JYOTHY LABORATORIES

INR 620-690

Edelweiss
Ideas create, values protect

Leveraging on distribution reach

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Demonstrated ability to build strong brands with high market shares

Jyothy Laboratories is present in fabric care, household insecticide, utensil cleaners, fragrances, personal care and other allied businesses. The company's management has demonstrated capability of building strong brands in each of these segments. Its brand, *Ujala,* is the market leader in the fabric whitener category with a market share of 68.9% while *Maxo*, in the mosquito repellant coil segment, has cornered 19.7% market share. Further, *Exo* dish wash brand has garnered 15.5% market share in South Indian markets.

Strong distribution reach

The company has a strong distribution reach across the country with over 1,500 sales staff servicing over 2,500 distributors and reaching nearly 2.8 mn outlets across the country. The company's strong distribution reach and rural focus have helped it gain market share in under-penetrated categories like mosquito repellants and fabric whiteners.

Leveraging distribution strengths through third party tie-ups and acquisition

To leverage its extensive distribution reach, Jyothy has formed a joint venture to distribute and market coffee and spiritual dhoops and an agreement to market tea. The company has acquired *More Light* and *Ruby* brands in past and is looking to acquire such smaller brands across categories to leverage its distribution reach.

Sourcing from tax free manufacturing facilities likely to improve profitability

Jyothy's effective income tax rate for the year ending June 2007 was lower at 12.6% mainly be due to manufacturing from tax efficient locations. Currently, the company has 21 manufacturing facilities spread across 14 locations, of which eight are tax efficient units. 60% of *Maxo* production is currently being outsourced, which is expected to decrease to 20% next year and is likely to be completely in sourced a year later with the Assam and Hyderabad units coming on stream. We expect this to aid gross margin expansion and contribute to higher profitability, going forward.

Outlook and valuations: Attractive; recommend SUBSCRIBE

We believe that the gross margins will improve due to increased in-sourcing of *Maxo*, leading to higher profitability. Based on our rough estimates, we expect the company to post EPS of INR 43.6 and INR 50.5 for FY08E and FY09E, respectively, which is a CAGR of 19.4% over FY07-09E. The stock is priced at P/E of 14.2x FY08E and 12.3x FY09E at the lower end of the price band, and at P/E of 15.8x FY08E and 13.7x FY09E at the upper end of the price band. The stock is at a discount to other peers in the FMCG space. We recommend 'SUBSCRIBE' to the issue.

Reuters	:	NA
Bloomberg	:	NA

Market Data

52-week range (INR)	:	NA
Post IPO share in issue (mn)	:	14.5
M cap (INR bn/USD mn)	:	NA
Avg. Daily Vol. BSE/NSE ('000)	:	NA

Share Holding Pattern Post IPO (%)

Promoters	:	68.5
Non Promoters	:	31.5

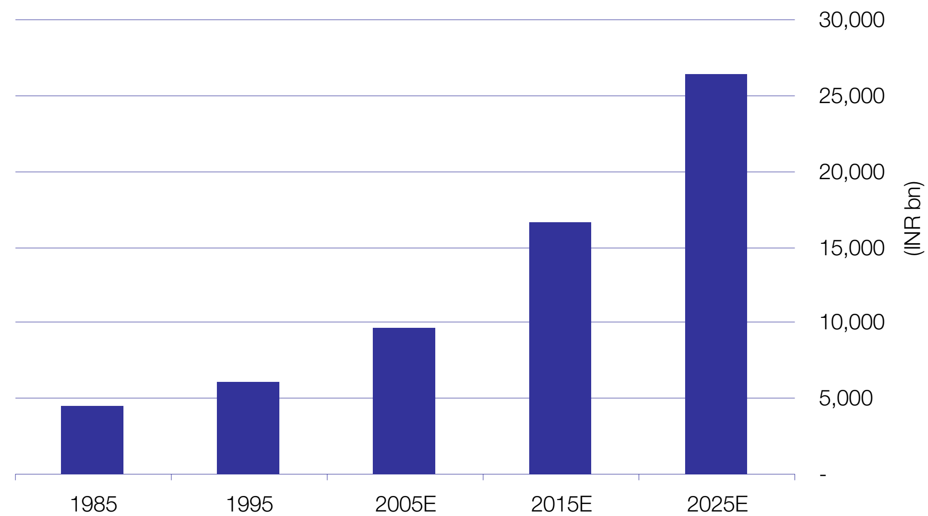
Financials

Year to March	FY04 *	FY05	FY06	FY07
Revenues (INR mn)	3,393	3,130	3,604	4,255
Growth (%)		*(7.8)*	*15.1*	*18.1*
EBITDA (INR mn)	(144.4)	334	463	530
Net profit (INR mn)	(230.8)	333	466	481
Shares outstanding (mn)	15	15	15	15
EPS (INR)	(15.9)	22.9	32.1	33.2
EPS growth (%)		*NA*	*40.0*	*3.3*
ROE (%)	(12.2)	15.3	18.4	16.5

Investment Rationale

The FMCG sector has been a major beneficiary of the booming economy and consequent higher purchasing power. This phenomenon has been further boosted by good monsoons, resulting in increase in the purchasing power of rural areas. Rural consumption is expected to grow at 5.1% (CAGR) from INR 9,688 bn to INR 26,383 bn over 2005-25E, according to McKinsey. Companies with a strong rural presence, such as Jyothy Laboratories, are likely to be better prepared to cash in on this growth opportunity.

Chart 1: Rural consumption—On the rise



Source: MGI India Consumer Demand Model, v1.0

Good mix of brands in portfolio

Jyothy Laboratories is present in fabric care, household insecticide, utensil cleaners, fragrances, personal care and other allied businesses. The company's management has demonstrated capability of building strong brands in each of these segments. Its flagship brand, *Ujala* contributed nearly 45% to the company's topline in 2007 and is currently the undisputed leader in the fabric whitener category. *Maxo,* its brand in the mosquito repellant segment, contributed 39% to the topline in 2007, while the rest was contributed by other brands.

Fig. 1: Jyothy Laboratory's Brand Portfolio

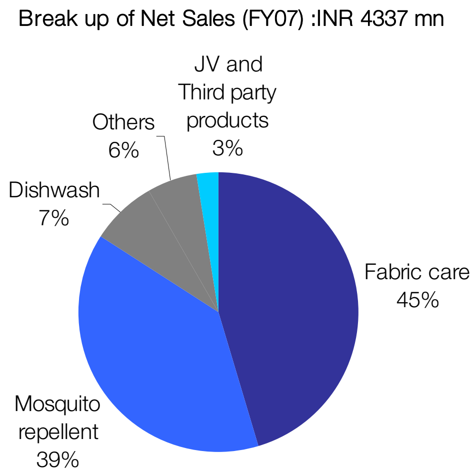
Jyothy Laboratories
- Fabric Care → Ujala Supreme | Ujala Washing Powder | Stiff & Shine
- Household Insecticide → Maxo Cyclothrin Coil | Maxo Cyclothrin Liquid | Maxo Aerosol
- Utensil Cleaners → Exo Dish Wash Bar | Exo Dish Wash Liquid
- Fragrances → Maya
- Personal Care → Jeeva Naturals
- Allied Business → Continental Speciale | Godrej Tea | Ekta`s Dhoop

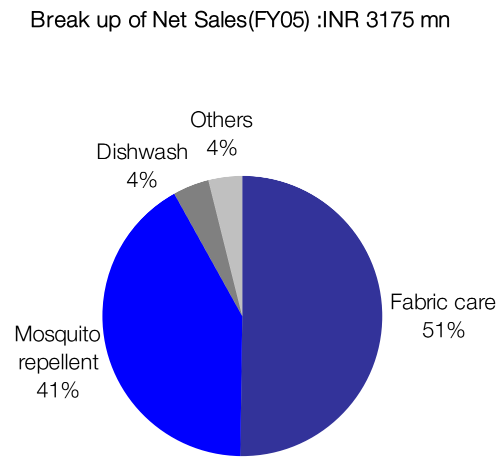
Source: Company, Edelweiss research

Jyothy has a good mix of brands in its portfolio, with *Ujala* being a cash cow, *Maxo* a star performer, and *Exo* a strong growing brand. The present structure is likely to help the company grow and establish its growing brands with the help of a strong distribution network.

Jyothy is primarily known for its fabric whitener, *Ujala*, which is the market leader with about 68.9% value market share. Over the years, the company's dependence on *Ujala* has been declining; its contribution to total net sales has declined from 51% in 2005 to 45% in 2007. The mosquito repellent category, which contributed 39% to the topline in 2005, has seen it rise to 41% in 2007.

Chart 2: Reduced dependence on *Ujala*





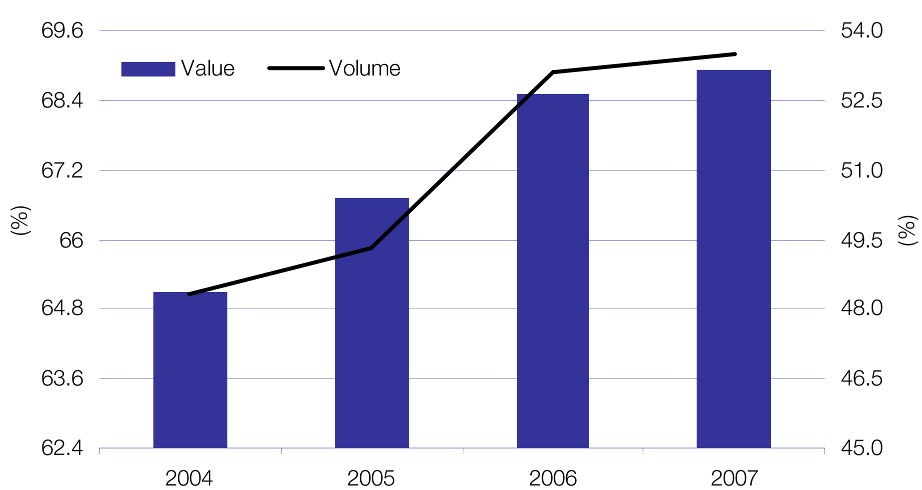
Source: Company, Edelweiss research

Improving market share across categories

Jyothy's brand, *Ujala,* is the market leader in the fabric whitener category, with a market share of 68.9% (in value terms as of June 30 2007; *Source: AC Nielsen*), while *Maxo* coils has cornered 19.7% market share (in value terms as of June 30, 2007; *Source: AC Nielsen*). Further, *Exo* has garnered 15.5% (in value terms) market share in South India. These brands have strong presence in their respective categories and enjoy a high brand recall.

Ujala enjoys high brand recall. As per estimates from Marketpulse-IMRB's Household Purchase Panel, *Ujala* was purchased by 75.4 mn surveyed households during April 1, 2006 to March 31, 2007. The company can leverage the brand by extending *Ujala Stiff and Shine* nationally in 2007.

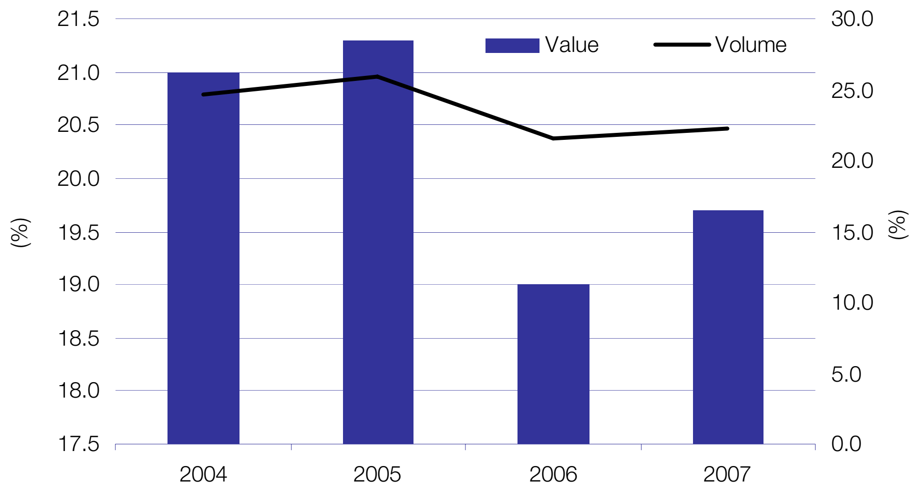
Chart 3: Ujala's market share—an undisputed leader



Source: Company

Potential for growth in the mosquito repellant category is high in India as current penetration of mosquito coils in the country is a meager 27%, against average 70% in other developing countries. Increasing awareness about mosquito related disease in India (dengue, chickengunia etc.,) will also contribute positively to *Maxo's* sales. We expect *Maxo* to register robust growth and increase its contribution in Jyothy's sales. Further, the company plans to increase the brand's market share by introducing vaporizers and aerosol-based mosquito repellants.

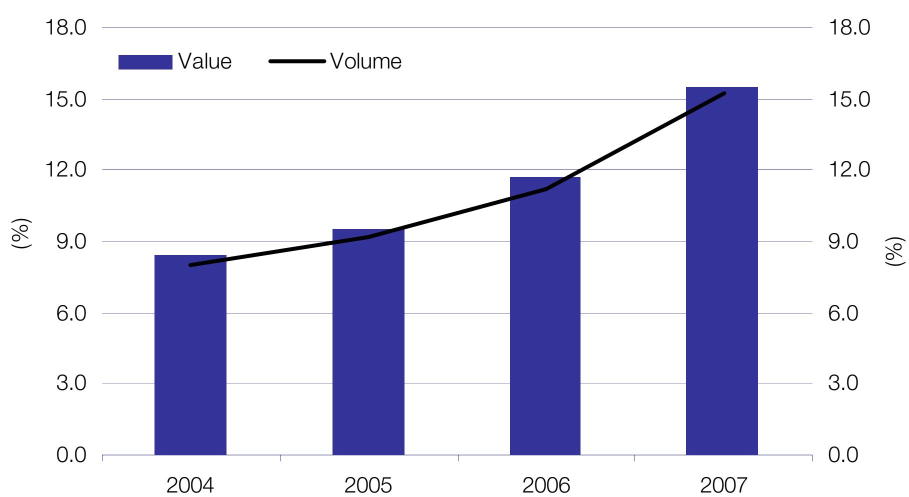
Chart 4: Maxo's market share—sustained and growing



Source: Company

Exo, which is currently present only in Southern states of India, will be expanded to other states. The dish wash has reported robust growth of 54% CAGR in sales during the past two years. We expect *Exo* to register strong growth with its national expansion.

Chart 5: Exo's market share in South India has been consistently increasing



Source: Company

Strong rural distribution reach

The company has a strong distribution reach across the country with over 1,500 sales staff, which services over 2,500 distributors and reaches nearly 2.8 mn outlets across the country. Jyothy has built an innovative product range catering to the masses, while retaining its value for money (VFM) positioning. The company's rural focus has helped it gain market share in under-penetrated categories like mosquito repellants and dish wash.

Acquisition and third party distribution to aid growth

To leverage its extensive distribution reach, Jyothy has formed a joint venture with Continental Speciale (India) (CSPL) to market and distribute latter's coffee brand. Balaji Telebrands, a 50:50 JV with Ekta Kapoor, markets and distributes spiritual dhoop. Also, Jyothy has an agreement with Godrej Tea to market the latter's tea products. The company has acquired *More Light* and *Ruby* brands for INR 9.5 mn each to strengthen its position in the whiteners category. The company plans to acquire smaller brands in various categories to grow inorganically and leverage its distribution network. It also plans to enter Bangladesh and other markets through joint ventures or the acquisition route.

Sourcing from tax free manufacturing facilities likely to improve profitability

The effective income tax rate for the year ending June 2007 for Jyothy was 12.6%; the lower rate can mainly be attributed to manufacturing from tax efficient locations. Currently, the company has 21 manufacturing facilities spread across 14 locations, of which eight are tax efficient units. 60% of *Maxo* production is currently being outsourced, which is expected to decrease to 20% next year and is likely to be completely in-sourced a year later with the Assam and Hyderabad units coming on stream. We expect this to aid gross margin expansion and contribute to higher profitability, going forward.

Outlook and valuations: Attractive; recommend SUBSCRIBE

We expect Jyothy to register 13% CAGR in net sales in FY07-09E. We believe that the gross margins will improve due to increased in-sourcing of *Maxo*, leading to higher profitability. Based on our rough estimates, we expect the company to post EPS of INR 43.6 and INR 50.5 for FY08E and FY09E, respectively which is a CAGR of 19.4% over FY07-09E. The stock is priced at P/E of 14.2x FY08E and 12.3x FY09E at the lower end of the price band, and at P/E of 15.8x FY08E and 13.7x FY09E at the upper end of the price band. The stock is at a discount to other peers in the FMCG space. We recommend 'SUBSCRIBE' to the issue.

Table 1: Peer comparison

Company	CMP (INR)	EPS (INR)		P/E (x)	
	(as on Nov 22, 2007)	FY08E	FY09E	FY08E	FY09E
Dabur	109	4.1	4.9	26.6	22.3
Colgate	382	15.9	20.6	24.0	18.5
Godrej Consumer	129	6.9	8.2	18.7	15.7
Marico	67	2.6	3	25.9	22.4
Nestle*	1400	44.6	52.8	31.4	26.5
Jyothy Laboratories	620-690	43.6	50.5	14.2-15.8	12.3-13.7

Source: Edelweiss research

*Note: * For Nestle it is CY07E and CY08E respectively.*

Risks and Concerns

- **High dependence on *Ujala* and *Maxo* brands**

  Ujala contributed 45% and *Maxo* 39% to the company's gross sales in 2007. More than 60% of the company's profits are obtained from the former and hence any adverse business conditions including aggressive competition or new entrants could dent the company's profitability.

- **Advertising cost could inflate**

  Jyothy spent about 18% of its net sales in FY07 on advertisements and sales promotion, which was higher compared to other FMCG companies. *Exo's* expansion and other product launches can result in higher advertising and sales promotion expenses. Also, increased competitive activity can adversely affect the company's margins.

- **Higher dependence on South India**

  The Company derives a significant proportion of its revenues from South India. Any adverse business conditions, including harsh climate or change in regional regulations, can impact the company's sales from the region.

- **Slowdown in rural spending**

  Jyothy derives a substantial portion of its revenue from rural India. A slowdown in the economy or a bad monsoon can lead to slower rural growth and lower rural spending. This could, in turn, affect the company's performance.

Company Description

Jyothy Laboratories started in 1983 as a proprietary firm by Mr. M P Ramachandran, was incorporated in 1992. Its key brands include *Ujala, Maxo, Exo, Jeeva*, and *Maya* encompassing fabric care, household insecticide, surface cleaning, personal care, and air care segments in the Indian FMCG market.

Jyothy is primarily known for its fabric whitener *Ujala*, which is the market leader with about 68.9% value market share. Over the years, the company has strategically worked towards reducing its dependence on *Ujala.* As a result, *Ujala*'s contribution to total net sales has declined from 51% in 2005 to 45% in 2007. At the same time, share of mosquito repellent category has increased to 41% in FY07 from 39% in FY05. Jyothy markets dishwash bars, liquids, and scrubbers under the *Exo* brand, which contributed 7.3% to total net sales in 2007. Other products under the kitty include *Jeeva* bath soaps and *Maya* incense sticks.

In order to leverage on its strong distribution network, the company has adopted a strategy of entering into joint ventures with other companies to distribute and market their products. It has one such JV with Continental Speciale (India) (CSPL) to market and distribute latter's coffee brand. Similarly, it has a 50:50 JV with Ekta Kapoor called Balaji Tele-brands that distributes and markets spiritual dhoop. In addition, Jyothy has an agreement with Godrej Tea to market latter's tea products. The company has acquired *More Light* and *Ruby* brands for INR 9.5 mn each to strengthen its position in the whiteners category.

Management Details

Mr. M. P. Ramachandran, (Promoter and CMD) holds a postgraduate degree in Financial Management from the University of Mumbai. He began his career as an accountant in 1971 in Mumbai. He set up Jyothy Laboratories in 1983 and has been instrumental in the company's success. He has over 36 years of experience in sales, production, and general management. In 2003 and 2004, he was nominated by *The Economics Times* for the "Entrepreneur of the Year Award".

Mr. K. Ullas Kamath, (Deputy Managing Director) is a qualified Chartered Accountant and Company Secretary and holds a bachelor's degree in Law and master's degree in Commerce. He has also participated in the Advanced Management Program at Wharton Business School. His responsibilities include business development, new projects, sales, financial management and supervision of day-to-day operations. He has been associated with Jyothy since its incorporation and has been on its board since 1997.

Ms. M. R. Jyothy, (Promoter and Executive Director), holds a bachelor's degree in Commerce from the University of Mumbai and an MBA from Wellingker's Management Institute, Mumbai. She has been on Jyothy's board since October 2005 and handles sales administration, marketing, and brand communication.

Issue Details

Jyothy is entering the market with an initial public offering (IPO) of 4.43 mn shares of face value of INR 5 at a price band of INR 620 - INR 690. The issue size is INR 27.5 bn at the lower price band and INR 30.6 bn at the upper end of the price band. The issue is open from November 22 to November 27, 2007.

The offer constitutes 31.5% of the post issue paid up capital of the company. Post issue, promoters' stake will remain at 61.5%. The major objective of the offer is to provide exit route to its existing investors, which include Canzone Limited, ICICI Bank Canada, ICICI Bank UK PLC, South Asia Regional Fund, and CDC Investment Holdings, by selling their stakes through this offer.

The IPO has received CARE IPO grade 4 indicating above average fundamentals.

Offer Details

Issue size Upper band (INR mn)	3,057
Issue size Lower band (INR mn)	2,747
No. of shares - Offer for sale (mn)	4.4
Face value (INR)	5
Price band (INR)	620-690
Issue mode	100% book Building
Book opening date	22-Nov-07
Book closing date	27-Nov-07
Pre issue - No of shares (mn)	14.5
Post issue - No. of shares (mn)	14.5
Market capitalization Lower band (INR mn)	8,999
Market capitalization Upper band (INR mn)	10,014

Source: Company

Shareholding pattern

	Before issue		Post issue	
Share holding pattern	No. of shares (mn)	% holding	No. of shares (mn)	% holding
Promoters/ Promoter Group	9.94	68.5	9.94	68.5
Canzone Ltd	0.78	5.4	-	-
ICICI Bank Canada	1.45	10.0	-	-
ICICI Bank UK PLC	1.41	9.8	-	-
South Asia Regional Fund	0.39	2.7	-	-
CDC Investment Holding Ltd	0.39	2.7	-	-
Public/Others	0.15	1.0	4.58	31.5
Total	14.51	100.0	14.51	100.0

Source: Company

Financial Statement

Income statement (INR mn)

Year ended 30 June	FY04 *	FY05	FY06	FY07
Gross sales	3,463	3,176	3,663	4,338
Excise duties	70	45	59	84
Net sales	3,393	3,130	3,604	4,255
Materials consumed	1,609	1,382	1,431	1,897
Gross profit	1,784	1,749	2,173	2,358
Employee costs	260	280	345	419
Advertisement & sales costs	1,028	579	674	738
Other expenditure	640	555	691	672
EBITDA	(144)	334	463	530
Depreciation/Amortization	58	50	57	66
EBIT	(202)	284	406	464
Other income	57	60	121	126
EBIT incl. other income	(145)	344	528	590
Net interest paid	20	1	1	2
PBT	(165)	344	526	588
Provision for taxation	(32)	60	92	74
PAT before prior period items	(133)	284	434	514
Prior period items (net of tax)	25	60	35	0
PAT beforea Adjustments	(158)	224	399	514
Adjustments	(73)	109	67	(33)
Profit after tax	(231)	333	466	481
Dividends inc. ESOP	0	25	103	104
Retained profit	(231)	308	362	377
Shares outstanding (mn)	15	15	15	15
EPS (INR) fully diluted	(15.9)	22.9	32.1	33.2
CEPS (INR) fully diluted	(11.9)	26.4	36.0	37.7
Dividend per share (INR)	0.0	1.7	7.1	7.2
Dividend payout ratio (%)	0.0	7.4	22.2	21.6

Common size metrics

Year ended 30 June	FY04 *	FY05	FY06	FY07
Materials consumed	47.4	44.1	39.7	44.6
Employee expense	7.7	9.0	9.6	9.8
Advertising and sales promotion	30.3	18.5	18.7	17.3
Operating expenditure	18.8	17.7	19.2	15.8
EBIDTA margin	(4.3)	10.7	12.8	12.4
EBIT margin	(6.0)	9.1	11.3	10.9
Net profit margin	(6.8)	10.6	12.9	11.3

Growth metrics

Year ended 30 June	FY04 *	FY05	FY06	FY07
Net revenues		(7.8)	15.1	18.1
EBITDA		(331.4)	38.6	14.4
EBIT		(240.5)	43.0	14.1
Net profit		(244.2)	40.0	3.3
EPS		(244.2)	40.0	3.3

Balance sheet (INR mn)

Year ended 30 June	FY04 *	FY05	FY06	FY07
Share capital	73	73	73	73
Reserves and surplus	1,817	2,100	2,466	2,843
Shareholders funds	1,889	2,172	2,538	2,916
Borrowings	34	0	1	6
Secured loans	34	0	0	0
Unsecured loans	0	0	1	6
Deferred tax (net)	5	20	53	61
Funds employed	1,928	2,193	2,592	2,983
Net fixed assets	653	770	844	1,077
Intangible assets	19	15	11	28
Capital work in progress	204	94	84	573
Investments	23	18	9	9
Current assets, loans and adv.	1,259	1,617	1,953	1,736
Inventories	217	199	250	414
Sundry debtors	261	334	324	407
Cash and bank balance	600	893	1,277	770
Other current assets	3	3	3	2
Loans & advances	178	189	99	143
Current liabilities	231	321	310	441
Liabilities	211	280	237	390
Provisions	20	41	72	50
Working capital	*1,028*	*1,296*	*1,644*	*1,295*
Misc expen not written off	0	0	0	0
Uses of funds	1,928	2,193	2,592	2,983
BV (INR)	130.2	149.7	174.9	200.9

Cash flow statement (INR mn)

Year ended 30 June	FY04 *	FY05	FY06	FY07
CFO before wkg cap changes	(264)	394	566	555
Cash for working capital	458	52	37	(1)
Income tax and dividend tax	(20)	(3)	(47)	(77)
Other operating cash flows	(149)	(53)	(44)	(154)
Net operating cash flow	26	390	511.91	324.41
Net purchase of fixed assets	(163)	(90)	(121)	(808)
Net purchase of investments	0	1	17	0
Other investing cash flows	50	38	72	76
Net cash flow from investing	(113)	(51)	(31)	(731)
Proceeds from LTB/STB	(30)	(33)	1	4
Proceeds from share capital	0	0	0	0
Dividend payments	(16)	(12)	(95)	(103)
Other financing cash flows	(20)	(1)	(1)	(2)
Net cash flow from financing	(66)	(46)	(96)	(101)
Net cash flow	(153)	293	385	(508)

Ratios

Year ended 30 June	FY04 *	FY05	FY06	FY07
ROE	(12.2)	15.3	18.4	16.5
ROCE	(12.2)	15.2	18.0	16.1
Debtor (days)	28	38	32	34
Inventory (days)	23	23	25	35
Fixed assets T/o	5.2	4.1	4.3	4.0
Debt/Equity	0.0	0.0	0.0	0.0
Interest coverage	(7.2)	430.6	358.9	329.6

Valuation parameters

Year ended 30 June	FY04 *	FY05	FY06	FY07
EPS (diluted) (INR)	(15.9)	22.9	32.1	33.2
Y-o-Y growth (%)		*(244.2)*	*40.0*	*3.3*
CEPS	(11.9)	26.4	36.0	37.7
Y-o-Y growth (%)		*(321.3)*	*36.5*	*4.8*

** For 15 mth period ending June 30, 2004*

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

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

Recent Research

Date	Report	Title	Price (INR)	Recos
31-Oct-07	Hindustan Unilever	Lock out impacts profits; *Result Update*	208	Accum.
26-Oct-07	ITC	Margin compression, cigarettes intact *Result Update*	181	Accum.
26-Oct-07	Colgate Palmolive	Promotional expenses hit margins *Result Update*	384	Buy.
25-Oct-07	Dabur India	Sustained growth momentum continues *Result Update*	108	Accum.

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Accumulate	Reduce	Sell	Total
Rating Distribution*	102	43	21	3	184

* 13 stocks under review / 2 rating withheld

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	89	64	31

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