

Hindustan Unilever

CMP: ₹ 481
TP: ₹ 455
Reduce

High Points

- Results below estimates on all parameters. Volume growth of 5%
- Royalty cost increased from 1.4% to 3.15% by FY18
- Reduce earnings by 1-2%. Recommend Reduce with a target price of ₹ 455

HUVR Q3FY13 results were below our estimate. Domestic FMCG business grew by 15% on back of a 5% volume growth. Revenue grew by 11.7% (adjusted for export business growth stood at 17.3%) to ₹ 66.5bn. Gross profit was up 12.5% as gross margin expanded by 34bps YoY.

EBITDA grew by 12.2% to ₹ 10.9bn as margins remained flat YoY at 16.4%. Other income at ₹ 1.34bn, boosted PBT by 16% to ₹ 11.56bn. Reported PAT grew by 15.6% to ₹ 8.7bn. Adjusted for exceptional item the PAT was up 14.6% to ₹ 8.7bn. Ad spends grew by 19% up 77bps YoY to 12.4% and other expenditure declined by 104bps to 14.8%.

HUL has entered into a new agreement with Unilever Plc with respect to the payment of royalty. Currently, royalty cost for HUL stand at 1.4% of turnover. As per the revised agreement royalty cost will increase to 3.15% of turnover by no later than 31st March 2018 in a phased manner. In the first year beginning Feb 2013 the royalty will increase to 1.90%.

We believe its earnings growth would be restricted due to 1) increase in royalty to some extent and 2) rising tax rate. We estimate earnings CAGR of 11% during FY13-15E which would result in the P/E to contract. We have downgraded our EPS estimate by 1-2% for FY14 and FY15. At a CMP of ₹ 482, the stock trades at 29x FY14E EPS of ₹ 16.8 and 26x FY15E EPS of ₹ 18.2. We recommend a Reduce with a price target of ₹ 455.

Scrip Details

Equity	₹ 2214mn
Face Value	₹ 1/-
Market Cap	₹ 1065bn
	USD 20bn
52 week High / Low	₹ 580 / 375
Avg. Volume (no)	2,646,981
BSE Sensex	19,981
NSE Nifty	6,049
Bloomberg Code	HUVR IN
Reuters Code	HLL.BO

Q3FY13 Result (₹ mn)

Particulars	Q3FY13	Q3FY12	YoY (%)	Q2FY13	QoQ (%)	9MFY13	9MFY12	YoY (%)
Net Sales	66,548	59,555	11.7	63,108	5.5	193,444	171,545	12.8
Expenditure	55,660	49,850	11.7	53,341	4.3	163,124	146,031	11.7
Consumption of Raw Materials	34,191	30,799	11.0	32,695	4.6	100,563	91,685	9.7
Staff Cost	3,427	2,741	25.0	3,305	3.7	10,061	8,477	18.7
Advertising cost	8,222	6,902	19.1	7,690	6.9	24,108	19,745	22.1
Other Expenditure	9,821	9,408	4.4	9,652	1.8	28,393	26,125	8.7
Operating Profit	10,888	9,705	12.2	9,767	11.5	30,320	25,514	18.8
Other Income	1,337	801	67.0	1,488	-10.1	4,666	2,118	120.3
Interest	75	5	1573	63	19.0	191	10	1795.0
Depreciation	593	568	4.3	577	2.8	1,746	1,701	2.6
Exceptional Items - Gain / (Loss)	(17)	(84)		16		5,030	768	
PBT	11,540	9,849	17.2	10,631	8.6	38,078	26,689	42.7
Tax	2,826	2,311	22.3	2,561	10.3	7,983	5,956	34.0
Net Profit	8,714	7,538	15.6	8,069	8.0	30,095	20,733	45.2
Adj Profit	8,731	7,622	14.6	8,053	8.4	25,065	19,965	25.5
Gross Margin (%)	48.6	48.3	33.8	48.2	43.0	48.0	46.6	146.1
OPM (%)	16.4	16.3	6.5	15.5	88.4	15.7	14.9	80.0
Advertising spend (%)	12.4	11.6	76.5	12.2	16.9	12.5	11.5	95.2
Tax rate (%)	24.5	23.5	102.3	24.1	39.6	21.0	22.3	-134.9
NPM (%)	13.1	12.7	43.6	12.8	30.7	15.6	12.1	347.1

Financials

Year	Net Sales	% Growth	EBIDTA	OPM%	PAT	Growth%	EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE(%)
FY12	221,205	12.1	32,897	14.9	25,640	18.9	11.9	11.9	40.5	83.1	134.2
FY13E	258,974	17.1	40,308	15.6	32,895	28.3	14.9	14.9	32.4	100.5	169.3
FY14E	296,357	14.4	47,651	16.1	37,145	12.9	16.8	16.8	28.7	103.2	177.2
FY15E	337,983	14.0	55,793	16.5	40,296	8.5	18.2	18.2	26.4	82.6	145.1

Figure in ₹ mn

Sr. Analyst: Amit Purohit

Tel : +9122 4096 9724

E-mail: amitp@dolatcapital.com

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Segmental Performance

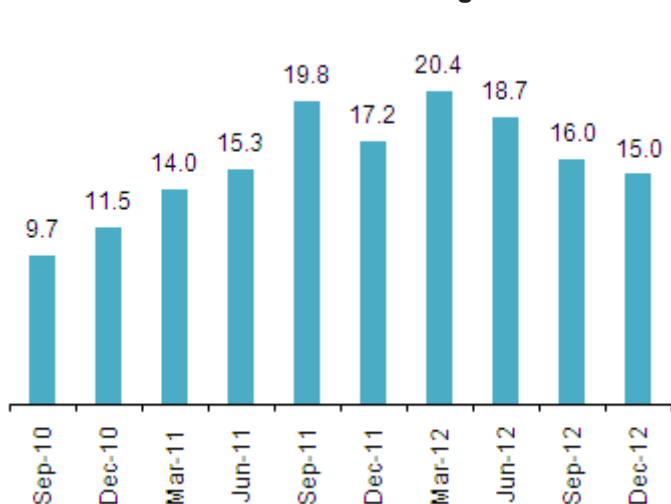
Net Sales (₹ m)	Q3FY13	Q3FY12	YoY (%)	Q2FY13	QoQ (%)	9MFY13	9MFY12	YoY (%)
Soaps & Detergent	31,712	26,481	19.8	31,762	(0.2)	95,104	78,019	21.9
Personal Products	20,489	18,134	13.0	17,445	17.4	56,405	49,519	13.9
Beeverages	7,929	6,709	18.2	7,196	10.2	21,666	19,343	12.0
Processed Foods	3,301	3,067	7.7	3,663	(9.9)	11,334	10,114	12.1
Others	2,902	5,104		2,884	0.6	8,425	14,400	
Total	66,334	59,495	11.5	62,949	5.4	192,935	171,394	12.6
EBIT (Rs m)								
Soaps & Detergent	3,937	3,559	10.6	4,536	(13.2)	12,325	9,132	35.0
Personal Products	5,789	4,865	19.0	4,226	37.0	14,771	12,937	14.2
Beeverages	1,404	1,052	33.5	1,031	36.2	3,384	2,683	26.1
Processed Foods	(26)	(60)	(55.9)	9	(392.2)	231	279	(17.3)
Exports	0	0						
Others	(186)	359		21	(1,009.3)	(209)	734	
Total	10,917	9,776	11.7	9,822	11.2	30,501	25,765	18.4
EBIT Margin								
Soaps & Detergent	12.4	13.4	(102.4)	14.3	(186.4)	13.0	11.7	125.5
Personal Products	28.3	26.8	142.2	24.2	402.7	26.2	26.1	6.2
Beeverages	17.7	15.7	202.7	14.3	338.3	15.6	13.9	174.7
Processed Foods	(0.8)	(1.9)	115.0	0.2	(104.2)	2.0	2.8	(72.3)
Others	(6.4)	7.0	(1,346.5)	0.7	(713.4)	(2.5)	5.1	(757.8)
Total	16.5	16.4	2.6	15.6	85.5	15.8	15.0	77.7

Key takeaways of Conference call:

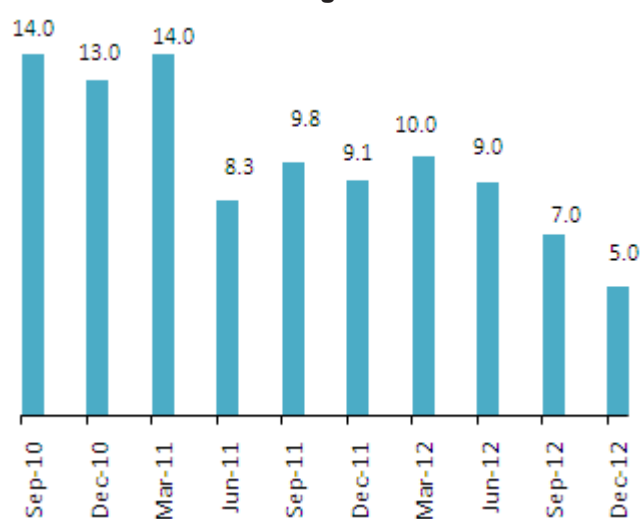
- Discretionary categories continue to witness some slowdown in consumption. Overall volume growth was lower than management expectation. Slowdown in Modern retail with closure of outlets also contributed to the lower volumes during the quarter.
- Slowdown in personal care was on account of lower volumes in Fair & Lovely post its re-launch at a higher price point.
- Company has taken corrective steps to improve the performance of Wheel through price action and ad-spend in the select regions.
- Management attributed muted gross margin expansion on account of change in product mix. We believe that Wheel and Fair & Lovely which posted a lower growth during the quarter enjoys higher percentage gross margin thereby restricting sharp expansion.
- Management indicated that volume growth may not be the right parameter to look at and their internal focus is to look at unit sales in each category. We believe overall value growth of 17% during the quarter is encouraging.
- Management seems confident of sustained premiumisation across categories over the next two years. Medium term outlook remains strong.

While premiumisation across categories continues and softening of raw material prices would improve the gross margin in the coming years, we believe its earnings growth would be restricted due to 1) increase in royalty to some extent and 2) rising tax rate. We believe that given the earnings CAGR of 11% during FY13-15E, the P/E would contract. We have revised our estimate to factor in increased royalty and improvement in margin due to softening of raw material cost. We have downgraded our EPS estimate by 1-2% for FY14 and FY15. At a CMP of ₹ 482, the stock trades at 29x FY14E EPS of ₹ 16.8 and 26x FY15E EPS of ₹ 18.2. We recommend a Reduce with a price target of ₹ 455.

Domestic FMCG sales growth %

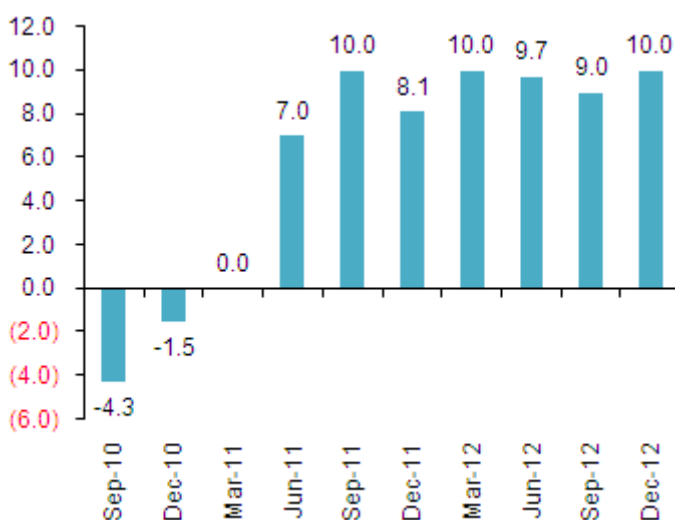


Volume growth %

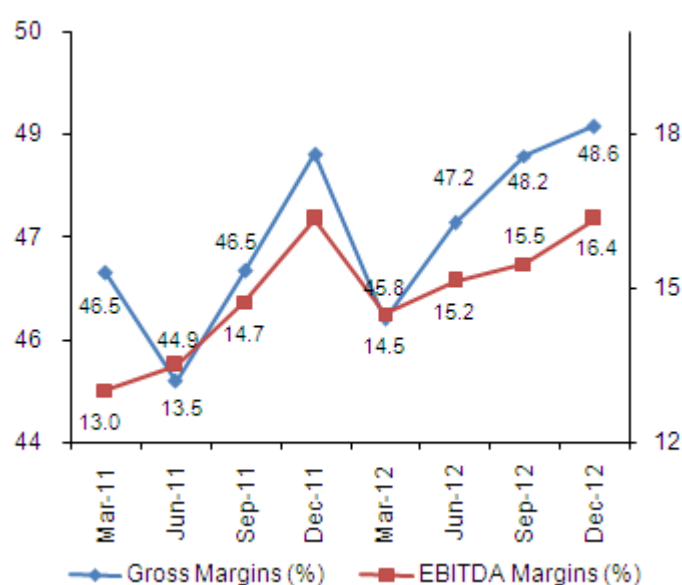


Source: Company, Dolat Research

Value Growth %

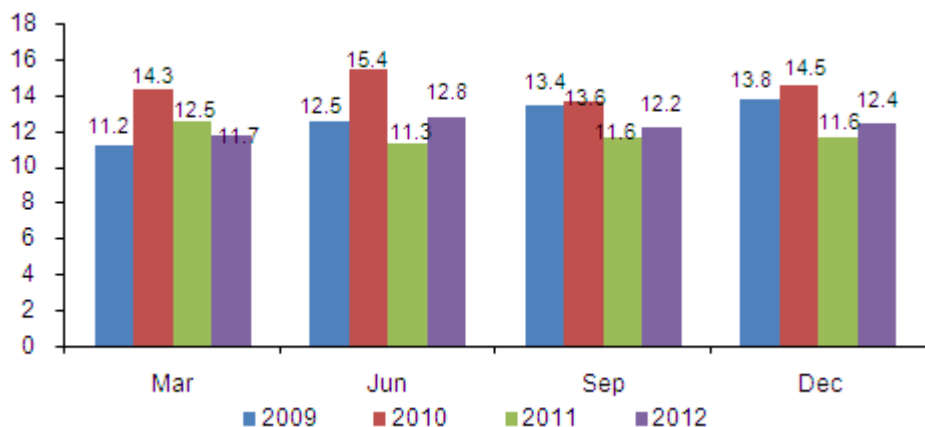


Quarterly trend in operating performance



Source: Company, Dolat Research

Decline in ad-spend to sales ratio (%)



Source: Company, Dolat Research

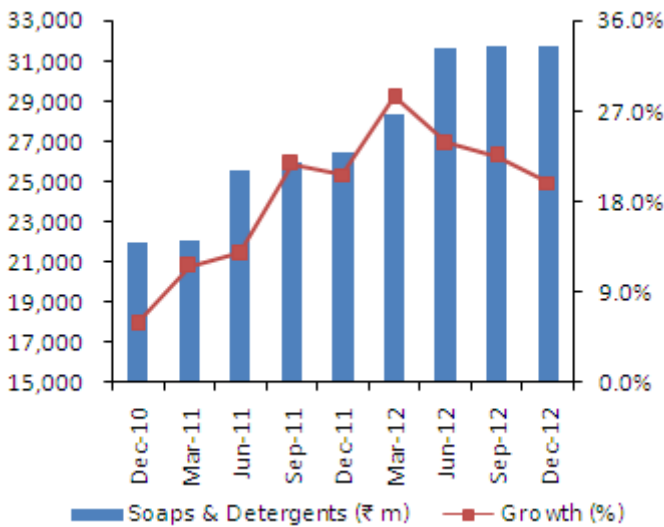
Soaps and Detergent performance

Soaps & Detergent revenue grew by 19.8% to ₹ 31.7bn. However, EBIT increased by just 11% to ₹ 3.9bn as margins expanded by declined by 100bps YoY to 12.4%.

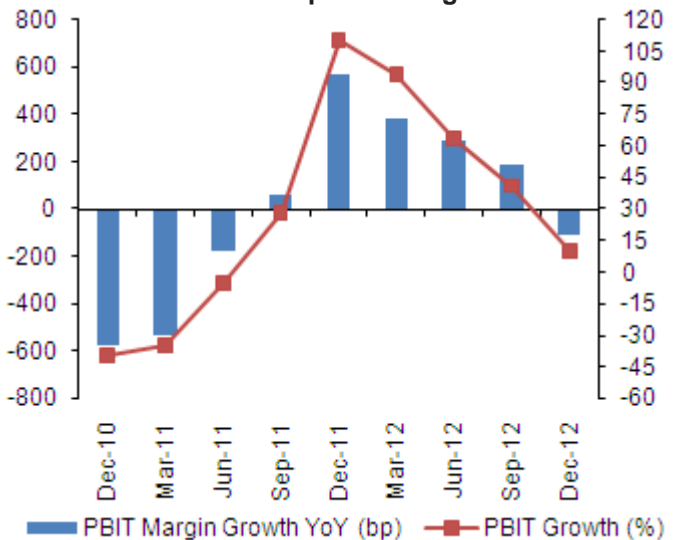
Soaps segment growth was mainly value led due to lower growth in wheel and premiumisation of the portfolio. Surf and Rin continued to drive category up-gradation with double digit volume growth. In the soap segment, Dove, Lux and Lifebuoy continue to register robust growth.

Operating margin was impacted due to un-favorable mix (lower growth of wheel) and increase in ad-spend.

Strong revenue growth in Soaps and Detergent Personal



Improvement in operating performance in the Soaps & Detergent



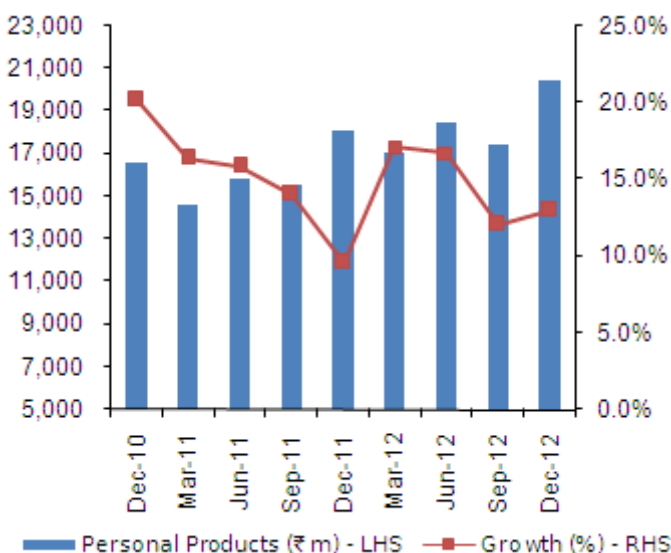
Source: Company, Dolat Research

Personal Products revenue growth

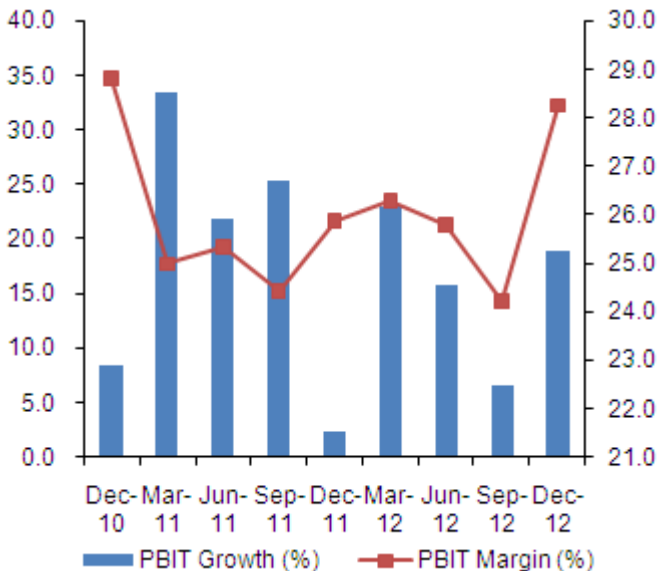
Personal Products revenue grew by 13% to ₹ 20.4bn and EBIT increased by 19% to ₹ 5.8bn as margins expanded by 140bps YoY to 28.3%.

Margin improve was led by premiumisation aided by strong growth in the Hair care portfolio which witness launch of Hair oil – Dove Elixir and Oral care which registered a volume led double digit growth.

Trend in Personal Products revenue growth



Trend in operating performance of Personal Products



Source: Company, Dolat Research

INCOME STATEMENT

₹ mn

Particulars	Mar12	Mar13E	Mar14E	Mar15E
Net Sales	217,367	252,822	289,381	330,071
Other operating income	3,838	6,152	6,976	7,912
Other income	2,692	5,775	5,469	6,109
Total Income	223,897	264,748	301,826	344,092
Total Expenditure	188,308	218,666	248,706	282,190
Other Expenses	1,017	1,040	1,127	1,223
EBIDTA (Excl. Other Income)	32,897	40,308	47,651	55,793
EBIDTA (Incl. Other Income)	35,589	46,082	53,120	61,901
Interest	12	200	160	130
Gross Profit	35,577	45,882	52,960	61,771
Depreciation	2,161	2,313	2,422	2,512
Profit Before Tax & EO Items	33,416	43,570	50,538	59,259
Extra Ordinary Exps/(Income)	(1,189)	(5,031)	0	0
Profit Before Tax	34,605	48,601	50,538	59,259
Tax	7,776	10,675	13,393	18,963
Net Profit	25,640	32,895	37,145	40,296

BALANCE SHEET

Particulars	Mar12	Mar13E	Mar14E	Mar15E
Sources of Funds				
Equity Capital	2,162	2,214	2,214	2,214
Share Premium	387	387	387	387
Other Reserves	32,580	27,759	39,001	53,393
Net Worth	35,129	30,360	41,602	55,995
Deferred Tax Liability	(2,142)	(2,293)	(2,453)	(2,625)
Total Capital Employed	32,987	28,068	39,149	53,369

Applications of Funds

Gross Block	38,117	39,617	41,117	42,617
Less: Accumulated Depreciation	16,642	18,955	21,377	23,889
Net Block	21,475	20,662	19,740	18,728
Capital Work in Progress	2,051	1,500	1,500	1,500
Investments	37,812	35,277	50,425	70,487

Current Assets, Loans & Advances

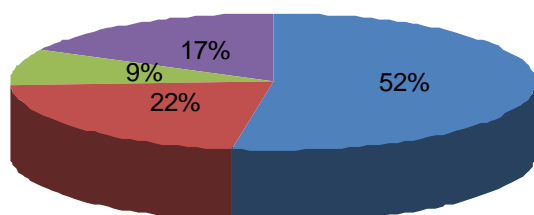
Inventories	25,167	33,710	38,584	44,010
Sundry Debtors	6,790	7,966	9,117	10,400
Cash and Bank Balance	4,974	4,465	5,530	5,105
Loans and Advances	8,820	9,231	9,668	10,132
Other Current Assets	353	370	389	408
<i>sub total</i>	46,102	55,742	63,288	70,054

Less : Current Liabilities & Provisions

Creditors	37,826	45,180	51,125	57,965
Other Liabilities	25,533	26,875	29,725	32,866
Provisions	11,094	13,059	14,954	16,569
<i>sub total</i>	74,454	85,113	95,805	107,400
Net Current Assets	(28,351)	(29,371)	(32,517)	(37,346)

Total Assets	32,986	28,068	39,149	53,369
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E-estimates

Shareholding Pattern as on Dec'12 (%)


■ Promoter ■ FII ■ DII ■ Public / Others

CASH FLOW

Particulars	Mar12	Mar13E	Mar14E	Mar15E
Profit before tax	34,605	48,601	50,538	59,259
Depreciation & w.o.	2,161	2,313	2,422	2,512
Net Interest Exp	12	200	160	130
Direct taxes paid	(7,776)	(10,675)	(13,393)	(18,963)
Change in Working Capital	4,354	512	4,210	4,405
(A) CF from Opt. Activities	33,355	40,950	43,937	47,343
Capex	(406)	(949)	(1,500)	(1,500)
Free Cash Flow	32,949	40,002	42,437	45,843
Inc./ (Dec.) in Investments	(11,704)	2,535	(15,148)	(20,062)
(B) CF from Invst. Activities	(12,110)	1,586	(16,648)	(21,562)
Issue of Equity/ Preference	381	53	0	0
Interest exp net	(12)	(200)	(160)	(130)
Dividend Paid (Incl. Tax)	(18,967)	(42,741)	(25,904)	(25,904)
Other	(560)	(51)	(162)	(172)
(C) CF from Financing	(19,158)	(42,940)	(26,225)	(26,206)
Net Change in Cash	2,087	(403)	1,064	(425)
Opening Cash balances	2,784	4,974	4,465	5,530
Closing Cash balances	4,974	4,465	5,530	5,105

E-estimates

IMPORTANT RATIOS

Particulars	Mar12	Mar13E	Mar14E	Mar15E
(A) Measures of Performance (%)				
Contribution Margin	46.9	47.8	48.6	49.1
EBIDTA Margin (excl. O.I.)	15.1	15.9	16.5	16.9
EBIDTA Margin (incl. O.I.)	15.9	17.4	17.6	18.0
Interest / Sales	0.0	0.1	0.1	0.0
Gross profit margin	15.9	17.3	17.5	18.0
Tax/PBT	22.5	22.0	26.5	32.0
Net Profit Margin	11.5	12.4	12.3	11.7

(B) As Percentage of Net Sales

Raw Material	54.0	53.5	52.6	52.1
Employee Expenses	5.1	5.2	5.2	5.2
Advertising exp	12.1	12.7	12.8	12.9
Selling & Administrative Expenses	10.7	10.7	11.1	11.1
Manufacturing exp	4.2	4.0	3.9	3.8
Other Expenses	0.5	0.4	0.4	0.4

(C) Measures of Financial Status

Interest Coverage (x)	2,965.7	230.4	332.0	476.2
Debtors Period (days)	11	12	12	12
Closing stock (days)	42	49	49	49
Inventory Turnover Ratio (x)	8.6	7.5	7.5	7.5
Fixed Assets Turnover (x)	5.7	6.4	7.0	7.7
Working Capital Turnover (x)	(7.7)	(8.6)	(8.9)	(8.8)
Non Cash Working Capital (₹ Mn)	(33,325)	(33,837)	(38,046)	(42,451)

(D) Measures of Investment

EPS (₹) (excl EO)	11.9	14.9	16.8	18.2
EPS (₹)	12.4	17.1	16.8	18.2
CEPS (₹)	12.9	15.9	17.9	19.3
DPS (₹)	7.5	16.5	10.0	10.0
Dividend Payout (%)	60.4	96.3	59.6	54.9
Profit Ploughback (%)	39.6	3.7	40.4	45.1
Book Value (₹)	16.3	13.7	18.8	25.3
RoANW (%)	83.1	100.5	103.2	82.6
RoACE (%)	90.2	111.9	110.9	87.3
RoAIC (%) (Excl Cash & Invest.)	134.4	169.6	177.2	145.1

(E) Valuation Ratios

CMP (₹)	481	481	481	481
P/E (x)	40.5	32.4	28.7	26.4
Market Cap. (₹ Mn.)	1,039,682	1,064,934	1,064,934	1,064,934
MCap/ Sales (x)	4.8	4.2	3.7	3.2
EV (₹ Mn.)	997,984	1,026,279	1,010,067	990,429
EV/Sales (x)	4.6	4.1	3.5	3.0
EV/EBDITA (x)	30.3	25.5	21.2	17.8
P/BV (x)	29.6	35.1	25.6	19.0
Dividend Yield (%)	1.6	3.4	2.1	2.1

E-estimates

BUY	Upside above 20%
ACCUMULATE	Upside above 5% and up to 20%
REDUCE	Upside of upto 5% or downside of upto 15%
SELL	Downside of more than 15%

Analyst	Sector/Industry/Coverage	E-mail	Tel.+91-22-4096 9700
Amit Khurana, CFA	Director - Research	amit@dolatcapital.com	91-22-40969745
Amit Purohit	Consumer	amitp@dolatcapital.com	91-22-40969724
Bhavin Shah	Pharma & Agro Chem	bhavin@dolatcapital.com	91-22-40969731
Mayur Milak	Auto & Auto Ancillary	mayur@dolatcapital.com	91-22-40969749
Nehal Shah	Midcaps	nehals@dolatcapital.com	91-22-40969753
Priyank Chandra	Oil & Gas	priyank@dolatcapital.com	91-22-40969737
Rahul Jain	IT Services	rahul@dolatcapital.com	91-22-40969754
Rajiv Pathak	Financial	rajiv@dolatcapital.com	91-22-40969750
Ram Modi	Metals & Mining	ram@dolatcapital.com	91-22-40969756
Prachi Save	Derivative Analyst	prachi@dolatcapital.com	91-22-40969733

Associates	Sector/Industry/Coverage	E-mail	Tel.+91-22-4096 9700
Dhaval S. Shah	Engineering & Capital Goods	dhaval@dolatcapital.com	91-22-40969726
Pranav Joshi	Financials	pranavj@dolatcapital.com	91-22-40969706

Equity Sales/Dealing	Designation	E-mail	Tel.+91-22-4096 9797
Purvag Shah	Principal	purvag@dolatcapital.com	91-22-40969747
Janakiram Karra	Director - Institutional Sales	janakiram@dolatcapital.com	91-22-40969712
Vikram Babulkar	Director - Institutional Sales	vikram@dolatcapital.com	91-22-40969746
Kapil Yadav	AVP - Institutional Sales	kapil@dolatcapital.com	91-22-40969735
Parthiv Dalal	AVP - Institutional Sales	parthiv@dolatcapital.com	91-22-40969705
Chirag Makati	AVP - Sales Trading	chiragm@dolatcapital.com	91-22-40969702
Jatin Padharia	Institutional Sales - FII	jatin@dolatcapital.com	91-22-40969748
Aadil R. Sethna	Head of Derivatives	aadil@dolatcapital.com	91-22-40969708
P. Sridhar	Head Dealing - Equities	sridhar@dolatcapital.com	91-22-40969728
Chandrakant Ware	Senior Sales Trader	chandrakant@dolatcapital.com	91-22-40969707
Jitendra Tolani	Sales Trader	jitendrat@dolatcapital.com	91-22-40969734

Dolat Capital Market Pvt. Ltd.

20, Rajabhadur Mansion, 1st Floor, Ambalal Doshi Marg, Fort, Mumbai - 400 001

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