

## EARNINGS REVIEW ITC (ITC.BO)

Buy

### In line with expectations: Robust cigarette profit growth in FY09

#### What surprised us

ITC's FY2009 results were broadly in line with our forecast, with EPS up 5% yoy to Rs8.64 vs. our expectation of 6% growth, despite a lower-than-expected performance in 4Q. Cigarette segment volume was down 3%-3.5% yoy, in line with our expectation, while its EBIT growth was strong at 15% and margin rose 140 bp yoy. FMCG – Others losses were below Rs5 bn in FY2009, a tad better than we forecast. However, EBIT in Hotels was lower than we forecast, reflecting a high base in 4QFY08 and a significant industry slowdown. Agri Business revenue and EBIT also fell short of our estimates, reflecting lower soya volumes and portfolio rationalization.

#### What to do with the stock

Maintain Buy on ITC; our 12-mo P/E-based TP of Rs211 implies 15% upside. FY2009 was a year of modest EPS growth as we had forecast, but we expect an acceleration to double-digit earnings growth in FY2010E, led by 1) robust cigarette EBIT growth – ITC delivered 15% pa growth in FY08-09 despite steep tax hikes and an increase in contraband volumes; ITC's consistent market share gains over the years reflect the strength of its brands and pricing power over peers; 2) we expect FMCG – Others losses to narrow; 3) Hotels should also stabilize in FY10E, while we expect strong growth in the paper business. **Risks** include adverse cigarette tax hikes, or any prolonged weakness in FMCG – Others and Hotels.

#### ITC FY2009 and 4QFY09 snapshot

Income Statement (Rs mn)	4QFY08	4QFY09E	4QFY09A	% yoy	FY08	FY09E	FY09A	% yoy
Gross sales	58,461	68,587	58,707	0%	213,559	241,316	231,435	8%
Less: Excise duty	(19,117)	(24,282)	(19,789)		(74,084)	(82,047)	(77,554)	
Net sales	39,344	44,305	38,918	-1%	139,475	159,268	153,881	10%
Other income	1,637	1,649	879		6,109	6,119	5,349	
Total Income	40,981	45,954	39,797	-3%	145,584	165,388	159,230	9%
EBIT	10,869	12,794	12,055	11%	45,764	49,180	48,441	6%
Interest (net)	27	7	137		46	54	183	
Net Profit before tax	10,842	12,787	11,918	10%	45,718	49,127	48,257	6%
Tax expense	3,485	4,123	3,828		14,517	15,917	15,622	
Net Profit after tax	7,356	8,664	8,090	10%	31,201	33,210	32,636	5%
Basic EPS (Rs)	1.95	2.30	2.15	10%	8.29	8.82	8.66	4%
Fully Diluted EPS (Rs)	1.93	2.28	2.14	11%	8.25	8.78	8.64	5%

Source: Company data, Goldman Sachs Research estimates.

#### INVESTMENT LIST MEMBERSHIP

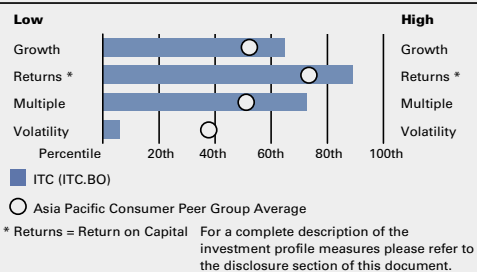
Asia Pacific Buy List

#### Coverage View: Neutral

India:  
Consumer Staples

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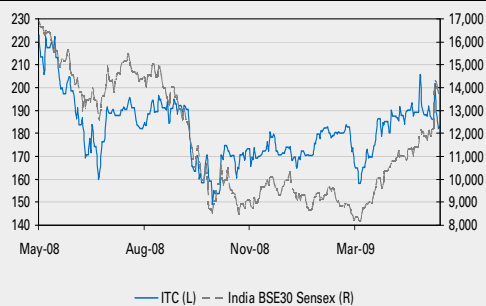
#### Investment Profile



Key data	Current
Price (Rs)	183.25
12 month price target (Rs)	211.00
Market cap (Rs mn / US\$ mn)	691,658.3 / 14,598.9
Foreign ownership (%)	--

	3/08	3/09E	3/10E	3/11E
EPS (Rs)	8.25	8.78	10.53	12.29
EPS growth (%)	15.1	6.4	19.9	16.8
EPS (diluted) (Rs)	8.25	8.78	10.53	12.29
EPS (basic pre-ex) (Rs)	8.29	8.82	10.58	12.35
P/E (X)	22.2	20.9	17.4	14.9
P/B (X)	5.7	5.0	4.4	3.8
EV/EBITDA (X)	14.4	13.5	11.1	9.4
Dividend yield (%)	1.9	2.0	2.4	2.8
ROE (%)	27.7	25.7	27.0	27.4

#### Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	1.7	7.4	(17.8)
Rel. to India BSE30 Sensex	(35.3)	(31.1)	0.0

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 5/22/2009 close.

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# ITC: Summary financials

Profit model (Rs mn)	3/08	3/09E	3/10E	3/11E	Balance sheet (Rs mn)	3/08	3/09E	3/10E	3/11E
<b>Total revenue</b>	<b>139,475.3</b>	<b>159,268.3</b>	<b>184,677.4</b>	<b>211,025.4</b>	Cash & equivalents	5,702.5	2,787.5	5,461.8	12,137.2
Cost of goods sold	(77,585.7)	(90,128.4)	(102,415.6)	(115,735.4)	Accounts receivable	7,369.3	8,508.9	9,866.3	11,274.0
SG&A	(22,234.8)	(26,078.8)	(29,757.4)	(33,119.9)	Inventory	40,505.2	47,383.0	56,023.0	65,605.2
R&D	--	--	--	--	Other current assets	16,615.7	17,446.5	18,318.8	19,234.7
Other operating profit/(expense)	2,535.9	2,670.2	2,795.2	2,926.5	<b>Total current assets</b>	<b>70,192.7</b>	<b>76,125.8</b>	<b>89,669.9</b>	<b>108,251.1</b>
<b>EBITDA</b>	<b>46,575.3</b>	<b>51,227.5</b>	<b>61,738.7</b>	<b>72,639.6</b>	Net PP&E	72,956.5	87,952.5	102,781.5	116,340.8
Depreciation & amortization	(4,384.6)	(5,496.2)	(6,439.0)	(7,543.0)	Net intangibles	0.0	0.0	0.0	0.0
<b>EBIT</b>	<b>42,190.7</b>	<b>45,731.3</b>	<b>55,299.6</b>	<b>65,096.6</b>	Total investments	29,345.5	29,345.5	29,345.5	29,345.5
Interest income	1,064.1	954.8	1,002.5	1,052.6	Other long-term assets	0.0	0.0	0.0	0.0
Interest expense	(46.1)	(53.6)	(53.6)	(53.6)	<b>Total assets</b>	<b>172,494.7</b>	<b>193,423.8</b>	<b>221,796.9</b>	<b>253,937.4</b>
Income/(loss) from uncons. subs.	0.0	0.0	0.0	0.0	Accounts payable	27,396.7	30,544.6	35,417.6	40,470.6
Others	2,509.0	2,494.4	2,494.4	2,494.4	Short-term debt	0.0	0.0	0.0	0.0
<b>Pretax profits</b>	<b>45,717.7</b>	<b>49,126.8</b>	<b>58,742.9</b>	<b>68,590.0</b>	Other current liabilities	16,926.3	17,822.1	20,911.1	24,000.1
Income tax	(14,516.7)	(15,917.1)	(18,915.2)	(22,086.0)	<b>Total current liabilities</b>	<b>44,323.0</b>	<b>48,366.7</b>	<b>56,328.6</b>	<b>64,470.7</b>
Minorities	0.0	0.0	0.0	0.0	Long-term debt	2,144.3	2,144.3	2,144.3	2,144.3
<b>Net income pre-preferred dividends</b>	<b>31,201.0</b>	<b>33,209.7</b>	<b>39,827.7</b>	<b>46,504.0</b>	Other long-term liabilities	5,450.7	5,450.7	5,450.7	5,450.7
Preferred dividends	0.0	0.0	0.0	0.0	Total long-term liabilities	7,595.0	7,595.0	7,595.0	7,595.0
<b>Net income (pre-exceptionals)</b>	<b>31,201.0</b>	<b>33,209.7</b>	<b>39,827.7</b>	<b>46,504.0</b>	<b>Total liabilities</b>	<b>51,918.0</b>	<b>55,961.7</b>	<b>63,923.6</b>	<b>72,065.7</b>
Post-tax exceptionals	0.0	0.0	0.0	0.0	Preferred shares	0.0	0.0	0.0	0.0
<b>Net income</b>	<b>31,201.0</b>	<b>33,209.7</b>	<b>39,827.7</b>	<b>46,504.0</b>	<b>Total common equity</b>	<b>120,576.7</b>	<b>137,462.1</b>	<b>157,873.3</b>	<b>181,871.7</b>
EPS (basic, pre-except) (Rs)	8.29	8.82	10.58	12.35	Minority interest	0.0	0.0	0.0	0.0
EPS (basic, post-except) (Rs)	8.29	8.82	10.58	12.35	<b>Total liabilities &amp; equity</b>	<b>172,494.7</b>	<b>193,423.8</b>	<b>221,796.9</b>	<b>253,937.4</b>
EPS (diluted, post-except) (Rs)	8.25	8.78	10.53	12.29	<b>BVPS (Rs)</b>	<b>32.00</b>	<b>36.44</b>	<b>41.86</b>	<b>48.22</b>
DPS (Rs)	3.50	3.71	4.41	5.11					
Dividend payout ratio (%)	42.3	42.0	41.7	41.4					
Free cash flow yield (%)	0.9	1.5	2.5	3.5					
<b>Growth &amp; margins (%)</b>	<b>3/08</b>	<b>3/09E</b>	<b>3/10E</b>	<b>3/11E</b>	<b>Ratios</b>	<b>3/08</b>	<b>3/09E</b>	<b>3/10E</b>	<b>3/11E</b>
Sales growth	14.7	14.2	16.0	14.3	ROE (%)	27.7	25.7	27.0	27.4
EBITDA growth	14.7	10.0	20.5	17.7	ROA (%)	19.4	18.2	19.2	19.6
EBIT growth	14.1	8.4	20.9	17.7	ROACE (%)	28.5	25.7	26.9	28.1
Net income growth	15.6	6.4	19.9	16.8	Inventory days	174.2	178.0	184.3	191.8
EPS growth	15.4	6.4	19.9	16.8	Receivables days	18.0	18.2	18.2	18.3
Gross margin	44.4	43.4	44.5	45.2	Payable days	119.6	117.3	117.5	119.7
EBITDA margin	33.4	32.2	33.4	34.4	Net debt/equity (%)	(3.0)	(0.5)	(2.1)	(5.5)
EBIT margin	30.2	28.7	29.9	30.8	Interest cover - EBIT (X)	NM	NM	NM	NM
<b>Cash flow statement (Rs mn)</b>	<b>3/08</b>	<b>3/09E</b>	<b>3/10E</b>	<b>3/11E</b>	<b>Valuation</b>	<b>3/08</b>	<b>3/09E</b>	<b>3/10E</b>	<b>3/11E</b>
Net income pre-preferred dividends	31,201.0	33,209.7	39,827.7	46,504.0	P/E (analyst) (X)	22.2	20.9	17.4	14.9
D&A add-back	4,384.6	5,496.2	6,439.0	7,543.0	P/B (X)	5.7	5.0	4.4	3.8
Minorities interests add-back	0.0	0.0	0.0	0.0	EV/EBITDA (X)	14.4	13.5	11.1	9.4
Net (inc)/dec working capital	(4,315.0)	(5,700.2)	(5,996.8)	(6,852.7)	Dividend yield (%)	1.9	2.0	2.4	2.8
Other operating cash flow	(896.1)	0.0	0.0	0.0					
<b>Cash flow from operations</b>	<b>28,037.5</b>	<b>30,511.4</b>	<b>37,775.5</b>	<b>44,699.9</b>					
Capital expenditures	(22,460.6)	(20,492.2)	(21,268.1)	(21,102.3)					
Acquisitions	(275,689.0)	0.0	0.0	0.0					
Divestitures	279,803.1	2,494.4	2,494.4	2,494.4					
Others	0.0	0.0	0.0	0.0					
<b>Cash flow from investments</b>	<b>(18,346.5)</b>	<b>(17,997.8)</b>	<b>(18,773.7)</b>	<b>(18,607.9)</b>					
Dividends paid (common & pref)	(13,571.9)	(15,431.8)	(16,327.6)	(19,416.6)					
Inc/(dec) in debt	(58.5)	0.0	0.0	0.0					
Common stock issuance (repurchase)	446.3	3.3	0.0	0.0					
Other financing cash flows	194.0	0.0	0.0	0.0					
<b>Cash flow from financing</b>	<b>(12,990.1)</b>	<b>(15,428.5)</b>	<b>(16,327.6)</b>	<b>(19,416.6)</b>					
<b>Total cash flow</b>	<b>(3,299.1)</b>	<b>(2,915.0)</b>	<b>2,674.3</b>	<b>6,675.4</b>					

Note: Last actual year may include reported and estimated data.  
Source: Company data, Goldman Sachs Research estimates.

## Analyst Contributors

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**Exhibit 1: ITC delivered 5% EPS growth in FY2009, broadly in line with our estimates**  
 FY2009 and 4Q estimates vs. actuals

Income Statement (Rs mn)	4QFY08	4QFY09E	4QFY09A	% yoy	FY08	FY09E	FY09A	% yoy
FMCG - Cigarettes	35,830	42,703	39,493	10%	138,256	154,361	151,151	9%
FMCG - Others	7,384	8,293	8,388	14%	25,111	30,045	30,140	20%
Hotels	3,393	2,211	2,413	-29%	11,002	10,000	10,203	-7%
Agri Business	10,781	11,259	5,259	-51%	38,684	44,460	38,460	-1%
Paperboards, paper and packaging	6,197	7,844	7,470	21%	23,643	28,593	28,220	19%
Less: Intersegment revenue	(5,124)	(3,722)	(4,317)		(23,137)	(26,144)	(26,738)	
<b>Gross sales</b>	<b>58,461</b>	<b>68,587</b>	<b>58,707</b>	<b>0%</b>	<b>213,559</b>	<b>241,316</b>	<b>231,435</b>	<b>8%</b>
Less: Excise duty	(19,117)	(24,282)	(19,789)		(74,084)	(82,047)	(77,554)	
<b>Net sales</b>	<b>39,344</b>	<b>44,305</b>	<b>38,918</b>	<b>-1%</b>	<b>139,475</b>	<b>159,268</b>	<b>153,881</b>	<b>10%</b>
Other income	1,637	1,649	879		6,109	6,119	5,349	
<b>Total Income</b>	<b>40,981</b>	<b>45,954</b>	<b>39,797</b>	<b>-3%</b>	<b>145,584</b>	<b>165,388</b>	<b>159,230</b>	<b>9%</b>
<b>Segment results</b>								
FMCG - Cigarettes	8,701	10,499	10,814	24%	36,340	41,523	41,838	15%
FMCG - Others	(1,179)	(1,386)	(1,173)		(2,635)	(5,048)	(4,835)	
Hotels	1,428	849	711	-50%	4,108	3,300	3,162	-23%
Agri Business	370	636	531	43%	1,292	2,668	2,562	98%
Paperboards, paper and packaging	1,227	1,637	1,519	24%	4,531	5,204	5,086	12%
<b>Total</b>	<b>10,547</b>	<b>12,235</b>	<b>12,401</b>	<b>18%</b>	<b>43,636</b>	<b>47,647</b>	<b>47,813</b>	<b>10%</b>
Add: Net unallocated expenses/income	322	559	(347)		2,128	1,533	628	
<b>EBIT</b>	<b>10,869</b>	<b>12,794</b>	<b>12,055</b>	<b>11%</b>	<b>45,764</b>	<b>49,180</b>	<b>48,441</b>	<b>6%</b>
Interest (net)	27	7	137		46	54	183	
<b>Net Profit before tax</b>	<b>10,842</b>	<b>12,787</b>	<b>11,918</b>	<b>10%</b>	<b>45,718</b>	<b>49,127</b>	<b>48,257</b>	<b>6%</b>
Tax expense	3,485	4,123	3,828		14,517	15,917	15,622	
<b>Net Profit after tax</b>	<b>7,356</b>	<b>8,664</b>	<b>8,090</b>	<b>10%</b>	<b>31,201</b>	<b>33,210</b>	<b>32,636</b>	<b>5%</b>
Exceptional Items, net of tax	0	0	0		0	0	0	
<b>Net profit available for equity shareholders</b>	<b>7,356</b>	<b>8,664</b>	<b>8,090</b>	<b>10%</b>	<b>31,201</b>	<b>33,210</b>	<b>32,636</b>	<b>5%</b>
<b>Basic EPS (Rs)</b>	<b>1.95</b>	<b>2.30</b>	<b>2.15</b>	<b>10%</b>	<b>8.29</b>	<b>8.82</b>	<b>8.66</b>	<b>4%</b>
<b>Fully Diluted EPS (Rs)</b>	<b>1.93</b>	<b>2.28</b>	<b>2.14</b>	<b>11%</b>	<b>8.25</b>	<b>8.78</b>	<b>8.64</b>	<b>5%</b>
<b>Segment margins</b>								
FMCG - Cigarettes	24.3%	24.6%	27.4%		26.3%	26.9%	27.7%	
FMCG - Others	-16.0%	-16.7%	-14.0%		-10.5%	-16.8%	-16.0%	
Hotels	42.1%	38.4%	29.5%		37.3%	33.0%	31.0%	
Agri Business	3.4%	5.7%	10.1%		3.3%	6.0%	6.7%	
Paperboards, paper and packaging	19.8%	20.9%	20.3%		19.2%	18.2%	18.0%	
<b>Total</b>	<b>18.0%</b>	<b>17.8%</b>	<b>21.1%</b>		<b>20.4%</b>	<b>19.7%</b>	<b>20.7%</b>	

Source: Company data, Goldman Sachs Research estimates.

## Reg AC

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