Institutional Equities
India Research

Jyothy Laboratories

MANAGEMENT MEET UPDATE

Bloomberg: JYL IN
Reuters: JYOI.BO

BUY

Better Earning Visibility; Boosts Confidence

Jyothy Laboratories (Jyothy) has come out well from the phase marked with tremendous pressure in terms of acquisition of Henkel India (Henkel), slower growth of core business due to distribution restructuring and liability of interest payment. Jyothy's H2FY12 performance was way ahead of H1FY12 performance with improved visibility in business, which it lost previously. Hence, the stock has run up by 45% in past 3 months. With a view to getting Jyothy's outlook, we recently met the Management of the Company. We observed that still there is enough scope for the stock, as better performance in ensuing quarters would drive the stock further.

Core business is in line, Exo is like "X" effect

In Jyothy's core business, Exo is placed as a key business driver. Exo clocked strong growth of 43% in FY12 owing to launch in four new states. Its Management plans pan-India launch of Exo by FY13-end, which we believe to help Exo to maintain its high growth momentum, going forward. Besides, the Company is confident of sustaining the market share of Ujala Supreme, as its Management feels that HUL's recently-launched Rin Fabric Whitener won't affect their business much. Its Management expects that Rin Fabric Whitener would find new consumers, who don't use Ujala Supreme.

Henkel – "Sleep is over"

After several years of poor performance, Henkel has started showing good numbers post acquisition by Jyothy. Prior to acquisition, Henkel was incurring loss even at EBITDA level, which has turned into healthy EBITDA margin in the aftermath of acquisition. Now, we expect that its sales growth to improve, as the Management plans to expand Henkel's product reach to 5-6 lakh outlets by FY13-end from 2 lakh outlets now.

Outlook & Valuation

We believe that the visibility in business scenario would improve with better performance in ensuing quarters. The stock has already run up by 42% in past 3 months owing to improved clarity in business. However, we believe there is still enough scope for appreciation in stock price, as the likely earnings growth would also play a key role in stock's performance, going forward. We give 17x multiple on FY14E earnings, which is 30% discount to the FMCG sector. With our target multiple, we derive target price of Rs. 290 per share, and hence we maintain our "BUY" recommendation on the stock.

Key Financials (Consolidated)

Y/E Mar (Rs mn)	FY10	FY11	FY12P	FY13E	FY14E
Revenue	5,975	6,174	9,130	13,795	16,414
EBITDA	929	727	841	1,810	2,277
Net Profits (Adj)	743	688	536	954	1,374
EPS (Rs)	9.2	8.5	6.6	11.8	17.0
PER (x)	25.6	27.7	35.5	19.9	13.9
EV/EBITDA (x)	19.3	22.4	27.4	12.3	9.4
RoE %	19.2	10.9	8.6	14.0	17.6

Source: Company, Karvy Institutional Research

Recommendation

CMP:	Rs238
Target Price:	Rs290
Upside (%)	22%

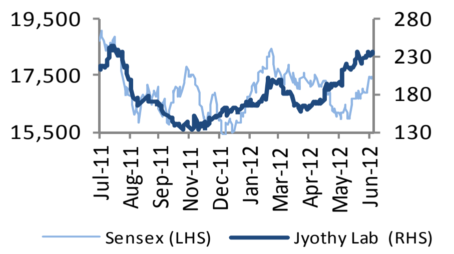
Stock Information

Market Cap. (Rs bn / US$ mn)	19/349
52-week High/Low (Rs)	252/125
3m ADV (Rs mn /US$ mn)	25/0.4
Beta	0.7
Sensex/ Nifty	17,472/5,302
Share outstanding (mn)	81

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	11.4	45.2	11.8	47.6
Rel. to Sensex	2.2	45.3	20.0	30.5

Performance



Source: Bloomberg, Karvy Institutional Research

Analysts Contact
Naveen Trivedi
022-6184 4316
naveen.trivedi@karvy.com

Meeting Key Takeaways

A. Core Business Outlook

Our Query: How would you see the competition from HUL's Rin Fabric Whitener?

Management Insight

- Its Management seems to be confident and assured that till now there is no sign of pressure. However, the Company remains watchful and plans to change few things in Ujala Supreme. But due to competition, the Company didn't disclose the changes, it plans to undertake. However, the Management assured that it won't emulate the competitor's strategy of aggressive marketing, rather focus more towards the development of the product.
- Its Management expects that only Rin Detergent users would move to Rin Fabric Whitener therefore should not impact the existing consumer base of Ujala Supreme.
- The Management has assured that the Company won't take any price cut in future to mitigate the competition.
- The Management expects that the competition would spur growth in the segment.

Karvy Comment

- We are not worried for the medium-term outlook of Ujala Whitener considering brand's large reach and strong brand positioning. However, we are cautious over the long-term outlook of the product and any performance issue on this front would impact the overall profitability of the Company.
- We are not fully convinced with the Management's assumption and expect that Rin Fabric Whitener would have certain impact on the demand for Jyothy's product in urban area.
- We agree with the Management's stance for not cutting the price, as that would only hurt the Company. The category growth is already at low single digit therefore by cutting the price, won't have any significant impact on the volume. As well as, Jyothy would have to sacrifice significant amount of profitability which they can't afford while Rin Fabric Whitener being a negligible product, HUL could bear any loss for long period.
- As Ujala Supreme is already available widely, we don't expect any major scope for growth on higher reach.

Our Query: What has been right for Exo to achieve such stellar performance in the past few quarters and what is the outlook?

Management Insight

- Exo was only available in Kerala till FY10-end, which in the phased manner launched in Delhi, Punjab, Haryana and West Bengal. The entry into newer markets has proved to be immensely beneficial for the Company. Besides, during FY11, Jyothy has also launched Exo in the round shape and consumer acceptance for it was extraordinary. Round shape Exo contributed 50% to the total sales of Exo bar in FY12. The Company plans for pan-India launch of Exo by FY13-end.
- In FY12, Exo witnessed 43% growth, which was ahead of the category growth to the tune of 21%. Its Management is very bullish on the growth outlook of category on account of shift from local style of utensils washing using ashes

and dust to the use of standardized utensils cleaners. The Management expects that Exo would continue to show stellar performance in next 2-3 years.

- Exo fetches ~35% gross margin and ~10-12% EBITDA margin. Its Management expects ~500bps rise in EBITDA margin in coming 2 years on the back of better scale of operations.

Karvy Comment

- The growth that Exo seen in the past one year was remarkable and as the Management plans to expand the brand's reach, we expect Exo to maintain high growth momentum, going forward. Strong category growth would also help Exo in achieving strong growth, going forward.

Our Query: What is the growth and profitability outlook of Maxo?

Management Insight

- Coil repellent will continue to dominate Jyothy's overall repellent sales; however, going forward the liquid repellent (8-10% of total repellent sales) would show strong growth. As coil repellent fetches mere 10% gross margin, Maxo incurs losses at EBITDA level. Liquid repellent is high-margin product (~45% gross margin) and its higher contribution in sales would improve the overall profitability. Besides, its Management also expects gross margin form coil to improve by 500bps to ~15% within a year.

Karvy Comment

- We are not very optimistic about the 500bps rise in Maxo coil gross margin in the near-term, as this is a settled brand and we expect the Company should have tried all options from raw material sourcing to better manufacturing process. Though we see moderate (100-150 bps) rise in margin, we don't subscribe to management's expectation of 500bps rise in margin.

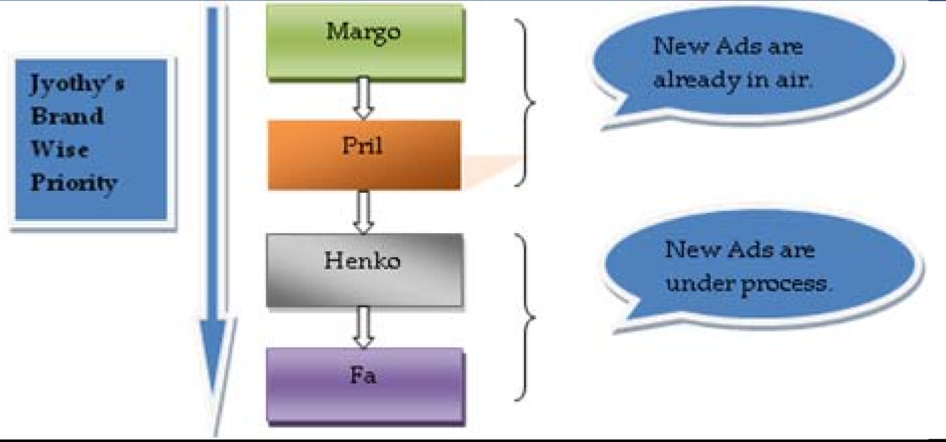
B. Henkel Outlook

Our Query: In Henkel, you guided for 25% volume growth in FY13, despite proposed 15% price-hike. What is your plan to achieve these numbers?

Management Insight

- Henkel's products were available at 2 lakh outlets, which would reach to 5-6 lakh outlets by FY13-end. Its Management expects expansion in the reach to start showing numbers from Q2FY13 onwards. It guided that Margo, Pril, Henko and Fa are in the focus area in the same order.

Exhibit 1: Jyothy's Brand Wise Priority for Henkel's Product



Source: Company, Karvy Institutional Research

Karvy Comment

- Henkel's low volume base of the previous year would also help in achieving strong volume growth guidance. We expect 22% sales CAGR in FY12-14E period, owing to better distribution reach and repositioning of certain brands.

Our Query: Post acquisition of Henkel, what would be the effective tax rate as Henkel has Rs. 5 bn accumulated loss?

Management Insight

- Jyothy would continue to pay MAT only which is at 21%. The Company can avail benefits of accumulated loss for the next 8 years.

Our Query: What is the status of the CSD sales?

Management Insight

- The impact of CSD sales was largely on Henkel's sales in which CSD contributes 22% to the total sales. There was ~10% decline in CSD sales in Q1FY13. However, its Management expects that the CSD sales would be normal in Q2FY13.

Our Query: Do you have debt restructuring plan in near to medium-term?

Management Insight

- No. There is no debt restructuring plan in near to medium-term. Jyothy would consider selling its idle assets only after the merger of Henkel, which is expected by Dec'12. Therefore, interest outgo would be ~Rs. 600 mn for the year.

"Rationalisation of distributors"

Jyothy plans to rationalize the distributor size to 2,000 from current 7,000 within a year and expects that it would help in controlling distribution cost and would improve the operational efficiency.

Mr. S. Raghunandan (CEO & Whole-time Director) has already experimented this idea at Dabur India and Paras Pharma during his tenure in those companies and confident that it would also help Jyothy.

"Karvy Comment"

- Rationalization of distributors can be helpful for the Company, in case the new distributors have enough muscle power to manage the big orders. Commitment of higher sales to distributors can provide bargain power to Jyothy in terms of negotiating the distribution margin.
- As the Company plans to do it in the phased manner, we would have to be very watchful of the implications of this rationalization. Therefore, as of now we consider it as neutral for the business, as with the chance of improvement in margin, there is also scope for reduction in sales.

Business Mix & Outlook

Substantial Change in Business Mix

Post the acquisition of Henkel India, Jyothy has decreased its dependence on Ujala Supreme, as the Company has multiple options to drive the business further.

We expect Ujala Supreme to maintain its profitability despite concerns over volume growth

In the core business, we are slightly cautious on the volume growth of Ujala Supreme especially in FY14, as HUL is marketing its recently-launched Rin Fabric Whitener. However, the Jyothy's Management is confident in maintaining the volume growth and expects Rin Fabric Whitener would only capture Rin detergent consumers, who don't use Ujala Supreme. As the Company doesn't plan emulate the similar marketing efforts, we believe that Ujala Supreme would maintain its profitability, going forward.

Core business would be supported by the exceptional growth of Exo

Besides, Exo has immerged as a key business driver and we expect with the expansion in the distribution reach, the high growth momentum would continue, going forward. Exo was available only in Kerala till FY10-end, which in the phased manner launched in Delhi, Punjab, Haryana and West Bengal. The entry into newer markets has proved to be immensely beneficial for the Company. Besides, in FY11, Jyothy has launched Exo in the round shape and consumer acceptance for has surprisingly very strong. Round shape Exo contributed 50% to the total sales of Exo bar in FY12. Jyothy plans to launch Exo in All-India by the end of FY13.

Maxo outlook is still not clear, management expects to improve Coil's gross margin by 500bps in a year

On Maxo, we feel that the Management was muted on its outlook and waiting for new strategy by the recently-joined business head. The Company expects better business from high-margin liquid repellent and plans to improve the gross margin of coil repellent by 500bps to 15% within a year.

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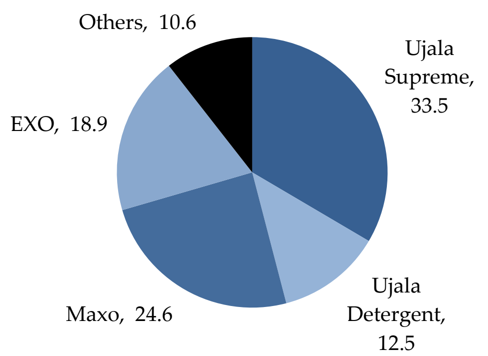
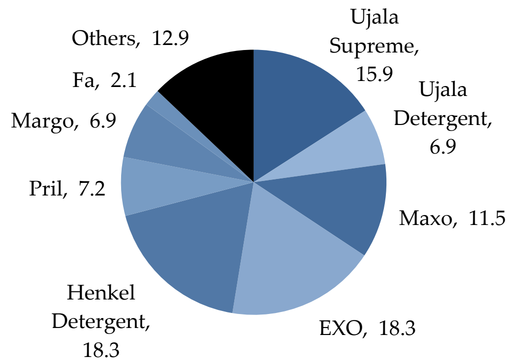
Exhibit 2: Jyothy's Sales Mix in FY11



Source: Company, Karvy Institutional Research

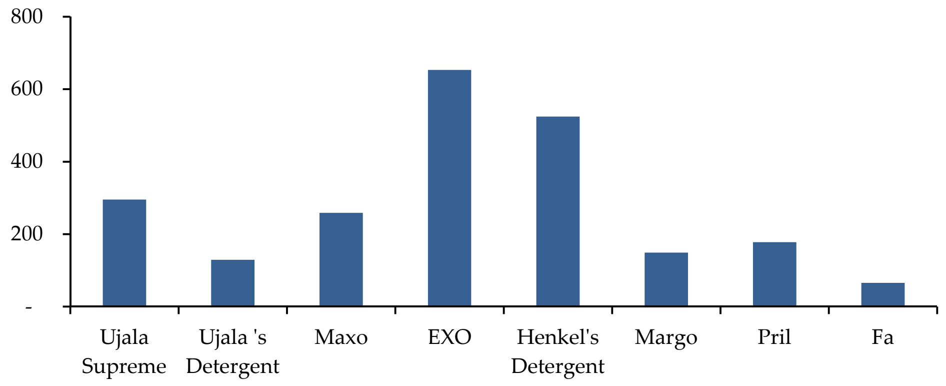
Exhibit 3: Jyothy's Sales Mix in FY14E



Source: Company, Karvy Institutional Research

Exo and Henkel's detergent would play a key role

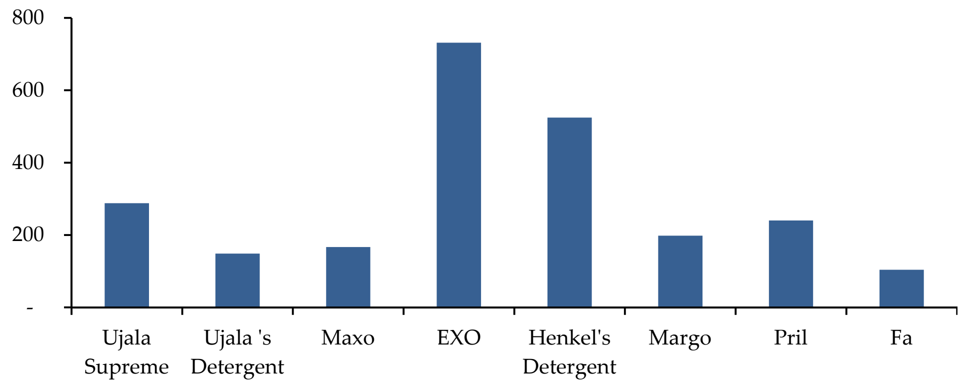
Exhibit 4: Breakup of Incremental Sales in FY13E (Rs mn)



Source: Company, Karvy Institutional Research

Margo, Pril and Fa would be critical from FY14 onwards

Exhibit 5: Breakup of Incremental Sales in FY14E (Rs mn)



Source: Company, Karvy Institutional Research

Outlook & Valuation

Jyothy has already run up by 45% in the past 3 months owing to improved business clarity. However, we believe that there is still enough room for appreciation in stock price, as the earnings growth would also play a key role in stock's performance, going forward. We give 17x multiple on FY14E earnings, which is 30% discount to the FMCG sector. We believe this discount at the current juncture is justified owing to Jyothy's low RoE profile. With our target multiple, we derive target price of Rs. 290 per share, and hence we maintain our **"BUY"** recommendation on the stock.

Exhibit 6: Peer Comparison

	CMP	Mkt Cap	Net Sales			EBITDA Margin			PAT Growth (%)			RoE (%)			P/E (x)		
	Rs	Rs. bn	FY12P	FY13E	FY14E	FY12P	FY13E	FY14E	FY12P	FY13E	FY14E	FY12P	FY13E	FY14E	FY12P	FY13E	FY14E
Jyothy Labs	238	19	9,130	13,795	16,414	10.2	13.1	13.9	-22.1	78.0	44.0	8.6	14.0	17.6	35.5	19.9	13.9
Dabur India	113	197	53,481	62,658	73,182	16.6	17.2	17.3	13.9	25.1	21	35.3	33.2	30.5	30.4	24.3	20.1
Emami *	496	75	14,540	17,350	20,440	19.1	18.2	18.1	15.9	19.3	18.4	24.6	22.7	21.2	29.1	24.2	20.5
Marico	182	112	40,073	48,907	58,822	12	13.1	13.4	19.2	31.9	29.6	26.9	20.4	21.6	35.2	28.0	21.6

*Source: Company, Karvy Institutional Research, *Bloomberg*

Financials - Consolidated

Exhibit 7: Profit & Loss

Y/E Mar (Rs mn)	FY10	FY11	FY12P	FY13E	FY14E
Net sales	**5,975**	**6,174**	**9,130**	**13,795**	**16,414**
EBIDTA	**929**	**727**	**841**	**1,810**	**2,277**
Depreciation	124	130	247	251	291
Interest Expense	17	21	238	541	481
PBT	**955**	**812**	**583**	**1,211**	**1,722**
Tax	215	154	199	212	261
Adj. PAT	**743**	**688**	**536**	**954**	**1,374**
EPS (Rs)	9.2	8.5	6.6	11.8	17.0
DPS (Rs)	4.0	5.0	2.5	4.0	4.0
Profit and Loss Ratios					
EBIDTA Margin %	15.6	11.8	10.2	13.1	13.9
Adj. Net Margin %	12.4	11.1	5.9	6.9	8.4
Valuation Multiples					
P/E (X)	25.6	27.7	35.5	19.9	13.9
EV/EBIDTA (X)	19.3	22.4	27.4	12.3	9.4
EV/Sales (X)	3.0	2.6	2.5	1.6	1.3

Source: Company, Karvy Institutional Research

Exhibit 8: Balance Sheet

Y/E Mar (Rs mn)	FY10	FY11	FY12P	FY13E	FY14E
Total Assets	**5,392**	**8,319**	**14,073**	**14,540**	**15,516**
Net Fixed Assets	2,378	2,607	9,383	9,432	9,441
Current Assets	3,013	5,104	4,690	5,108	6,075
Other Assets	1	607	-	-	-
Total Liabilities	**5,392**	**8,319**	**14,073**	**14,540**	**15,516**
Net worth	3,878	6,311	6,213	6,790	7,786
Debt	130	690	5,407	4,807	4,307
Current Liabilities	1,203	1,097	2,171	2,616	3,008
Deferred Tax & Minority Int	181	220	282	327	415
Balance Sheet Ratios					
RoE %	19.2	10.9	8.6	14.0	17.6
RoCE %	23.2	10.4	7.2	15.5	18.5
Net Dept/Equity	(0.3)	(0.3)	0.6	0.5	0.3
Equity/Total Assets	1.0	0.9	0.5	0.6	0.6
P/BV (X)	4.4	3.0	3.1	2.8	2.4

Source: Company, Karvy Institutional Research

Exhibit 9: Cash Flow

Y/E Mar (Rs mn)	FY10	FY11	FY12P	FY13E	FY14E
PBT	955	812	636	1,211	1,722
Depreciation	124	130	225	251	291
Tax	(157)	(225)	(121)	(212)	(261)
Change in Wkg Cap	(290)	(583)	60	279	(199)
CF from Operations	**503**	**(55)**	**1,241**	**2,070**	**2,034**
Capex	(326)	(348)	(6,838)	(300)	(300)
Investments	(132)	(2,172)	607	-	-
CF from Investing	**(363)**	**(2,430)**	**(6,231)**	**(300)**	**(300)**
Change in Equity	-	2,244	-	-	-
Change in Debt	129	560	4,717	(600)	(500)
Dividends & others	(171)	(338)	(850)	(377)	(377)
CF from Financing	**(59)**	**2,444**	**3,427**	**(1,518)**	**(1,358)**
Change in Cash	81	(41)	(1,563)	252	375

Source: Company, Karvy Institutional Research

Exhibit 10: Key Ratios

Y/E Mar (Rs mn)	FY10	FY11	FY12P	FY13E	FY14E
Revenue	5,975	6,174	9,130	13,795	16,414
EBITDA	929	727	841	1,810	2,277
Net Profits (Adj)	743	688	536	954	1,374
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EV/EBITDA (x)	19.3	22.4	27.4	12.3	9.4
RoE %	19.2	10.9	8.6	14.0	17.6
RoCE %	23.2	10.4	7.2	15.5	18.5

Source: Company, Karvy Institutional Research

Institutional Equities Team

Rangachari Muralikrishnan	**Head – Institutional Equities**	**+91-22 61844301**	**muralikrishnan@karvy.com**
Shridhar Iyer	**Head - Institutional Sales**	**+91-22 61844302**	**shridhar.iyer@karvy.com**
K. Anant Rao	**Head - Sales-Trading & Derivatives**	**+91-22 61844303**	**k.anantrao@karvy.com**
Uday Raval	**Karvy Inc. USA**	**(212) 2674334**	**udayr@karvy.com**
INSTITUTIONAL RESEARCH			
Analysts	**Industry / Sector**	**Desk Phone**	**Email ID**
Dwaipayan Poddar	Derivatives/Technical Research	+91-22 61844372	dwaipayan.poddar@karvy.com
Hatim Broachwala, CFA	Banking	+91-22 61844329	
Jagadishwar Pasunoori	MidCap	+91-40-44857912	jagadishwar.p@karvy.com
Madhavi Arora	Economy	+91-22 61844320	madhavi.arora@karvy.com
Manoj Kumar Manish	Derivatives Research	+91-22 61844327	manojkumar.m@karvy.com
Maruti Kadam	Auto & Auto Ancillaries / Metals & Mining	+91-22 61844326	
Mitul Shah	Auto & Auto Ancillaries	+91-22 61844312	mitul.shah@karvy.com
Nishith Sanghvi	Pharmaceuticals	+91-22 61844325	nishith.s@karvy.com
Naveen Trivedi	FMCG	+91-22-61844316	naveen.trivedi@karvy.com
Pallav Agarwal	Metals & Mining	+91-22 61844317	agarwal.pallav@karvy.com
Paresh Jain	BFSI	+91-22 61844324	paresh.jain@karvy.com
Parikshit Kandpal	Infra / Real Estate	+91-22 61844311	parikshit.kandpal@karvy.com
Rahul Sharma	Pharmaceuticals	+91-22 61844310	rahul.sharma@karvy.com
Rahul Singh	MidCap	+91-40-44857912	rahulsingh@karvy.com
Rajesh Kumar Ravi	Cement & Logistics	+91-22 61844313	rajesh.ravi@karvy.com
Rupesh Sankhe	Power/Capital Goods	+91-22 61844315	rupesh.sankhe@karvy.com
Sameer Pardikar	Telecom, Media and Oil & Gas	+91-22 61844323	sameer.pardikar@karvy.com
Vinay Nair	Oil & Gas	+91-22 61844319	vinaynair@karvy.com
INSTITUTIONAL SALES			
Dinesh Bajaj	Sales	+91-22 61844341	dinesh.bajaj@karvy.com
Dipesh Jain	Sales	+91-22 61844342	dipesh.jain@karvy.com
R. Sriram	Sales	+91-22 61844340	sriram.rangarajan@karvy.com
Shabbir Dahodwala	Sales (USA)	+1-212-2674334	shabbir@karvy.com
Tejash Gandhi	Sales	+91-22 61844345	tejash.gandhi@karvy.com
INSTITUTIONAL SALES TRADING & DEALING			
Bhavesh Gandhi	Institutional Dealer	+91-22 61844368 /69	bhavesh.gandhi@karvy.com
Prashant Oza	Institutional Dealer	+91-22 61844370 /71	prashant.oza@karvy.com
Parag Shah	Sales Trader	+91-22 61844364 /65	parag.shah@karvy.com
Sriram Jagdish	Sales Trader	+91-22 61844366 /67	sriram.jagdish@karvy.com
PRODUCTION			
Asim Kumar Mohapatra	Editor	+91-22 61844318	asim.mohapatra@karvy.com
Vishal Randive	Database	+91-22 61844321	vishal.randive@karvy.com
Vijayalaxmi Moolya	Production	+91-22 61844328	vijayalaxmi.m@karvy.com

Stock Ratings		Absolute Returns
Buy	:	> 15%
Hold	:	5-15%
Sell	:	< 5%

For further enquiries please contact:

research@karvy.com

Tel: +91-22-6184 4300

Disclosures Appendix

Analyst certification

The following analyst(s), who is (are) primarily responsible for this report, certify (ies) that the views expressed herein accurately reflect his (their) personal view(s) about the subject security (ies) and issuer(s) and that no part of his (their) compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report.

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Karvy Stock Broking Limited

Institutional Equities

Office No. 702, 7th Floor, Hallmark Business Plaza, Opp.-Gurunanak Hospital, Mumbai 400 051

Regd Off : 46, Road No 4, Street No 1, Banjara Hills, Hyderabad – 500 034.

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