

Institutional Equity Research

# Hindustan Unilever

FMCG | India

3QFY18 Result Update | January 18, 2018

|                        |         |
|------------------------|---------|
| CMP* (Rs)              | 1,371   |
| Upside/ (Downside) (%) | 10      |
| Bloomberg Ticker       | HUVR IN |
| Market Cap. (Rs bn)    | 2,961   |
| Free Float (%)         | 33      |
| Shares O/S (mn)        | 2164    |

**BUY** 

Target Price: Rs1,514

## Stellar Performance on Lower Base & Demand Recovery

On the back of lower base effect coupled with increased growth momentum, Hindustan Unilever (HUL) has reported strong set of numbers for 3QFY18. While net sales came in at Rs83.2bn (vs. our estimate of Rs83.7bn), EBITDA grew by 24% YoY to Rs16.8bn (vs. our estimate of Rs16.5bn) and net profit before exceptional items surged 30.2% YoY to Rs12bn (vs. our estimate of Rs11bn). Revenues on comparable base grew by a healthy 17% YoY. Growth in net profit was also aided by 83% YoY increase in other income to Rs1.5bn (Dividend from subsidiary). Volume growth for the quarter was largely in line at 11% YoY, which can be attributed to lower base effect (4% YoY volume de-growth in 3QFY17).

Looking ahead, we believe strong recovery in rural demand, increasing footprint in ayurvedic space, continued trend of premiumisation, benefits of GST and cost savings will drive 11.6% revenue and 17.5% earnings CAGR for HUL through FY17-20E. **We maintain our BUY recommendation on the stock with a revised Target Price of Rs1,514 (from Rs1,429 earlier).**

### Lower Base Aids Volume Growth

A healthy 11% YoY growth in volume not only reflects lower base effect but also recovery in growth across channels. Home Care segment witnessed comparable sales growth of 20%YoY with double-digit volume growth, while Personal Care segment reported 17% YoY revenue growth on comparable basis. The Management stated that the trade conditions have normalised with gradual improvement in demand. We expect volume growth trajectory to be around 6-7% in the coming quarters.

### Premiumisation & Cost Savings to Drive Margins

Gross margins improved 290bps YoY to 53.1% aided by lower input cost on YoY basis and continued focus on premiumisation. However, input prices have been increasing sequentially, which could impact gross margins in coming quarters unless HUL undertakes commensurate price hikes. While A&P spend increased by 150bps YoY to 13.3% of sales, on absolute basis A&P grew by 25% YoY to Rs11.1bn to aid new product launches such as Ayush and renovations. Other expenses declined by 60bps YoY owing to continued focus on cost saving. Resultant EBITDA margins expanded 200bps YoY to 19.6% of sales(110bps on comparable basis).

### Outlook & Valuation

With disruptions relating to GST coming to an end, we expect recovery in the growth numbers in coming quarters. HUL derives ~35-40% revenues from rural markets, which is expected to lead the overall FMCG growth on the back of normal monsoons for two consecutive years, recovery in MSPs of key crops and increased direct distribution reach. Based on expected EPS of 31.9, the stock currently trades at rich multiples of 42.9x FY20E earnings. **We maintain our BUY recommendation on the stock with a revised Target Price of Rs1,514 (from Rs1,429 earlier).**

| Key Financials (Rs mn) | FY17    | FY18E   | FY19E   | FY20E   |
|------------------------|---------|---------|---------|---------|
| Sales                  | 312,980 | 340,833 | 385,149 | 435,549 |
| EBITDA                 | 54,550  | 65,505  | 76,093  | 87,739  |
| Net profit             | 42,490  | 51,723  | 59,975  | 68,992  |
| EPS (Rs)               | 19.7    | 23.9    | 27.8    | 31.9    |
| DPS (Rs)               | 17.0    | 20.0    | 23.0    | 26.0    |
| P/E (x)                | 69.7    | 57.3    | 49.4    | 42.9    |
| P/B (x)                | 45.6    | 45.4    | 45.0    | 43.8    |
| EV/EBITDA (x)          | 53.4    | 44.6    | 38.3    | 33.2    |
| ROE (%)                | 66.6    | 79.5    | 91.5    | 103.4   |
| Dividend yield (%)     | 1.2     | 1.5     | 1.7     | 1.9     |

Source: Company, RSec Research

| Share price (%)      | 1 mth | 3 mth | 12 mth |
|----------------------|-------|-------|--------|
| Absolute performance | 2.0   | 10.7  | 52.9   |
| Relative to Nifty    | (2.2) | 7.5   | 34.4   |

| Shareholding Pattern (%) | Sep'17 | Dec'17 |
|--------------------------|--------|--------|
| Promoter                 | 67.2   | 67.2   |
| Public                   | 32.8   | 32.8   |

### 1 Year Stock Price Performance



Note: \* CMP as on Jan. 17, 2018

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**BUY** 

Target Price: Rs1,514

### Risks to the View

- ▶ Delay in recovery in consumer demand
- ▶ Sharp spike in input costs

Exhibit 1: Trend in quarterly revenue growth

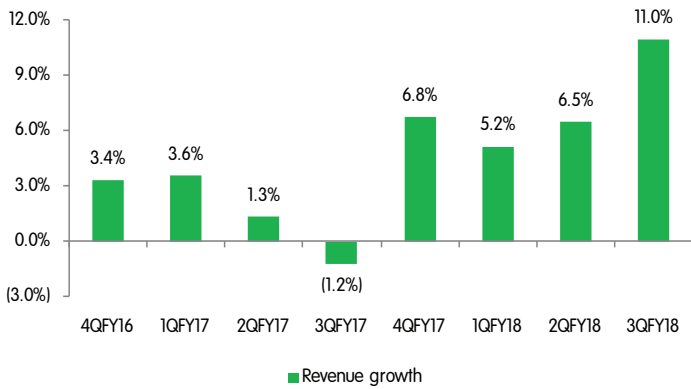
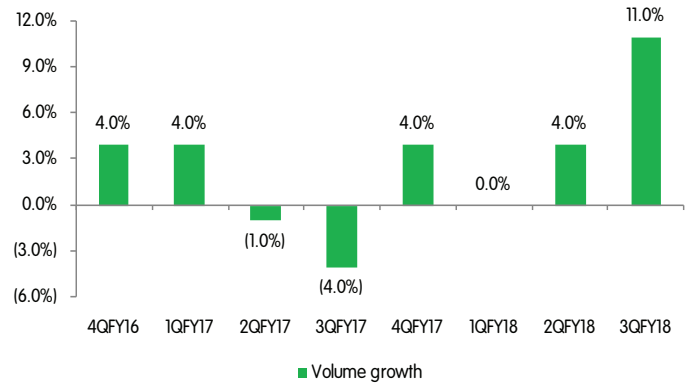


Exhibit 2: Quarterly volume growth



Source: Company, RSec Research

Exhibit 3: Trend in gross margins

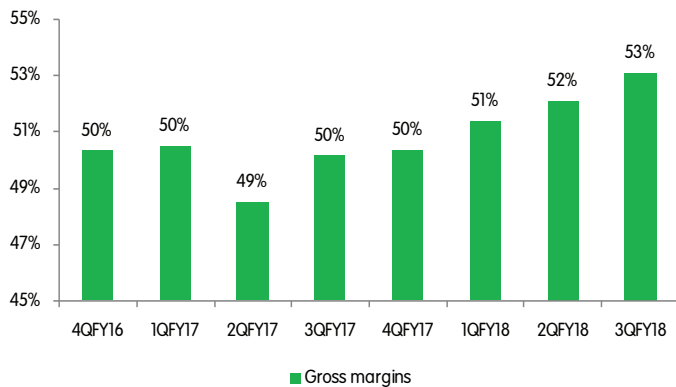
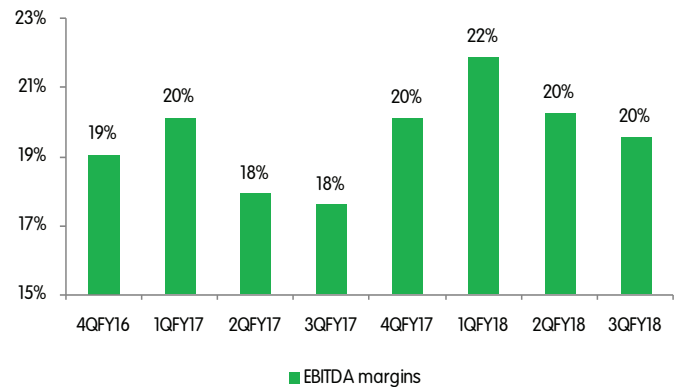


Exhibit 4: Trend in EBITDA margins



Source: Company, RSec Research

Exhibit 5: Trend in A&P to sales

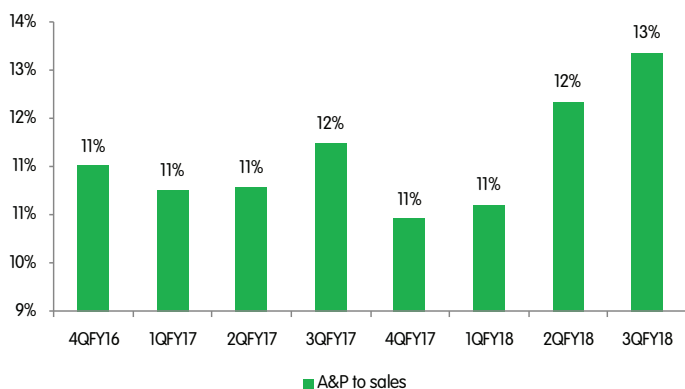
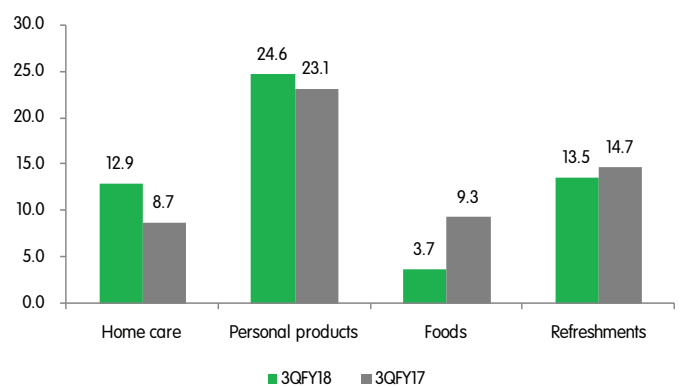


Exhibit 6: Quarterly segmental margins



Source: Company, RSec Research

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**BUY** 

Target Price: Rs1,514

## Exhibit 7: Income Statement Analysis

| (Rs mn)                  | 3QFY18        | 3QFY17        | % yoy       | 2QFY18        | % qoq         | 9MFY18         | 9MFY17         | % yoy       |
|--------------------------|---------------|---------------|-------------|---------------|---------------|----------------|----------------|-------------|
| <b>Net Sales</b>         | <b>83,230</b> | <b>75,120</b> | <b>10.8</b> | <b>81,990</b> | <b>1.5</b>    | <b>249,230</b> | <b>231,980</b> | <b>7.4</b>  |
| Consumption of RM        | 39,050        | 37,440        | 4.3         | 39,290        | (0.6)         | 119,180        | 116,620        | 2.2         |
| (% of Sales)             | 46.9          | 49.8          |             | 47.9          |               | 47.8           | 50.3           |             |
| Staff Costs              | 4,910         | 4,090         | 20.0        | 4,350         | 12.9          | 13,450         | 12,320         | 9.2         |
| (% of Sales)             | 5.9           | 5.4           |             | 5.3           |               | 5.4            | 5.3            |             |
| Advertising              | 11,070        | 8,850         | 25.1        | 10,230        | 8.2           | 30,350         | 26,160         | 16.0        |
| (% of Sales)             | 13.3          | 11.8          |             | 12.5          |               | 12.2           | 11.3           |             |
| Other Expenses           | 14,070        | 13,120        | 7.2         | 12,400        | 13.5          | 39,020         | 37,720         | 3.4         |
| (% of Sales)             | 16.9          | 17.5          |             | 15.1          |               | 15.7           | 16.3           |             |
| <b>Total Expenditure</b> | <b>69,100</b> | <b>63,500</b> | <b>8.8</b>  | <b>66,270</b> | <b>4.3</b>    | <b>202,000</b> | <b>192,820</b> | <b>4.8</b>  |
| <b>Operating Profit</b>  | <b>14,130</b> | <b>11,620</b> | <b>21.6</b> | <b>15,720</b> | <b>(10.1)</b> | <b>47,230</b>  | <b>39,160</b>  | <b>20.6</b> |
| OPM                      | 17.0          | 15.5          |             | 19.2          |               | 19.0           | 16.9           |             |
| Depreciation             | 1,210         | 1,000         | 21.0        | 1,150         | 5.2           | 3,500          | 2,880          | 21.5        |
| <b>EBIT</b>              | <b>12,920</b> | <b>10,620</b> | <b>21.7</b> | <b>14,570</b> | <b>(11.3)</b> | <b>43,730</b>  | <b>36,280</b>  | <b>20.5</b> |
| Interest                 | 50            | 50            |             | 60            | (16.7)        | 160            | 150            |             |
| Other Income             | 4,190         | 2,760         | 51.8        | 3,140         | 33.4          | 9,740          | 9,220          | 5.6         |
| <b>PBT</b>               | <b>17,060</b> | <b>13,330</b> | <b>28.0</b> | <b>17,650</b> | <b>(3.3)</b>  | <b>53,310</b>  | <b>45,350</b>  | <b>17.6</b> |
| (% of Sales)             | 20.5          | 17.7          |             | 21.5          |               | 21.4           | 19.5           |             |
| Provision for Taxation   | 3,590         | 4,480         | (19.9)      | 5,250         | (31.6)        | 14,570         | 14,540         | 0.2         |
| (% of PBT)               | 21.0          | 33.6          |             | 29.7          |               | 27.3           | 32.1           |             |
| <b>PAT (recurring)</b>   | <b>11,980</b> | <b>9,200</b>  | <b>30.2</b> | <b>12,400</b> | <b>(3.4)</b>  | <b>37,260</b>  | <b>31,297</b>  | <b>19.1</b> |
| Extr. Income/(Expense)   | (210)         | 1,530         |             | 360           |               | 20             | 2,420          |             |
| <b>Reported PAT</b>      | <b>13,260</b> | <b>10,380</b> | <b>27.7</b> | <b>12,760</b> | <b>3.9</b>    | <b>38,760</b>  | <b>33,230</b>  | <b>16.6</b> |
| PATM                     | 15.9          | 13.8          |             | 15.6          |               | 15.6           | 14.3           |             |
| Equity shares (mn)       | 2,160         | 2,160         |             | 2,160         |               | 2,160          | 2,160          |             |
| <b>EPS (Rs)</b>          | <b>5.5</b>    | <b>4.3</b>    | <b>30.2</b> | <b>5.7</b>    | <b>(3.4)</b>  | <b>17.3</b>    | <b>14.5</b>    | <b>19.1</b> |

Source: Company, RSec Research

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**BUY** 

Target Price: Rs1,514

## Exhibit 8: Segmental Results

| (Rs mn)                            | 3QFY18        | 3QFY17        | % yoy       | 2QFY18        | % qoq          | FY17           | 9MFY17         | % yoy       |
|------------------------------------|---------------|---------------|-------------|---------------|----------------|----------------|----------------|-------------|
| <b>Segment Revnue</b>              |               |               |             |               |                |                |                |             |
| Home care                          | 27,410        | 26,890        | 1.9         | 27,390        | 0.1            | 85,270         | 83,420         | 2.2         |
| Personal products                  | 40,900        | 39,800        | 2.8         | 39,100        | 4.6            | 123,680        | 122,300        | 1.1         |
| Foods                              | 3,000         | 2,790         | 7.5         | 2,820         | 6.4            | 8,660          | 8,290          | 4.5         |
| Refreshments                       | 12,480        | 11,640        | 7.2         | 12,220        | 2.1            | 38,160         | 35,480         | 7.6         |
| Others                             | 2,110         | 1,950         | 8.2         | 1,500         | 40.7           | 5,290          | 6,170          | (14.3)      |
| <b>Total</b>                       | <b>85,900</b> | <b>83,070</b> | <b>3.4</b>  | <b>83,030</b> | <b>3.5</b>     | <b>261,060</b> | <b>255,660</b> | <b>2.1</b>  |
| Less: Intersegment sales           | -             | -             | -           | -             | -              | -              | -              | -           |
| <b>Gross sales from operations</b> | <b>85,900</b> | <b>83,070</b> | <b>3.4</b>  | <b>83,030</b> | <b>(100.0)</b> | <b>261,060</b> | <b>255,660</b> | <b>2.1</b>  |
| <b>Segment EBIT</b>                |               |               |             |               |                |                |                |             |
| Home care                          | 3,540         | 2,340         | 51.3        | 3,830         | (7.6)          | 11,850         | 870            | 1262.1      |
| Personal products                  | 10,070        | 9,210         | 9.3         | 9,480         | 6.2            | 30,340         | 28,650         | 5.9         |
| Foods                              | 110           | 260           | (57.7)      | 170           | (35.3)         | 690            | 570            | 21.1        |
| Refreshments                       | 1,690         | 1,710         | (1.2)       | 2,140         | (21.0)         | 6,380          | 5,360          | 19.0        |
| Others                             | (110)         | (160)         | -           | (60)          | -              | (230)          | (170)          | 35.3        |
| <b>Total segment PBIT</b>          | <b>15,300</b> | <b>13,360</b> | <b>14.5</b> | <b>15,560</b> | <b>(99.9)</b>  | <b>49,030</b>  | <b>35,280</b>  | <b>39.0</b> |
| <b>Segment Margins (%)</b>         |               |               |             |               |                |                |                |             |
| Home care                          | 12.9          | 8.7           | 4.2         | 14.0          | (1.1)          | 13.9           | 1.0            | 12.9        |
| Personal products                  | 24.6          | 23.1          | 1.5         | 24.2          | 0.4            | 24.5           | 23.4           | 1.1         |
| Foods                              | 3.7           | 9.3           | (5.7)       | 6.0           | (2.4)          | 8.0            | 6.9            | 1.1         |
| Refreshments                       | 13.5          | 14.7          | (1.1)       | 17.5          | (4.0)          | 16.7           | 15.1           | 1.6         |
| Others                             | (5.2)         | (8.2)         | 3.0         | (4.0)         | (1.2)          | (4.3)          | (2.8)          | (1.6)       |
| <b>Aggregate PBIT margins</b>      | <b>17.8</b>   | <b>16.1</b>   | <b>1.7</b>  | <b>18.7</b>   | <b>(17.0)</b>  | <b>18.8</b>    | <b>13.8</b>    | <b>5.0</b>  |

Source: Company, RSec Research

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**BUY** 

Target Price: Rs1,514

**Profit & Loss Statement**

| Y/E Mar (Rs mn)                  | FY17           | FY18E          | FY19E          | FY20E          |
|----------------------------------|----------------|----------------|----------------|----------------|
| <b>Net Sales</b>                 | <b>312,980</b> | <b>340,833</b> | <b>385,149</b> | <b>435,549</b> |
| <b>Total operating income</b>    | <b>312,980</b> | <b>340,833</b> | <b>385,149</b> | <b>435,549</b> |
| % chg                            | 2.6            | 8.9            | 13.0           | 13.1           |
| Total Expenditure                | 258,430        | 275,328        | 309,056        | 347,810        |
| Cost of Materials                | 156,850        | 164,452        | 186,605        | 211,024        |
| Advertising Exp (Incl Promotion) | 34,700         | 40,048         | 44,292         | 50,088         |
| Personnel                        | 16,200         | 17,658         | 19,424         | 21,366         |
| Others                           | 50,680         | 53,170         | 58,735         | 65,332         |
| <b>EBITDA</b>                    | <b>54,550</b>  | <b>65,505</b>  | <b>76,093</b>  | <b>87,739</b>  |
| % chg                            | 5.2            | 20.1           | 16.2           | 15.3           |
| (% of Net Sales)                 | 17.4           | 19.2           | 19.8           | 20.1           |
| Depreciation & Amortisation      | 3,960          | 4,682          | 5,175          | 5,677          |
| <b>EBIT</b>                      | <b>50,590</b>  | <b>60,823</b>  | <b>70,918</b>  | <b>82,062</b>  |
| % chg                            | 4.0            | 20.2           | 16.6           | 15.7           |
| (% of Net Sales)                 | 16.2           | 17.8           | 18.4           | 18.8           |
| Interest & other Charges         | 220            | 230            | 218            | 206            |
| Other Income                     | 11,180         | 12,257         | 13,772         | 15,316         |
| (% of PBT)                       | 18.2           | 16.8           | 16.3           | 15.8           |
| <b>Recurring PBT</b>             | <b>61,550</b>  | <b>72,850</b>  | <b>84,472</b>  | <b>97,172</b>  |
| % chg                            | 3.0            | 18.4           | 16.0           | 15.0           |
| <b>PBT (reported)</b>            | <b>61,550</b>  | <b>72,850</b>  | <b>84,472</b>  | <b>97,172</b>  |
| Tax                              | 19,060         | 21,126         | 24,497         | 28,180         |
| (% of PBT)                       | 31.0           | 29.0           | 29.0           | 29.0           |
| <b>PAT (recurring)</b>           | <b>42,490</b>  | <b>51,723</b>  | <b>59,975</b>  | <b>68,992</b>  |
| % chg                            | 2.0            | 21.7           | 16.0           | 15.0           |
| (% of Net Sales)                 | 13.6           | 15.2           | 15.6           | 15.8           |
| Extraordinary income             | 2,410          | 230            | -              | -              |
| <b>Net profit</b>                | <b>44,900</b>  | <b>51,953</b>  | <b>59,975</b>  | <b>68,992</b>  |
| <b>Basic EPS (Rs)</b>            | <b>19.7</b>    | <b>23.9</b>    | <b>27.8</b>    | <b>31.9</b>    |
| <b>Fully Diluted EPS (Rs)</b>    | <b>19.7</b>    | <b>23.9</b>    | <b>27.8</b>    | <b>31.9</b>    |
| % chg                            | 2.0            | 21.7           | 16.0           | 15.0           |

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Target Price: Rs1,514

## Balance Sheet

| Y/E Mar (Rs mn)          | FY17          | FY18E         | FY19E         | FY20E         |
|--------------------------|---------------|---------------|---------------|---------------|
| Share capital            | 2,160         | 2,160         | 2,160         | 2,160         |
| Reserves                 | 62,740        | 63,108        | 63,667        | 65,494        |
| Net worth                | 64,900        | 65,268        | 65,827        | 67,654        |
| Total borrowings         | 4,590         | 3,840         | 3,640         | 3,440         |
| <b>Total liabilities</b> | <b>69,490</b> | <b>69,108</b> | <b>69,467</b> | <b>71,094</b> |
| Gross block              | 68,070        | 80,570        | 88,070        | 95,570        |
| Less: Acc. depreciation  | 27,830        | 32,512        | 37,687        | 43,364        |
| Net block                | 40,240        | 48,058        | 50,383        | 52,206        |
| CWIP                     | 2,030         | 2,030         | 2,030         | 2,030         |
| Goodwill                 | -             | 1             | 2             | 3             |
| Deferred tax             | 1,600         | 1,960         | 1,960         | 1,960         |
| Investments              | 37,790        | 37,790        | 37,790        | 37,790        |
| Other assets             |               |               |               |               |
| Current assets           | 65,850        | 62,072        | 71,352        | 83,463        |
| Inventories              | 23,620        | 25,562        | 28,886        | 32,666        |
| Debtors                  | 9,280         | 10,106        | 11,420        | 12,914        |
| Cash                     | 16,710        | 8,338         | 11,159        | 16,625        |
| Loans and advances       | 16,240        | 18,066        | 19,887        | 21,257        |
| Current liabilities      | 66,340        | 69,168        | 78,641        | 88,932        |
| Provisions               | 11,680        | 13,633        | 15,406        | 17,422        |
| Net current assets       | (12,170)      | (20,730)      | (22,695)      | (22,891)      |
| <b>Total assets</b>      | <b>69,490</b> | <b>69,108</b> | <b>69,467</b> | <b>71,094</b> |

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## Cash Flow Statement

| Y/E Mar (Rs mn)            | FY17            | FY18E           | FY19E           | FY20E           |
|----------------------------|-----------------|-----------------|-----------------|-----------------|
| Net profit                 | 44,900          | 51,953          | 59,975          | 68,992          |
| Depn and w/o               | 3,960           | 4,682           | 5,175           | 5,677           |
| Deferred tax               | (410)           | 0               | 0               | 0               |
| Change in working cap      | 5,990           | 188             | 4,787           | 5,662           |
| <b>Operating cash flow</b> | <b>54,440</b>   | <b>56,823</b>   | <b>69,937</b>   | <b>80,332</b>   |
| Capital expenditure        | (12,420)        | (12,500)        | (7,500)         | (7,500)         |
| Investments/ Acquisition   | (9,990)         | 0               | 0               | 0               |
| <b>Investing cash flow</b> | <b>(22,410)</b> | <b>(12,500)</b> | <b>(7,500)</b>  | <b>(7,500)</b>  |
| Free cash                  | 42,020          | 44,323          | 62,437          | 72,832          |
| Dividend                   | (43,916)        | (51,666)        | (59,415)        | (67,165)        |
| Fresh equity               | 0               | 0               | 0               | 0               |
| Debt/Preference shares     | 200             | (750)           | (200)           | (200)           |
| <b>Financing cash flow</b> | <b>(43,716)</b> | <b>(52,416)</b> | <b>(59,615)</b> | <b>(67,365)</b> |
| Others                     | 806             | (280)           | 0               | 0               |
| <b>Net change in cash</b>  | <b>(10,880)</b> | <b>(8,372)</b>  | <b>2,821</b>    | <b>5,466</b>    |
| <b>Opening cash</b>        | <b>27,590</b>   | <b>16,710</b>   | <b>8,338</b>    | <b>11,159</b>   |
| <b>Closing cash</b>        | <b>16,710</b>   | <b>8,338</b>    | <b>11,159</b>   | <b>16,625</b>   |

## Key Ratio

| Y/E Mar                                | FY17 | FY18E | FY19E | FY20E |
|--|------|-------|-------|-------|
| <b>Valuation Ratio (x)</b>             |      |       |       |       |
| P/E (on FDEPS)                         | 69.7 | 57.3  | 49.4  | 42.9  |
| P/CEPS                                 | 60.6 | 52.5  | 45.5  | 39.7  |
| P/BV                                   | 45.6 | 45.4  | 45.0  | 43.8  |
| Dividend yield (%)                     | 1.2  | 1.5   | 1.7   | 1.9   |
| EV/Sales                               | 9.3  | 8.6   | 7.6   | 6.7   |
| EV/EBITDA                              | 53.4 | 44.6  | 38.3  | 33.2  |
| <b>Per Share Data (Rs)</b>             |      |       |       |       |
| EPS (Basic)                            | 19.7 | 23.9  | 27.8  | 31.9  |
| Cash EPS                               | 22.6 | 26.1  | 30.2  | 34.6  |
| DPS                                    | 17.0 | 20.0  | 23.0  | 26.0  |
| Book Value                             | 30.0 | 30.2  | 30.5  | 31.3  |
| <b>Returns (%)</b>                     |      |       |       |       |
| RoCE                                   | 62.4 | 74.9  | 86.8  | 98.4  |
| RoE                                    | 66.6 | 79.5  | 91.5  | 103.4 |
| <b>Turnover ratios (x)</b>             |      |       |       |       |
| Asset Turnover (Gross Block)           | 4.6  | 4.9   | 5.6   | 6.2   |
| Inventory / Sales (days)               | 11   | 11    | 11    | 11    |
| Receivables (days)                     | 55   | 57    | 57    | 57    |
| Payables (days)                        | 120  | 119   | 119   | 119   |
| Working capital cycle (ex-cash) (days) | (54) | (52)  | (52)  | (52)  |

Institutional Equity Research

# Hindustan Unilever

FMCG | India

|                        |         |
|------------------------|---------|
| CMP* (Rs)              | 1,371   |
| Upside/ (Downside) (%) | 10      |
| Bloomberg Ticker       | HUVR IN |



Target Price: Rs1,514

### Rating Guides

| Rating | Expected absolute returns (%) over 12 months |
|--------|--|
| BUY    | >10%   |
| HOLD   | -5% to 10%                                   |
| REDUCE | >-5%   |

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