

Better operational efficiency drives profitability...

After two quarters of moderation in volume growth, HUL's volume growth remained on the slower path at 5%. Net sales increased 6.7% to ₹ 9,852 crore while operating margins expanded 293 bps to 24.8% on account of tight control over operating costs in addition to Ind-AS 116 accounting effect. On a comparable basis, margins expanded 200 bps. Led by healthy sales growth, strong margins and lower corporate tax rates, net profit for the quarter grew 21.2% YoY to ₹ 1,848 crore. The company has announced an interim dividend of ₹ 11/share.

Premiumisation trend to help drive higher revenues/margins

Driven by premiumisation trend across segments, HUL's revenue has grown 9% in the last 10 years. On the back of premiumisation, the FMCG major has gained market share in most of its key categories like laundry, personal wash, hair care and beverages. Over the years, HUL has launched premium products across its key categories. Its most successful premium products (Surf, Dove, Lipton) have been growing significantly, ahead of market growth. As a result, HUL's operating margins has seen consistent expansion in the last 10 years from 14.7% in FY09 to 22.6% in FY19. We expect HUL to maintain its high margin territory, going forward also. We expect the company to post 22.6% margins in FY20E and 22.5% margins in FY21E. We expect the premiumisation trend along with strong brands performance across categories to help revenue CAGR of 12.7% in FY19-21E.

Margin expansion to continue led by benign commodity costs

Gross margins expanded 250 bps on the back of lower palm oil and crude oil prices on a YoY basis, which aided home care and personal care segment EBIT margins. Though input costs were inflationary for the F&R segment, margin expansion is likely to remain strong for the company in the near term on the back of tighter cost control and Ind-AS accounting effect. A&P spends were stepped up by 8% during the quarter. This should help support new launches, going forward. The company may utilise tax cut benefits to increase brand investments in the future.

Valuation & Outlook

On a high base and visible signs of slowdown, the company posted 5% volume growth during the quarter. Though we believe slower growth would continue for another quarter or so; with 25% operating margins and current A&P spend, the company has largest war chest to propel growth. Reduction in corporate tax rate would help increase HUL's EPS by ~4%. The company is best placed within the sector to use this windfall to balance between strengthening its competitive position and improving profitability. However, valuations at 50x FY21E provide little headroom for strong upside. Hence, we maintain our **HOLD** recommendation with a target price of ₹ 2075.



Particulars	
Particular (₹ crore)	Amount
Market Capitalization	440,640.0
Total Debt (FY19)	0.0
Cash and Investments (FY19)	6,381.0
EV	434,259.0
52 week H/L (₹)	2101 / 1501
Equity capital	216.0
Face value	₹ 1
FII Holding (%)	12.4
DII Holding (%)	6.7

Key Highlights

- Home care (35% of revenue) posted robust growth of 9.4% with 151 bps expansion in EBIT margins to 17.7%, driven by premiumisation
- Personal care (45% of revenue) grew 5.3% impacted by muted growth in soaps. However, lower palm oil prices aided margins by 258 bps to 28.9%
- Foods & refreshments (F&R) (20% of revenue) grew 8.4% driven by beverages, ice-creams and frozen foods segments. However, EBIT margins declined 139 bps to 15.9% on account of increase in A&P spend

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Key Financial Summary

Key Financials	FY17	FY18	FY19	FY20E	FY21E	CAGR (FY19-21E)
Total Operating Income	34487.0	34487.0	38224.0	42655.2	48561.3	12.7%
EBITDA	6046.8	7276.0	8637.0	10482.4	11914.1	17.4%
EBITDA Margin %	17.5	21.1	22.6	24.6	24.5	
Net Profit	5036.7	5237.0	6036.0	7502.5	8791.3	20.7%
EPS (₹)	23.32	24.25	27.94	34.73	40.70	
P/E	87.5	84.1	73.0	58.7	50.1	
RoNW %	74.9	74.7	80.9	89.7	96.5	
RoCE (%)	74.9	79.9	85.3	103.9	111.2	

Source: Company, ICICI Direct Research

Exhibit 1: Variance Analysis

Particulars (₹ crore)	Q2FY20	Q2FY20E	Q2FY19	YoY (%)	Q1FY20	QoQ (%)	Comments
Total Operating Income	9,852.0	9,856.4	9,234.0	6.7	10,114.0	-2.6	Net sales witnessed growth 6.7% led by 5% volume growth
Other Operating Income	144.0	108.3	96.0	50.0	130.0	10.8	
Raw Material Expenses	4,485.0	4,768.7	4,435.0	1.1	4,648.0	-3.5	
Employee Expenses	430.0	453.8	438.0	-1.8	452.0	-4.9	Savings of 38 bps in employee expenses to sales due to one-offs
Marketing Expenses	1,198.0	1,140.9	1,106.0	8.3	1,161.0	3.2	
Other operating expenses	1,296.0	1,263.4	1,236.0	4.9	1,206.0	7.5	Savings of 23 bps in overhead expenditure to sales mainly due to change in the Ind-AS 116
EBITDA	2,443.0	2,229.6	2,019.0	21.0	2,647.0	-7.7	
EBITDA margin (%)	24.8	22.6	21.9	293 bps	26.2	-137 bps	On a comparable basis, operating margins improved 200 bps mainly due to lower material costs
Depreciation	237.0	197.1	130.0	82.3	214.0	10.7	
Interest	31.0	24.0	7.0	N.A.	24.0	N.A.	
Other Income	180.0	182.6	305.0	-41.0	147.0	22.4	
PBT	2,355.0	2,191.1	2,187.0	7.7	2,563.0	-8.1	
Exceptional Items	-47.0	0.0	-35.0	N.A.	7.0	N.A.	
Tax Outgo	460.0	504.0	627.0	-26.6	808.0	-43.1	
PAT	1,848.0	1,687.2	1,525.0	21.2	1,755.0	5.3	Higher EBITDA and reduction in corporate tax rates led to earnings growth of 21%
Key Metrics growth YoY (%)							
Home care	9.4		12.4		10.0		Home care segment continue to witness premiumisation trend
Personal care	5.3		10.4		4.0		Muted personal care growth segment on account of weak performance of soaps segment
Foods & Refreshments	8.4		13.3		8.0		Healthy growth in F&R segment due to strong growth from beverages and ice creams segment

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY20E			FY21E			Comments
	Old	New	% Change	Old	New	% Change	
Sales	43,057.0	42,066.3	-2.3	49,010.8	47,890.8	-2.3	Slight change in revenue estimates due to weak growth from personal care segment
EBITDA	9,832.4	10,482.4	6.6	11,140.5	11,914.1	6.9	
EBITDA Margin (%)	22.5	24.6	205 bps	22.4	24.5	212 bps	We revise our operating margin estimates upwards on account of benign input costs
PAT	7,486.0	7,502.5	0.2	8,545.0	8,791.3	2.9	
EPS (₹)	34.6	34.7	0.3	39.6	40.7	2.8	

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

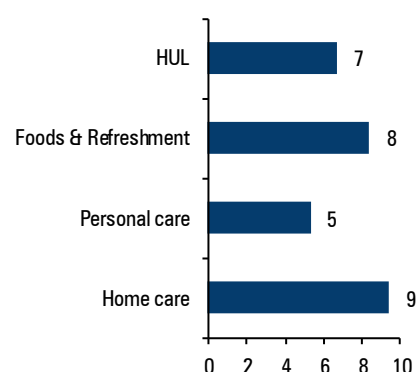
(₹ crore)	Current				Earlier			Comments
	FY17	FY18	FY19	FY20E	FY21E	FY20E	FY21E	
Home care	11,123.0	11,464.0	12,763.0	14,422.2	16,585.5	14,421.1	16,584.3	
Personal care	16,078.0	16,132.0	17,323.0	19,055.3	21,723.0	19,773.6	22,541.9	Personal care segment growth revised downwards due to sluggish growth in soaps
Refreshments	4,795.0	6,425.0	7,068.0	8,057.5	9,024.4	8,274.3	9,267.2	

Source: Company, ICICI Direct Research

Conference Call Highlights

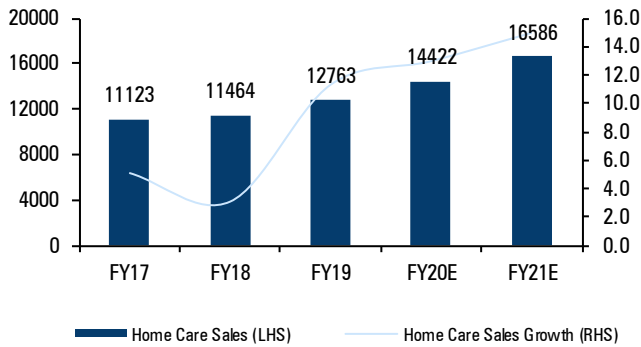
- The home care segment continued to witness strong growth of 9% on the back of premiumisation trend. Growth momentum in the home care segment was driven by liquids upgradation and increased penetration in bars. Strong topline growth in fabric wash was driven by focus on core and market development initiatives. Good growth was witnessed in the premium segment in the purifiers segment
- In the beauty & personal care segment, 5% muted growth can be attributed to soaps. The company has taken some pricing action in Lux & Lifebuoy mainly passing on the benefit of a decline in palm oil prices. In skin care, the company posted strong double digit growth backed by a robust performance across brands. The hair care segment delivered a steady performance across its portfolio. Growth momentum was sustained in colour cosmetics with focus in channels. The oral care segment recorded good portfolio growth driven by freshness and naturals proposition. EBIT margins of personal care segment expanded 258 bps driven by premiumisation
- In foods & refreshment segment, HUL posted 8% growth. Beverages witnessed good growth driven by leveraging purpose led brands and communication. Ice cream & frozen foods saw strong growth driven by geographical expansion of Adityaa Milk. Kissan brand equity strengthened further
- Apart from competitive intensity in the oral care segment, the company is not foreseeing any major pressure in other segments
- The company launched Magic Rinse powder sachet in Tamil Nadu with water conservation perspective. Premium brand Love & Care was launched in select channels. Close-up white attraction variants was also launched in select geographies. TRESemme was launched in sachets
- As per market data by Nielsen, rural growth indexed to urban is now at 0.5x vs. 1.4x in Q2FY19 and 1x in Q1FY20. Rural sales contributes ~40% to sales. The company has indicated that near term demand outlook, especially in rural areas, remains challenging
- Overall commodity basket remains benign while volatility in crude price is expected to continue. With a decline in palm oil prices, HUL has taken 4-6% price cut in Lux and Lifebuoy in the quarter. It will further take pricing action of 3-4% in Dove and Pears in Q3FY20
- The company reported a 293 bps improvement in operating margins. However, adjusting for Ind-AS 116, improvement has been ~200 bps
- A&P spends were stepped up by 8% during the quarter in a bid to support new launches
- The effective corporate tax rate for the company would be ~27% for FY20E and ~26% for FY21E due to certain tax disallowances and re-measurement of deferred tax assets
- HUL-GSK Consumer integration may witness a delay of a couple of months to February 2020 due to a delay in sanction of NCLT

Sales growth on YoY basis (%)



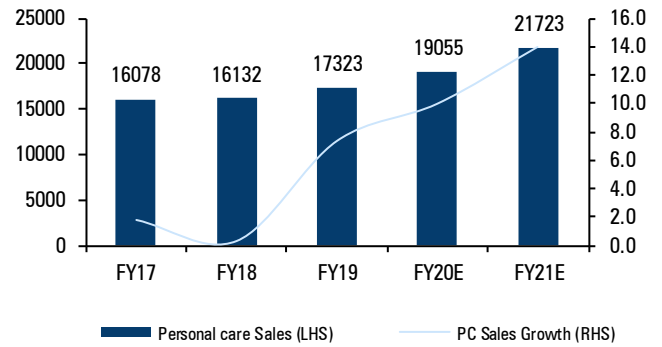
Key Metrics

Exhibit 4: Home care revenue (₹ crore) and YoY growth (%)



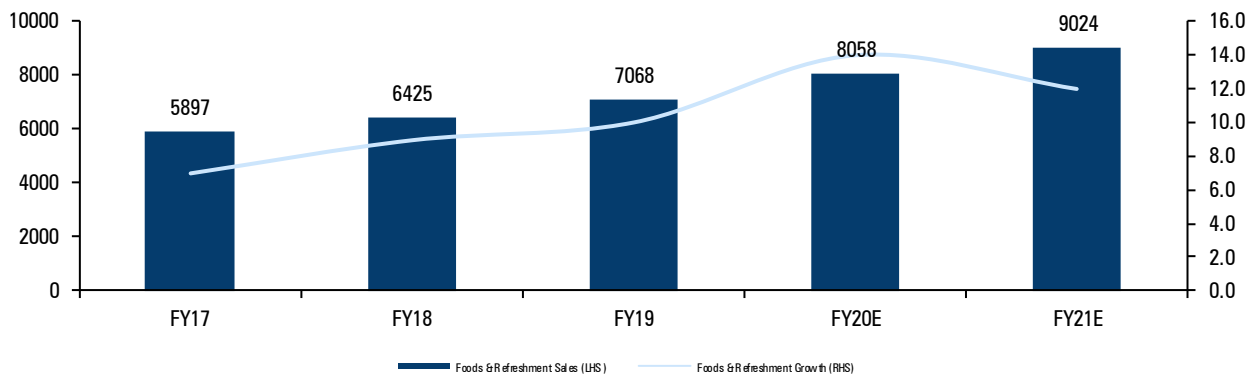
Source: ICICI Direct Research, Company

Exhibit 5: Personal care revenue (₹ crore) & growth (%) trend



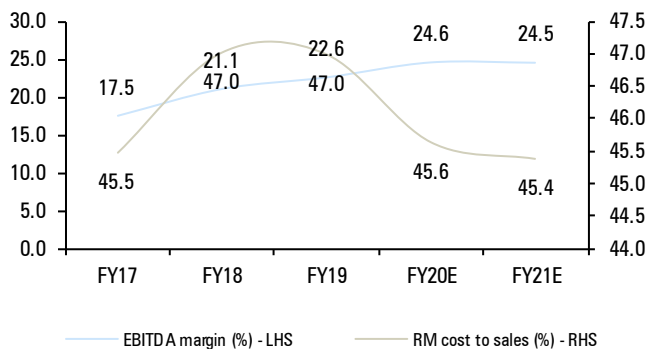
Source: ICICI Direct Research, Company

Exhibit 6: Foods & refreshment revenue (₹ crore) and growth (%) trend



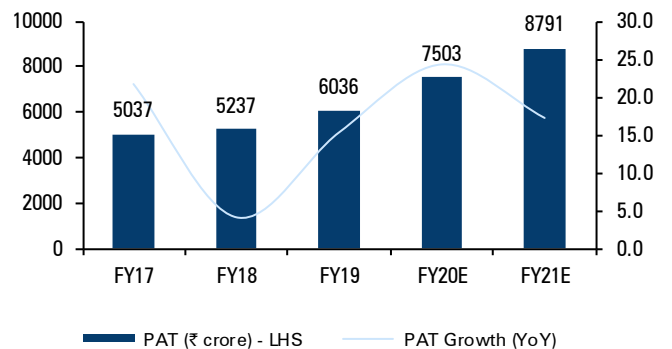
Source: Company, ICICI Direct Research

Exhibit 7: EBITDA margin and raw material trend



Source: Company, ICICI Direct Research

Exhibit 8: PAT to grow at CAGR of 20.7% in FY19-21E



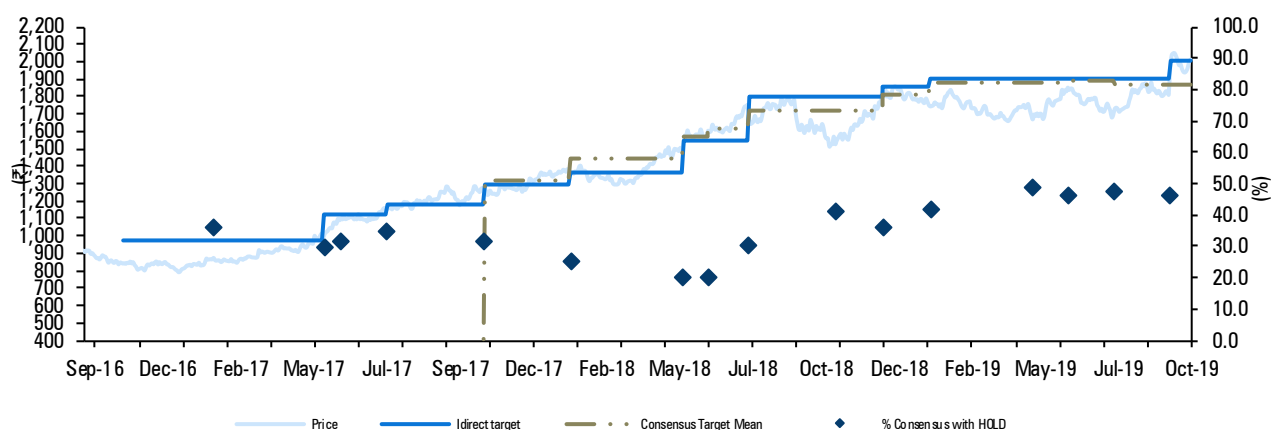
Source: Company, ICICI Direct Research

Exhibit 9: Valuation

	Sales	Growth	EPS	Growth	PE	EV/EBITDA	RoNW	RoCE
	(₹ cr)	(%)	(₹)	(%)	(x)	(x)	(%)	(%)
FY18	33926.0	12.4	24.2	21.4	84.1	60.1	74.7	79.9
FY19	37660.0	11.0	27.9	15.3	73.0	50.6	80.9	85.3
FY20E	42066.3	11.7	34.7	24.3	58.7	41.7	89.7	103.9
FY21E	47890.8	13.8	40.7	17.2	50.1	36.6	96.5	111.2

Source: Company, ICICI Direct Research

Exhibit 10: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 11: Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Unilever PLC	30-Jun-19	67.18	1,454.4	0.0
2	The Vanguard Group, Inc.	31-Aug-19	1.18	25.5	0.2
3	BlackRock Institutional Trust Company, N.A.	30-Sep-19	0.91	19.6	0.0
4	SBI Funds Management Pvt. Ltd.	31-Aug-19	0.64	13.9	0.3
5	Nomura Asset Management Co., Ltd.	31-May-19	0.59	12.7	0.0
6	Aberdeen Standard Investments (Asia) Limited	31-Aug-19	0.40	8.6	-0.1
7	UTI Asset Management Co. Ltd.	30-Sep-19	0.24	5.1	0.0
8	Aberdeen Asset Managers Ltd.	30-Sep-19	0.22	4.7	0.0
9	APG Asset Management N.V.	31-Mar-19	0.21	4.6	0.1
10	ICICI Prudential Asset Management Co. Ltd.	30-Sep-19	0.20	4.4	0.0

Source: Reuters, ICICI Direct Research

Exhibit 12: Recent Activity

Buys			Sells		
Investor name	Value	Shares	Investor name	Value	Shares
Motilal Oswal Asset Management Company Ltd.	10.54m	0.40m	Aditya Birla Sun Life AMC Limited	-30.32m	-1.15m
L&T Investment Management Limited	8.48m	0.32m	Kotak Mahindra Asset Management Company Ltd.	-25.70m	-0.98m
SBI Funds Management Pvt. Ltd.	7.11m	0.27m	Florida State Board of Administration	-9.32m	-0.38m
Ostrum Asset Management	5.70m	0.22m	Edelweiss Asset Management Ltd.	-9.04m	-0.34m
BlackRock Advisors (UK) Limited	5.77m	0.21m	Axis Asset Management Company Limited	-8.54m	-0.32m

Source: Reuters, ICICI Direct Research

Exhibit 13: Shareholding Pattern

(in %)	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19
Promoter	67.2	67.2	67.2	67.2	67.2
FII	12.1	12.0	11.8	12.1	12.4
DII	7.3	7.4	7.0	6.9	6.7
Others	13.4	13.4	14.0	13.8	13.7

Source: Company, ICICI Direct Research

Financial summary

Exhibit 14: Profit and loss statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Total operating income	34,525.0	38,224.0	42,655.2	48,561.3
Growth (%)	0.1	10.7	11.6	13.8
Raw Material Expenses	16,232.0	17,960.0	19,468.8	22,040.5
Employee Expenses	1,745.0	1,747.0	1,977.1	2,298.8
Marketing Expenses	4,105.0	4,552.0	4,963.8	5,699.0
Administrative Expenses	1,968.0	1,994.0	2,145.4	2,490.3
Other expenses	3,199.0	3,334.0	3,617.7	4,118.6
Total Operating Expenditure	27,249.0	29,587.0	32,172.8	36,647.2
EBITDA	7,276.0	8,637.0	10,482.4	11,914.1
Growth (%)	20.3	18.7	21.4	13.7
Depreciation	478.0	524.0	836.4	750.9
Interest	20.0	28.0	99.0	79.2
Other Income	569.0	664.0	730.4	796.1
Exceptional Income	-62.0	-227.0	0.0	0.0
PBT	7,285.0	8,522.0	10,277.4	11,880.2
Total Tax	2,048.0	2,486.0	2,774.9	3,088.8
PAT	5,237.0	6,036.0	7,502.5	8,791.3
Growth (%)	4.0	15.3	24.3	17.2
EPS (₹)	24.2	27.9	34.7	40.7

Source: Company, ICICI Direct Research

Exhibit 15: Cash flow statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Profit after Tax	5,153.0	5,837.0	7,502.5	8,791.3
Add: Depreciation	478.0	524.0	836.4	750.9
(Inc)/dec in Current Assets	-768.0	-228.0	-1,879.8	-1,324.5
Inc/(dec) in CL and Provisions	1,587.0	-33.0	636.5	1,244.7
CF from operating activities	5,916.0	5,728.0	7,095.7	9,462.4
(Inc)/dec in Investments	-897.0	27.0	-100.0	-100.0
(Inc)/dec in loans & advances	-29.0	35.0	-25.0	-25.0
(Inc)/dec in Fixed Assets	-837.0	-724.0	173.0	-200.0
Others	499.0	398.0	-128.6	19.2
CF from investing activities	-1264.0	-264.0	-80.6	-305.8
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	0.0	0.0	0.0	0.0
Dividend paid & dividend tax	-4,627.0	-5,459.0	-6,794.3	-8,052.5
Inc/(dec) in Sec. premium	0.0	0.0	0.0	0.0
Others	-24.0	-3.0	0.0	0.0
CF from financing activities	-4,651.0	-5,462.0	-6,794.3	-8,052.5
Net Cash flow	1.0	2.0	220.8	1,104.1
Opening Cash	572.0	573.0	575.0	795.8
Closing Cash*	3,373.0	3,688.0	3,908.8	5,012.9

Source: Company, ICICI Direct Research *includes cash in bank

Exhibit 16: Balance sheet				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Liabilities				
Equity Capital	216.0	216.0	216.0	216.0
Reserve and Surplus	6,859.0	7,443.0	8,151.2	8,890.1
Total Shareholders funds	7,075.0	7,659.0	8,367.2	9,106.1
Other Non Current Liabilities	666.0	804.0	804.0	804.0
Long Term Provisions	772.0	1049.0	112.5	131.9
Total Liabilities	8,513.0	9,512.0	9,283.8	10,041.9
Assets				
Gross Block	4,868.0	5,476.0	5,676.0	5,876.0
Less: Acc Depreciation	1,092.0	1,569.0	2,405.4	3,156.3
Net Block	3,776.0	3,907.0	3,270.6	2,719.7
Capital WIP	430.0	373.0	0.0	0.0
Total Fixed Assets	4,206.0	4,280.0	3,270.6	2,719.7
Net Intangible Assets	366.0	400.0	400.0	400.0
Other Investments	256.0	256.0	356.0	456.0
Liquid Investments	0	0	0	0
Inventory	2,359.0	2,422.0	2,881.3	3,280.2
Debtors	1,147.0	1,673.0	1,267.8	1,443.3
Loans and Advances	0.0	0.0	230.5	262.4
Investments & Other CA	1,405.0	898.0	1,152.5	1,312.1
Cash	3,373.0	3,688.0	3,908.8	5,012.9
Total Current Assets	11,139.0	11,374.0	13,474.5	15,903.1
Creditors	7,013.0	7,070.0	7,491.3	8,528.5
Provisions & other CL	1,623.0	1,283.0	1,498.3	1,705.7
Total Current Liabilities	8,636.0	8,353.0	8,989.5	10,234.2
Net Current Assets	2,503.0	3,021.0	4,485.0	5,668.9
Others Non-Current Assets	665.0	746.0	771.0	796.0
Application of Funds	8,513.0	9,512.0	9,283.8	10,041.9

Source: Company, ICICI Direct Research

Exhibit 17: Key ratios				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Per share data (₹)				
EPS	24.2	27.9	34.7	40.7
Cash EPS	26.5	30.4	38.6	44.2
BV	32.8	35.5	38.7	42.2
DPS	18.0	21.0	27.0	32.0
Cash Per Share	15.6	17.1	18.1	23.2
Operating Ratios (%)				
EBITDA/Total Operating Income	21.1	22.6	24.6	24.5
PBT Margin	21.3	22.9	24.1	24.5
PAT Margin	15.2	15.8	17.6	18.1
Inventory days	25	23	25	25
Debtor days	12	16	11	11
Creditor days	75	69	65	65
Return Ratios (%)				
RoE	74.7	80.9	89.7	96.5
RoCE	79.9	85.3	103.9	111.2
Valuation Ratios (x)				
P/E	84.1	73.0	58.7	50.1
EV / EBITDA	60.1	50.6	41.7	36.6
EV / Net Sales	12.9	11.6	10.4	9.1
Market Cap / Sales	13.0	11.7	10.5	9.2
Price to Book Value	62.3	57.5	52.7	48.4
Solvency Ratios				
Debt/EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	0.9	0.9	1.1	1.1
Quick Ratio	0.6	0.6	0.7	0.7

Source: Company, ICICI Direct Research

Exhibit 18: ICICI Direct coverage universe (FMCG)

Sector / Company	CMP	TP	M Cap	EPS (₹)				P/E (x)		Price/Sales (x)			RoCE (%)			RoE (%)			
	(₹)	(₹) Rating		(₹ Cr)	FY19E	FY20E	FY21E	Y19E	FY20E	FY21E	Y19E	FY20E	FY21E	Y19E	FY20E	FY21E	Y19E	FY20E	FY21E
Colgate (COLPAL)	1,550	1,400	Hold	37,806	28.5	34.0	37.1	54.4	45.6	41.8	8.5	7.9	7.3	70.7	73.5	69.4	52.2	57.2	53.9
Dabur India (DABIND)	450	520	Buy	78,164	8.2	9.3	10.3	55.0	48.5	43.8	9.2	8.4	7.6	29.6	29.9	30.0	25.7	26.8	26.7
GSK CH (GLACON)	8,685	8,780	Hold	35,327	233.7	272.5	N.A.	37.2	31.9	N.A.	7.4	6.8	N.A.	36.1	32.6	N.A.	24.0	24.8	N.A.
Hindustan Unilever (HINLEV)	2,040	2,075	Hold	440,640	27.9	34.7	40.7	73.0	58.7	50.1	11.7	10.5	9.2	85.3	103.9	111.2	80.9	89.7	96.5
ITC Limited (ITC)	247	320	Buy	289,108	10.3	12.6	14.1	24.1	19.6	17.5	6.5	5.9	5.4	30.8	31.9	31.7	21.5	24.3	24.1
Jyothy Lab (JYOLAB)	160	180	Hold	5,817	5.3	5.9	6.4	30.1	27.3	24.9	3.3	3.1	2.8	28.6	29.3	30.7	22.6	22.3	23.3
Marico (MARLIM)	380	440	Buy	49,028	8.8	8.9	10.0	43.2	42.8	38.0	6.7	6.0	5.4	38.0	42.3	44.4	31.6	35.2	36.8
Nestle (NESIND)	14,060	14,575	Hold	129,685	166.7	223.9	267.9	84.4	62.8	52.5	11.6	10.3	9.1	42.9	43.0	44.6	45.6	48.8	47.7
Tata Global Bev (TATGLO)	275	300	Buy	16,409	7.2	7.9	8.7	38.0	34.8	31.5	2.3	2.1	2.0	8.4	9.1	9.5	6.5	7.2	7.6
VST Industries (VSTIND)	3,790	4,600	Buy	5,714	146.9	193.1	210.5	25.8	19.6	18.0	5.2	4.5	4.2	51.4	50.7	48.6	34.2	38.1	36.5
Varun Beverage (VARBEV)	630	700	Hold	17,464	11.7	16.4	16.4	53.7	38.4	38.5	4.4	3.4	2.4	12.7	14.2	14.5	12.1	15.0	13.4

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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