

- Q1 net sales up 14% yoy to Rs31.8bn driven by 10% growth in HPC and 23% in foods. Exports increased 28% yoy to Rs3.5bn led by FMCG exports.
- Slower growth in high margin HPC segment remains an area of concern.
- Margins down 40bps at 11.4% due to higher adspend and firm raw material prices.
- Net profit increased by 14% yoy to Rs3.3bn. APAT after exceptional items down by 11% yoy to Rs3.9bn.

Financial Highlights

Period to	03/07	03/06	Growth	12/06	12/05	Growth
(Rs mn)	(3)	(3)	(%)	(12)	(12)	(%)
Sales	31,843	27,981	13.8	121,034	110,606	9.4
Expenditure	(28,224)	(24,675)	14.4	(104,553)	(96,172)	8.7
Operating profit	3,620	3,306	9.5	16,481	14,433	14.2
Other income	908	694	30.9	3,545	3,048	16.3
Interest	(51)	(21)	150.2	(107)	(192)	(44.0)
Depreciation	(329)	(339)	(2.8)	(1,302)	(1,245)	4.6
PBT	4,147	3,640	13.9	18,617	16,045	16.0
Tax	(809)	(700)	15.5	(3,220)	(2,500)	28.8
PAT	3,339	2,940	13.6	15,397	13,545	13.7
Extraordinary items	590	1,489	-	3,157	536	-
APAT	3,929	4,429	(11.3)	18,554	14,081	31.8
OPM (%)	11.4	11.8	-	13.6	13.0	-
Equity	2,207	2,201	-	2,207	2,201	-
EPS (Rs) Annualized	7.1	8.0	-	8.4	6.4	-
EPS excluding extraordinary	6.1	5.3	-	7.0	6.2	-
P/E @ CMP of Rs199	28.0	-	-	23.7	-	-

Slower growth in high margin HPC segment

HLL recorded 13.8% yoy growth in net sales at Rs31.8bn in Q1 F12/07 driven by 10% yoy growth in HPC (driven by double-digit growth in laundry and shampoo segment) and 22.9% yoy growth in foods segment. The slower growth in high margin HPC segment remains an area of concern.

Revenue Break-up

(Rs mn)	03/07	03/06	Growth	12/06	12/05	Growth
	(3)	(3)	(%)	(12)	(12)	(%)
Domestic FMCG - HPC	22,517	20,467	10.0	88,514	77,869	13.7
Domestic FMCG - Foods	5,312	4,321	22.9	18,408	16,881	9.0
a) Domestic FMCG - Total	27,829	24,788	12.3	106,922	94,750	12.8
b) Exports	3,519	2,755	27.7	12,789	13,478	(5.1)
c) Others	495	220	125.3	1,106	1,596	(30.7)
Total Continuing businesses (a+b+c)	31,843	27,763	14.7	120,817	109,824	10.0
Discontinued businesses	-	217	-	217	782	(72.2)
Total	31,843	27,981	13.8	121,034	110,606	9.4

Broad based growth across categories

Soaps & detergents segment recorded 9.6% yoy growth at Rs14.4bn aided by strong growth in laundry (driven by Surf and Wheel) and personal wash (led by Lifebuoy and Lux) category during Q1 F12/07. Revenues in the personal care products segment increased by 7.3% yoy to Rs8.2bn. The company has lost market share in the shampoo and tea segments. After adjusting for the disposal of Nihar brand, the segment has recorded a 10.5% yoy growth during the quarter.

Beverages segment recorded strong 16.6% yoy growth in revenues at Rs3.7bn, driven by strong growth in tea (led by Brooke Bond) and coffee (led by Bru Instant Coffee) segment. Revenues from the processed foods (led by Kissan and Knorr portfolio) and ice creams (recorded 20%+ growth) segments increased by 48.7% yoy and 21.9% yoy respectively. Exports recorded a strong growth of 27.7% yoy to Rs3.5bn led mainly by FMCG exports (HPC, tea and coffee exports also recorded good growth).

Sales trend (Rs mn)

Segments	F12/04				F12/05				F12/06				F12/07
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Soaps & Det.	10,320	11,776	11,131	11,480	11,368	12,876	12,429	12,969	13,186	14,559	13,933	14,281	14,445
Personal Prod.	5,534	6,368	5,853	6,967	6,026	7,474	7,291	8,713	7,659	8,467	8,538	8,934	8,221
Beverages	3,030	2,695	2,914	3,306	3,024	3,122	3,240	3,388	3,177	3,006	3,455	3,670	3,705
Processed Foods	795	822	611	622	674	783	815	865	882	973	973	1,022	1,311
Ice Creams	201	351	207	131	204	376	230	172	265	505	338	263	322
Exports	3,037	3,294	2,957	3,202	3,421	3,225	2,731	3,573	2,755	3,287	3,274	3,473	3,519
Others	933	743	654	672	704	786	894	553	340	379	480	603	631
Total	23,850	26,049	24,327	26,380	25,421	28,643	27,629	30,232	28,263	31,175	30,991	32,246	32,156

Margin pressure continues

Operating profit for the quarter increased by 9.5% yoy to Rs3.6bn. Operating margins declined by 40bps to 11.4% due to higher raw material cost (on account of firm vegetable and crude oil prices) and sharp 17.5% yoy increase in adspend at Rs3.6bn. The company had taken selective price increases to maintain margins. The raw materials are expected to remain inflationary going forward. The company is likely to maintain the high levels of adspend (between 10-15%) going forward.

Cost Analysis

Period	03/07	03/06	Inc/Dec	12/06	12/05	Inc/Dec
As % of net sales	(3)	(3)		(12)	(12)	
RM	38.3	41.0	(2.8)	39.3	41.1	(1.9)
Purchase of goods	17.2	13.5	3.8	14.5	14.6	(0.1)
Staff	5.6	5.6	0.0	5.3	5.3	(0.0)
Advertising & Promotion	11.2	10.8	0.4	10.5	9.1	1.4
Other expenditure	16.3	17.3	(0.9)	16.8	16.8	0.0

Personal product profitability improves marginally

EBIT margins in the personal product segment (contributing 25.6% to revenues and 46.2% to EBIT) improved marginally by 30bps while, margins in the soaps and detergents segment (contributing 44.9% to revenues and 39.7% of profitability) recorded a 50bps increase on yoy basis. Margins in the ice cream segment increased by 90bps while, beverages segment (11.2% of EBIT) witnessed a 450bps drop in EBIT margins during the quarter.

Margin trend

EBIT Margins (%)	Q1 F12/04	Q2 F12/04	Q3 F12/04	Q4 F12/04	Q1 F12/05	Q2 F12/05	Q3 F12/05	Q4 F12/05	Q1 F12/06	Q2 F12/06	Q3 F12/06	Q4 F12/06	Q1 F12/07
Soaps & Det.	20.1	14.5	14.8	20.1	11.4	13.3	13.9	15.7	11.6	14.3	13.2	15.6	12.1
Personal Prod.	31.7	32.1	33.3	33.3	24.0	27.7	29.6	31.6	24.4	28.5	28.2	31.9	24.7
Beverages	20.0	18.8	20.1	20.9	21.0	17.3	17.5	20.0	19.5	13.5	15.3	19.7	15.0
Processed Foods	(8.9)	(33.3)	(21.2)	(55.3)	(3.1)	(5.8)	(7.6)	(3.9)	0.4	4.3	4.2	6.3	5.6
Ice Creams	(15.9)	8.0	(2.0)	(29.7)	(15.2)	13.5	11.4	(6.9)	3.2	21.5	13.8	10.7	4.1
Exports	3.9	2.7	1.3	4.7	1.8	0.7	0.7	6.0	2.9	4.7	6.8	5.9	3.8
Others	(10.9)	(12.9)	(3.4)	(16.2)	(3.9)	(16.8)	(9.5)	(9.3)	(14.8)	(50.7)	(12.6)	(41.3)	(24.9)

Net profit up 14%

Other income for the quarter was higher at Rs908mn (operational Rs497.3mn + financial Rs410.7mn) compared to Rs694mn in Q1 F12/06. Effective tax rate was at 19.5% resulting in a tax outgo of Rs809mn. Net profit grew by 13.6% yoy to Rs3.3bn. Adjusted net profit after extraordinary income of Rs590mn (Rs1.5bn in Q1 F12/06) declined by 11.3% yoy to Rs3.9bn. Annualized EPS for the quarter stood at Rs7.1 per share.

Following are the one time income and writeoff's:

	Q1 F12/07	Q1 F12/06
Profit from transfer of two factory units (Jamnagar and Shamnagar) and Janmam land to three separate subsidiaries	175	-
Reduction in tax liability arising from the amalgamation of Modern Foods	458	-
Profit on disposal of a brand - Nihar	-	2,018
Other one off items aggregating to a net expenditure of	(43)	-
Residual costs on disposal of plantation subsidiaries	-	(58)
Provision for diminution in value of investments in a subsidiary	-	(27)
Provision for retirement benefits and voluntary retirement	-	(444)
Total	590	1,489

Outlook

The company is more focused on the renovation and product extensions within the existing categories rather than a new innovation. Over the past 7-8 years, it has not made a single innovation. This lack of innovations and new market entry remains an area of concern. Another key challenge for HLL would be to maintain margins in the personal products and soap & detergent businesses, which account for ~87% of profits. Increasing palm oil and crude oil prices will drive up raw material as well as packaging cost in these businesses. Heavy onslaught of competition in the core categories will necessitate even higher adspends in the future and may pull down profit growth. We therefore expect that going forward, HLL's growth would primarily be driven by growth momentum in the topline.

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