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Rural revival to drive volume growth ahead

Hindustan Unilever Limited (HUL), a subsidiary of Unilever Plc, is India's leading consumer products company. It has a dominant market share in categories like soaps, laundry, skin care, shampoos & tea.

Investment Rationale

☞ **Strong growth in topline:** On a comparable basis, revenue grew by a strong 9% YoY in Q2FY18 driven largely by robust volume growth of 4% YoY as consumer offtake remains steady. Management indicated that wholesale and CSD channels have started to recover and are expected to stabilize gradually. Despite higher advertisement and promotion (A&P) spend due to launch of Lever Ayush nationally, EBITDA margin expanded by 180 bps YoY (on a like-to-like basis) on the back of lower raw material cost and benefits of operating leverage & cost saving initiatives. While EBITDA grew by ~20% YoY, Adj. PAT growth stood at 15% due to lower other income.

☞ **Broad-based growth across key categories:** In Q2FY18 Home care category reported robust comparable sales growth of 13% YoY led by laundry segment which witnessed double-digit growth coupled with continued strong performance of household care led by Vim. Similarly, Personal Care segment witnessed decent growth of 8% YoY (comparable basis) driven by robust performance of brands across Personal Wash and Personal Products category. Dove led the growth in Hair Care with Indulekha continuing its strong growth momentum. Lever Ayush witnessed good traction after its launch on a pan-India basis. Foods category saw a growth of 11% YoY (comparable basis) driven mainly by Ketchups while multiple new variants were launched under both Soups and Noodles categories. Strong growth in tea led to 10% YoY (comparable basis) growth in Refreshment segment.

☞ **Rural demand improving gradually:** As per the management, the rural demand which was lagging the urban demand previously is now broadly in-line with urban demand (generally rural demand outpaces the urban demand given lower penetration). Further, the reduction in GST rates from 28% to 18% in some of the key categories such as detergents, shampoos, cosmetics will drive strong volume growth ahead as the company will pass on the benefit to the consumers. Broad-based product portfolio, innovative pipeline, strong distribution network and government's thrust on rural economy to drive Revenue/PAT CAGR of ~11%/17% over FY17-20E. We expect EBITDA margin of 20.5%/21.4%/22.2% over FY18/19/20E.

Outlook and Valuation:

HUL is best placed to capitalize on demand recovery. Further, it has the potential to deliver industry leading growth rates going ahead. This coupled with high dividend payout and RoEs justify rich valuations. The stock is currently trading at 46.4x FY19E and 39.9x FY20E EPS. We recommend BUY rating on the stock with a target price of Rs. 1,412.

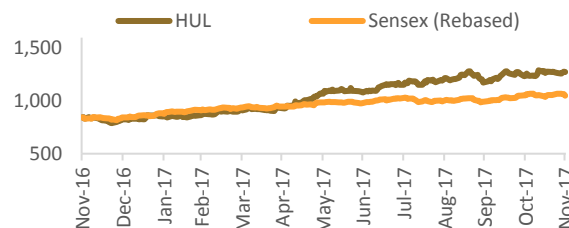
Market Data

Rating	BUY
CMP (Rs.)	1,252
Target (Rs.)	1,412
Potential Upside	13%
Duration	Long Term
Face Value (Rs.)	1
52 week H/L (Rs.)	1,314/783
Decline from 52WH (%)	3.0
Rise from 52WL (%)	62.7
Beta	1.0
Mkt. Cap (Rs.Cr)	270,946

Fiscal Year Ended

Y/E	FY17	FY18E	FY19E	FY20E
Revenue (Rs.Cr)	31,890	34,386	38,646	43,303
Adj. profit (Rs.Cr)	4,249	4,980	5,846	6,792
Adj. EPS (Rs.)	19.6	23.0	27.0	31.4
P/E (x)	63.8	54.4	46.4	39.9
P/BV (x)	41.7	41.5	40.7	38.9
ROE (%)	66.5	76.5	88.6	99.6

One year Price Chart



Source: Company, In-house research

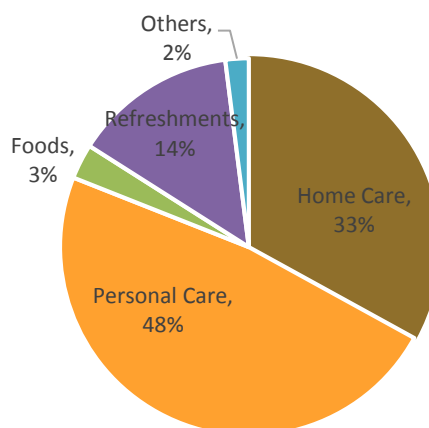
Shareholding Pattern

	Sep-17	Jun-17	Chg.
Promoters	67.2	67.2	0
FII's	13.3	13.4	-0.1
MFs/Insti	5.7	5.6	0.1
Public	11.7	11.8	-0.1
Others	2.1	2.0	0.1

Hindustan Unilever Ltd: Business overview

Hindustan Unilever Limited (HUL), a subsidiary of Unilever Plc, is India's leading consumer products company. It has a dominant market share in categories like soaps, laundry, skin care, shampoos & tea. The company has over 35 brands spanning 20 distinct categories such as soaps, detergents, shampoos, skin care, toothpastes, deodorants, cosmetics, tea, coffee, packaged foods, ice cream, and water purifiers.

Segmental revenue breakup (FY17)



Source: Company, In-house research

Quarterly financial performance (Standalone)

(Rs cr)	YoY Growth		QoQ Growth		YoY Growth			
	Q2FY18	Q2FY17	%	Q1FY18	%	H1FY18	H1FY17	%
Sales	8,309	7,842	6.0	8,529	(2.6)	16,838	15,969	5.4
EBITDA	1,682	1,405	19.7	1,866	(9.9)	3,548	3,040	16.7
EBITDA Margin (%)	20.2	17.9	233bps	21.9	(164bps)	21.1	19.0	203bps
Depreciation	115	94	22.3	114	0.9	229	187	22.5
EBIT	1,567	1,311	19.5	1,752	(10.6)	3,319	2,853	16.3
Interest	6	5	20.0	6	-	12	11	9.1
Other Income	204	253	(19.4)	113	80.5	317	361	(12.2)
Exceptional Items	36	18	-	(13)	-	23	89	-
PBT	1,801	1,577	14.2	1,846	(2.4)	3,647	3,292	10.8
Tax	525	480	9.4	563	(6.7)	1,088	1,021	6.6
PAT	1,276	1,097	16.3	1,283	(0.5)	2,559	2,271	12.7
Minority Interest	-	-	-	-	-	-	-	-
Reported PAT	1,276	1,097	16.3	1,283	(0.5)	2,559	2,271	12.7
Adjustment	(36)	(18)	-	13	-	(23)	(89)	-
Adj PAT	1,240	1,079	14.9	1,296	(4.3)	2,536	2,182	16.2
No. of shares (cr)	216.4	216.4	-	216.4	-	216.4	216.4	-
EPS (Rs)	5.7	5.0	14.9	6.0	(4.3)	11.7	10.1	16.2

Source: Company, In-house research

Strong growth in topline

On a comparable basis, revenue grew by a strong 9% YoY in Q2FY18 driven largely by robust volume growth of 4% YoY as consumer offtake remains steady. Management indicated that wholesale and CSD channels have started to recover and are expected to stabilize gradually. Despite higher advertisement and promotion (A&P) spend due to launch of Lever Ayush nationally, EBITDA margin expanded by 180 bps YoY (on a like-to-like basis) on the back of lower raw material cost and benefits of operating leverage & cost saving initiatives. While EBITDA grew by ~20% YoY, Adj. PAT growth stood at 15% due to lower other income.

Broad-based growth across key categories

Home care category reported robust comparable sales growth of 13% YoY led by laundry segment which witnessed double-digit growth coupled with continued strong performance of household care led by Vim. Similarly, Personal Care segment witnessed decent growth of 8% YoY (comparable basis) driven by robust performance of brands across Personal Wash and Personal Products category. Dove led the growth in Hair Care with Indulekha continuing its strong growth momentum. Lever Ayush witnessed good traction after its launch on a pan-India basis. Foods category saw a growth of 11% YoY (comparable basis) driven mainly by Ketchups while multiple new variants were launched under both Soups and Noodles categories. Strong growth in tea led to 10% YoY (comparable basis) growth in Refreshment segment.

Segment-wise Revenue

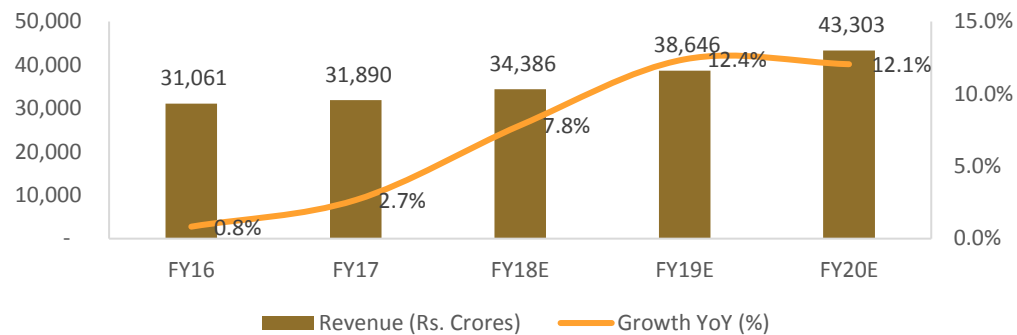
(Rs cr)	Q2FY18	Q2FY17	YoY Growth		QoQ Growth		YoY Growth	
			%	Q1FY18	%	H1FY18		H1FY17
Home Care	2,739	2,777	(1.4)	3,047	(10.1)	5,786	5,653	2.4
Personal Care	3,910	4,028	(2.9)	4,368	(10.5)	8,278	8,250	0.3
Foods	282	278	1.5	284	(0.7)	566	550	2.9
Refreshments	1,222	1,169	4.5	1,346	(9.2)	2,568	2,384	7.7
Others	150	218	(31.2)	168	(10.7)	318	422	(24.6)
Total segment Revenue	8,303	8,470	(2.0)	9,213	(9.9)	17,516	17,259	1.5

Source: Company, In-house research

Rural demand improving gradually

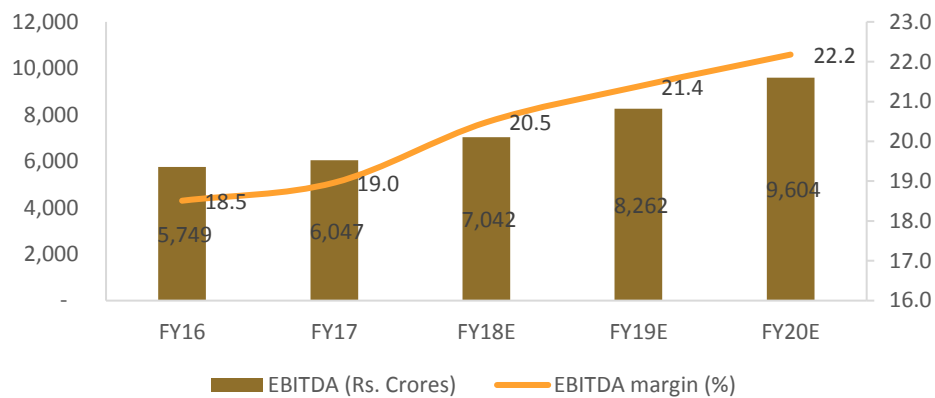
As per the management, the rural demand which was lagging the urban demand previously is now broadly in-line with urban demand (generally rural demand outpaces the urban demand given lower penetration). Further, the reduction in GST rates from 28% to 18% in some of the key categories such as detergents, shampoos, cosmetics will drive strong volume growth ahead as the company will pass on the benefit to the consumers. Broad-based product portfolio, innovative pipeline, strong distribution network and government's thrust on rural economy to drive Revenue/PAT CAGR of ~11%/17% over FY17-20E. We expect EBITDA margin of 20.5%/21.4%/22.2% over FY18/19/20E.

Revenue to grow at 11% CAGR over FY17-20E

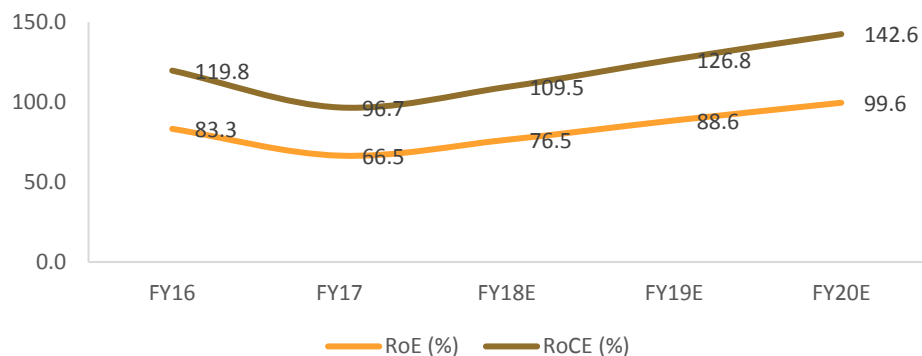


Source: Company, In-house research

EBITDA to grow at 16% CAGR over FY17-20E



Return ratios to remain healthy



Source: Company, In-house research

Key Risks

- Increasing competition
- Depreciation of Indian currency will impact cost of raw materials
- Weak rural demand

Profit & Loss Account (Standalone)

Y/E (Rs. Cr)	FY17	FY18E	FY19E	FY20E
Total operating Income	31,890	34,386	38,646	43,303
EBITDA	6,047	7,042	8,262	9,604
Depreciation	396	469	496	535
EBIT	5,651	6,573	7,766	9,069
Interest cost	22	22	22	22
Other Income	526	563	608	656
Profit before tax	6,155	7,114	8,352	9,704
Tax	1,906	2,134	2,506	2,911
Profit after tax	4,249	4,980	5,846	6,792
Minority Interests	-	-	-	-
P/L from Associates	-	-	-	-
Adjusted PAT	4,249	4,980	5,846	6,792
E/o income / (Expense)	241	23	-	-
Reported PAT	4,490	5,003	5,846	6,792

Balance Sheet (Standalone)

Y/E (Rs. Cr)	FY17	FY18E	FY19E	FY20E
Paid up capital	216	216	216	216
Reserves and Surplus	6,274	6,319	6,451	6,751
Net worth	6,490	6,536	6,668	6,967
Minority interest	-	-	-	-
Total Debt	-	-	-	-
Other non-current liabilities	1,059	1,059	1,059	1,059
Total Liabilities	7,549	7,595	7,727	8,026
Total fixed assets	4,227	4,308	4,312	4,277
Goodwill	-	-	-	-
Investments	3,779	3,779	3,779	3,779
Net Current assets	(1,310)	(1,346)	(1,218)	(883)
Deferred tax assets (Net)	160	160	160	160
Other non-current assets	693	693	693	693
Total Assets	7,549	7,595	7,727	8,026

Cash Flow Statement (Standalone)

Y/E (Rs. Cr)	FY17	FY18E	FY19E	FY20E
Pre-tax profit	6,155	7,114	8,352	9,704
Depreciation	396	469	496	535
Changes in W.C	666	144	303	299
Others	(460)	(541)	(586)	(634)
Tax paid	(1,804)	(2,134)	(2,506)	(2,911)
C.F.O	4,953	5,052	6,059	6,992
Capital exp.	(1,024)	(550)	(500)	(500)
Change in inv.	(970)	-	-	-
Other invest.CF	1,242	563	608	656
C.F - investing	(752)	13	108	156
Issue of equity	-	0	-	-
Issue/repay debt	-	-	-	-
Dividends paid	(4,264)	(4,935)	(5,714)	(6,493)
Other finance.CF	-	(22)	(22)	(22)
C.F - Financing	(4,264)	(4,957)	(5,736)	(6,515)
Chg. in cash	(63)	108	431	633

Key Ratios (Standalone)

Y/E	FY17	FY18E	FY19E	FY20E
Growth (%)				
Net Sales	2.6	9.9	12.4	12.1
EBITDA	5.2	16.5	17.3	16.2
Net profit	1.9	17.2	17.4	16.2
Margin (%)				
EBITDA	19.0	20.5	21.4	22.2
EBIT	17.7	19.1	20.1	20.9
NPM	13.3	14.5	15.1	15.7
Return Ratios (%)				
RoE	66.5	76.5	88.6	99.6
RoCE	96.7	109.5	126.8	142.6
Per share data (Rs.)				
EPS	19.6	23.0	27.0	31.4
DPS	17.0	19.0	22.0	25.0
Valuation(x)				
P/E	63.8	54.4	46.4	39.9
EV/EBITDA	44.5	38.2	32.5	27.9
EV/Net Sales	8.6	7.8	7.0	6.2
P/B	41.7	41.5	40.7	38.9
Turnover Ratios (x)				
Net Sales/GFA	7.9	6.9	7.0	7.2
Sales/Total Assets	2.2	2.3	2.5	2.6

Rating Criteria

Large Cap.	Return	Mid/Small Cap.	Return
Buy	More than equal to 10%	Buy	More than equal to 15%
Hold	Upside or downside is less than 10%	Accumulate*	Upside between 10% & 15%
Reduce	Less than equal to -10%	Hold	Between 0% & 10%
		Reduce/sell	Less than 0%

* To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.

* HUL is a large-cap company.

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