

# Marico Industries (MRCO IN)

Saffola growth revives; gross margins surprise positively

INDIA | FMCG | Quarterly Update

1 February 2016

## Top takeaways from Q3FY16

- ✓ Revenue growth was above our/consensus estimates as growth in *Saffola* and value-added hair oils surprised positively while *Parachute* rigids struggled
- ⇔ Domestic volume growth of 10.5% was above estimates; however, price deflation of 3.5% in domestic business will affect value growth.
- ✓ International business grew 10% yoy in CC led by MENA, South East Asia, and South Africa; Bangladesh grew 1% due to price cuts in *Parachute* coconut oil
- ✓ Gross margin surprised positively on higher commodity deflation (copra/LLP/HDPE down 28%/35%/14% yoy), which helped EBIDTA and PAT beat estimates.

## Conference call takeaways

- ⇔ Rural markets (33% of sales) grew by 7% yoy and urban markets (general and modern trade) grew by 6% yoy; MT saw some demand improvement (+20%) in Q3
- ✓ The company expects volume growth of 8-10% with paramount importance to market share gains; medium term EBIDTA margin target of 16-17%
- \* Primary volume growth was affected as traders reduced stocks, anticipating a fall in prices; they are maintaining a lower trade pipeline until prices stabilise
- ✓ *Saffola* growth was helped by regional pricing strategy, broadening of consumer base, reduction in price premium, and favourable base; it expects 10%+ growth going forward
- ✓ International business growth improved as growth stabilised in the Middle East, South East Asia and Egypt; Bangladesh is doing well after price corrections
- ⇔ Gel is doing well, company expects deodorants growth to rise; serum affected by counterfeits
- ✓ Project ONE has helped improve direct coverage in top six metros by 60% leading to incremental turnover of Rs 650-750mn by FY16 end; to be extended to 14 more towns
- ⇔ A&P/sales to be in 11-12% band in the medium term; significant part of A&P has been invested for new products such as VAHO, foods and the youth portfolio in India
- ⇔ Staff costs driven by annual increment/capability building in South East Asia/Bangladesh
- ⇔ Planned capex in FY16/17 is likely to be around Rs 1-1.25bn each year

**Outlook and valuation:** We have increased our estimates to factor significant fall in input costs and lower tax rate, coupled with lower realisations. We value the stock at Rs 215 (32x our FY17 earnings) vs. Rs 180 earlier and upgrade it to Neutral due to 1) significant fall in input prices and Marico's ability to maintain gross margins in such scenarios, 2) industry beating volume growth in a deflationary environment and 3) revival of *Saffola*. Key upside risk to our recommendation – further fall in commodity costs. Downside risks – further price cuts and escalation of A&P spends to maintain market share in a competitive environment.

## Neutral (Upgrade)

CMP RS 226 / TARGET Rs 215 (-5%)

### COMPANY DATA

O/S SHARES (MN) :	1290
MARKET CAP (RSBN) :	280
MARKET CAP (USDBN) :	4.13
52 - WK HI/LO (RS) :	234 / 170
LIQUIDITY 3M (USDMN) :	8.6
PAR VALUE (RS) :	1

### SHARE HOLDING PATTERN, %

	Sep 15	Jun 15	Mar 15
PROMOTERS :	59.7	59.7	59.7
FII / NRI :	29.0	29.6	28.1
FI / MF :	4.3	4.2	4.6
NON PRO :	1.0	0.8	0.9
PUBLIC & OTHERS :	6.4	6.0	7.0

### Key Financials

Rs mn	FY15	FY16E	FY17E
Net Sales	57,203	61,279	67,287
EBIDTA	8,535	10,714	12,741
Net Profit	5,569	7,235	8,663
EPS, Rs	4.3	5.6	6.7
PER, x	<b>52.3</b>	<b>40.3</b>	<b>33.7</b>
EV/EBIDTA, x	34.4	27.0	22.3
PBV, x	16.0	12.8	10.5
ROE, %	30.5	31.8	31.0

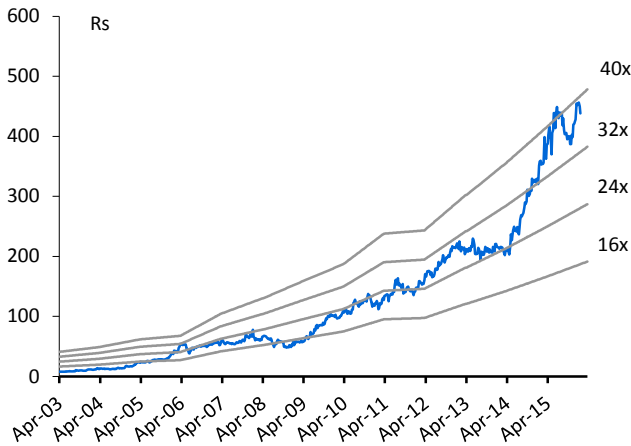
### CHANGE IN ESTIMATES

Rs bn	Revised Est.		% Revision	
	FY16E	FY17E	FY16E	FY17E
Revenue	61,279	67,287	0.6%	-2.5%
EBIDTA	10,714	12,741	0.8%	10.1%
Core PAT	7,235	8,663	3.5%	13.1%
EPS (Rs)	5.6	6.7	3.9%	12.8%

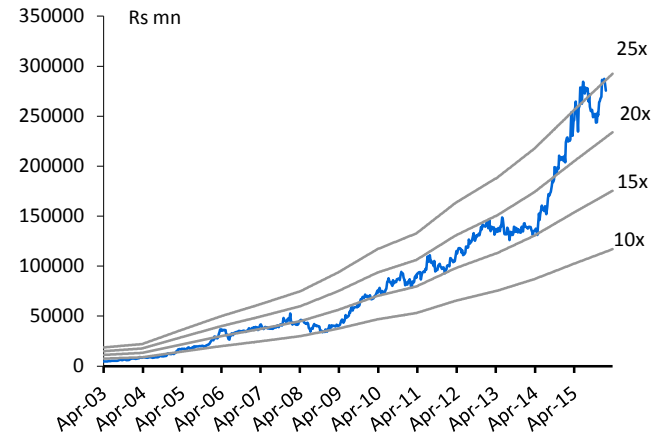
Naveen Kulkarni and Jubil Jain

(Rs mn)	Q3FY16	Q2FY16	qoq growth %	Q3FY15	yoy vs. expectations growth %	Comments	
Volume growth (% yoy)	10.5	5.5		5.0	350 bps	Saffola/VAHO volume growth surprised positively	
Price growth (%yoy)	(3.5)	(1.5)		21.0	-150 bps	Higher Parachute price cut surprised negatively	
Net Sales	15,546	14,835	4.8	14,489	7.3	2.2	
Gross Profits	8,042	7,298	10.2	6,567	22.5	6.6	
Gross Margin (%)	51.7	49.2	254 bps	45.3	641 bps	213 bps	Significant decline in input costs
Staff costs	913	853	7.1	783	16.6	5.3	
Ad spends	1,878	2,176	-13.7	1,530	22.7	2.9	Input cost benefits were passed partly into A&P spends
Other operating expenses	2,331	1,991	17.1	1,919	21.4	12.7	
EBIDTA	2,938	2,297	27.9	2,369	24.0	4.0	
EBIDTA margin (%)	18.9	15.5	342 bps	16.4	255 bps	34 bps	
PBT	2,805	2,164	29.6	2,184	28.4	5.3	
Tax rate (%)	28.5	28.8	-31 bps	25.7	275 bps	150 bps	
PAT	1,978	1,507	31.2	1,599	23.7	3.0	
Adj. PAT	1,978	1,507	31.2	1,599	23.7	3.0	

**One-year forward P/E band**

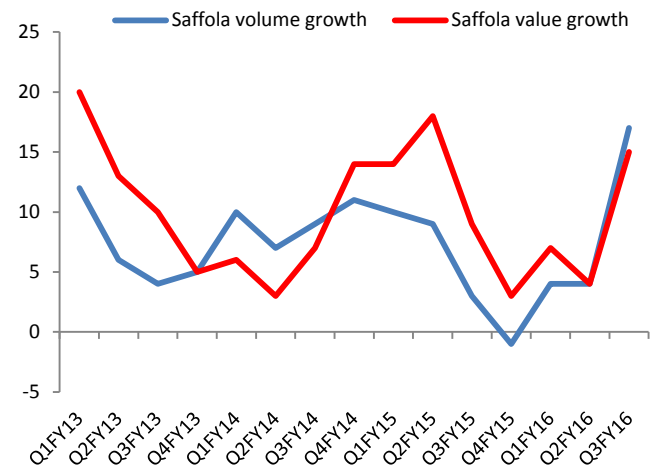
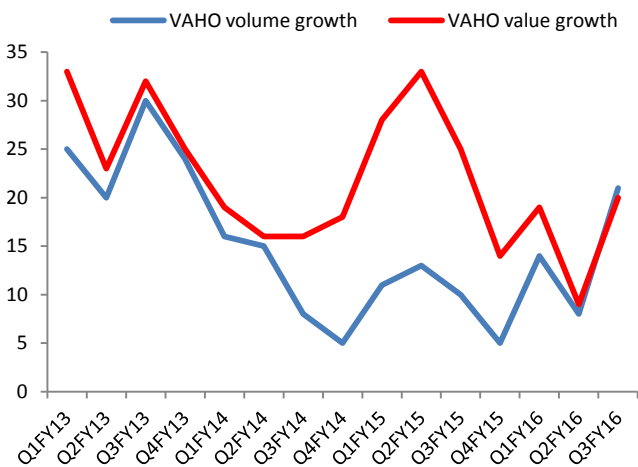
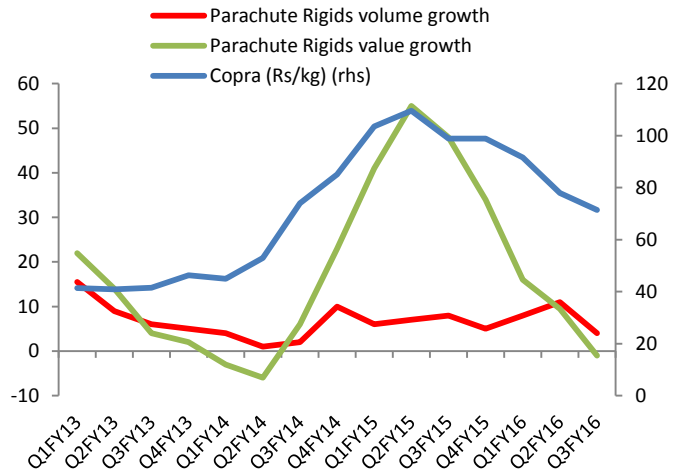
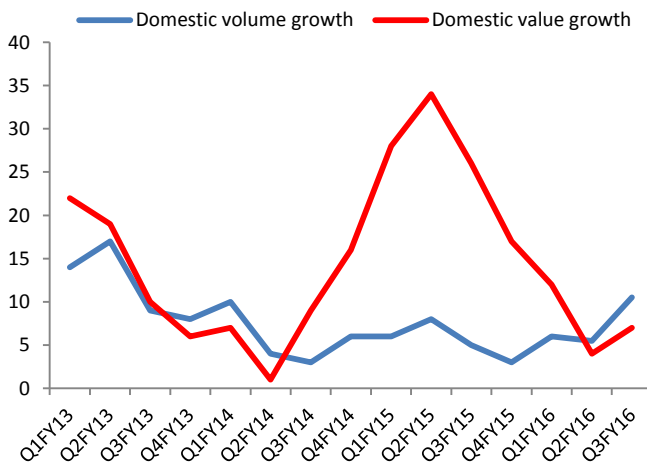


**EV/EBITDA band**



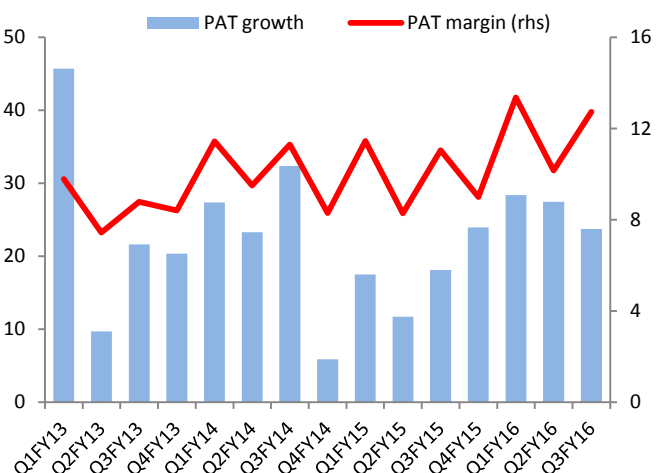
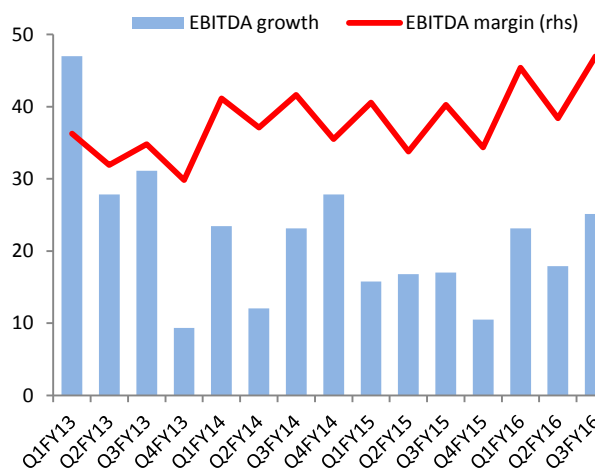
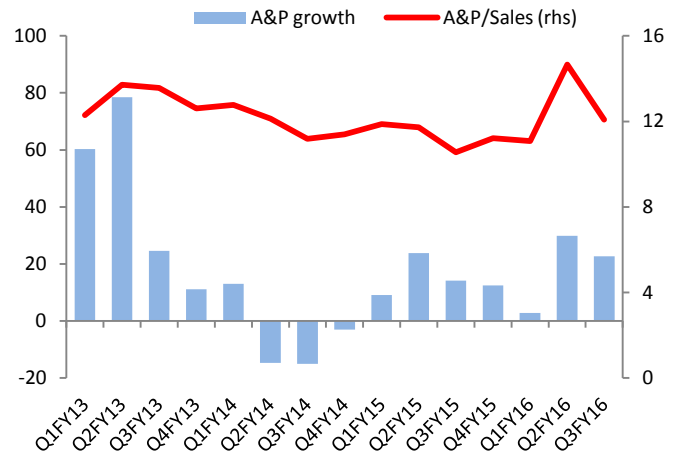
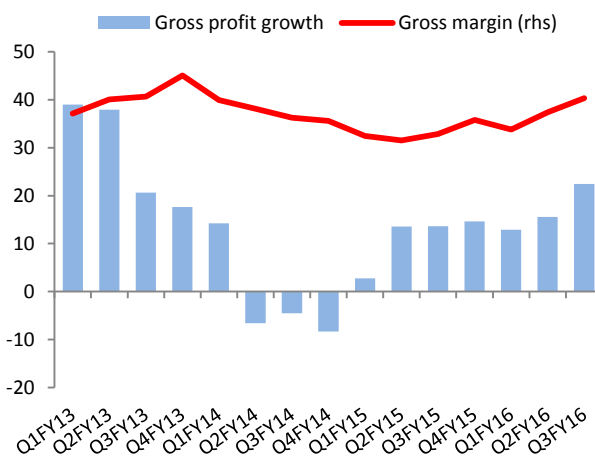
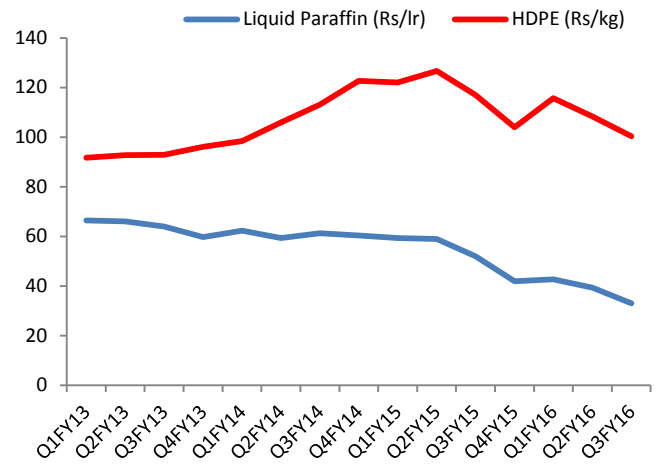
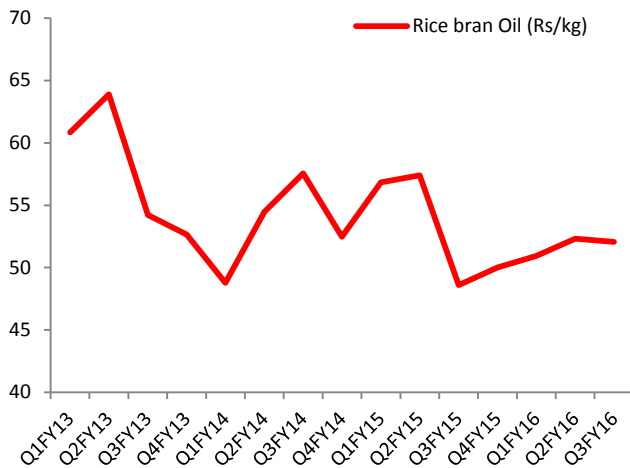
Source: PhillipCapital India Research Estimates

**Focus charts**



Source: Company, PhillipCapital India Research

Focus charts



Source: Company, PhillipCapital India Research

## Financials

### Income Statement

Y/E Mar, Rs mn	FY14	FY15e	FY16e	FY17e
<b>Net sales</b>	<b>46,762</b>	<b>57,203</b>	<b>61,279</b>	<b>67,287</b>
Growth, %	2	22	7	10
Other income	103	127	94	106
Total income	46,865	57,330	61,373	67,393
Raw material expenses	-23,992	-31,190	-31,043	-32,407
Employee expenses	-2,847	-3,251	-3,512	-3,968
Other Operating expenses	-12,643	-14,353	-16,104	-18,277
<b>EBITDA (Core)</b>	<b>7,384</b>	<b>8,535</b>	<b>10,714</b>	<b>12,741</b>
Growth, %	18.8	15.6	25.5	18.9
Margin, %	15.8	14.9	17.5	18.9
Depreciation	-769	-843	-912	-1,012
<b>EBIT</b>	<b>6,615</b>	<b>7,692</b>	<b>9,802</b>	<b>11,729</b>
Growth, %	23.7	16.3	27.4	19.7
Margin, %	14.1	13.4	16.0	17.4
Interest paid	-345	-229	-196	-196
Other Non-Operating Income	579	589	750	850
<b>Pre-tax profit</b>	<b>6,850</b>	<b>8,051</b>	<b>10,357</b>	<b>12,384</b>
Tax provided	-1,905	-2,368	-3,003	-3,591
<b>Profit after tax</b>	<b>4,945</b>	<b>5,684</b>	<b>7,353</b>	<b>8,793</b>
Others (Minorities, Associates)	-187	-114	-118	-130
<b>Net Profit</b>	<b>4,758</b>	<b>5,569</b>	<b>7,235</b>	<b>8,663</b>
Growth, %	32.8	17.1	29.9	19.7
<b>Net Profit (adjusted)</b>	<b>4,758</b>	<b>5,569</b>	<b>7,235</b>	<b>8,663</b>
Unadj. shares (m)	1,290	1,290	1,290	1,290
Wtd avg shares (m)	1,290	1,290	1,290	1,290

### Balance Sheet

Y/E Mar, Rs mn	FY14	FY15e	FY16e	FY17e
Cash & bank	<b>4,064</b>	<b>2,049</b>	<b>7,068</b>	<b>11,393</b>
Debtors	2,232	1,768	2,015	2,397
Inventory	7,962	9,947	10,788	12,173
Loans & advances	3,366	3,861	3,861	3,861
Other current assets	0	0	0	0
Total current assets	17,624	17,625	23,733	29,824
Investments	3,105	2,838	2,838	2,838
Gross fixed assets	9,634	9,841	11,041	12,341
Less: Depreciation	-3,301	-3,973	-4,885	-5,897
Add: Capital WIP	44	30	30	30
Net fixed assets	6,378	5,898	6,186	6,474
Non-current assets	2,543	4,891	4,891	4,891
<b>Total assets</b>	<b>29,554</b>	<b>31,174</b>	<b>37,570</b>	<b>43,949</b>
Current liabilities	7,822	7,461	9,212	10,346
Provisions	857	1,039	1,039	1,039
Total current liabilities	8,679	8,500	10,251	11,385
Non-current liabilities	6,897	4,279	4,279	4,279
Total liabilities	15,576	12,779	14,531	15,664
Paid-up capital	645	645	1,290	1,290
Reserves & surplus	12,961	17,603	21,484	26,599
Shareholders' equity	13,978	18,394	23,039	28,284
<b>Total equity &amp; liabilities</b>	<b>29,554</b>	<b>31,174</b>	<b>37,569</b>	<b>43,948</b>

### Cash Flow

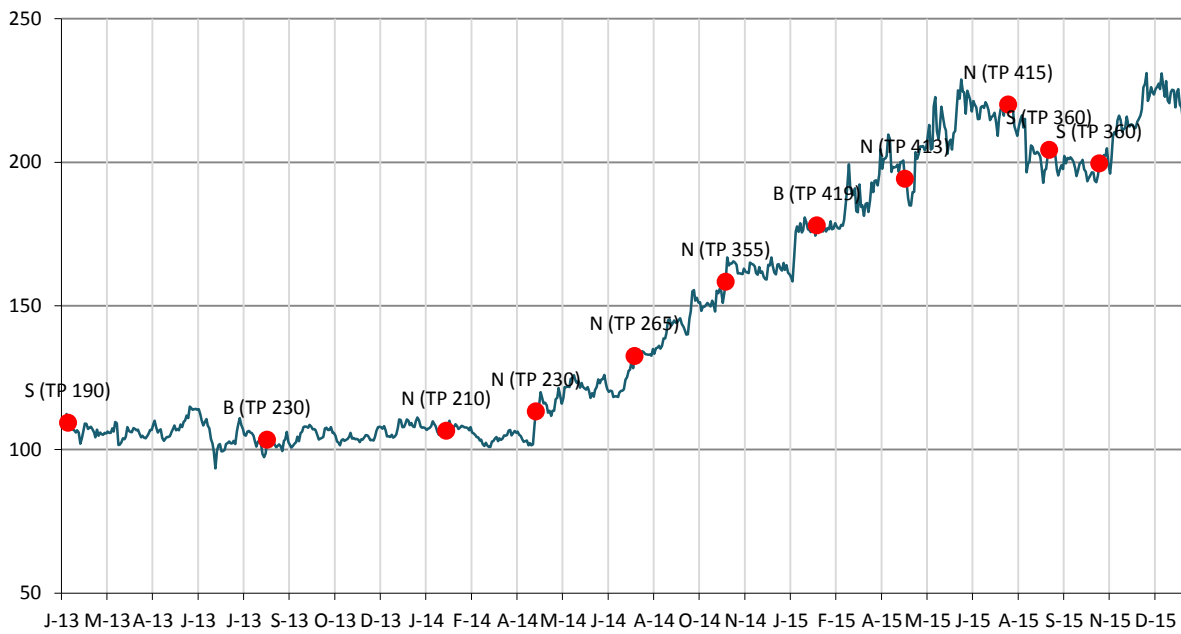
	FY14	FY15e	FY16e	FY17e
Pre-tax profit	6,850	8,051	10,357	12,384
Depreciation	769	843	912	1,012
Chg in working capital	3,153	-4,560	663	-633
Total tax paid	-1,905	-2,368	-3,003	-3,591
Other operating activities	-2,547	-820	-563	215
<b>Cash flow from operating activities</b>	<b>6,319</b>	<b>1,147</b>	<b>8,365</b>	<b>9,387</b>
Capital expenditure	912	457	-1,045	-400
Chg in investments	-1,589	267	0	0
<b>Cash flow from investing activities</b>	<b>-678</b>	<b>724</b>	<b>-1,045</b>	<b>-400</b>
Free cash flow	5,642	1,871	7,320	8,987
Equity raised/(repaid)	-1,423	-56	645	0
Debt raised/(repaid)	-1,832	-2,618	0	0
Dividend (incl. tax)	-2,673	-1,745	-2,709	-3,547
<b>Cash flow from financing activities</b>	<b>-6,108</b>	<b>-4,754</b>	<b>-2,064</b>	<b>-3,547</b>
Net chg in cash	-466	-2,883	5,256	5,439

### Valuation Ratios

	FY14	FY15e	FY16e	FY17e
<b>Per Share data</b>				
EPS (INR)	3.7	4.3	5.6	6.7
Growth, %	32.0	17.0	29.9	19.7
Book NAV/share (INR)	10.6	14.2	17.7	21.6
FDEPS (INR)	3.7	4.3	5.6	6.7
CEPS (INR)	4.3	5.0	6.3	7.5
CFPS (INR)	5.2	2.9	6.3	6.5
DPS (INR)	2.0	1.2	1.8	2.4
<b>Return ratios</b>				
Return on assets (%)	15.5	19.2	21.8	21.9
Return on equity (%)	34.9	30.5	31.8	31.0
Return on capital employed (%)	19.9	25.7	28.7	28.8
<b>Turnover ratios</b>				
Asset turnover (x)	2.8	4.4	4.5	4.8
Sales/Total assets (x)	1.4	1.9	1.8	1.7
Sales/Net FA (x)	4.5	9.3	10.1	10.6
Working capital/Sales (x)	0.1	0.1	0.1	0.1
Fixed capital/Sales (x)	0.7	0.5	0.5	0.5
Working capital days	44.8	51.8	44.4	43.9
<b>Liquidity ratios</b>				
Current ratio (x)	2.3	2.4	2.6	2.9
Quick ratio (x)	1.2	1.0	1.4	1.7
Dividend cover (x)	19.2	33.5	50.1	60.0
Dividend cover (x)	1.8	3.5	3.1	
Total debt/Equity (%)	50.6	23.4	18.8	15.3
Net debt/Equity (%)	20.8	12.2	(12.2)	(25.5)
<b>Valuation</b>				
PER (x)	61.3	52.3	40.3	33.7
Price/Book (x)	21.4	16.0	12.8	10.5
Yield (%)	0.9	0.6	0.8	
EV/Net sales (x)	6.3	5.1	4.7	4.2
EV/EBITDA (x)	39.9	34.4	27.0	22.3
EV/EBIT (x)	44.5	38.2	29.5	24.3

Source: Company, PhillipCapital India Research Estimates

### 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**

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