

Hindustan Unilever

Volumes surge on focused brand building measures

Hindustan Unilever (HUL) clocked a strong 5% growth in its volumes during Q3FY10 (up 1% QoQ). This, along with absence of price hikes, translated into a 4.6% YoY growth in net sales to Rs 45bn, in line with our estimates. The operating margin remained flat YoY as incremental savings in material costs were ploughed back as brand investments. The stock is likely to remain under pressure in the near-term due to regular price cuts taken by the company to augment volume growth. We therefore maintain Hold on the stock with a price target of Rs 257, valuing it a 23x its FY11E earnings.

Net sales in line with estimates: HUL's net sales for Q3FY10 increased by 4.6% YoY at Rs 45bn, in line with our estimate, entirely driven by higher volumes. Segment-wise, revenue growth was led by personal products (up 15.5% YoY), beverages (up 7.9% YoY) and processed foods (up 9.2% YoY). The soaps & detergents segment, however, slumped 2.4% YoY. Segments such as soaps, laundry, and personal products also booked higher volumes in the quarter, which were partly offset by price reductions in the laundry segment.

Margins remain flat: HUL's EBITDA grew 3.7% YoY to Rs 7.2bn with an operating margin of 16% that remained flat YoY. The gross profit margin expanded 480bps YoY mainly on account of lower commodity prices and efficient cost management in sourcing raw materials. Bulk savings emanating from lower raw material costs were invested back by the company in the form of higher A&P investments that grew 66% YoY to Rs 6.3bn. A&P expenses, as a percentage of sales, increased 530bps YoY to 14.1% while personnel and other expenses remained flat YoY.

Adj. PAT drops to Rs 6bn: HUL's reported PAT increased 5.4% YoY to Rs 6.5bn on account of profit on sale of properties. However, adjusting for exceptional items, adj. PAT declined 8.8% YoY to Rs 6bn, lower than our estimate. Consequently, the adj. PAT margin also plunged 200bps YoY to 13.4%.

Maintain Hold: Currently, HUL is trading at a P/E of 24.9x and 21.9x its FY10E and FY11E earnings. We have lowered our earnings estimates for FY10 and FY11 by 2.7% and 4.3% respectively. We have also downgraded our target P/E multiple from 24x to 23x to factor in the intensifying competition in the domestic FMCG space. Our price target also stands revised to Rs 257 (from Rs 274 previously). Maintain Hold.

What's New? Target Rating Estimates

CMP	TARGET	RATING	RISK
Rs 244	Rs 257	HOLD	LOW

BSE	NSE	BLOOMBERG
500696	HINDUNILVR	HUVR IN

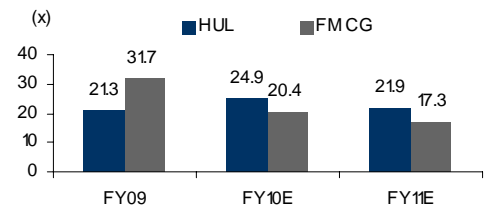
Company data

Market cap (Rs mn / US\$ mn)	532,905 / 11,540
Outstanding equity shares (mn)	2,183
Free float (%)	48
Dividend yield (%)	3.2
52-week high/low (Rs)	307 / 211
2-month average daily volume	2,988,908

Stock performance

Returns (%)	CMP	1-mth	3-mth	6-mth
HUL	242	(8.6)	(14.4)	(9.7)
BSE FMCG	2,725	(3.6)	(3.6)	5.5
Sensex	16,358	(6.0)	1.9	7.8

P/E comparison



Valuation matrix

(x)	FY09*	FY10E	FY11E	FY12E
P/E @ CMP	21.3	24.9	21.9	19.7
P/E @ Target	22.4	26.2	23.0	20.7
EV/EBITDA @ CMP	19.4	19.6	17.4	15.9

* 15 months period ending March 2009

Financial highlights

(Rs mn)	FY09*	FY10E	FY11E	FY12E
Revenue	202,393	175,531	200,033	223,725
Growth (%)	47.5	(13.3)	14.0	11.8
Adj net income	25,007	21,435	24,386	27,061
Growth (%)	34.3	(14.3)	13.8	11.0
FDEPS (Rs)	11.5	9.8	11.2	12.4
Growth (%)	34.0	(14.3)	13.8	11.0

Profitability and return ratios

(%)	FY09*	FY10E	FY11E	FY12E
EBITDA margin	13.2	15.1	14.9	14.6
EBIT margin	12.3	14.1	13.9	13.5
Adj PAT margin	12.4	12.2	12.2	12.1
ROE	142.9	100.6	107.1	79.1
ROIC	134.1	92.4	87.0	81.4
ROCE	125.7	84.1	88.4	68.9

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RHH Research is also available on Bloomberg FTIS <GO> and Thomson First Call





Result highlights

Fig 1 - Actual vs. estimated performance

(Rs mn)	Actual	Estimate	% Variance
Revenue	45,043	45,662	(1.4)
EBITDA	7,185	8,343	(13.9)
Adj net income	6,046	6,702	(9.8)
FDEPS (Rs)	2.77	3.07	(9.8)

Source: RHH

Fig 2 - Quarterly performance

(Rs mn)	Q3FY10	Q3FY09	% Chg YoY	Q2FY10	% Chg QoQ
Revenue	45,043	43,077	4.6	42,281	6.5
Expenditure	37,857	36,147	4.7	36,172	4.7
Operating profit	7,185	6,931	3.7	6,110	17.6
Other income	1,079	1,045	3.2	884	22.0
Interest	2	44	(95.7)	15	(87.0)
Depreciation	450	406	10.9	462	(2.7)
PBT	8,257	7,141	15.6	6,517	26.7
Tax	1,766	896	97.1	878	101.1
PAT	6,046	6,630	(8.8)	4,287	41.1
EBITDA margin (%)	16.0	16.1	(14bps)	14.4	150bps
FDEPS (Rs)	2.77	3.04	(9.0)	1.97	40.8

Source: Company, RHH

Fig 3 - Revised estimates

Key parameters (Rs mn)	FY10E			FY11E		
	Old	New	% Chg	Old	New	% Chg
Revenue	175,022	175,531	0.3	200,333	200,033	(0.1)
EBITDA	25,156	26,558	5.6	29,682	29,897	0.7
EBITDA margin (%)	14.4	15.1	76bps	14.8	14.9	13bps
Net profit	22,029	21,435	(2.7)	25,495	24,386	(4.3)
FDEPS (Rs)	10.10	9.82	(2.7)	11.70	11.17	(4.3)

Source: RHH

Key highlights of the management conference call

- ❖ The domestic FMCG market has seen subdued growth primarily on account of lower prices in the laundry segment; this is attributed to the price cuts taken by the company. Downtrading in some segments like laundry and tea and high food price inflation has impacted demand for these products.
- ❖ Costs for commodities like palm oil, soda ash, LAB, and tea have firmed up.
- ❖ The company has seen volume growth in the laundry segment, both for powders and bars; however, value shares have declined on account of downtrading. *Wheel* powder has seen a 140bps improvement in market share with the share of *Wheel* bars surging 120bps on double-digit volume growth.
- ❖ The market share of HUL's soaps segment has improved 10bps QoQ on strong volume growth arising from the re-launch of *Lux*. *Lifebuoy* has still not attained the projected growth.

Higher A&P expenses dent performance

Net sales growth completely driven by increase in volumes

Savings from lower input costs ploughed back as brand investments, leading to flattish margins

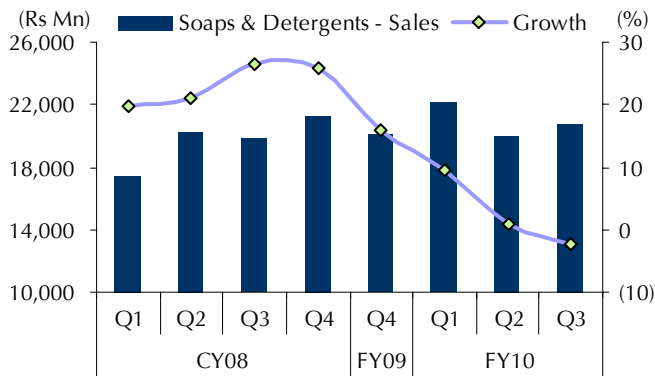
Earnings pruned to reflect lower other income and higher tax estimates



- ❖ In terms of Skin care, *Fair & Lovely*, and *Ponds* have reported strong volume growth, led by the premium category. *Fair & Lovely* (winter fairness) has also been successfully launched. The *Vaseline* winter range witnessed double-digit volume growth during the quarter.
- ❖ In terms of Hair care, *Clinic Plus*, and *Dove* led the volume growth through introduction of new variants. *Sunsilk* was also re-launched in November.
- ❖ The volumes for the oral care segment surged on account of the re-launch of *Pepsodent* and a pepper mint variant of *Close-up*.
- ❖ The growth in beverages was impacted due to lower growth in tea as downtrading by consumers impacted sales of *Taaza* and *Red Label*. HUL's market share in the tea segment was impacted due its absence in the discount segment. Therefore, the company has recently launched *Brooke Bond Sehatmand* in the discount segment to take advantage of the downtrading seen in this segment. For coffee, *Bru Cappuchino* has seen a good volume growth. The ice cream segment has also seen growth in the impulse and take-home categories.
- ❖ The company's gross margin has improved on account of benefits flowing in from better global scale, buying efficiencies, and lower commodity costs YoY.
- ❖ The company has recently taken some price cuts in the laundry segment, with prices of *Rin* lowered by 30% from Rs 70/kg to Rs 50/kg and prices of *Surf Excel Blue* reduced by 10% from Rs 91/kg to Rs 82/kg.

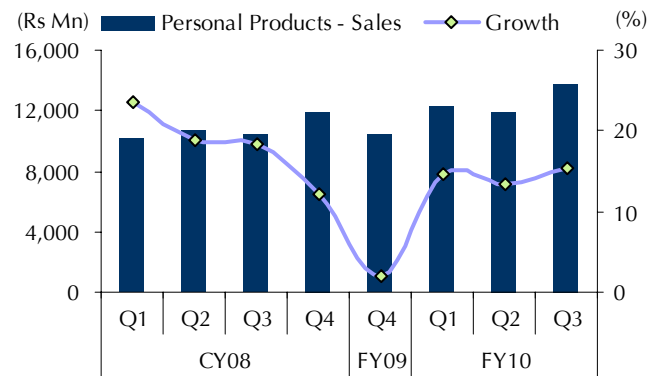


Fig 4 - Value growth in soaps & detergents continues to decline



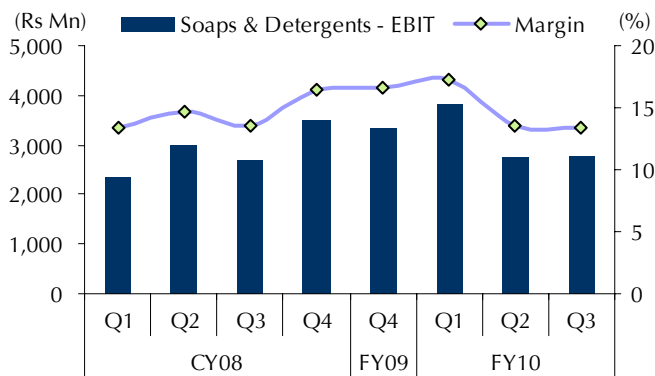
Source: RHH, Company

Fig 5 - Value growth remains steady in personal products



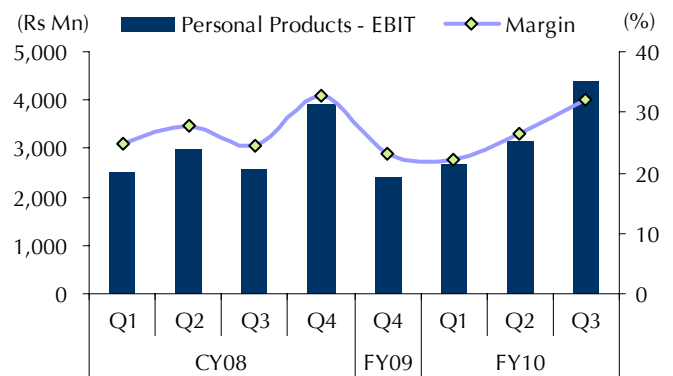
Source: RHH, Company

Fig 6 - EBIT margin for soaps & detergents remains suppressed



Source: RHH, Company

Fig 7 - EBIT margin for personal products remains stable YoY



Source: RHH, Company



Standalone financials

Profit and Loss statement

Y/E March (Rs mn)	FY09*	FY10E	FY11E	FY12E
Revenues	202,393	175,531	200,033	223,725
Growth (%)	47.5	(13.3)	14.0	11.8
EBITDA	26,780	26,558	29,897	32,702
Growth (%)	35.3	(0.8)	12.6	9.4
Depreciation & amortisation	1,953	1,828	2,185	2,497
EBIT	24,827	24,730	27,712	30,204
Growth (%)	34.9	(0.4)	12.1	9.0
Interest	253	362	415	445
Other income	5,678	3,470	4,373	5,386
EBT	30,251	27,837	31,670	35,145
Income taxes	5,244	6,403	7,284	8,083
Effective tax rate (%)	17.3	23.0	23.0	23.0
Extraordinary items	(43)	-	-	-
Min into / inc from associates	-	-	-	-
Reported net income	24,965	21,435	24,386	27,061
Adjustments	(43)	-	-	-
Adjusted net income	25,007	21,435	24,386	27,061
Growth (%)	34.3	(14.3)	13.8	11.0
Shares outstanding (mn)	2,178.6	2,178.6	2,178.6	2,178.6
FDEPS (Rs) (adj)	11.5	9.8	11.2	12.4
Growth (%)	34.0	(14.3)	13.8	11.0
DPS (Rs)	7.5	7.9	8.9	9.9

Cash flow statement

Y/E March (Rs mn)	FY09*	FY10E	FY11E	FY12E
Net income + Depreciation	22,137	26,792	23,620	26,883
Non-cash adjustments	2,669	(3,530)	2,951	2,675
Changes in working capital	(3,289)	4,017	1,825	757
Cash flow from operations	21,516	27,279	28,397	30,315
Capital expenditure	(6,295)	(7,209)	(6,859)	(5,523)
Change in investments	11,668	-	-	-
Other investing cash flow	1,926	-	-	-
Cash flow from investing	7,299	(7,209)	(6,859)	(5,523)
Issue of equity	381	0	0	19,619
Issue/repay debt	3,334	606	727	31
Dividends paid	(16,766)	(17,663)	(20,391)	(23,842)
Other financing cash flow	-	-	-	-
Change in cash & cash eq	15,765	3,014	1,874	20,599
Closing cash & cash eq	17,773	20,787	22,661	43,260

Economic Value Added (EVA) analysis

Y/E March	FY09*	FY10E	FY11E	FY12E
WACC (%)	13.5	13.5	13.5	13.5
ROIC (%)	134.1	92.4	87.0	81.4
Invested capital (Rs mn)	19,015	22,185	26,866	30,254
EVA (Rs mn)	22,934	17,521	19,758	20,564
EVA spread (%)	120.6	79.0	73.5	68.0

Balance sheet

Y/E March (Rs mn)	FY09*	FY10E	FY11E	FY12E
Cash and cash eq	17,773	20,787	22,661	43,260
Accounts receivable	5,369	6,733	8,221	9,194
Inventories	25,289	24,729	28,351	32,231
Other current assets	7,579	11,058	12,802	14,318
Investments	3,326	3,326	3,326	3,326
Gross fixed assets	28,817	35,318	41,363	46,262
Net fixed assets	16,068	20,741	24,600	27,002
CWIP	4,721	5,429	6,243	6,867
Intangible assets	-	-	-	-
Deferred tax assets, net	2,548	2,548	2,548	2,548
Other assets	-	-	-	-
Total assets	82,673	95,351	108,752	138,747
Accounts payable	33,050	38,093	43,411	48,076
Other current liabilities	9,508	10,959	12,489	13,831
Provisions	15,280	19,486	23,753	26,359
Debt funds	4,219	4,825	5,552	5,583
Other liabilities	-	-	-	-
Equity capital	2,180	2,180	2,180	21,799
Reserves & surplus	18,435	19,807	21,368	23,100
Shareholder's funds	20,615	21,987	23,548	44,898
Total liabilities	82,673	95,351	108,752	138,747
BVPS (Rs)	9.5	10.1	10.8	20.6

Financial ratios

Y/E March	FY09*	FY10E	FY11E	FY12E
Profitability & Return ratios (%)				
EBITDA margin	13.2	15.1	14.9	14.6
EBIT margin	12.3	14.1	13.9	13.5
Net profit margin	12.4	12.2	12.2	12.1
ROE	142.9	100.6	107.1	79.1
ROCE	125.7	84.1	88.4	68.9
Working Capital & Liquidity ratios				
Receivables (days)	9	13	14	14
Inventory (days)	75	99	93	94
Payables (days)	104	141	142	142
Current ratio (x)	1.3	1.3	1.3	1.6
Quick ratio (x)	0.5	0.6	0.6	0.8
Turnover & Leverage ratios (x)				
Gross asset turnover	7.3	5.5	5.2	5.1
Total asset turnover	2.7	2.0	2.0	1.8
Interest coverage ratio	98.0	68.4	66.8	67.8
Adjusted debt/equity	0.2	0.2	0.2	0.1
Valuation ratios (x)				
EV/Sales	2.6	3.0	2.6	2.3
EV/EBITDA	19.4	19.6	17.4	15.9
P/E	21.3	24.9	21.9	19.7
P/BV	25.8	24.2	22.6	11.9



Quarterly trend

Particulars	Q4CY08	Q1CY09	Q1FY10	Q2FY10	Q3FY10
Revenue (Rs mn)	43,077	39,883	44,757	42,281	45,043
YoY growth (%)	16.8	5.1	7.8	5.0	4.6
QoQ growth (%)	6.9	(7.4)	12.2	(5.5)	6.5
EBITDA (Rs mn)	6,931	5,493	6,881	6,110	7,185
EBITDA margin (%)	1,608.9	1,377.2	1,537.4	1,445.0	1,595.2
Adj net income (Rs mn)	6,630	5,021	5,367	4,287	6,046
YoY growth (%)	22.8	32.7	(3.9)	(2.1)	(8.8)
QoQ growth (%)	51.4	(24.3)	6.9	(20.1)	41.1

DuPont analysis

(%)	CY07	FY09*	FY10E	FY11E	FY12E
Tax burden (Net income/PBT)	(5.0)	28.6	15.4	15.4	15.4
Interest burden (PBT/EBIT)	123.8	121.9	112.6	114.3	116.4
EBIT margin (EBIT/Revenues)	13.4	12.3	14.1	13.9	13.5
Asset turnover (Revenues/Avg TA)	196.6	271.6	197.2	196.0	180.8
Leverage (Avg TA/Avg equity)	335.3	425.8	417.9	448.2	361.6
Return on equity	89.5	142.9	100.6	107.1	79.1

Company profile

HUL, the largest FMCG Company in India (in terms of sales) has presence in soaps & detergents, personal care products, beverages, foods and ice creams. HUL's primary strengths are strong brands and a wide distribution network with direct reach of over 1 mn retail outlets. This combined with the company's strengths in its business, its well developed distribution network; a strong brand portfolio will help it maintain market share.

Shareholding pattern

(%)	Jun-09	Sep-09	Dec-09
Promoters	52.1	52.1	52.0
FII's	14.3	14.7	14.7
Banks & FI's	14.9	14.3	14.3
Public	18.7	18.9	19.0

Recommendation history

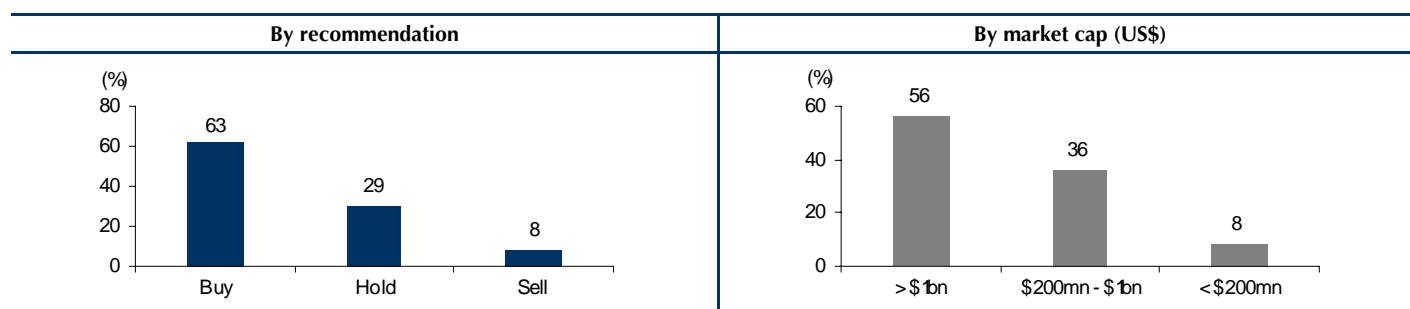
Date	Event	Reco price	Tgt price	Reco
21-Aug-08	RHH Compendium	240	275	Hold
27-Oct-08	Results Review	224	260	Hold
28-Jan-09	Results Review	259	280	Hold
18-Mar-09	Company Update	234	280	Buy
11-May-09	Results Review	227	280	Buy
29-Jul-09	Results Review	268	280	Hold
2-Nov-09	Results Review	283	280	Hold
16-Dec-09	Flash Note	266	274	Hold
30-Jan-10	Results Review	244	257	Hold

Stock performance





Coverage Profile



Recommendation interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and -5%
Sell	Less than -5%

Recommendation structure changed with effect from March 1, 2009

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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