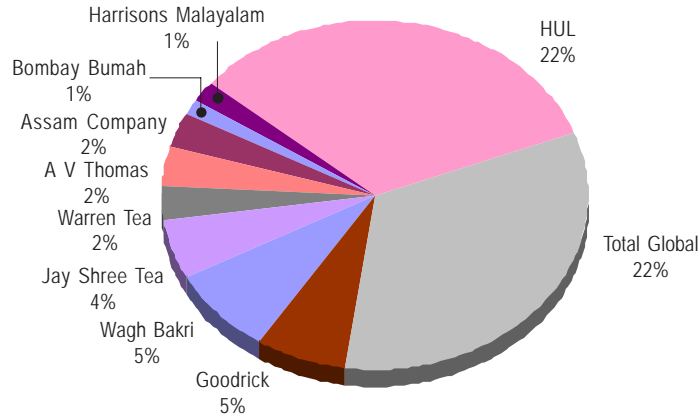
Exhibit 57 - Beverage Business Breakup



Source: PINC Research, Company

HUL and Tata Global Beverage are the leaders in the domestic tea business with almost equal market share. Tea market in India is largely dominated by the small players and we believe these small players are snatching market share from the big players.

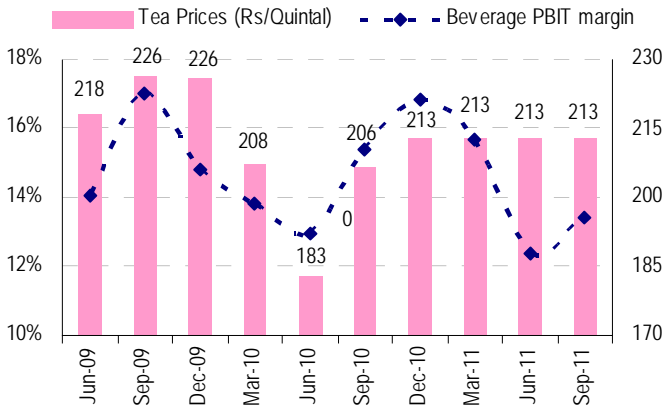
Exhibit 58 - Tea Players' Market Share



Source: PINC Research, Industry, Capitaline

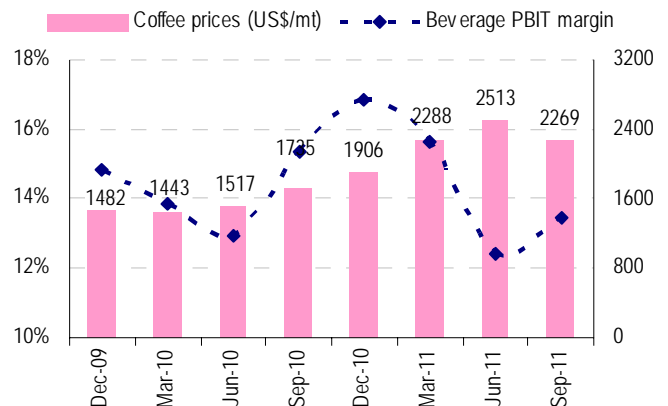
Tea and Coffee prices in India are sensitive to global prices therefore macro level changes impact a lot on the domestic price scenario. Beverage contribution in HUL's sales and PBIT has increased in past 4 years and being one of the critical segments for HUL. We expect HUL's beverage business to show 12% CAGR during FY11-14E.

Exhibit 59 - Tea Prices and Beverage PBIT Margin



Source: PINC Research, Bloomberg

Exhibit 60 - Coffee Prices and Beverage PBIT Margin



Source: PINC Research, Bloomberg

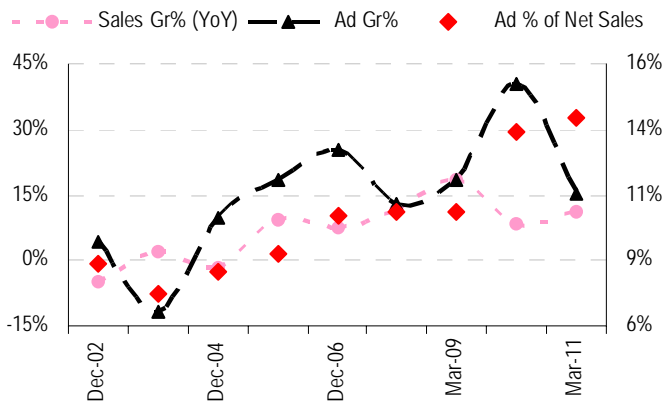
Impact of advertisement spending on sales growth

We observe that most of the FMCG companies were very aggressive during FY10 and spent huge amount on advertisements. Favourable input prices scenario had supported that extra money spent on branding. While the benefit in terms of sales growth was not in line. In most of the cases growth in advertisement spending was higher than the sales growth achieved while Colgate and ITC were only exceptional.

HUL's slower sales growth despite spending too much on advertisement has made it one of the highest spending companies on advertisement. This led to a jump in HUL's advertisement expense (% of net sales) by 360bps in the last two years. However, robust sales growth has helped other FMCG companies in maintaining advertisement expenses level during FY09-11. In the last two years, advertisement level has improved moderately for Nestle, Marico and Dabur by 34bps, 90bps and 87bps while there was decline for Colgate and ITC by 26bps and 28bps respectively.

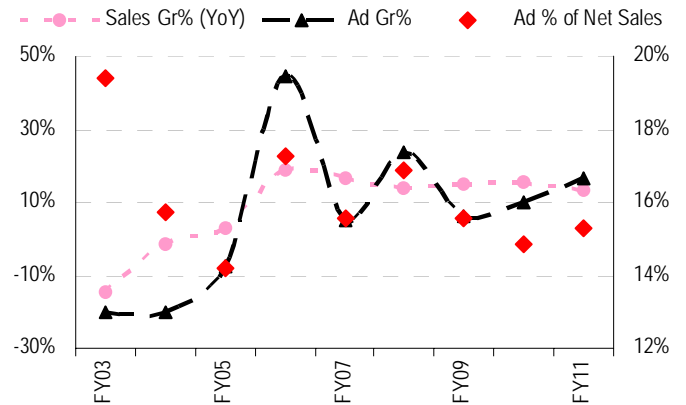
We expect HUL's advertisement expenses (% of net sales) would be lower at ~11% in FY12 v/s 14% in FY11 on account of pressure of commodity prices. While due to the ease in the input price pressure and higher advertisement requirement for personal care products, we expect advertisement spend should be ~11.5% and ~12% in FY13E and FY14E respectively.

Exhibit 61 - HUL



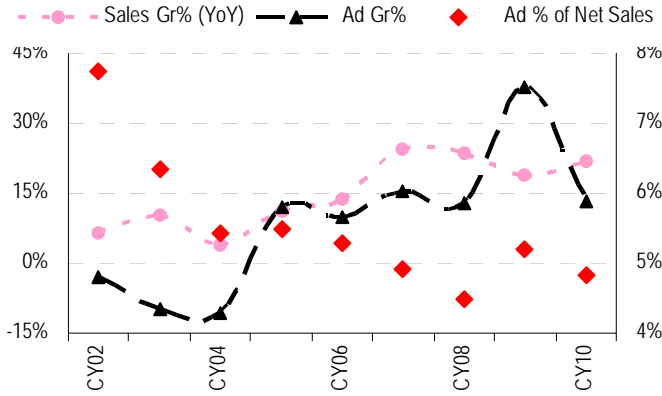
Source: PINC Research, Company

Exhibit 62 - Colgate



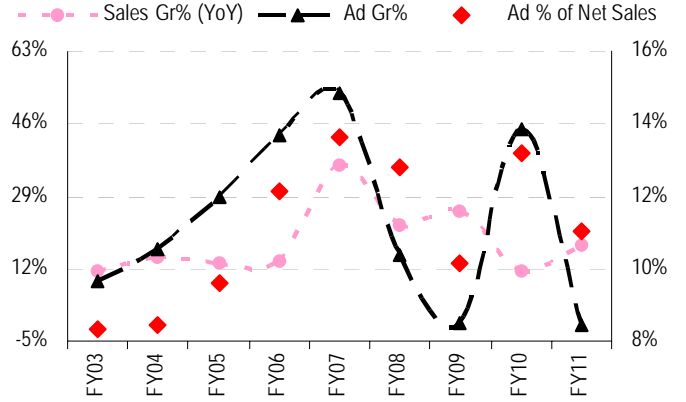
Source: PINC Research, Company

Exhibit 63 - Nestle



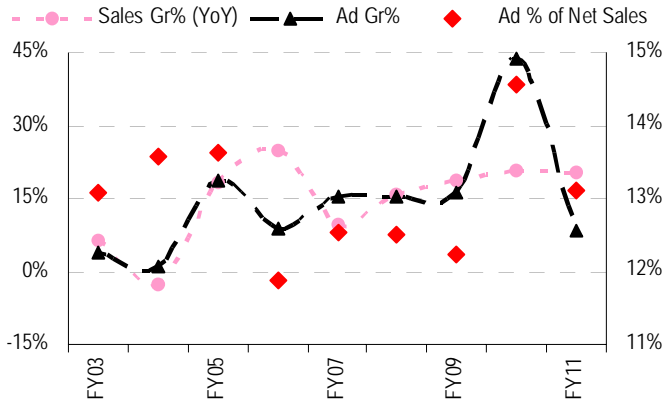
Source: PINC Research, Company

Exhibit 64 - Marico



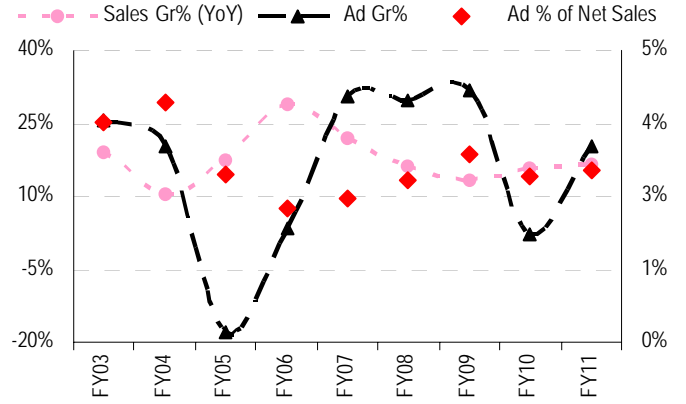
Source: PINC Research, Company

Exhibit 65 - Dabur



Source: PINC Research, Company

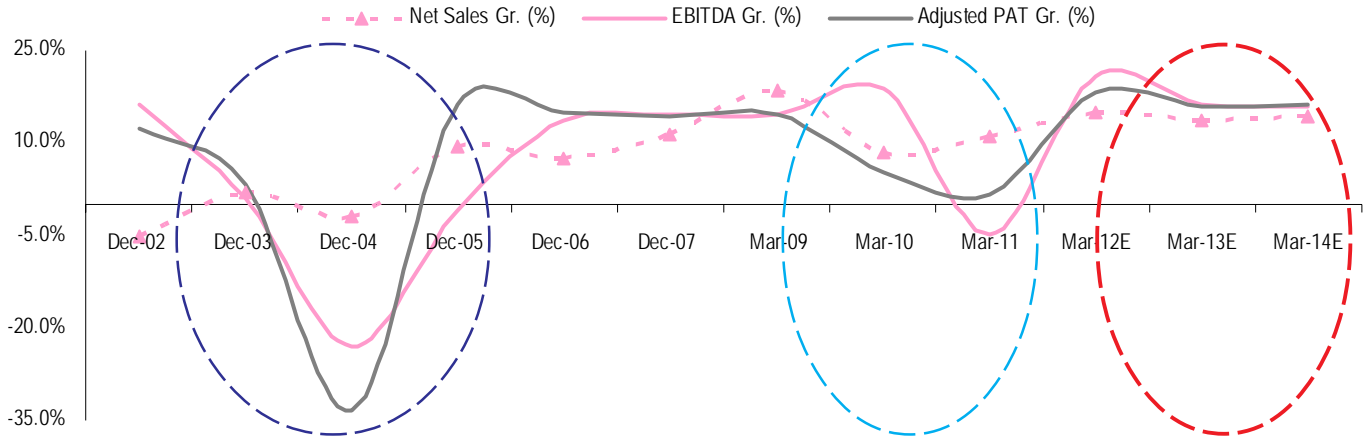
Exhibit 66 - ITC



Source: PINC Research, Company

Financial Analysis

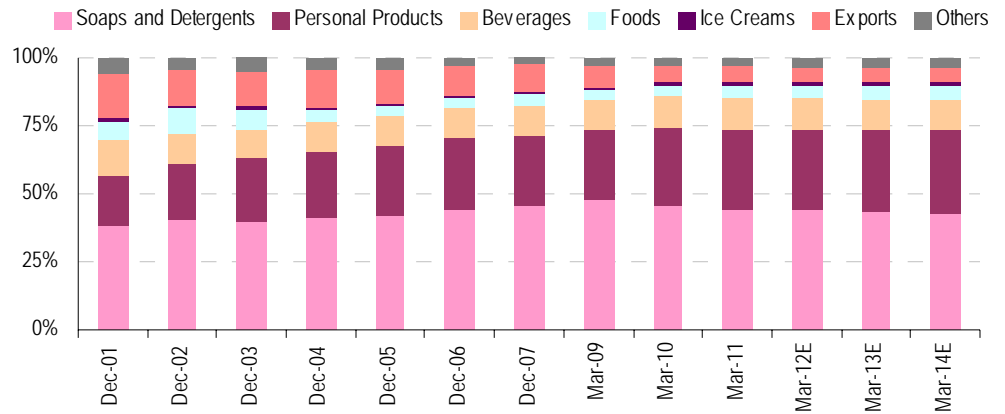
Exhibit 67 - HUL's Business Performance



Source: PINC Research, Company

- HUL's performance during 2003-2005 was extremely under pressure owing to industrywide slowdown. Most of the FMCG companies faced volume pressure, sector sales growth during that time was <5%. HUL's PBIT margin for 'Soaps and Detergent' segment during that time was declined by >1000bps and it resulted into >500bps decline in overall EBITDA margin.
- HUL faced sales growth pressure during FY10 and net sales grew by mere 8%. This slower growth was account of higher peer pressure on 'Soaps and Detergent' segment which displayed >5% growth during FY10. HUL's profitability in FY11 was impact due to higher input price pressure and down trading in soaps and detergents segment.
- Going forward we expect similar growth in sales, EBITDA and PAT.

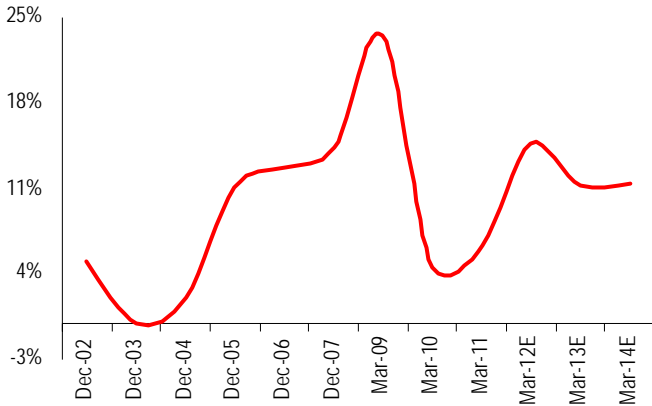
Exhibit 68 - HUL's Business Mix



Soaps and Detergent segment dominate in HUL's business...

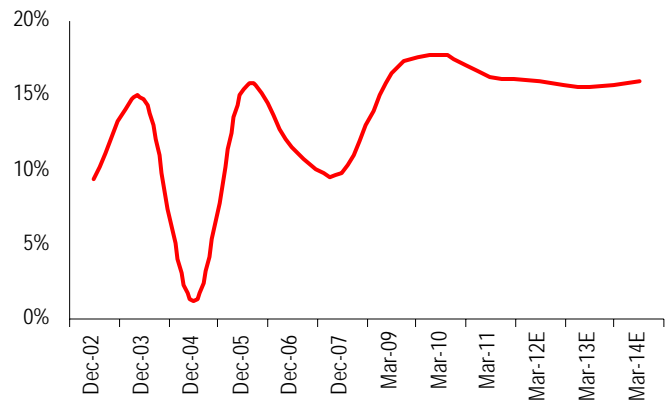
Source: PINC Research, Company

Exhibit 69 - Soaps and Detergent Gr. (%)



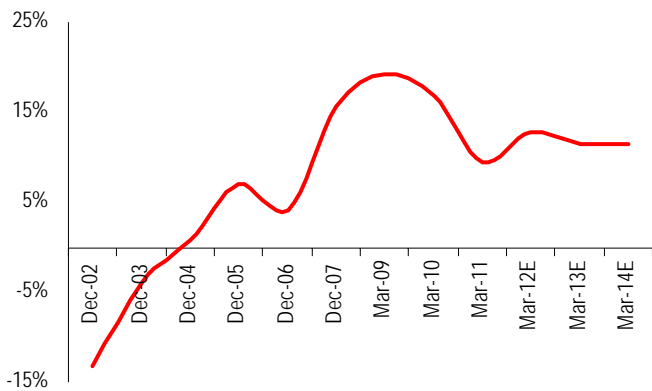
Source: PINC Research, Company

Exhibit 70 - Personal Care Gr. (%)



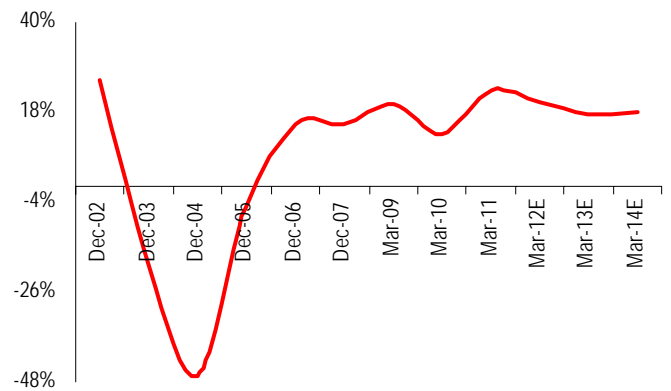
Source: PINC Research, Company

Exhibit 71 - Beverage Business Gr. (%)



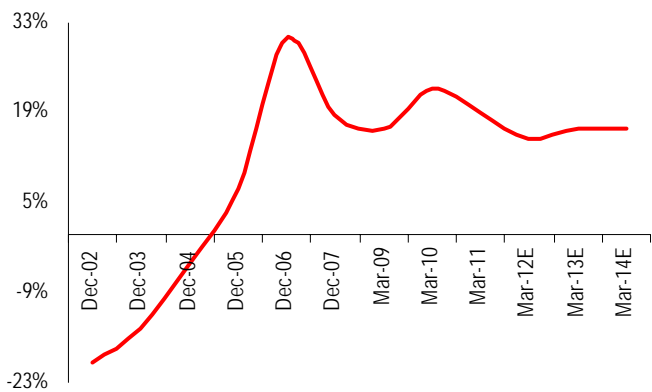
Source: PINC Research, Company

Exhibit 72 - Food Business Gr. (%)



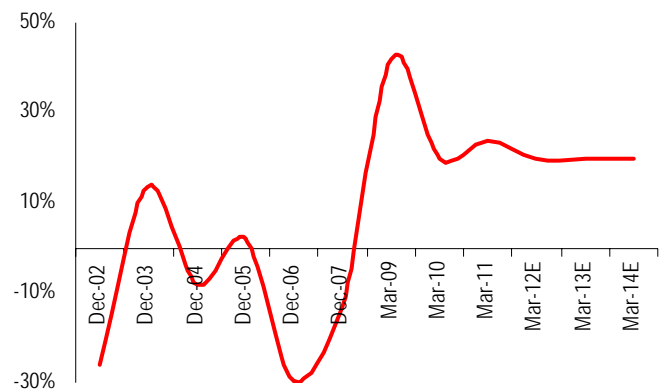
Source: PINC Research, Company

Exhibit 73 - Ice Cream Gr. (%)



Source: PINC Research, Company

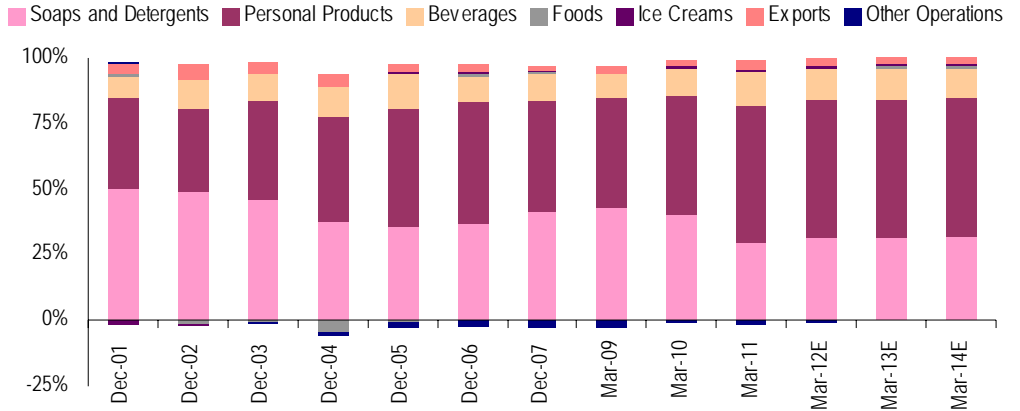
Exhibit 74 - Other Business Gr. (%)



Source: PINC Research, Company

Exhibit 75 - Profitability Mix (%)

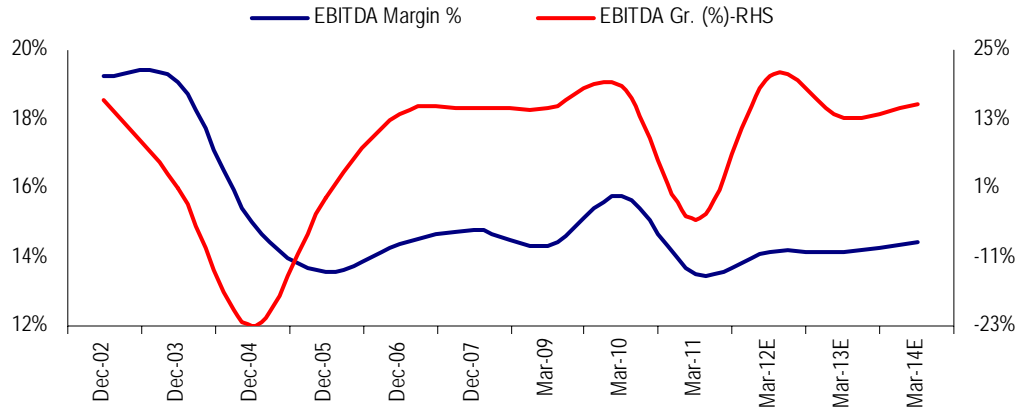
High margin of Personal care business has changed the profitability mix...



Source: PINC Research, Company

Exhibit 76 - EBITDA Margin and YoY Gr. (%)

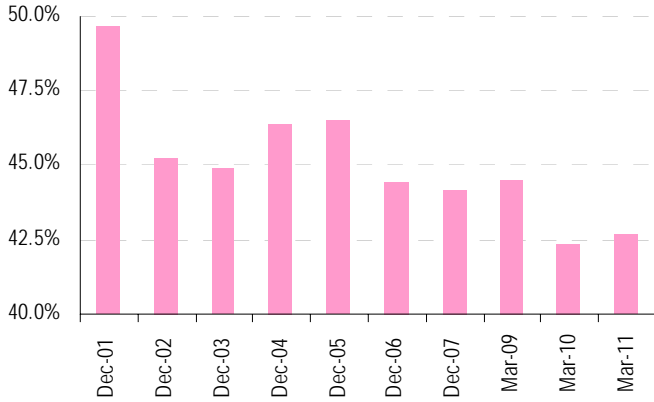
Profitability has gradually come down...



Source: PINC Research, Company

We observed HUL's long history and found that the profitability had impacted a lot on account of higher focus on branding. Better revenue mix reduced the raw material cost (% of net sales) by 250bps in past 10 years while EBITDA margin shrunk by >600bps due to higher discretionary spending.

Exhibit 77 - RM Cost (% of net sales)



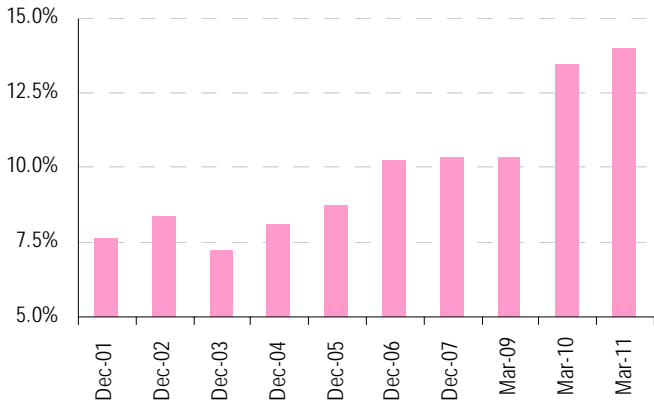
Source: PINC Research, Company

Exhibit 78 - Packaging Cost (% of net sales)



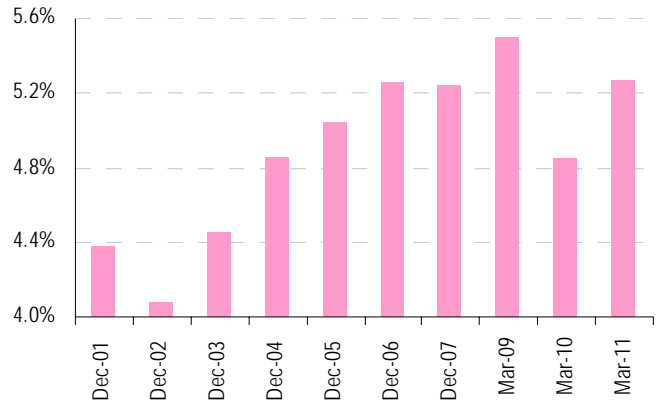
Source: PINC Research, Company

Exhibit 79 - Advertisement Cost (% of net sales)



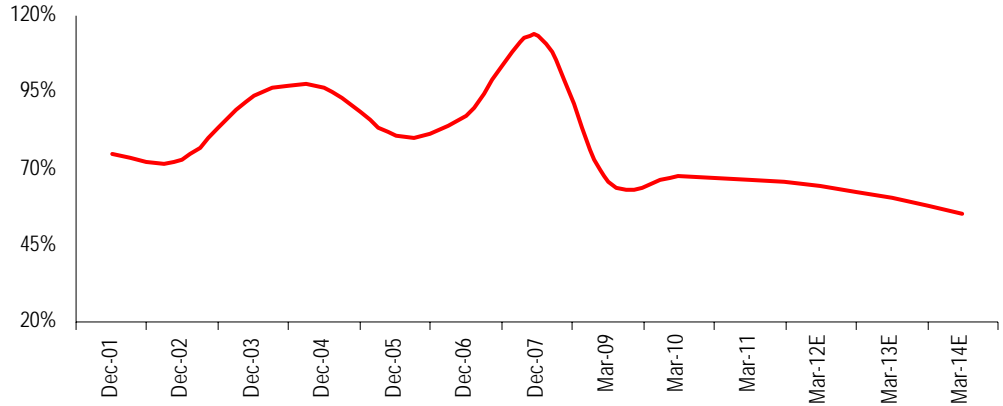
Source: PINC Research, Company

Exhibit 80 - Distribution Cost (% of net sales)



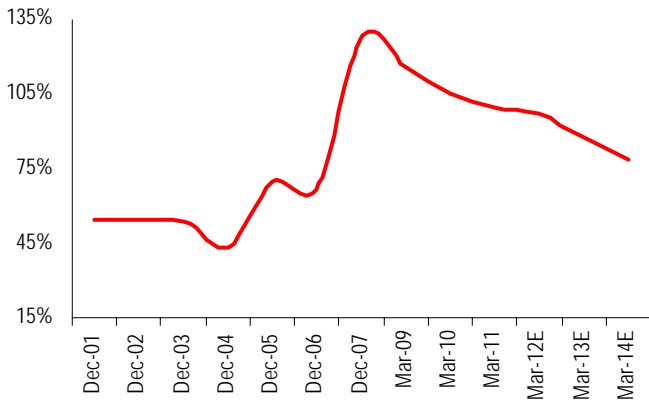
Source: PINC Research, Company

Exhibit 81 - Dividend Payout Ratio (%)



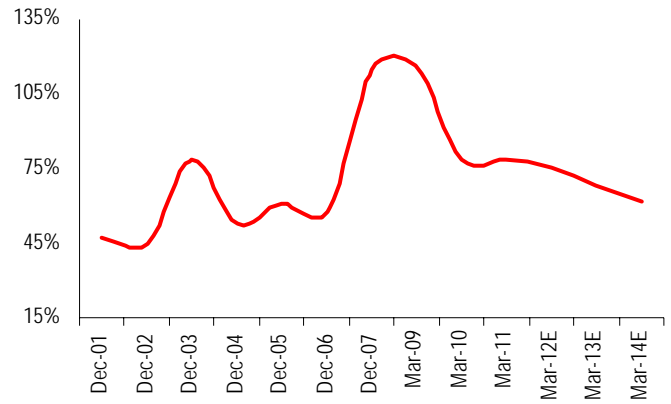
Source: PINC Research, Company

Exhibit 82 - ROCE (%)



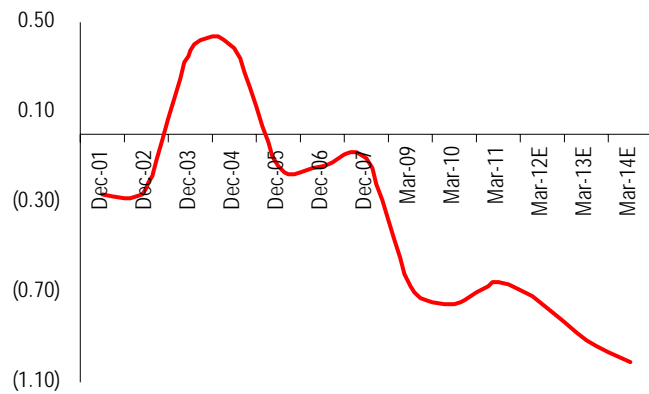
Source: PINC Research, Company

Exhibit 83 - ROE (%)



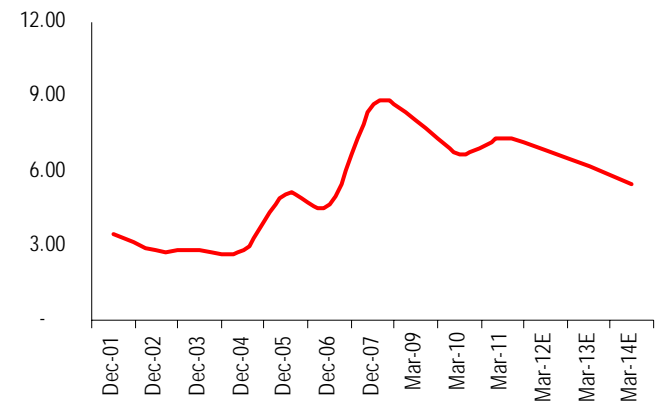
Source: PINC Research, Company

Exhibit 84 - Net Debt Equity Ratio (%)



Source: PINC Research, Company

Exhibit 85 - Asset Turn Ratio (%)



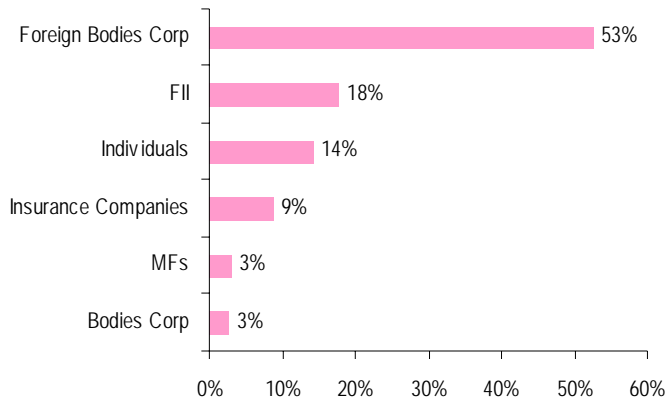
Source: PINC Research, Company

Company Background

HUL is the largest FMCG manufacturer in India, having presence in Soaps, Detergents, Skin care, Oral care, Hair Care, Staple Foods and Beverages. HUL was formed in 1933 as Lever Brothers India Ltd and came into being in 1956 as Hindustan Lever Ltd (HLL) through a merger of Lever Brothers, Hindustan Vanaspathi Manufacturing Company Ltd and United Traders Ltd. Later in mid 2007, the company was renamed as "Hindustan Unilever Ltd."

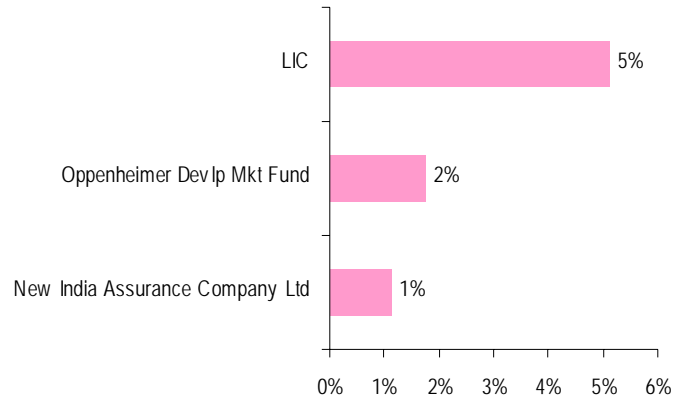
HUL is owned by the European company Unilever and owns ~52% majority stake. HUL is one of the key script in the stock indices and carries >3% weightage in the BSE SENSEX.

Exhibit 86 - Shareholding Pattern (%)



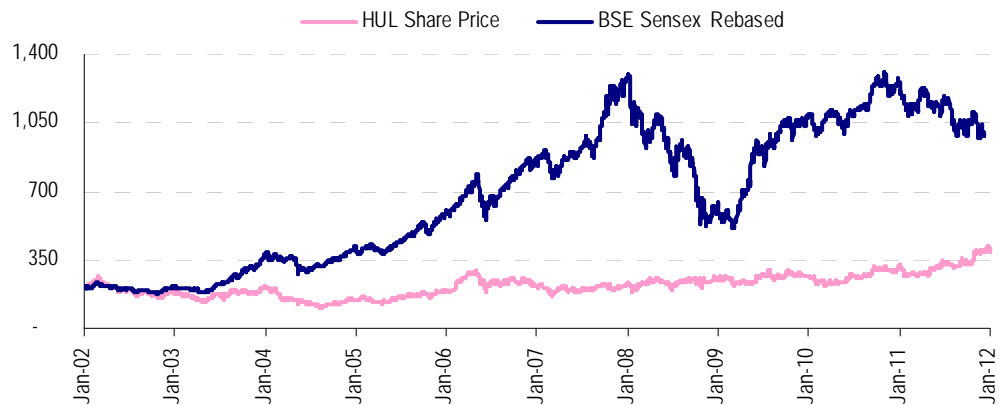
Source: PINC Research, BSE Sep'2011 Shareholdings

Exhibit 87 - Holding More Than 1% of the Total Shares



Source: PINC Research, BSE Sep'2011 Shareholdings

Exhibit 88 - HUL Share Price History v/s BSE Sensex Rebased



Source: PINC Research, Bloomberg

Exhibit 89 - HUL's Business History

| Announce Date | Target Name | Acquirer Name | Seller Name | Announced Total Value (Rs mn) | Payment Type |
|---------------|---------------------------------------|----------------------------------|-------------------------|-------------------------------|--------------|
| 12-Feb-98 | Ponds India Ltd | Hindustan Unilever Ltd | | 40,424 | Stock |
| 27-Jan-06 | Nihar brand | Marico Ltd | Hindustan Unilever Ltd | 2,160 | Cash |
| 28-Mar-01 | Quest International India Ltd | Akzo Nobel India Ltd | Hindustan Unilever Ltd | 1,520 | Cash |
| 11-Oct-00 | International Bestfoods Ltd | Hindustan Unilever Ltd | | 1,306 | Stock |
| 1-Apr-02 | Paras Extra Growth Seeds Ltd | India Seeds Holdings Ltd | Hindustan Unilever Ltd | 1,150 | Undisclosed |
| 27-Feb-01 | Modern Food Industries India Ltd | Hindustan Unilever Ltd | Republic of India | 1,050 | Cash |
| 20-Jun-03 | Edible oils & fats business | Bunge Ltd | Hindustan Unilever Ltd | 900 | Cash |
| 1-Mar-06 | Tea Estates India Ltd/India | Woodbriar Group | Hindustan Unilever Ltd | 710 | Cash |
| 25-Sep-07 | Hindustan Unilever Ltd | Shareholders | | 626 | |
| 13-Dec-05 | Doom Dooma Tea Co | BM Khaitan Group | Hindustan Unilever Ltd | 690 | Cash |
| 26-May-06 | Quest International India Ltd | Akzo Nobel India Ltd | Hindustan Unilever Ltd | 540 | Cash |
| 9-Aug-05 | Vashishti Detergents Ltd | Hindustan Unilever Ltd | | 494 | Stock |
| 15-Jan-01 | Gold Mohur Foods & Feeds Ltd | Godrej Industries Ltd | Hindustan Unilever Ltd | 450 | Cash |
| 27-Feb-02 | Modern Food Industries India Ltd | Hindustan Unilever Ltd | Republic of India | 440 | Cash |
| 20-Nov-01 | Catalyst business | Akzo Nobel India Ltd | Hindustan Unilever Ltd | 210 | Cash |
| 3-May-99 | Industrial Perfumes Ltd | Hindustan Unilever Ltd | Unilever NV | N/A | Stock |
| 20-Sep-01 | Gold Mohur Foods & Feeds Ltd | Godrej Industries Ltd | Hindustan Unilever Ltd | N/A | Undisclosed |
| 8-Apr-03 | Shrimp & crabmeat business | Hindustan Unilever Ltd | Amalgam Enterprises Ltd | N/A | Undisclosed |
| 17-Apr-03 | Glucose drink brand | Wipro Ltd | Hindustan Unilever Ltd | N/A | Undisclosed |
| 9-Aug-05 | Functionalised biopolymer business | Riddhi Siddhi Gluco Biols Ltd | Hindustan Unilever Ltd | N/A | Undisclosed |
| 7-Sep-06 | Capgemini Business Services India Ltd | Cap Gemini SA | Hindustan Unilever Ltd | N/A | Undisclosed |
| 29-Mar-10 | Capgemini Business Services India Ltd | Cap Gemini SA | Hindustan Unilever Ltd | N/A | Undisclosed |
| 27-Jul-10 | Hindustan Field Services Pvt Ltd | Smollan Holdings Proprietary Ltd | Hindustan Unilever Ltd | N/A | Undisclosed |

Source: PINC Research, Bloomberg

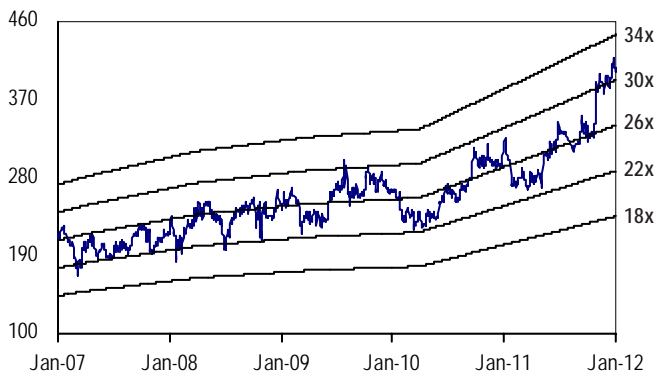
| Income Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|------------------------|---------|---------|---------|---------|---------|
| Gross Sales | 183,678 | 204,701 | 236,575 | 269,014 | 307,138 |
| Net sales | 180,256 | 200,185 | 229,960 | 261,492 | 298,550 |
| Growth (%) | 8.3 | 11.1 | 14.9 | 13.7 | 14.2 |
| EBITDA | 28,374 | 27,045 | 32,676 | 37,980 | 43,996 |
| Growth (%) | 18.8 | (4.7) | 20.8 | 16.2 | 15.8 |
| Depreciation | 1,919 | 2,293 | 2,372 | 2,552 | 2,612 |
| Other Income | 827 | 2,618 | 3,043 | 3,203 | 3,523 |
| EBIT | 27,281 | 27,370 | 33,346 | 38,630 | 44,906 |
| Interest Paid | 75 | 10 | 2 | 2 | 2 |
| PBT (before E/o items) | 27,206 | 27,360 | 33,345 | 38,628 | 44,905 |
| Tax Provision | 6,153 | 5,919 | 8,003 | 9,271 | 10,777 |
| Minority Interest | 80 | 106 | 116 | 128 | 141 |
| E/o income/(loss) | 594 | 1,624 | - | - | - |
| Reported PAT | 21,568 | 22,960 | 25,225 | 29,229 | 33,987 |
| Adjusted PAT | 20,974 | 21,336 | 25,225 | 29,229 | 33,987 |
| Growth (%) | 5.3 | 1.7 | 18.2 | 15.9 | 16.3 |
| Diluted EPS (Rs) | 9.6 | 9.9 | 11.7 | 13.5 | 15.7 |
| Diluted EPS Growth (%) | 5.2 | 2.8 | 18.2 | 15.9 | 16.3 |

| Cash Flow Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|----------|----------|----------|----------|----------|
| Pre-tax profit | 27,205 | 27,360 | 33,345 | 38,628 | 44,905 |
| Depreciation | 1,919 | 2,293 | 2,372 | 2,552 | 2,612 |
| Total Tax Paid | (6,735) | (6,710) | (7,808) | (9,076) | (10,582) |
| Chg in working capital | 14,627 | (1,521) | (78) | 2,967 | 2,674 |
| Other operating activities | (2,220) | (2,320) | 2 | 2 | 2 |
| Cash flow from oper (a) | 34,797 | 19,102 | 27,833 | 35,074 | 39,610 |
| Capital Expenditure | (5,520) | (3,106) | (2,000) | (2,000) | (2,000) |
| Chg in investments | (9,218) | 848 | - | - | - |
| Other investing activities | 3,303 | 3,834 | - | - | - |
| Cash flow from inv.(b) | (11,436) | 1,576 | (2,000) | (2,000) | (2,000) |
| Free cash flow (a+b) | 23,361 | 20,677 | 25,833 | 33,074 | 37,610 |
| Equity raised/(repaid) | - | - | - | - | - |
| Debt raised/(repaid) | (4,233) | (82) | - | - | 1 |
| Interest paid | (75) | (10) | (2) | (2) | (2) |
| Dividend (incl. Tax) | (15,284) | (14,264) | (16,196) | (19,436) | (23,755) |
| Other financing activities | (2,360) | (8,585) | (2,674) | (3,208) | (3,921) |
| Cash flow from fin. (c) | (21,952) | (22,940) | (18,872) | (22,646) | (27,676) |
| Net chg in cash (a+b+c) | 1,409 | (2,263) | 6,961 | 10,428 | 9,934 |

| Balance Sheet | FY10 | FY11 | FY12E | FY13E | FY14E |
|--------------------------|----------|----------|----------|----------|----------|
| Equity Share Capital | 2,182 | 2,160 | 2,160 | 2,160 | 2,160 |
| Reserves & surplus | 24,507 | 24,934 | 31,291 | 37,878 | 44,191 |
| Shareholders' funds | 26,689 | 27,094 | 33,450 | 40,037 | 46,350 |
| Minorities interests | 105 | 146 | 262 | 390 | 531 |
| Total Debt | 108 | 27 | 27 | 27 | 27 |
| Capital Employed | 26,902 | 27,266 | 33,739 | 40,454 | 46,908 |
| Net fixed assets | 24,943 | 25,231 | 24,859 | 24,306 | 23,694 |
| Cash & Cash Eq. | 20,124 | 17,873 | 24,835 | 35,265 | 45,201 |
| Net Other current assets | (32,891) | (29,793) | (29,715) | (32,682) | (35,355) |
| Investments | 12,245 | 11,885 | 11,885 | 11,885 | 11,885 |
| Net Deferred tax Assets | 2,482 | 2,070 | 1,875 | 1,680 | 1,485 |
| Total Assets | 26,903 | 27,266 | 33,739 | 40,454 | 46,909 |

| Key Ratios | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|--------|--------|--------|--------|--------|
| OPM (%) | 15.7 | 13.5 | 14.2 | 14.5 | 14.7 |
| Net Margin (%) | 11.6 | 10.7 | 11.0 | 11.2 | 11.4 |
| Div. Yield (%) | 1.6 | 1.6 | 1.9 | 2.3 | 2.8 |
| Net debt/Equity (x) | (0.7) | (0.7) | (0.7) | (0.9) | (1.0) |
| Net Working Capital (days) | (66.6) | (54.3) | (47.2) | (45.6) | (43.2) |
| ROCE (%) | 105.5 | 99.2 | 96.8 | 93.9 | 93.8 |
| RoE (%) | 78.6 | 78.7 | 75.4 | 73.0 | 73.3 |
| EV/Net Sales (x) | 4.6 | 4.1 | 3.6 | 3.1 | 2.7 |
| EV/EBITDA (x) | 29.4 | 30.6 | 25.1 | 21.3 | 18.2 |
| PER (x) | 41.3 | 40.2 | 34.0 | 29.3 | 25.2 |
| PCE (x) | 37.8 | 36.3 | 31.1 | 27.0 | 23.4 |
| Price/Book (x) | 32.5 | 31.6 | 25.6 | 21.4 | 18.5 |

1-Year forward P/E Band



Key Assumptions

| | FY10 | FY11 | FY12E | FY13E | FY14E |
|-----------------------------|-------|---------|-------|-------|-------|
| Soaps Sales Gr. (%) | 8.3% | 5.7% | 15.6% | 12.8% | 13.3% |
| Detergents Sales Gr. (%) | -0.4% | 6.4% | 14.5% | 12.5% | 13.5% |
| Personal Care Sales Gr. (%) | 13.7% | 16.0% | 15.1% | 16.0% | 16.4% |
| Beverages Sales Gr. (%) | 16.7% | 9.4% | 12.8% | 11.5% | 11.5% |
| Food Sales Gr. (%) | 12.7% | 23.5% | 20.4% | 17.7% | 17.8% |
| EBITDA Change (bps) | 139.5 | (223.1) | 69.9 | 31.5 | 21.2 |
| Effective tax rate (%) | 23% | 22% | 24% | 24% | 24% |

Company Update
 Sector: FMCG
 BSE Sensex: 15,868

NESTLE INDIA

 Maintain SELL
 CMP Rs4,143
 TP Rs3,618

09 January 2012

 Naveen Trivedi +91-22-6618 6384
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Slower volume growth, Valuations expensive

Nestle India (Nestle) underperformed BSE FMCG by 7% but its valuations are still very expensive. Nestle's 9MCY09 performance was in line with our expectation and 21% top line growth was lower at 18% in net earnings. Rising competition along with sharp price hike on all the key brands resulted into volume growth of 9% during 9MCY11 which was slowest in past 5 years.

We believe going forward Nestle would have to focus more on volume growth as the company is in the capacity expansion mode. Higher marketing efforts would be required for retaining volume leadership which would pressure on profitability. We expect 23% and 20% net sales and net earnings CAGR during CY10-13E.

We maintain our SELL rating on the stock with revise TP of Rs3,618.

Slower volume across all the categories

Nestle reported 9% volume growth during 9MCY11 which is the slowest growth in the past 5 years. Milk Product & Nutrition, Prepared Dishes and Chocolates registered slower volume growth of 4%, 15% and 1% respectively during 9MCY11. Rise in competition and sharp price hike on all the key brands were the key reason for slower volume growth performance.

Profitability intake despite high RM inflation

Despite facing high RM inflation, Nestle protected EBITDA margin during 9MCY09. We expect limited scope of further price hike along with higher A&P spending to protect volume market share would lower down the EBITDA margin by 90bps during CY10-13E.

VALUATIONS AND RECOMMENDATION

Nestle's monopoly in Maggi noodles would be difficult to maintain for long time post the entrance of big players. Competition is rising in almost all the categories while Nestle is expanding capacities which would force the company to maintain volume market share. Therefore, we expect pressure on pricing power of key brands. Nestle trades at a ~31% premium to the FMCG sector and we argue that this premium would narrow. We peg 30x P/E multiple on 12-months forward earnings and revise our TP to Rs3,618 (Rs3,578 earlier). We maintain 'SELL' rating on the stock.

KEY FINANCIALS

| | (Rs mn) | | | | |
|-----------------|---------|--------|--------|--------|---------|
| | CY09 | CY10 | CY11E | CY12E | CY13E |
| Net Sales | 51,395 | 62,609 | 76,556 | 94,350 | 117,129 |
| YoY Gr. (%) | 18.8 | 21.8 | 22.3 | 23.2 | 24.1 |
| Op. Profits | 10,448 | 12,559 | 15,122 | 18,419 | 22,431 |
| OPM (%) | 20.3 | 20.1 | 19.8 | 19.5 | 19.2 |
| Adj. Net Profit | 6,575 | 8,188 | 9,648 | 11,405 | 14,102 |
| YoY Gr. (%) | 21.7 | 24.5 | 17.8 | 18.2 | 23.7 |

KEY RATIOS

| | | | | | |
|---------------|-------|-------|-------|-------|-------|
| Dil EPS (Rs) | 68.2 | 84.9 | 100.1 | 118.3 | 146.3 |
| ROCE (%) | 179.7 | 146.8 | 88.9 | 81.4 | 81.0 |
| RONW (%) | 113.1 | 95.7 | 80.3 | 70.8 | 66.6 |
| P/E (x) | 60.8 | 48.8 | 41.4 | 35.0 | 28.3 |
| EV/Sales (x) | 7.7 | 6.3 | 5.2 | 4.3 | 3.4 |
| EV/EBITDA (x) | 37.9 | 31.5 | 26.5 | 21.9 | 17.8 |

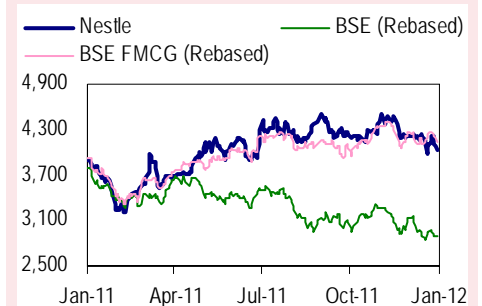
STOCK DATA

| | |
|-----------------------------|---------------|
| Market cap | Rs399bn |
| Book Value per share | Rs89 |
| Shares O/S (F.V. Rs10) | 96mn |
| Free Float | 37% |
| Avg. Trade Value (6 months) | Rs112mn |
| 52 week High/Low | Rs4,549/3,160 |
| Bloomberg Code | NESTIN |
| Reuters Code | NEST.BO |

PERFORMANCE (%)

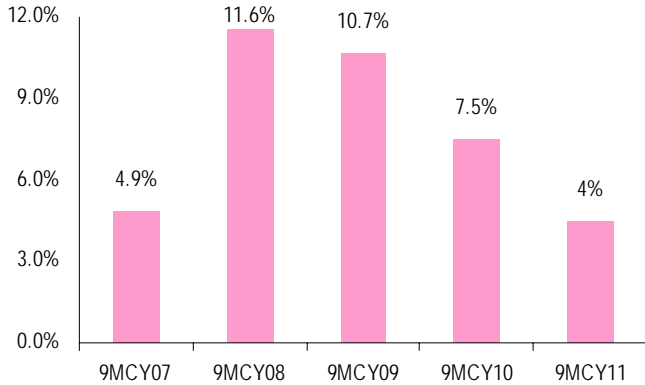
| | 1M | 3M | 12M |
|----------|-------|-------|------|
| Absolute | (2.9) | (2.3) | 5.3 |
| Relative | 2.6 | (2.7) | 35.5 |

RELATIVE PERFORMANCE



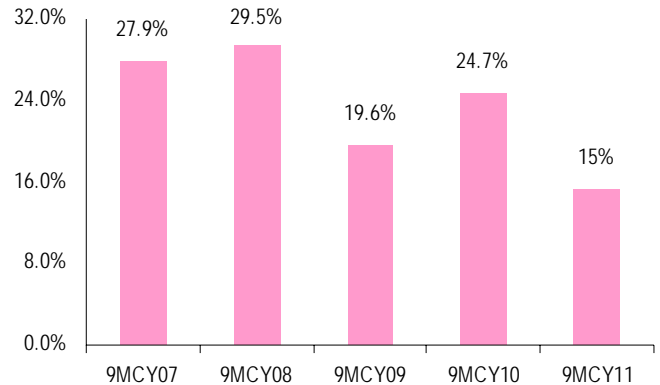
Slower volume growth performance across all the categories...

Exhibit 1 - Volume growth of Milk Product & Nutrition



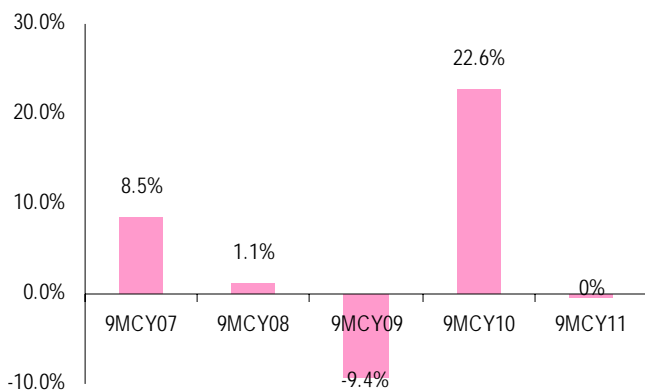
Source: PINC Research, Company

Exhibit 2 - Volume growth of Prepared Dishes



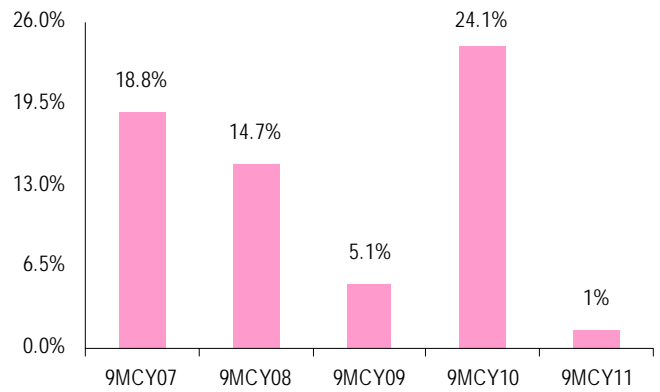
Source: PINC Research, Company

Exhibit 3 - Volume growth of Beverages



Source: PINC Research, Company

Exhibit 4 - Volume growth of Chocolates & Confect.



Source: PINC Research, Company

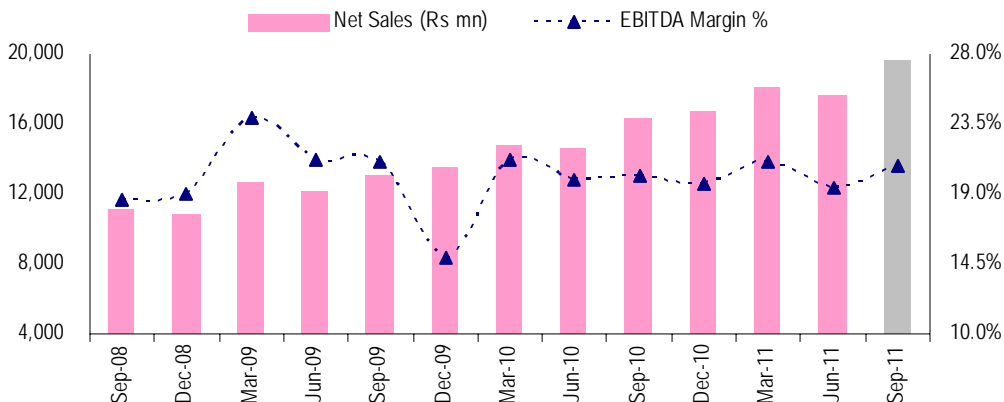
Exhibit 5 - 9MCY11 Earnings Summary (Rs mn)

| Particulars (Rs mn) | Sep-10 | Sep-11 | YoY Gr% | Jun-11 | QoQ Gr% | 9MCY10 | 9MCY11 | YoY Gr% | PINC Comments |
|----------------------------|--------|--------|---------|--------|---------|--------|--------|---------|---|
| Net Sales | 16,372 | 19,631 | 19.9 | 17,631 | 11.3 | 45,837 | 55,361 | 20.8 | Mix of volume and price growth |
| Other Operating Income | 41 | 62 | 50.5 | 50 | 23.2 | 143 | 156 | | |
| Total Income | 16,413 | 19,693 | 20.0 | 17,681 | 11.4 | 45,980 | 55,517 | 20.7 | |
| Raw Material Consumed | 7,283 | 8,224 | | 8,539 | | 22,499 | 25,859 | | |
| Stock Adjustment | 471 | 892 | | (76) | | (629) | 337 | | |
| Purchase of Finished Goods | 278 | 338 | | 255 | | 729 | 817 | | |
| Total RM cost | 8,032 | 9,454 | 17.7 | 8,718 | 8.4 | 22,599 | 27,013 | 19.5 | |
| Gross Profit | 8,381 | 10,239 | 22.2 | 8,962 | 14.2 | 23,382 | 28,504 | 21.9 | |
| Gross margin (%) | 51.1% | 52.0% | 93bps | 50.7% | 130bps | 50.9% | 51.3% | 49bps | Gross margin expansion was on improvement in product/channel mix |
| Employee Expenses | 1,041 | 1,424 | 36.8 | 1,375 | 3.5 | 3,155 | 4,004 | 26.9 | Commissioning of Maggi plant in Nanjangud has led to rise in staff cost |
| Other Expenses | 4,079 | 4,650 | 14.0 | 4,092 | 13.6 | 10,884 | 12,943 | 18.9 | Largely on higher A&P spending |
| Total Expenditures | 13,106 | 15,590 | 19.0 | 14,244 | 9.4 | 36,610 | 44,149 | 20.6 | |
| EBITDA | 3,307 | 4,103 | 24.1 | 3,437 | 19.4 | 9,370 | 11,368 | 21.3 | |
| EBITDA Margin % | 20.1% | 20.8% | 69bps | 19.4% | 140bps | 20.4% | 20.5% | 10bps | |
| Other Income | 54 | 59 | 9.3 | 30 | 98.7 | 144 | 172 | 19.1 | Low cash for investments as the Nestle is in the high capex mode |
| Interest | 1 | 12 | 2,200.0 | 6 | 98.3 | 10 | 17 | 78.4 | |
| Depreciation | 305 | 385 | 26.2 | 367 | 5.0 | 919 | 1,079 | 17.4 | Higher depreciation was on commissioning of Nanjangud plant |
| PBT | 3,056 | 3,754 | 22.8 | 3,094 | 21.3 | 8,586 | 10,432 | 21.5 | |
| Total Tax | 840 | 1,134 | 35.0 | 956 | 18.6 | 2,404 | 3,116 | 29.6 | |
| Effective tax (%) | 27% | 30% | 271bps | 31% | -70bps | 28% | 30% | 188bps | 100% tax benefits as Pantnagar facility has reduced to 30% |
| Reported PAT | 2,216 | 2,620 | 18.3 | 2,138 | 22.5 | 6,182 | 7,316 | 18.3 | |
| EPS (Adjusted) | 23.0 | 27.2 | 18.3 | 22.2 | 22.5 | 64.1 | 75.9 | 18.3 | |

Source: PINC Research, Company

Exhibit 6 - Net Sales (Rs mn) and EBITDA Margin (%) Trajectory

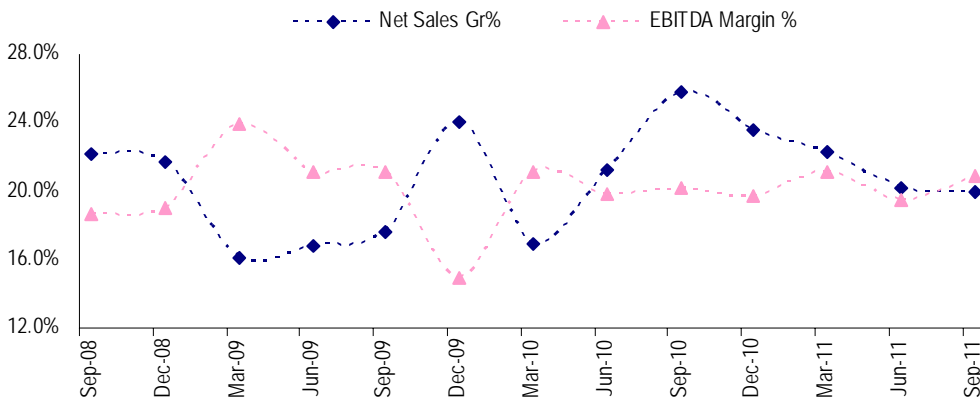
Higher gross level profitability and slower other expenses led to EBITDA margin expansion...



Source: Company, PINC Research

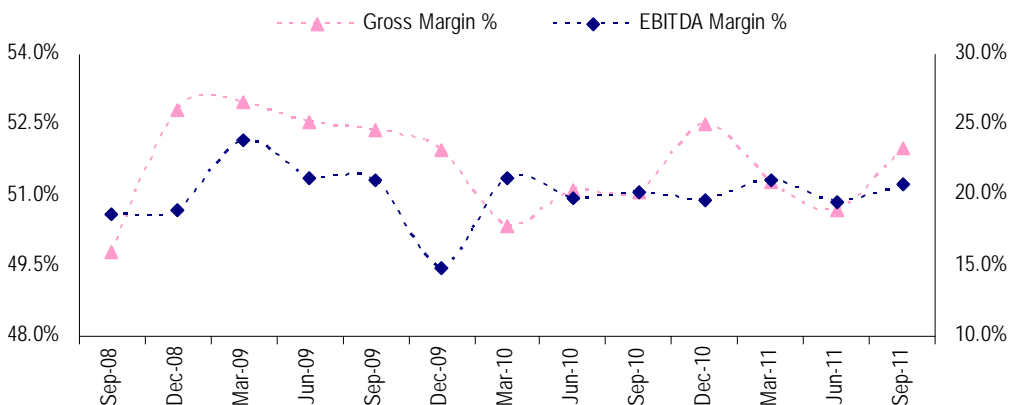
Exhibit 7 - Net Sales Gr% and EBITDA Margin (%) Relationship

Generally inverse relationship...



Source: Company, PINC Research

Exhibit 8 - Gross and EBITDA Margin (%)



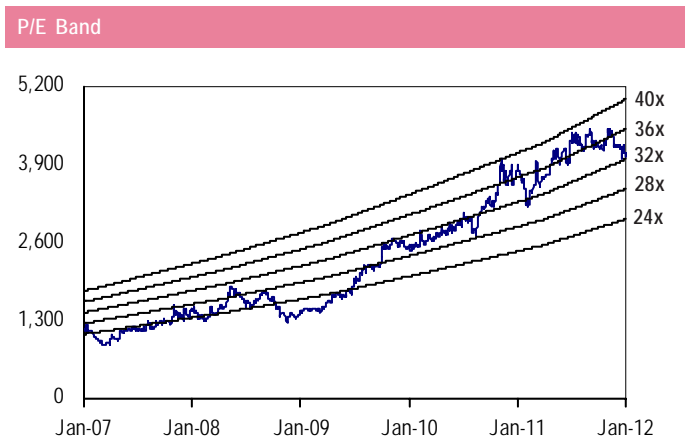
Source: Company, PINC Research

| Income Statement | CY09 | CY10 | CY11E | CY12E | CY13E |
|------------------------|--------|--------|--------|--------|---------|
| Gross Sales | 52,224 | 63,766 | 77,957 | 96,077 | 119,274 |
| Growth (%) | 16.8 | 22.1 | 22.3 | 23.2 | 24.1 |
| Net sales | 51,395 | 62,609 | 76,556 | 94,350 | 117,129 |
| Growth (%) | 18.8 | 21.8 | 22.3 | 23.2 | 24.1 |
| EBITDA | 10,448 | 12,559 | 15,122 | 18,419 | 22,431 |
| Growth (%) | 20.2 | 20.2 | 20.4 | 21.8 | 21.8 |
| Depreciation | 1,112 | 1,278 | 1,523 | 2,144 | 2,743 |
| Other Income | 276 | 365 | 395 | 374 | 544 |
| EBIT | 9,613 | 11,647 | 13,994 | 16,648 | 20,232 |
| Interest Paid | 14 | 11 | 125 | 288 | 325 |
| PBT (before E/o items) | 9,173 | 11,452 | 13,686 | 16,177 | 19,724 |
| Tax Provision | 2,619 | 3,264 | 4,037 | 4,772 | 5,621 |
| E/o income/(loss) | (22) | - | - | - | - |
| Reported Net Profit | 6,553 | 8,188 | 9,648 | 11,405 | 14,102 |
| Adjusted Net Profit | 6,575 | 8,188 | 9,648 | 11,405 | 14,102 |
| Growth (%) | 21.7 | 24.5 | 17.8 | 18.2 | 23.7 |
| Diluted EPS (Rs) | 68.2 | 84.9 | 100.1 | 118.3 | 146.3 |
| Diluted EPS Growth (%) | 21.7 | 24.5 | 17.8 | 18.2 | 23.7 |

| Cash Flow Statement | CY09 | CY10 | CY11E | CY12E | CY13E |
|----------------------------|---------|---------|----------|----------|---------|
| Pre-tax profit | 9,170 | 11,451 | 13,686 | 16,177 | 19,724 |
| Depreciation | 1,113 | 1,278 | 1,523 | 2,144 | 2,743 |
| Total Tax Paid | (2,692) | (3,207) | (3,912) | (4,647) | (5,496) |
| Chg in working capital | 1,545 | 756 | (20) | 948 | 1,154 |
| Other operating activities | 145 | 90 | 125 | 288 | 325 |
| Cash flow from oper (a) | 9,280 | 10,368 | 11,401 | 14,910 | 18,450 |
| Capital Expenditure | (2,554) | (4,459) | (10,000) | (10,000) | (6,000) |
| Chg in investments | (1,684) | 526 | - | - | - |
| Other investing activities | - | - | - | - | - |
| Cash flow from inv.(b) | (4,237) | (3,933) | (10,000) | (10,000) | (6,000) |
| Free cash flow (a+b) | 5,043 | 6,435 | 1,401 | 4,910 | 12,450 |
| Equity raised/(repaid) | - | - | - | - | - |
| Debt raised/(repaid) | - | - | 5,000 | 1,500 | - |
| Interest paid | (14) | (11) | (125) | (288) | (325) |
| Dividend (incl. Tax) | (4,624) | (4,654) | (5,307) | (6,273) | (7,756) |
| Other financing activities | (787) | (774) | (876) | (1,036) | (1,281) |
| Cash flow from fin. (c) | (5,424) | (5,438) | (1,308) | (6,096) | (9,362) |
| Net chg in cash (a+b+c) | (381) | 997 | 93 | (1,186) | 3,088 |

| Balance Sheet | CY09 | CY10 | CY11E | CY12E | CY13E |
|--------------------------|---------|---------|---------|---------|----------|
| Equity Share Capital | 964 | 964 | 964 | 964 | 964 |
| Reserves & surplus | 4,848 | 7,590 | 11,056 | 15,152 | 20,218 |
| Shareholders' funds | 5,813 | 8,554 | 12,020 | 16,116 | 21,182 |
| Total Debt | - | - | 5,000 | 6,500 | 6,500 |
| Capital Employed | 5,813 | 8,554 | 17,020 | 22,616 | 27,682 |
| Net fixed assets | 9,758 | 13,616 | 22,094 | 29,950 | 33,207 |
| Cash & Cash Eq. | 1,555 | 2,553 | 2,646 | 1,460 | 4,548 |
| Net Other current assets | (7,212) | (8,789) | (8,769) | (9,717) | (10,871) |
| Investments | 2,032 | 1,505 | 1,505 | 1,505 | 1,505 |
| Misc Exp not written off | - | - | - | - | - |
| Net Deferred tax Assets | (320) | (333) | (458) | (583) | (708) |
| Total Assets | 5,813 | 8,554 | 17,020 | 22,616 | 27,682 |

| Key Ratios | CY09 | CY10 | CY11E | CY12E | CY13E |
|----------------------------|--------|--------|--------|--------|--------|
| OPM (%) | 20.3 | 20.1 | 19.8 | 19.5 | 19.2 |
| Net Margin (%) | 12.8 | 13.1 | 12.6 | 12.1 | 12.0 |
| Div. Yield (%) | 1.2 | 1.2 | 1.4 | 1.7 | 2.0 |
| Net debt/Equity (x) | (0.3) | (0.3) | 0.2 | 0.3 | 0.1 |
| Net Working Capital (days) | (51.2) | (51.2) | (41.8) | (37.6) | (33.9) |
| ROCE (%) | 179.7 | 146.8 | 88.9 | 81.4 | 81.0 |
| RoE (%) | 113.1 | 95.7 | 80.3 | 70.8 | 66.6 |
| EV/Net Sales (x) | 7.7 | 6.3 | 5.2 | 4.3 | 3.4 |
| EV/EBITDA (x) | 37.9 | 31.5 | 26.5 | 21.9 | 17.8 |
| PER (x) | 60.8 | 48.8 | 41.4 | 35.0 | 28.3 |
| PCE (x) | 52.0 | 42.2 | 35.8 | 29.5 | 23.7 |
| Price/Book (x) | 68.7 | 46.7 | 33.2 | 24.8 | 18.9 |



| Key Assumptions | CY09 | CY10 | CY11E | CY12E | CY13E |
|-----------------------|------|------|-------|-------|-------|
| Sales Gr.% | 18.8 | 21.8 | 22.3 | 23.2 | 24.1 |
| Volume Gr.% | 14.9 | 17.0 | 18.6 | 19.7 | 20.4 |
| Gross Margin % | 52.4 | 51.2 | 51.2 | 51.1 | 50.8 |
| SG&A (% of net Sales) | 16.9 | 17.0 | 17.3 | 17.7 | 18.0 |
| EBITDA Margin % | 20.3 | 20.1 | 19.8 | 19.5 | 19.2 |
| Effective tax rate % | 28.6 | 28.5 | 29.5 | 29.5 | 28.5 |
| DPS (Rs) | 48.5 | 48.5 | 58.2 | 69.8 | 83.8 |
| | | | | | |
| | | | | | |
| | | | | | |
| | | | | | |

Company Update
 Sector: FMCG
 BSE Sensex: 15,868

DABUR INDIA

 Maintain ACCUMULATE
 CMP Rs99
 TP Rs109

09 January 2012

Valuations factors near term worry

Dabur India's (Dabur) rural segment is facing slowdown which impacted its H1FY12 performance. Consolidated net sales shown robust 31% growth led by recent acquisitions (Hobi Kozmetic and Namaste Group), excluding the same, sales grew at a slower pace of 13% during H1FY12. Profitability was also subdued on account of input price pressure and higher sales contribution from low EBITDA margin acquisitions.

We expect softening of input prices along with better rural traction would improve the performance going forward. We expect net sales and net earnings to show 17% and 19% CAGR during FY11-14E. We maintain our ACCUMULATE rating with TP of Rs109.

Domestic business slowing down

Dabur's domestic business (68% of sales) displayed mere ~12% growth during H1FY12 and impacted overall performance. Hair oil and food categories were the exception and clocked strong growth of 21% and 30% during H1FY12. While skin care, health supplement, oral care and home care displayed muted growth of 7%, 4%, 9% and 10% growth respectively during H1FY12. Shampoo business could not recover due to sharp shampoo price cut by its peers and posted 24% decline in H1FY12.

International business growth sustainable

Dabur's international business (excluding recent acquisitions) displayed 18% growth in H1FY12 which was lower as compared to past three years' >25% history. GCC, Egypt and Nigeria continue to perform well and registered 27%, 27% and 36% growth during H1FY12 respectively.

EBITDA margin to be lower

We expect EBITDA margin during FY12-14E would be lower than FY10-11 as we believe higher contribution of low margin acquisitions. Hobi Kozmetic and Namaste Group fetch low profitability profile which would change the overall profitability profile of the company. We expect Hobi and Namaste would combined contribute 13% and 10% of consolidated sales and EBITDA of FY14.

VALUATIONS AND RECOMMENDATION

Dabur's strong presence in the domestic market through its robust portfolio and regular entrance in geographies enabled it to maintain its high growth momentum. We retain our 25x multiple on 12-month forward earnings and derive TP of Rs109 (earlier Rs107). We maintain our 'ACCUMULATE' rating on the stock.

KEY FINANCIALS (CONSOLIDATED)

| | (Rs mn) | | | | |
|-----------------|---------|--------|--------|--------|--------|
| | FY10 | FY11 | FY12E | FY13E | FY14E |
| Net Sales | 34,056 | 40,962 | 51,672 | 59,628 | 69,055 |
| YoY Gr. (%) | 20.8 | 20.3 | 26.1 | 15.4 | 15.8 |
| Op. Profits | 6,383 | 7,544 | 8,766 | 10,297 | 12,144 |
| OPM (%) | 18.7 | 18.4 | 17.0 | 17.3 | 17.6 |
| Adj. Net Profit | 4,904 | 5,688 | 6,507 | 7,935 | 9,560 |
| YoY Gr. (%) | 31.6 | 16.0 | 14.4 | 21.9 | 20.5 |

KEY RATIOS

| | | | | | |
|---------------|------|------|------|------|------|
| Dil EPS (Rs) | 2.8 | 3.3 | 3.7 | 4.6 | 5.5 |
| ROCE (%) | 55.5 | 30.2 | 33.4 | 34.9 | 35.2 |
| RONW (%) | 52.4 | 40.9 | 35.4 | 32.7 | 30.1 |
| P/E (x) | 35.1 | 30.3 | 26.5 | 21.7 | 18.0 |
| EV/Sales (x) | 5.0 | 4.3 | 3.4 | 2.9 | 2.4 |
| EV/EBITDA (x) | 26.6 | 23.3 | 19.7 | 16.5 | 13.7 |

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STOCK DATA

| | |
|-----------------------------|----------|
| Market cap | Rs172bn |
| Book Value per share | Rs8 |
| Shares O/S (F.V. Rs1) | 1,741mn |
| Free Float | 31% |
| Avg. Trade Value (6 months) | Rs125mn |
| 52 week High/Low | Rs122/87 |
| Bloomberg Code | DABUR IN |
| Reuters Code | DABU.BO |

PERFORMANCE (%)

| | 1M | 3M | 12M |
|----------|------|-------|-------|
| Absolute | 5.8 | (0.7) | (2.0) |
| Relative | 11.8 | (1.2) | 26.0 |

RELATIVE PERFORMANCE

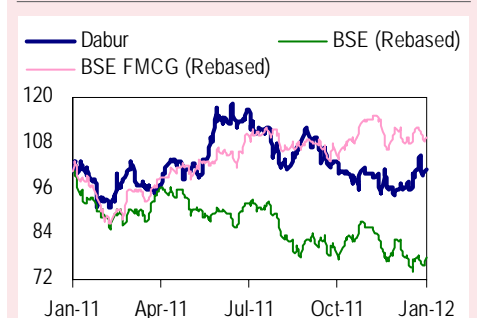


Exhibit 1 - Contribution of Hobi Kozmetic and Namaste Group

| Particular (Rs mn) | FY12E | FY13E | FY14E | PINC Comments |
|---|---------------|---------------|---------------|---|
| Revenue | | | | |
| Sales Ex Hobi & Namaste | 44,958 | 51,849 | 60,127 | |
| YoY Gr% | 14.2% | 15.3% | 16.0% | |
| Hobi Sales (Rs mn) | 1,439 | 1,591 | 1,782 | Launch of products in domestic market and higher traction in MENA and Africa regions would enable it to maintain high growth momentum |
| YoY Gr% | 7.8% | 10.5% | 12.0% | |
| Namaste (Rs mn) | 5,275 | 6,188 | 7,147 | Focus on Africa business would result in higher sales growth, long term plans are very strong |
| YoY Gr% | 18.0% | 17.3% | 15.5% | |
| Total Sales | 51,672 | 59,628 | 69,055 | |
| YoY Gr% | 25.7% | 15.4% | 15.8% | |
| Operating Performance | | | | |
| EBITDA Ex Hobi & Namaste | 7,899 | 9,270 | 10,947 | |
| EBITDA Margin % | 17.6% | 17.9% | 18.2% | |
| Hobi EBITDA | 151 | 169 | 196 | |
| EBITDA Margin % | 10.5% | 10.6% | 11.0% | |
| Namaste EBITDA | 717 | 857 | 1,001 | |
| EBITDA Margin % | 13.6% | 13.9% | 14.0% | We expect slight improvement in the profitability through better operational management |
| Total EBITDA | 8,766 | 10,297 | 12,144 | |
| Consolidated EBITDA Margin % | 17.0% | 17.3% | 17.6% | |
| Sales contribution by Hobi and Namaste % | 13.0% | 13.0% | 12.9% | |
| EBITDA contribution by Hobi and Namaste % | 9.9% | 10.0% | 9.9% | |

Source: PINC Research, Company

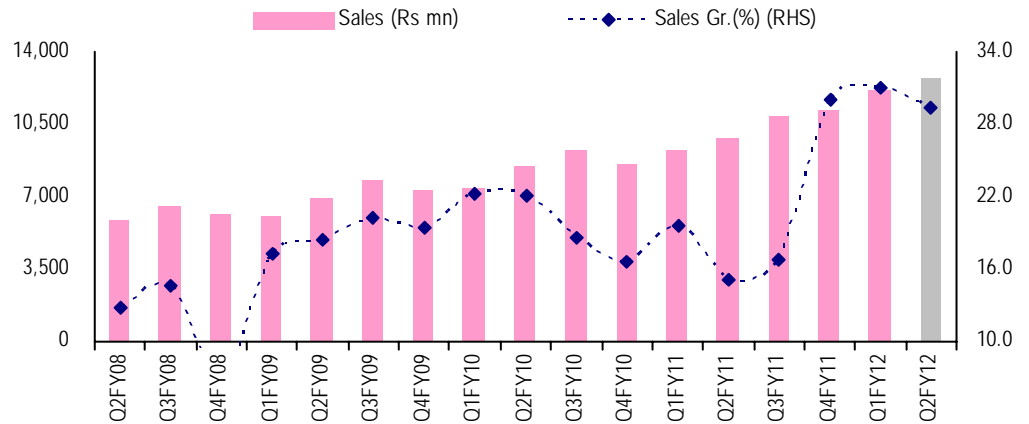
Exhibit 2 - H1FY12 Earning Summary (Rs mn)

| Quarter Ended (Rs mn) | Q2FY11 | Q2FY12 | YoY Gr% | Q1FY12 | QoQ Gr% | H1FY11 | H1FY12 | YoY Gr% | PINC Comments |
|-----------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---|
| Net Sales | 9,728 | 12,623 | 29.8 | 12,046 | 4.8 | 18,893 | 24,669 | 30.6 | Excluding sales of Hobi Kozmetic and Namaste, net sales grew by 13% during Q2FY12 |
| YoY Gr% | 14.7% | 29.8% | | 31.4% | | 16.9% | 30.6% | | |
| Other Operating Income | 101 | 84 | (17.0) | 80 | 4.9 | 187 | 163 | (12.7) | |
| Total Income | 9,828 | 12,707 | 29.3 | 12,125 | 4.8 | 19,079 | 24,832 | 30.2 | |
| YoY Gr% | 15.1% | 29.3% | | 31.1% | | 17.3% | 30.2% | | |
| Total RM | 4,585 | 6,309 | 37.6 | 6,290 | 0.3 | 8,931 | 12,599 | 41.1 | Input price pressure continued during both the quarters |
| YoY Gr% | 20.1% | 37.6% | | 44.7% | | 20.0% | 41.1% | | |
| Gross Profit | 5,244 | 6,398 | 22.0 | 5,836 | 9.6 | 10,148 | 12,233 | 20.5 | |
| YoY Gr% | 11.0% | 22.0% | | 19.0% | | 14.9% | 20.5% | | |
| Gross Margin (%) | 53.4% | 50.3% | -300bps | 48.1% | 222bps | 53.2% | 49.3% | -393bps | RM growth was higher than our expectation and resulted in gross margin decline |
| YoY Expansion (bps) | -195bps | -300bps | | -489bps | | -108bps | -393bps | | |
| Employee Expenses | 779 | 1,014 | 30.3 | 951 | 6.6 | 1,506 | 1,965 | 30.5 | Maintained at ~8% of sales |
| YoY Gr% | 7.8% | 30.3% | | 30.7% | | 10.9% | 30.5% | | |
| % of sales | 7.9% | 8.0% | 6bps | 7.8% | 14bps | 7.9% | 7.9% | 2bps | |
| Expansion (bps) | -54bps | 6bps | | -2bps | | -46bps | 2bps | | |
| Advertisement and publicity | 1,215 | 1,278 | 5.1 | 1,515 | (15.7) | 2,722 | 2,792 | 2.6 | A substantial cut down in SG&A was to protect the profitability |
| YoY Gr% | 1.1% | 5.1% | | 0.5% | | 12.1% | 2.6% | | |
| % of sales | 12.4% | 10.1% | -231bps | 12.5% | -244bps | 14.3% | 11.2% | -302bps | |
| Expansion (bps) | -170bps | -231bps | | -380bps | | -65bps | -302bps | | |
| Provisions & Write Offs | 47 | 42 | (10.8) | 57 | (25.7) | 57 | 99 | 73.0 | |
| YoY Gr% | 230.1% | -10.8% | | 472.7% | | 108.4% | 73.0% | | |
| % of sales | 0.5% | 0.3% | -15bps | 0.5% | -14bps | 0.3% | 0.4% | 10bps | |
| Other Expenses | 1,121 | 1,657 | 47.8 | 1,583 | 4.7 | 2,337 | 3,239 | 38.6 | Were stable at 13% of sales |
| YoY Gr% | 13.9% | 47.8% | | 30.1% | | 15.6% | 38.6% | | |
| % of sales | 11.4% | 13.0% | 163bps | 13.1% | -1bps | 12.2% | 13.0% | 79bps | |
| Expansion (bps) | -12bps | 163bps | | -10bps | | -17bps | 79bps | | |
| Total Expenditures | 7,747 | 10,300 | 33.0 | 10,395 | (0.9) | 15,554 | 20,695 | 33.1 | |
| EBITDA | 2,082 | 2,407 | 15.6 | 1,731 | 39.1 | 3,526 | 4,138 | 17.4 | |
| YoY Gr% | 15.6% | 15.6% | | 19.9% | | 17.7% | 17.4% | | |
| EBITDA Margin % | 21.2% | 18.9% | -224bps | 14.3% | 467bps | 18.5% | 16.7% | -182bps | EBITDA margin were better than our expectation |
| YoY Expansion (bps) | 9bps | -224bps | | -133bps | | 7bps | -182bps | | |
| Other Income | 67 | 106 | 58.1 | 151 | (30.2) | 102 | 257 | 150.9 | |
| Depreciation | 142 | 175 | 23.0 | 154 | 13.8 | 277 | 329 | 18.7 | Acquisition impact |
| EBIT | 2,006 | 2,338 | 16.5 | 1,728 | 35.3 | 3,351 | 4,066 | 21.3 | |
| YoY Gr% | 14.7% | 16.5% | | 28.5% | | 17.2% | 21.3% | | |
| EBIT Margin % | 20.4% | 18.4% | -202bps | 14.3% | 415bps | 17.6% | 16.4% | -119bps | |
| Interest | 46 | 172 | 274.7 | 126 | 36.2 | 54 | 298 | 455.5 | Large debt in books to acquire Hobi and Namaste |
| PBT | 1,960 | 2,166 | 10.5 | 1,602 | 35.2 | 3,297 | 3,767 | 14.3 | |
| Total Tax | 356 | 427 | 20.0 | 323 | 32.4 | 619 | 750 | 21.1 | |
| Effective tax rate % | 18.2% | 19.7% | 156bps | 20.1% | -41bps | 18.8% | 19.9% | 113bps | Met the year guidance |
| Reported PAT | 1,604 | 1,739 | 8.4 | 1,279 | 35.9 | 2,671 | 3,018 | 13.0 | |
| YoY Gr% | 15.4% | 8.4% | | 19.8% | | 16.9% | 13.0% | | |
| Diluted EPS (Adjusted) | 0.92 | 1.00 | 8.4 | 0.73 | 35.9 | 1.53 | 1.73 | 13.0 | |
| YoY Gr% | 14.8% | 8.4% | | 19.8% | | 16.3% | 13.0% | | |

Source: PINC Research, Company

Exhibit 3 - Quarterly Sales and Sales Growth

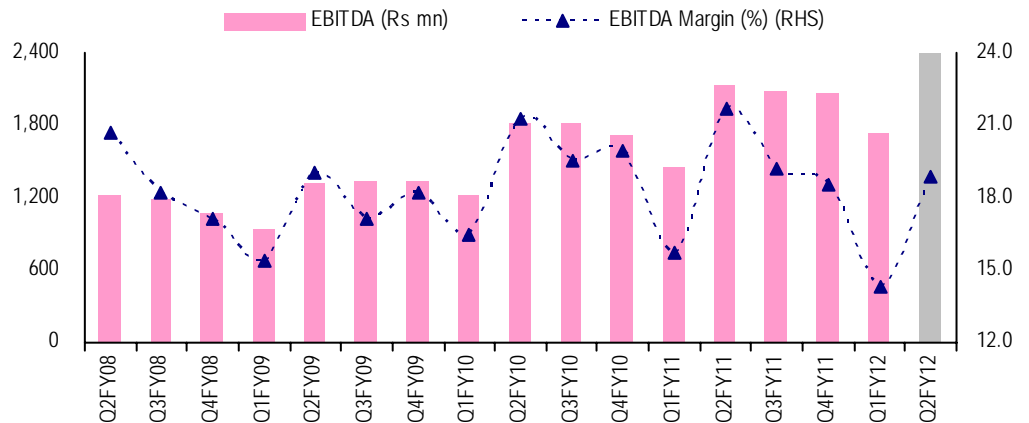
Dabur has consistently improved the size through organic and inorganic route...



Source: Company, PINC Research

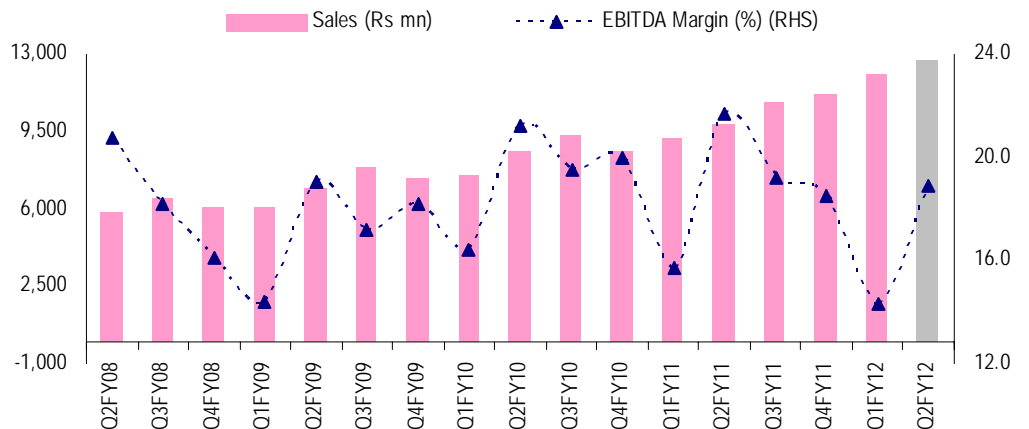
Exhibit 4 - EBITDA and EBITDA Margin

Lowest EBITDA margin in past 20 quarters...



Source: Company, PINC Research

Exhibit 5 - Sales and EBITDA performance



Source: Company, PINC Research

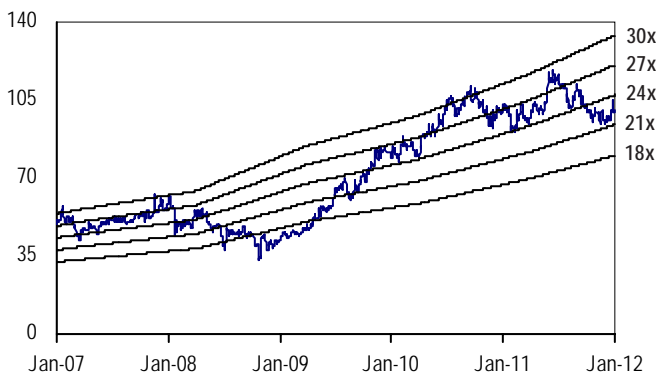
| Income Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|------------------------|---------------|---------------|---------------|---------------|---------------|
| Net Sales | 33,914 | 40,774 | 51,415 | 59,331 | 68,712 |
| Growth (%) | 20.9 | 20.2 | 26.1 | 15.4 | 15.8 |
| Other operating income | 142 | 187 | 257 | 297 | 344 |
| Total Revenue | 34,056 | 40,962 | 51,672 | 59,628 | 69,055 |
| YoY Gr% | 20.8 | 20.3 | 26.1 | 15.4 | 15.8 |
| EBITDA | 6,383 | 7,544 | 8,766 | 10,297 | 12,144 |
| YoY Gr% | 32.9 | 18.2 | 16.2 | 17.5 | 17.9 |
| Other Income | 331 | 465 | 611 | 725 | 800 |
| Depreciation | 503 | 624 | 719 | 817 | 916 |
| Interest | 202 | 303 | 521 | 281 | 73 |
| PBT | 6,009 | 7,081 | 8,138 | 9,923 | 11,954 |
| Total tax | 1,005 | 1,390 | 1,628 | 1,985 | 2,391 |
| Minority Interest | (8) | 3 | 3 | 3 | 3 |
| Reported PAT | 5,013 | 5,688 | 6,507 | 7,935 | 9,560 |
| Adjusted PAT | 4,904 | 5,688 | 6,507 | 7,935 | 9,560 |
| YoY Gr% | 31.6 | 16.0 | 14.4 | 21.9 | 20.5 |
| Diluted EPS | 2.8 | 3.3 | 3.7 | 4.6 | 5.5 |
| YoY Gr% | 31.6 | 16.0 | 14.4 | 21.9 | 20.5 |

| Cash Flow Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|---------------------------------|----------------|-----------------|----------------|----------------|----------------|
| Pre-tax profit | 6,009 | 7,079 | 8,138 | 9,923 | 11,954 |
| Depreciation | 503 | 624 | 719 | 817 | 916 |
| Total tax paid | (1,045) | (1,250) | (1,628) | (1,985) | (2,391) |
| Chg in working capital | (394) | (1,346) | (485) | (2,461) | (2,713) |
| Other operating activities | (84) | (96) | - | - | - |
| Cash flow from oper. (a) | 4,989 | 5,011 | 6,744 | 6,295 | 7,767 |
| Capital expenditure | (1,340) | (9,260) | (1,850) | (1,850) | (1,850) |
| Chg in investments | (1,041) | (1,538) | - | - | - |
| Other investing activities | 79 | 158 | - | - | - |
| Cash flow from inv. (b) | (2,302) | (10,640) | (1,850) | (1,850) | (1,850) |
| Free cash flow (a+b) | 2,687 | (5,628) | 4,894 | 4,445 | 5,917 |
| Equity raised/(repaid) | 3 | 1 | 0 | 0 | (0) |
| Debt raised/(repaid) | (556) | 8,705 | (3,000) | (2,600) | (2,600) |
| Chg in Minorities int. | - | - | - | - | - |
| Dividend (incl. tax) | (1,520) | (1,952) | (2,037) | (2,037) | (2,037) |
| Other financing activities | (257) | (325) | - | - | - |
| Cash flow from fin. (c) | (2,331) | 6,430 | (5,037) | (4,637) | (4,637) |
| Net chg in cash (a+b+c) | 357 | 801 | (142) | (192) | 1,280 |

| Balance Sheet | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|---------------|---------------|---------------|---------------|---------------|
| Equity capital | 869 | 1,741 | 1,741 | 1,741 | 1,741 |
| Reserves & surplus | 8,485 | 12,170 | 16,641 | 22,540 | 30,063 |
| Shareholders' funds | 9,354 | 13,911 | 18,382 | 24,280 | 31,804 |
| Minorities interests | 38 | 41 | 44 | 47 | 50 |
| Total Debt | 1,793 | 10,510 | 7,510 | 4,910 | 2,310 |
| Capital Employed | 11,185 | 24,462 | 25,936 | 29,238 | 34,165 |
| Net fixed assets | 6,767 | 15,417 | 16,548 | 17,581 | 18,515 |
| Cash & Cash Eq. | 1,923 | 2,720 | 2,759 | 2,567 | 3,847 |
| Net other Current Assets | (68) | 1,230 | 1,715 | 4,176 | 6,889 |
| Investments | 2,641 | 4,274 | 4,274 | 4,274 | 4,274 |
| Net Deferred Tax Assets | (107) | (190) | (190) | (190) | (190) |
| Total assets | 11,185 | 24,462 | 25,936 | 29,238 | 34,165 |

| Key Ratios | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|-------|------|-------|-------|-------|
| OPM (%) | 18.7 | 18.4 | 17.0 | 17.3 | 17.6 |
| Net margin (%) | 14.4 | 13.9 | 12.6 | 13.3 | 13.8 |
| Dividend yield (%) | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 |
| Net debt/Equity (x) | (0.0) | 0.6 | 0.3 | 0.1 | (0.0) |
| Net Working Capital (days) | (0.7) | 11.0 | 12.2 | 25.7 | 36.6 |
| ROCE (%) | 55.5 | 30.2 | 33.4 | 34.9 | 35.2 |
| RoE (%) | 52.4 | 40.9 | 35.4 | 32.7 | 30.1 |
| EV/Net sales (x) | 5.0 | 4.3 | 3.4 | 2.9 | 2.4 |
| EV/EBITDA (x) | 26.6 | 23.3 | 19.7 | 16.5 | 13.7 |
| PER (x) | 35.1 | 30.3 | 26.5 | 21.7 | 18.0 |
| PCE (x) | 31.9 | 27.3 | 23.8 | 19.7 | 16.4 |
| Price/Book (x) | 18.4 | 12.4 | 9.4 | 7.1 | 5.4 |

P/E Band



Key Assumptions

| | FY11 | FY12E | FY13E | FY14E |
|-------------------------------|--------|---------|-------|-------|
| Sales Gr% | 20.3 | 26.0 | 15.6 | 15.8 |
| Gross Margin % | 53.5 | 50.4 | 52.2 | 52.8 |
| Packing cost (% of net sales) | 16.4 | 16.8 | 16.5 | 16.1 |
| EBITDA margin expansion (bps) | -33bps | -153bps | 38bps | 32bps |
| Effective tax rate (%) | 19.6 | 20.0 | 20.0 | 20.0 |

Company Update
 Sector: FMCG
 BSE Sensex: 15,868

COLGATE-PALMOLIVE (INDIA)

 Upgrade REDUCE
 CMP Rs981
 TP Rs937

09 January 2012

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Towards market share gain

Colgate's H1FY12 performance was a mixed bag as sales growth was better than our expectation while profitability was under pressure. Colgate maintained volume growth at ~12.5% during H1FY12 although it took price hike on most of the brands. Average price growth in H1FY12 was ~5% v/s flat growth in H1FY11 and 2.5% growth in H1FY10. Colgate's A&P spending was higher than our expectation and that impacted the H1FY12 performance. We believe higher A&P spending was to gain the market share as most of the players cut down A&P expense to protect their profitability.

We believe oral care industry is set for premiumisation and better realisation growth is expected in FY13 and FY14. However, to maintain the healthy volume growth, we expect Colgate's A&P spending would continue to be high in FY13 and FY14. We increase our target multiple from 24x to 25x on 12-month forward earnings as Colgate's aggressive marketing efforts would further strengthen its position in the oral care industry. We raise our TP to Rs937 (earlier Rs878) and upgrade our recommendation to 'REDUCE' from 'SELL'.

Oral care market is set for premiumisation

In our sector thesis we mentioned that oral care is one of the personal categories which also has low weightage in the monthly household budget therefore its price sensitivity is low. We also witnessed this thesis in Colgate's H1FY12 performance in which volume growth was maintained despite taking price hike on most of the brands. We expect better price growth in FY13 and FY14.

High A&P spend

Colgate is the only company in FMCG space increase in A&P spent in H1FY12 while most of the other players were protecting profitability through lower A&P spends. Colgate's aggression was to expand its market share as well as to promote sensitive oral care segment. We believe Colgate would continue to spend high on A&P in FY13 and FY14 to maintain its double digit volume growth.

VALUATIONS AND RECOMMENDATION

We expect volume growth to sustain owing to Colgate's regular product launches, higher rural focus and continued dental awareness programmes. We increase our target multiple from 24x to 25x on 12-month forward earnings and arrive at a TP of Rs937 (earlier Rs878). We upgrade our recommendation to 'REDUCE' from 'SELL'.

KEY FINANCIALS

| | (Rs mn) | | | | |
|-----------------|---------|--------|--------|--------|--------|
| | FY10 | FY11 | FY12E | FY13E | FY14E |
| Net Sales | 20,173 | 22,847 | 26,739 | 31,276 | 36,130 |
| YoY Gr. (%) | 15.4 | 13.3 | 17.0 | 17.0 | 15.5 |
| Op. Profits | 4,803 | 5,148 | 5,857 | 7,049 | 8,188 |
| OPM (%) | 23.8 | 22.5 | 21.9 | 22.5 | 22.7 |
| Adj. Net Profit | 4,039 | 4,026 | 4,449 | 5,244 | 6,072 |
| YoY Gr. (%) | 38.3 | (0.3) | 10.5 | 17.9 | 15.8 |

KEY RATIOS

| | | | | | |
|---------------|-------|-------|-------|-------|-------|
| Dil EPS (Rs) | 29.7 | 29.6 | 32.7 | 38.6 | 44.7 |
| ROCE (%) | 145.2 | 134.0 | 135.8 | 138.2 | 131.2 |
| RONW (%) | 123.8 | 104.8 | 103.2 | 102.8 | 97.3 |
| P/E (x) | 33.0 | 33.1 | 30.0 | 25.4 | 22.0 |
| EV/Sales (x) | 6.4 | 5.6 | 4.8 | 4.0 | 3.5 |
| EV/EBITDA (x) | 27.0 | 25.1 | 21.8 | 18.0 | 15.2 |

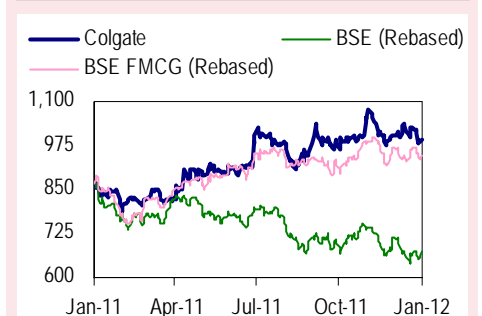
STOCK DATA

| | |
|-----------------------------|-------------|
| Market cap | Rs133bn |
| Book Value per share | Rs24 |
| Shares O/S (F.V. Rs1) | 136mn |
| Free Float | 49.0% |
| Avg. Trade Value (6 months) | Rs79mn |
| 52 week High/Low | Rs1,084/783 |
| Bloomberg Code | CLGTIN |
| Reuters Code | COLG.BO |

PERFORMANCE (%)

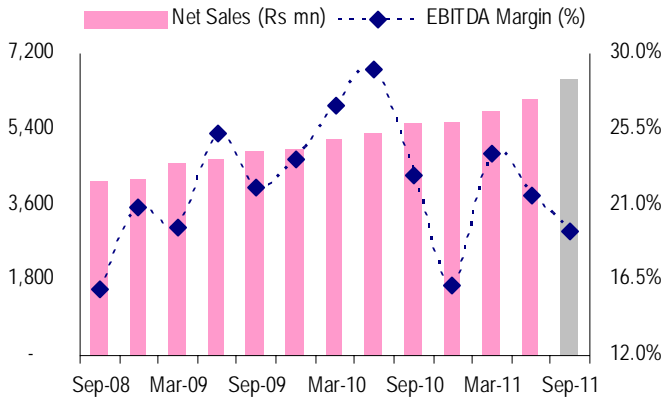
| | 1M | 3M | 12M |
|----------|-------|-----|------|
| Absolute | (1.0) | 0.6 | 13.9 |
| Relative | 4.7 | 0.2 | 46.5 |

RELATIVE PERFORMANCE



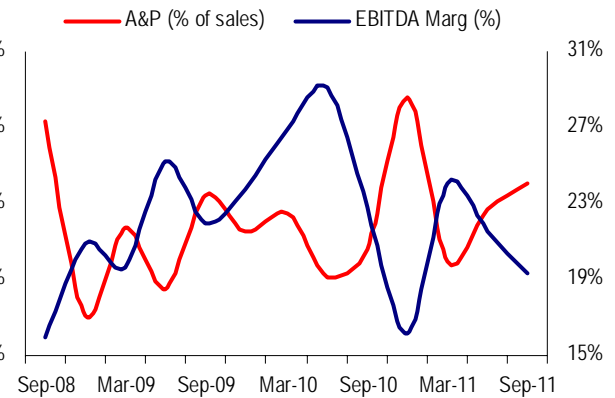
- Sales growth was healthy in H1FY12 while EBITDA margin was under pressure on higher RM cost and A&P spending.
- Colgate's A&P spending is higher than peers therefore we witnessed high volatility in quarterly EBITDA margin with the change in A&P spends.

Exhibit 1 - Net Sales (Rs mn) and EBITDA Margin (%)



Source: PINC Research, Company

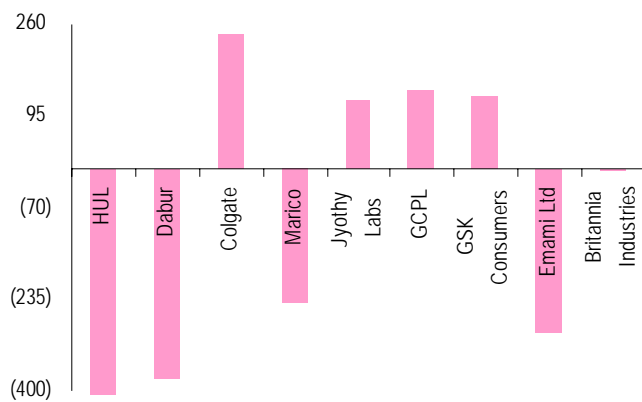
Exhibit 2 - A&P Spend and EBITDA Margin



Source: PINC Research, Company

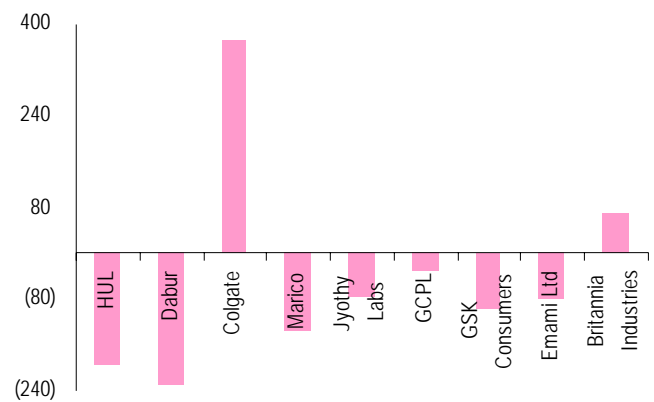
- Higher A&P spending was to gain the market share as most of the players cut down A&P expense to protect their profitability.

Exhibit 3 - Change in A&P Spending in Q1FY12



Source: PINC Research, Company

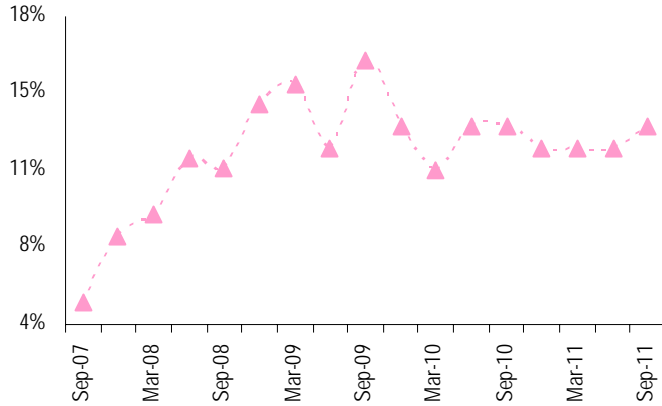
Exhibit 4 - Change in A&P Spending in Q2FY12



Source: PINC Research, Company

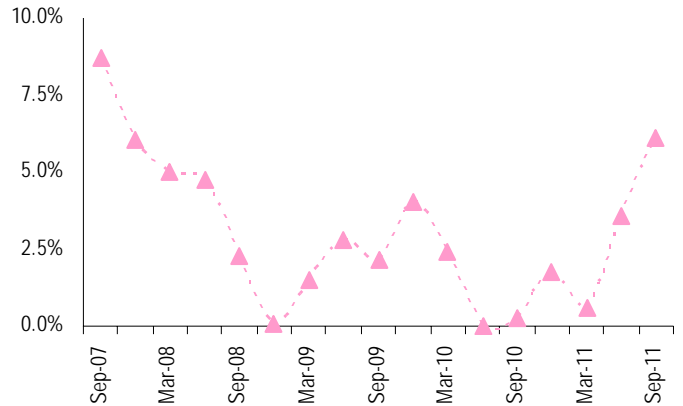
- Colgate maintained healthy volume growth in H1FY12 although it took price hike on most of the brands.

Exhibit 5 - Volume Growth (%)



Source: PINC Research, Company

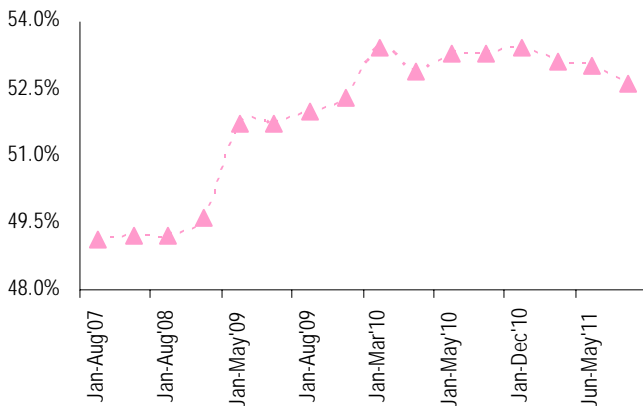
Exhibit 6 - Realisation Growth (%)



Source: PINC Research, Company

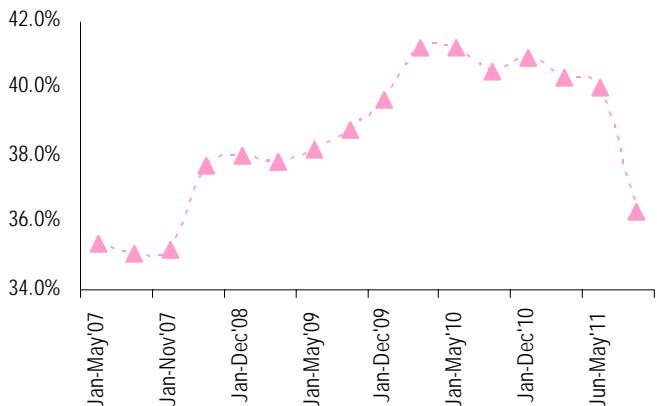
- Regular product launches couple with aggressive field level marketing has resulted into consistent improvement in volume market share.
- Colgate reported sharp decline in toothbrush market share Q2FY12.

Exhibit 7 - Toothpaste Volume Market Share



Source: PINC Research, Company

Exhibit 8 - Toothbrush Volume Market Share



Source: PINC Research, Company

Exhibit 9 - Toothpaste MRPs

| Brands | Unit | Qty | MRP | MRP/unit |
|------------------------------|------|-----|-----|----------|
| Colgate Sensitive Pro Relief | gm | 80 | 120 | 1.50 |
| Colgate Sensitive Original | gm | 80 | 80 | 1.00 |
| Colgate Total | gm | 150 | 82 | 0.55 |
| Colgate Max White | gm | 150 | 65 | 0.43 |
| Colgate Max Fresh | gm | 150 | 62 | 0.41 |
| Colgate Active Salt | gm | 100 | 35 | 0.35 |
| Colgate Dental Cream | gm | 200 | 62 | 0.31 |
| Colgate Herbal | gm | 200 | 58 | 0.29 |
| Colgate Cibaca | gm | 200 | 35 | 0.18 |

Source: PINC Research, Retail Market Dec'2011

Exhibit 10 - H1FY12 Earning Summary (Rs mn)

| Quarter Ended (Rs in Mn.) | Sep-10 | Sep-11 | YoY Gr % | Jun-11 | QoQ Gr% | H1FY11 | H1FY12 | YoY Gr % | PINC Comments |
|---------------------------|--------------|--------------|--------------|--------------|--------------|---------------|---------------|--------------|--|
| Net Sales | 5,518 | 6,572 | 19.1 | 6,111 | 7.6 | 10,806 | 12,683 | 17.4 | On the back of ~13% volume and 6% price growth |
| Operating income | 175 | 183 | 4.5 | 183 | 0.2 | 384 | 366 | (4.8) | |
| Total Revenue | 5,693 | 6,755 | 18.7 | 6,294 | 7.3 | 11,190 | 13,049 | 16.6 | |
| Expenditures | | | | | | | | | |
| RM cost | 2,201 | 2,637 | 19.8 | 2,467 | 6.9 | 4,168 | 5,103 | 22.4 | |
| Gross Profit | 3,491 | 4,119 | 18.0 | 3,827 | 7.6 | 7,022 | 7,946 | 13.2 | |
| Gross Profit Margin (%) | 61.3% | 61.0% | -36bps | 60.8% | 16bps | 62.8% | 60.9% | -186bps | |
| Employees Cost | 533 | 605 | 13.5 | 498 | 21.5 | 977 | 1,104 | 12.9 | Also includes VRS cost of Rs82mn |
| A&P expense | 789 | 1,143 | 44.8 | 988 | 15.7 | 1,483 | 2,131 | 43.7 | Launch of new products along with focus on premium products required higher spending on branding |
| Other Expenditure | 872 | 1,063 | 21.8 | 985 | 7.8 | 1,667 | 2,048 | 22.8 | |
| EBITDA | 1,297 | 1,308 | 0.9 | 1,356 | (3.5) | 2,895 | 2,664 | (8.0) | |
| EBITDA Margin (%) | 22.8% | 19.4% | -341bps | 21.5% | -218bps | 25.9% | 20.4% | -546bps | |
| Adjusted EBITDA | 1,297 | 1,390 | 7.2 | 1,356 | 2.6 | 2,895 | 2,664 | (8.0) | Excluding one time VRS cost of Rs82mn |
| Adj. EBITDA Margin (%) | 22.8% | 20.6% | -220bps | 21.5% | -96bps | 25.9% | 20.4% | -546bps | Operating performance was under pressure |
| Other Income | 81 | 95 | 16.8 | 120 | (21.0) | 135 | 215 | 58.9 | |
| Depreciation | 84 | 106 | 25.8 | 88 | 20.1 | 163 | 194 | 18.5 | |
| EBIT | 1,294 | 1,297 | 0.3 | 1,387 | (6.5) | 2,866 | 2,685 | (6.3) | |
| EBIT Margin % | 22.7% | 19.2% | -352bps | 22.0% | -284bps | 25.6% | 20.6% | -504bps | |
| Interest | 6 | 8 | 23.0 | 6 | 23.0 | 10 | 14 | 43.2 | |
| PBT | 1,288 | 1,290 | 0.2 | 1,381 | (6.6) | 2,857 | 2,671 | (6.5) | |
| Tax | 285 | 293 | 2.8 | 377 | (22.4) | 635 | 670 | 5.4 | |
| Effective tax rate % | 22.1% | 22.7% | 59bps | 27.3% | -460bps | 22.2% | 25.1% | 284bps | Effective tax rate was lower than our expectation of 27%, however, we maintain our full year effective tax rate at 27% |
| Reported PAT | 1,003 | 997 | (0.6) | 1,004 | (0.7) | 2,222 | 2,001 | (9.9) | |
| Adjusted PAT | 1,003 | 1,065 | 6.2 | 1,004 | 6.1 | 2,222 | 2,070 | (6.9) | Excluding one time VRS cost (net of taxes) |
| EPS (adjusted) | 7.4 | 7.8 | 6.2 | 7.4 | 6.1 | 16.3 | 15.2 | (6.9) | |

Source: PINC Research, Company

Exhibit 11 - Expenditure Breakup (%)

| Expenditure (% of net sales) | Sep-10 | Sep-11 | YoY Gr % | Jun-11 | QoQ Gr% | H1FY11 | H1FY12 | YoY Gr % | PINC Comments |
|--|--------------|--------------|---------------|--------------|---------------|--------------|--------------|---------------|--|
| Total expenditures | 77.2% | 80.6% | 341bps | 78.5% | 218bps | 74.1% | 79.6% | 546bps | |
| Consumption of raw materials | 38.7% | 39.0% | 36bps | 39.2% | -16bps | 37.2% | 39.1% | 186bps | |
| Other Expenditure | 15.3% | 15.7% | 41bps | 15.7% | 7bps | 14.9% | 15.7% | 80bps | Should sustain between 15.5% to 16% |
| Advertisement & Sales Promotion Expenses | 13.9% | 16.9% | 306bps | 15.7% | 122bps | 13.3% | 16.3% | 308bps | Launch of new products along with focus on premium products required higher spending on branding |
| Employees Cost | 9.4% | 9.0% | -41bps | 7.9% | 104bps | 8.7% | 8.5% | -27bps | |

Source: PINC Research, Company

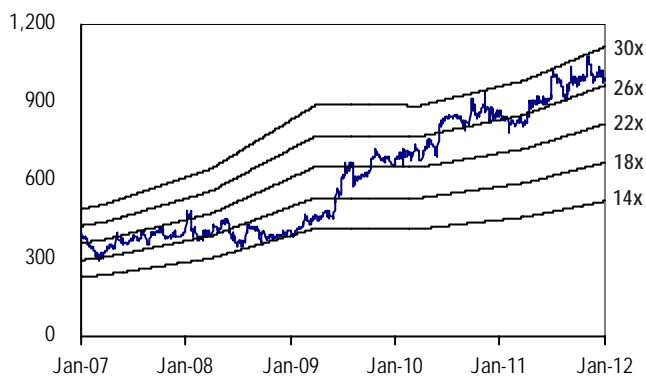
| Income Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|-------------------------------|---------------|---------------|---------------|---------------|---------------|
| Net sales | 19,625 | 22,206 | 25,989 | 30,365 | 35,078 |
| Growth (%) | 15.8 | 13.2 | 17.0 | 16.8 | 15.5 |
| Other Operating Income | 548 | 641 | 750 | 911 | 1,052 |
| Total Income | 20,173 | 22,847 | 26,739 | 31,276 | 36,130 |
| EBITDA | 4,803 | 5,148 | 5,857 | 7,049 | 8,188 |
| Growth (%) | 53.0 | 7.2 | 13.8 | 20.4 | 16.1 |
| Depreciation | 376 | 343 | 350 | 371 | 391 |
| Other Income | 436 | 427 | 589 | 656 | 638 |
| EBIT | 4,863 | 5,232 | 6,095 | 7,335 | 8,434 |
| Interest Paid | 15 | 33 | 0 | 0 | 0 |
| PBT (before E/o items) | 4,848 | 5,199 | 6,095 | 7,334 | 8,434 |
| Tax Provision | 643 | 1,166 | 1,646 | 2,090 | 2,361 |
| E/o income/(loss) | 194 | - | - | - | - |
| Reported PAT | 4,233 | 4,026 | 4,449 | 5,244 | 6,072 |
| Adjusted PAT | 4,039 | 4,026 | 4,449 | 5,244 | 6,072 |
| Growth (%) | 38.3 | (0.3) | 10.5 | 17.9 | 15.8 |
| Diluted EPS (Rs) | 29.7 | 29.6 | 32.7 | 38.6 | 44.7 |
| Diluted EPS Growth (%) | 38.3 | (0.3) | 10.5 | 17.9 | 15.8 |

| Cash Flow Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|--------------------------------|----------------|----------------|----------------|----------------|----------------|
| Pre-tax profit | 5,004 | 5,199 | 6,095 | 7,334 | 8,434 |
| Depreciation | 307 | 342 | 350 | 371 | 391 |
| Total Tax Paid | (799) | (1,042) | (1,646) | (2,090) | (2,361) |
| Chg in working capital | (225) | (321) | 459 | 345 | 391 |
| Other operating activities | (250) | (263) | 0 | 0 | 0 |
| Cash flow from oper (a) | 4,037 | 3,916 | 5,259 | 5,960 | 6,855 |
| Capital Expenditure | (313) | (409) | (150) | (150) | (150) |
| Chg in investments | 119 | (192) | (500) | (500) | (500) |
| Other investing activities | 485 | 455 | - | - | - |
| Cash flow from inv.(b) | 291 | (145) | (650) | (650) | (650) |
| Free cash flow (a+b) | 4,328 | 3,771 | 4,609 | 5,310 | 6,205 |
| Equity raised/(repaid) | - | - | - | - | - |
| Debt raised/(repaid) | (1) | (45) | - | - | - |
| Interest paid | (15) | (16) | (0) | (0) | (0) |
| Dividend (incl. Tax) | (2,879) | (2,716) | (3,978) | (4,455) | (4,932) |
| Other financing activities | (493) | (452) | - | - | - |
| Cash flow from fin. (c) | (3,388) | (3,230) | (3,978) | (4,455) | (4,933) |
| Net chg in cash (a+b+c) | 940 | 541 | 631 | 855 | 1,272 |

| Balance Sheet | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|--------------|--------------|--------------|--------------|--------------|
| Equity Share Capital | 136 | 136 | 136 | 136 | 136 |
| Reserves & surplus | 3,125 | 3,705 | 4,176 | 4,965 | 6,105 |
| Shareholders' funds | 3,261 | 3,841 | 4,312 | 5,101 | 6,241 |
| Minorities interests | - | - | - | - | - |
| Total Debt | 46 | 1 | 1 | 1 | 1 |
| Capital Employed | 3,307 | 3,841 | 4,312 | 5,101 | 6,241 |
| Net fixed assets | 2,531 | 2,673 | 2,473 | 2,252 | 2,010 |
| Cash & Cash Eq. | 3,476 | 3,956 | 4,587 | 5,442 | 6,714 |
| Net Other current assets | (3,089) | (3,344) | (3,803) | (4,148) | (4,539) |
| Investments | 210 | 387 | 887 | 1,387 | 1,887 |
| Net Deferred tax Assets | 179 | 168 | 168 | 168 | 168 |
| Total Assets | 3,307 | 3,841 | 4,312 | 5,101 | 6,241 |

| Key Ratios | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|--------|--------|--------|--------|--------|
| OPM (%) | 23.8 | 22.5 | 21.9 | 22.5 | 22.7 |
| Net Margin (%) | 20.0 | 17.6 | 16.6 | 16.8 | 16.8 |
| Div. Yield (%) | 2.0 | 2.2 | 2.5 | 2.9 | 3.2 |
| Net debt/Equity (x) | (1.1) | (1.0) | (1.1) | (1.1) | (1.1) |
| Net Working Capital (days) | (55.9) | (53.4) | (51.9) | (48.4) | (45.9) |
| ROCE (%) | 145.2 | 134.0 | 135.8 | 138.2 | 131.2 |
| RoE (%) | 123.8 | 104.8 | 103.2 | 102.8 | 97.3 |
| EV/Net Sales (x) | 6.4 | 5.6 | 4.8 | 4.0 | 3.5 |
| EV/EBITDA (x) | 27.0 | 25.1 | 21.8 | 18.0 | 15.2 |
| PER (x) | 33.0 | 33.1 | 30.0 | 25.4 | 22.0 |
| PCE (x) | 35.8 | 35.7 | 32.6 | 28.2 | 24.8 |
| Price/Book (x) | 40.9 | 34.7 | 30.9 | 26.2 | 21.4 |

1-Year forward P/E Band



Key Assumptions

| | FY11 | FY12E | FY13E | FY14E |
|------------------------------------|-------|-------|-------|-------|
| Net Sales Gr. (%) | 13.2% | 17.0% | 16.8% | 15.5% |
| Gross Profit Margin % | 61.8% | 61.6% | 62.4% | 62.4% |
| Advertisement Expense (% of sales) | 15.3% | 16.2% | 16.3% | 16.3% |
| Royalty (% of sales) | 5.0% | 5.0% | 5.0% | 5.0% |
| EBITDA Margin % | 22.5% | 21.9% | 22.5% | 22.7% |

Company Update
 Sector: FMCG
 BSE Sensex: 15,868

MARICO

 Maintain REDUCE
 CMP Rs151
 TP Rs144

09 January 2012

Fairly Valued

Marico clocked robust sales growth of 29% during H1FY12 driven by strong sales growth in Parachute hair oil which witnessed a sharp price hike along with above expected volume growth. However, we don't expect such high growth in Parachute hair oil to sustain going forward due to limited scope of price growth.

Besides, we expect softening of input prices would help in improving gross level profitability which would be set off by higher A&P spending for the new launches and development of international business. We expect EBITDA margin would be capped at ~13%.

Slower growth in depreciation and lower interest burden on repayment of debt would translate ~19% EBITDA CAGR into ~22% net earnings CAGR during FY11-14E.

Robust H1FY12 sales growth unsustainable

Marico's 29% sales growth in H1FY12 is not sustainable in our opinion. Marico has already taken sharp price hike on Parachute which limits the scope of further price hike. Parachute volume growth at ~17% during H1FY12 was ahead of our expectation and we expect it to taper down.

Softening of input prices would be set off by higher A&P spend

Marico guided higher A&P spending for new product launches and requirement of higher marketing efforts in the international business. It would force Marico to escalate A&P (% of sales) spending by 200-250bps going forward from 9.7% in H1FY12.

Slower growth in depreciation and interest cost

Marico plans for ~Rs2bn capex over the next three years which includes ~Rs1bn capex during FY12. Besides, the company also plans to repay half of its foreign currency loans over the next 12 months. Factoring these guidance, we see slower growth in depreciation cost and decline in interest burden. This would help net earnings to grow faster than EBITDA growth.

VALUATIONS AND RECOMMENDATION

On account of limited product portfolio, higher exposure to commodity prices and moderate scope for further price hike on key brands, we maintain Marico's P/E discount over FMCG sector. We retain our 24x multiple on 12-month forward earnings and raise TP to Rs144 (earlier Rs141). We maintain our 'REDUCE' rating on the stock.

KEY FINANCIALS (CONSOLIDATED) (Rs mn)

| | FY10 | FY11 | FY12E | FY13E | FY14E |
|-----------------|--------|--------|--------|--------|--------|
| Net Sales | 26,608 | 31,283 | 39,243 | 45,905 | 53,600 |
| YoY Gr. (%) | 11.4 | 17.6 | 25.4 | 17.0 | 16.8 |
| Op Profits | 3,752 | 4,098 | 4,791 | 5,751 | 6,901 |
| OPM (%) | 14.1 | 13.1 | 12.2 | 12.5 | 12.9 |
| Adj. Net Profit | 2,535 | 2,668 | 3,108 | 3,853 | 4,863 |
| YoY Gr. (%) | 26.8 | 4.4 | 16.5 | 24.0 | 26.2 |

KEY RATIOS

| | | | | | |
|---------------|------|------|------|------|------|
| Dil. EPS (Rs) | 4.2 | 4.3 | 5.1 | 6.3 | 7.9 |
| ROCE (%) | 33.7 | 24.0 | 28.6 | 31.6 | 32.2 |
| ROE (%) | 38.8 | 29.1 | 26.7 | 26.2 | 26.2 |
| P/E (x) | 36.3 | 34.8 | 29.8 | 24.1 | 19.1 |
| EV/Sales (x) | 3.6 | 3.1 | 2.5 | 2.0 | 1.7 |
| EV/EBIDT (x) | 25.2 | 23.8 | 20.1 | 16.3 | 13.1 |

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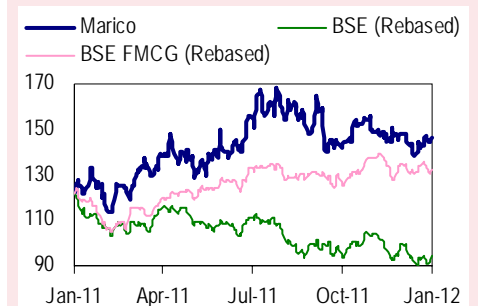
STOCK DATA

| | |
|-----------------------------|-----------|
| Market cap | Rs93bn |
| Book Value per share | Rs15 |
| Shares O/S (F.V. Rs1) | 614mn |
| Free Float | 37% |
| Avg. Trade Value (6 months) | Rs55mn |
| 52 week High/Low | Rs173/112 |
| Bloomberg Code | MRCOIN |
| Reuters Code | MRCO.BO |

PERFORMANCE (%)

| | 1M | 3M | 12M |
|----------|-------|-----|------|
| Absolute | (1.1) | 2.7 | 18.4 |
| Relative | 4.5 | 2.2 | 52.3 |

RELATIVE PERFORMANCE



Sharp price hike on Parachute hair oil had resulted into robust sales growth in the past 4 quarters. However, on account of limited scope of further price hike we believe H2FY12 and FY13 may witness slower sales growth...

Exhibit 1 - Parachute weighted average price growth (QoQ)

| | 20ml | 50ml | 100ml | 200ml | 250ml | 500ml | Weighted Avg. Price Gr.% |
|---------|------|------|-------|-------|-------|-------|--------------------------|
| Q1FY10 | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| Q2FY10 | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| Q3FY10 | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| Q4FY10 | 0% | -1% | 0% | 1% | 0% | 0% | 0% |
| Q1FY11 | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| Q2FY11 | 0% | 0% | 0% | 1% | 0% | 1% | 3% |
| Q3FY11 | 0% | 1% | 1% | 5% | 1% | 3% | 10% |
| Q4FY11 | 2% | 1% | 1% | 5% | 2% | 5% | 16% |
| Q1FY12 | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| Q2FY12 | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| Q3FY12E | 0% | 0% | 0% | 0% | 0% | 0% | 0% |

Source: PINC Research, Company

We observe the similar price jump in Saffola brand in the past 4 quarters and we expect the marginal sales growth in H2FY12 and FY13...

Exhibit 2 - Saffola weighted average price growth (QoQ)

| | Saffola Kardi Oil | Saffola Tasty | Saffola Gold | Saffola Active | Weighted Avg. price growth |
|---------|-------------------|---------------|--------------|----------------|----------------------------|
| Q1FY10 | 0% | -2% | -3% | 0% | -5% |
| Q2FY10 | 0% | 0% | 0% | 0% | 0% |
| Q3FY10 | 0% | 0% | 0% | 0% | 1% |
| Q4FY10 | 0% | 0% | 1% | 0% | 1% |
| Q1FY11 | 0% | 0% | 0% | 0% | 0% |
| Q2FY11 | 0% | 0% | 1% | 0% | 1% |
| Q3FY11 | 2% | 1% | 5% | 1% | 9% |
| Q4FY11 | 1% | 2% | 3% | 1% | 6% |
| Q1FY12 | 0% | 1% | 1% | 0% | 2% |
| Q2FY12 | 0% | 0% | 0% | 0% | 0% |
| Q3FY12E | 0% | 0% | 0% | 0% | 0% |

Source: PINC Research, Company

Copra forms ~40% of total input cost and its prices are on rising mode...

Exhibit 3 - Copra and Safflower prices are expected to soften

| | Copra Price (Rs/Quintal) | QoQ Gr% | Safflower Price (Rs/Quintal) | QoQ Gr% |
|---------|--------------------------|---------|------------------------------|---------|
| Q1FY10 | 3,287 | -14% | 2,463 | -4% |
| Q2FY10 | 3,160 | -4% | 2,397 | -3% |
| Q3FY10 | 3,215 | 2% | 2,422 | 1% |
| Q4FY10 | 3,473 | 8% | 2,260 | -7% |
| Q1FY11 | 3,428 | -1% | 2,213 | -2% |
| Q2FY11 | 3,972 | 16% | 2,227 | 1% |
| Q3FY11 | 5,214 | 31% | 2,315 | 4% |
| Q4FY11 | 6,388 | 23% | 2,531 | 9% |
| Q1FY12 | 6,727 | 5% | 2,522 | 0% |
| Q2FY12 | 5,976 | -11% | 2,714 | 8% |
| Q3FY12E | 5,436 | -9% | 2,729 | 1% |

Source: PINC Research, Company

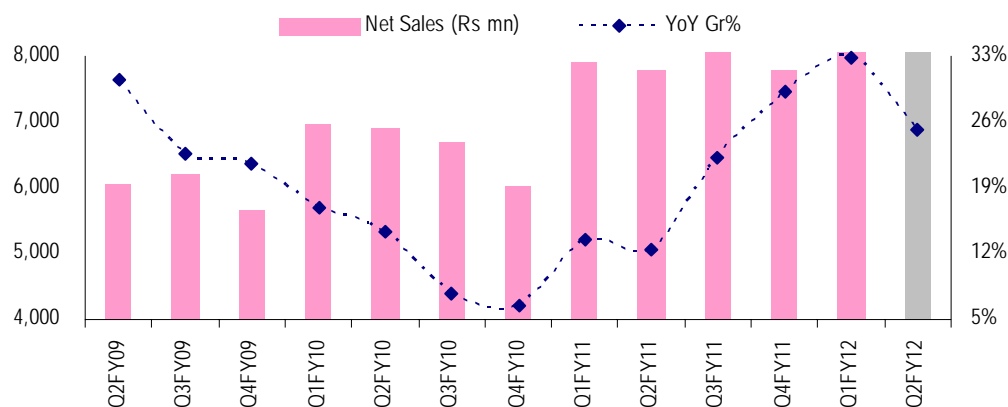
Exhibit 4 - H1FY12 Earning Summary (Rs mn)

| Year End March | Q2FY11 | Q2FY12 | YoY Gr% | Q1FY12 | QoQ Gr% | H1FY11 | H1FY12 | YoY Gr% |
|----------------------------------|------------|--------------|-------------|--------------|--------------|--------------|--------------|-------------|
| Net Sales | 7,788 | 9,745 | 25.1 | 10,486 | | 15,689 | 20,231 | 28.9 |
| RM Cost | 3,880 | 5,330 | 37.4 | 5,947 | (10.4) | 7,913 | 11,277 | 42.5 |
| Gross Profit | 3,908 | 4,415 | 13.0 | 4,539 | (2.7) | 7,776 | 8,954 | 15.1 |
| Gross Margin % | 50.2% | 45.3% | -488bps | 43.3% | 202bps | 49.6% | 44.3% | -531bps |
| Staff cost | 582 | 725 | 24.6 | 706 | 2.6 | 1,122 | 1,431 | 27.5 |
| % of net sales | 7.5% | 7.4% | -3bps | 6.7% | 70bps | 7.2% | 7.1% | -8bps |
| Advertisements & sales promotion | 949 | 941 | (0.8) | 1,023 | (8.0) | 1,887 | 1,965 | 4.1 |
| % of net sales | 12.2% | 9.7% | -252bps | 9.8% | -10bps | 12.0% | 9.7% | -231bps |
| Other Expenses | 1,385 | 1,582 | 14.2 | 1,558 | 1.5 | 2,720 | 3,140 | 15.5 |
| % of net sales | 17.8% | 16.2% | -155bps | 14.9% | 137bps | 17.3% | 15.5% | -181bps |
| Total expenditures | 6,795 | 8,578 | 26.2 | 9,235 | (7.1) | 13,642 | 17,813 | 30.6 |
| EBITDA | 993 | 1,166 | 17.5 | 1,251 | (6.8) | 2,047 | 2,417 | 18.1 |
| EBITDA margin % | 12.7% | 12.0% | -78bps | 11.9% | 4bps | 13.0% | 11.9% | -110bps |
| Other Income | 71 | 106 | 48.9 | 90 | 18.6 | 116 | 196 | 69.4 |
| Depreciation | 140 | 177 | 26.9 | 169 | 4.8 | 260 | 346 | 33.2 |
| PBIT | 924 | 1,095 | 18.5 | 1,172 | (6.5) | 1,903 | 2,267 | 19.1 |
| PBIT margin % | 11.9% | 11.2% | -63bps | 11.2% | 7bps | 12.1% | 11.2% | -92bps |
| Interest | 65 | 91 | 40.8 | 97 | (5.7) | 135 | 188 | 39.3 |
| PBT | 860 | 1,004 | 16.8 | 1,075 | (6.6) | 1,768 | 2,080 | 17.6 |
| Total tax | 126 | 205 | 62.4 | 210 | (2.4) | 288 | 416 | 44.3 |
| Effective tax rate % | 14.7% | 20.4% | 574bps | 19.6% | 88bps | 16.3% | 20.0% | 369bps |
| minority interest | 17 | 17 | | 15 | | 17 | 32 | |
| Reported PAT | 716 | 783 | 9.2 | 850 | (7.9) | 1,463 | 1,633 | 11.6 |
| EPS (Rs) | 1.2 | 1.3 | 8.3 | 1.4 | (7.9) | 2.4 | 2.7 | 10.6 |

Source: PINC Research, Company

Exhibit 5 - Net Sales Performance

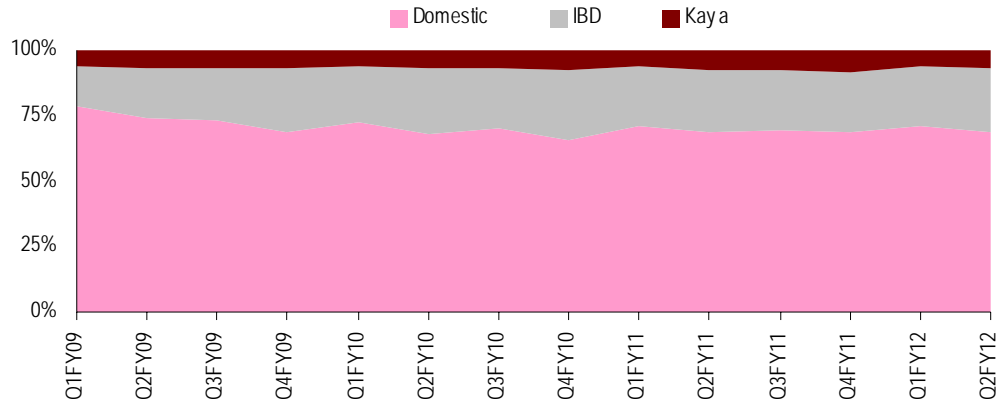
Strong top line growth after several quarters was led by price and volume increases on key brands and better IBD traction...



Source: PINC Research, Company

Exhibit 6 - Revenue Breakup

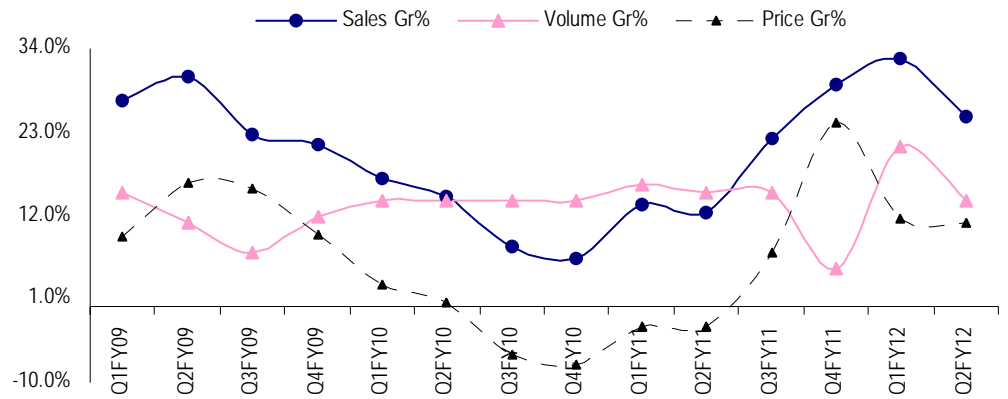
Higher growth in international business changes the mix ...



Source: PINC Research, Company

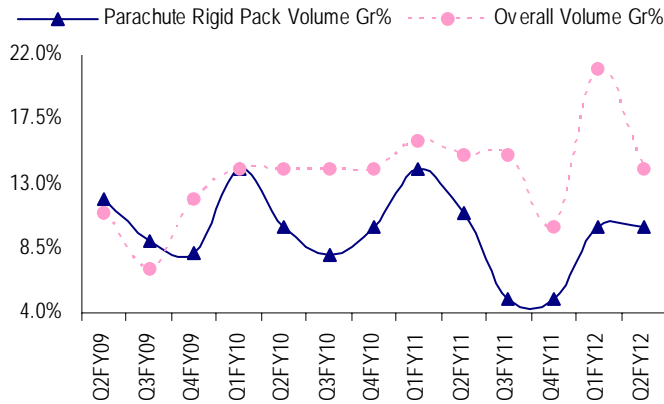
Exhibit 7 - Relationship between Sales, Volume and Price Growth

Strong volume expansion in H1FY12...



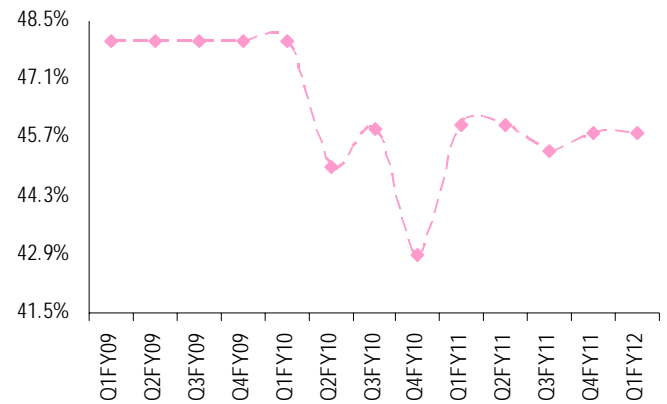
Source: PINC Research, Company

Exhibit 8 - High Dependence on Parachute Growth



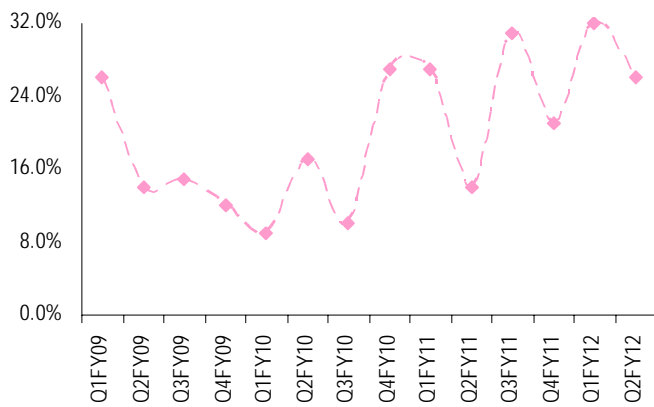
Source: PINC Research, Company

Exhibit 9 - Decline in Parachute's Market Share



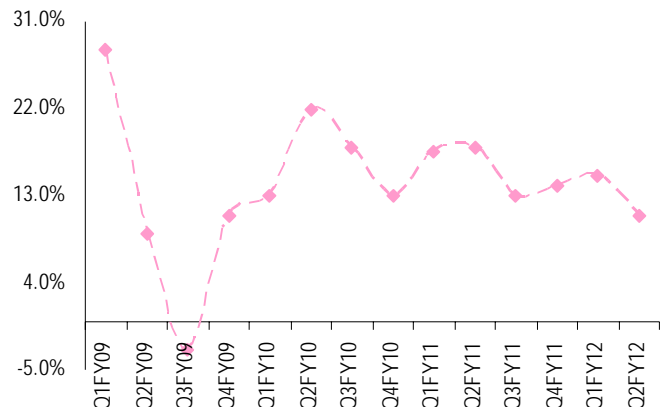
Source: PINC Research, Company

Exhibit 10 - Hair Oil Volume Growth



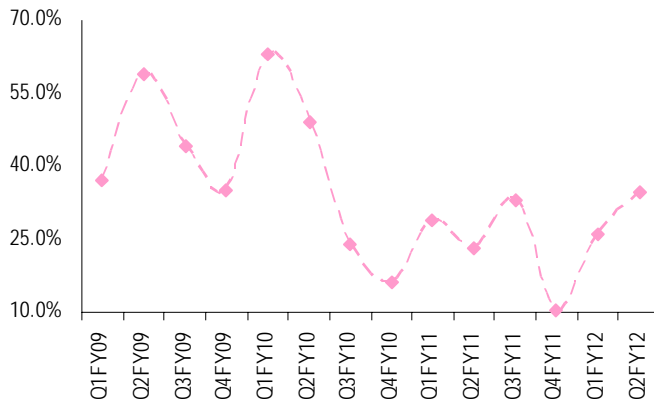
Source: PINC Research, Company

Exhibit 11- Saffola Volume Traction



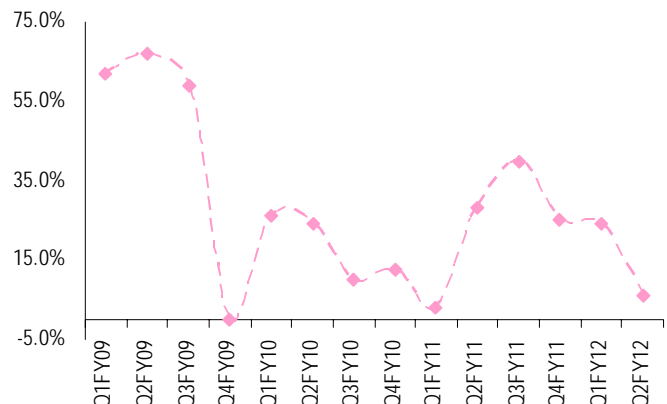
Source: PINC Research, Company

Exhibit 12 - Performance of IBD business



Source: PINC Research, Company

Exhibit 13 - Performance of Kaya



Source: PINC Research, Company

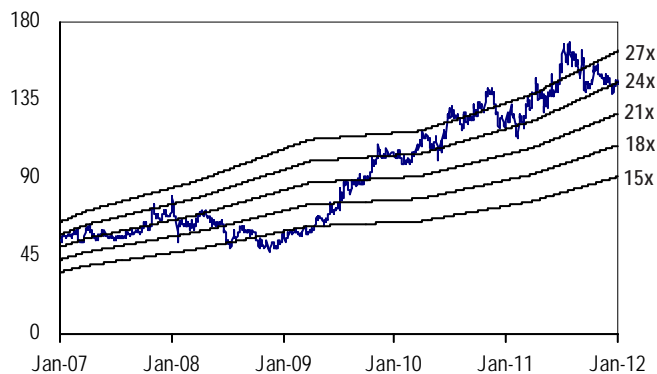
| Income Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|------------------------|--------|--------|--------|--------|--------|
| Net sales | 26,608 | 31,283 | 39,243 | 45,905 | 53,600 |
| YoY Gr (%) | 11.4 | 17.6 | 25.4 | 17.0 | 16.8 |
| Gross Profit | 13,992 | 15,104 | 18,052 | 21,757 | 25,648 |
| YoY Gr (%) | 26.8 | 7.9 | 19.5 | 20.5 | 17.9 |
| EBITDA | 3,752 | 4,098 | 4,791 | 5,751 | 6,901 |
| YoY Gr (%) | 29.8 | 9.2 | 16.9 | 20.0 | 20.0 |
| Depreciation | 601 | 708 | 732 | 857 | 913 |
| Other income | 183 | 279 | 313 | 282 | 386 |
| EBIT | 3,334 | 3,669 | 4,371 | 5,176 | 6,374 |
| Interest paid | 257 | 393 | 395 | 260 | 183 |
| PBT (before E/o items) | 2,979 | 3,764 | 3,976 | 4,916 | 6,191 |
| Tax provision | 613 | 534 | 815 | 1,008 | 1,269 |
| Effective tax rate% | 21.6 | 22.6 | 20.5 | 20.5 | 20.5 |
| Reported PAT | 2,317 | 2,864 | 3,108 | 3,853 | 4,863 |
| YoY Gr (%) | 22.8 | 23.6 | 8.5 | 24.0 | 26.2 |
| Adjusted PAT | 2,535 | 2,668 | 3,108 | 3,853 | 4,863 |
| Diluted EPS (Rs) | 4.2 | 4.3 | 5.1 | 6.3 | 7.9 |
| Diluted EPS Growth (%) | 26.8 | 4.4 | 16.5 | 24.0 | 26.2 |

| Cash Flow Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|---------|---------|---------|---------|---------|
| Pre-tax profit | 2,979 | 3,764 | 3,976 | 4,916 | 6,191 |
| Depreciation | 601 | 708 | 732 | 857 | 913 |
| Total tax paid | (629) | (534) | (815) | (1,008) | (1,269) |
| Chg in working capital | (1,287) | (1,198) | (1,243) | (766) | (1,045) |
| Other operating activities | 358 | 393 | 395 | 260 | 183 |
| Cash flow from oper. (a) | 2,021 | 3,134 | 3,045 | 4,260 | 4,972 |
| Capital expenditure | (1,526) | (4,966) | (1,000) | (600) | (600) |
| Chg in investments | (706) | (63) | - | - | - |
| Other investing activities | 158 | - | - | - | - |
| Cash flow from inv. (b) | (2,074) | (5,029) | (1,000) | (600) | (600) |
| Free cash flow (a+b) | (53) | (1,895) | 2,045 | 3,660 | 4,372 |
| Equity raised/(repaid) | 218 | 5 | - | - | - |
| Debt raised/(repaid) | 1,001 | 3,259 | (2,880) | (1,670) | (700) |
| Chg in Minorities int. | - | - | - | - | - |
| Dividend (incl. tax) | (472) | (546) | (627) | (784) | (980) |
| Other financing activities | (466) | (393) | (395) | (260) | (183) |
| Cash flow from fin. (c) | 281 | 2,325 | (3,903) | (2,714) | (1,863) |
| Net chg in cash (a+b+c) | 229 | 430 | (1,858) | 945 | 2,509 |

| Balance Sheet | FY10 | FY11 | FY12E | FY13E | FY14E |
|--------------------------|--------|--------|--------|--------|--------|
| Equity capital | 609 | 614 | 614 | 614 | 614 |
| Reserves & surplus | 5,930 | 8,540 | 11,021 | 14,090 | 17,973 |
| Shareholders' funds | 6,540 | 9,155 | 11,636 | 14,704 | 18,587 |
| Minorities interests | 125 | 219 | 271 | 327 | 385 |
| Total Debt | 4,459 | 7,718 | 4,838 | 3,168 | 2,468 |
| Capital Employed | 11,124 | 17,091 | 16,744 | 18,198 | 21,440 |
| Net fixed assets | 4,847 | 8,872 | 9,139 | 8,882 | 8,569 |
| Cash & Cash Eq. | 1,115 | 2,112 | 255 | 1,200 | 3,709 |
| Net other Current Assets | 3,719 | 4,916 | 6,160 | 6,925 | 7,970 |
| Investment | 827 | 890 | 890 | 890 | 890 |
| Net Deferred Tax Assets | 616 | 301 | 301 | 301 | 301 |
| Total assets | 11,124 | 17,091 | 16,744 | 18,198 | 21,440 |

| Key Ratios | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|------|------|-------|-------|-------|
| OPM (%) | 14.1 | 13.1 | 12.2 | 12.5 | 12.9 |
| Net margin (%) | 9.5 | 8.5 | 7.9 | 8.4 | 9.1 |
| Dividend yield (%) | 0.4 | 0.5 | 0.6 | 0.7 | 0.9 |
| Net debt/Equity (x) | 0.5 | 0.6 | 0.4 | 0.1 | (0.1) |
| Net Working Capital (days) | 51.0 | 57.4 | 57.3 | 55.1 | 54.3 |
| ROCE (%) | 33.7 | 24.0 | 28.6 | 31.6 | 32.2 |
| RoE (%) | 38.8 | 29.1 | 26.7 | 26.2 | 26.2 |
| EV/Net sales (x) | 3.6 | 3.1 | 2.5 | 2.0 | 1.7 |
| EV/EBITDA (x) | 25.2 | 23.8 | 20.1 | 16.3 | 13.1 |
| PER (x) | 36.3 | 34.8 | 29.8 | 24.1 | 19.1 |
| PCE (x) | 29.3 | 27.5 | 24.2 | 19.7 | 16.1 |
| Price/Book (x) | 14.1 | 10.1 | 8.0 | 6.3 | 5.0 |

1-Year forward P/E Band



Key Assumptions

| | FY11 | FY12E | FY13E | FY14E |
|--------------------------------|---------|--------|-------|-------|
| Coconut Hair Oil Sales Mix (%) | 31.9% | 32.8% | 31.7% | 30.5% |
| Saffola Sales Mix (%) | 15.5% | 15.9% | 16.6% | 17.3% |
| IBD Sales Mix (%) | 23.8% | 23.5% | 23.7% | 24.0% |
| Kaya Sales Mix (%) | 7.6% | 7.7% | 7.9% | 8.1% |
| EBITDA Margin Expansion (bps) | (100.1) | (89.1) | 32.1 | 34.6 |
| Effective Tax Rate % | 22.6% | 20.5% | 20.5% | 20.5% |
| | | | | |
| | | | | |
| | | | | |
| | | | | |

Company Update
 Sector: FMCG
 BSE Sensex: 15,868

JYOTHY LABORATORIES

 Maintain BUY
 CMP Rs160
 TP Rs212

09 January 2012

Expectation of operational improvement

We believe Jyothy Labs (Jyothy) standalone business should recover from H2FY12 onwards. Except Maxo, the dynamics of the standalone business are still at the same level. National launch of Exo has already started showing strong numbers and reported 23% growth in H1FY12. While 7% price hike on Ujala Supreme along with higher focus on the core business should result into better fabric care growth.

Slight uncertainty remains over Maxo as its dynamics has changed in the past one year post the reduction in the distribution margin and higher competitive intensity. While the launch of advance version of liquid mosquito repellent and higher growth in disposable income in the Eastern region (key market for Maxo) can surprise going forward.

We introduce FY14E numbers and maintain 'BUY' recommendation with TP of Rs212.

Standalone EBITDA margin to improve

We believe Jyothy's standalone low EBITDA margin in H1FY12 is not sustainable going forward. Ujala Supreme contributes >70% of the standalone EBITDA and post the stability in the sales distribution we expect better business from this front. Ujala Supreme sales in H1FY12 was down by ~10% which why overall profitability was under pressure. We don't see reasons for pressure on its consumer demand.

Henke India's (Henkel) performance encouraging

Improvement in Henkel's profitability since acquisition has been encouraging. However, the key challenge will be to harness the synergy by improving the sales of Henkel brands. Other thing to watch out for will be monetization of idle assets available with Henkel which will help the company in reducing the interest burden.

Synergy benefits to come

We remain positive on the long term growth potential of the combined business. The combined entity represents several synergies i.e. better revenue mix, optimum rural/urban ratio and cost saving on distribution. Jyothy now has multiple drivers to run the business and better execution can reduce timing of turnaround in Henkel India.

VALUATIONS AND RECOMMENDATION

Jyothy's under performance in the past three quarters has resulted into 40% decline in the stock price in last 9 months. We believe investor's visibility in the business would be clearer with each quarter's better performance. We maintain 16x multiple to Jyothy's FY13 earnings and add Rs12/share NPV on tax saving of Rs1.2bn at 12% discount rate. We maintain our 'BUY' recommendation with TP of Rs212.

KEY FINANCIALS (CONSOLIDATED)

(Rs mn)

| | FY10 | FY11 | FY12E | FY13E | FY14E |
|-----------------|-------|-------|--------|--------|--------|
| Net Sales | 5,975 | 6,174 | 11,675 | 13,754 | 15,678 |
| YoY Gr. (%) | 23.5 | 3.3 | 89.1 | 17.8 | 14.0 |
| Op. Profits | 929 | 727 | 1,132 | 1,775 | 2,004 |
| OPM (%) | 15.6 | 11.8 | 9.7 | 12.9 | 12.8 |
| Adj. Net Profit | 743 | 688 | 452 | 1,000 | 1,212 |
| YoY Gr. (%) | 45.2 | (7.4) | (34.3) | 121.4 | 21.2 |

KEY RATIOS

| | | | | | |
|---------------|------|------|------|------|------|
| Dil EPS (Rs) | 9.2 | 8.5 | 5.6 | 12.4 | 15.0 |
| ROCE (%) | 23.2 | 10.4 | 10.5 | 16.8 | 18.2 |
| RONW (%) | 19.2 | 10.9 | 8.5 | 16.9 | 17.9 |
| P/E (x) | 17.4 | 18.8 | 28.6 | 12.9 | 10.6 |
| EV/Sales (x) | 2.0 | 1.6 | 1.5 | 1.2 | 1.0 |
| EV/EBITDA (x) | 12.7 | 14.0 | 15.7 | 9.5 | 8.0 |

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 naveent@pinc.co.in

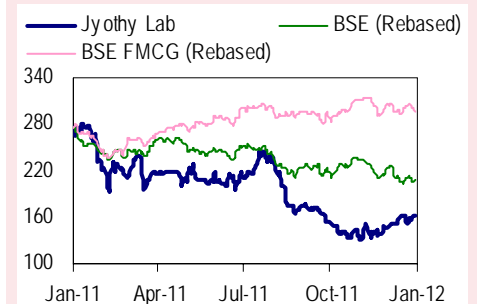
STOCK DATA

| | |
|-----------------------------|-----------|
| Market cap | Rs13bn |
| Book Value per share | Rs53 |
| Shares O/S (F.V. Rs1) | 81mn |
| Free Float | 35% |
| Avg. Trade Value (6 months) | Rs15mn |
| 52 week High/Low | Rs284/125 |
| Bloomberg Code | JYL IN |
| Reuters Code | JYOI.BO |

PERFORMANCE (%)

| | 1M | 3M | 12M |
|----------|------|-----|--------|
| Absolute | 10.6 | 7.2 | (41.1) |
| Relative | 16.9 | 6.7 | (24.3) |

RELATIVE PERFORMANCE



Standalone EBITDA margin to improve

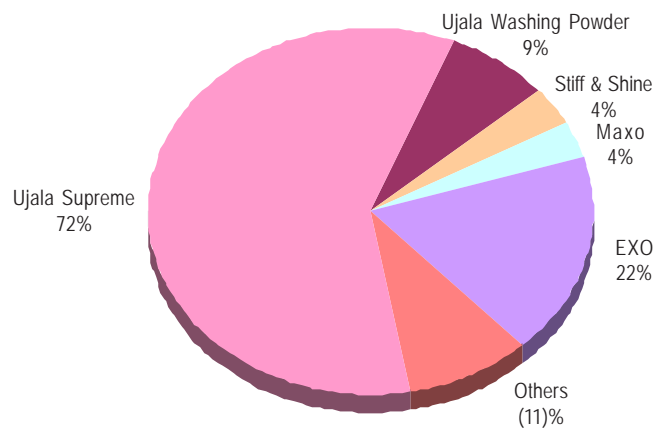
Jyothy’s standalone operational performance in the past two quarters was under severe pressure. EBITDA margin dipped to 9% and 5% during Q1FY12 and Q2FY12 on account of lower sales of high margin Ujala Supreme, higher input pressure and change in the distribution model. We believe Ujala Supreme consists >70% of the overall EBITDA hence lower sales of that business impacted the overall margin profile of the company. We believe Jyothy’s standalone low EBITDA margin in H1FY12 is not sustainable going forward. Ujala Supreme sales in H2FY12 should be better than H1FY12 due to stability in the distribution model and 7% price hike. Better revenue mix in H2FY12 would expand the EBITDA margin.

Exhibit 1 - Segment Performance

| | Sep-09 | Dec-09 | Mar-10 | Jun-10 | Sep-10 | Dec-10 | Mar-11 | Jun-11 | Sep-11 |
|--------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Sales Mix (Rs mn) | | | | | | | | | |
| Fabric Care | 650 | 665 | 751 | 826 | 699 | 760 | 713 | 677 | 651 |
| Maxo | 312 | 396 | 726 | 282 | 372 | 336 | 469 | 183 | 390 |
| Exo | 247 | 210 | 322 | 292 | 272 | 296 | 280 | 294 | 398 |
| Others | 91 | 83 | 99 | 113 | 105 | 85 | 98 | 77 | 108 |
| Total | 1,301 | 1,354 | 1,899 | 1,513 | 1,449 | 1,477 | 1,560 | 1,230 | 1,547 |
| Sales Mix (%) | | | | | | | | | |
| Fabric Care | 18% | 21% | 37% | 26% | 7% | 14% | -5% | -18% | -7% |
| Maxo | -10% | 15% | 111% | 24% | 19% | -15% | -35% | -35% | 5% |
| Exo | 58% | 35% | 106% | 29% | 10% | 41% | -13% | 1% | 46% |
| Others | 21% | 10% | 32% | 35% | 15% | 3% | -1% | -32% | 3% |
| Total | 16% | 20% | 69% | 27% | 11% | 9% | -18% | -19% | 7% |
| EBITDA Margin (%) | 13% | 14% | 19% | 22% | 13% | 12% | 11% | 9% | 5% |

Source: PINC Research, Company

Exhibit 2 - EBITDA Mix (FY11)



Source: PINC Research

Encouraging performance of Henkel

Henkel displayed positive EBITDA post the acquisition by Jyothy and it was encouraging particularly when Henkel was making operational losses since so many years. Jyothy cut down several operational expenses of Henkel to achieve this profitability. Now we believe the key challenge will be to harness the synergy by improving the sales of Henkel's brands.

Exhibit 3 - Henkel India's 9MCY11 Performance (Rs mn)

| Henkel Consolidated | Sep-10 | Sep-11 | YoY Gr. | Jun-11 | QoQ Gr. | 9MCY10 | 9MCY11 | YoY Gr. | PINC Comments |
|-----------------------------|--------------|------------|---------------|--------------|---------------|--------------|--------------|---------------|---|
| Net Sales | 1,354 | 1,075 | (20.6) | 1,231 | -12.7% | 4,195 | 3,498 | (16.6) | Sales decline was expected |
| Total RM cost | 822 | 591 | (28.1) | 712 | -17.0% | 2,349 | 1,967 | (16.3) | |
| Gross Profit | 532 | 484 | (9.1) | 520 | -6.8% | 1,846 | 1,531 | (17.1) | |
| Gross margin (%) | 39.3% | 45.0% | 572bps | 42.2% | 284bps | 44.0% | 43.8% | -23bps | |
| Employee Expenses | 107 | 51 | (52.3) | 73 | -29.4% | 306 | 224 | (26.6) | Due to sharp reduction in staff |
| Other Expenses | 469 | 296 | (36.9) | 400 | -25.9% | 1,702 | 1,205 | (29.2) | |
| Total Expenditures | 1,398 | 938 | (32.9) | 1,184 | -20.7% | 4,357 | 3,396 | (22.1) | |
| EBITDA | (44) | 136 | na | 47 | 189.0% | (161) | 102 | na | Strong EBITDA on account of control on several overheads cost |
| EBITDA Margin % | -3.3% | 12.7% | na | 3.8% | 886bps | -3.8% | 2.9% | na | |
| Other Income | - | (13) | na | 62 | na | 1 | 54 | na | |
| Interest | 90 | 128 | 42.3 | 96 | 33.5% | 201 | 317 | 57.9 | |
| Depreciation | 15 | 23 | 48.7 | 14 | 56.9% | 46 | 52 | 11.9 | |
| PBT before exceptional item | (150) | (28) | na | (2) | 1517.6% | (407) | (213) | na | |
| Exceptional item | - | - | na | 254 | na | - | 254 | na | |
| PBT after exceptional item | (150) | (28) | na | 252 | na | (407) | 41 | na | |
| Tax | - | - | na | - | na | - | - | na | |
| Reported PAT | (150) | (28) | na | 252 | na | (407) | 41 | na | |
| Adjusted PAT | (150) | (28) | na | (2) | na | (407) | (213) | na | |

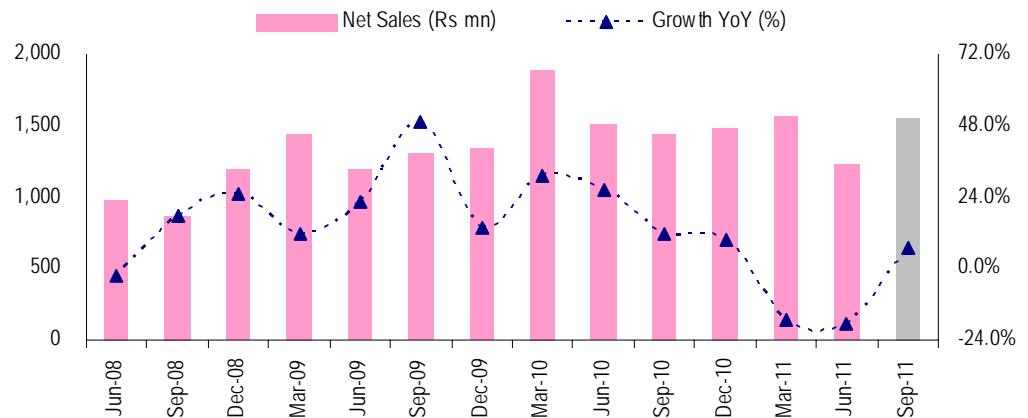
Source: PINC Research, Company

Synergy benefits to come

We are positive on the long term growth potential of the business. The combined entity represents several synergies i.e. better revenue mix, optimum rural/urban ratio and cost saving on distribution. Jyothy's product portfolio is now more balanced and it has multiple drivers to run the business. Jyothy was already trying to reduce its dependence over Ujala Supreme therefore investing high on Maxo and Exo. Through Henkel, Jyothy now has extended its detergent presence as well as entered into personal care segment too. Under the Jyothy's management, Henkel's business can show consistent profitable performance.

Exhibit 4 - Net Sales Performance

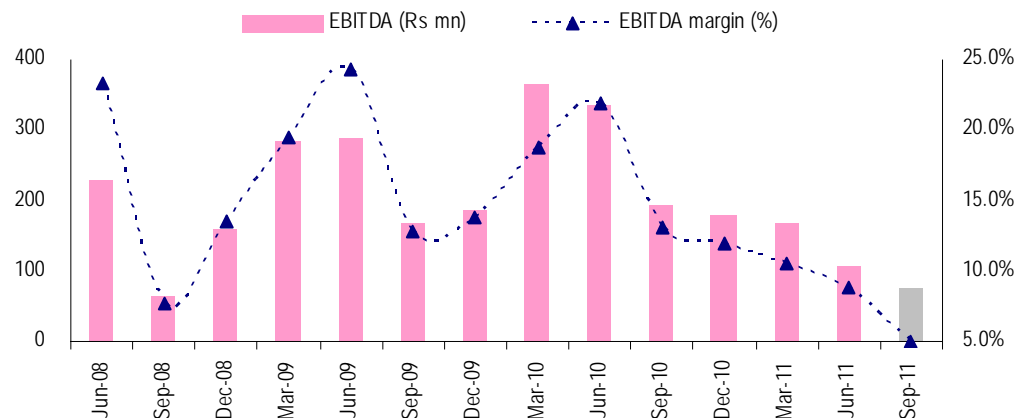
Despite the sales had quarter variability, annual sales were consistently moving in up trend...



Source: Company, PINC Research

Exhibit 5 - EBITDA (Rs mn) and Margin (%)

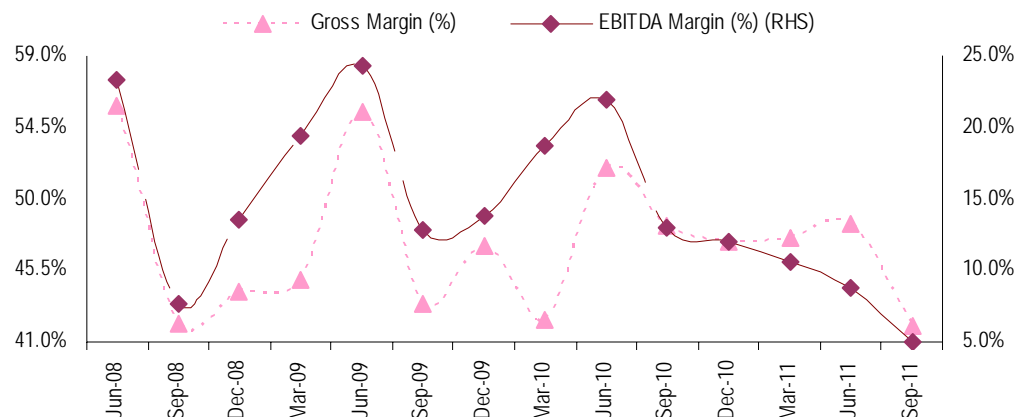
Seasonality and withdrawal of sales promotion in Maxo and high investment for Ujala brand were the main reasons for inconsistency in operating performance...



Source: Company, PINC Research

Exhibit 6 - Margins Movement (%)

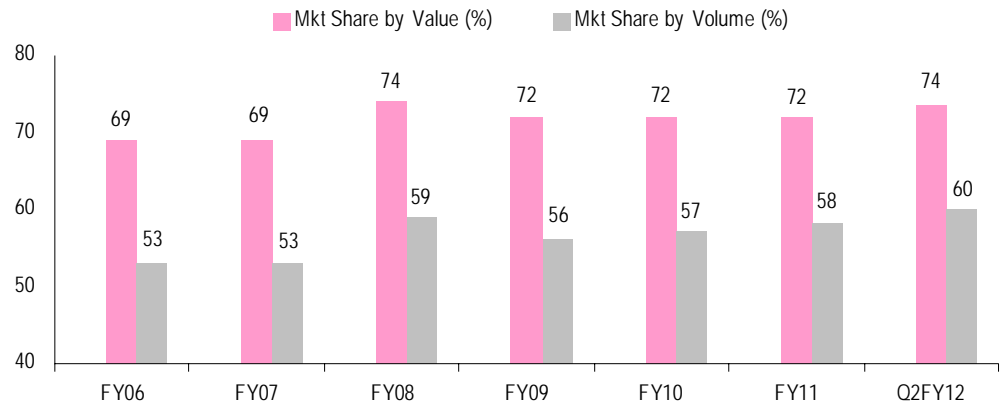
RM has high relevance on overall operating performance...



Source: Company, PINC Research

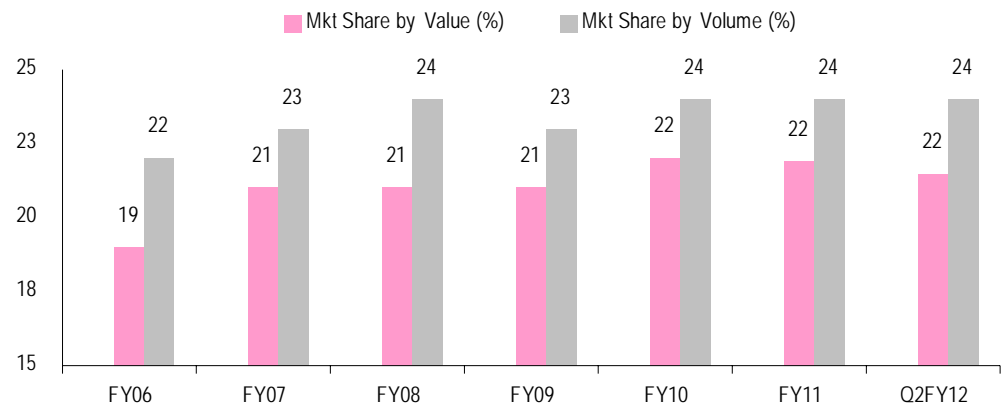
Exhibit 7 - Ujala Supreme's Improvement in Market Share

Leadership in the product leads to ~300bps improvement in value market share and ~500bps in volume market share...



Source: Company, PINC Research

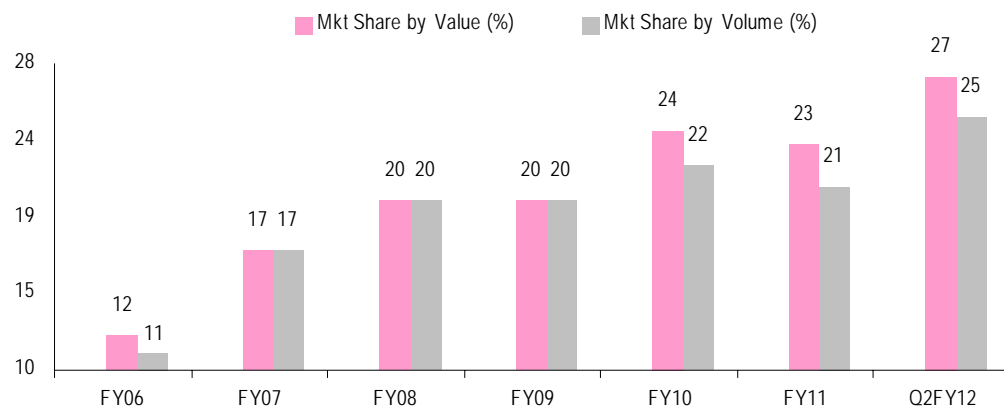
Exhibit 8 - Maxo Market Share



Source: Company, PINC Research

Exhibit 9 - Exo Market Share Trajectory in South India

Exo market has been doubled in Southern India in past 5 years ...



Source: Company, PINC Research

| Income Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|-------------------------|-------|--------|--------|--------|--------|
| Net sales | 5,975 | 6,174 | 11,675 | 13,754 | 15,678 |
| YoY Growth (%) | 23.5 | 3.3 | 89.1 | 17.8 | 14.0 |
| EBITDA | 929 | 727 | 1,132 | 1,775 | 2,004 |
| YoY Growth (%) | 40.8 | (21.8) | 55.7 | 56.8 | 12.9 |
| Depreciation | 124 | 130 | 234 | 261 | 301 |
| Other Income # | 166 | 237 | 122 | 126 | 130 |
| EBIT | 971 | 833 | 1,020 | 1,640 | 1,832 |
| Interest Paid | 17 | 21 | 408 | 460 | 409 |
| PBT (before E/o items) | 955 | 812 | 612 | 1,180 | 1,423 |
| Exceptional gain/(loss) | - | - | 254 | - | - |
| Tax Provision | 215 | 154 | 113 | 160 | 167 |
| Minority Interest | (3) | (30) | 47 | 68 | 103 |
| Reported PAT | 743 | 688 | 705 | 1,000 | 1,212 |
| Adjusted PAT | 743 | 688 | 452 | 1,000 | 1,212 |
| YoY Growth (%) | 45.2 | (7.4) | (34.3) | 121.4 | 21.2 |
| Diluted EPS (Rs) | 9.2 | 8.5 | 5.6 | 12.4 | 15.0 |
| Diluted EPS Growth (%) | 45.2 | (7.4) | (34.3) | 121.4 | 21.2 |

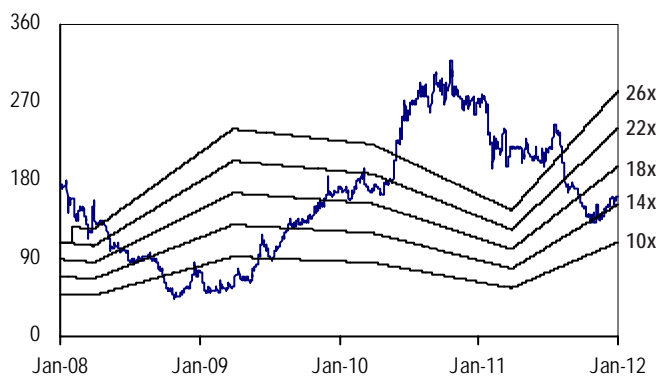
Excluding interest income from Henkel India

| Balance Sheet | FY10 | FY11 | FY12E | FY13E | FY14E |
|--------------------------|-------|-------|--------|--------|--------|
| Equity Share Capital | 73 | 81 | 81 | 81 | 81 |
| Reserves & surplus | 3,805 | 6,230 | 5,216 | 5,838 | 6,673 |
| Shareholders' funds | 3,878 | 6,311 | 5,297 | 5,919 | 6,753 |
| Minorities interests | 5 | 5 | 52 | 120 | 223 |
| Total Debt | 130 | 690 | 5,407 | 4,507 | 4,007 |
| Capital Employed | 4,013 | 7,006 | 10,756 | 10,546 | 10,983 |
| Net fixed assets | 2,378 | 2,607 | 9,375 | 9,414 | 9,412 |
| Cash & Cash Eq. | 1,224 | 2,809 | 592 | 505 | 807 |
| Net Other current assets | 586 | 1,199 | 1,005 | 843 | 980 |
| Investments | 1 | 607 | - | - | - |
| Net Deferred tax Assets | (178) | (216) | (216) | (216) | (216) |
| Total Assets | 4,011 | 7,006 | 10,756 | 10,546 | 10,983 |

| Cash Flow Statement | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|-------|---------|---------|---------|---------|
| Pre-tax profit | 955 | 812 | 612 | 1,227 | 1,481 |
| Depreciation | 124 | 130 | 234 | 261 | 301 |
| Total Tax Paid | (157) | (225) | (113) | (160) | (167) |
| Chg in working capital | (290) | (583) | 194 | 162 | (137) |
| Other operating activities | (129) | (190) | 408 | 460 | 409 |
| Cash flow from oper (a) | 503 | (55) | 1,334 | 1,950 | 1,888 |
| Capital Expenditure | (326) | (348) | (6,748) | (300) | (300) |
| Chg in investments | (132) | (2,172) | 607 | - | - |
| Other investing activities | 96 | 90 | - | - | - |
| Cash flow from inv.(b) | (363) | (2,430) | (6,141) | (300) | (300) |
| Free cash flow (a+b) | 140 | (2,485) | (4,807) | 1,650 | 1,588 |
| Equity raised/(repaid) | - | 2,244 | - | - | - |
| Debt raised/(repaid) | 129 | 560 | 4,717 | (900) | (500) |
| Interest paid | (17) | (21) | (408) | (460) | (409) |
| Dividend (incl. Tax) | (170) | (338) | (323) | (323) | (323) |
| Other financing activities | (1) | - | (1,397) | (55) | (55) |
| Cash flow from fin. (c) | (59) | 2,444 | 2,590 | (1,738) | (1,286) |
| Net chg in cash (a+b+c) | 81 | (41) | (2,217) | (87) | 302 |

| Key Ratios | FY10 | FY11 | FY12E | FY13E | FY14E |
|----------------------------|-------|-------|-------|-------|-------|
| OPM (%) | 15.6 | 11.8 | 9.7 | 12.9 | 12.8 |
| Net Margin (%) | 12.4 | 11.1 | 3.9 | 7.3 | 7.7 |
| Div. Yield (%) | 2.5 | 3.1 | 2.5 | 2.5 | 2.5 |
| Net debt/Equity (x) | (0.3) | (0.3) | 0.9 | 0.7 | 0.5 |
| Net Working Capital (days) | 35.8 | 70.9 | 31.4 | 22.4 | 22.8 |
| ROCE (%) | 23.2 | 10.4 | 10.5 | 16.8 | 18.2 |
| RoE (%) | 19.2 | 10.9 | 8.5 | 16.9 | 17.9 |
| EV/Net Sales (x) | 2.0 | 1.6 | 1.5 | 1.2 | 1.0 |
| EV/EBITDA (x) | 12.7 | 14.0 | 15.7 | 9.5 | 8.0 |
| PER (x) | 17.4 | 18.8 | 28.6 | 12.9 | 10.6 |
| PCE (x) | 14.7 | 15.8 | 18.8 | 10.2 | 8.5 |
| Price/Book (x) | 3.0 | 2.0 | 2.4 | 2.2 | 1.9 |

1-Year forward P/E Band



Key Assumptions

| | FY11 | FY12E | FY13E | FY14E |
|-------------------------------------|-------|-------|-------|-------|
| Net Sales Gr. (%) | 13.2% | 17.0% | 16.8% | 15.5% |
| Gross Profit Margin % | 61.8% | 61.6% | 62.4% | 62.4% |
| Advertisement Expense (% of sales) | 15.3% | 16.2% | 16.3% | 16.3% |
| Royalty (% of sales) | 5.0% | 5.0% | 5.0% | 5.0% |
| EBITDA Margin % | 22.5% | 21.9% | 22.5% | 22.7% |
| | | | | |
| | | | | |
| | | | | |
| | | | | |

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| Rating Objective | | |
|-------------------|---------------------|---------------------|
| Rating | Large Caps | Mid Caps |
| | M.Cap > USD1bn | M.Cap <= USD1bn |
| Return % | | |
| BUY | More than 15 | More than 20 |
| Accumulate | 5 to 15 | 10 to 20 |
| Reduce | (-)5 to +5 | 0 to 10 |
| Sell | Below (-)5 | Less than 0 |



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