

# Hindustan Unilever

<b>BSE SENSEX</b>	<b>S&amp;P CNX</b>
25,991	7,749
Bloomberg	HUVR IN
Equity Shares (m)	2,163.1
MCap INR b/USD b	1,484.9/24.7
52-Week Range (INR)	691/536
1, 6, 12 Rel. Per (%)	8/-5/-28

## Financials & Valuation (INR b)

Y/E MAR	2015E	2016E	2017E
Net Sales	308.8	348.7	400.9
EBITDA	52.3	59.4	68.5
Adj PAT	40.1	44.7	49.8
AdjEPS(INR)	18.5	20.7	23.0
Gr. (%)	10.2	11.5	11.4
BV/Sh (INR)	17.3	19.3	21.2
RoE (%)	114.3	113.1	113.8
RoCE (%)	148.0	149.3	155.6
P/E (x)	37.0	33.2	29.8
P/BV (x)	39.7	35.6	32.4

**CMP: INR686**
**TP: INR620**
**Sell**

- HUVR's 1QFY15 performance was ahead of expectations with sales growth of 13.3% to INR77.1b (est. 74.5b) led by volume growth of 6%, EBITDA growth of 18.3% to INR12.8b (est. INR12.1b) and adjusted PAT growth of 14.2% to INR10.1b.
- Key positives: a) Double digit sales growth across all segments. b) Strong EBIT growth of 21.1% and 27.4% for the S&D and PP segment respectively along with 270bp margin expansion in PP.
- Gross margin contracted 60bp to 48.3% (est. 49.3%) despite price hikes in Soaps and curtailment of promotions. Savings in ad spends (down 80bp to 12.2%), other expenses (down 20bp to 14.6%) and staff cost (down 20bp to 4.8%) led to EBITDA margin expansion of 70bp to 16.6% (est. 16.3%) despite higher royalty rates. Adjusting for the INR324.4mn credit in employee expenses pertaining to unutilized pension corpus, EBITDA registered robust 18.3% YoY growth to INR 12.8b (est. INR12.1b)
- Other income was up 14.3% YoY to INR 2.02b (est. INR2.03b). Flat depreciation and interest expenses aided the 18.8% PBT growth. Recurring tax rate increased 290 bps YoY to 28.5%, dragging the PAT growth marginally to 14.2% to INR10.1b (est. INR 9.6b).
- S&D posted 12.9% sales growth; led by pricing (soaps) and mix improvement (detergents). EBIT grew 21.1% with 90bp margin expansion to 13.8%.
- Personal products sales grew 27.4% led by double digit growth in Hair Care. PP margins expanded 80bp YoY to 27.6% on account of pick up in F&L and lower ad spends. F&L re-launch continued to build momentum, per management.
- Valuations & view:** We have revised our estimates upwards by 2-3%. While HUVR's 1QFY15 performance was healthy given the overall market context and relatively subdued performance of its FMCG peers, given the premium valuations it trades at, (37.0x FY15 and 33.2x FY16 EPS) we see little room, if any, for upside. Maintain **Sell** with a revised target price of INR620 (30x FY16 EPS).

## Quarterly performance

Y/E March	FY14				FY15				(INR Million)			
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE	FY14	FY15E	Estimate	Variance
Volume Growth (%)	4.0	5.0	4.0	3.0	5.0	5.0	6.0	6.0	4.0	5.5	5.0	
Net Sales (incl service inc)	68,090	68,926	72,234	70,941	77,163	76,853	81,624	78,896	280,191	314,536	74,559	3.5%
YoY Change (%)	6.7	9.2	8.5	9.7	13.3	11.5	13.0	11.2	26.7	12.3	9.5	
COGS	34,828	34,699	36,601	37,308	39,896	38,273	40,975	39,703	143,436	158,847	37,801	5.5%
Gross Profit	33,262	34,227	35,633	33,633	37,267	38,580	40,649	39,193	136,755	155,689	36,758	1.4%
Margin %	48.9	49.7	49.3	47.4	48.3	50.2	49.8	49.7	48.8	49.5	49.3	
Operating Exp	22,406	23,374	23,365	22,857	24,426	26,053	26,365	26,550	92,003	103,394	24,604	-0.7%
% to sales	32.9	33.9	32.3	32.2	31.7	33.9	32.3	33.7	32.8	32.9	33.0	
EBITDA	10,856	10,853	12,268	10,776	12,841	12,527	14,284	12,643	44,753	52,295	12,153	5.7%
YoY Change (%)	12.3	11.1	12.7	10.9	18.3	15.4	16.4	17.3	36.0	16.9	11.9	
Margins (%)	15.9	15.7	17.0	15.2	16.6	16.3	17.5	16.0	16.0	16.6	16.3	
Depreciation	664	639	644	658	667	769	816	597	2,606	2,849	746	-10.5%
Interest	62	63	182	53	63	75	75	88	360	301	75	
Other Income	1,768	1,510	1,427	1,506	2,021	1,736	1,641	1,932	6,210	7,330	2,033	
PBT	11,897	11,661	12,868	11,571	14,132	13,420	15,033	13,890	47,997	56,476	13,365	5.7%
Tax	3,046	2,831	3,321	3,246	4,026	3,825	4,435	4,092	12,444	16,378	3,742	
Rate (%)	25.6	24.3	25.8	28.1	28.5	28.5	29.5	29.5	25.9	29.0	28.0	
Adjusted PAT	8,851	8,830	9,547	8,325	10,106	9,595	10,599	9,798	35,553	40,097	9,623	5.0%
YoY Change (%)	3.6	9.6	9.4	6.6	14.2	8.7	11.0	17.7	37.1	12.8	8.7	

E: MOSL Estimates

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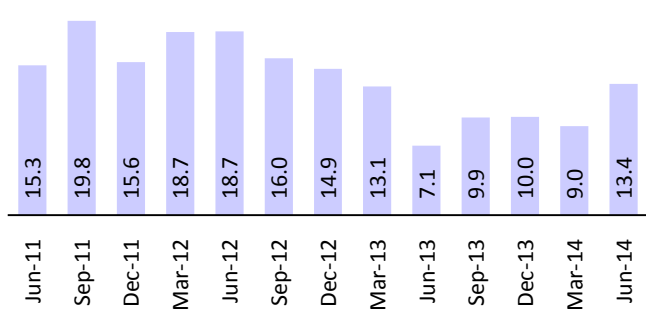
Investors are advised to refer through disclosures made at the end of the Research Report.

**1QFY15 volumes up 6%; EBITDA margins expands 7bp YoY**

- Sales grew 13.3% to INR77.2b (est. INR74.6b), led by volume growth of 6% (est. 5%). Domestic FMCG business growth at 13.4% was best in 6 quarters, with HPC growing at 13.3% and Foods reporting a growth of 13.4%.
- Volume growth for the quarter came in at 6%. However adjusting for the low base post pipeline filling in 4Q13 ahead of transporter's strike volume growth would have been 5%.
- Gross margin declined 60bp to 48.3% led by RM inflation.
- Savings in ad spends (down 80bp to 12.2%), other expenses (down 20bp to 14.6%) and staff cost (down 20bp to 4.8%) led to EBITDA margin expansion of 70bp to 16.6% (est. 16.3%).
- We have taken INR324.4m credit in employee expenses pertaining to adjustments in unutilized pension corpus as exceptional item (company, in its calculation of PAT before exceptional has treated it as recurring item).
- Thus, EBITDA registered robust 18.3% YoY growth to INR 12.8b (est. INR12.1b)
- Other income was up 14.3% YoY to INR 2.02b (est. INR2.03b). Flat depreciation and interest expenses aided the 18.8% PBT growth.
- Recurring tax rate increased 290bp YoY to 28.5%, dragging the PAT growth marginally to 14.2% to INR10.1b (est. INR 9.6b).

**Domestic FMCG sales up 13.4%; best in six quarters**

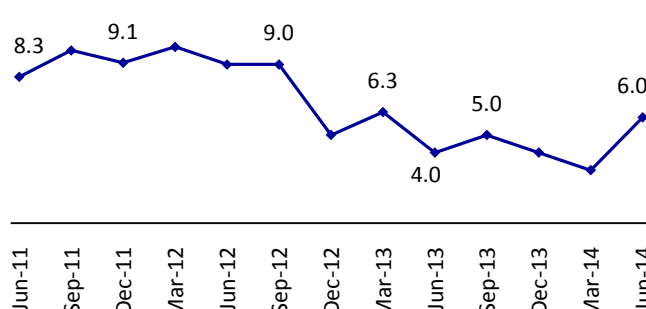
■ FMCG Sales Growth (%)



Source: MOSL, Company

**HUVR posted 6% volume growth in 1Q**

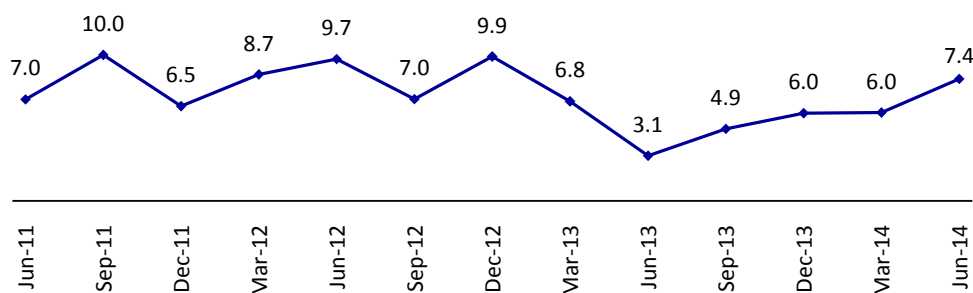
— Volume growth (%)



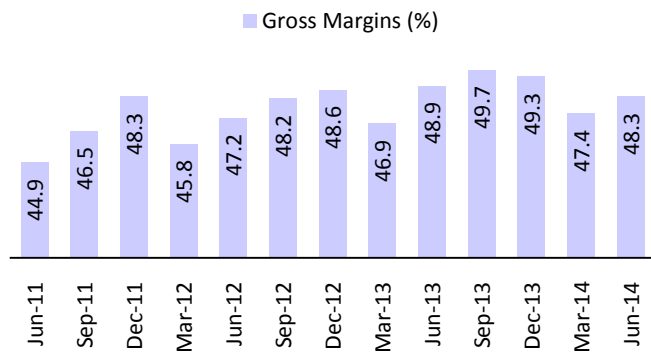
Source: MOSL, Company

**Pricing growth picks up QoQ**

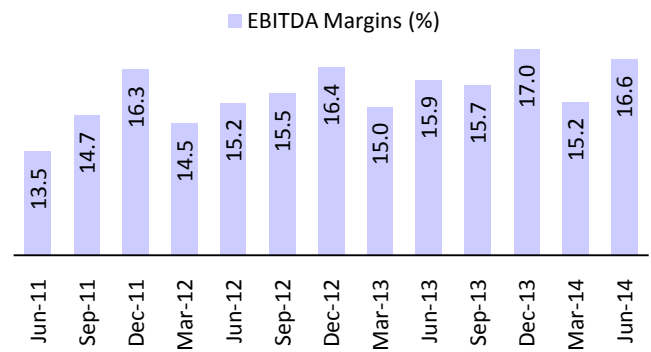
— Pricing growth %



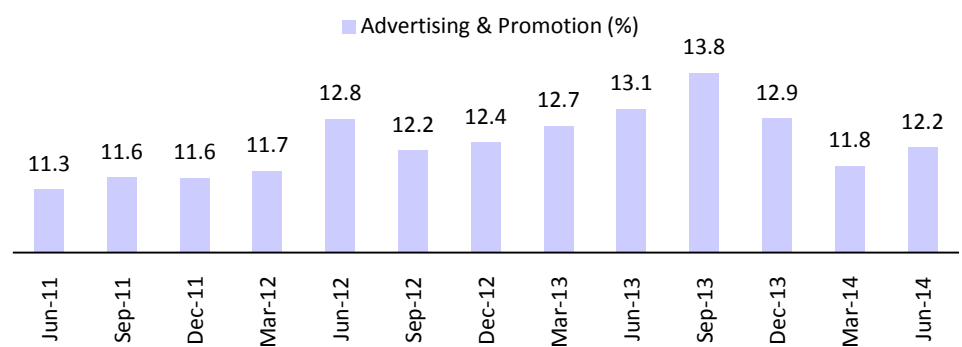
Source: MOSL, Company

**Gross margins contracted 60bp in 1Q**

Source: Company, MOSL

**While EBITDA margins expanded 70bp**

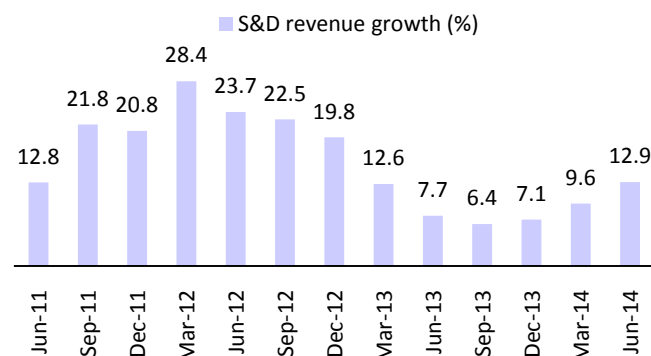
Source: Company, MOSL

**A&P down 90bp YoY; media intensity came off as per management**

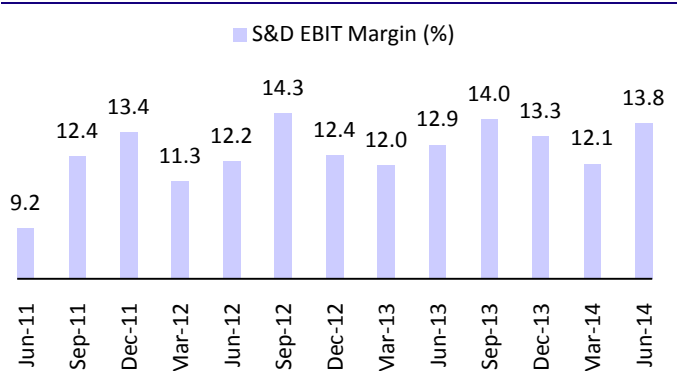
Source: Company, MOSL

**Soaps and Detergents**

- Soaps and Detergent: S&D sales grew 12.9% YoY with Soaps performance led by pricing while Detergents saw mix improvement with Surf delivering double digit growth.
- Skin cleansing witnessed double digit growth driven by pricing action to offset palm oil inflation. Pears, Lux, Liril, Hamam and Lifebuoy posted double digit growth.
- Detergents performance was driven by Surf & Rin while Wheel is seeing good traction after the re-launch in 3Q14.
- Margins expanded 90bp YoY to 13.8% driven by pricing actions and promotions withdrawal.

**S&D posted 12.9% sales growth in 1Q; aided by pricing**

Source: MOSL, Company

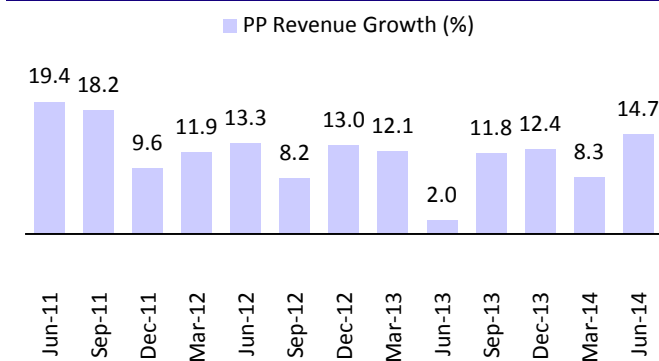
**S&D EBIT margins expanded 90bp YoY**

Source: MOSL, Company

### Personal Products

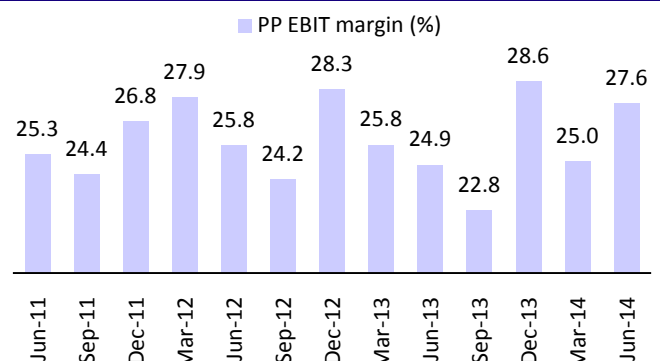
- Personal Products: Sales grew 14.7%, helped by low base (2% growth in base). Shampoos posted another quarter of double digit growth. However, sachets and small packs outperformed bottles in Hair Care.
- F&L was re-launched towards the end of 2Q14 with changed packaging and formulation. Since then it has gained traction and recovery continued even in 1Q15. Any improvement in F&L adds delta to PP EBIT margins and drives mix improvement.
- Oral Care performance was mixed. Pepsodent was impacted by high competitive intensity in the category while Close Up delivered double digit growth.
- EBIT margins expanded 280bps YoY to 27.6% owing to mix improvement and lower adspends.

PP sales up 14.7% on lower base; F&L gains traction



Source: MOSL, Company

PP EBIT margins expanded 270bp YoY led by mix improvement

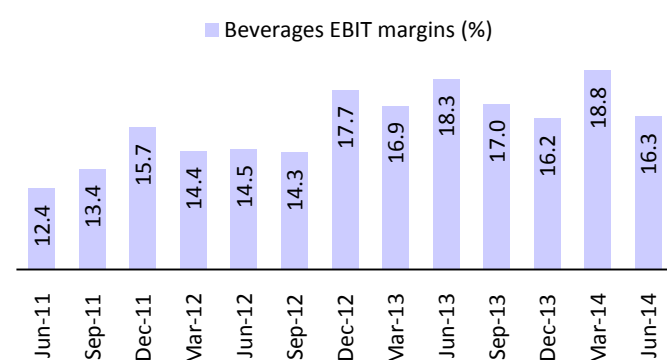


Source: MOSL, Company

### Beverages & Processed Foods

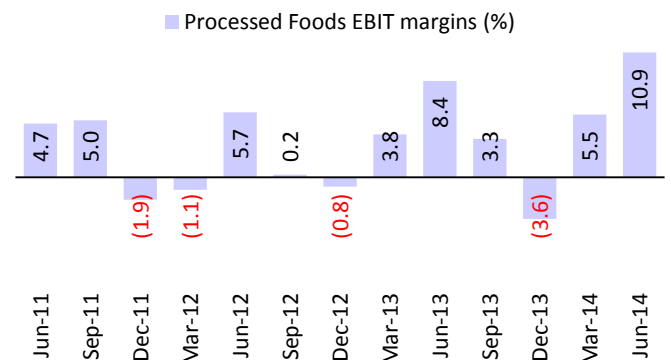
- **Beverages:** Sales were up 10.5% YoY driven by volumes as pricing component has fade off further in Tea.
- Margins declined 200bps YoY to 16.3%. EBIT declined 1.8% YoY.
- **Processed Foods:** Sales growth of 18.8% was led by Kissan, Knorr Soups (more than doubled volumes YoY) and Ice Creams. EBIT posted solid 53.8% growth with 250bps YoY margin expansion to 10.9%.

Beverages EBIT margins down 200bp YoY



Source: MOSL, Company

Processed foods margins expand 250bps YoY



Source: MOSL, Company

**Segmental snapshot**

Segmental	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14	2QFY14	3QFY14	4QFY14	1QFY15	Change %
<b>Net Sales (INR m)</b>										
Soaps and Detergents	31,631	31,762	31,712	31,914	34,077	33,808	33,979	34,971	38,476	12.9
Personal Products	18,471	17,445	20,489	18,311	18,834	19,503	23,039	19,833	21,596	14.7
Beverages	6,541	7,196	7,929	8,081	7,574	8,354	8,500	8,690	8,366	10.5
Processed Foods	4,370	3,663	3,301	3,723	4,579	3,980	3,728	4,197	5,438	18.8
Others	2,640	2,884	2,902	2,502	2,791	3,049	2,766	2,958	3,029	8.5
<b>EBIT (INR m)</b>										
Soaps and Detergents	3,852	4,536	3,937	3,830	4,393	4,739	4,509	4,217	5,318	21.1
Personal Products	4,757	4,226	5,789	4,717	4,682	4,449	6,592	4,958	5,967	27.4
Beverages	950	1,031	1,404	1,362	1,387	1,417	1,373	1,630	1,363	-1.8
Processed Foods	248	9	-26	140	384	133	-134	230	591	53.8
Others	-43	21	-186	-181	-31	46	-135	-251	-155	401.6
<b>EBIT Margin (%)</b>										
Soaps and Detergents	12.2	14.3	12.4	12.0	12.9	14.0	13.3	12.1	13.8	
Personal Products	25.8	24.2	28.3	25.8	24.9	22.8	28.6	25.0	27.6	
Beverages	14.5	14.3	17.7	16.9	18.3	17.0	16.2	18.8	16.3	
Processed Foods	5.7	0.2	-0.8	3.8	8.4	3.3	-3.6	5.5	10.9	

Source: Company, MOSL

**Concall highlights**

- Market growth slowed down further in JQ14.
- Media intensity has come off though competitive intensity remains high.
- Hair Care: Shampoo sachets grow > bottles. Aspiration to buy premium products being met via smaller packs / sku's.
- Oral care: Small packs leading growth
- Skin Care: F&L continued to recover post re-launch.
- Tea: Pricing growth fading off.
- Knorr: Instant soups sales more than doubled.
- Coffee bounced back to double digit growth.
- Modern Trade growth is significantly lower vs. earlier but is stabilizing.
- PP margin expansion: Recovery in F&L business plus relatively benign media intensity drove margin expansion in PP.
- Packaged Foods is a very nascent category and HUL will continue to focus on developing emerging categories.

**Valuation and view: Expensive valuations + weak volume growth backdrop; Maintain Sell**

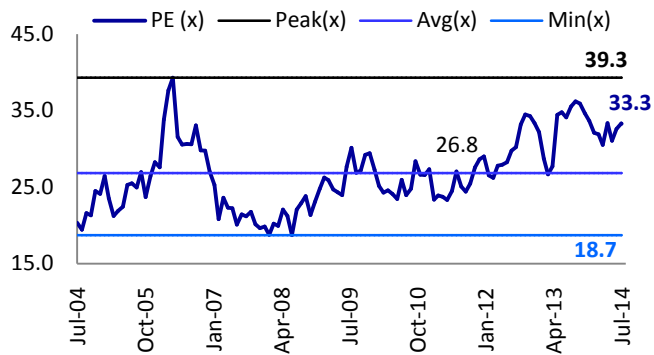
- We have revised our estimates upwards by 2-3% to cognise for better than expected 1QFY15 performance.
- While HUV's 1QFY15 performance was healthy given the overall market context and relatively subdued performance of its FMCG peers, given the premium valuations it trades at, (37.0x FY15 and 33.2x FY16 EPS) we see little room, if any, for upside.
- Maintain **Sell** with a revised target price of INR620 (30x FY16 EPS).

## Revised estimates upwards 2-3%

	New			Old			Change		
	FY15E	FY16E	FY17E	FY15E	FY16E	FY17E	FY15E	FY16E	FY17E
<b>Sales</b>	314,536	355,225	409,068	313,376	353,589	407,206	0.4%	0.4%	0.5%
<b>EBITDA</b>	52,295	59,390	68,513	51,183	58,400	66,870	2.2%	2.2%	1.7%
<b>PAT</b>	40,097	44,702	49,779	39,124	43,379	48,228	2.5%	2.5%	3.1%

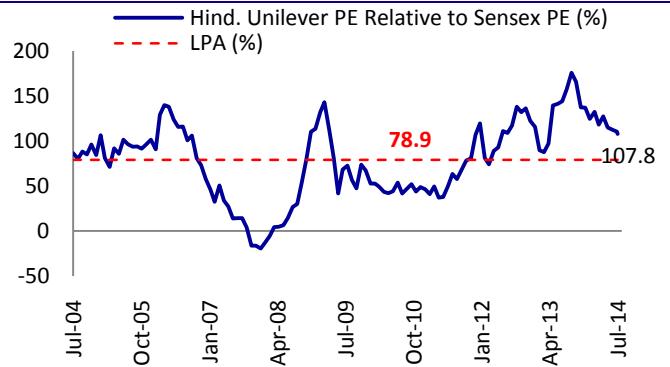
Source: Company, MOSL

## P/E multiple still rich



Source: Company, MOSL

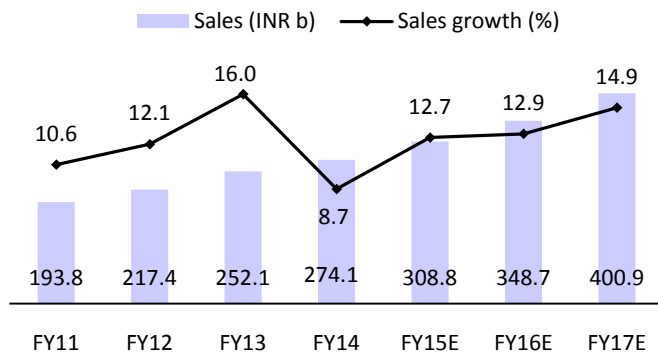
## Relative valuations have corrected a bit



Source: Company, MOSL

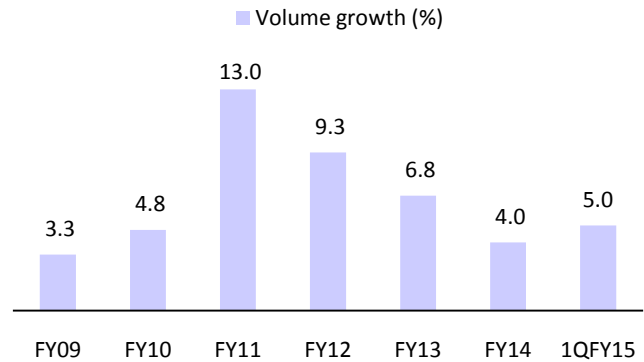
## Story in Charts

### Sales growth moderated to high single digits in FY14



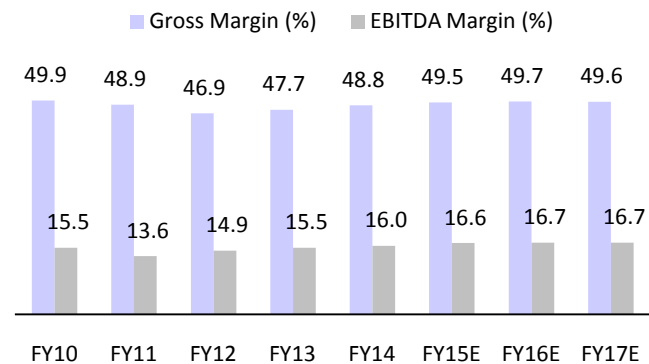
Source: Company, MOSL

### ..led by softness in broad based portfolio volume growth



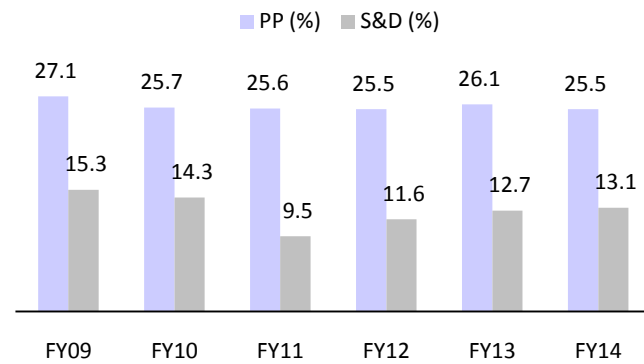
Source: Company, MOSL

### EBITDA margins were up 50bps YoY in FY14



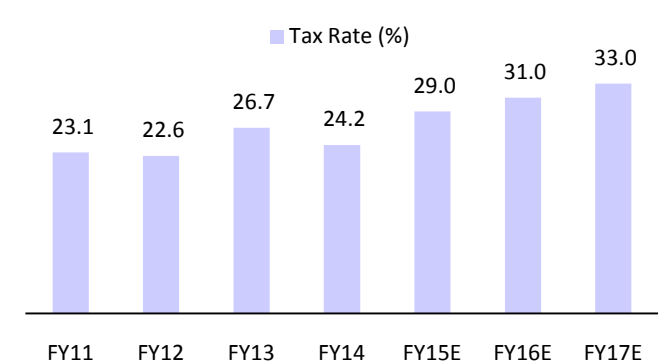
Source: Company, MOSL

### Driven by 40bp increase in S&D EBIT margins



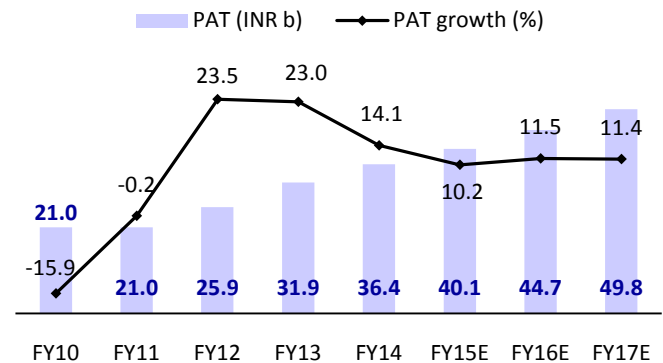
Source: Company, MOSL

### Increasing tax rate owing to completion of tax holidays



Source: Company, MOSL

### PAT growth down to mid single digits in FY14



Source: Company, MOSL

## Hindustan Unilever: an investment profile

### Company description

HUL is the largest company in the FMCG industry, with market leadership in soaps, detergents and personal care categories. It has a wide distribution network with direct reach of over 1m retail outlets. The company is a subsidiary of Anglo Dutch FMCG giant Unilever.

### Key investment argument

- Market leader in most of the categories and has strong brands.
- Wide product range across categories, with presence at all price points.
- Decline in raw material prices would result in margins improvement.

### Key investment risk

- Slowdown in GDP is showing lagged impact on consumption. This poses biggest risk to HUL's volumes.
- Competitive pressure has intensified with more companies entering personal care and toilet soap and detergents, which account for 80% of HUL's profits.

### Recent developments

- Relaunched Pears and Wheel.
- Introduced Lakme Winter Moisturizer.

### Valuation and view

- We are maintaining our **Sell** rating owing to expensive valuations and subdued demand outlook.
- HUL's valuations (37x FY15E and 33.2x FY16E) does not leave any margin for error given the market context of slowing consumption growth.

### Sector view

- We have a cautious view on the sector on back of inflationary pressure in the economy.
- Companies with competitive position would be better placed to withstand any slowdown in a particular segment.
- Longer term prospects bright, given rising incomes and low penetration.
- We prefer companies with earnings visibility in an environment where consumption is moderating.

### Comparative valuations

		HUL	ITC	NEST
P/E (x)	FY15E	37.0	27.1	40.3
	FY16E	33.2	23.4	34.1
EV/EBITDA (x)	FY15E	27.2	18.0	23.4
	FY16E	23.9	15.5	20.1
EV/Sales (x)	FY15E	4.6	6.8	4.9
	FY16E	4.1	5.9	4.3
P/BV (x)	FY15E	39.7	11.0	19.5
	FY16E	35.6	10.0	17.8

### Shareholding pattern (%)

	Jun-14	Mar-14	Jun-13
Promoter	67.2	67.3	52.5
DII	4.1	4.1	7.1
FII	14.6	14.1	20.2
Others	14.1	14.5	20.2

Note: FII Includes depository receipts

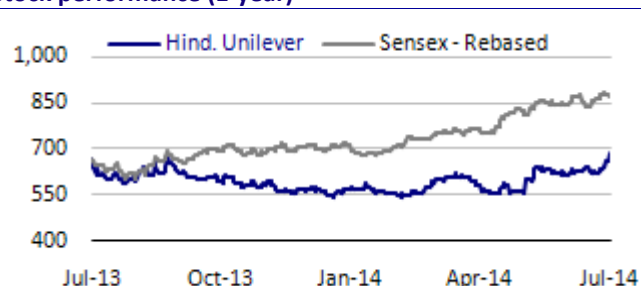
### EPS: MOSL forecast v/s consensus (INR)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY15	18.5	18.4	0.4
FY16	20.7	20.5	0.9

### Target price and recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
686	620	-9.7	Sell

### Stock performance (1-year)



## Financials and valuation

Income statement		(INR Billion)			
Y/E March	2014	2015E	2016E	2017E	
<b>Net Sales</b>	<b>274.1</b>	<b>308.8</b>	<b>348.7</b>	<b>400.9</b>	
Change (%)	8.7	12.7	12.9	14.9	
<b>EBITDA</b>	<b>44.8</b>	<b>52.3</b>	<b>59.4</b>	<b>68.5</b>	
EBITDA Margin (%)	16.0	16.6	16.7	16.7	
Depreciation	2.6	2.8	3.1	3.5	
<b>EBIT</b>	<b>42.1</b>	<b>49.4</b>	<b>56.3</b>	<b>65.0</b>	
Interest	0.4	0.3	0.3	0.3	
Other Income	6.2	7.3	8.7	9.5	
<b>PBT</b>	<b>48.0</b>	<b>56.5</b>	<b>64.8</b>	<b>74.3</b>	
Tax	11.6	16.4	20.1	24.5	
Tax Rate (%)	24.2	29.0	31.0	33.0	
<b>Profit After Taxes</b>	<b>36.4</b>	<b>40.1</b>	<b>44.7</b>	<b>49.8</b>	
Non-rec. (Exp)/Income	2.3	0.0	0.0	0.0	
<b>Reported PAT</b>	<b>38.7</b>	<b>40.1</b>	<b>44.7</b>	<b>49.8</b>	
Change (%)	3.7	3.6	11.5	11.4	

Balance sheet		(INR Billion)			
Y/E March	2014	2015E	2016E	2017E	
Share Capital	2.2	2.2	2.2	2.2	
Reserves	30.6	35.3	39.5	43.7	
<b>Net Worth</b>	<b>32.8</b>	<b>37.4</b>	<b>41.6</b>	<b>45.9</b>	
Debt	0.0	0.0	0.0	0.0	
Deferred Tax	-1.6	-1.7	-1.9	-2.0	
<b>Total Capital Employed</b>	<b>31.2</b>	<b>35.7</b>	<b>39.8</b>	<b>43.8</b>	
Gross Fixed Assets	45.5	49.5	53.5	58.5	
Less: Acc Depreciation	-17.4	-20.3	-23.3	-26.8	
<b>Net Fixed Assets</b>	<b>28.1</b>	<b>29.2</b>	<b>30.1</b>	<b>31.7</b>	
Capital WIP	3.1	2.5	2.5	2.5	
Investments	48.4	56.0	59.5	63.8	
<b>Current Assets</b>	<b>48.8</b>	<b>54.2</b>	<b>64.5</b>	<b>76.8</b>	
Inventory	27.5	32.5	36.7	43.6	
Debtors	8.2	10.2	14.3	16.5	
Cash & Bank	7.0	5.2	7.0	10.0	
Loans & Adv, Others	6.1	6.3	6.5	6.7	
<b>Curr Liabs &amp; Provns</b>	<b>97.2</b>	<b>106.2</b>	<b>116.9</b>	<b>130.9</b>	
Curr. Liabilities	79.8	87.3	96.6	109.0	
Provisions	17.4	18.9	20.4	21.9	
<b>Net Current Assets</b>	<b>-48.4</b>	<b>-52.0</b>	<b>-52.4</b>	<b>-54.1</b>	
<b>Total Assets</b>	<b>31.2</b>	<b>35.7</b>	<b>39.8</b>	<b>43.8</b>	

E: MOSL Estimates

Ratios					
Y/E March	2014	2015E	2016E	2017E	
<b>Basic (INR)</b>					
<b>EPS</b>	<b>16.8</b>	<b>18.5</b>	<b>20.7</b>	<b>23.0</b>	
Cash EPS	18.0	19.9	22.1	24.6	
Book Value	15.2	17.3	19.3	21.2	
DPS	13.0	14.0	16.0	18.0	
Payout (incl. Div. Tax.)	77.3	75.5	77.4	78.2	
<b>Valuation(x)</b>					
P/E	40.8	37.0	33.2	29.8	
Cash P/E	38.1	34.6	31.1	27.9	
Price / Book Value	45.3	39.7	35.6	32.4	
EV/Sales	5.2	4.6	4.1	3.5	
EV/EBITDA	31.9	27.2	23.9	20.6	
Dividend Yield (%)	1.9	2.0	2.3	2.6	
<b>Profitability Ratios (%)</b>					
RoE	122.3	114.3	113.1	113.8	
RoCE	151.0	148.0	149.3	155.6	

<b>Turnover Ratios (%)</b>					
Asset Turnover (x)	8.4	8.2	8.4	8.7	
Debtors (No. of Days)	10.9	12.0	15.0	15.0	
<b>Leverage Ratios (%)</b>					
Debt/Equity (x)	0.0	0.0	0.0	0.0	

Cash flow statement		(INR Billion)			
Y/E March	2014	2015E	2016E	2017E	
OP/(Loss) before Tax	44.8	52.3	59.4	68.5	
Interest	5.9	7.0	8.5	9.3	
Direct Taxes Paid	-11.4	-15.8	-19.4	-23.8	
(Inc)/Dec in Wkg Cap	7.9	1.8	2.2	4.8	
Others	0.4	-0.1	-0.1	-0.2	
Extraordinary items (net)	2.3	0.0	0.0	0.0	
<b>CF from Op. Activity</b>	<b>72.6</b>	<b>76.8</b>	<b>89.3</b>	<b>106.2</b>	
(Inc)/Dec in FA & CWIP	-4.1	-3.4	-4.0	-5.0	
(Pur)/Sale of Invnt	-8.8	-7.6	-3.6	-4.3	
<b>CF from Inv. Activity</b>	<b>-12.9</b>	<b>-10.9</b>	<b>-7.6</b>	<b>-9.3</b>	
Inc/(Dec) in Net Worth	0.1	0.0	0.0	0.0	
Inc / (Dec) in Debt	0.0	0.0	0.0	0.0	
Other Financing Activities	-23.9	-32.2	-39.5	-48.3	
Divd Paid (incl Tax)	-32.8	-35.4	-40.5	-45.5	
<b>CF from Fin. Activity</b>	<b>-56.6</b>	<b>-67.6</b>	<b>-80.0</b>	<b>-93.8</b>	
<b>Inc/(Dec) in Cash</b>	<b>3.1</b>	<b>-1.8</b>	<b>1.7</b>	<b>3.0</b>	
Add: Opening Balance	4.0	7.0	5.2	7.0	
<b>Closing Balance</b>	<b>7.0</b>	<b>5.2</b>	<b>7.0</b>	<b>10.0</b>	

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