RESULTS REVIEW

Share Data

Market Cap	Rs. 784.4 bn
Price	Rs. 208.3
BSE Sensex	15,587.62
Reuters	ITC.BO
Bloomberg	ITC IN
Avg. Volume (52 Week)	1.3 mn
52-Week High/Low	Rs. 239.40 / 148.50
Shares Outstanding	3,765.8 mn

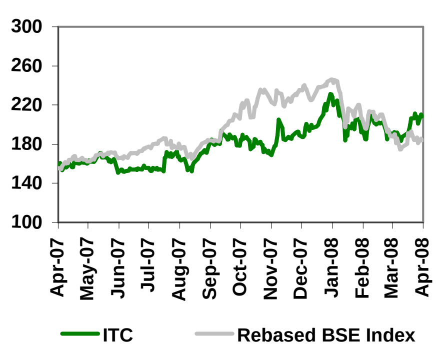
Valuation Ratios (Consolidated)

Year to 31 March	2008E	2009E
EPS (Rs.)	8.6	10.2
+/- (%)	16.7%	19.7%
PER (x)	24.4x	20.3x
EV/ Sales (x)	5.7x	4.7x
EV/ EBITDA (x)	17.4x	14.7x

Shareholding Pattern (%)

Promoters	0
FIIs	14
Institutions	38
Public & Others	48

Relative Performance



ITC Limited — Hold

Ban on export affected Agri business

ITC Limited reported a double digit growth of 11% yoy in net sales for Q3'08 to Rs. 34.6 bn with a strong growth of 50% yoy in the non-cigarette FMCG business coupled with a healthy increase in revenues from Hotels and Paperboard & Packaging business. The growth in the Non-Cigarette businesses mitigated the subdued growth of the Company's Cigarette business. The Cigarette business continued to suffer the full impact of VAT imposition by most states, applicable CST and trade taxes in the state of U.P along with the increase in excise duties on cigarettes in excess of 6%. The Company's Agri Business declined 9.4% yoy owing to the restrictions on the export of non-basmati rice. EBITDA for Q3'08 improved 10.8% yoy to Rs. 12 bn; however, the margin remained relatively flat at 34.7%. Net profit margin improved 100 bps yoy to 24%.

We believe that ITC's future prospects would continue to revolve around the success of the non-cigarette FMCG business. The Company is aggressively launching new products to sustain its leading edge in the highly competitive FMCG industry. We are optimistic on account of the Company's diversified business model and extensive management.

Taking into consideration, the muted volume growth in the Cigarette business and weak performance of the Agri business during the quarter, we downgrade our net sales estimate by 2% each for FY08E and FY09E. Similarly, we have calibrated our EBITDA estimate downward by 3% and 6% for FY08E and FY09E, respectively. At the current price of Rs. 208.3, the stock is trading at a forward PE of 24.4x and 20.3x for FY08E and FY09E, respectively. We feel that there is limited upside potential from the current levels and reiterate our Hold rating on the stock.

Key Figures (Standalone)

Quarterly Data	Q3'07	Q2'08	Q3'08	YoY%	QoQ%	9M'07	9M'08	YoY%
(Figures in Rs. mn, except per share data)								
Net Sales	31,147	32,734	34,580	11.0%	5.6%	88,001	100,252	13.9%
EBITDA	10,828	10,320	11,997	10.8%	16.3%	30,261	33,593	11.0%
Net Profit	7,174	7,709	8,307	15.8%	7.8%	20,493	23,845	16.4%
Margins(%)								
EBITDA	34.8%	31.5%	34.7%			34.4%	33.5%	
NPM	23.0%	23.5%	24.0%			23.3%	23.8%	
Per Share Data (Rs.)								
Normalised EPS	1.9	2.0	2.2	15.8%	7.8%	5.4	6.3	16.4%

Result Highlights

Net sales for the third quarter went up by 11% yoy despite subdued performance by the cigarette business (which contributes around 44% to sales) and subdued performance by the agri business (which contributes around 17.2% to sales). The growth was driven by a robust 50% yoy jump in the non-cigarette FMCG business and healthy performance by Hotels (10.3% yoy) and Paperboard & Packaging business (11.6% yoy). EBITDA for the quarter improved 10.8% yoy to Rs. 12 bn while EBITDA margin remained comparatively flat at 34.7%. Net profit grew 15.8% yoy to Rs. 8.3 bn, attributable to 96.9% yoy rise in other income. However, net profit margin improved by a considerable 100 bps yoy to 24%.

Segmental Highlights

'Cigarette' business registered an increase of 11.4% yoy to Rs. 16.9 bn despite muted volumes during the quarter owing to a substantial rise in taxes on cigarettes in the current fiscal. The increase in cigarette business was primarily driven by the various price hikes undertaken by the Company. The additional burden of indirect taxes during the quarter aggregated to Rs. 5.1 bn, consequent to the staggering increase in taxes of 29% per pack over the corresponding period last year. EBIT for the cigarette business increased 16% yoy to Rs. 9.6 bn and EBIT margin jumped by a steep 230 bps yoy to 56.8%. High rates of taxation at nearly 132% of the value of the product (ex factory price) will drive consumers to switch to cheaper and inferior forms of tobacco. Moreover, the proposed statutory requirement for pictorial health warnings on tobacco packs might hamper the short term demand scenario.

U.P under VAT regime with effect from 1st Jan, 2008

'FMCG Others' recorded a strong growth of 50% yoy to Rs. 6.5 bn with an increase in revenue contribution by 4.3 pts to 17% of net sales. The segment witnessed strong growth led by 60% yoy improvement in the Branded Packaged Foods (Biscuits – 58%, Aashirvaad Atta – 39%, Ready to eat food – 63% and Confectionery category – 38%), 39% yoy in Stationery business and 26% yoy in Lifestyle Retailing. 'Bingo', a range of salty snacks, has emerged as a major brand within barely three quarters of its launch. Further, the recent launch of Aashirvaad MP Chakki Atta has

Strong performance by Non-Cigarette FMCG business

received excellent response and is being extended to the target markets. During the quarter, the Sunfeast range of buiscuits was further enhanced with launch of 'Coconut' and 'Nice' variants and the addition of 'Sunfeast BenneVita Flaxseed' biscuits. With these constant new launches and rising sales of higher value variants like Creams, Crackers and Cookies, we expect the product mix to improve further.

New pulp mill is expected to ease margin pressure

'Paperboard, Speciality Paper & Packaging' business posted healthy growth with segment revenues improving by 11.6% yoy to Rs. 5.5 bn. The performance was driven by a 14% increment in volumes of the Value Added Portfolio of paper and paperboards as well as the strong performance of the packaging business. EBIT for the quarter grew 13.6% yoy to Rs. 1.2 bn and EBIT margin rose by 40 bps yoy to 21.4%. The new pulp mill project is nearing completion and is slated for commissioning in the last quarter of FY08E. The pulp mill with a capacity of 120,000 tons of hardwood pulp will provide a distinct cost advantage, apart from removing the dependency on imported hardwood pulp.

ITC plans a five star hotel in Mauritius with an investment of around Rs. 2 bn

The ***'Hotels'*** business grew 10% yoy to Rs. 2.9 bn and 16.3% yoy increase in EBIT to Rs. 1.4 bn, driven by improved REVPAR (revenue per available room) and superior food & beverage performance. The renovation of the premium Towers Block at Maurya – New Delhi was successfully completed during the quarter. Moreover, the Company also completed product upgradation and renovation at three other hotels consistent with the premium positioning of the chain. ITC Welcom Group is planning to invest around Rs. 40 bn till 2010 to set up luxury offerings in Goa, Hyderabad, Ahmadabad, Kerala and Bangalore. This investment is in addition to the group's previously announced projects that include the Rs. 10 bn Grand Chola in Chennai and the Rs. 4 bn ITC Gardenia in Bangalore. With massive expansion plans and building additional room capacity, we believe that Hotels business would put a strong show FY10E onwards.

Restriction on export of non-basmati rice impacted Agri business

Though the ***'Agri Business'*** segment revenues declined 9.4% yoy primarily due to restrictions on the export of non-basmati rice, the business posted robust gain in profits riding on record exports of leaf tobacco. EBIT for the ‘Agri Business’ grew 28.1% yoy and the EBIT margin improved by a steep 120 bps yoy to 4.2%. The cigarette leaf tobacco exports grew by 37% yoy during the quarter. To offset the impact of the appreciating rupee, the Company has successfully re-negotiated pricing of the export orders. ITC is heading a pilot project for retailing fresh fruits and vegetables through Choupal Fresh Cash & Carry Stores and six Choupal Fresh retail stores. The Company has set up a comprehensive supply chain for ensuring the availability of fresh products in the market, besides establishing direct linkages with the farmers.

Key Events

Extension of ‘Fiama Di Wills’ range

- Following the successful launch of Fiama Di Wills Shampoos and Shower Gels, ITC has recently launched Fiama Di Wills Soaps and Fiama Di Wills Polishing Drops to further enhance the personal care portfolio.
- The Company issued and alloted 18,95,110 ordinary shares of Re. 1/- each under the ITC Employee Stock option Scheme.
- New product launches during the quarter are:
  Sunfeast – Coconut and Nice variant buiscuits
  Sunfeast BenneVita Flaxseed biscuits
  Aashirvaad MP Chakki Atta
  Spectra -Paper cups

Key Risks

Key risks to our rating include:

- The requirement of pictorial health warnings on tobacco products might further hamper the declining volumes in the cigarette industry.
- Any further imposition or relaxation of taxes on cigarettes might pose a serious risk to our rating.

Outlook

With non-cigarette FMCG business posting robust growth for the past three quarters of FY08E, we believe ITC’s growth story will progress with the success of this business. To further extend the product range and fight the cut-throat competition in the FMCG industry, the Company is aggressively

ITC playing safe with well diversified business model

launching new products. ITC's cigarette segment continues to register a growth in revenues despite 20% price hike and the sharp rise in taxes. The implementation of VAT in U.P with effect from 1st January, 2008 and the concurrent withdrawal of trade tax in the state is a welcome development. However, we believe that if the pictorial health warning on the cigarette pack becomes mandatory, then volumes in the cigarette business is likely to suffer a setback in the short run. Further, excise duty on non-filter cigarettes, which do not exceed 60 mm in length, was increased nearly five times to 82 paise per stick from the earlier 17 paise per stick in the budget for 2008-09. The impact of the excise duty hike will be marginal on ITC, as only 20 per cent of the Company's cigarette sales are generated from non-filter cigarettes.

While the agri business revenue for the quarter declined, the business posted robust gain in profits riding on record exports of leaf tobacco. With completion of renovation at various hotels and reduction of dependency on imported hardwood pulp, we expect Hotels and Paperboard & Packaging business to report healthy numbers in the forthcoming period. Hence, we maintain our positive outlook on the Company on account of its diversified business model and increasing contribution from the non-cigarette FMCG business.

We expect ITC's net sales to grow at a CAGR of 13.2% to Rs. 135.6 bn and Rs. 165 bn in FY08E and FY09E, respectively. Net profit is expected to grow at a CAGR of 18.3% to Rs. 38.7 bn in FY09E. We feel that there is limited upside potential from the current levels and reiterate our Hold rating on the stock.

Key Figures (Consolidated)

Year to March	FY05	FY06	FY07	FY08E	FY09E	CAGR (%)
(Figures in Rs mn, except per share data)						(FY07-09E)
Net Sales	80,578	103,176	128,737	135,599	165,000	13.2%
EBITDA	29,026	34,522	41,076	44,680	52,800	13.4%
Net Profit	18,979	23,506	27,633	32,298	38,675	18.3%
Margins(%)						
EBITDA	36.0%	33.5%	31.9%	33.0%	32.0%	
NPM	23.6%	22.8%	21.5%	23.8%	23.4%	
Per Share Data (Rs.)						
Adj EPS	5.1	6.2	7.3	8.6	10.2	18.2%
PER (x)	28.0x	28.2x	28.7x	24.4x	20.3x	

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