HSBC Global Research

India FMCG

Volume growth is key

8 June 2009

Percy Panthaki*
Analyst
HSBC Securities and Capital Markets (India) Private Limited
+91 22 2268 1240 percypanthaki@hsbc.co.in

Maya Shivani*
Associate
Bangalore

- **With limited scope for price / margin increase, volume growth is the key**
- **Overweight on Colgate and Dabur, Neutral on HUL, ITC and Marico**

In this report, we (1) analyse trends at FMCG companies as reflected in the results; (2) assess the outlook for the year ahead in light of recent trends. The main insights are:

- Overall sales growth in the FMCG sector continues at 20%+ with the balance tilted towards price growth in large categories. However, recent product price cuts mean that future growth will be dominated by volumes.
- Unorganised/regional competition has become more active as expected, and this is partially responsible for the market share losses of larger players. We believe that market shares will settle at June quarter 2009 levels.
- Although gross margins will expand, the quantum of expansion will be lower than originally estimated due to the recent rally in commodity prices. We estimate gross margin expansion of 55bp for our coverage universe as compared to our earlier estimate of 100bp.
- Focus on cost control should become even more important in light of reduced scope for gross margin improvement. Operating expenses as a percentage of sales declined 20bp y-o-y in the March quarter and will continue to be a focus area in FY10e, resulting in a 50bp EBIT margin increase for our coverage universe.
- The sector has recently re-rated and valuations overall look fair. But we see upside for Dabur and Colgate as these are two volume-backed stories in our coverage and hence rate them Overweight. We are Neutral on ITC, HUL and Marico.

Snapshot of companies under coverage

	Dabur - India	Colgate Palmolive	Hindustan Unilever	ITC	Marico Industries
Ticker	DABUR IN	CLGT IN	HUVR IN	ITC IN	MRCO IN
Market cap (USDm)	2,071	1,404	11,101	16,276	911
Rating	OW (V)	OW	Neutral	Neutral	Neutral (V)
Target price (INR)	123.0	540.0	249.0	193.0	69.4
Current price (INR)	112.9	486.2	239.7	203.1	70.5
PE (on FY09e)	25.0x	22.8x	24.7x	23.0x	21.0x
ROE (last reported FY08)	60.9%	106.1%	92.7%	27.5%	62.5%
% change from 1-Jan-09	34.5%	19.4%	-4.4%	18.3%	22.3%

*Price data as on 3 June 2009.
Source: Company, HSBC

Contents

The road ahead

- Volume growth to drive top line, backed by new products and rural consumer demand
- Volatile commodity prices hint at conservative gross margin expansion
- Controlling overhead costs more important than ever

What will drive top line?

Volumes, not prices

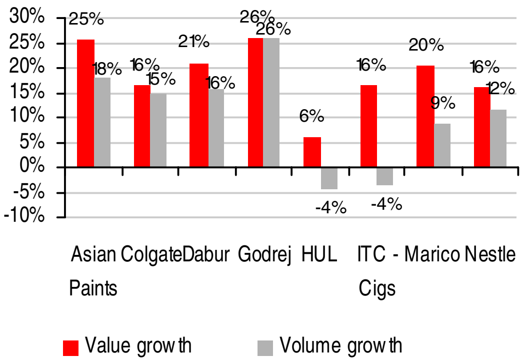
Over October 2008 to March 2009, consumer companies raised prices to varying degrees to protect margins and bottom lines. With commodity costs declining and volume growth slowing due to reduced customer buying, there was downward pressure on product prices.

Companies have cut prices for several products in response in the April to June 2009 period. Marico, for example, has taken a 4% price reduction in its Saffola franchise to regain volume growth. Saffola had suffered over the previous two quarters since the premium to other oil brands had increased.

HUL's sales volume declined 4.2% in the January to March 2009 quarter because of significant price increases, sales volume reduction, and pipeline contraction by traders, in anticipation of price cuts. HUL has now taken price cuts on its soaps and detergents portfolio or increased the pack size to spur volumes.

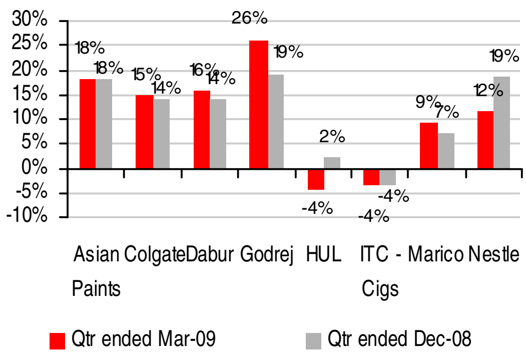
Price growth for consumer companies should be subdued in FY10. Although prices have been cut q-o-q, they will still increase y-o-y due to roll-over pricing, and such an increase will obviously be modest. Sales growth, therefore, will be volume-driven, rather than price-driven, as was the case in FY09.

Volume growth vs total sales growth (qtr. Ended March '09)



Source: Company, HSBC

Volume growth (qtr. ended March '09)



Source: Company, HSBC

New product launches – added boost

Given renewed consumer confidence, new launches and product variants might give the required boost to top line growth. For example, Dabur plans to launch variants in hair oils and shampoos, a new ayurvedic skincare range and a new fruit drink. Marico will build on its functional foods range. HUL will start reaping the benefits of its investments in the water business, and gain from the extension of its hair care (Dove and Clinic All Clear) and skin care (Ponds and Vaseline) ranges.

Additionally, product variants in smaller pack sizes (priced below INR10) are also becoming a focus group across the sector to target mid-income consumers. HUL launched ketchup penny packs in the March 2009 quarter. Currently, small packs or popularly positioned products (PPPs) form 40% of the Indian FMCG market.

Rural India going strong

Rural incomes are holding up strongly due to increase in minimum support prices of agricultural crops over the last two years. We expect this to drive volume growth as per capita consumption increases through the introduction of new users and increase in consumption by existing users. Rural segment growth is an important factor, as rural exposure is 50% each for HUL and Dabur, 25% for Marico and 35% for Colgate (35% is at the company level, but rural exposure in toothpowder is much higher).

Most of the companies that we interact with indicate that rural consumption is growing 200-300bp faster than urban consumption. Factors such as rising rural incomes, healthy agricultural growth, improved consumer sentiment, increasing consumerism across India, increased penetration of the rural market by consumer products should contribute to the high growth and rapid expansion of the consumer industry in rural India.

Gross margins to expand, but lower than anticipated

Commodity costs as seen in the charts on page 13-14 had softened during the December 2008 and March 2009 quarters, but are on a growth trajectory now. Volatile commodity markets could wreak havoc and affect margins. From their troughs, input costs have gone up anywhere between 5% and 75%. Malaysian Palm Oil rose 75.4%, Coffee, 37.5%, Tea, 49.3%, groundnut oil, 12.8% and HDPE, 51.9% (refer table 'Snapshot of movement in commodity prices').

Companies that have strengthened measures to protect gross profit margins will stay ahead. For instance, Dabur has taken to extensive commodity hedging on international exchanges to safeguard margins. So while the competition raised prices by 15-20%, Dabur raised them just 5%. As per a news report (source: LiveMint, April 2009), Dabur plans to source 50% of its basic raw material through trading on international exchanges.

We therefore believe that there will be overall margin expansion, albeit lower than we earlier expected. HUL is likely to be affected the most, with palm oil going up significantly and affecting the bulk of its input costs.

Cost control is key

Operating cost efficiency is the need of the hour as these are to a larger extent within the management's control. While we expect companies on the whole to maintain the ratio of ad spend to sales, there will be a tightening in other overheads, including staff costs.

While we do not expect a major slowdown in annual increments as it is necessary to retain good talent, there could be a slower growth in staff welfare expenses, variable pay, and head count.

HSBC

Category-wise volume growth for coverage universe in FY10e

Dabur		Colgate		HUL		Marico	
Category	Volume growth	Category	Volume growth	Category	Volume growth	Category	Volume growth
Hair care	8.8%	Paste	9.5%	Soaps & detergents	4%	Coconut	7.0%
Oral care	15.0%	Powder	3.0%	Personal products	4%	Other hair oil	11.0%
Health supplements	13.0%	Brush	13.0%	Coffee& Tea	4%	Edible oils	12.5%
Digestives	9.5%			Ice-cream	4%	Other products	7.0%
Baby/skin (incl. Femcare)	114.1%			Foods	4%	International business	15.0%
Home care	16.6%			Exports	4%		
Foods	22.3%			Others	4%		
Consumer health division	3.2%						
International business	15.2%						

Source: HSBC

Other expenses are likely to be closely scrutinised. For example, HUL has declared a 'war on waste' and all discretionary spends such as travel, are being questioned.

Our forecasts

Top line

Volume growth of some categories such as detergents has been adversely impacted by the steep price increases taken last year and might take time to pick up, but in most of the other categories, volume growth is not a cause for concern. On the whole we expect sales growth to be lower than that in FY09e, but in line with the longer term trend.

We estimate the following top line and volume growth for our coverage universe in FY10e:

- **HUL:** 9.7% increase in sales, driven 4% through volume and 5.5% through price. We expect growth to be price-led in H1 and volume-led in H2. Overall sales growth will soften in H2 as price increases on y-o-y basis slow down.
- **ITC (cigarettes):** Low taxation scenario – 7% annualised increase in average selling prices and 6.4% annualised increase in volumes; high taxation scenario – 12.5% annualised increase in average selling prices and 0.2% annualised increase in volumes.
- **Dabur:** 18% sales growth in FY10e with 3% coming from acquisition of Femcare and 15% being organic growth. Of its organic growth we expect 12-13% to be driven by volume and 2-3% by price. It has not increased prices aggressively and hence volumes should be robust. New variants will help.

Snapshot of movement in commodity prices

Commodity	FY09	H1 FY10e	H1 FY10e vs FY09	Current prices	FY10e (Avg of H1 and current prices)	FY10e vs FY09	Trough (October 2008 - March 2009)	Current vs trough
HDPE (USD/MT)	1,492.1	973.8	-34.7%	1,147.0	1,060	-28.9%	755.0	51.9%
Malaysian palm oil (USD/MT)	945.7	496.5	-47.5%	570.0	533.2	-43.6%	325.0	75.4%
Groundnut oil index (INR)	671.4	541.7	-19.3%	542.9	542.3	-19.2%	481.2	12.8%
Copra cochin (INR/quintal)	4,020.1	3,631.1	-9.7%	3,215.0	3,423.1	-14.9%	3,525.0	-8.8%
Indian wholesale price index Tea (INR)	175.9	182.9	4.0%	244.5	213.7	21.5%	163.8	49.3%
Indian wholesale price index Sugar (INR)	152.8	179.1	17.2%	193.4	186.2	21.9%	159.2	21.5%
S&P GSCI Coffee Spot Index (USD)	102.7	91.0	-11.4%	109.3	100.2	-2.5%	79.5	37.5%
S&P GSCI Cocoa Spot Index (USD)	99.9	98.4	-1.5%	103.7	101.0	1.2%	75.1	38.1%
Calcium carbonate (USD/tonne)	98.3	99.0	0.7%	96.0	97.5	-0.8%	97.0	-1.0%
Titanium dioxide (cents/lb)	107.1	114.5	6.9%	116.0	115.3	7.6%	109.0	6.4%
LAB (INR/kg)	98.1	75.1	-23.4%	76.1	75.6	-22.9%	76.1	0.0%

Source: Bloomberg, DataStream, HSBC

- **Colgate:** 13.3% top line growth, largely driven by volume. Industry growth likely to remain robust on increased conversions from toothpowder to toothpaste.
- **Marico:** 12.2% sales growth, of which 9.9% should be from volumes. Non-coconut hair oils and Saffola to lead the growth.

Gross margins

We believe that gross margins will expand since the commodity costs are off their peaks; however, we expect the impact to be subdued due to an uncertain 2H FY10e. While commodities fell sharply from their peaks, they have, in the last few months, gone up quite a bit from their troughs (see table, 'Snapshot of movement in commodity prices').

HSBC forecasts

		FY08	FY09e	FY10e	FY11e
HUL*	Sales growth	11.8%	15.5%	9.7%	10.8%
	Gross margins	47.0%	46.6%	47.0%	47.7%
	EBITDA margins	13.7%	13.8%	14.5%	15.4%
	EBIT margins	12.7%	12.8%	13.5%	14.4%
	EPS growth	16.5%	15.5%	11.5%	13.8%
ITC	Sales growth	15.7%	11.4%	19.1%	13.4%
	Gross margins	59.5%	60.8%	59.7%	60.1%
	EBITDA margins	31.2%	31.1%	30.5%	30.9%
	EBIT margins	27.9%	27.5%	27.4%	27.8%
	EPS growth	14.2%	5.5%	17.9%	14.8%
Colgate	Sales growth	13.8%	15.0%	13.3%	13.9%
	Gross margins	59.4%	59.8%	60.2%	60.4%
	EBITDA margins	20.8%	21.2%	21.6%	21.8%
	EBIT margins	19.4%	19.5%	20.0%	20.2%
	EPS growth	22.9%	22.5%	15.7%	8.7%
Dabur	Sales growth	15.6%	18.8%	17.9%	16.2%
	Gross margins	49.7%	50.9%	52.1%	52.4%
	EBITDA margins	17.3%	16.8%	17.4%	18.0%
	EBIT margins	15.6%	15.0%	15.8%	16.1%
	EPS growth	18.1%	17.2%	18.4%	22.6%
Marico	Sales growth	22.4%	25.4%	12.2%	16.2%
	Gross margins	48.5%	46.5%	48.5%	48.7%
	EBITDA margins	12.9%	12.6%	13.3%	13.5%
	EBIT margins	11.3%	11.1%	11.8%	11.9%
	EPS growth	58.2%	19.1%	17.9%	18.6%

*Adjusted for change in financial year to ensure like for like comparison
Source: Company, HSBC

We therefore believe that gross margin expansion may be lower than we had earlier estimated. For our coverage universe, we now expect a 55bp gross margin expansion instead of 100bp which we had estimated earlier.

EBIT margin

As mentioned earlier, aggressive cost control is likely to partially offset the disappointment in gross margin expansion. We expect operating cost as a percentage of sales in FY10e to contract 43bp y-o-y on weighted average, driving EBIT margin expansion by 50bp (70bp estimated earlier).

Valuation

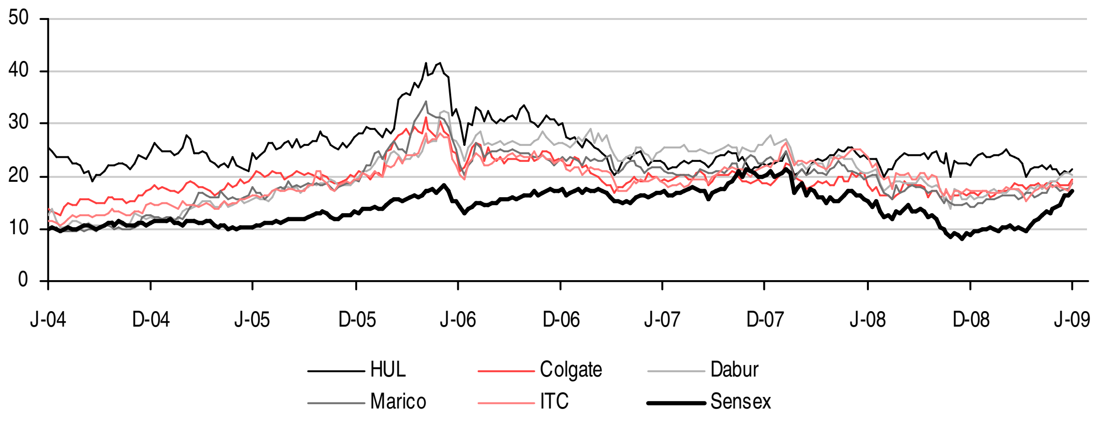
12-month forward PE

	5 yr average	2 yr average	1 year average	3 month average	Curr. PE	Target PE (on March 10e EPS)
HUL	25.3	22.9	22.8	21.4	21.5	23.0
ITC	19.2	20.0	18.4	17.5	19.0	18.6
Colgate	19.6	18.5	17.5	18.5	19.4	22.0
Dabur	20.4	21.2	17.9	18.7	20.3	23.0
Marico	19.2	19.1	16.7	17.2	18.6	19.0
Simple average	**20.8**	**20.3**	**18.7**	**18.7**	**19.8**	**21.1**
HUL premium to sector*	22.1%	12.6%	22.0%	14.5%	9.0%	8.8%
ITC discount to sector*	7.6%	1.7%	1.3%	6.1%	3.8%	12.0%

* Sector as defined by average of these 5 stocks. Price Data as on 3 June 2009
Source: DataStream, HSBC

FMCG stocks under our coverage are trading below their 5-year and 2-year averages, but higher than 1-year and 3-month averages. With the broad stock market recovery, there has been a minor PE re-rating for the FMCG sector too. The large caps' premium to the sector has decreased (or discount has increased) considerably. This is a complete about-turn from the scenario in our last quarterly report dated 6 February 2009, *India FMCG: What the future holds*, where the large caps were trading at higher-than-average premium to the mid-caps. The reason for the premium contracting now is the issue with HUL's performance (volume decline and market share losses) and tax overhang on ITC, due to which investors are wary of buying aggressively despite reasonable valuations. We believe that as and when the performance for HUL improves and if the Central Budget is not

12-month forward PE band chart

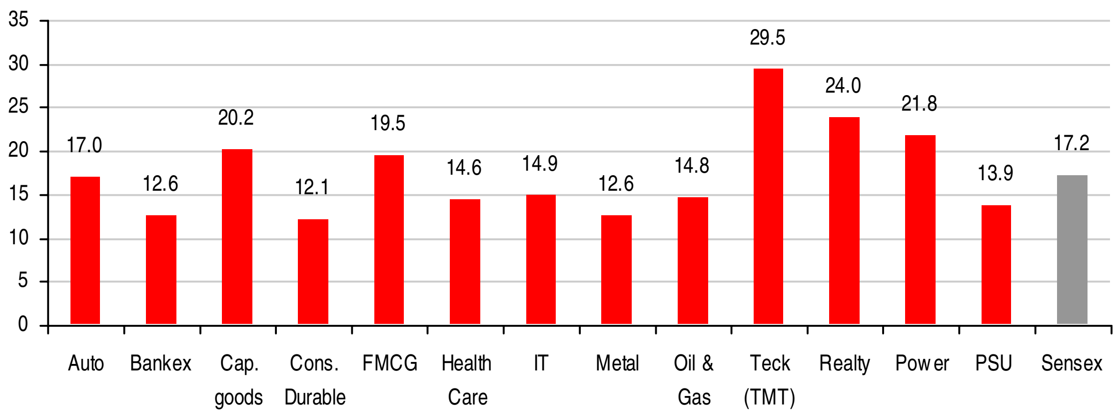


Source: DataStream, HSBC
Price data as on 3 June 2009

adverse for ITC, there could be a re-rating for these stocks. But since both these events are fraught with uncertainty we prefer to keep these stock ratings Neutral.

The BSE FMCG index is currently trading at a 12 month forward PE of 19.5x, as compared to 17.2x for Sensex. The premium to Sensex has reduced considerably – when Sensex hit its trough on 9 March, its PE was 9.6x 12-months forward and BSE FMCG index, at 16.1x – more as a result of other sectors improving, rather than any substantial change in the FMCG sector. However, some investors were getting uncomfortable with the premium that FMCG traded at earlier and those concerns have now been allayed.

12-month forward PE comparison across sectors



Source: Thomson Financial, IBES, HSBC Note: PE is based on 3 June 2009 price

Relative valuation

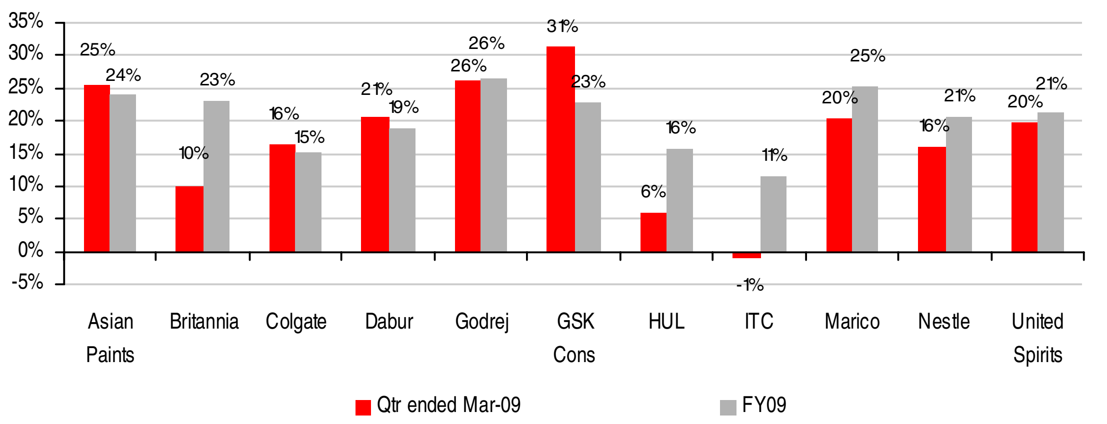
	Mkt cap (USD)	PE FY09	PE FY10	EPS CAGR FY08-10	P/BV FY08	PEG FY09	EBIT margin FY09	ROE FY08	ROA FY08
COLGATE-PALMOLIVE INDIA	1,404	22.8x	19.7x	19.1%	39.5x	1.5x	19.5%	106.1%	33.1%
DABUR INDIA	2,071	25.0x	21.1x	17.8%	15.7x	1.4x	15.0%	60.9%	27.0%
HINDUSTAN UNILEVER	11,101	24.7x	22.1x	11.7%	35.0x	2.1x	12.2%	92.7%	26.7%
ITC	16,276	23.0x	19.6x	11.5%	6.2x	1.3x	27.5%	27.5%	19.2%
MARICO	911	21.0x	19.3x	18.5%	13.6x	2.3x	11.1%	62.5%	22.8%
COVERED STOCKS AVERAGE		**23.3x**	**20.4x**	**15.7%**	**22.0x**	**1.7x**	**17.1%**	**70.0%**	**25.8%**
BRITANNIA INDS.*	833	21.7x	18.4x	9.5%	5.7x	1.2x	5.3%	27.6%	14.1%
GODREJ CONSUMER PRODUCTS*	1,017	27.3x	21.2x	11.6%	188.3x	1.0x	13.5%	108.5%	25.4%
NESTLÉ INDIA*	3,495	29.4x	24.7x	22.6%	35.8x	1.5x	18.3%	106.8%	32.5%
TATA TEA*	1,037	13.3x	11.5x	-47.7%	3.8x	0.9x	14.7%	42.6%	20.5%
UNITED SPIRITS*	2,083	23.5x	18.3x	30.2%	3.7x	0.8x	16.1%	15.8%	3.9%
ASIAN PAINTS*	2,302	27.8x	22.8x	7.9%	11.0x	1.3x	11.7%	43.6%	4.8%
GLXSK.CSM. HEALTHCARE*	773	18.9x	16.9x	12.7%	5.2x	1.6x	16.1%	27.2%	19.2%
UNCOVERED STOCKS AVERAGE		**23.1x**	**19.1x**	**6.7%**	**36.2x**	**1.2x**	**13.7%**	**53.2%**	**17.2%**
SECTOR AVERAGE		**23.2x**	**19.6x**	**10.4%**	**30.3x**	**1.4x**	**15.1%**	**60.2%**	**20.8%**

Price data as on 3 June 2009
* Bloomberg estimates for stocks not under coverage
Source: HSBC, Bloomberg, DataStream

Trend analysis

- Mid-caps and sector-specific stocks grow at 16-26% during the quarter; outperforming the biggies
- Volatile commodity markets lead to 13% gross profit growth with a margin expansion of +120bp
- Sharp cutback in operating costs led to 17% growth in PBT

Sales growth



Source: Company, HSBC

Top line dynamics

The quarter ended March 2009, with a weighted average sales growth of 10% y-o-y, has been the worst in FY09, pulling down the year-end numbers from a weighted average growth of 19.3% for the period April–December 2008 to 17.2% for the year ended March 2009.

Mid-caps outperform

Mid-cap FMCG companies such as Marico, Dabur, Nestlé and Godrej Consumer recorded sales growth of 16-26% and outperformed the biggies like HUL that clocked 6% top line growth during the quarter, and ITC which actually decelerated 1.1% in the quarter despite cigarette sales recording 16.3% growth for the 3 months ended March 2009.

Sector focus pays off

Sector-specific companies such as Colgate Palmolive, Asian Paints and United Spirits too have fared well.

Marico

Sales growth for the year at 25% was driven equally by volume and price. For the quarter, sales growth was 20.5%, of which 9ppts was contributed by volumes. Though overall volume growth of 9% in 4Q for the company was higher than 7% in 3Q, we believe that the core portfolio continues to be under pressure. Growth of its Parachute brand slowed to 7% in 4Q from 9% in 3Q, Saffola though showed a small improvement but was way off its comfort zone of double digit growth.

Dabur

Dabur posted sales growth of 20.6% in 4Q and 18.8% in FY09, making this year's organic growth the highest in a decade. Moreover, 4Q results have shown that the growth has become more broad-based, with categories such as Foods, Oral Care and Digestives improving their growth rates.

Colgate Palmolive

Colgate's net sales increased 16.4% for the 4Q and 15.0% for the year, growing faster than the market. Market shares improved 200bp for the quarter and 10bp for the year on a y-o-y basis in the toothpaste segment. While toothpowder quarterly sales declined 2.6%, due to conversion of users to toothpaste, healthy 15% volume growth was recorded in the toothpowder segment. There was a marked shift of c300bp from toothpowder to toothpaste as explained by category penetration numbers.

ITC

Cigarettes grew 16.3% during the quarter and FMCG others saw reasonable growth at 13.5%. Agri business dropped 51.2% but that was due to ITC rationalising its agri-commodity portfolio, necessitated by increasing policy intervention and volatility in commodity markets. A revenue increase of 25.7% in paperboard for 4Q was largely driven by capacity ramp-up at a new plant, with further back-end support to the stationery business. Hotels bore the brunt, decelerating 29.3% during the quarter, and pulled down overall numbers.

HUL

While sales growth for the quarter was just 6%, FMCG sales growth of 11.8% was in line with market expectations and the lower overall number was due to a decline in non-core exports. A volume decline of 4.2% during the quarter was a result of price increases taken over the last 12-15 months, and the recent price declines having not yet fully reached retail shelves.

Soaps and detergents, beverages and ice creams grew 15.8%, 13.5% and 22.4% respectively during the quarter, while exports dropped 44.7%. Growth in personal products was disappointing at 1.9%, driven by loss in market shares and outlet consolidation in modern trade.

Nestlé

Nestlé recorded 16% y-o-y growth in the quarter ended March 2009 and 22.4% in the April 2008-March 2009 period

The 16% growth rate recorded during the quarter was due to strong domestic performance. Domestic sales were up 10.7% in volume and 18.7% in value terms. Exports suffered, with a 25.3% drop in volumes and 15.1% in sales.

Godrej Consumer

Godrej Consumer retained its position as the second largest toilet soap player in the country with a market share of 9.9% in 4Q. Soap sales increased 46% y-o-y in the quarter backed by re-launch of the Cinthol and FairGlow brands, launch of a new variant in Godrej No. 1 during the year and market share gains. Market share in hair colorants stood at 32.6% in 4Q with sales growing 20% y-o-y.

Glaxo Consumer

2009 was kick-started with the launch of a nutritional snack "Horlicks Nutribar". 4Q saw the launch of "ActiGrow", a high protein baby food and recorded 31.3% top line growth.

"Boost" was the official energy drink for one of the teams participating in the IPL (Indian Premier League) 2009, and also contributed to healthy top line numbers for 4Q and the full year.

Asian Paints

Sales grew 25% for the quarter and 24% for the year. Demand for decorative paints improved in 4Q, while industrial coatings business continued to be impacted by the slowdown in demand.

Commodities volatile

Copra

Average copra prices declined 9% in the quarter ended March 2009 over the previous nine months (April – December 2008). The trend has continued and they are currently 15% below the average for 4Q (January – March 2009) and 20% below the average for FY09 (April 2008 – March 2009).

Palm oil

Average Malaysian palm oil prices witnessed a sharp fall of 44.4% in the quarter ended March 2009, over the previous nine months (April – December 2008). However, they are on an upward move again and are currently 16% higher than the average for 4Q (January – March 2009).

Groundnut oil index

Groundnut oil index prices had softened with the average for the quarter ended March 2009 down 20% over the average for the previous nine months (April – December 2008). However, prices have increased slightly thereafter; currently 3% above the average for 4Q (January – March 2009).

Cocoa and Coffee

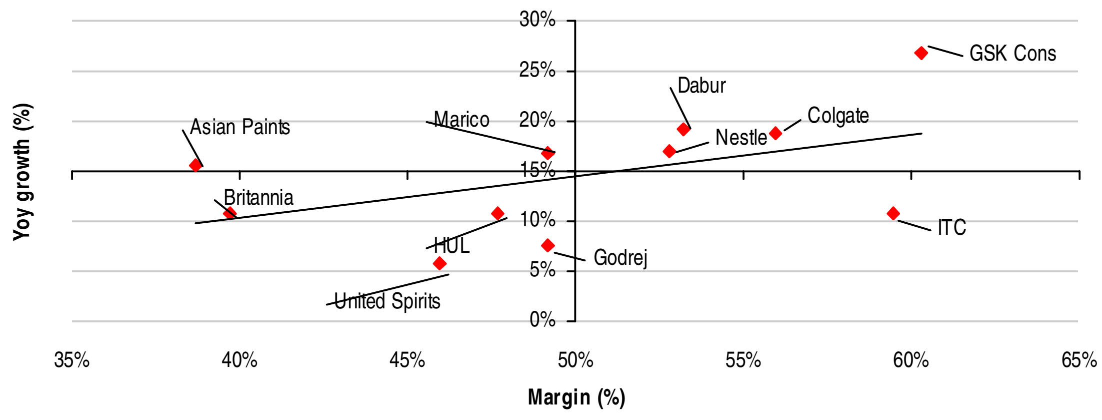
Cocoa prices have held firm since April 2008. Currently they are 3% above the average for FY09 (April 2008 – March 2009).

Average coffee prices on the other hand saw a 12% decline in 4Q (January – March 2009) over the average for the previous nine months (April – December 2008), but the trend reversed thereafter and prices are currently 24% above the average for 4Q (January – March 2009).

Sugar

Sugar has been on a growth trajectory since January 2008. Currently the price is 21% above the average for FY09 (April 2008 – March 2009). Industry source ISMA (Indian Sugar Mills Association) now believes that Indian sugar production for the 2008-09 crushing season will be 14-15mt, down from 22mt estimated in September 2008 and 19mt estimates in February 2009. Given this view, we estimate sugar prices to continue their climb.

Gross profit margin and y-o-y growth (quarter ended Mar-09)



Source: Company, HSBC

Tea

Indian wholesale tea prices softened in 3Q (October – December 2008) and 4Q (January - March 2009) but are on the upward move again, currently 30% above the average for FY09 (April 2008 – March 2009).

LAB (liner alkyl benzene)

LAB is used in detergents and dropped 27% in 4Q (January - March 2009) as compared to the previous nine months (April – December 2008). Currently the prices are at the same level as recorded in 4Q.

HDPE HK spot

Average prices, having fallen 37.3% in the quarter ended March 2009 over the previous nine months (April – December 2008), are currently 25.8% above the average of 4Q (January -March 2009); regaining a large part of the drop.

Gross profit growth and margin

Mixed impact of volatile commodity markets led to a weighted average gross profit growth of 12.8% during the quarter with a margin expansion of 126bp.

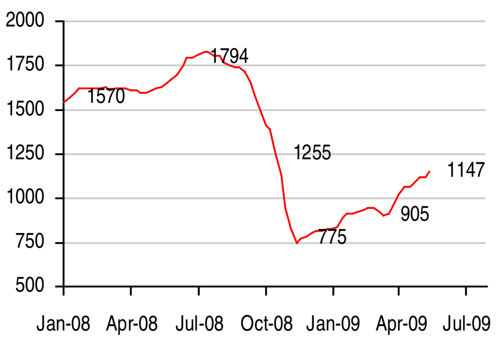
For the quarter ended March 2009, Marico, Dabur and Glaxo Consumer witnessed gross margin compression of 150bp, 66bp and 216bp respectively on a y-o-y basis. Nestlé and Britannia ended with almost flat margins, expanding a mere 46bp and 26bp respectively. United Spirits saw deceleration of 604bp during the quarter.

Sub sector leaders such as HUL, ITC, Colgate and Asian Paints expanded margins y-o-y by 206bp, 634bp, 115bp and 326bp respectively by tinkering with prices.

Mass market player Godrej Consumer was the worst hit, with margins contracting 846bp y-o-y for the quarter ended March 2009.

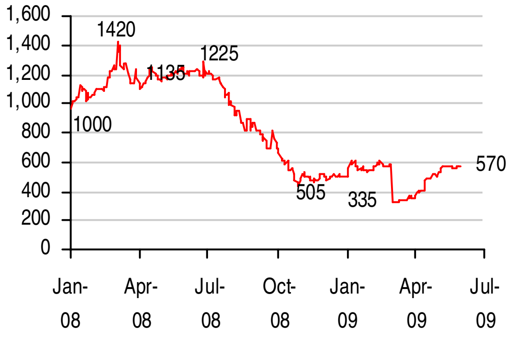
Commodity cost trends

HDPE HK Spot (USD/MT)



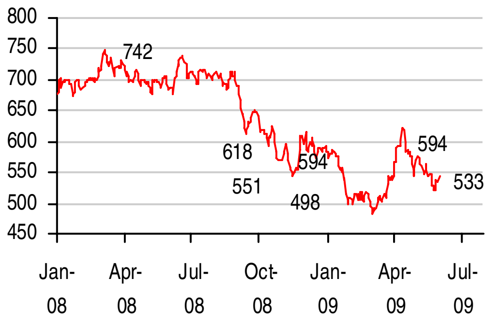
Source: DataStream

Palm oil – Malaysian Rdam (USD/MT)



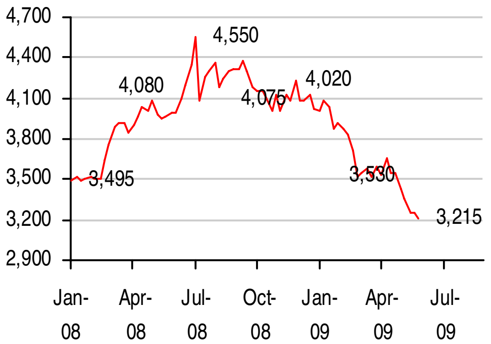
Source: DataStream

Groundnut oil index (INR)



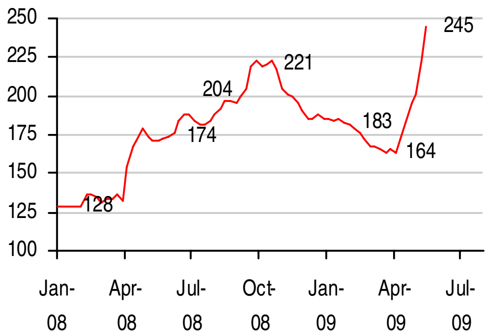
Source: Bloomberg (Ticker: MCXGNUT)

Copra cochin (INR/quintal)



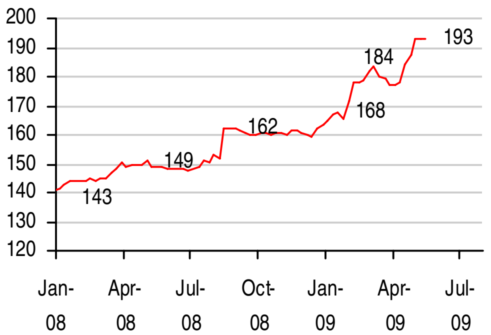
Source: Bloomberg (Ticker: COMICOPR)

Indian wholesale price index – Tea (INR)



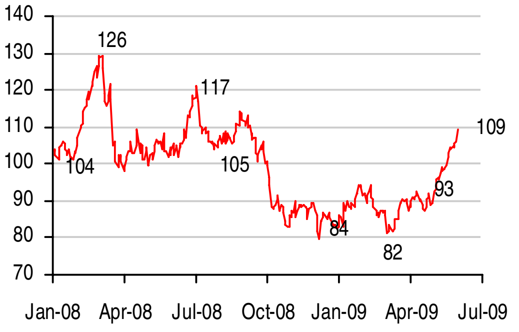
Source: Bloomberg (Ticker: INWPTEA)

Indian wholesale price index – Sugar (INR)



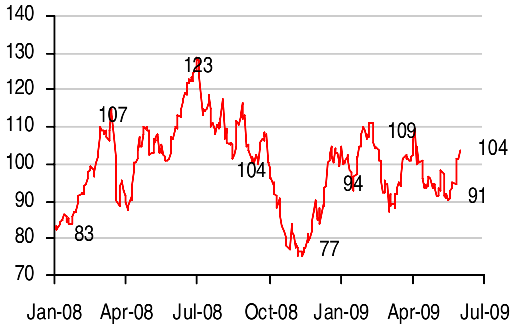
Source: Bloomberg (Ticker: INWPSUGA)

S&P GSCI Coffee index spot (USD)



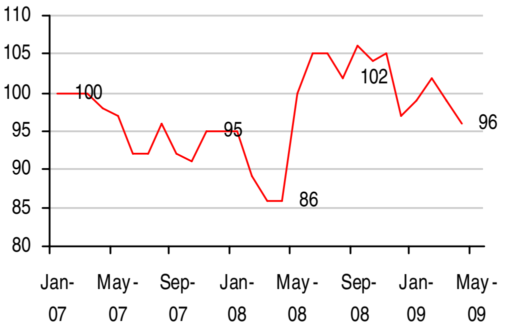
Source: Bloomberg (Ticker: SPGSKC)

S&P GSCI Cocoa index spot (USD)



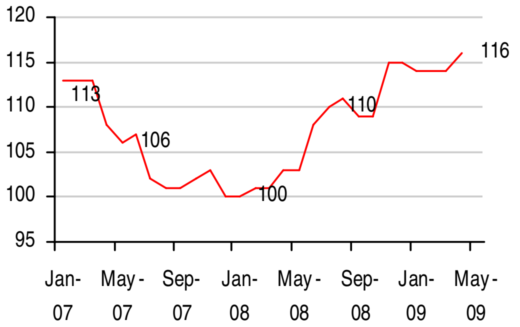
Source: Bloomberg (Ticker: SPGSCC)

Calcium carbonate (USD/ton)



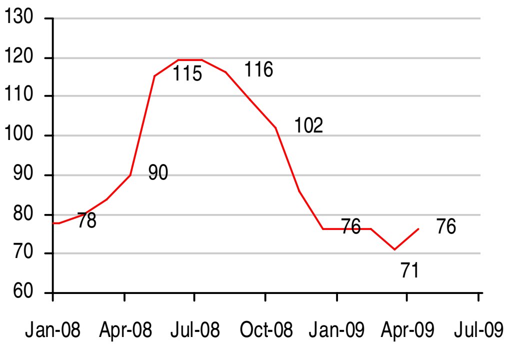
Source: Bloomberg (Ticker: PURDP064 INDEX)

Titanium dioxide (cents/lb)



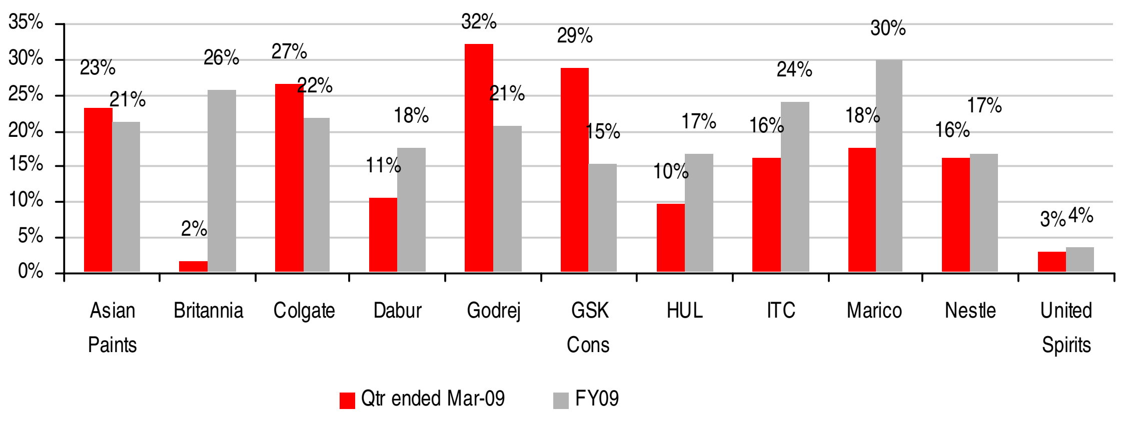
Source: Bloomberg (Ticker: PURDP097 INDEX)

LAB prices (INR/kg)



Source: RIL, HSBC

Employee costs y-o-y growth



Source: Company, HSBC

Operating expenses – sharp cutbacks

Tight control over operating expenses has been the trend across the board for the quarter ended March 2009, taking into account the period after the trend reversal started in 3Q FY09.

Employee costs

Though employee costs as a percentage of sales have remained in the 6-7% range, y-o-y growth in the quarter ended March 2009 at 14.9% was visibly lower than the 18.8% growth registered in the previous nine months.

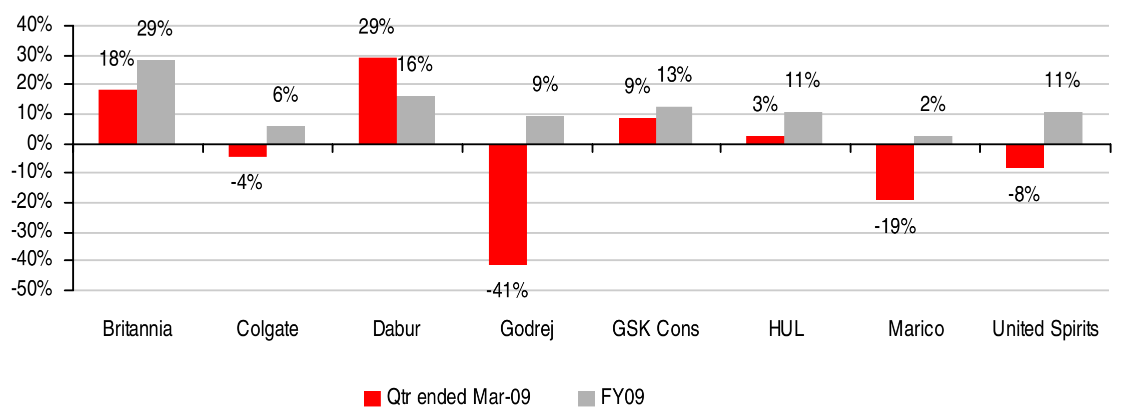
Ad spend

Advertisement and promotion expenses saw the most prominent cut backs. Ad spend during the quarter remained flat with 1% growth against 14.4% growth in the previous nine months.

Other expenses

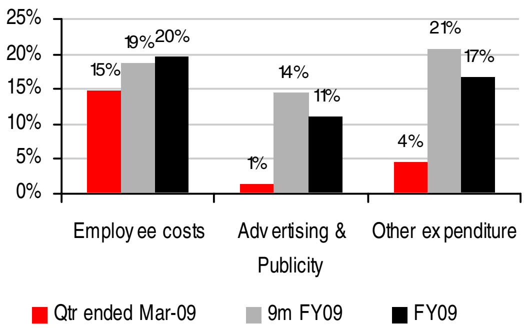
This category too saw some stringent measures with the weighted average growth during the quarter at 4.5% compared to 21% during the previous nine months.

Advertisement costs y-o-y growth



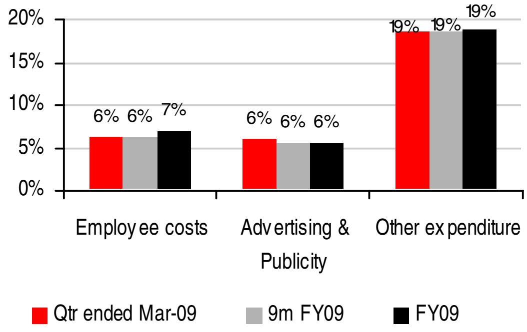
Source: Company, HSBC

Operating expenses y-o-y growth



Source: Company, HSBC
Note: calculated on a weighted average basis

Operating expenses as a % of sales



Source: Company, HSBC
Note: calculated on a weighted average basis

Profit before tax

Reported PBT

Reported PBT grew 11.6% during the quarter and 7.7% for the year ended March 2009.

Margins expanded 27bp for the March 2009 quarter as against a compression of 238bp during the previous nine months. A sharp cut back in operating expenses was responsible for this trend reversal.

PBT before exceptional items

PBT before exceptional items grew 17.3% during the quarter with a margin expansion of 119bp. The top performers were Marico, Godrej Consumer, Glaxo Consumer and Colgate Palmolive, which grew 74.5%, 40.6%, 53.3% and 43.6%, respectively.

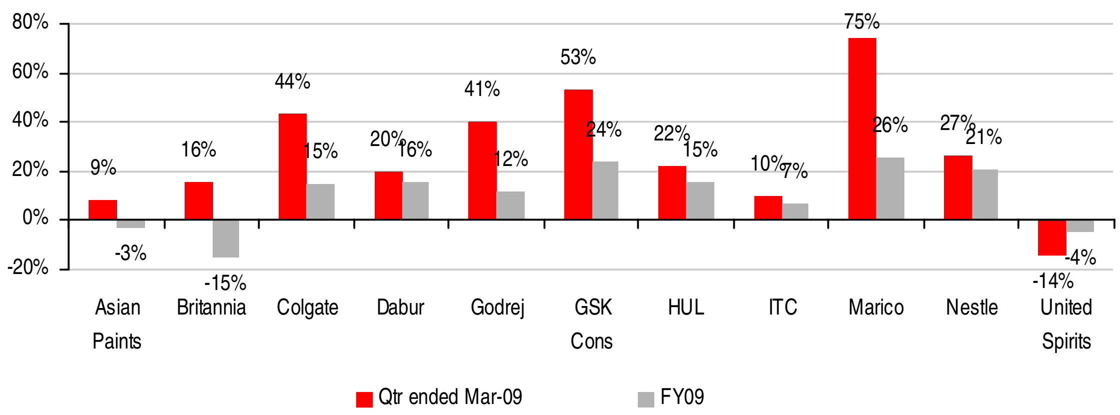
United Spirits was the only company that saw a deceleration of 14.2%; largely due to 71.9% increase in interest expense and a 59.5% drop in other operational income.

On a full-year basis, profit before exceptional items grew 9.4% but margins compressed 133bp y-o-y, due to the impact of the first nine months of the year.

Net profit

Accordingly, net profit grew 11.1% during the quarter and 8% for the year ended March 2009.

PBT (before exceptional items) y-o-y growth



Source: Company, HSBC

March qtr FY09 vs March qtr FY08

Income statement snapshot	Marico	Dabur	HUL	GCPL	Britannia	Glaxo Consumer	Colgate Palmolive	Nestlé	ITC	Asian Paints	United Spirits
Net Sales	5,612	7,317	39,883	3,427	7,620	5,394	4,555	12,659	38,918	14,249	9,078
Other operational income	0	47	470	0	28	0	167	49	356	0	151
Gross profit	2,760	3,894	19,027	1,684	3,025	3,253	2,549	6,682	23,141	5,511	4,172
Gross profit margin	49.2%	53.2%	47.7%	49.1%	39.7%	60.3%	56.0%	52.8%	59.5%	38.7%	46.0%
Employee costs	427	592	2,344	242	237	498	389	874	2,222	1,000	619
As a % of sales	7.6%	8.1%	5.9%	7.1%	3.1%	9.2%	8.5%	6.9%	5.7%	7.0%	6.8%
Advertising & Publicity	568	963	4,506	153	577	606	702	NA	NA	NA	796
As a % of sales	10.1%	13.2%	11.3%	4.5%	7.6%	11.2%	15.4%	NA	NA	NA	8.8%
Other expenditure	1,032	1,044	6,685	628	1,526	963	649	2,711	8,293	2,720	1,306
As a % of sales	18.4%	14.3%	16.8%	18.3%	20.0%	17.9%	14.3%	21.4%	21.3%	19.1%	14.4%
EBIT	629	1,198	5,551	621	625	1,081	864	2,785	11,532	1,590	1,505
EBIT margin	11.2%	16.4%	13.9%	18.1%	8.2%	20.0%	19.0%	22.0%	29.6%	11.2%	16.6%
Interest expense	113	83	0	-60	7	13	1	1.6	136.8	75	565
Other income	80	43	181	7	47	256	38	53.8	522.5	114	13
PBT (before exceptional)	595	1,158	5,731	688	664	1,324	950	2,837	11,918	1,629	898
PBT margin	10.6%	15.8%	14.4%	20.1%	8.7%	24.5%	20.9%	22.4%	30.6%	11.4%	9.9%
PBT (after exceptional)	595	1,158	4,660	688	641	1,324	901	2,837	11,918	1,629	898
PBT margin	10.6%	15.8%	11.7%	20.1%	8.4%	24.5%	19.8%	22.4%	30.6%	11.4%	9.9%
Tax	1	106	710	101	235	485	131	864	3,828	530	342
Effective tax rate	0.2%	9.1%	15.2%	14.6%	36.7%	36.6%	14.5%	30.5%	32.1%	32.5%	38.0%
Reported net profit	444	1,043	3,950	594	406	839	771	1,973	8,090	1,011	556
Net profit margin	7.9%	14.3%	9.9%	17.3%	5.3%	15.6%	16.9%	15.6%	20.8%	7.1%	6.1%
Reported Basic EPS	0.73	1.22	1.81	2.31	17.00	19.95	5.67	20.46	2.15	10.54	5.55
Reported Diluted EPS	0.73	1.21	1.81	2.31	17.00	19.95	5.67	20.46	2.14	10.54	5.55

Source: Company, HSBC
Consolidated – Marico, Dabur, GCPL, Asian Paints
Standalone – HUL, Britannia, Glaxo Consumer, Colgate Palmolive, Nestlé, ITC, United Spirits

FY09 vs FY08

Income statement snapshot	Marico	Dabur	HUL	GCPL	Britannia	Glaxo Consumer	Colgate Palmolive	Nestlé	ITC	Asian Paints	United Spirits
Net Sales	23,884	28,054	165,396	13,930	34,212	16,716	16,952	44,992	163,323	54,632	38,478
Other operational income	0	256	2,849	37	150	135	646	109	2,178	0	425
Gross profit	11,106	14,293	76,840	6,234	13,022	10,259	10,143	23,175	99,377	20,926	17,103
Gross profit margin	46.5%	50.9%	46.5%	44.8%	38.1%	61.4%	59.8%	51.5%	60.8%	38.3%	44.4%
Employee costs	1,648	2,347	9,386	876	1,587	1,831	1,509	3,268	13,228	3,715	2,361
As a % of sales	6.9%	8.4%	5.7%	6.3%	4.6%	11.0%	8.9%	7.3%	8.1%	6.8%	6.1%
Advertising & Publicity	2,504	3,433	16,644	997	2,356	1,990	2,717	NA	NA	NA	3,354
As a % of sales	10.5%	12.2%	10.1%	7.2%	6.9%	11.9%	16.0%	NA	NA	NA	8.7%
Other expenditure	3,934	3,808	28,109	2,324	6,781	3,673	2,929	10,665	35,427	10,517	5,130
As a % of sales	16.5%	13.6%	17.0%	16.7%	19.8%	22.0%	17.3%	23.7%	21.7%	19.2%	13.3%
EBIT	2,662	4,468	23,961	1,882	1,789	2,481	3,303	8,099	47,092	5,950	6,328
EBIT margin	11.1%	15.9%	14.5%	13.5%	5.2%	14.8%	19.5%	18.0%	28.8%	10.9%	16.4%
Interest expense	357	232	0	-160	239	70	15	17.1	186.9	263	1,830
Other income	142	213	1,602	51	233	890	198	272.5	2,942.7	517	57
PBT (before exceptional)	2,447	4,448	25,562	2,092	1,783	3,301	3,534	8,355	49,848	6,204	4,639
PBT margin	10.2%	15.9%	15.5%	15.0%	5.2%	19.7%	20.8%	18.6%	30.5%	11.4%	12.1%
PBT (after exceptional)	2,447	4,448	25,456	2,092	1,963	3,301	3,485	8,324	49,848	6,204	4,639
PBT margin	10.2%	15.9%	15.4%	15.0%	5.7%	19.7%	20.6%	18.5%	30.5%	11.4%	12.1%
Tax	409	540	4,136	366	530	1,144	603	2,611	16,254	1,974	1,666
Effective tax rate	16.7%	12.1%	16.2%	17.5%	27.0%	34.7%	17.3%	31.4%	32.6%	31.8%	35.9%
Reported net profit	1,887	3,912	21,155	1,733	1,515	2,157	2,858	5,712	33,246	3,978	2,972
Net profit margin	7.9%	13.9%	12.8%	12.4%	4.4%	12.9%	16.9%	12.7%	20.4%	7.3%	7.7%
Reported Basic EPS	3.10	4.52	9.71	6.83	63.41	51.29	21.01	59.25	8.82	41.48	29.68
Reported Diluted EPS	3.10	4.50	9.71	6.83	63.40	51.29	21.01	59.25	8.81	41.48	29.68

Source: Company, HSBC
Consolidated – Marico, Dabur, GCPL, Britannia, Colgate Palmolive, ITC, Asian Paints
Standalone – HUL, Glaxo Consumer, Nestlé, United Spirits

March qtr FY09 vs March qtr FY08

Y-o-y Change	Marico	Dabur	HUL	GCPL	Britannia	Glaxo Consumer	Colgate Palmolive	Nestlé	ITC	Asian Paints	United Spirits	Simple average	Weighted average
Net Sales	20.5%	20.6%	6.0%	26.1%	10.1%	31.3%	16.4%	16.0%	-1.1%	25.4%	19.6%	17.4%	10.0%
Other operational income	NA	-52.4%	-39.1%	-100.0%	-18.0%	NA	2.6%	109.8%	-67.1%	NA	101.9%	-7.8%	-43.9%
Gross profit	16.9%	19.2%	10.8%	7.6%	10.8%	26.7%	18.8%	17.1%	10.7%	15.7%	5.7%	14.5%	12.8%
Gross profit margin	-150bp	-66bp	206bp	-846bp	26bp	-216bp	115bp	46bp	634bp	-326bp	-604bp	-107bp	126bp
Employee costs	17.5%	10.6%	9.8%	32.2%	1.6%	28.8%	26.5%	16.2%	16.3%	23.2%	3.2%	16.9%	14.9%
As a % of sales	-19bp	-73bp	20bp	33bp	-26bp	-18bp	69bp	1bp	85bp	-13bp	-109bp	-5bp	27bp
Advertising & Publicity	-19.4%	29.4%	2.6%	-41.4%	17.9%	9.0%	-4.4%	NA	NA	NA	-8.3%	-1.8%	1.4%
As a % of sales	-500bp	89bp	-37bp	-516bp	50bp	-230bp	-335bp	NA	NA	NA	-267bp	-218bp	-51bp
Other expenditure	23.2%	3.3%	1.8%	10.4%	6.6%	18.1%	11.2%	9.9%	-2.9%	14.7%	10.8%	9.7%	4.5%
As a % of sales	41bp	-240bp	-70bp	-261bp	-65bp	-200bp	-67bp	-119bp	-40bp	-178bp	-114bp	-119bp	-98bp
EBIT	67.0%	24.9%	23.7%	18.7%	17.3%	53.7%	37.6%	26.4%	11.8%	11.4%	16.7%	28.1%	19.3%
EBIT margin	312bp	56bp	199bp	-112bp	51bp	293bp	293bp	180bp	342bp	-140bp	-42bp	130bp	148bp
Interest expense	29.8%	135.0%	NA	-277.4%	-47.1%	-47.6%	-69.4%	77.8%	406.7%	91.0%	71.9%	37.1%	57.5%
Other income	53.7%	7.8%	-10.1%	NA	-15.9%	37.8%	2.7%	37.6%	-5.9%	3.2%	-59.5%	5.1%	3.6%
PBT (before exceptional)	74.5%	20.2%	22.2%	40.6%	15.7%	53.3%	43.6%	26.6%	9.9%	8.8%	-14.2%	27.4%	17.3%
PBT margin	329bp	-6bp	191bp	207bp	42bp	352bp	395bp	186bp	307bp	-175bp	-390bp	131bp	119bp
PBT (after exceptional)	74.5%	20.2%	-1.1%	40.6%	-14.2%	53.3%	36.3%	26.6%	9.9%	8.8%	-14.2%	21.9%	11.6%
PBT margin	329bp	-6bp	-84bp	207bp	-238bp	352bp	288bp	186bp	307bp	-175bp	-390bp	71bp	27bp
Tax	-97.5%	-19.5%	-21.5%	24.0%	71.2%	62.6%	24.0%	35.0%	9.8%	11.0%	-13.7%	7.8%	9.5%
Effective tax rate	-1126bp	-449bp	-395bp	-195bp	1829bp	211bp	-143bp	190bp	-3bp	64bp	25bp	1bp	-183bp
Reported net profit	8.9%	30.9%	3.7%	45.4%	-33.4%	48.3%	38.6%	23.2%	10.0%	7.0%	-14.6%	15.3%	11.1%
Net profit margin	-84bp	112bp	-22bp	230bp	-349bp	179bp	271bp	91bp	209bp	-122bp	-245bp	25bp	14bp
Reported Basic EPS	9.0%	27.1%	3.4%	27.6%	-33.5%	48.3%	38.6%	23.2%	10.3%	7.0%	-16.8%	13.1%	4.8%
Reported Diluted EPS	9.0%	27.4%	3.4%	27.6%	-33.5%	48.3%	38.6%	23.2%	10.9%	7.0%	-15.7%	13.3%	5.0%

Source: Company, HSBC

Apr-Dec 2009 vs Apr-Dec 2008

Y-o-y Change	Marico	Dabur	HUL	GCPL	Britannia	Glaxo Consumer	Colgate Palmolive	Nestlé	ITC	Asian Paints	United Spirits	Simple average	Weighted average
Net Sales	27.2%	18.2%	19.2%	26.1%	24.2%	18.9%	14.5%	22.4%	14.8%	23.4%	22.1%	21.0%	19.3%
Other operational income	-92.7%	47.2%	49.2%	NA	328.6%	20.4%	26.1%	191.2%	25.9%	NA	73.4%	74.4%	41.4%
Gross profit	21.8%	14.3%	15.9%	5.7%	18.9%	12.9%	11.7%	20.5%	13.5%	13.9%	8.3%	14.3%	14.6%
Gross profit margin	-203bp	-173bp	-131bp	-833bp	-172bp	-333bp	-142bp	-83bp	-69bp	-320bp	-562bp	-275bp	-201bp
Employee costs	35.0%	20.4%	19.5%	16.9%	7.6%	11.1%	15.1%	16.9%	23.3%	20.4%	3.9%	17.3%	18.8%
As a % of sales	38bp	15bp	2bp	-47bp	-47bp	-83bp	4bp	-35bp	40bp	-17bp	-104bp	-21bp	-3bp
Advertising & Publicity	11.1%	14.5%	13.8%	29.2%	17.3%	14.3%	10.1%	NA	NA	NA	17.1%	15.9%	14.4%
As a % of sales	-154bp	-38bp	-45bp	19bp	-39bp	-50bp	-66bp	NA	NA	NA	-38bp	-51bp	-25bp
Other expenditure	27.1%	16.6%	17.7%	10.9%	24.5%	24.7%	14.6%	22.7%	21.8%	24.7%	19.7%	20.5%	20.8%
As a % of sales	-2bp	-18bp	-21bp	-221bp	5bp	110bp	2bp	5bp	118bp	19bp	-26bp	-3bp	22bp
EBIT	18.2%	10.7%	17.4%	-12.4%	17.0%	-0.5%	12.8%	17.8%	5.7%	-5.0%	0.2%	7.4%	8.4%
EBIT margin	-85bp	-106bp	-22bp	-528bp	-47bp	-241bp	-30bp	-65bp	-250bp	-323bp	-358bp	-187bp	-180bp
Interest expense	14.9%	12.3%	NA	-205.6%	118.5%	63.9%	-8.3%	134.8%	142.9%	9.3%	33.5%	31.6%	18.0%
Other income	-39.5%	180.5%	-19.5%	5.9%	-0.9%	46.0%	14.1%	32.9%	-10.2%	-17.0%	54.6%	22.4%	-5.8%
PBT (before exceptional)	15.4%	14.2%	13.7%	1.3%	11.8%	9.4%	12.5%	18.1%	4.2%	-6.6%	-5.5%	8.0%	7.1%
PBT margin	-104bp	-55bp	-76bp	-326bp	-88bp	-152bp	-38bp	-62bp	-322bp	-365bp	-372bp	-178bp	-216bp
PBT (after exceptional)	15.4%	14.2%	9.3%	1.3%	6.9%	9.4%	13.0%	18.3%	4.2%	-6.6%	-5.5%	7.3%	6.1%
PBT margin	-104bp	-55bp	-150bp	-326bp	-116bp	-152bp	-29bp	-60bp	-322bp	-365bp	-372bp	-186bp	-238bp
Tax	27.4%	15.8%	-7.3%	31.8%	3.9%	9.3%	-15.6%	10.2%	6.9%	-7.2%	-5.2%	6.4%	3.1%
Effective tax rate	207bp	18bp	-294bp	436bp	-49bp	-4bp	-558bp	-233bp	82bp	-19bp	9bp	-37bp	-103bp
Reported net profit	12.5%	13.3%	12.3%	-3.8%	7.5%	9.5%	21.1%	22.5%	2.9%	-5.7%	-5.6%	7.9%	7.0%
Net profit margin	-103bp	-60bp	-84bp	-337bp	-92bp	-100bp	93bp	0bp	-246bp	-227bp	-241bp	-127bp	-161bp
Reported Basic EPS	12.3%	13.8%	13.2%	-13.9%	7.6%	9.5%	21.0%	22.5%	2.7%	-5.7%	-8.5%	6.8%	6.5%
Reported Diluted EPS	12.3%	13.9%	13.2%	-13.9%	7.6%	9.5%	21.0%	22.5%	2.8%	-5.7%	-7.2%	6.9%	6.7%

Source: Company, HSBC

FY09 vs FY08

Y-o-y Change	Marico	Dabur	HUL	GCPL	Britannia	Glaxo Consumer	Colgate Palmolive	Nestlé	ITC	Asian Paints	United Spirits	Simple average	Weighted average
Net Sales	25.4%	18.8%	15.7%	26.3%	23.2%	22.7%	15.0%	20.6%	11.4%	24.0%	21.3%	20.4%	17.2%
Other operational income	NA	6.6%	20.3%	160.3%	94.5%	20.4%	15.2%	147.6%	-12.2%	NA	38.3%	54.6%	9.4%
Gross profit	20.2%	14.7%	14.6%	6.6%	20.2%	16.9%	15.8%	19.5%	14.0%	14.4%	7.9%	15.0%	14.7%
Gross profit margin	-201bp	-181bp	-46bp	-827bp	-96bp	-301bp	42bp	-47bp	139bp	-321bp	-549bp	-217bp	-109bp
Employee costs	30.0%	17.8%	16.9%	20.7%	25.7%	15.4%	21.9%	16.7%	24.0%	21.2%	3.6%	19.4%	19.6%
As a % of sales	24bp	-8bp	6bp	-29bp	9bp	-69bp	50bp	-24bp	82bp	-16bp	-105bp	-7bp	14bp
Advertising & Publicity	2.3%	16.1%	10.5%	9.0%	28.6%	12.6%	5.9%	NA	NA	NA	10.7%	12.0%	11.2%
As a % of sales	-236bp	-28bp	-47bp	-114bp	28bp	-106bp	-138bp	NA	NA	NA	-83bp	-91bp	-30bp
Other expenditure	28.4%	11.5%	13.5%	12.8%	25.2%	22.9%	20.9%	19.2%	15.0%	22.0%	12.5%	18.5%	16.7%
As a % of sales	39bp	-89bp	-33bp	-200bp	31bp	4bp	84bp	-28bp	67bp	-32bp	-104bp	-24bp	-8bp
EBIT	23.5%	14.2%	18.8%	-4.8%	-10.8%	17.6%	15.0%	20.6%	8.4%	-1.1%	6.3%	9.8%	11.0%
EBIT margin	-17bp	-64bp	38bp	-443bp	-199bp	-64bp	-1bp	1bp	-80bp	-275bp	-232bp	-121bp	-100bp
Interest expense	17.0%	38.2%	NA	-224.2%	58.4%	17.1%	25.2%	128.0%	197.6%	24.4%	42.4%	32.4%	27.6%
Other income	48.8%	112.1%	-18.5%	93.1%	-7.9%	43.6%	-0.7%	33.8%	-13.0%	-13.3%	-7.5%	24.6%	-5.1%
PBT (before exceptional)	25.8%	15.7%	15.5%	11.6%	-15.4%	23.6%	15.1%	20.9%	6.6%	-3.0%	-4.4%	10.2%	9.4%
PBT margin	3bp	-43bp	-3bp	-199bp	-238bp	15bp	2bp	5bp	-137bp	-316bp	-323bp	-112bp	-133bp
PBT (after exceptional)	25.8%	15.7%	7.2%	11.6%	-10.0%	23.6%	13.9%	21.0%	6.6%	-3.0%	-4.4%	9.8%	7.7%
PBT margin	3bp	-43bp	-122bp	-199bp	-212bp	15bp	-20bp	6bp	-137bp	-316bp	-323bp	-123bp	-165bp
Tax	13.8%	6.7%	-10.1%	29.6%	27.4%	26.9%	-12.9%	17.3%	8.6%	-2.9%	-4.1%	9.1%	5.3%
Effective tax rate	-175bp	-103bp	-312bp	243bp	793bp	91bp	-534bp	-97bp	59bp	3bp	11bp	-2bp	-106bp
Reported net profit	11.6%	17.5%	10.6%	8.8%	-14.6%	21.9%	21.2%	22.7%	5.3%	-2.8%	-4.5%	8.9%	8.0%
Net profit margin	-97bp	-16bp	-59bp	-201bp	-196bp	-8bp	86bp	22bp	-119bp	-200bp	-209bp	-91bp	-114bp
Reported Basic EPS	11.5%	17.4%	11.2%	-3.1%	-14.6%	21.9%	21.2%	22.7%	5.1%	-2.8%	-6.8%	7.6%	4.1%
Reported Diluted EPS	11.5%	17.5%	11.2%	-3.1%	-14.6%	21.9%	21.2%	22.7%	5.5%	-2.8%	-5.5%	7.8%	4.3%

Source: Company, HSBC

Flashnote

HSBC Global Research

Consumer & Retail
Personal Products
Equity – India

Dabur India (DABUR)

Overweight (V)

Target price (INR)	**123.00**
Share price (INR)	**101.50**
Potential total return (%)	**23.2**

Performance	1M	3M	12M
Absolute (%)	8.3	16.7	-3.6
Relative^ (%)	-1.1	-1.8	49.2

Index^	BOMBAY SE IDX
RIC	DABU.BO
Bloomberg	DABUR IN
Market cap (USDm)	1,738
Market cap (INRm)	87,805
Enterprise value (INRm)	85,128
Free float (%)	22

Note: (V) = volatile (please see disclosure appendix)

30 April 2009

Percy Panthaki*
Analyst
HSBC Securities and Capital Markets (India) Private Limited
+9122 2268 1240
percypanthaki@hsbc.co.in

Maya Shivani*
Associate
Bangalore

View HSBC Global Research at:
http://www.research.hsbc.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/qualified pursuant to NYSE and/or NASD regulations

Issuer of report: HSBC Securities and Capital Markets (India) Private Limited

Disclaimer & Disclosures

This report must be read with the disclosures and the analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it

Reiterate OW(V): A strong performance

- **Results show Dabur is gaining strong sales traction across categories; growth becoming more broad based**
- **Margin expansion and new launches planned to drive growth for FY10e; we increase FY10e EPS estimates by 1.5%**
- **Raise TP from INR94.5 to INR123; 20% CAGR over two years to drive stock**

Sales growth gains traction and becomes broad based. Dabur posted sales growth of 20.6% in 4Q and 18.8% for FY09, making this year's organic growth the highest in a decade. Moreover, 4Q results have shown that the growth has become more broad based, with categories such as Foods, Oral Care and Digestives improving their growth rates.

Margins turning the corner. Gross margin declined by 66bps this quarter, much lower than the 355bps in 3Q as the impact of lower commodity prices has started showing up. We believe that from next quarter onwards we are likely to see gross margin expansion. We have built in 112bps gross margin expansion for FY10e.

New variants/launches to power growth. FY10e is likely to see an increase in the number of new products/variants being launched. On average, Dabur gains 4-5% growth due to new variants, but the figure is likely to be higher this year and should help offset any recessionary impact. A new fruit drink, light hair oil variants, an ayurvedic skincare brand and the national rollout of Chywan Junior are slated for FY10e.

Increase EPS estimates, raise TP to INR123, maintain OW(V). We increase our FY10e EPS estimates marginally by 1.5% on the back of FY09e numbers being better than expected. With the growth becoming broader based, new launches planned and increased overall sales traction, we believe the stock is likely to undergo a multiple re-rating. We value Dabur at 23x PE (18x earlier), which is in line with its three-year average PE multiple. We increase our price target from INR94.5 to INR123 and retain our OW(V) rating. A good set of numbers combined with likely consensus upgrades and a 20.5% EPS CAGR for the next two years are likely to drive the stock steadily upwards.

Dabur: Snapshot (INRm)

Year to Mar	Sales	y-o-y	EBIT	y-o-y	Net profit	y-o-y	EPS (INR)	PE	ROE	ROA
FY08	23,611	15.6%	3,672	18.9%	3,339	18.0%	3.84	26.4x	60.9%	27.0%
FY09e	28,054	18.8%	4,212	14.7%	3,912	17.2%	4.50	22.5x	54.5%	24.7%
FY10e	33,078	17.9%	5,215	23.8%	4,630	18.4%	5.33	19.0x	49.1%	24.5%
FY11e	38,446	16.2%	6,199	18.9%	5,676	22.6%	6.53	15.5x	46.4%	25.6%

Source: Company, HSBC

Financials & valuation

Financial statements

Year to	03/2008a	03/2009e	03/2010e	03/2011e
Profit & loss summary (INRm)				
Revenue	23,611	28,054	33,078	38,446
EBITDA	4,093	4,705	5,771	6,929
Depreciation & amortisation	-421	-492	-556	-731
Operating profit/EBIT	3,672	4,212	5,215	6,199
Net interest	-168	-232	-247	-250
PBT	3,844	4,448	5,318	6,549
Taxation	-507	-540	-693	-879
Net profit	3,339	3,912	4,630	5,676
HSBC net profit	3,339	3,912	4,630	5,676
Cash flow summary (INRm)				
Cash flow from operations	4,077	3,110	3,564	5,469
Capex	-1,124	-1,288	-4,500	-400
Dividends	-758	-1,521	-2,070	-2,345
Change in net debt	-766	567	1,180	-3,133
FCF equity	3,164	2,089	-936	5,069
Balance sheet summary (INRm)				
Tangible fixed assets	4,653	5,592	9,550	9,220
Current assets	7,739	9,507	9,194	13,698
Cash & others	766	1,483	326	3,482
Total assets	14,568	18,655	20,816	25,189
Operating liabilities	6,563	7,059	6,635	7,652
Gross debt	992	2,276	2,299	2,322
Net debt	226	793	1,973	-1,160
Shareholders funds	6,176	8,175	10,699	13,792
Invested capital	5,063	6,557	11,783	11,784

Ratio, growth and per share analysis

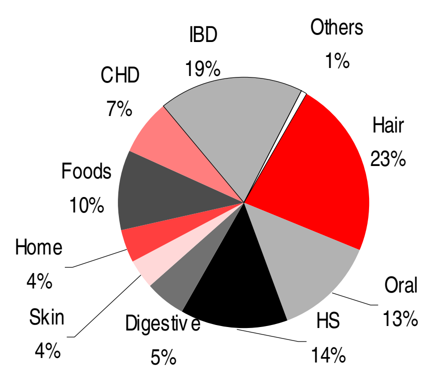
Year to	03/2008a	03/2009e	03/2010e	03/2011e
Y-o-y % change				
Revenue	15.6	18.8	17.9	16.2
EBITDA	17.0	14.9	22.7	20.1
Operating profit	18.9	14.7	23.8	18.9
PBT	20.3	15.7	19.6	23.1
HSBC EPS	18.1	17.2	18.4	22.6
Ratios (%)				
Revenue/IC (x)	4.7	4.8	3.6	3.3
ROIC	62.9	63.1	49.3	45.2
ROE	60.9	54.5	49.1	46.4
ROA	27.0	24.7	24.5	25.6
EBITDA margin	17.3	16.8	17.4	18.0
Operating profit margin	15.6	15.0	15.8	16.1
EBITDA/net interest (x)	24.4	20.3	23.4	27.8
Net debt/equity	3.6	9.6	18.4	-8.4
Net debt/EBITDA (x)	0.1	0.2	0.3	-0.2
Per share data (INR)				
EPS reported (fully diluted)	3.84	4.50	5.33	6.53
HSBC EPS (fully diluted)	3.84	4.50	5.33	6.53
DPS	1.49	1.75	2.07	2.54
Book value	7.16	9.47	12.40	15.98

Valuation data

Year to	03/2008a	03/2009e	03/2010e	03/2011e
EV/sales	3.6	3.0	2.7	2.2
EV/EBITDA	21.0	18.1	15.2	12.2
EV/IC	17.0	13.0	7.4	7.2
PE*	26.4	22.5	19.0	15.5
P/Book value	14.2	10.7	8.2	6.4
FCF yield (%)	3.7	2.5	-1.1	5.9
Dividend yield (%)	1.5	1.7	2.0	2.5

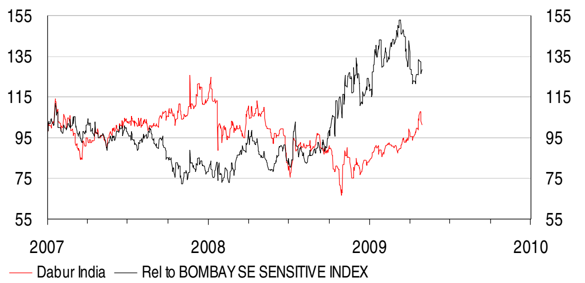
Note: * = Based on HSBC EPS (fully diluted)

Revenue break up FY09



Source: Company, HSBC

Price relative



Source: HSBC

Note: Price at close of 28 Apr 2009

Results analysis

Dabur: 4Q FY09 and FY09 results snapshot (INRm)

	4Q FY09	4Q FY08	y-o-y (%)	FY09	FY08	y-o-y (%)
Net sales	7,317	6,065	20.6%	28,054	23,611	18.8%
Other operating income	47	98	-52.4%	256	240	6.6%
Gross profit	3,894	3,268	19.2%	14,293	12,457	14.7%
Gross profit margin	53.2%	53.9%	-66 bps	50.9%	52.8%	-181 bps
Advertising & Publicity	963	744	29.4%	3,433	2,955	16.1%
Employees Cost	592	535	10.6%	2,347	1,993	17.8%
Other Expenditure	1,044	1,011	3.3%	3,808	3,415	11.5%
EBITDA	1,342	1,076	24.7%	4,960	4,333	14.5%
EBITDA margin	18.3%	17.7%	60 bps	17.7%	18.4%	-67 bps
Depreciation and amortization	144	117	22.9%	492	421	17.0%
EBIT	1,198	959	24.9%	4,468	3,912	14.2%
EBIT margin	16.4%	15.8%	56 bps	15.9%	16.6%	-64 bps
Interest expense	83	35	135.0%	232	168	38.2%
Other income	43	40	7.8%	213	100	112.1%
PBT	1,158	964	20.2%	4,448	3,844	15.7%
PBT margin	15.8%	15.9%	-6 bps	15.9%	16.3%	-43 bps
Tax	106	131	-19.5%	540	507	6.7%
Net profit	1,043	796	30.9%	3,912	3,329	17.5%
Net profit margin	14.3%	13.1%	112 bps	13.9%	14.1%	-16 bps
Basic EPS	1.22	0.96	27.1%	4.52	3.85	17.4%
Diluted EPS	1.21	0.95	27.4%	4.50	3.83	17.5%

Source: Company, HSBC

- 4Q sales growth was robust at 20.6%. Sales growth was broad based with Foods and Oral Care, categories which were earlier subdued, doing better.
- Gross profit margins contracted 66bps for the quarter but show an improving trend (181bps decline for FY09e and 355bps decline for 3Q FY09).
- EBITDA margins expanded by 60bps for 4Q, again showing an improving trend as compared to 67bps decline for FY09e.
- Retail losses for the quarter are down to INR21m, compared to INR179m for FY09e.

New launches likely in FY10e

A range of variants/new products is scheduled to be introduced in FY10e. Activity on this front is likely to be higher than normal and should offset the impact of a slowdown in consumer demand in the established business.

- Chywan Junior (malted beverage) to be launched nationally.
- New variants in shampoos under the Vatika brand.
- Light hair oils under the Vatika and Dabur Amla brands.
- A new brand in ayurvedic skin care.
- A new brand in fruit drinks.

Segment wise sales growth

	1Q FY09	2Q FY09	3Q FY09	4Q FY09	FY09
CCD	9.9%	12.7%	14.4%	18.1%	13.8%
- Hair oils	12.2%	19.8%	27.0%	20.9%	19.4%
- Shampoos	26.3%	36.3%	34.0%	33.2%	31.6%
- Oral care	5.5%	3.3%	3.0%	7.9%	4.8%
- Health supplements	19.1%	7.7%	10.0%	11.9%	11.3%
- Digestive	0.0%	7.4%	13.0%	31.3%	11.8%
- Baby and Skin care (excl Vatika soap)	12.5%	23.7%	24.0%	24.5%	14.4%
- Home care	0.8%	18.8%	14.0%	6.4%	9.7%
- Foods	15.2%	8.6%	12.0%	23.1%	14.4%
CHD	24.5%	20.7%	17.7%	15.2%	18.9%
IBD	39.5%	40.8%	48.2%	31.4%	39.9%
Total	15.5%	17.8%	19.4%	19.9%	18.3%

Source: Company, HSBC

Femcare acquisition impact

The full impact of Femcare profits will not be visible in FY10e. This is because a large part of the EBIT contributed by Femcare will be negated by reduced interest income (Dabur will have to sell some of its investments to finance the acquisition). Hence, while EBITDA growth for FY10e is estimated at 22.7%, EPS is expected to grow at 18.4%. On the other hand, in FY11e, the investments will be recouped through internal cash flows and hence interest income will grow at a fast rate. For FY11e, we build in 20.1% EBITDA growth but higher EPS growth (22.6%) due to increased interest income.

The road ahead

We build in 18% sales growth for FY10e – 15% organic and 3% from Femcare. We believe that this will be driven by an organic volume growth of 12-13% and a price growth of 2-3%. With commodity costs coming down, we build in a 112bps gross margin expansion. Moreover, losses on New U are likely to come down to INR100m from INR179m in FY09e. We increase our EPS for FY10e by 1.5% from INR5.25 to INR5.33 on the back of FY09e performance (INR4.5 vs earlier estimate of INR4.4). We keep our EPS estimate for FY11e unchanged.

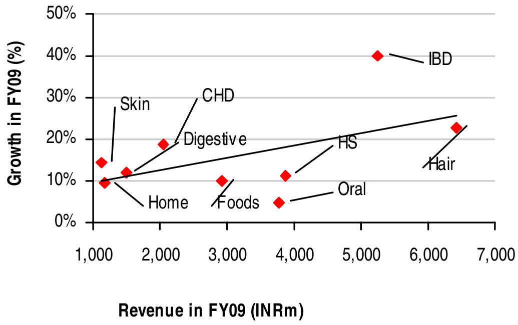
Valuation

We believe that Dabur is likely to undergo a PE re-rating and will return to trading at mean multiples from the lows seen recently. We therefore raise our PE multiple target from 18x to 23x on FY10e EPS. The reasons are (1) 23x is the average multiple over last three years; (2) Sales growth has now become broader based – this was one of the main concerns we mentioned in our earlier reports; (3) We expect robust growth of 20.5% EPS CAGR over next two years. We arrive at a 12-month target price of INR123 for Dabur. Our target price implies a 19x PE multiple on our FY11e EPS.

Rating

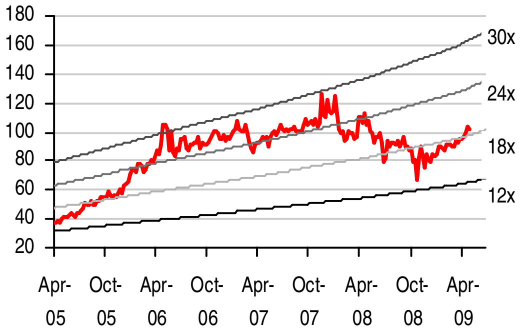
Under our research model, for stocks with a volatility indicator, the Neutral rating band is 10 percentage points above and below the hurdle rate for Indian stocks of 11%. This translates into a Neutral band of 1% to 21% around the current share price. Our target price of INR123 represents a total potential return of 23.2% (including dividend yield of 2%), which is above the Neutral band. We therefore reiterate our Overweight (V) rating.

Segment wise growth and size



Source: Company, HSBC

One year forward PE band



Source: NSE India, HSBC

Risks

Downside risks are (1) A macro-economic slowdown may result in lower consumer spending and may affect volume growth for FMCG companies; (2) Organised retail companies may ask for products at cheaper prices which may result in margin contraction; (3) Retail losses could be higher than we estimate; (4) Competitive pressures are increasing in the FMCG industry and this could affect Dabur on revenue and/or costs by requiring a higher ad spend than previously estimated; (5) Synergies expected with FCPL do not flow through.

Consumer & Retail
Household Products
Equity – India

Colgate-Palmolive India (CLGT)

Overweight

Target price (INR)	**540.00**
Share price (INR)	**474.25**
Potential total return (%)	**17.9**

Performance	1M	3M	12M
Absolute (%)	-0.6	1.9	10.6
Relative^ (%)	-20.7	-36.6	26.2

Index^	BOMBAY SE IDX
RIC	COLG.BO
Bloomberg	CLGT IN
Market cap (USDm)	1,355
Market cap (INRm)	64,495
Enterprise value (INRm)	60,312
Free float (%)	48

29 May 2009

Percy Panthaki *
Analyst
HSBC Securities and Capital Markets (India) Private Limited
+9122 2268 1240
percypanthaki@hsbc.co.in

View HSBC Global Research at:
http://www.research.hsbc.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/qualified pursuant to NYSE and/or NASD regulations

Issuer of report: HSBC Securities and Capital Markets (India) Private Limited

Maintain OW; volume story continues

- **Q4 EPS grew 39% on the back of healthy volumes, abating material costs, and reduced ad spends**
- **The growth story should continue in FY10; we are raising our FY10 and FY11 EPS estimates by 4%**
- **Shifting from blended DCF-PE to PE basis; target price rises to INR540 from INR470; reiterate Overweight rating**

A strong performance: Colgate posted a strong performance for Q4, with sales growth of 15%, backed by 15% volume growth in the toothpaste category, gross margin expansion of 115bps, and PAT growth of 39%. The company expanded its toothpaste market share by 200bps on a y-o-y basis. Penetration figures for the industry show marked up-trading from toothpowder to toothpaste, but with toothpaste penetration still at just 57%, we see ample room for growth.

The road ahead and changes in our estimates: We believe that Colgate will continue on the growth path in FY10e. We build in a marginal slowdown in sales growth from 15% in FY09e to 13.3% in FY10e and a 50bps increase in ad spend as a percentage of sales for the same period to account for increased activity by competitors. However, we are raising our FY10e and FY11e EPS by 4% to account for higher savings in input costs and for our advertising cost estimates being a bit more conservative than seems warranted.

Valuation: We are changing from a blended DCF-PE basis to a PE basis. We had used a blended basis, as multiples were affected by weakness in market sentiment, and the DCF valuation was substantially higher than the PE valuation, which is not the case now. Our preferred valuation methodology for all consumer staples stocks is PE-based. We value Colgate at 22x FY10e PE, slightly above the three-year average forward PE of 20.4x, due to improved performance but at a slight discount to Dabur's 23x to account for a lower EPS growth rate and the risk of being a single-product company. We are thus raising our 12-month target price to INR540 from INR470. Our new target suggests a potential total return, including dividend yield, of 17.9%. Catalysts for the stock, in our view, include continued volume growth and savings on input cost and overheads.

Colgate-Palmolive: Snapshot (INRm)

Year to Mar	Revenue	y-o-y (%)	EBIT	y-o-y (%)	Net profit	y-o-y (%)	EPS (INR)	PE (x)	ROE (%)	ROA (%)
FY08	14,739	13.8	2,861	59.3	2,358	58.9	17.34	27.4	106.1	33.1
FY09e	16,952	15.0	3,303	15.5	2,858	21.2	21.01	22.6	162.3	33.4
FY10e	19,200	13.3	3,841	16.3	3,337	16.8	24.54	19.3	175.5	31.5
FY11e	21,861	13.9	4,417	15.0	3,631	8.8	26.70	17.8	177.7	30.0

Source: Company reports, HSBC

HSBC

Financials & valuation

Financial statements

Year to	03/2008a	03/2009e	03/2010e	03/2011e
Profit & loss summary (INRm)				
Revenue	14,739	16,952	19,200	21,861
EBITDA	3,070	3,585	4,150	4,762
Depreciation & amortisation	-209	-283	-309	-345
Operating profit/EBIT	2,861	3,303	3,841	4,417
Net interest	199	182	263	531
PBT	3,059	3,485	4,105	4,948
Taxation	-693	-627	-739	-1,287
Net profit	2,358	2,833	3,337	3,631
HSBC net profit	2,365	2,898	3,354	3,645
Cash flow summary (INRm)				
Cash flow from operations	3,112	3,916	4,153	4,983
Capex	-692	-634	-633	-657
Cash flow from investment	-115	-1,677	-972	-962
Dividends	-1,479	-1,121	-2,631	-3,315
Change in net debt	-329	-1,093	-521	-675
FCF equity	2,385	2,758	3,385	3,778
Balance sheet summary (INRm)				
Tangible fixed assets	2,403	2,763	3,087	3,399
Current assets	3,954	5,285	6,052	7,009
Cash & others	1,481	2,575	3,096	3,771
Total assets	7,292	10,026	11,457	13,031
Operating liabilities	3,521	3,915	4,396	4,976
Gross debt	47	47	47	47
Net debt	-1,434	-2,528	-3,049	-3,724
Shareholders funds	1,673	1,899	1,922	2,180
Invested capital	1,612	1,815	1,904	1,918

Ratio, growth and per share analysis

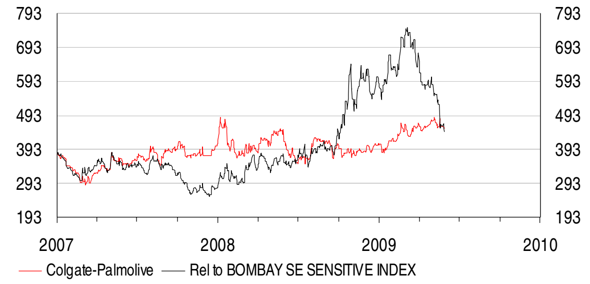
Year to	03/2008a	03/2009e	03/2010e	03/2011e
Y-o-y % change				
Revenue	13.8	15.0	13.3	13.9
EBITDA	54.2	16.8	15.8	14.7
Operating profit	59.3	15.5	16.3	15.0
PBT	56.5	13.9	17.8	20.6
HSBC EPS	22.9	22.5	15.7	8.7
Ratios (%)				
Revenue/IC (x)	9.4	9.9	10.3	11.4
ROIC	142.3	160.4	170.3	171.8
ROE	106.1	162.3	175.5	177.7
ROA	33.1	33.1	31.5	30.0
EBITDA margin	20.8	21.2	21.6	21.8
Operating profit margin	19.4	19.5	20.0	20.2
EBITDA/net interest (x)				
Net debt/equity	-83.7	-130.3	-155.4	-167.7
Net debt/EBITDA (x)	-0.5	-0.7	-0.7	-0.8
Per share data (INR)				
EPS reported (fully diluted)	17.34	20.84	24.54	26.70
HSBC EPS (fully diluted)	17.39	21.31	24.66	26.81
DPS	13.00	15.00	18.90	19.22
Book value	12.30	13.97	14.13	16.03

Valuation data

Year to	03/2008a	03/2009e	03/2010e	03/2011e
EV/sales	4.2	3.6	3.1	2.7
EV/EBITDA	20.3	16.8	14.3	12.3
EV/IC	38.7	33.2	31.2	30.5
PE*	27.3	22.3	19.2	17.7
P/Book value	38.6	34.0	33.6	29.6
FCF yield (%)	3.7	4.4	5.4	6.1
Dividend yield (%)	2.7	3.2	4.0	4.1

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Source: HSBC

Note: price at close of 29 May 2009

Results snapshot

Colgate-Palmolive: Results snapshot

(INRm)	Stand-alone			Consolidated		
	Q4 FY09	Q4 FY08	Change	FY09	FY08	Change
Net sales	4555	3913	16.4%	16952	14739	15.0%
Operating income	167	163	2.6%	646	561	15.2%
Total revenue	4722	4076	15.8%	17598	15300	15.0%
Cost of goods sold	2005	1768	13.4%	6809	5982	13.8%
Gross profit	2549	2145	18.8%	10143	8756	15.8%
Gross margin	56.0%	54.8%	115 bps	59.8%	59.4%	42 bps
Employee cost	389	307	26.5%	1509	1238	21.9%
Voluntary retirement scheme	49	0	NA	49	10	386.0%
Advertisement & sales promotion	702	735	-4.4%	2717	2565	5.9%
Other expenditure	649	584	11.2%	2929	2422	20.9%
EBITDA	928	683	35.9%	3585	3082	16.3%
Depreciation	64	55	16.5%	283	209	35.0%
EBIT	864	628	37.6%	3303	2873	15.0%
EBIT margin	18.3%	15.4%	290 bps	18.8%	18.8%	1 bps
Clean EBIT	913	628	45.4%	3352	2883	16.3%
Clean EBIT margin	19.3%	15.4%	393 bps	19.0%	18.8%	20 bps
Other income	38	37	2.7%	198	199	-0.7%
Interest	1	4	-69.4%	15	12	25.2%
PBT	901	662	36.3%	3485	3059	13.9%
Tax	131	105	24.0%	603	693	-12.9%
PAT	771	556	38.6%	2882	2367	21.8%
Minority interest	0	0	NA	25	9	166.3%
Net profit	771	556	38.6%	2858	2358	21.2%
EPS	5.67	4.09	38.6%	21.01	17.34	21.2%

Source: Company reports, HSBC

Colgate's net sales increased 16.4% for the latest quarter and 15.0% for the year, growing faster than the market. Market shares improved by 200bps for the quarter and 10bps for the year on y-o-y basis in toothpaste, and 30bps and 210bps, respectively, in toothpowder; and changed -20bps and 280bps, respectively, in toothbrushes. While toothpowder quarterly sales declined 2.6% quarter due to conversion of users to toothpaste, healthy 15% volume growth in the toothpowder segment was clocked. There was a marked shift of c300 bps from toothpowder to toothpaste as explained by category penetration numbers.

Gross margin expanded 115bps for the quarter and 42bps for the year, which we regard as commendable in an inflationary year, although part of this can be explained by Q4 FY08's being burdened by increases in raw-material costs granted to suppliers with a retrospective effect. Advertisings cost as a percentage of sales declined by 335bps for the quarter and 138bps for the year, resulting in 'clean' (ie excluding VRS expenses) EBIT growth of 45.4% and 16.3%, respectively.

The company has considerably stepped up its promotional activities: The oral health month, held annually in October, has had a 24% increase in participating dentists this year over last, and the number of towns covered totaled 200 versus 50 in 2005. A total of 0.76m dental checkups were carried out versus 0.42m last year. Colgate as a brand recommended by dentists moved up to 80% in 2007 from 75% in 2005, and 87% of dentists themselves use Colgate, up from 82% two years back.

The road ahead

We believe that FY10e sales growth may slow marginally to 13.3% from 15.0% in FY09e due to increased competitive activity. With HUL recording market share losses over the past few quarters, we believe there will be an increased effort on its part. HUL recently reduced its Pepsodent INR13 pack to

INR10 and its INR6 pack to INR5. However, we believe that Colgate will be able to maintain market shares at last year's levels due to its focus, innovation, and marketing initiatives, but that it will not have the advantage of sales being boosted by market share gains in FY10e, as was the case in FY09. As commodity cost has softened, we are building in a 30bps increase in gross margins for FY10e, but an increase in ad spend as a percentage of sales of 50bps, which we believe will be necessary to combat the increase in competition that we expect. However, we believe that employee cost will expand only 15%, compared with 22% this year owing to the voluntary retirement scheme.

Changes to our estimates

Colgate-Palmolive: Changes to our estimates

(INRm)	FY10e			FY11e		
	Old	New	Variance	Old	New	Variance
Sales	19,200	19,200	0.0%	21,861	21,861	0.0%
EBIT	3,620	3,841	6.1%	4,194	4,417	5.3%
PAT	3,206	3,337	4.1%	3,493	3,631	3.9%
EPS (INR)	23.57	24.54	4.1%	25.68	26.70	4.0%

Source: HSBC

Though we are keeping our sales estimates unchanged (see the table immediately above), we believe that our earlier estimates of material costs and advertisement expenses were on the higher side, as has been the case for FY09, too, and therefore we are reducing these, and our EPS estimates increase 4%.

Valuation

We previously valued Colgate on an average of DCF and PE methodologies, as markets were suppressed at that time, and the DCF value was coming out substantially stronger than the PE valuation. However, with the markets having recovered, the PE multiples are no longer depressed. We therefore are switching to a PE valuation basis, which is our preferred valuation methodology for all consumer staples stocks.

We are increasing our target price to INR540 from INR470. We value Colgate on a PE multiple of 22x for FY10e (our previous target price of INR470 implied a multiple of 20x). Over the past three years, the stock has fluctuated in a band of 31.2x and 16.1x, averaging 20.4x on a 12-month forward basis. We believe that the stock should trade slightly above its average PE due to the robust volume growth that it has clocked recently and that we expect in the future.

Our multiple of 22x is slightly lower than Dabur's 23x. While Colgate has higher return ratios and better free cash flows, compared to Dabur, it has a lower EPS growth rate and the disadvantage of being a single-product company. Applying 22x to our FY10e EPS of INR24.54, we arrive at our new target price of INR540.

Under our research model, for stocks without a volatility indicator, the Neutral band is five percentage points above and below the hurdle rate for Indian stocks of 11%. This translates into a Neutral band of 6% to 16% around the current share price. Our new 12-month target price of INR540 for Colgate-Palmolive India shares represents 13.9% absolute upside potential, and adding the anticipated 4.0% dividend yield, this suggests a potential total return of 17.9%, which is above the Neutral band. Thus, we reiterate our Overweight rating on the shares.

Risks

We see the following downside risks:

- Higher effective tax rates will hit the company after FY10e as the manufacturing facility at Baddi moves out of 100% tax incentives. We assume an increase in tax to 26% from 18%, but a higher increase could be a risk.
- Market share losses may happen if competition intensifies more than our expectations. Colgate has recovered from the shocks of low-price competition by Babool, Anchor, Ajanta, and Amar, but another price war could be a risk.
- Volumes are clocking double-digit growth, but there is a risk that volume growth might moderate due to the macroeconomic slowdown.
- Cost increases could reduce our gross margin estimates
- New entrants such as P&G or ITC could erode Colgate's market share.

Flashnote

HSBC Global Research

Consumer Brands & Retail
Household Products
Equity – India

Hindustan Unilever Ltd

Neutral

Target price (INR)	249.00
Share price (INR)	227.15
Potential total return (%)	12.9

Performance	1M	3M	12M
Absolute (%)	-2.5	-12.4	-9.8
Relative^ (%)	-11.3	-29.0	27.1

Index^	BOMBAY SE IDX
RIC	HLL.BO
Bloomberg	HUVR IN
Market cap (USDm)	10,048
Market cap (INRm)	495,159
Enterprise value (INRm)	477,176
Free float (%)	49

11 May 2009

Percy Panthaki *
Analyst
HSBC Securities and Capital Markets (India) Private Limited
+ 9122 2268 1240
percypanthaki@hsbc.co.in

Maya Shivani *
Associate
Bangalore

Maintain Neutral; going through a rough patch

- **Volume de-growth and lacklustre growth in personal products in MQ results is cause for concern, we believe**
- **Company has taken corrective action and we expect recovery in H2 FY10e; cutting our EPS estimates by c4%+**
- **Lowering target price to INR249 from INR255 and maintaining Neutral rating; value should emerge at cINR215**

Quality of growth an issue: HUL reported 12% FMCG sales growth and 23% EBIT growth for the March 09 quarter, but this was accompanied by a 4.2% volume decline, low 1.9% sales growth in the personal products segment, and market share losses in most segments. The sudden drop in volumes in the quarter followed general trade de-stocking in anticipation of price declines, reductions in modern trade outlets, and competitive pressures.

We expect a recovery in H2 FY10e: The company has taken actions to address the volume decline viz price reductions, volume increases, consolidation of distributors, reduction in distributor inventory, and hand-held recorders given to sales staff, eg, which we believe will start showing results in the next six months.

Cutting EPS estimates: We are reducing our EPS estimate for FY10e by 4.3%; we now expect y-o-y EPS growth of 11.5%, based on sales growth of 9.7%, gross margin expansion of 50 bps, an overhead increase of 9% y-o-y, and a 370bps increase in the effective tax rate. Similarly, we are cutting our FY11e EPS by 4.6%.

Lowering target price to INR249 from INR255, maintaining Neutral rating: We value HUL at INR249 based on a 23x FY10e PE multiple, same as that for Dabur. While HUL traditionally trades at a 15-20% premium to smaller consumer companies such as Dabur, we believe that the shrinkage of the premium to zero is justified, given the subpar performance. Our 23x PE multiple is a 15-20% discount to the average of the last three years. Our target price implies a potential total return of 12.9% including dividend yield.

Hindustan Unilever Ltd: Snapshot (INRm)

Year to Dec	Revenue	y-o-y	EBIT	y-o-y	PAT	y-o-y	EPS (INR)	PE	ROE	ROA
CY07	138,711	11.8%	17,550	18.9%	19,149	1.3%	8.69	26.1x	92.7%	26.7%
FY09e	205,011	47.8%	25,029	42.6%	25,045	30.8%	11.47	19.8x	126.9%	32.5%
FY10e	183,831	-10.3%	24,844	-0.7%	23,666	-5.5%	10.84	21.0x	95.6%	27.0%
FY11e	203,715	10.8%	29,281	17.9%	26,922	13.8%	12.33	18.4x	97.8%	28.0%

*2007 is December year end; FY09e is for the period Jan-08 to Mar-09. FY10e and FY111e are for the 12-month period ending March.
Source: Company reports, HSBC

Financials & valuation

Financial statements

Year to	12/2007a	03/2009e	03/2010e	03/2011e
Profit & loss summary (INRm)				
Revenue	138,711	205,011	183,831	203,715
EBITDA	18,969	27,029	26,697	31,339
Depreciation & amortisation	-1,419	-2,000	-1,853	-2,057
Operating profit/EBIT	17,550	25,029	24,844	29,281
Net interest	1,975	1,632	1,625	1,814
PBT	23,272	30,279	29,644	34,588
Taxation	-4,084	-5,179	-5,929	-7,609
Net profit	19,149	25,045	23,666	26,922
Cash flow summary (INRm)				
Cash flow from operations	18,109	24,232	26,557	30,234
Capex	-3,346	-5,661	-3,872	-4,134
Cash flow from investment	8,544	-6,375	-5,372	-5,784
Dividends	-22,924	-16,044	-18,542	-20,922
Change in net debt	2,081	-1,374	-2,643	-3,527
FCF equity	14,992	13,428	19,173	22,253
Balance sheet summary (INRm)				
Tangible fixed assets	17,477	21,577	23,596	25,672
Current assets	34,196	44,631	46,891	53,997
Cash & others	2,624	3,998	6,641	10,168
Total assets	70,060	85,515	91,509	102,568
Operating liabilities	45,418	50,516	54,807	59,702
Gross debt	1,021	1,021	1,021	1,021
Net debt	-1,603	-2,976	-5,620	-9,147
Shareholders funds	15,082	24,398	25,097	29,958
Invested capital	5,774	13,945	11,402	12,280

Ratio, growth and per share analysis

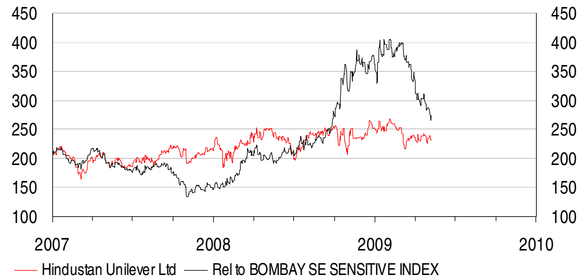
Year to	12/2007a	03/2009e	03/2010e	03/2011e
Y-o-y % change				
Revenue	11.8	47.8	-10.3	10.8
EBITDA	17.7	42.5	-1.2	17.4
Operating profit	18.9	42.6	-0.7	17.9
PBT	4.5	30.1	-2.1	16.7
HSBC EPS	1.4	32.0	-5.5	13.8
Ratios (%)				
Revenue/IC (x)	24.2	20.8	14.5	17.2
ROIC	276.8	241.3	179.0	218.7
ROE	92.7	126.9	95.6	97.8
ROA	26.7	32.5	27.0	28.0
EBITDA margin	13.7	13.2	14.5	15.4
Operating profit margin	12.7	12.2	13.5	14.4
Net debt/equity	-10.6	-12.2	-22.3	-30.3
Net debt/EBITDA (x)	-0.1	-0.1	-0.2	-0.3
Per share data (INR)				
EPS reported (fully diluted)	8.69	11.47	10.84	12.33
HSBC EPS (fully diluted)	8.69	11.47	10.84	12.33
DPS	9.00	7.50	7.61	8.65
Book value	6.84	11.20	11.52	13.75

Valuation data

Year to	12/2007a	03/2009e	03/2010e	03/2011e
EV/sales	3.5	2.3	2.6	2.3
EV/EBITDA	25.3	17.7	17.7	14.9
EV/IC	83.0	34.2	41.5	38.1
PE*	26.1	19.8	21.0	18.4
P/Book value	33.2	20.3	19.7	16.5
FCF yield (%)	3.1	2.8	4.0	4.7
Dividend yield (%)	4.0	3.3	3.3	3.8

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Source: HSBC

Note: price at close of 11 May 2009

HSBC

March 2009 quarter: performance snapshot

Hindustan Unilever Ltd: March 2009 quarter and full-year stand-alone results snapshot

(INRm)	Jan – Mar 2009	Jan – Mar 2008	y-o-y growth	Apr – Mar 2009	Apr – Mar 2008	y-o-y growth
Net sales	39,883	37,626	6.0%	164,768	142960	15.3%
Total income	40,354	38,399	5.1%	167,617	145484	15.2%
COGS	20,856	20,452	2.0%	87,928	75884	15.9%
Gross profit	19,027	17,174	10.8%	76,840	67,076	14.6%
Gross profit margin	47.7%	45.6%	206 bps	46.6%	46.9%	-28 bps
Employee costs	2343.5	2135.2	9.8%	9,386	8027	16.9%
Advertisement and sales promotion	4505.5	4391.4	2.6%	16,918	15057	12.4%
Other expenditure	6685.1	6569.4	1.8%	27,835	24677	12.8%
EBITDA	5,963	4,851	22.9%	25,551	21,840	17.0%
EBITDA margin	15.0%	12.9%	206 bps	15.5%	15.3%	23 bps
Depreciation	412.5	363	13.6%	1,590	1418	12.2%
EBIT	5,551	4,488	23.7%	23,961	20,422	17.3%
EBIT margin	13.9%	11.9%	199 bps	14.5%	14.3%	26 bps
PBT	4,660	4,714	-1.1%	25,374	22387	13.3%
PBT margin	11.7%	12.5%	-84 bps	15.4%	15.7%	-26 bps
Tax expense	710.4	904.8	-21.5%	4,131	4251	-2.8%
Effective tax rate	15.2%	19.2%	-395 bps	16.3%	19.0%	-271 bps
Net profit	3,950	3,810	3.7%	21,155	19110	10.7%
Net profit margin	9.9%	10.1%	-22 bps	12.8%	13.4%	-53 bps
*Diluted EPS (bei)	1.81	1.75	3.4%	9.73	8.33	16.8%
**Diluted EPS (aei)	1.81	1.75	3.4%	9.69	8.78	10.4%

* Before extraordinary items. ** After extraordinary items. Apr–Mar 2008 numbers have been derived from quarterlies and might not match the adjusted company-guided memorandum numbers for the full year.
Source: Company reports, HSBC

- While sales growth for the quarter was just 6%, FMCG sales growth at 11.8% was in line with market expectations and the lower overall number was due to a decline in non core exports. Volume decline of 4.2% for the quarter was a result of price increases taken over last 12-15 months, and the recent price declines have not yet fully reached retail shelves.

- Gross and EBIT margin grew by c200bps as a result of cuts in product prices lagging behind reductions in commodity costs. While A&P spends grew just 2.6% y-o-y, EBIT growth would still have been robust at 15% (instead of the reported 23%) if A&P spends had grown in line with FMCG sales.

Hindustan Unilever Ltd: March 2009 quarter segment results

(INRm)	Sales			Segment PBT			Segment margins	
	Mar-09	Mar-08	y-o-y growth	Mar-09	Mar-08	y-o-y growth	Mar-09	Mar-08
Soaps and detergents	20121.9	17382	15.8%	3335.3	2325.1	43.4%	16.6%	13.4%
Personal products	10386	10188.8	1.9%	2389.4	2458.1	-2.8%	23.0%	24.1%
Beverages	4892.9	4309.7	13.5%	655.1	535	22.4%	13.4%	12.4%
Processed foods	1633.9	1519.8	7.5%	-44.7	34.3	-230.3%	-2.7%	2.3%
Ice creams	452.8	369.8	22.4%	-18.6	-25	-25.6%	-4.1%	-6.8%
Exports	2204.7	3989.3	-44.7%	143.6	177.9	-19.3%	6.5%	4.5%
Others	675	441.3	53.0%	-242.2	-305.3	-20.7%	-35.9%	-69.2%
Total	**40,367**	**38,201**	**5.7%**	**6,218**	**5,200**	**19.6%**		

Source: Company reports, HSBC

- On a segment basis, growth in personal products disappointed, at 1.9%, driven by loss in market shares and outlet consolidation in modern trade.

- For the year, performance was better, with the company reporting the following on memorandum basis for the 12 months ended March 09 vs. 12 months ended March 08. Sales grew 15.5%, driven by 3.1% growth in volumes. EBIT margin expanded by 40 bps, and EBIT grew 18.8% y-o-y. PAT after exceptional items grew 10.6% y-o-y.

The road ahead

Following the disappointing March quarter, we believe that HUL is aware of the problems it faces and is taking corrective action such as (1) cutting product prices in the mass-market segment, where it has had the highest volume losses, (2) hastening the 'speed to market', ie time it takes for company actions to reach the consumer, (3) improving the front end by enabling the salesforce with hand-held recorders, which give outlet level data and can improve insights, (4) distributor consolidation, appointing larger and fewer distributors instead of many smaller ones, enabling ease of management and implementation of technology-driven solutions, and (5) working on near-zero levels of inventory at distributor levels in urban areas, preventing de-stocking.

We believe that in FY10e, HUL will be able to increase sales 9.7%, driven 4pptsthrough volume and 5.5ppts through price. While the first half of the fiscal may be tilted towards price growth, the second half should be tilted towards volume growth. We believe that a 50bps increase in gross margins is possible due to declining input costs. Overhead growth should be limited to 9% y-o-y (7% increase in employee costs, 15% in A&P spends, and 6% in other expenses) due to cost-efficiency plans. EBIT thus would grow 16.2% y-o-y (70bps margin expansion) but PAT growth is likely to be lower due to a 370bps increase in the effective tax rate.

Hindustan Unilever Ltd: Comparable consolidated earnings snapshot (INRm)

12 month period ended:	Mar-08	Mar-09e	Mar-10e	Mar-11e
Net sales	145,048	167,530	183,831	203,715
y-o-y growth		15.5%	9.7%	10.8%
EBIT	18,130	21,384	24,844	29,281
y-o-y growth		18.0%	16.2%	17.9%
EPS (INR)	8.87	9.70	10.84	12.33
y-o-y growth		9.4%	11.7%	13.8%
EPS without exceptional / extraordinary items (INR)	8.42	9.72	10.84	12.33
y-o-y growth		15.5%	11.5%	13.8%

Source: Company reports, HSBC

Changes in our estimates

Hindustan Unilever Ltd: Changes in our forecasts

12 month period ended:	FY10e			FY11e		
	Old	New	Variance	Old	New	Variance
Sales	188,506	183,831	-2.5%	211,126	203,715	-3.5%
EBIT	24,397	24,844	1.8%	28,154	29,281	4.0%
EBIT margin	12.9%	13.5%	57 bps	13.3%	14.4%	104 bps
PBT	30,142	29,644	-1.7%	34,399	34,588	0.5%
PBT margin	16.0%	16.1%	14 bps	16.3%	17.0%	69 bps
Tax	5,426	5,929	9.3%	6,192	7,609	22.9%
Tax rate %	18.0%	20.0%	200 bps	18.0%	22.0%	400 bps
Net profit	24,665	23,666	-4.1%	28,149	26,922	-4.4%
Net profit margin	13.1%	12.9%	-21 bps	13.3%	13.2%	-12 bps
Diluted EPS (INR)	11.32	10.84	-4.3%	12.92	12.33	-4.6%

Source: HSBC

Valuation

We are lowering our target price to INR249 from INR255. We value HUL on 23x FY10e PE at INR249 per share. We equate our target multiple for Dabur and HUL at 23x. Traditionally, HUL has traded at 15-20% premiums to smaller consumer stocks such as Dabur. However, we believe that the deterioration in the quality of growth will erode that premium. While on one hand, Dabur's EPS growth of c20% is higher than HUL's c12%, on the other hand return ratios for HUL are higher with ROE of 95.6% vs. Dabur's 49.1%. We believe that until HUL restores the quality of its growth (ie better volume growth and halting market-share losses), it is unlikely to command the premium valuation at which it usually trades. We therefore believe that a PE multiple of 23x is appropriate. Our target multiple is 15-20% lower than what HUL has traded at over the past three years. While correlation between HUL's PE and Sensex's PE is very low, we believe improvement in broader market multiples justifies a marginal increase from 22.5x to 23x in our target PE multiple for HUL.

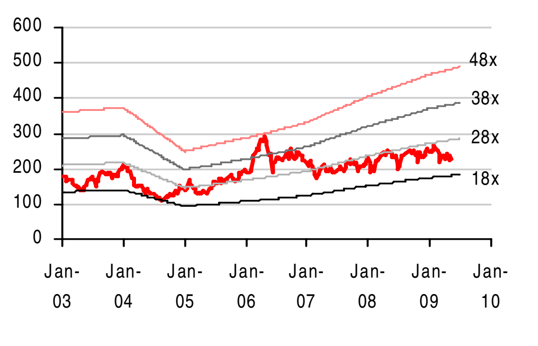
Under our research model, for stocks without a volatility indicator, the Neutral band is five percentage points above and below the hurdle rate for Indian stocks of 11%. This translates into a Neutral band of 6% to 16% around the current share price. Our new target price of INR249 for HUL shares represents 9.6% absolute upside potential; added this the anticipated 3.3% dividend yield suggests a potential total return of 12.9%, which is within the Neutral band. We therefore reiterate our Neutral rating on HUL shares.

Risks

Upside risks: (1) HUL re-asserts it leadership and starts gaining market share decisively; (2) FMCG industry growth is more resilient than we expect; and (3) HUL's margins expand due to a fall in raw-material costs and cost-efficiency measures.

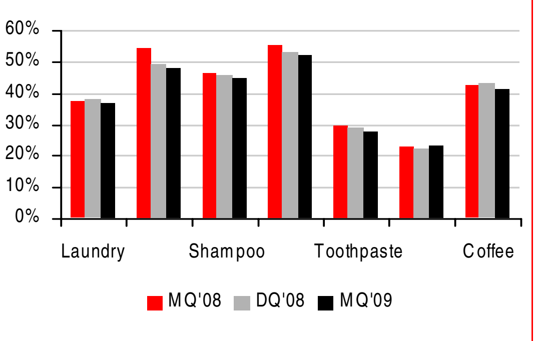
Downside risks: (1) Regional/unorganised players could become active, with commodity prices falling, and this may result in further market share erosion for HUL; (2) a macroeconomic slowdown may result in lower consumer spending and may affect volume growth for FMCG companies; (3) organised retail may flex its muscle and ask for products at lower cost, which may result in margin contraction.

Hindustan Unilever Ltd: 12-month spot PE band chart



Source: NSE India, HSBC

Hindustan Unilever Ltd: Falling market share



Source: Company reports, HSBC

Flashnote

HSBC Global Research

Consumer Brands & Retail
Tobacco
Equity – India

ITC

Neutral

Target price (INR)	**193.00**
Share price (INR)	**183.60**
Potential total return (%)	**7.5**

Performance	1M	3M	12M
Absolute (%)	-3.6	1.9	-17.8
Relative^ (%)	-24.1	-34.4	1.2

Index^	BOMBAY SE IDX
RIC	ITC.BO
Bloomberg	ITC IN
Market cap (USDm)	14,627
Market cap (INRm)	692,980
Enterprise value (INRm)	651,279
Free float (%)	70

22 May 2009

Percy Panthaki*
Analyst
HSBC Securities and Capital Markets (India) Private Limited
+9122 2268 1240
percypanthaki@hsbc.co.in

Maya Shivani*
Associate
Bangalore

View HSBC Global Research at:
http://www.research.hsbc.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/qualified pursuant to NYSE and/or NASD regulations

Issuer of report: HSBC Securities and Capital Markets (India) Private Limited

Maintain N – Decent performance; all eyes on budget

- **Q4 PAT growth marginally below expectations, but quality of growth does leave us with much cause for concern**
- **Cigarettes EBIT growth strong at 24%, but hotels hit by slowdown and FMCG losses within expectations**
- **We maintain our 12-month target price of INR193 and reiterate our Neutral rating on ITC shares**

Core categories do well: ITC reported Q4 FY09 (March) revenues of INR38.9bn (-1.1%growth) and PAT of INR8.09bn (10% growth). The cigarettes division did well, with growth of 16.3% in sales and 24.3% in EBIT. Hotels bore the brunt of the slowdown, with sales and profits down 29.3% and 50.2%, respectively. The FMCG business also did well, with 13.5% sales growth and losses restricted to INR1.2bn. While agri division sales fell 51.2%, due to defocusing non-core exports, profits rose 43.4%, and the paperboards division received a boost from the paper sales through the stationery division.

Road ahead: We keep our estimates unchanged, and we expect double-digit EPS growth for FY10. For the cigarettes division, we build two scenarios: (a) high taxes and big price increases, and therefore a volume decline, and (b) low taxes and small price increases, and therefore volume growth. We derive different EPS values for each scenario, and we use a 14x PE multiple in scenario 'a' and a 19x PE multiple in scenario 'b' on the cigarette EPS. For FMCG, we expect losses to narrow to INR3.6bn, and for the hotels business, we expect a flattish year, as a lot of damage has already been done in H2 FY09. The agri business will concentrate on core commodities, and this may reduce volatility of margins. The paperboard business is likely to be helped by the stationery business.

Valuation and rating: We value ITC on an SOTP basis at INR193 per share. Our high-tax scenario suggests an INR167 target price and our low-tax scenario INR218. We take an average of these to arrive at our INR193 target price, which implies a potential total return of 7.5%. We maintain our Neutral rating on the stock.

ITC: Snapshot (INRm)

Year to 31 March	Sales	y-o-y	EBIT	y-o-y	Net profit	y-o-y	EPS (INR)	PE (x)	ROE	ROA
FY08	146,591	15.7%	40,953	10.9%	31,578	14.6%	8.35	22.0	27.5%	19.2%
FY09e	163,323	11.4%	44,914	9.7%	33,246	5.3%	8.81	20.8	25.3%	18.0%
FY10e	194,511	19.1%	53,295	18.7%	39,268	18.1%	10.38	17.7	26.2%	18.7%
FY11e	220,652	13.4%	61,310	15.0%	45,089	14.8%	11.92	15.4	26.3%	18.8%

Source: HSBC

Financials & valuation

Financial statements

Year to	03/2008a	03/2009e	03/2010e	03/2011e
Profit & loss summary (INRm)				
Revenue	146,591	163,323	194,511	220,652
EBITDA	45,681	50,723	59,231	68,142
Depreciation & amortisation	-4,729	-5,809	-5,937	-6,832
Operating profit/EBIT	40,953	44,914	53,295	61,310
Net interest	-63	-187	-30	-30
PBT	46,830	49,909	58,222	66,854
HSBC PBT	46,752	49,848	58,118	66,736
Taxation	-14,970	-16,254	-18,598	-21,356
Net profit	31,578	33,246	39,268	45,089
HSBC net profit	31,578	33,246	39,268	45,089
Cash flow summary (INRm)				
Cash flow from operations	30,067	36,716	39,668	47,681
Capex	-23,263	-11,337	-15,605	-20,616
Cash flow from investment	-19,681	-12,413	-21,252	-26,264
Dividends	-13,827	-15,432	-16,340	-19,360
Change in net debt	3,337	-9,027	-2,259	-2,269
FCF equity	4,645	20,606	19,462	21,900
Balance sheet summary (INRm)				
Tangible fixed assets	78,193	83,721	93,389	107,173
Current assets	73,340	86,605	101,127	111,850
Cash & others	7,768	16,775	19,014	21,262
Total assets	177,616	197,485	227,323	257,477
Operating liabilities	29,708	31,621	38,362	42,590
Gross debt	2,249	2,229	2,209	2,189
Net debt	-5,519	-14,546	-16,805	-19,073
Shareholders funds	122,878	139,784	159,692	182,552
Invested capital	114,056	121,930	137,140	155,170

Ratio, growth and per share analysis

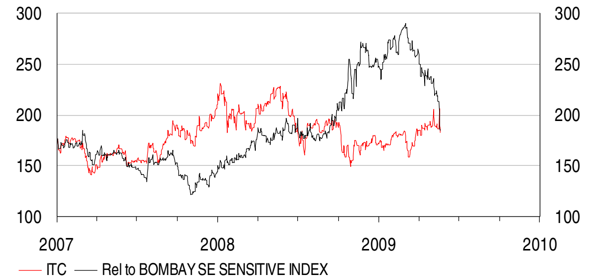
Year to	03/2008a	03/2009e	03/2010e	03/2011e
Y-o-y % change				
Revenue	15.7	11.4	19.1	13.4
EBITDA	11.8	11.0	16.8	15.0
Operating profit	10.9	9.7	18.7	15.0
PBT	15.5	6.6	16.7	14.8
HSBC EPS	14.2	5.5	17.9	14.8
Ratios (%)				
Revenue/IC (x)	1.4	1.4	1.5	1.5
ROIC	25.1	24.3	26.8	27.3
ROE	27.5	25.3	26.2	26.3
ROA	19.2	18.0	18.7	18.8
EBITDA margin	31.2	31.1	30.5	30.9
Operating profit margin	27.9	27.5	27.4	27.8
EBITDA/net interest (x)	727.4	271.4	1974.4	2271.4
Net debt/equity	-4.5	-10.3	-10.4	-10.4
Net debt/EBITDA (x)	-0.1	-0.3	-0.3	-0.3
Per share data (INR)				
EPS reported (fully diluted)	8.35	8.81	10.38	11.92
HSBC EPS (fully diluted)	8.35	8.81	10.38	11.92
DPS	3.49	3.70	4.34	4.98
Book value	32.49	36.96	42.23	48.27

Valuation data

Year to	03/2008a	03/2009e	03/2010e	03/2011e
EV/sales	4.5	4.0	3.3	2.9
EV/EBITDA	14.5	12.8	10.9	9.3
EV/IC	5.8	5.3	4.7	4.1
PE*	22.0	20.8	17.7	15.4
P/Book value	5.7	5.0	4.3	3.8
FCF yield (%)	0.7	3.1	2.9	3.3
Dividend yield (%)	1.9	2.0	2.4	2.7

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Source: HSBC

Note: price at close of 22 May 2009

HSBC

Results snapshot

ITC: Stand-alone segment results analysis (INRm)

	Q4 FY09	Q4 FY08	y-o-y %	FY09	FY08	y-o-y %
Cigarettes	20,115	17,302	16.3%	75,568	66,350	13.9%
FMCG other	8,368	7,373	13.5%	30,056	25,096	19.8%
Hotels	2,210	3,125	-29.3%	9,355	10,121	-7.6%
Agri business	5,259	10,781	-51.2%	38,460	38,684	-0.6%
Paperboards	7,136	5,677	25.7%	26,471	21,579	22.7%
Net sales (before segment elimination)	**43,089**	**44,259**	**-2.6%**	**179,910**	**161,830**	**11.2%**
Cigarettes	10,814	8,701	24.3%	41,838	36,340	15.1%
FMCG other	-1,173	-1,179	-0.5%	-4,835	-2,635	83.5%
Hotels	711	1,428	-50.2%	3,162	4,108	-23.0%
Agri business	531	370	43.4%	2,562	1,292	98.3%
Paperboards	1,519	1,227	23.8%	5,086	4,531	12.2%
Segment EBIT	**12,401**	**10,547**	**17.6%**	**47,813**	**43,636**	**9.6%**
Un-allocable inc. net of un-allocable exp.	-347	322	-207.7%	628	2,128	-70.5%
Interest	137	27	406.7%	183	46	297.4%
PBT	11,918	10,842	9.9%	48,257	45,718	5.6%
Net profit	8,090	7,356	10.0%	32,636	31,201	4.6%
Basic EPS	2.15	1.95	10.3%	8.66	8.29	4.5%
Diluted EPS	**2.14**	**1.93**	**10.9%**	**8.64**	**8.25**	**4.7%**
Margins						
Cigarettes	53.8%	50.3%	347 bps	55.4%	54.8%	59 bps
FMCG other	-14.0%	-16.0%	197 bps	-16.1%	-10.5%	-558 bps
Hotels	32.2%	45.7%	-1351 bps	33.8%	40.6%	-679 bps
Agri business	10.1%	3.4%	666 bps	6.7%	3.3%	332 bps
Paperboards	21.3%	21.6%	-33 bps	19.2%	21.0%	-178 bps

Source: Company reports, HSBC

Cigarettes: Q4 FY09 saw a 16.3% increase in revenues but 24.3% growth in EBIT. This was due to a 13-14% increase in the weighted average selling price on a y-o-y basis. While volume declined 3.0-3.5% in FY09 and Q4, the cumulative impact of price increases taken since July 2008 led to a 13.9% increase in net revenues and 15.1% in EBIT on a y-o-y basis.

FMCG others: FY09 saw 19.8% top-line growth in the other FMCG businesses, with a loss at the EBIT level that narrowed to INR2.6bn in FY09 from INR4.8bn in FY08. For the quarter, losses were maintained at last year's level. In this category for FY09, the biscuits category grew 14%, the Agarbatti business 20%, and the stationery business a robust 60%. The lifestyle retailing business achieved robust growth of 32% in exports, despite tough economic conditions in the target US and European markets, driven largely by an improved product mix. The branded packaged-foods business clocked reasonable growth but was adversely impacted by high raw-material costs. The personal care business strengthened its 'Vivel' range and continued launching differentiated products in the market.

Hotels: The gloomy macroeconomic environment has been weighing heavily on the hotels business for the past two quarters. This, combined with the terrorist strikes in Mumbai and the loss of IPL business as it moved to South Africa, resulted in poor H2 results. Accordingly, the hotels business saw revenue decreases of 14% in Q3 and 29.3% in Q4, resulting in a 7.6% decline for FY09. Furthermore, average occupancy rates (ARR) across the sector dropped sharply, which led to a 23% deceleration at the EBIT level for FY09.

Agri business: In Q4 FY09, ITC rationalised its agri-commodity portfolio, necessitated by increasing policy intervention and volatility in commodity markets. Thus, it moved out of commodities such as rice, pulses, and sesame seeds, while increasing concentration on commodities used in its other FMCG businesses such as leaf tobacco, wheat, soya, and potatoes. This resulted in a 51.2% fall in revenues for Q4 and a flat FY09. However, these were low-margin commodities, resulting in a 43.4% jump in Q4 and 98.3% growth for FY09 at the EBIT level on a y-o-y basis. Robust performance was achieved by the leaf tobacco portfolio. However, if the impact of leaf tobacco sold to the cigarettes division were excluded, EBIT would be lower by about INR250m; this is accounted for in the unallocated other expenses line item.

Paperboards: Sales of value-added paperboards grew 13% in the year. FY09 saw a new paper manufacturing plant with a capacity of 0.1m TPA commencing operations. A revenue increase of 25.7% for Q4 FY09 was largely driven by capacity ramp-up at this plant, with further back-end support to the stationery business.

The road ahead

Going forward, we expect hotels business revenues to remain under pressure in Q1 FY10. We expect Q2 revenues to be relatively flat, with a marginal recovery in Q3 and Q4. Accordingly, we estimate that revenues will end flat in FY10e. We estimate FMCG other will clock 20-22% revenue growth, driven by the personal care portfolio and the foods business, and that losses will narrow to INR3.6bn.

In the case of cigarettes, we believe that one of the main issues affecting ITC is taxation. With heavy taxes on cigarettes over the last two years, there is apprehension that taxes could be high next year, too. If this happens, it should require large price increases and thereby affect volume and EPS. We therefore evaluate two scenarios – one of a normal 5% excise duty increase and the other with a 15% excise duty increase. Our estimates of the impact on revenue and profit for FY10 are in the following table.

ITC: Tax scenarios

Scenario	Impact on FY10e assumptions	Rationale
Low taxation: 5% increase in excise duty (annualised 3.6%)	7% annualised increase in average selling prices (4.2% after budget) 6.4% annualised increase in volumes (6.5% after budget) 9% increase in overheads	Demonstrated ability to pass on increases higher than required to offset increased taxes Growth in cigarette volumes has not been affected during moderate tax and price increase regime Trade and distribution support based on historical spend levels
High taxation: 15% increase in excise duty (annualised 10.9%)	12.5% annualised increase in average selling prices (11.7% after budget) 0.2% annualised increase in volumes (2% decline after budget) 12% increase in overheads	Pass on the entire burden of higher taxes through matching price increases Third successive year of higher-than-normal price increases to affect medium-term consumer demand Increased trade and distribution support to contain volume declines and loss of market share

Source: HSBC

- **Low taxation (best case).** Net sales to grow 15.5% for the company and 17.6% for the cigarettes business for FY10. EBIT to grow 18.5% for the company and 19% for the cigarettes business. This results in diluted EPS of INR10.56, or growth of 18.5%.

- **High taxation (worst case).** Net sales to grow 14.1% for the company and 14.3% for the cigarettes business for FY10. EBIT to grow 14.3% for the company and 13.7% for the cigarettes business. This results in diluted EPS of INR10.19, a growth of 14.3%.

Valuation

ITC: Scenario analysis

		Best case			Worst case			Average		
(INR)	Business	Multiple	Per share	Price	Multiple	Per share	Price	Multiple	Per share	Price
EPS	Cigarettes	19.0x	9.1	174	14.0x	8.8	123	16.5x	9.0	149
	Hotels	15.0x	0.6	9	15.0x	0.6	9	15.0x	0.6	9
	Agribusiness	6.0x	0.5	3	6.0x	0.5	3	6.0x	0.5	3
	Paperboards	5.0x	1.0	5	5.0x	1.0	5	5.0x	1.0	5
Sales	FMCG - Others	1.5x	9.9	15	1.5x	9.9	15	1.5x	9.9	15
Cash	Cash per share			12			12			12
	Target price			**218**			**167**			**193**

Source: HSBC

We value ITC on an SOTP basis at INR193 per share on the average of valuations derived for the scenarios of normal and high taxation.

While we note little difference in EPS from cigarettes in the two scenarios, because ITC can recover much of what it loses in volumes through price increases, we believe that market will pay a better multiple for volume growth. In our view, low volume growth reduces the long-term sustainability of EPS growth, as large price increases cannot be taken every year. We accordingly attribute 19x in a normal taxation scenario and 14x in a high-taxation scenario. We believe that uncertainty until the Indian government budget is announced will weigh on the market, and we apply a 16.5x multiple to our average case scenario.

Rating

Under our research model, for stocks without a volatility indicator, the Neutral band is five percentage points above and below our hurdle rate for Indian stocks of 11%, or 6% to 16% around the current share price. Our 12-month target price of INR193 for ITC shares represents a potential total return, including a 2.4% dividend yield, of 7.5%, which is within the Neutral band; thus, we reiterate our Neutral rating.

Risks

Upside risks, in our view, include moderate or marginal tax increases on cigarettes, another round of price increases beyond the full-year average of c14%, FMCG losses contained due to successful garnering of high market shares for personal products, and an earlier-than-anticipated turnaround of the foods business.

Downside risks that we see include tobacco volumes' failure to continue momentum, an adverse regulatory environment including tough implementation of smoking bans and changes in the Cigarette and Other Tobacco Products Act 2003 (COTPA), and the PE multiple for the cigarette business contracting more than we estimate.

Consumer & Retail
Personal Products
Equity – India

Marico Industries

Downgrade to Neutral (V); fairly priced

- **Q4 results boosted by ad spend cuts, in line with expectations adjusting for this; thus, share price spurt surprising**
- **We believe that top-line growth will slow substantially; we are cutting EPS estimates for FY10 and FY11 by 3.4% each**
- **We are lowering our target price to INR69.4 from INR72 and downgrading our rating to Neutral (V) from Overweight (V) as the stock price now appears near fair value**

Neutral (V)

Target price (INR)	69.40
Share price (INR)	67.30
Potential total return (%)	4.1

Performance	1M	3M	12M
Absolute (%)	15.6	14.7	-5.7
Relative^ (%)	-4.9	-7.3	45.2

Index^	BOMBAY SE IDX
RIC	MRCO.BO
Bloomberg	MRCO IN
Market cap (USDm)	812
Market cap (INRm)	40,986
Enterprise value (INRm)	43,698
Free float (%)	37

Note: (V) = volatile (please see disclosure appendix)

Q4 (March) results boosted by reduction in ad spends: Marico reported a 74% increase in PBT before one-off items; however, ad spends declined 20% y-o-y, fuelling most of this increase. Adjusting for that, we believe the results are in line with our and the consensus expectations, and the 5%+ increase in the stock price is therefore surprising. Gross margins remain be under pressure, although we expect this to reverse in coming quarters. Though overall volume growth at 9% was higher than the 7% in Q3, growth in the core portfolio – ie Parachute, Other hair oils, and Saffola – did not improve substantially. Kaya same-store sales growth dropped to single digits from 20%+ growth 3-4 quarters ago.

The road ahead and changes in our estimates: We believe that the year ahead will be more challenging than the past year. Sales growth will fall from 25% (changed from 15%) in FY09e to 12% in FY10e, as most of the growth should be volume-led and pricing levers absent. While we estimate gross margins will increase by 200bps, 150bps will be eaten away by the increase in ad spends, and EBITDA margins will expand by 70bps. We therefore are lowering our EPS estimates for FY10 and FY11 by 3.4% each.

Valuation: We retain our PE multiple of 19x for valuing Marico, as we believe that any reduction due to our lowering our EPS estimates is offset by improved multiples across the market. We derive a revised target price of INR69.4, down from INR72. Our new target price suggests a potential total return, including dividend yield, of 4.1%. Thus, we are downgrading our rating to Neutral (V) from Overweight (V).

22 April 2009

Percy Panthaki *
Analyst
HSBC Securities and Capital Markets (India) Private Limited
+9122 2268 1240
percypanthaki@hsbc.co.in

Maya Shivani *
Associate
Bangalore

View HSBC Global Research at:
http://www.research.hsbc.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/qualified pursuant to NYSE and/or NASD regulations

Issuer of report: HSBC Securities and Capital Markets (India) Private Limited

Marico Industries: Snapshot (INRm)

Year to Mar	Revenue	y-o-y chge	EBIT	y-o-y chge	HSBC net profit	y-o-y chge	HSBC EPS (INR)	PE	ROE	ROA
FY08	19,050	22.4%	2,155	47.1%	1,585	63.4%	2.60	25.9x	62.5%	22.8%
FY09e	23,884	25.4%	2,662	23.5%	2,037	28.6%	3.34	20.1x	53.0%	20.0%
FY10e	26,803	12.2%	3,156	18.6%	2,225	9.2%	3.65	18.4x	41.4%	19.8%
FY11e	31,149	16.2%	3,721	17.9%	2,640	18.6%	4.33	15.5x	36.8%	20.6%

Source: HSBC

Financials & valuation

Financial statements

Year to	03/2008a	03/2009e	03/2010e	03/2011e
Profit & loss summary (INRm)				
Revenue	19,050	23,884	26,803	31,149
EBITDA	2,462	3,020	3,565	4,199
Depreciation & amortisation	-307	-358	-409	-478
Operating profit/EBIT	2,155	2,662	3,156	3,721
Net interest	-305	-357	-356	-262
PBT	2,051	2,296	2,854	3,521
HSBC PBT	1,945	2,447	2,854	3,521
Taxation	-360	-409	-628	-880
Net profit	1,691	1,887	2,225	2,640
HSBC net profit	1,585	2,037	2,225	2,640
Cash flow summary (INRm)				
Cash flow from operations	1,185	1,466	2,342	2,734
Capex	-1,614	-865	-855	-948
Cash flow from investment	-1,614	-865	-855	-948
Dividends	-325	-486	-573	-679
Change in net debt	746	-115	-914	-1,106
FCF equity	-740	609	1,434	1,724
Balance sheet summary (INRm)				
Intangible fixed assets	842	842	842	842
Tangible fixed assets	2,573	3,080	3,526	3,995
Current assets	5,281	7,203	7,739	8,575
Cash & others	753	1,245	1,357	1,398
Total assets	9,678	12,107	13,089	14,394
Operating liabilities	2,560	3,180	3,294	3,651
Gross debt	3,579	3,956	3,155	2,089
Net debt	2,827	2,711	1,797	691
Shareholders funds	3,146	4,548	6,200	8,161
Invested capital	6,366	7,682	8,438	9,345

Ratio, growth and per share analysis

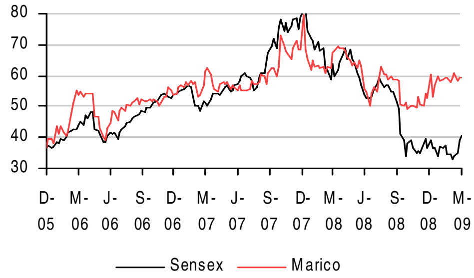
Year to	03/2008a	03/2009e	03/2010e	03/2011e
Y-o-y % change				
Revenue	22.4	25.4	12.2	16.2
EBITDA	23.9	22.6	18.0	17.8
Operating profit	47.1	23.5	18.6	17.9
PBT	36.7	11.9	24.3	23.4
HSBC EPS	58.2	28.6	9.2	18.6
Ratios (%)				
Revenue/IC (x)	3.6	3.4	3.3	3.5
ROIC	34.1	32.4	30.5	31.7
ROE	62.5	53.0	41.4	36.8
ROA	22.8	20.0	19.8	20.6
EBITDA margin	12.9	12.6	13.3	13.5
Operating profit margin	11.3	11.1	11.8	11.9
EBITDA/net interest (x)	8.1	8.5	10.0	16.0
Net debt/equity	89.8	59.6	29.0	8.5
Net debt/EBITDA (x)	1.1	0.9	0.5	0.2
Per share data (INR)				
EPS reported (fully diluted)	2.78	3.10	3.65	4.33
HSBC EPS (fully diluted)	2.60	3.34	3.65	4.33
DPS	0.66	0.68	0.80	0.95
Book value	5.17	7.47	10.18	13.40

Valuation data

Year to	03/2008a	03/2009e	03/2010e	03/2011e
EV/sales	2.3	1.8	1.6	1.3
EV/EBITDA	17.8	14.5	12.0	9.9
EV/IC	6.9	5.7	5.1	4.5
PE*	25.9	20.1	18.4	15.5
P/Book value	13.0	9.0	6.6	5.0
FCF yield (%)	-1.8	1.5	3.5	4.2
Dividend yield (%)	1.0	1.0	1.2	1.4

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Source: HSBC

Note: price at close of 22 Apr 2009

Q4 and FY09 results snapshot

Marico Industries: Q4 FY09 results analysis

(INRm)	Q4 FY09	Q4 FY08	Y-o-y %	FY09	FY08	Y-o-y %
Income from sales and services	5,612	4,659	20.5%	23,884	19,050	25.4%
COGS	2,851	2,297	24.1%	12,779	9,809	30.3%
Gross profit	2,760	2,361	16.9%	11,106	9,242	20.2%
Gross profit margin	49.2%	50.7%	-150 bps	46.5%	48.5%	-201 bps
Employee cost	427	363	17.5%	1,648	1,268	30.0%
Advertisement & sales promotion	568	705	-19.4%	2,504	2,447	2.3%
Other expenses	1,032	838	23.2%	3,934	3,064	28.4%
EBITDA	733	455	60.9%	3,020	2,462	22.6%
EBITDA margin	13.1%	9.8%	328 bps	12.6%	12.9%	-28 bps
Depreciation & amortisation	104	79	31.8%	358	307	16.4%
EBIT	629	376	67.0%	2,662	2,155	23.5%
EBIT margin	11.2%	8.1%	312 bps	11.1%	11.3%	-17 bps
Interest	113	87	29.8%	357	305	17.0%
PBT	595	341	74.5%	2,447	1,945.216	25.8%
PBT margin	10.6%	7.3%	329 bps	10.2%	10.2%	3 bps
Tax expense	1	39	-97.5%	409	360	13.8%
Effective tax rate	0.2%	11.4%	-1126 bps	16.7%	18.5%	-175 bps
Exceptional	-150	106		-150	106	
Net profit	444	408	8.9%	1,887	1,691	11.6%
Net profit margin	7.9%	8.8%	-84 bps	7.9%	8.9%	-97 bps
Basic & diluted EPS	**0.73**	**0.67**	**9.0%**	**3.1**	**2.78**	**11.5%**

Source: Company reports, HSBC

- Volume growth for Q4 slowed slightly. While Parachute growth slowed to 7% from 9% in Q3, Saffola had a small improvement but must go back into the double-digit zone for us to feel comfortable. Hair oils also slowed, to 10%. Though overall volume growth of 9% for the company was higher than 7% in Q3, we believe that the core portfolio has not improved as much.

Marico Industries: Volume growth

	Q1 FY09	Q2 FY09	Q3 FY09	Q4 FY09	FY09
Parachute	8%	12%	9%	7%	9%
Hair oils	26%	14%	15%	10%	17%
Saffola	28%	9%	3%	5%	11%
Company level	**15%**	**11%**	**7%**	**9%**	**12%**

Source: Company reports, HSBC

- Sales growth for the year at 25% was driven equally by volume and price. For the quarter, sales growth was 20.5%, of which 9ppts was contributed by volumes.

- Gross margins for the quarter declined by 150bps. While prices of commodities such as Copra, Kardi, and plastics have gone down, the impact will come following a lag, and we expect the current quarter to show an expansion. For the year, gross margins declined by 200bps, as the company was wary of passing on an equal percentage increase in prices as cost increases to protect volumes.

- Advertising costs declined 20%, partly due to a high base last year but also due to reduced advertising activity. For the full year, ad spends as a percentage of sales fell to 10.5% in FY09 from 12.8% in FY08. The company guided that this could rise back to 12% in FY10e.
- The company plans to divest itself of the Sundari business in the US and took a loss of INR150m in the consolidated P&L as the difference between the fair value and book value of the assets. However, the impact at the PAT level is negligible due to tax write-offs that are expected on this transaction.

The road ahead

We believe that FY10e will be a challenging year for Marico. On the one hand, volume growth is likely to be marginally depressed versus FY09e due to lagged impact of the recession on demand, price increases, and general inflation. On the other hand, price increases, which were heavy in FY09e, should be difficult to come by in FY10e due to reduced commodity prices. The company has taken price declines of 4% in the Saffola franchise. We believe that Marico will be able to manage sales growth of 12.2% next year, predominantly driven by volumes.

We expect a gross margin expansion of 200bps in FY10e due to reductions in prices of commodities. However, a 150bps increase in advertising spends is likely to ensure that the expansion at EBITDA level is just 70bps, we estimate. A marginal reduction in interest expenses due to reduction in debt levels is likely to help, and we expect EPS growth of 17.9% for FY10e.

Changes in our estimates

Marico Industries: Changes in HSBC forecasts

(INRm)	FY10e			FY11e		
	Old	New	Change %	Old	New	Change %
Sales	27,666	26,803	-3.1%	32,159	31,149	-3.1%
EBITDA	3,625	3,565	-1.6%	4,409	4,199	-4.8%
EBITDA margin	13.1%	13.3%	20 bps	13.7%	13.5%	-23 bps
EBIT	3,215	3,156	-1.8%	3,929	3,721	-5.3%
EBIT margin	11.6%	11.8%	15 bps	12.2%	11.9%	-27 bps
Interest	325	356	9.5%	359	262	-26.9%
PBT	2,954	2,854	-3.4%	3,644	3,521	-3.4%
PBT margin	10.7%	10.6%	-3 bps	11.3%	11.3%	-3 bps
Tax	650	628	-3.4%	911	880	-3.4%
Net income	2,303	2,225	-3.4%	2,732	2,640	-3.4%
Net income margin	8.3%	8.3%	-2 bps	8.5%	8.5%	-2 bps
EPS (INR)	3.78	3.65	-3.4%	4.48	4.33	-3.4%

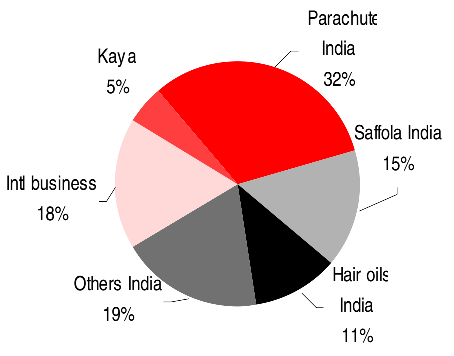
Source: HSBC

Valuation

We value Marico at 19x FY10e EPS of INR3.65, or INR69.4, which is our new target price, down from INR72. We are maintaining our multiple at 19x, because we believe that any decline in the multiple due to the decreases in our estimates of EPS growth is offset by an improvement in the multiples of the market across the board. Our multiple of 19x works out to a 15% discount to our target multiple on Hindustan Unilever. The stock has averaged a PE multiple of 20x on 12-month forward EPS for the last three years.

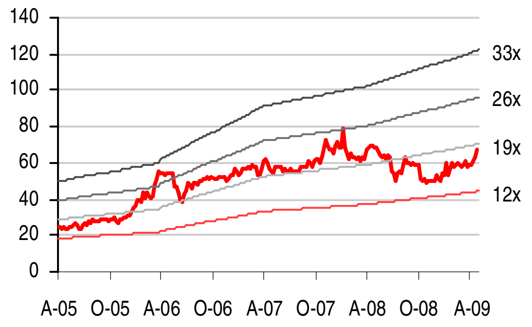
Under our research model, for stocks with a volatility indicator, the Neutral band is 10 percentage points above and below our hurdle rate for Indian stocks of 11%, or 1-21% around the current share price. Our

Marico Industries: Revenue mix, FY09e



Source: Company reports, HSBC

Marico Industries: One-year forward PE band



Source: HSBC, NSE India

new 12-month target price of INR69.4 for Marico shares represents upside potential of 3.1%, and adding this to the anticipated 1.0% dividend yield, this suggests a potential total return of 4.1%, which is within the Neutral band. Thus, we are downgrading our rating on Marico shares to Neutral (V) from Overweight (V).

Risks

Upside risks

- Volumes in the core portfolio are more than estimated.
- Commodity costs drop further and therefore gross margin expansion is higher.
- Ad spends do not reach previous levels of 12% of sales, and Marico is able exercise cost-efficiency measures.

Downside risks

- Volume growth slows more than expected due to macroeconomic factors or competition.
- Government support price for Copra has been announced higher than current market price and may put upward pressure on market prices, reducing the quantum of cost decline over the last year.
- Though Kaya recorded 57% y-o-y sales growth in FY09, it is still not profitable at PBT and continues to draw on the group's resources for its investment needs. Moreover, due to the weak economic environment, footfalls may decline, driving the business into further losses.
- The tax holiday at some production units is close to expiring, which means that Marico will bear an increased tax burden. Although a higher effective tax rate, compared with previous years, has been built into our estimates, any further increase could result in lower net profits accordingly,
- International operations are subject to risks of taxation and economic or political turmoil in other regions.

HSBC Global Research website

To maximise your access to HSBC Global Research please visit our website at www.research.hsbc.com where you can:

- View the latest research and access archived reports
- Visit the dedicated product pages, including Emerging Markets and Climate Change
- Filter estimates for more than 1,000 companies under equity coverage
- Set up personal filters to put your research interests at your fingertips
- Look up HSBC research analyst contact details

E-mail subscriptions

You can receive research directly via e-mail as soon as it is published. To set up subscriptions to research reports, contact your Relationship Manager.

If you are having problems or need assistance with the website service, please contact your HSBC Relationship Manager or e-mail: ecare@hsbcib.com.

http://www.research.hsbc.com

Disclosure appendix

Analyst certification

The following analyst(s), who is(are) primarily responsible for this report, certifies(y) that the opinion(s) on the subject security(ies) or issuer(s) and any other views or forecasts expressed herein accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Percy Panthaki

Important disclosures

Stock ratings and basis for financial analysis

HSBC believes that investors utilise various disciplines and investment horizons when making investment decisions, which depend largely on individual circumstances such as the investor's existing holdings, risk tolerance and other considerations. Given these differences, HSBC has two principal aims in its equity research: 1) to identify long-term investment opportunities based on particular themes or ideas that may affect the future earnings or cash flows of companies on a 12 month time horizon; and 2) from time to time to identify short-term investment opportunities that are derived from fundamental, quantitative, technical or event-driven techniques on a 0-3 month time horizon and which may differ from our long-term investment rating. HSBC has assigned ratings for its long-term investment opportunities as described below.

This report addresses only the long-term investment opportunities of the companies referred to in the report. As and when HSBC publishes a short-term trading idea the stocks to which these relate are identified on the website at www.hsbcnet.com/research. Details of these short-term investment opportunities can be found under the Reports section of this website.

HSBC believes an investor's decision to buy or sell a stock should depend on individual circumstances such as the investor's existing holdings and other considerations. Different securities firms use a variety of ratings terms as well as different rating systems to describe their recommendations. Investors should carefully read the definitions of the ratings used in each research report. In addition, because research reports contain more complete information concerning the analysts' views, investors should carefully read the entire research report and should not infer its contents from the rating. In any case, ratings should not be used or relied on in isolation as investment advice.

Rating definitions for long-term investment opportunities

Stock ratings

HSBC assigns ratings to its stocks in this sector on the following basis:

For each stock we set a required rate of return calculated from the risk free rate for that stock's domestic, or as appropriate, regional market and the relevant equity risk premium established by our strategy team. The price target for a stock represents the value the analyst expects the stock to reach over our performance horizon. The performance horizon is 12 months. For a stock to be classified as Overweight, the implied return must exceed the required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands are classified as Neutral.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation of coverage, change of volatility status or change in price target). Notwithstanding this, and although ratings are subject to ongoing management review, expected returns will be permitted to move outside the bands as a result of normal share price fluctuations without necessarily triggering a rating change.

*A stock will be classified as volatile if its historical volatility has exceeded 40%, if the stock has been listed for less than 12 months (unless it is in an industry or sector where volatility is low) or if the analyst expects significant volatility. However, stocks which we do not consider volatile may in fact also behave in such a way. Historical volatility is defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility has to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Prior to this, from 7 June 2005 HSBC applied a ratings structure which ranked the stocks according to their notional target price vs current market price and then categorised (approximately) the top 40% as Overweight, the next 40% as Neutral and the last 20% as Underweight. The performance horizon is 2 years. The notional target price was defined as the mid-point of the analysts' valuation for a stock.

From 15 November 2004 to 7 June 2005, HSBC carried no ratings and concentrated on long-term thematic reports which identified themes and trends in industries, but did not make a conclusion as to the investment action that potential investors should take.

Prior to 15 November 2004, HSBC's ratings system was based upon a two-stage recommendation structure: a combination of the analysts' view on the stock relative to its sector and the sector call relative to the market, together giving a view on the stock relative to the market. The sector call was the responsibility of the strategy team, set in co-operation with the analysts. For other companies, HSBC showed a recommendation relative to the market. The performance horizon was 6-12 months. The target price was the level the stock should have traded at if the market accepted the analysts' view of the stock.

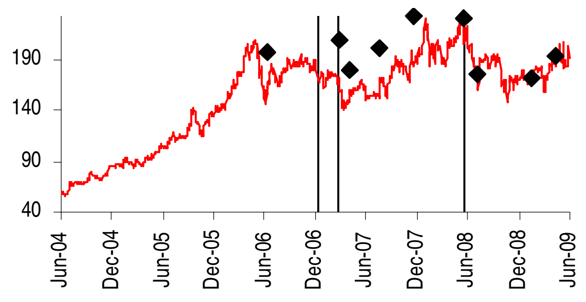
Rating distribution for long-term investment opportunities

As of 08 June 2009, the distribution of all ratings published is as follows:

Overweight (Buy)	34%	(33% of these provided with Investment Banking Services)
Neutral (Hold)	39%	(32% of these provided with Investment Banking Services)
Underweight (Sell)	27%	(28% of these provided with Investment Banking Services)

Share price and rating changes for long-term investment opportunities

ITC (ITC.BO) Share Price performance INR Vs HSBC rating history



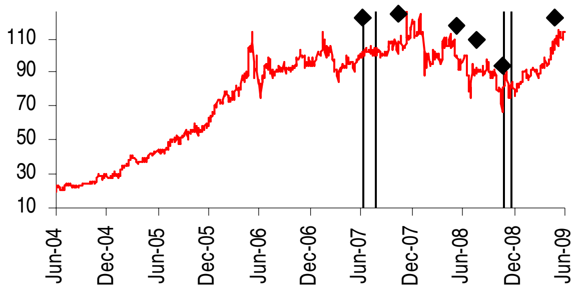
Source: HSBC

Recommendation & price target history

From	To	Date
Overweight	Neutral	19 December 2006
Neutral	Overweight	01 March 2007
Overweight	Neutral	23 May 2008
Target Price	**Value**	**Date**
Price 1	197.00	19 June 2006
Price 2	210.00	01 March 2007
Price 3	180.00	09 April 2007
Price 4	201.00	27 July 2007
Price 5	233.00	26 November 2007
Price 6	231.00	23 May 2008
Price 7	175.00	16 July 2008
Price 8	172.00	20 January 2009
Price 9	193.00	17 April 2009

Source: HSBC

Dabur India (DABU.BO) Share Price performance INR Vs HSBC rating history



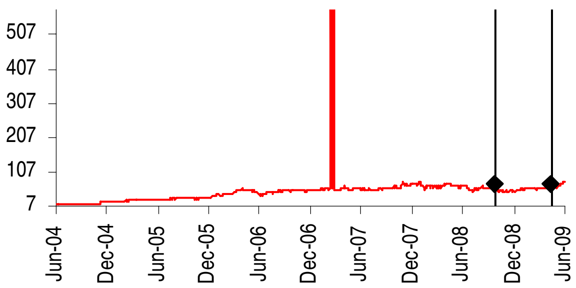
Source: HSBC

Recommendation & price target history

From	To	Date
N/A	Overweight (V)	15 June 2007
Overweight (V)	Overweight	24 July 2007
Overweight	Neutral (V)	31 October 2008
Neutral (V)	Overweight (V)	24 November 2008
Target Price	**Value**	**Date**
Price 1	123.00	15 June 2007
Price 2	125.00	24 October 2007
Price 3	118.00	16 May 2008
Price 4	110.00	29 July 2008
Price 5	94.50	31 October 2008
Price 6	123.00	30 April 2009

Source: HSBC

Marico Industries (MRCO.BO) Share Price performance INR Vs HSBC rating history



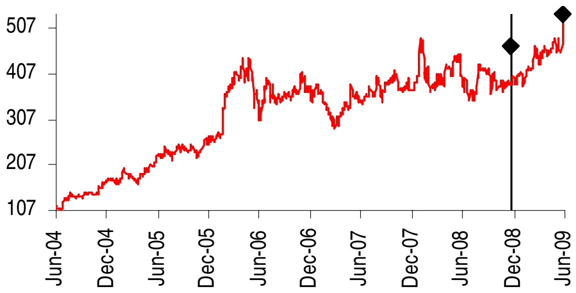
Source: HSBC

Recommendation & price target history

From	To	Date
N/R	Overweight (V)	30 September 2008
Overweight (V)	Neutral (V)	22 April 2009
Target Price	**Value**	**Date**
Price 1	72.00	30 September 2008
Price 2	69.40	22 April 2009

Source: HSBC

Colgate-Palmolive (COLG.BO) Share Price performance INR Vs HSBC rating history



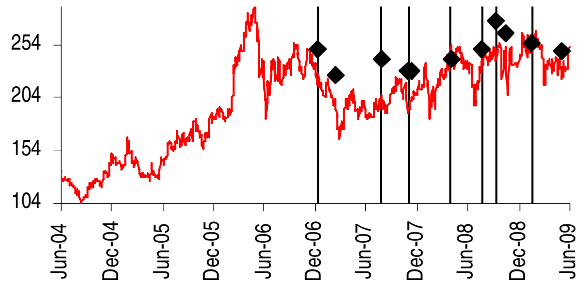
Source: HSBC

Recommendation & price target history

From	To	Date
N/R	Overweight	26 November 2008
Target Price	**Value**	**Date**
Price 1	470.00	26 November 2008
Price 2	540.00	29 May 2009

Source: HSBC

Hindustan Unilever Ltd (HLL.BO) Share Price performance INR Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
Overweight	Neutral	18 December 2006
Neutral	Overweight	30 July 2007
Overweight	Neutral	02 November 2007
Neutral	Underweight	07 April 2008
Underweight	Neutral	28 July 2008
Neutral	Overweight	15 September 2008
Overweight	Neutral	26 January 2009
Target Price	**Value**	**Date**
Price 1	250.61	18 December 2006
Price 2	225.02	21 February 2007
Price 3	241.00	30 July 2007
Price 4	230.00	02 November 2007
Price 5	230.00	21 November 2007
Price 6	241.00	07 April 2008
Price 7	251.00	28 July 2008
Price 8	277.00	15 September 2008
Price 9	266.00	24 October 2008
Price 10	255.00	26 January 2009
Price 11	249.00	11 May 2009

Source: HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
COLGATE-PALMOLIVE	COLG.NS	529.30	05-Jun-2009	2, 4, 5, 6, 7
HINDUSTAN UNILEVER LTD	HLL.NS	252.00	05-Jun-2009	1, 4, 5
ITC	ITC.BO	191.35	05-Jun-2009	6

Source: HSBC

1 HSBC* has managed or co-managed a public offering of securities for this company within the past 12 months.
2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.
3 At the time of publication of this report, HSBC Securities (USA) Inc. is a Market Maker in securities issued by this company.
4 As of 30 April 2009 HSBC beneficially owned 1% or more of a class of common equity securities of this company.
5 As of 30 April 2009, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of investment banking services.
6 As of 30 April 2009, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-investment banking-securities related services.
7 As of 30 April 2009, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-securities services.
8 A covering analyst/s has received compensation from this company in the past 12 months.
9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.
10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.
11 At the time of publication of this report, HSBC is a non-US Market Maker in securities issued by this company and/or in securities in respect of this company

Analysts are paid in part by reference to the profitability of HSBC which includes investment banking revenues.

For disclosures in respect of any company, please see the most recently published report on that company available at www.hsbcnet.com/research.

** HSBC Legal Entities are listed in the Disclaimer below.*

Additional disclosures

1 This report is dated as at 08 June 2009.
2 All market data included in this report are dated as at close 03 June 2009, unless otherwise indicated in the report.
3 HSBC has procedures in place to identify and manage any potential conflicts of interest that arise in connection with its Research business. HSBC's analysts and its other staff who are involved in the preparation and dissemination of Research operate and have a management reporting line independent of HSBC's Investment Banking business. Chinese Wall procedures are in place between the Investment Banking and Research businesses to ensure that any confidential and/or price sensitive information is handled in an appropriate manner.
4 As of 30 April 2009, HSBC beneficially owned 2% or more of a class of common equity securities of the following company(ies) : HINDUSTAN UNILEVER LTD
5 As of 30 April 2009, HSBC and/or its affiliates (including the funds, portfolios and investment clubs in securities managed by such entities) either, directly or indirectly, own or are involved in the acquisition, sale or intermediation of, 1% or more of the total capital of the subject companies securities in the market for the following Company(ies) : HINDUSTAN UNILEVER LTD

Disclaimer

** Legal entities as at 22 October 2008*
'UAE' HSBC Bank Middle East Limited, Dubai; 'HK' The Hongkong and Shanghai Banking Corporation Limited, Hong Kong; 'TW' HSBC Securities (Taiwan) Corporation Limited; 'CA' HSBC Securities (Canada) Inc, Toronto; HSBC Bank, Paris branch; HSBC France; 'DE' HSBC Trinkaus & Burkhardt AG, Dusseldorf; 000 HSBC Bank (RR), Moscow; 'IN' HSBC Securities and Capital Markets (India) Private Limited, Mumbai; 'JP' HSBC Securities (Japan) Limited, Tokyo; 'EG' HSBC Securities Egypt S.A.E., Cairo; 'CN' HSBC Investment Bank Asia Limited, Beijing Representative Office; The Hongkong and Shanghai Banking Corporation Limited, Singapore branch; The Hongkong and Shanghai Banking Corporation Limited, Seoul Securities Branch; HSBC Securities (South Africa) (Pty) Ltd, Johannesburg; 'GR' HSBC Pantelakis Securities S.A., Athens; HSBC Bank plc, London, Madrid, Milan, Stockholm, Tel Aviv, 'US' HSBC Securities (USA) Inc, New York; HSBC Yatirim Menkul Degerler A.S., Istanbul; HSBC México, S.A., Institución de Banca Múltiple, Grupo Financiero HSBC, HSBC Bank Brasil S.A. - Banco Múltiplo, HSBC Bank Australia Limited, HSBC Bank Argentina S.A., HSBC Saudi Arabia Limited.

Issuer of report
HSBC Securities and Capital Markets (India) Private Limited
Registered Office
52/60 Mahatma Gandhi Road
Fort, Mumbai 400 001, India
Telephone: +91 22 2267 4921
Fax: +91 22 2263 1983
Website: www.research.hsbc.com

This document has been issued by HSBC Securities and Capital Markets (India) Private Limited ("HSBC") for the information of its customers only. HSBC Securities and Capital Markets (India) Private Limited is regulated by the Securities and Exchange Board of India. If it is received by a customer of an affiliate of HSBC, its provision to the recipient is subject to the terms of business in place between the recipient and such affiliate. This document is not and should not be construed as an offer to sell or the solicitation of an offer to purchase or subscribe for any investment. HSBC has based this document on information obtained from sources it believes to be reliable but which it has not independently verified; HSBC makes no guarantee, representation or warranty and accepts no responsibility or liability as to its accuracy or completeness. Expressions of opinion are those of the Research Division of HSBC only and are subject to change without notice. HSBC and its affiliates and/or their officers, directors and employees may have positions in any securities mentioned in this document (or in any related investment) and may from time to time add to or dispose of any such securities (or investment). HSBC and its affiliates may act as market maker or have assumed an underwriting commitment in the securities of companies discussed in this document (or in related investments), may sell them to or buy them from customers on a principal basis and may also perform or seek to perform investment banking or underwriting services for or relating to those companies and may also be represented in the supervisory board or any other committee of those companies. The information and opinions contained within the research reports are based upon publicly available information and rates of taxation applicable at the time of publication which are subject to change from time to time. Past performance is not necessarily a guide to future performance. The value of any investment or income may go down as well as up and you may not get back the full amount invested. Where an investment is denominated in a currency other than the local currency of the recipient of the research report, changes in the exchange rates may have an adverse effect on the value, price or income of that investment. In case of investments for which there is no recognised market it may be difficult for investors to sell their investments or to obtain reliable information about its value or the extent of the risk to which it is exposed.

HSBC Securities (USA) Inc. accepts responsibility for the content of this research report prepared by its non-US foreign affiliate. All U.S. persons receiving and/or accessing this report and wishing to effect transactions in any security discussed herein should do so with HSBC Securities (USA) Inc. in the United States and not with its non-US foreign affiliate, the issuer of this report.

In the UK this report may only be distributed to persons of a kind described in Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001. The protections afforded by the UK regulatory regime are available only to those dealing with a representative of HSBC Bank plc in the UK. In Singapore, this publication is distributed by The Hongkong and Shanghai Banking Corporation Limited, Singapore Branch for the general information of institutional investors or other persons specified in Sections 274 and 304 of the Securities and Futures Act (Chapter 289) (“SFA”) and accredited investors and other persons in accordance with the conditions specified in Sections 275 and 305 of the SFA. This publication is not a prospectus as defined in the SFA. It may not be further distributed in whole or in part for any purpose. The Hongkong and Shanghai Banking Corporation Limited Singapore Branch is regulated by the Monetary Authority of Singapore. In Australia, this publication has been distributed by The Hongkong and Shanghai Banking Corporation Limited (ABN 65 117 925 970, AFSL 301737) for the general information of its “wholesale” customers (as defined in the Corporations Act 2001). Where distributed to retail customers, this research is distributed by HSBC Bank Australia Limited (AFSL No. 232595). These respective entities make no representations that the products or services mentioned in this document are available to persons in Australia or are necessarily suitable for any particular person or appropriate in accordance with local law. No consideration has been given to the particular investment objectives, financial situation or particular needs of any recipient.

In Japan, this publication has been distributed by HSBC Securities (Japan) Limited. In Hong Kong, this document has been distributed by The Hongkong and Shanghai Banking Corporation Limited in the conduct of its Hong Kong regulated business for the information of its institutional and professional customers; it is not intended for and should not be distributed to retail customers in Hong Kong. The Hongkong and Shanghai Banking Corporation Limited makes no representations that the products or services mentioned in this document are available to persons in Hong Kong or are necessarily suitable for any particular person or appropriate in accordance with local law. All inquiries by such recipients must be directed to The Hongkong and Shanghai Banking Corporation Limited.

Indian Research Team

India

Automobiles
Sachin Gupta
Analyst
+91 22 2268 1079 sachin1gupta@hsbc.co.in

Banks
Saumya Agarwal
Analyst
+91 22 2268 1235 saumyaagarwal@hsbc.co.in

Construction Materials, Metals & Mining
Jatin Kotian
Analyst
+91 22 2268 1638 jatinkotian@hsbc.co.in

Consumer & Retail
Percy Panthaki
Analyst
+91 22 2268 1240 percypanthaki@hsbc.co.in

Electric Utilities, Machinery, Transport Infrastructure
Sumeet Agrawal
Analyst
+91 22 2268 1243 sumeetagrawal@hsbc.co.in

Infrastructure, Real Estate
Ashutosh Narkar
Analyst
+91 22 2268 1474 ashutoshnarkar@hsbc.co.in

IT Services
Yogesh Aggarwal
Analyst
+91 22 2268 1246 yogeshaggarwal@hsbc.co.in

Oil & Gas
Kirtan Mehta, CFA
Analyst
+91 80 3001 3779 kirtanmehta@hsbc.co.in

Small & Mid-cap
Sandeep Somani
Analyst
+91 22 2268 1245 sandeepsomani@hsbc.co.in

Telecom
Rajiv Sharma
Analyst
+91 22 2268 1239 rajivsharma@hsbc.co.in

Strategy
Vivek R Misra
Strategist
+91 80 3001 3699 vivekmisra@hsbc.co.in

Singapore

Economics
Robert Prior-Wandesforde
Economist
+65 6239 0840 robert.prior-wandesforde@hsbc.com.sg

Hong Kong

Strategy
Garry Evans
Head of Pan-Asian Equity Strategy
+852 2996 6916 garryevans@hsbc.com.hk

Airlines
Mark Webb
Analyst
+852 2996 6574 markwebb@hsbc.com.hk

Banks
Todd Dunivant
Analyst
+852 2996 6599 tdunivant@hsbc.com.hk

Telecom
Tucker Grinnan
Analyst
+852 2822 4686 tuckergrinnan@hsbc.com.hk