

DABUR INDIA**INR 81****FCPL acquisition expensive, but synergistic****ACCUMULATE**

November 25, 2008

Dabur acquires Fem Care at EV of INR 3 bn

Dabur India (Dabur) recently acquired Fem Care Pharma (FCPL) at an enterprise value (EV) of INR 3 bn (per share value at INR 800), entirely through internal accruals. FCPL currently has a market cap of INR 2 bn and reported turnover of INR 945 mn in FY08, with PAT of INR 80 mn; in H1FY09, the company reported turnover of INR 545 mn and PAT of INR 97.5 mn.

Under the deal structure, Dabur will buy 72.15% stake in FCPL and will make an open offer for another 20% stake subsequently. FCPL's specialty chemical division and some investments (not of interest to Dabur) will be bought back by FCPL's erstwhile promoters at the book value or market value, whichever is higher (on payment of INR ~210 mn towards the same).

Dabur to benefit from acquisition synergies

FCPL has a wide range of products in the skin care segment, which augurs well for Dabur since it has been looking to expand presence in the high-growth skin care segment. FCPL is particularly strong in the bleaching category, with its bleach portfolio (comprising *Fem* range of bleach) dominating 60% of the segment; the company derives 53% of its consolidated revenues from its bleach portfolio.

Further, Dabur is likely to benefit from FCPL's extensive parlour reach (25,000 parlours), while FCPL's products can gain from Dabur's higher distribution reach, especially in the modern and institutional trade arena.

Outlook and valuations: FCPL expensive but a good fit; maintain 'ACCUMULATE'

FCPL is a good fit for Dabur, since Dabur has been looking to beef up its skin care segment for a while. Though at INR 3 bn FCPL looks expensive (at 3.2x sales and 20.3x EV/EBITDA based on FY08 numbers), its acquisition could prove beneficial for Dabur in the long term, since the skin care segment is still at a nascent stage in India. Also, FCPL enjoys strong brand equity in its skin care products, especially in the bleach segment, and enjoys high margins.

The acquisition is expected to add ~4% to Dabur's revenue and 2% to its earnings for FY10E, based on our 20% growth assumption and some cost benefits for FCPL. We have not factored in FCPL for FY09E, since the acquisition is unlikely to be consolidated until FY09 end. We view the acquisition as timely entry for Dabur into the fast-growing mass skin care segment. At CMP of INR 81, Dabur is trading at P/E of 18.5x and 15.6x and EV/EBITDA of 15.0x and 12.2x our FY09E and FY10E estimates, respectively. We maintain our 'ACCUMULATE' recommendation on the stock.

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Market Data

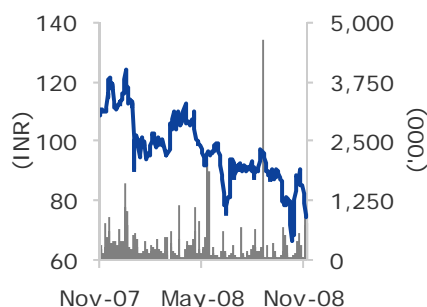
52-week range (INR) : 127 / 60
 Share in issue (mn) : 865.1
 M cap (INR bn/USD mn) : 70.0 / 1,404.2
 Avg. Daily Vol. BSE/NSE ('000) : 988.7

Share Holding Pattern (%)

Promoters : 70.7
 MFs, FIs & Banks : 11.8
 FIIs : 10.3
 Others : 7.2

Relative Performance (%)

	Sensex	Stock	Stock over Sensex
1 month	(12.3)	(7.0)	5.3
3 months	(38.1)	(18.5)	19.6
12 months	(51.9)	(31.7)	20.1

**Financials**

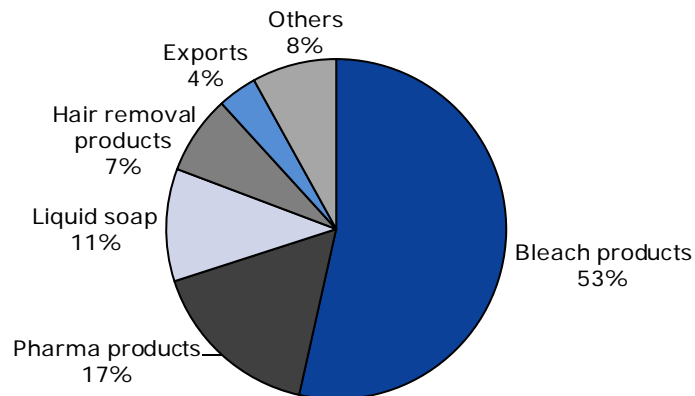
Year to March	FY07	FY08	FY09E	FY10E
Revenues (INR mn)	20,413	23,597	27,365	32,614
Rev. growth (%)	18.5	15.6	16.0	19.2
EBITDA (INR mn)	3,432	4,037	4,548	5,490
Net profit (INR mn)	2,831	3,339	3,769	4,471
Shares outstanding (mn)	863	864	864	864
Diluted EPS (INR)	3.3	3.9	4.4	5.2
EPS growth (%)	24.5	18.1	12.9	18.6
Diluted P/E (x)	24.7	20.9	18.5	15.6
EV/EBITDA (x)	20.1	16.3	15.0	12.2
ROAE (%)	61.3	62.8	54.1	49.6

FCPL: Company profile

FCPL began operations in 1982, and was listed in 1994. It currently has a market cap of INR 2 bn, and reported turnover of INR 945 mn in FY08 with a PAT of INR 80 mn. During H1FY09, it reported turnover of INR 545 mn and PAT of INR 97.5 mn. Promoters currently hold ~67% stake in the company, which is expected to go up to 72% post the approval for merger of its marketing venture with itself. The company has a distribution reach of 125,000 outlets and also covers 25,000 parlours. It has manufacturing units in Nashik (Maharashtra) and Baddi (Himachal Pradesh). The Baddi unit enjoys both excise and IT benefits. FCPL exports to UAE, Oman, Yemen, Maldives, Mauritius, Malaysia, Sri Lanka, Bangladesh, Myanmar, and Nepal.

FCPL is present in three major categories viz. consumer products, pharmaceutical products, and specialty chemicals. Consumer products accounts for 77% of revenues and includes brands such as *Oxybleach* (premium cream bleach), *Fem Stratum* (hair conditioners), *Saka* (men's bleach), and *Botanica* (skin firming and anti-wrinkle cream). It also has products in liquid soaps, hair removing cream, hair curlers, fabric softeners, after-shave lotions, amongst others, in the personal care segment. Nearly 70% of its consumer products revenue is, however, contributed by the bleach portfolio. Pharmaceutical products contribute 17% to revenues, with a wide range of products in dermatology (with brands such as *Aloederm*, *Restoderm*, and *Femnicol A*), antibiotics, and others. Specialty chemicals and contract manufacturing contribute 3% each to the consolidated revenues.

Segment-wise revenue break-up



Source: Company, Edelweiss research

Dabur expected to benefit from acquisition synergies

Revenue synergy

- Dabur gets access into the fast-expanding skin care market, at mass price points.
- Higher reach/penetration for FCPL's portfolio through Dabur's distribution network.
- Potential for extending *Fem* brands into other related skin care categories.
- Dabur could expand its international footprint through FCPL's *Fem* and *Jaquiline* brands that have presence in GCC/Middle East markets.
- FCPL's parlour reach (25,000 parlours) to be leveraged for promoting Dabur's personal care portfolio.

Cost synergy

- Combined businesses of both the companies are likely to unlock synergies in sales and distribution, marketing, supply chain, sourcing, and manufacturing.
- FCPL's Baddi unit synergistic with Dabur's own skin care plans.
- Greater efficiencies possible in trade and distribution.
- Combined advertising and sale promotion spends (ASP) can be leveraged to reduce media costs.

Key takeaway from Dabur's conference call

Skin care product platform: Dabur intends to model its skin care business under three platforms viz., herbal (*Gulabari* range), ayurvedic, and synthetic (comprising FCPL products). The *Gulabari* range is likely to be expanded vigorously during the current year, and ayurvedic skin care initiative will also be focused upon. However, post acquisition, Dabur is expected to take a more holistic view of its overall skin care offering. Herbal bleach is currently being developed by FCPL.

Manufacturing synergy: FCPL's Baddi facility is currently running at ~35% capacity and will enjoy tax and excise benefits till FY16. This facility is located near Dabur's new plant in Baddi, and therefore, is expected to be logistically friendly for Dabur. Dabur could also explore manufacturing synergies by looking at manufacturing certain products either in its own facility or at FCPL's.

Expansion of global footprint: Dabur intends to focus on bleach, liquid soaps, and dermatology segments of FCPL, and expand them internationally too. Currently, FCPL is the leader in the INR ~850 mn bleach segment, growing at 15% annually, with 60% market share, followed by Jolen at the No. 2 position with 15% market share. In the hair removal category (INR 1.1 bn in value terms), FCPL has a market share of 7%, and is growing at over 20% annually.

Pay-back period and distribution synergy: FCPL's erstwhile promoters shall not engage in any competitive activity in future, as per the deal agreement. Dabur expects the deal to pay back within the next five-six years on the back of scaling up of business and leveraging of synergy. Dabur is expected to benefit from FCPL's 25,000 parlours–reach, which it could use to cross-sell its personal care products; simultaneously, FCPL's products could access Dabur's distribution reach, especially in the modern and institutional trade arena.

Outlook and valuations: FCPL expensive but a good fit; maintain 'ACCUMULATE'

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Company Description

Dabur has three divisions in India apart from its international operations. Consumer care division (CCD) offers a wide range of products in hair care, oral care, health supplements, digestives and candies, and baby and skin care products, based on ayurveda. The consumer health division (CHD) includes over-the-counter (OTC) products, Asavs, and branded ethical, and classic products. The third division, Dabur Foods produces fruit juices, cooking pastes, sauces, and items for institutional food purchases. Dabur is unique among its FMCG peers because of its positioning as an Indian company whose products are derived from exotic sources such as ancient ayurvedic texts and natural ingredients such as herbs.

The company has various brand leaders in different market segments - *Dabur Chyawanprash*, a health tonic, and *Hajmola* - a digestive tablet. *Real*, launched during 1996-97, has also successfully carved its niche in the market.

Investment Theme

Dabur's broad product portfolio provides a good play on Indian FMCG spend by virtue of its strong presence in less-penetrated and high growth categories. Dabur's positioning on the 'health and wellness' platform, backed by its ANH (ayurvedic/natural/herbal) image is very progressive. This, combined with its demonstrated ability to create new categories and sub-categories, makes it best-placed to capture lifestyle changes-led growth in the FMCG space. Dabur has also demonstrated its ability to make and integrate smart acquisitions (Balsara) that complement its product portfolio, and thereby, drive inorganic growth. Improvement in margins of foods and international businesses are expected to better margins for the consolidated operations.

Key Risks

A slowdown in rural demand due to lower government spending or a monsoon failure could impact Dabur's revenues significantly; the company's products such as *Dabur Chyawanprash* and *Dabur Lal Tail* are prominently sold in the rural areas, and hence, depend on growth in rural demand.

Further, Ayush, the Ayurvedic Association of India, has recently declared strict adherence to ayurvedic norms; the body asked many companies to change the formulation of chyawanprash. Any such changes in future could dampen the sales, especially during the change of formulation, when the product is taken off the shelf.

Financial Statements

Income statement					
(INR mn)					
Year to March	FY06	FY07	FY08	FY09E	FY10E
Net revenues	17,228	20,413	23,597	27,365	32,614
Cost of materials	8,077	9,711	11,010	12,862	15,150
Gross profit	9,151	10,702	12,587	14,503	17,464
Employee costs	1,450	1,667	1,993	2,309	2,840
Advertisement & sales costs	2,217	2,559	2,955	3,489	4,226
Other general expenditure	2,619	3,045	3,602	4,157	4,907
EBITDA	2,866	3,432	4,037	4,548	5,490
Depreciation	269	343	364	420	504
EBIT	2,596	3,090	3,672	4,128	4,986
Other income	133	255	339	401	396
EBIT incl. other income	2,729	3,345	4,012	4,529	5,382
Net interest	163	150	167	157	174
PBT	2,566	3,195	3,844	4,372	5,209
Provision for taxation	300	373	507	603	737
Core PAT	2,266	2,822	3,338	3,769	4,471
Extraordinary items	(127)	-	-	-	-
Profit after tax	2,139	2,822	3,338	3,769	4,471
Minority interest	(3)	(9)	(1)	-	-
Profit after tax after minority interest	2,142	2,831	3,339	3,769	4,471
Equity shares outstanding (mn)	863	863	864	864	864
EPS (INR) basic	2.6	3.3	3.9	4.4	5.2
Diluted shares (mn)	863	863	864	864	864
EPS (INR) fully diluted	2.6	3.3	3.9	4.4	5.2
CEPS (INR)	3.0	3.7	4.3	4.8	5.8
DPS	1.2	1.4	1.5	1.9	2.2
Dividend payout ratio (%)	50.5	49.3	45.4	50.5	50.5

Common size metrics

Year to March	FY06	FY07	FY08	FY09E	FY10E
Cost of materials	46.9	47.6	46.7	47.0	46.5
Employee costs	8.4	8.2	8.4	8.4	8.7
Advertising & sales costs	12.9	12.5	12.5	12.8	13.0
Other general expenditure	15.2	14.9	15.3	15.2	15.0
Depreciation	1.6	1.7	1.5	1.5	1.5
Net interest expenditure	0.9	0.7	0.7	0.6	0.5
EBITDA margin	16.6	16.8	17.1	16.6	16.8
EBIT margin	15.1	15.1	15.6	15.1	15.3
Net profit margin	13.2	13.8	14.1	13.8	13.7

Growth metrics

Year to March	FY06	FY07	FY08	FY09E	FY10E
Revenues	25.4	18.5	15.6	16.0	19.2
EBITDA	38.2	19.8	17.6	12.7	20.7
PBT	45.7	24.5	20.3	13.7	19.1
Net profit	37.5	32.2	18.0	12.9	18.6
EPS	44.3	24.5	18.1	12.9	18.6

Balance sheet		(INR mn)				
As at 31st March	FY06	FY07	FY08	FY09E	FY10E	
Share capital	573	863	864	864	864	
Reserves	4,397	3,933	5,312	7,178	9,392	
Shareholders' funds	4,971	4,796	6,176	8,042	10,257	
Secured loans	808	1,204	976	976	976	
Unsecured loans	235	395	16	16	16	
Borrowings	1,043	1,599	992	992	992	
Minority interests	55	45	48	48	48	
Deferred tax (net)	158	245	33	33	33	
Sources of funds	6,227	6,684	7,248	9,114	11,328	
Gross block	7,215	6,172	7,297	10,175	11,540	
Less depreciation	2,090	2,381	2,644	3,064	3,568	
Net fixed assets	5,125	3,792	4,653	7,111	7,971	
Investments	421	807	2,037	837	837	
<i>Current assets</i>	4,713	6,405	7,739	8,056	9,886	
Inventories	2,128	2,571	3,025	3,316	3,800	
Sundry debtors	744	1,420	1,723	1,712	1,962	
Cash and bank balance	512	607	766	803	1,899	
Loans and advances	1,330	1,807	2,225	2,225	2,225	
Current liabilities	4,361	4,518	7,321	7,030	7,506	
Liabilities	3,028	3,615	4,580	4,289	4,765	
Provisions	1,333	902	2,741	2,741	2,741	
Working capital	352	1,887	418	1,027	2,380	
Misc expenditure	329	198	140	140	140	
Uses of funds	6,227	6,684	7,248	9,114	11,328	
BV (INR)	5.4	5.3	7.0	9.1	11.7	

Cash flow statement		(INR mn)				
Year to March	FY06	FY07	FY08	FY09E	FY10E	
Net profit	2,142	2,831	3,339	3,769	4,471	
Depreciation	269	343	364	420	504	
Deferred tax	35	(14)	8	0	0	
Others	(229)	634	(1,406)	0	(0)	
Gross cash flow	2,217	3,794	2,305	4,189	4,976	
Less: Changes in WC	(90)	1,440	(1,628)	571	257	
Operating cash flow	2,307	2,354	3,933	3,617	4,719	
Less: Capex	2,449	(990)	1,225	2,878	1,365	
Free cash flow	(141)	3,344	2,708	739	3,353	

Cash flow metric		(INR mn)				
Year to March	FY06	FY07	FY08	FY09E	FY10E	
Operating cash flow	2,307	2,354	3,933	3,617	4,719	
Financing cash flow	(1,456)	(1,472)	(1,402)	(1,910)	(2,271)	
Investing cash flow	(488)	(787)	(2,372)	(1,670)	(1,352)	
NET CASH FLOW	364	95	159	37	1,096	
Capex	(2,449)	990	(1,225)	(2,878)	(1,365)	
Dividends paid	(861)	(1,768)	(665)	(1,626)	(1,929)	
Share issuance / (buyback)	0	2	1	0	0	

Ratios

Year to March	FY06	FY07	FY08	FY09E	FY10E
ROAE	55.2	61.3	62.8	54.1	49.6
ROACE	58.4	52.9	66.2	61.2	53.1
Debtor days	16	19	24	23	21
Inventory days	94	88	93	90	86
Payable days	189	167	196	204	175
Current ratio	1.1	1.4	1.1	1.1	1.3
Debt/EBITDA	0.4	0.5	0.2	0.2	0.2
Cash conversion cycle days	(79)	(59)	(79)	(91)	(69)
Debt/Equity	0.2	0.3	0.2	0.1	0.1
Adjusted debt/equity	0.2	0.3	0.2	0.1	0.1
Interest coverage (x)	15.9	20.6	21.9	26.3	28.7

Operating ratios

Year to March	FY06	FY07	FY08	FY09E	FY10E
Total asset turnover	3.0	3.2	3.4	3.3	3.2
Fixed asset turnover	4.3	4.6	5.6	4.7	4.3
Equity turnover	4.0	4.2	4.3	3.8	3.6

Du pont analysis

Year to March	FY06	FY07	FY08	FY09E	FY10E
NP margin (%)	13.2	13.9	14.2	13.8	13.7
Total assets turnover	3.0	3.2	3.4	3.3	3.2
Leverage multiplier	1.4	1.4	1.3	1.2	1.1
ROAE (%)	55.2	61.3	62.8	54.1	49.6

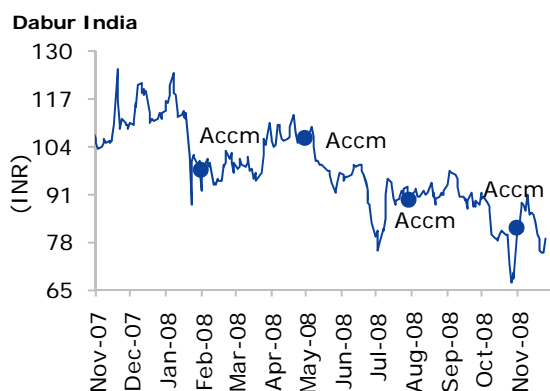
Valuation parameters

Year to March	FY06	FY07	FY08	FY09E	FY10E
Diluted EPS (INR)	2.6	3.3	3.9	4.4	5.2
Y-o-Y growth (%)	44.3	24.5	18.1	12.9	18.6
CEPS (INR)	3.0	3.7	4.3	4.8	5.8
Diluted P/E (x)	30.7	24.7	20.9	18.5	15.6
Price/BV (x)	15.0	15.1	11.6	8.8	6.9
EV/Sales (x)	4.0	3.4	2.8	2.5	2.1
EV/EBITDA (x)	24.2	20.1	16.3	15.0	12.2
Dividend yield (%)	1.4	1.8	1.9	2.3	2.8

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Coverage group(s) of stocks by primary analyst(s): FMCG

Asian Paints, Colgate, Dabur, Godrej Consumer, Hindustan Lever, ITC, Marico and Nestle



Recent Research

Date	Company	Title	Price (INR)	Recons
07-Nov-08	FMCG	Sunny days ahead; <i>Sector Update</i>		
31-Oct-08	Dabur India	Steady performance; <i>Result Update</i>	82	Accum.
29-Oct-08	Godrej Consumer	Margin pain to ease; <i>Result Update</i>	100	Accum.
27-Oct-08	Colgate Pamolive	Higher brand spends; impacts margin; <i>Result Update</i>	393	Buy

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Accumulate	Reduce	Sell	Total
Rating Distribution*	82	56	29	8	178

* 2 stocks under review / 1 rating withheld

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	67	54	57

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 20% over a 12-month period
Accumulate	appreciate up to 20% over a 12-month period
Reduce	depreciate up to 10% over a 12-month period
Sell	depreciate more than 10% over a 12-month period

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