

Hindustan Unilever Ltd (HUVR IN)

Volume growth continues to struggle

INDIA | FMCG | Quarterly Update

18 July 2016

Top takeaways from Q1FY17

- ✘ Revenue growth was lower than our/street estimates due to lower-than-expected volume growth and sluggish growth in Personal Care
- ✓ Margins continued to see expansion because of lower input prices of key raw materials

Key highlights: Domestic Consumer grew 4% yoy with underlying volume growth of 4% yoy and flattish price growth. Cessation of excise-duty benefits affected sales by -40bps and PBIT by -15bps. Home Care/Personal Care/Foods/Refreshments sales grew 7%/2%/5%/5% yoy.

Conference call takeaways

- ✘ Market growth slowed down further in Q1FY17; value growth is down to half its level in Q4FY16 and one fourth its level in Q1FY16
- ✘ Demand slowdown has been more prominent in general trade and in areas that are drought affected; rural growth continues to lag urban growth since the last few quarters
- ✓ Management is optimistic about the medium-term impact of the 7th pay commission payouts and normal monsoons
- ✓ Modern Trade growth was satisfactory; premium segments continue to grow ahead of overall portfolio
- ✓ Undertook channel spends realignment in Q3/Q4, which led to 1% qoq growth in Q1FY17
- ✓ Deflation cycle may have bottomed out, input costs have started increasing; have taken price hikes in Soaps and Detergents
- ✓ In Home Care, premium segment drove growth; Surf grew in double digits
- ✓ In Personal Care, growth was driven by *Lifebuoy*, *Pears*, *Dove*, and *Fair & Lovely*; *Pepsodent* continued to be subdued; *Indulekha* (hair oil) acquisition completed in Q1FY17
- ✓ A&P growth in Q1FY17 was low because of the high base last year; however A&P spends were similar, and competitive activity remains high
- ✓ To invest Rs 10bn in Assam to set up a new manufacturing unit for Personal Care; expect it to be commissioned in early 2017
- ✓ Royalty levels not to increase further till 2023

Outlook and valuation: We have largely maintained our estimates for FY17/18. HUL has been struggling from sluggish volume growth for the past four quarters, and we expect it to underperform the sector in terms of volume growth by ~200bps. The stock currently trades at 39x FY18 earnings; with expected earnings CAGR of just 12% in FY16-19, we see the stock de-rating to 36x FY18 earnings over the next year. We value the stock at Rs 830 (previously Rs 765) and maintain Sell.

Sell (Maintain)

CMP RS 911 / TARGET RS 830 (-9%)

COMPANY DATA

O/S SHARES (MN) :	2164
MARKET CAP (RSBN) :	2034
MARKET CAP (USDBN) :	30.37
52 - WK HI/LO (RS) :	949 / 765
LIQUIDITY 3M (USDMN) :	19.8
PAR VALUE (RS) :	1

SHARE HOLDING PATTERN, %

	Mar 16	Dec 15	Sep 15
PROMOTERS :	67.2	67.2	67.2
FII / NRI :	14.2	13.9	13.9
FI / MF :	4.8	5.0	4.8
NON PRO :	1.7	1.8	0.8
PUBLIC & OTHERS :	12.1	12.1	13.2

Key Financials

Rs mn	FY16E	FY17E	FY18E
Net Sales	314,253	339,681	374,689
EBIDTA	62,306	70,219	77,435
Net Profit	41,226	45,179	50,113
EPS, Rs	19.0	20.8	23.1
PER, x	47.9	43.7	39.4
EV/EBIDTA, x	31.3	27.7	25.1
P/BV, x	53.6	54.3	56.4
ROE, %	111.8	124.1	143.2

CHANGE IN ESTIMATES

Rs bn	Revised Est.		% Revision	
	FY17E	FY18E	FY17E	FY18E
Revenue	339,681	374,689	(1.4)	(2.5)
EBITDA	70,219	77,435	3.0	1.6
Core PAT	45,166	50,111	0.5	(0.4)
EPS (Rs)	20.8	23.1	0.7	(0.4)

Naveen Kulkarni and Jubil Jain

(Rs mn)	Q1FY17	Q4FY16	QoQ growth %	Q1FY16	YoY growth %	PC yoy growth expectations %	Comments
Volume growth (% yoy)	4.0	4.0		6.0		5.0	Volume growth lower due to PP underperformance
Price growth (%yoy)	-	(1.0)		1.0		0.0	
Net Sales	79,877	75,849	5.3	77,127	3.6	5.0	
Gross Profits	40,323	38,161	5.7	38,151	5.7	6.9	
Gross Margin (%)	50.5	50.3		49.5		93 bps	
Staff costs	4,265	4,426	(3.6)	3,579	19.2	10.1	Higher staff cost growth is due to provision reversal in Q1FY16
A&P spends	8,798	8,655	1.7	8,927	(1.5)	5.5	A&P expenses while low were maintained at competitive levels
Other operating expenses	12,306	11,740	4.8	11,842	3.9	5.3	Other expenses lower due to better cost management
EBITDA	16,359	14,703	11.3	15,120	8.2	8.4	
EBITDA margin (%)	20.5	19.4		19.6		61 bps	
PBT	17,150	15,338	11.8	15,651	9.6	7.7	
Tax rate (%)	0.3	0.3		0.3		0 bps	
PAT	11,739	11,135	5.4	10,692	9.8	7.7	
Adj. PAT	11,280	10,310	9.4	10,628	6.1	8.4	PAT growth impacted by higher depreciation and interest

Segment operating performance

Rs mn	Q1FY17	Q1FY16	Yoy growth
Segmental Revenue (Rs mn)			
Home Care	23,972	25,596	6.8
Personal Care	38,171	38,986	2.1
Foods	2,550	2,670	4.7
Refreshments	11,297	11,912	5.4
Others	1,975	1,975	(16.2)
Total	77,965	81,139	3.6
Segmental Revenue Contribution (%)			
Home Care	30.6	31.5	
Personal Care	48.7	48.0	
Foods	3.3	3.3	
Refreshments	14.4	14.7	
Others	3.0	2.4	
Segment Results (Rs mn)			
Home Care	2,910	3,559	22.3
Personal Care	10,184	10,214	0.3
Foods	214	170	
Refreshments	1,786	1,921	7.5
Others	(21)	(95)	
Total	15,073	15,768	4.6
Segment EBIT margins (%)			
Soaps & Detergents	12.1	13.9	
Personal Products	26.7	26.2	
Beverages	8.4	6.4	
Processed Foods	15.8	16.1	
Others			
EBIT Contribution %			
Home Care	19.3	22.6	
Personal Care	67.6	64.8	
Foods	1.4	1.1	
Refreshments	11.8	12.2	
Others			

Source: Company, PhillipCapital India Research

PE table (based on consensus estimates)

PC FMCG Universe	Current PE				Current PE premium to historical avg			Premium to sector multiple ex-ITC			
	Current PE	3 yr avg	5 yr avg	10 yr avg	3 yr avg	5 yr avg	10 yr avg	Current	3 yr avg	5 yr avg	10 yr avg
Agro Tech	33.6	43.6	36.8	29.3	-23%	-9%	15%	-16%	18%	9%	2%
Bajaj Corp	22.1	21.2	18.5	17.8	4%	19%	24%	-45%	-43%	-45%	-38%
Britannia	34.2	29.2	25.7	25.1	17%	33%	36%	-15%	-21%	-24%	-12%
Colgate	37.3	38.1	36.2	29.0	-2%	3%	29%	-7%	3%	7%	1%
Dabur	36.8	33.1	30.1	27.1	11%	22%	36%	-8%	-10%	-11%	-6%
Emami	39.1	34.0	29.2	23.5	15%	34%	66%	-3%	-8%	-14%	-18%
GCPL	38.5	32.6	30.3	23.5	18%	27%	64%	-4%	-12%	-11%	-18%
GSKConsumer	33.5	34.1	31.4	24.1	-2%	7%	39%	-17%	-8%	-8%	-16%
HUL	41.7	39.0	34.9	30.2	7%	19%	38%	4%	5%	3%	5%
Marico	40.3	31.3	30.5	26.4	29%	32%	53%	0%	-15%	-10%	-8%
Nestle	46.8	47.9	45.0	36.1	-2%	4%	30%	16%	30%	32%	26%
Asian Paints	44.6	39.3	36.1	28.5	14%	24%	57%	11%	6%	6%	-1%
ITC	25.7	27.3	26.6	23.7	-6%	-3%	9%	-36%	-26%	-22%	-17%
Total	34.0	32.8	30.7	26.5	4%	11%	28%	-15%	-11%	-9%	-8%
Total Ex-ITC	40.2	37.0	33.9	28.6	9%	18%	40%				

Source: Bloomberg, PhillipCapital India Research Estimates; as on 15th July 2016

Financials

Income Statement

Y/E Mar, Rs mn	FY15	FY16	FY17E	FY18E
Net sales	301,705	314,253	339,681	374,689
Growth, %	10.1	4.2	8.1	10.3
Other income	12,535	10,625	11,365	12,048
Total income	314,240	324,878	351,046	386,737
Raw material expenses	-156,236	-153,130	-163,477	-179,665
Employee expenses	-15,789	-15,920	-16,805	-18,486
Other Operating expenses	-83,949	-93,522	-100,544	-111,151
EBITDA (Core)	58,266	62,306	70,219	77,435
Growth, %	14.3	6.9	12.7	10.3
Margin, %	19.3	19.8	20.7	20.7
Depreciation	-2,867	-3,208	-3,463	-3,739
EBIT	55,399	59,098	66,756	73,696
Growth, %	14.6	6.7	13.0	10.4
Margin, %	18.4	18.8	19.7	19.7
Interest paid	-168	-2	-2	-2
Pre-tax profit	55,240	59,108	66,766	73,694
Tax provided	-16,795	-17,882	-21,588	-23,582
Profit after tax	38,445	41,226	45,179	50,113
Net Profit	38,445	41,226	45,179	50,113
Growth, %	4.0	7.2	9.6	10.9
Net Profit (adjusted)	38,445	41,226	45,179	50,113
Unadj. shares (m)	2,162	2,168	2,168	2,168
Wtd avg shares (m)	2,162	2,168	2,168	2,168

Balance Sheet

Y/E Mar, Rs mn	FY15	FY16	FY17E	FY18E
Cash & bank	25,376	27,588	26,954	28,896
Debtors	7,829	10,645	11,596	12,854
Inventory	26,027	25,284	27,036	28,904
Loans & advances	12,407	12,546	14,673	16,111
Other current assets	593	625	406	406
Total current assets	72,232	76,688	80,666	87,171
Investments	32,779	29,666	29,666	29,666
Gross fixed assets	47,214	53,787	58,787	64,287
Less: Depreciation	-22,638	-24,640	-28,104	-31,845
Add: Capital WIP	4,790	3,860	3,860	3,860
Net fixed assets	29,365	33,007	34,543	36,302
Non-current assets	4	2	2	2
Total assets	136,341	141,670	147,184	155,448
Current liabilities	75,590	79,988	81,802	88,287
Provisions	23,502	24,810	29,694	32,864
Total current liabilities	99,093	104,797	111,496	121,150
Total liabilities	99,093	104,797	110,788	120,442
Paid-up capital	2,164	2,164	2,164	2,164
Reserves & surplus	35,084	34,709	34,232	32,842
Shareholders' equity	37,248	36,873	36,396	35,006
Total equity & liabilities	136,341	141,670	147,184	155,448

Source: Company, PhillipCapital India Research Estimates
Numbers in Indian GAAP format

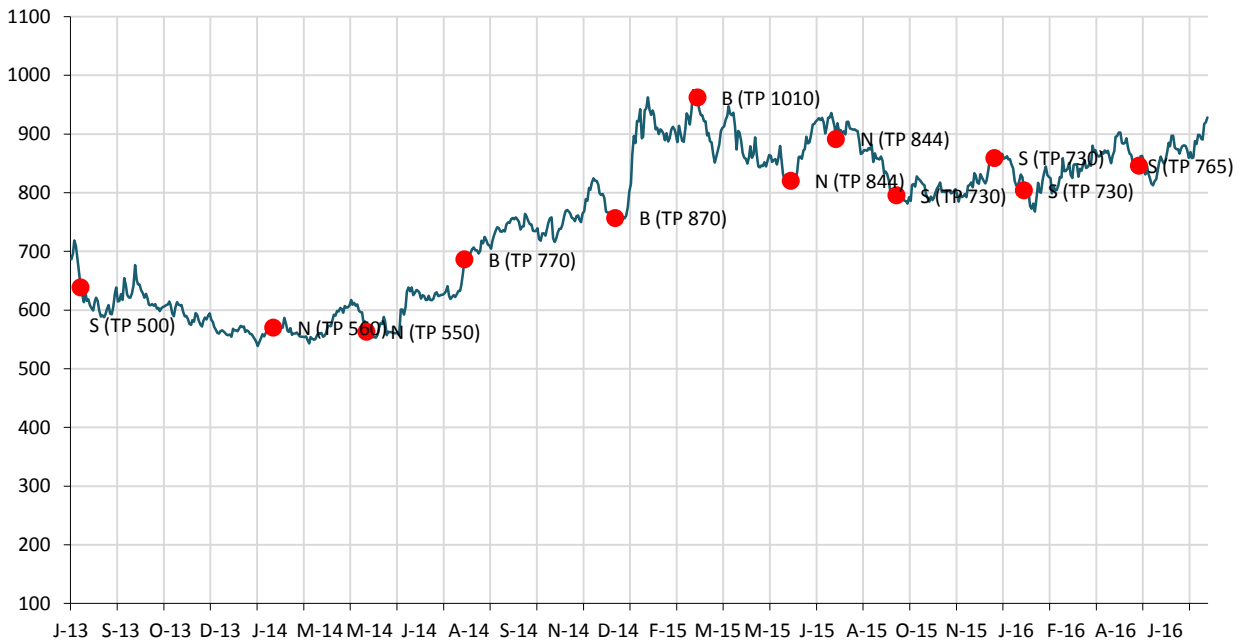
Cash Flow

Y/E Mar, Rs mn	FY15	FY16	FY17E	FY18E
Pre-tax profit	55,240	59,108	66,766	73,694
Depreciation	2,867	3,208	3,463	3,739
Chg in working capital	-1,653	2,157	-3,506	1,921
Total tax paid	-15,920	-18,010	-15,621	-22,576
Cash flow from operating activities	45,240	46,057	51,085	56,777
Capital expenditure	-4,814	-6,849	-4,999	-5,498
Cash flow from investing activities	-6,649	-3,731	-4,995	-5,498
Free cash flow	38,591	42,325	46,090	51,279
Dividend (incl. tax)	-35,561	-40,309	-47,433	-49,337
Cash flow from financing activities	-35,424	-40,112	-47,433	-49,337
Net chg in cash	3,166	2,213	-1,343	1,942

Valuation Ratios

	FY15	FY16	FY17E	FY18E
Per Share data				
EPS (INR)	17.8	19.0	20.8	23.1
Growth, %	4.0	6.9	9.6	10.9
Book NAV/share (INR)	17.2	17.0	16.8	16.1
FDEPS (INR)	17.8	19.0	20.8	23.1
CEPS (INR)	19.1	20.5	22.4	24.8
CFPS (INR)	18.7	21.4	23.6	26.2
DPS (INR)	15.0	16.0	18.0	20.0
Return ratios				
Return on assets (%)	29.0	29.7	31.3	33.1
Return on equity (%)	103.2	111.8	124.1	143.2
Return on capital employed (%)	110.1	111.2	124.5	143.2
Turnover ratios				
Asset turnover (x)				
Sales/Total assets (x)	2.3	2.3	2.4	2.5
Sales/Net FA (x)	10.6	10.1	10.1	10.6
Working capital/Sales (x)	(0.2)	(0.2)	(0.2)	(0.2)
Working capital days	(63.2)	(64.7)	(62.1)	(61.2)
Liquidity ratios				
Current ratio (x)	0.7	0.7	0.7	0.7
Quick ratio (x)	0.5	0.5	0.5	0.5
Interest cover (x)				
Dividend cover (x)	1.2	1.2	1.2	
Net debt/Equity (%)				
Valuation				
PER (x)	51.2	47.9	43.7	39.4
Price/Book (x)	52.9	53.6	54.3	56.4
Yield (%)	1.6	1.8	2.0	
EV/Net sales (x)	6.4	6.2	5.7	5.2
EV/EBITDA (x)	33.4	31.3	27.7	25.1
EV/EBIT (x)	35.1	33.0	29.2	26.4

Stock Price, Price Target and Rating History



Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year.

Rating	Criteria	Definition
BUY	$\geq +15\%$	Target price is equal to or more than 15% of current market price
NEUTRAL	$-15\% > \text{to} < +15\%$	Target price is less than +15% but more than -15%
SELL	$\leq -15\%$	Target price is less than or equal to -15%.

Management

Vineet Bhatnagar (Managing Director)	(91 22) 2483 1919
Kinshuk Bharti Tiwari (Head – Institutional Equity)	(91 22) 6667 9946
Jignesh Shah (Head – Equity Derivatives)	(91 22) 6667 9735

Research

Automobiles		IT Services		Pharma & Speciality Chem	
Dhawal Doshi	(9122) 6667 9769	Vibhor Singhal	(9122) 6667 9949	Surya Patra	(9122) 6667 9768
Nitesh Sharma, CFA	(9122) 6667 9965	Shyamal Dhruve	(9122) 6667 9992	Mehul Sheth	(9122) 6667 9996
Banking, NBFCs		Infrastructure		Strategy	
Manish Agarwalla	(9122) 6667 9962	Vibhor Singhal	(9122) 6667 9949	Naveen Kulkarni, CFA, FRM	(9122) 6667 9947
Pradeep Agrawal	(9122) 6667 9953	Deepak Agarwal	(9122) 6667 9944	Anindya Bhowmik	(9122) 6667 9764
Pareesh Jain	(9122) 6667 9948	Logistics, Transportation & Midcap		Telecom	
Consumer & Retail		Vikram Suryavanshi	(9122) 6667 9951	Naveen Kulkarni, CFA, FRM	(9122) 6667 9947
Naveen Kulkarni, CFA, FRM	(9122) 6667 9947	Media		Manoj Behera	(9122) 6667 9973
Jubil Jain	(9122) 6667 9766	Manoj Behera	(9122) 6667 9973	Technicals	
Preeyam Tolia	(9122) 6667 9950	Metals		Subodh Gupta, CMT	(9122) 6667 9762
Cement		Dhawal Doshi	(9122) 6667 9769	Production Manager	
Vaibhav Agarwal	(9122) 6667 9967	Yash Doshi	(9122) 6667 9987	Ganesh Deorukhkar	(9122) 6667 9966
Economics		Midcap		Editor	
Anjali Verma	(9122) 6667 9969	Amol Rao	(9122) 6667 9952	Roshan Sony	98199 72726
Engineering, Capital Goods		Mid-Caps & Database Manager		Sr. Manager – Equities Support	
Jonas Bhutta	(9122) 6667 9759	Deepak Agarwal	(9122) 6667 9944	Rosie Ferns	(9122) 6667 9971
Sales & Distribution		Oil & Gas		Corporate Communications	
Ashvin Patil	(9122) 6667 9991	Sabri Hazarika	(9122) 6667 9756	Zarine Damania	(9122) 6667 9976
Shubhangi Agrawal	(9122) 6667 9964	Sales Trader		Bharati Ponda	(9122) 6667 9943
Kishor Binwal	(9122) 6667 9989	Dilesh Doshi	(9122) 6667 9747		
Bhavin Shah	(9122) 6667 9974	Suniil Pandit	(9122) 6667 9745		
Ashka Mehta Gulati	(9122) 6667 9934	Execution			
Archan Vyas	(9122) 6667 9785	Mayur Shah	(9122) 6667 9945		

Contact Information (Regional Member Companies)

SINGAPORE: Phillip Securities Pte Ltd 250 North Bridge Road, #06-00 RafflesCityTower, Singapore 179101 Tel : (65) 6533 6001 Fax: (65) 6535 3834 www.phillip.com.sg	MALAYSIA: Phillip Capital Management Sdn Bhd B-3-6 Block B Level 3, Megan Avenue II, No. 12, Jalan Yap Kwan Seng, 50450 Kuala Lumpur Tel (60) 3 2162 8841 Fax (60) 3 2166 5099 www.poems.com.my	HONG KONG: Phillip Securities (HK) Ltd 11/F United Centre 95 Queensway Hong Kong Tel (852) 2277 6600 Fax: (852) 2868 5307 www.phillip.com.hk
JAPAN: Phillip Securities Japan, Ltd 4-2 Nihonbashi Kabutocho, Chuo-ku Tokyo 103-0026 Tel: (81) 3 3666 2101 Fax: (81) 3 3664 0141 www.phillip.co.jp	INDONESIA: PT Phillip Securities Indonesia ANZ Tower Level 23B, Jl Jend Sudirman Kav 33A, Jakarta 10220, Indonesia Tel (62) 21 5790 0800 Fax: (62) 21 5790 0809 www.phillip.co.id	CHINA: Phillip Financial Advisory (Shanghai) Co. Ltd. No 550 Yan An East Road, Ocean Tower Unit 2318 Shanghai 200 001 Tel (86) 21 5169 9200 Fax: (86) 21 6351 2940 www.phillip.com.cn
THAILAND: Phillip Securities (Thailand) Public Co. Ltd. 15th Floor, Vorawat Building, 849 Silom Road, Silom, Bangrak, Bangkok 10500 Thailand Tel (66) 2 2268 0999 Fax: (66) 2 2268 0921 www.phillip.co.th	FRANCE: King & Shaxson Capital Ltd. 3rd Floor, 35 Rue de la Bienfaisance 75008 Paris France Tel (33) 1 4563 3100 Fax : (33) 1 4563 6017 www.kingandshaxson.com	UNITED KINGDOM: King & Shaxson Ltd. 6th Floor, Candlewick House, 120 Cannon Street London, EC4N 6AS Tel (44) 20 7929 5300 Fax: (44) 20 7283 6835 www.kingandshaxson.com
UNITED STATES: Phillip Futures Inc. 141 W Jackson Blvd Ste 3050 The Chicago Board of Trade Building Chicago, IL 60604 USA Tel (1) 312 356 9000 Fax: (1) 312 356 9005	AUSTRALIA: PhillipCapital Australia Level 10, 330 Collins Street Melbourne, VIC 3000, Australia Tel: (61) 3 8633 9800 Fax: (61) 3 8633 9899 www.phillipcapital.com.au	SRI LANKA: Asha Phillip Securities Limited Level 4, Millennium House, 46/58 Navam Mawatha, Colombo 2, Sri Lanka Tel: (94) 11 2429 100 Fax: (94) 11 2429 199 www.ashaphillip.net/home.htm

INDIA
PhillipCapital (India) Private Limited

No. 1, 18th Floor, Urmi Estate, 95 Ganpatrao Kadam Marg, Lower Parel West, Mumbai 400013
Tel: (9122) 2300 2999 Fax: (9122) 6667 9955 www.phillipcapital.in

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