

## EARNINGS REVIEW

**Hindustan Unilever (HLL.BO)**

Sell

Equity Research

**Below expectations: Weak volumes, increased royalty payments****What surprised us**

Hindustan Unilever (HUL) reported 3QFY13 profit before tax (before exceptional items) of Rs10.9 bn (4% below GSe, 12% yoy) on account of lower margins for soaps and detergents. Key highlights: 1) HUL reported 5% volume growth vs GSe 7% due to lower volume growth in Wheel, disruption in FAL volumes (price increase to Rs8 from Rs7) and higher base effect in Dove sachets; 2) GM was down yoy due to higher proportion of sales from Soaps & Detergents vs. Personal Products, which have higher gross margins; 3) Higher gross margins for Soaps & Detergents were offset by increased A&P spend, leading to overall Soaps & Detergents margins missing our estimates by 158bp; 4) HUL's board has approved an increase in royalty payments to 3.15% of sales by FY18 from 1.4% currently. Payments would be increased in a phased manner +50bp in FY14 and +30-70bp until FY18; and 5) Mgmt guided for a tax rate of 26.5% in FY14 and 29%-33% in FY15.

**What to do with the stock**

We retain our Sell rating on HUL. We revise our FY13-15E EPS by -6% to +3%, adjusting for higher other income for FY13 and increased royalty/taxes for FY14/15E. Thus, our 12-month target price moves down to Rs414 (from Rs423), still based on 26X FY14E P/E. We now estimate near-term volume growth of 7-7.5%, in line with the 7.2% long-term average. We estimate 8.4% EPS CAGR over FY13-15E, lower than 11.9% over FY08-13E. Despite this, HUL trades at expensive levels at 31X 1-yr fwd EPS, over 1SD above the 10-year average. Key risks: (1) Sharp margin rebound in laundry segment; (2) higher-than-expected volume.

**Hindustan Unilever – 3QFY13 results summary**

Rs mn	3QFY13 Actual	3QFY13 GS est.	var	3QFY12 Actual	yoy	2QFY13 Actual	qoq
Net sales	64,337	66,092	-3%	58,527	10%	61,554	5%
PAT	8,714	8,918	-2%	7,538	16%	8,069	8%

Source: Company data, Goldman Sachs Research estimates.

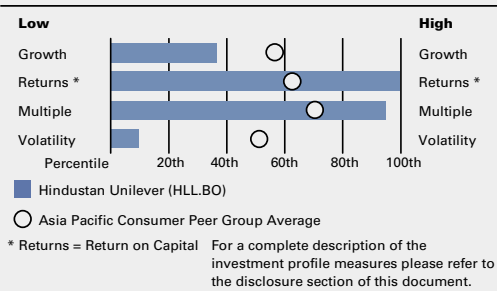
**INVESTMENT LIST MEMBERSHIP**

Asia Pacific Sell List

**Coverage View: Neutral**

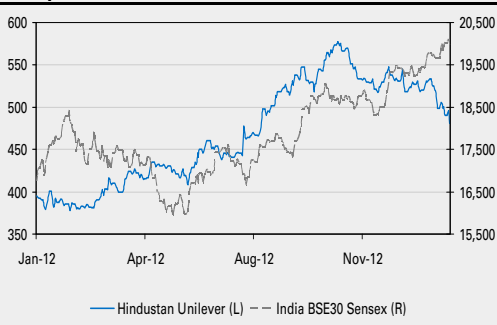
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**Investment Profile**

Key data	Current
Price (Rs)	481.55
12 month price target (Rs)	414.00
Market cap (Rs mn / US\$ mn)	1,050,173.7 / 19,514.5
Foreign ownership (%)	--

	3/12	3/13E	3/14E	3/15E
<b>EPS (Rs) New</b>	<b>11.90</b>	<b>14.50</b>	<b>15.90</b>	<b>17.05</b>
EPS revision (%)	0.0	3.0	(2.3)	(6.4)
EPS growth (%)	12.0	21.9	9.6	7.2
<b>EPS (dil) (Rs) New</b>	<b>12.45</b>	<b>17.28</b>	<b>15.90</b>	<b>17.05</b>
P/E (X)	40.5	33.2	30.3	28.3
P/B (X)	29.6	24.3	21.1	17.6
EV/EBITDA (X)	22.3	25.3	22.2	19.6
Dividend yield (%)	1.6	2.8	2.1	2.3
ROE (%)	87.6	95.7	74.5	68.0
CROCI (%)	143.8	162.7	121.4	113.1

**Price performance chart**

Share price performance (%)	3 month	6 month	12 month
Absolute	(15.4)	8.0	23.2
Rel. to India BSE30 Sensex	(20.4)	(7.3)	3.2

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 1/22/2013 close.

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# Hindustan Unilever: Summary Financials

Profit model (Rs mn)	3/12	3/13E	3/14E	3/15E	Balance sheet (Rs mn)	3/12	3/13E	3/14E	3/15E
<b>Total revenue</b>	<b>217,356.0</b>	<b>252,534.3</b>	<b>284,744.0</b>	<b>319,640.7</b>	Cash & equivalents	18,300.4	22,143.0	25,874.2	35,047.0
Cost of goods sold	(119,560.1)	(136,960.3)	(153,574.8)	(171,437.1)	Accounts receivable	6,789.9	12,277.3	13,843.2	15,539.7
SG&A	(70,872.7)	(84,801.3)	(95,163.1)	(107,119.2)	Inventory	25,166.5	38,348.9	43,000.9	48,002.4
R&D	--	--	--	--	Other current assets	5,210.4	5,210.4	5,210.4	5,210.4
Other operating profit/(expense)	3,807.7	6,900.0	6,900.0	6,900.0	<b>Total current assets</b>	<b>55,467.2</b>	<b>77,979.6</b>	<b>87,928.7</b>	<b>103,799.6</b>
<b>EBITDA</b>	<b>32,913.5</b>	<b>40,208.4</b>	<b>45,765.3</b>	<b>51,193.9</b>	Net PP&E	23,629.2	26,144.2	28,979.9	32,163.1
Depreciation & amortization	(2,182.5)	(2,535.7)	(2,859.2)	(3,209.6)	Net intangibles	0.0	0.0	0.0	0.0
<b>EBIT</b>	<b>30,731.0</b>	<b>37,672.7</b>	<b>42,906.1</b>	<b>47,984.3</b>	Total investments	26,524.5	26,524.5	26,524.5	26,524.5
Interest income	1,177.0	549.0	664.3	776.2	Other long-term assets	3,961.8	3,961.8	3,961.8	3,961.8
Interest expense	(12.4)	0.0	0.0	0.0	<b>Total assets</b>	<b>109,582.7</b>	<b>134,610.0</b>	<b>147,394.9</b>	<b>166,449.0</b>
Income/(loss) from uncons. subs.	0.0	0.0	0.0	0.0	Accounts payable	46,229.6	52,532.7	58,905.4	65,756.7
Others	1,606.1	5,200.0	3,500.0	3,500.0	Short-term debt	0.0	0.0	0.0	0.0
<b>Pretax profits</b>	<b>33,501.6</b>	<b>43,421.7</b>	<b>47,070.4</b>	<b>52,260.5</b>	Other current liabilities	18,257.4	29,217.4	29,212.1	31,630.1
Income tax	(7,776.3)	(12,069.8)	(12,709.0)	(15,416.9)	<b>Total current liabilities</b>	<b>64,487.0</b>	<b>81,750.1</b>	<b>88,117.5</b>	<b>97,386.8</b>
Minorities	0.0	0.0	0.0	0.0	Long-term debt	0.0	0.0	0.0	0.0
<b>Net income pre-preferred dividends</b>	<b>25,725.3</b>	<b>31,351.9</b>	<b>34,361.4</b>	<b>36,843.7</b>	Other long-term liabilities	9,966.4	9,966.4	9,966.4	9,966.4
Preferred dividends	0.0	0.0	0.0	0.0	Total long-term liabilities	9,966.4	9,966.4	9,966.4	9,966.4
<b>Net income (pre-exceptionals)</b>	<b>25,725.3</b>	<b>31,351.9</b>	<b>34,361.4</b>	<b>36,843.7</b>	<b>Total liabilities</b>	<b>74,453.4</b>	<b>91,716.5</b>	<b>98,083.9</b>	<b>107,353.2</b>
Post-tax exceptionals	1,188.7	6,000.0	0.0	0.0	<b>Preferred shares</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
<b>Net income</b>	<b>26,914.0</b>	<b>37,351.9</b>	<b>34,361.4</b>	<b>36,843.7</b>	<b>Total common equity</b>	<b>35,129.3</b>	<b>42,893.5</b>	<b>49,311.0</b>	<b>59,095.8</b>
EPS (basic, pre-exception) (Rs)	11.91	14.51	15.90	17.05	Minority interest	0.0	0.0	0.0	0.0
EPS (basic, post-exception) (Rs)	12.46	17.29	15.90	17.05	<b>Total liabilities &amp; equity</b>	<b>109,582.7</b>	<b>134,610.0</b>	<b>147,394.9</b>	<b>166,449.0</b>
EPS (diluted, post-exception) (Rs)	12.45	17.28	15.90	17.05	<b>BVPS (Rs)</b>	<b>16.25</b>	<b>19.84</b>	<b>22.81</b>	<b>27.34</b>
DPS (Rs)	7.50	13.51	10.00	11.01	<b>Ratios</b>	<b>3/12</b>	<b>3/13E</b>	<b>3/14E</b>	<b>3/15E</b>
Dividend payout ratio (%)	60.2	78.1	62.9	64.5	CROCI (%)	143.8	162.7	121.4	113.1
Free cash flow yield (%)	3.5	3.2	3.0	3.5	ROE (%)	87.6	95.7	74.5	68.0
<b>Growth &amp; margins (%)</b>	<b>3/12</b>	<b>3/13E</b>	<b>3/14E</b>	<b>3/15E</b>	ROA (%)	25.6	30.6	24.4	23.5
Sales growth	12.0	16.2	12.8	12.3	ROACE (%)	185.5	164.7	153.3	152.9
EBITDA growth	21.9	22.2	13.8	11.9	Inventory days	81.3	84.6	96.7	96.9
EBIT growth	24.0	22.6	13.9	11.8	Receivables days	13.6	13.8	16.7	16.8
Net income growth	16.7	38.8	(8.0)	7.2	Payable days	142.7	131.6	132.4	132.7
EPS growth	17.3	38.8	(8.0)	7.2	Net debt/equity (%)	(52.1)	(51.6)	(52.5)	(59.3)
Gross margin	45.0	45.8	46.1	46.4	Interest cover - EBIT (X)	NM	NM	NM	NM
EBITDA margin	15.1	15.9	16.1	16.0	<b>Valuation</b>	<b>3/12</b>	<b>3/13E</b>	<b>3/14E</b>	<b>3/15E</b>
EBIT margin	14.1	14.9	15.1	15.0	P/E (analyst) (X)	40.5	33.2	30.3	28.3
<b>Cash flow statement (Rs mn)</b>	<b>3/12</b>	<b>3/13E</b>	<b>3/14E</b>	<b>3/15E</b>	P/B (X)	29.6	24.3	21.1	17.6
Net income pre-preferred dividends	25,725.3	31,351.9	34,361.4	36,843.7	EV/EBITDA (X)	22.3	25.3	22.2	19.6
D&A add-back	2,182.5	2,535.7	2,859.2	3,209.6	EV/GCI (X)	34.9	37.0	30.7	27.3
Minorities interests add-back	0.0	0.0	0.0	0.0	Dividend yield (%)	1.6	2.8	2.1	2.3
Net (inc)/dec working capital	2,036.3	(1,406.6)	149.4	2,571.2					
Other operating cash flow	(2,436.5)	0.0	0.0	0.0					
<b>Cash flow from operations</b>	<b>28,696.4</b>	<b>38,481.0</b>	<b>37,370.0</b>	<b>42,624.5</b>					
Capital expenditures	(2,522.1)	(5,050.7)	(5,694.9)	(6,392.8)					
Acquisitions	(6,935.4)	0.0	0.0	0.0					
Divestitures	0.0	0.0	0.0	0.0					
Others	0.0	0.0	0.0	0.0					
<b>Cash flow from investments</b>	<b>(9,457.5)</b>	<b>(5,050.7)</b>	<b>(5,694.9)</b>	<b>(6,392.8)</b>					
Dividends paid (common & pref)	(17,546.3)	(29,587.7)	(27,943.9)	(27,058.8)					
Inc/(dec) in debt	0.0	0.0	0.0	0.0					
Common stock issuance (repurchase)	335.5	0.0	0.0	0.0					
Other financing cash flows	(12.4)	0.0	0.0	0.0					
<b>Cash flow from financing</b>	<b>(17,223.2)</b>	<b>(29,587.7)</b>	<b>(27,943.9)</b>	<b>(27,058.8)</b>					
<b>Total cash flow</b>	<b>2,015.7</b>	<b>3,842.6</b>	<b>3,731.2</b>	<b>9,172.8</b>					

Note: Last actual year may include reported and estimated data.  
Source: Company data, Goldman Sachs Research estimates.

## Analyst Contributors

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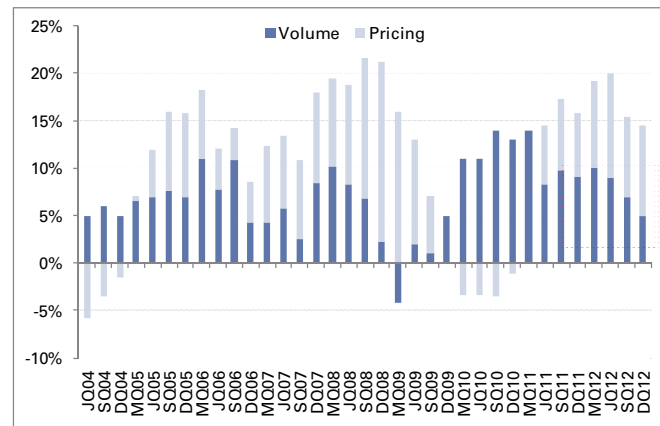
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**Exhibit 1: 3QFY13 profit before tax (before exceptionals) was 4% below GSe, +12% yoy**  
 3QFY13 segment results

Segment results Rs mn	3QFY13 Actual	3QFY13 GS est.	var bps	3QFY12 Actual	yoy bps	2QFY13 Actual	qoq bps
<b>Revenue</b>							
Soaps and detergents	31,712	31,752	0%	26,460	20%	31,762	0%
Personal Products	20,489	21,880	-6%	18,862	9%	17,445	17%
Beverages	7,929	7,508	6%	6,704	18%	7,196	10%
Processed foods	3,301	3,585	-8%	3,064	8%	3,663	-10%
Exports	-	-	NM	3,375	NM	-	NM
Others	2,902	2,357	23%	982	195%	2,884	1%
<b>Total (includes sevice income)</b>	<b>66,334</b>	<b>67,082</b>	<b>-1%</b>	<b>59,446</b>	<b>12%</b>	<b>62,949</b>	<b>5%</b>
<b>EBIT</b>							
Soaps and detergents	3,937	4,445	-11%	3,559	11%	4,536	-13%
Personal Products	5,789	5,798	0%	4,881	19%	4,226	37%
Beverages	1,404	1,201	17%	1,052	33%	1,031	36%
Processed foods	(26)	(36)	-27%	(60)	-56%	9	NM
Exports	-	-	NM	446	NM	-	NM
Others	(186)	(47)	NM	(103)	NM	21	NM
<b>Total</b>	<b>10,917</b>	<b>11,362</b>	<b>-4%</b>	<b>9,776</b>	<b>12%</b>	<b>9,822</b>	<b>11%</b>
<b>Margins</b>							
Soaps and detergents	12.4%	14.0%	(158)	13.5%	(103)	14.3%	(186)
Personal Products	28.3%	26.5%	175	25.9%	237	24.2%	403
Beverages	17.7%	16.0%	170	15.7%	201	14.3%	338
Processed foods	-0.8%	-1.0%	20	-1.9%	115	0.2%	(104)
Exports	NA	NA	NA	13.2%	NA	NA	NA
Others	-6.4%	-2.0%	(442)	-10.5%	403	0.7%	(713)
<b>Total</b>	<b>16.5%</b>	<b>16.9%</b>	<b>(48)</b>	<b>16.4%</b>	<b>1</b>	<b>15.6%</b>	<b>85</b>

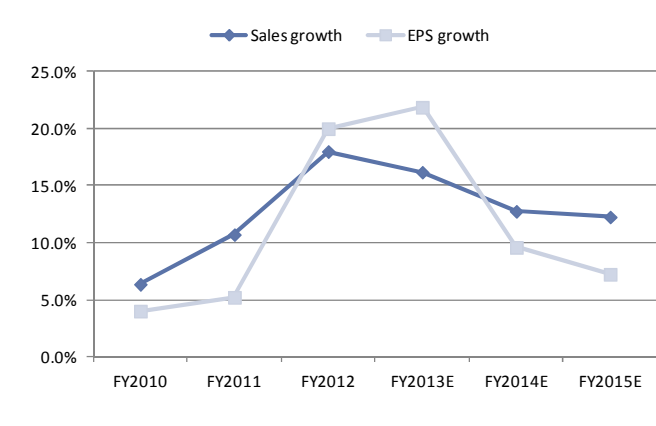
Source: Company data, Goldman Sachs Research estimates.

**Exhibit 2: HUL volume growth has declined to trend**  
 Quarterly volume and value growth



Source: Company data, Goldman Sachs Research.

**Exhibit 3: Sales and EPS growth to decline from FY14E**  
 Sales growth and EPS growth



Source: Company data, Goldman Sachs Research estimates.

**Exhibit 4: Royalty expenses and tax set to rise**

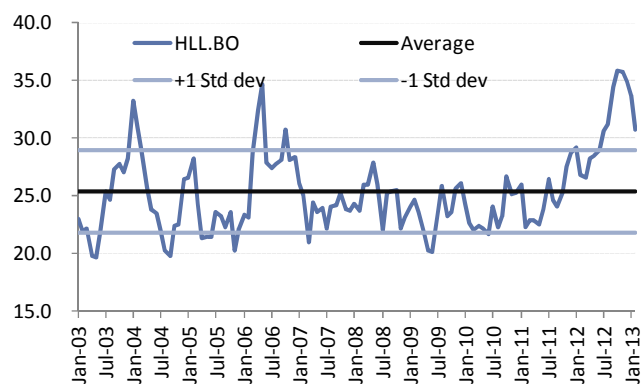
Common size P&L (Sales indexed to 100)

Common size P&L	FY2012	FY2012	FY2013E	FY2014E	FY2015E
Sales	100.0	100.0	100.0	100.0	100.0
COGS	(51.8)	(54.0)	(53.2)	(52.9)	(52.6)
<b>Royalty</b>	<b>(1.4)</b>	<b>(1.3)</b>	<b>(1.4)</b>	<b>(1.9)</b>	<b>(2.4)</b>
Other expenses	(33.1)	(29.5)	(29.4)	(29.0)	(28.9)
EBITDA	13.7	15.1	15.9	16.1	16.0
D&A	(1.1)	(1.0)	(1.0)	(1.0)	(1.0)
EBIT	12.6	14.1	14.9	15.1	15.0
Net interest/Other income	1.5	1.3	2.3	1.5	1.3
PBT	14.1	15.4	17.2	16.5	16.3
<b>Tax</b>	<b>(3.0)</b>	<b>(3.6)</b>	<b>(4.8)</b>	<b>(4.5)</b>	<b>(4.8)</b>
PAT	11.1	11.8	12.4	12.1	11.5

Source: Company data, Goldman Sachs Research estimates.

**Exhibit 5: Trading more than 1SD above long-term mean**

Rolling 12-month fwd P/E



Source: Datastream, Goldman Sachs Research estimates.

# Disclosure Appendix

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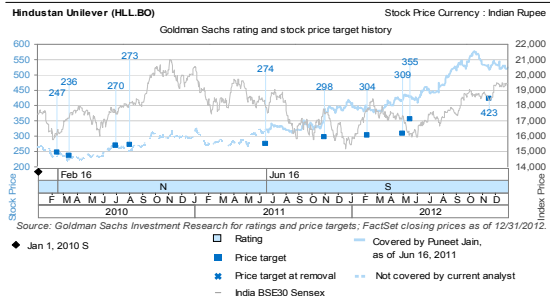
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