



Hindustan Unilever

STOCK INFO.	BLOOMBERG
BSE Sensex: 17,016	HUVR IN
	REUTERS CODE
S&P CNX: 5,090	HLL.BO

28 April 2008

Neutral

Previous Recommendation: Neutral

Rs247

		YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
		END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
Equity Shares (m)	2,177.5	12/06A	121,034	15,397	7.0	17.5	35.4	20.0	56.5	67.0	4.3	31.4
52-Week Range	256/170	12/07A	137,178	17,691	8.1	14.9	30.4	37.4	122.9	144.7	3.8	27.7
1,6,12 Rel. Perf. (%)	-2/25/-5	12/08E	160,277	20,456	9.4	15.6	26.3	29.8	113.4	135.4	3.2	22.9
M.Cap. (Rs b)	538.5	12/09E	180,442	23,907	11.0	16.9	22.5	23.8	105.8	127.2	2.8	19.4
M.Cap. (US\$ b)	13.5											

- 1QCY08 sales at Rs37.9b up 19.1% YoY was higher than our estimate of Rs36.2b while adj. PAT stood at Rs3.78b v/s estimate of Rs3.8b. Volume growth at 10.2% is the highest in recent times. Gross margins increased 80bp to 48.3% due to margin expansion in Soaps and Detergents and strong growth in Personal Care (23% YoY).
- EBIDTA margin declined 60bp YoY to 10.7% (est. 40bp increase) due to 22% increase in adspend, 19.5% increase in staff costs and 27.7% increase in overheads. EBIDTA grew 12.7%, lower than our estimate of 18.2% growth.
- Personal Care reported 23.5% sales growth v/s just 7.3% in 1QCY07 and 19.1% in 4QCY07 aided by strong growth in skin creams due to the prolonged winter. Soaps and Detergents grew 19.9% in sales and 34% in PBIT as margins expanded 250bp. Food portfolio reported sedate performance with 14% increase in sales and 24% decline in PBIT.
- We have been positively surprised by the strong volume growth. Although a part of it can be attributed to new businesses like Pure IT and the low base effect in Personal Care, high double digit sales growth in Soaps and Detergents is very positive. Food business has displayed severe margin pressure and we expect the same to sustain in the coming quarters. We expect increased spend on advertising and overheads due to launch of new businesses.
- We are increasing our estimate of other income from Rs4.04b to Rs4.64b due to 55% increase in operational other income during 1QCY08. We are increasing sales growth estimates for CY08 and CY09 to 16.8% (v/s 13.7%) and 12.6% (v/s 11.5%). We expect 30bp margin expansion in CY08 and 50bp in CY09 v/s earlier estimates of 70bp and 40bp respectively. We are increasing CY08 and CY09 EPS estimates to Rs9.4 and Rs11 from earlier levels of Rs 9.3 and Rs10.7 respectively. The stock trades at 26.3x CY08E and 22.5x CY09E with EPS CAGR of 16%.

QUARTERLY PERFORMANCE											(Rs Million)
Y/E DECEMBER	CY07				CY08				CY07	CY08E	
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			
Net Sales (incl service inc)	31,843	34,814	33,646	36,874	37,939	40,250	39,500	42,587	137,178	160,277	
YoY Change (%)	13.8	12.9	9.7	16.8	19.1	15.6	17.4	15.5	13.3	16.8	
Total Expenditure	28,224	29,695	29,170	31,232	33,861	34,092	34,010	35,805	118,321	137,767	
EBITDA	3,620	5,120	4,476	5,642	4,078	6,158	5,491	6,783	18,857	22,510	
YoY Change (%)	9.5	23.5	11.1	12.8	12.7	20.3	22.7	20.2	14.4	19.4	
Margins (%)	11.4	14.7	13.3	15.3	10.7	15.3	13.9	15.9	13.7	14.0	
Depreciation	329	333	353	369	363	353	362	356	1,384	1,434	
Interest	51	110	68	26	35	75	55	35	255	200	
Other Income	908	1,063	1,059	1,597	1,009	950	900	1,485	4,627	4,344	
PBT	4,147	5,739	5,114	6,844	4,689	6,680	5,974	7,877	21,845	25,220	
Tax	809	1,020	1,021	1,305	905	1,202	1,165	1,492	4,155	4,764	
Rate (%)	19.5	17.8	20.0	19.1	19.0	18.0	19.5	18.9	19.0	18.9	
Adjusted PAT	3,339	4,719	4,093	5,540	3,784	5,478	4,809	6,385	17,691	20,456	
YoY Change (%)	13.6	24.4	6.9	14.6	13.3	16.1	17.5	15.3	14.9	15.6	
Extraordinary Inc/(Exp)	590	212	-12	775	25	0	0	0	1,564	25	
Reported Profit	3,929	4,931	4,081	6,314	3,810	5,478	4,809	6,385	19,255	20,481	
YoY Change (%)	-11.3	29.6	-21.6	23.5	-3.0	11.1	17.8	1.1	3.8	6.4	

E: MOST Estimates

SEGMENTAL PERFORMANCE

	1QCY08	1QCY07	CHG %	CY07	CY06	CHG. %
Net Sales (Rs m)						
Soaps and Detergents	17,382	14,499	19.9	63,745	55,959	13.9
Personal Products	10,189	8,252	23.5	36,718	33,598	9.3
Beverages	4,310	3,721	15.8	15,328	13,307	15.2
Processed Foods	1,520	1,316	15.5	5,377	3,849	39.7
Ice Creams	370	324	14.1	1,606	1,371	17.2
Exports	3,989	3,533	12.9	13,423	12,789	5
Others	755	510	48.1	2,853	1,802	58.3
EBIT (Rs M)						
Soaps and Detergents	2,325	1,731	34.3	9,967	7,380	35.1
Personal Products	2,517	2,018	24.7	10,362	9,234	12.2
Beverages	498	551	-9.5	2,316	2,085	11.1
Processed Foods	17	73	-76.2	187	98	92
Ice Creams	-29	12	-337.7	137	176	-22.5
Exports	177	132	33.9	474	633	-25.2
Others	-305	-163	87.5	-1,127	-676	66.8
EBIT Margin (%)						
Soaps and Detergents	13.4	11.9		15.6	13.2	
Personal Products	24.7	24.5		28.2	27.5	
Beverages	11.6	14.8		15.1	15.7	
Processed Foods	1.1	5.5		3.5	2.5	
Ice Creams	-7.8	3.8		8.5	12.8	
Exports	4.4	3.7		3.5	4.9	
Others	-40.4	-31.9		-39.5	-37.5	

Source: Company/Motilal Oswal Securities

Strong volume growth backed by growth in key segments

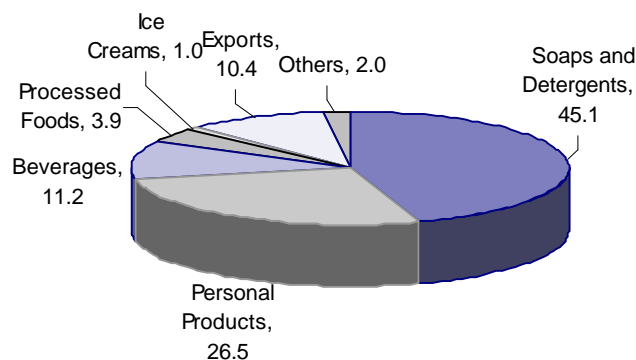
HUL's 1QCY07 topline growth at 19% was above our expectations although operational PAT growth at 13.3% was marginally lower than our estimate. Higher growth in sales was on account of strong growth witnessed in key segments namely Personal Care and Soaps & Detergents. Volume growth for the company was 10.2% — the highest volume growth in recent times.

Highest revenue growth in recent times

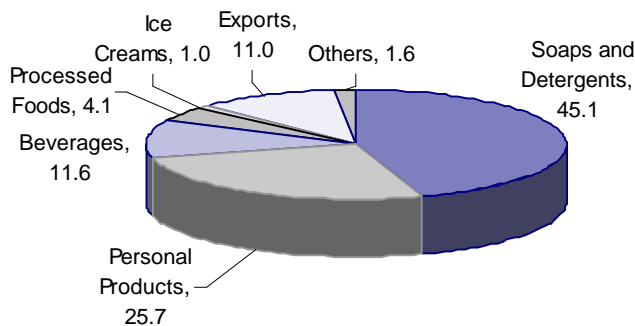
Personal Care reported 23.5% sales growth v/s just 7.3% in 1QCY07 and 19.1% in 4QCY07. High growth during the current quarter was on account of strong growth in skin creams due to the prolonged winter season. All its premium skin care products posted strong growth with Dove, Fair & Lovely and high-end Ponds gaining ground.

Soaps and Detergents maintained its momentum with 19.9% increase in revenue. Strong growth in the high-penetration

PRODUCT MIX - 1QCY08 (%)



PRODUCT MIX - 1QCY07 (%)



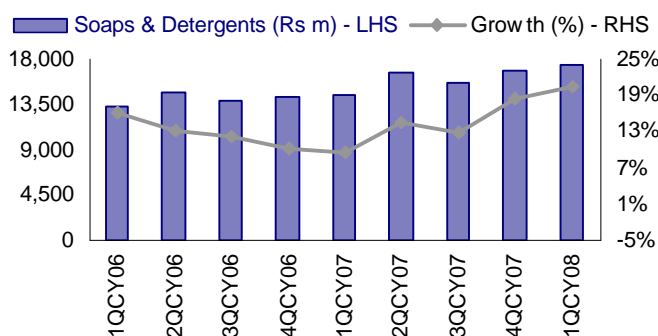
Source: Company/Motilal Oswal Securities

Soaps and Detergents segment has positively surprised us. The company maintained its 54.3% share in Toilet Soaps. We estimate low single-digit volume growth in Soaps and close to double-digit volume growth in Detergents ahead. Increase in margins in this segment indicates the success of the company in passing on the cost increase to the consumers particularly as the prices of key inputs like Palm Oil, Soda Ash and LAB have been ruling high. Lifebuoy led the soap sales growth while detergents growth is broad based with Surf Excel, Rin and Wheel growing in tandem.

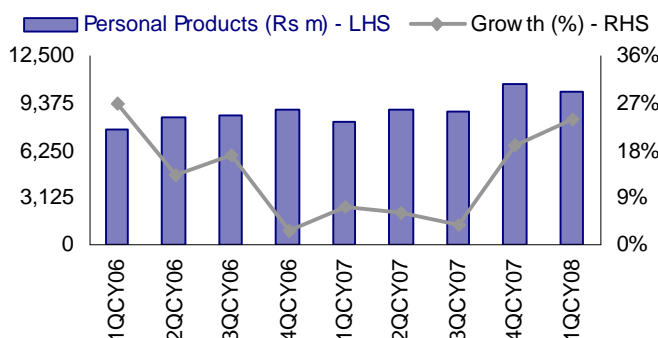
Food Products reported all-round sedate performance with 14% increase in sales and 24% decline in PBIT. Beverages reported 15.5% increase in sales and 9.5% decline in PBIT. Both tea and coffee reported strong growth. Processed Food reported 15.5% increase in sales but 76% decline in PBIT. Ice creams reported 14% sales growth with EBIDTA losses of Rs29m versus a profit of Rs12m last year.

Other businesses reported 48% increase in sales to Rs755m while losses jumped 87% to 305m, which appears to be due to expenses associated with the national rollout of Pure IT. Pure IT has been extended to 19 states and 170 cities during the quarter.

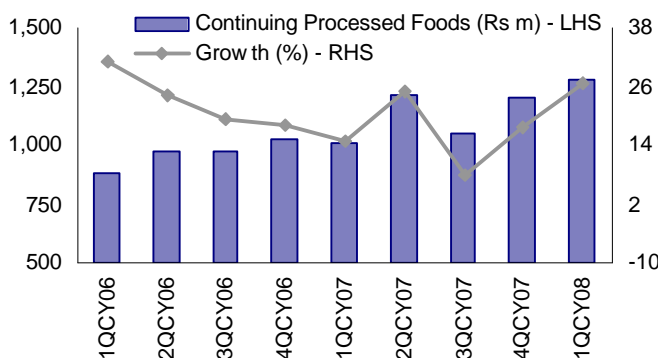
SOAP & DETERGENT - RISING GROWTH



TURNAROUND IN PERSONAL PRODUCTS PERFORMANCE



STEADY GROWTH IN PROCESSED FOODS



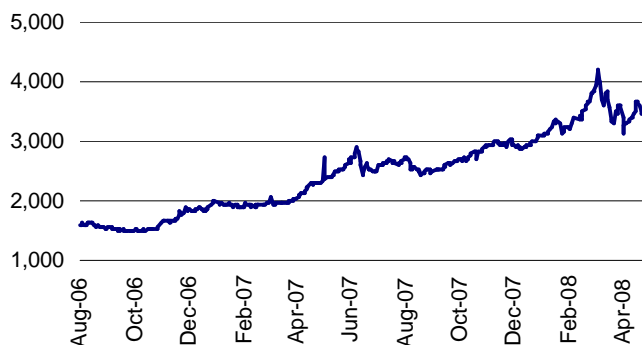
Source: Company/Motilal Oswal Securities

Cost pressures sustain; selective price increases and volume growth critical factors

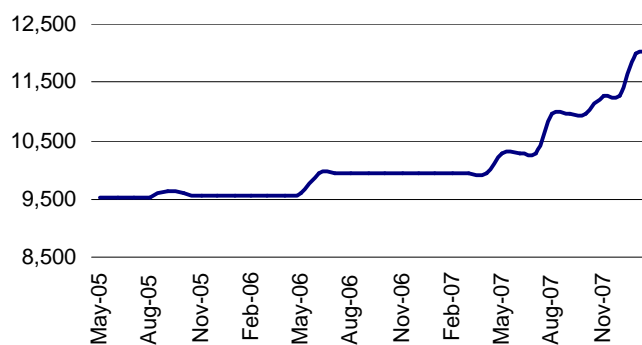
All the key inputs like palm oil, LAB, soda ash, tea, coffee and wheat are witnessing a sharp increase in prices due to global increase in agri commodity and crude prices. Some

of the crude-based inputs like LAB, soda ash and palm oil are unlikely to cool off significantly unless the global crude oil prices take a hit. Food product inputs are on a boil due to shortage of food products globally. We believe ability to undertake selective price increases and maintain volume growth on increased prices holds the key to future growth potential. Rising expenses on food and groceries is putting pressure on consumer budgets which might result in slowdown in volume growth in the coming quarters. We expect CY08 volume growth at 8% versus 10.2% volume growth in 1QCY08.

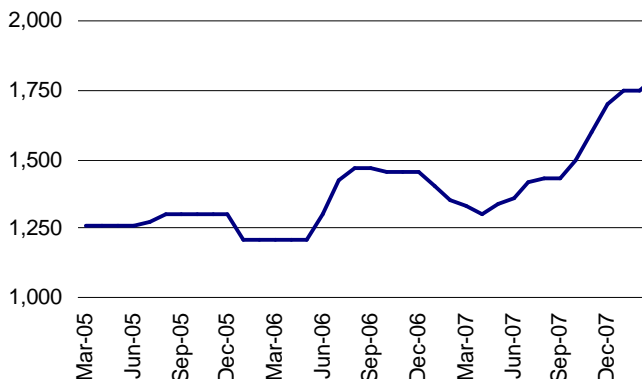
TREND IN PALM OIL PRICES (RINGGITS/TON)



TREND IN SODA ASH PRICE (RS/TON)



TREND IN LAB PRICES (US\$/TON)



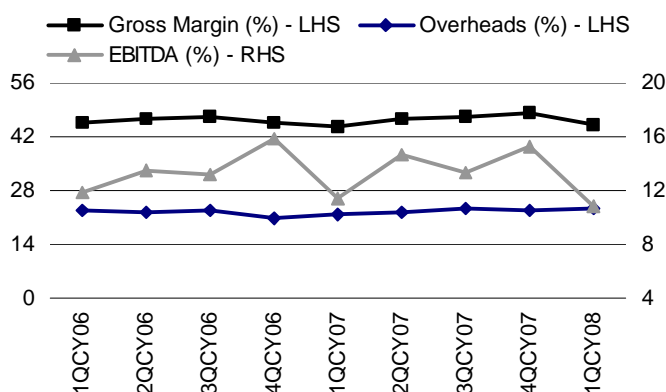
Source: Company/Motilal Oswal Securities

Rising overheads to keep margin expansion in check

HUL has reported 60bp decline in EBIDTA margin to 10.7% compared with our estimate of 40bp increase in EBIDTA margins in 1QCY08, despite 80 bp increase in gross margins. The decline in margins has been due to sharp increase in overheads like staff costs and other expenses. Adspend although seasonal has also increased 22%. Thus EBIDTA has grown by only 12.4% and is Rs200m lower than our estimate of Rs4,270m. We expect the overheads growth rate to remain strong due to rising investments on new initiatives like Pure IT, Kissan Amaze Food and Ponds Age Miracle range. In addition, we expect competition to intensify across products and segments due to entry of players like ITC, Dabur, and Nestle etc. in key product segments.

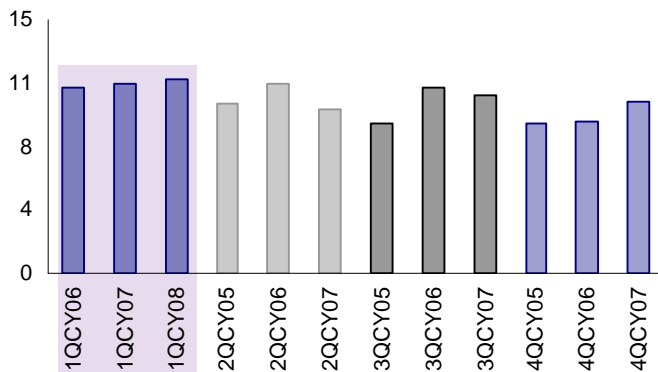
Initiatives to launch new products in the foods portfolio and roll-out of the water business will increase costs further. Adspend as a percentage of sales increased from 10.8% to 11.2% in 1QCY07. We believe that the trend in adspend will continue to be high on account of increased competitive pressures resulting in higher spend by the company to maintain its market share.

HIGHER OVERHEADS PUT PRESSURE ON EBIDTA MARGINS



Source: Company/Motilal Oswal Securities

RISING AD SPEND



Source: Company/Motilal Oswal Securities

LOW PENETRATION ATTRACTING NEW PLAYERS

	PENETRATION (%)		
	ALL INDIA	URBAN	RURAL
Deodorants	2.1	5.5	0.6
Instant Coffee	6.6	15.5	2.8
Skin Cream	22.0	31.5	17.8
Utensil Cleaner	28.0	59.9	14.6
Toothpastes	48.6	74.9	37.6
Shampoo	38.0	52.1	31.9
Washing Powder	86.1	90.7	84.1
Detergent Bar	88.6	91.4	87.4
Toilet Soap	91.5	97.4	88.9

Source: Company/Motilal Oswal Securities

Revising estimates; maintain Neutral

We are increasing other income estimates from Rs4.04b to Rs4.64b due to 55% increase in operational other income during 1QCY08. We are increasing sales growth estimates for CY08 and CY09 to 16.8% (v/s 13.7%) and 12.6% (v/s 11.5%) due to higher volume growth in key categories of Soaps, Detergents and Personal Care (70% of sales). We expect 30bp margin expansion in CY08 and 50bp in CY09 v/s earlier estimates of 70bp and 40bp respectively. Lower margin expansion takes into account rising input costs as well as overheads due to new initiatives.

We are increasing our EPS estimates for CY08 and CY09 to Rs9.4 and Rs11 from the earlier levels of Rs9.3 and Rs10.7 respectively. The stock trades at 26.3x CY08E and 22.5x CY09E with EPS CAGR of 16%. **Maintain Neutral.**

Hindustan Unilever: an investment profile

Company description

HUL is the largest company in the FMCG industry, with market leadership in soaps, detergents and personal care categories.

It has a wide distribution network with direct reach of over 1m retail outlets. The company is a subsidiary of Unilever, the Anglo Dutch FMCG giant.

Key investment arguments

- Sales growth in Personal Care has been lagging industry growth.
- Food products led by Ice Cream, Beverages and *Knorr* range are growing in high double digits.

Key investment risks

- Competitive pressure could intensify with more companies entering personal care and toilet soaps which account for more than 50% of HLL sales.
- High crude prices would increase material costs.

Recent developments

- Pure IT launch extended to 170 cities in 149 states.
- Launched new products like Ponds White Beauty Range, Dove Hair Care and Kid Nutritional product for Kids.
- Reduce toilet soap prices by 6-18% in select brands and SKUs to pass on excise exemption

Valuation and view

- We estimate CY08 EPS estimate at Rs9.4 and CY09 EPS estimate at Rs11.
- The stock trades at 26.3x CY08E and 22.5x CY09E with EPS CAGR of 16%. We maintain **Neutral**.

Sector view

- We are positive on the sector. The sector is showing strong volume growth across product categories with improving pricing power for leading players.
- Companies with low competitive pressures and brought product portfolios will be able to better withstand any slowdown in a particular segment.
- Longer term prospects bright, given rising incomes and low penetration.

COMPARATIVE VALUATIONS

		HLL	ITC	NESTLE
P/E (x)	CY08E	26.3	22.1	27.3
	CY09E	22.5	18.6	21.4
EV/EBITDA (x)	CY08E	22.9	14.5	17.7
	CY09E	19.4	11.8	13.9
EV/Sales (x)	CY08E	3.2	4.5	3.6
	CY09E	2.8	3.7	3.0
P/BV (x)	CY08E	29.8	5.8	23.9
	CY09E	23.8	5.1	18.5

SHAREHOLDING PATTERN (%)

	MAR-08	DEC-07	MAR-07
Promoter	52.1	52.1	51.4
Domestic Inst	15.2	15.4	16.5
Foreign	15.4	14.6	12.6
Others	17.3	17.9	19.5

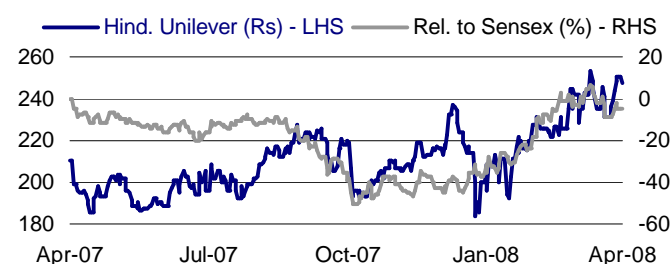
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
CY08	9.4	9.4	0.1
CY09	11.0	11.0	-0.3

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
247	242	-	Neutral

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					
(RS MILLION)					
Y/E DECEMBER	2005	2006	2007	2008E	2009E
Net Sales	110,605	121,034	137,178	160,277	180,442
Change (%)	11.4	9.4	13.3	16.8	12.6
Total Expenditure	-96,172	-104,553	-118,321	-137,767	-154,276
EBITDA	14,433	16,481	18,857	22,510	26,166
Change (%)	0.4	14.2	14.4	19.4	16.2
Margin (%)	13.0	13.6	13.7	14.0	14.5
Depreciation	-1,245	-1,302	-1,384	-1,434	-1,484
Int. and Fin. Charges	-192	-107	-255	-200	-200
Other Income - Recurring	3,048	3,545	4,627	4,344	4,972
Profit before Taxes	16,045	18,617	21,845	25,220	29,454
Change (%)	6.6	16.0	17.3	15.4	16.8
Margin (%)	14.5	15.4	15.9	15.7	16.3
Tax	-2,530	-2,952	-3,765	-4,310	-5,016
Deferred Tax	-410	-268	-389	-454	-530
Tax Rate (%)	-18.3	-17.3	-19.0	-18.9	-18.8
Profit after Taxes	13,105	15,397	17,691	20,456	23,907
Change (%)	10.6	17.5	14.9	15.6	16.9
Margin (%)	11.8	12.7	12.9	12.8	13.2
Non-rec. (Exp)/Income	976	3,157	1,564	25	0
Reported PAT	14,081	18,554	19,255	20,481	23,907

BALANCE SHEET					
(RS MILLION)					
Y/E DECEMBER	2005	2006	2007	2008E	2009E
Share Capital	2,201	2,207	2,177	2,177	2,177
Reserves	20,855	25,028	12,215	15,865	20,418
Net Worth	23,056	27,235	14,392	18,041	22,595
Loans	569	726	885	726	726
Capital Employed	23,626	27,961	15,278	18,767	23,321
Gross Block	23,751	24,627	26,691	27,691	28,691
Less: Accum. Deprn.	-9,896	-10,619	-11,466	-12,899	-14,383
Net Fixed Assets	13,855	14,007	15,225	14,791	14,308
Capital WIP	980	1,103	1,856	1,856	1,856
Investments	20,142	24,139	14,408	19,068	25,311
Deferred Charges	2,201	2,245	2,124	2,269	2,424
Curr. Assets, L&A	27,630	31,697	32,774	37,976	43,694
Inventory	13,218	15,477	19,536	20,035	22,555
Account Receivables	5,228	4,404	4,434	5,269	5,932
Cash and Bank Balance	3,550	4,169	2,009	5,272	7,144
Others	5,634	7,646	6,796	7,401	8,062
Curr. Liab. and Prov.	41,183	45,231	51,110	57,219	64,297
Account Payables	23,450	24,637	28,785	33,064	37,026
Other Liabilities	11,572	13,369	15,610	16,210	18,001
Provisions	6,162	7,224	6,716	7,945	9,269
Net Current Assets	-13,553	-13,534	-18,336	-19,218	-20,578
Application of Funds	23,626	27,961	15,278	18,767	23,321

E: MOSI Estimates

RATIOS					
Y/E DECEMBER	2005	2006	2007	2008E	2009E
Basic (Rs)					
EPS	6.0	7.0	8.1	9.4	11.0
Cash EPS	6.5	7.6	8.8	10.1	11.7
BV/Share	10.5	12.3	6.6	8.3	10.4
DPS	5.0	6.0	9.1	6.6	7.6
Payout %	84.0	86.0	111.7	70.2	69.2
Valuation (x)					
P/E		35.4	30.4	26.3	22.5
Cash P/E		32.7	28.2	24.6	21.2
EV/Sales		4.3	3.8	3.2	2.8
EV/EBITDA		31.4	27.7	22.9	19.4
P/BV		20.0	37.4	29.8	23.8
Dividend Yield (%)		2.4	3.7	2.7	3.1
Return Ratios (%)					
RoE	56.8	56.5	122.9	113.4	105.8
RoCE	68.7	67.0	144.7	135.4	127.2
Working Capital Ratios					
Debtor (Days)	17	13	12	12	12
Asset Turnover (x)	4.7	4.3	9.0	8.5	7.7
Leverage Ratio					
Debt/Equity (x)	0.0	0.0	0.1	0.0	0.0

CASH FLOW STATEMENT					
(RS MILLION)					
Y/E DECEMBER	2005	2006	2007	2008E	2009E
OP/(loss) before Tax	13,189	15,179	17,473	21,076	24,682
Int./Div. Received	3,048	3,545	4,627	4,344	4,972
Depreciation and Amort.	1,245	1,302	1,384	1,434	1,484
Interest Paid	-192	-107	-255	-200	-200
Direct Taxes Paid	-2,530	-2,952	-3,765	-4,310	-5,016
(Incr)/Decr in WC	6,030	600	2,641	4,145	3,233
Change in Deff	-59	44	-122	145	155
CF from Operations	20,731	17,610	21,983	26,634	29,309
Extraordinary Items	976	3,157	1,564	25	0
(Incr)/Decr in FA	-645	-998	-2,818	-1,000	-1,000
(Pur)/Sale of Investments	2,154	-3,997	9,731	-4,660	-6,243
CF from Invest.	2,485	-1,838	8,478	-5,635	-7,243
Issue of Shares	0	0	-6,263	0	1
(Incr)/Decr in Debt	-14,141	157	159	-159	0
Dividend Paid	-11,006	-15,100	-23,316	-16,807	-19,354
Others	-1,498	-210	-3,202	-794	-841
CF from Fin. Activity	-26,645	-15,153	-32,622	-17,736	-20,194
Incr/Decr of Cash	-3,430	619	-2,161	3,263	1,872
Add: Opening Balance	6,980	3,550	4,169	2,009	5,272
Closing Balance	3,551	4,169	2,008	5,272	7,144

N O T E S



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Disclosure of Interest Statement

Hindustan Unilever

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|---|----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
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