Encouraging Performance; Maintain BUY

Est. Vs. Actual for Q2FY24: Revenue – MISS; EBITDA – BEAT ; PAT – BEAT

Changes in Estimates post Q2FY24

FY25E/FY26E – Revenue: 0%/0%; **EBITDA:** 0%/0%; **PAT:** 0%/0%

Recommendation Rationale

- **Inline results:** The company's Q2FY24 results were in line with our estimates. The Cigarettes segment continued its strong momentum with volume growth of ~5-6% vs. our estimates of 5%, led by market share gains from illicit trade, targeted market interventions, and new product launches. FMCG/Hotels maintained its strong growth momentum, while the Agri/Paper board business declined due to the wheat ban and subdued demand in the paperboard business. Gross revenue (excluding agri-business) grew by 8.9% YoY.
- We believe that the ITC business continues to strengthen as all businesses are on track: – 1) Growth in cigarette volume is stable, thanks to stable taxation, market share gains and new product launches; 2) FMCG business has reached the inflexion point as EBIT margins continue to increase, driven by – the ramp up in the outlet coverage, effective implementation of localization strategy, premiumization, use of demand and supply side technologies, and moderating raw material input cost; 3) Demerger of Hotel's business will strengthen ITC's balance sheet and improve return ratios; 4) Stable and decent performance in paperboard and agribusiness continues. In addition, the reasonable valuation provides a margin of safety.

Sector Outlook: Positive

Company Outlook & Guidance: We maintain our PAT estimates to factor in strong earnings visibility across business verticals.

Current Valuation: 27x Jun'25 EPS (Earlier Valuation: Unchanged).

Current TP: Rs 540/share (Earlier TP: Unchanged).

Recommendation With an upside potential of 20% from the CMP, we **maintain** our BUY rating on the stock.

Alternative BUY Ideas from our Sector Coverage: HUL (TP – Rs 2,900)

Financial Performance: The company's revenue grew by 3% YoYto Rs 16,394 Cr, mainly due to subdued performance in the agriculture and paperboard businesses. Gross margins stood at 56.9%, up 43bps YoY, due to a sequential decline in raw material prices. EBITDA margins were 36.9% (flat), due to higher Opex. Reported PAT was Rs 4,927 Cr (up 10% YoY).

A) Cigarettes (~80% of EBIT) – The company's cigarette division continued its strong momentum with sales growth of 10% (volume growth of 4-5%), led by market share gains from illicit trade, targeted market interventions, and new product launches. Over the years, discriminatory and punitive taxation on cigarettes has led the entire legal cigarette industry to grapple with the loss in market share and volumes from illicit trade. However, stable taxation in recent years has led to a recovery in market share and volumes. We also expect the company's cigarette margins to increase slightly in the future as realisation per stick improves.

Outlook: The stock is currently trading at 23x FY25E EPS and a 3-4% dividend yield provides a margin of safety compared to its peers. While valuations of other players stand elevated, ITC makes a better play in the entire FMCG pack on account of a stable outlook for the cigarette volume growth (led by stable taxation, market share gain from illicit trade along with new product launches), the FMCG business reaching the inflexion point with its EBIT margins inching up further, strong and stable growth witnessed in hotels, and steady and decent performance outlook in paperboard and agribusiness.

Valuation & Recommendation: We estimate the company to post Revenue/EBITDA/PAT growth of 10%/12%/12% CAGR over FY23-26E and maintain a BUY rating on the stock with an unchanged TP of Rs 540/share. **We value the company at 27x June-25 EPS. The TP implies an upside of 20% from the CMP.**

Key Financials (Standalone)

(Rs Cr)	Q2FY24	QoQ (%)	YoY (%)	Axis Est.	Variance (%)
Net Sales	16,394	4.6	2.8	16,495	-0.6
EBITDA	6,042	-3.3	3.0	6,142	-1.6
EBITDA Margin (%)	36.9	-302 bps	7 bps	37.2	-38 bps
Net Profit	4,927	0.5	10.3	4,649	6.0
EPS (Rs)	4.0	0.5	10.2	3.7	6.0

Source: Company, Axis Research

(CMP as of 19th October 2023)

CMP (Rs)	450
Upside /Downside (%)	20%
High/Low (Rs)	499/325
Market cap (Cr)	561,565
Avg. daily vol. (6m)Shrs.'000	11485.74
No. of shares (Cr)	1246

Shareholding (%)

	Mar-23	Jun-23	Sep-23
Promoter	0.0	0.0	0.0
FIIs	43.4	43.6	43.3
MFs / UTI	9.5	9.2	9.4
Banks / FIs	7.9	7.9	7.9
Others	39.3	39.3	39.3

Financial & Valuations

Y/E Mar (Rs Cr)	FY24E	FY25E	FY26E
Net Sales	72,161	79,127	86,860
EBITDA	27,413	30,475	33,452
Net Profit	21,488	23,919	26,304
EPS (Rs.)	17.3	19.2	21.2
PER (x)	26.0	23.3	21.2
EV/EBITDA (x)	19.6	17.5	15.7
P/BV (x)	7.7	7.1	6.4
ROE (%)	29.7	30.3	30.0

Change in Estimates (%)

Y/E Mar	FY25E	FY26E
Sales	0%	0%
EBITDA	0%	0%
PAT	0%	0%

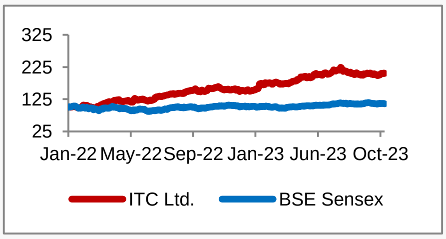
ESG disclosure Score**

Environmental Disclosure	61.91
Social Disclosure Score	38.81
Governance Disclosure	89.86
Total ESG Disclosure Score	**63.57**
Sector Average	**44.87**

Source: Bloomberg, Scale: 0.1-100

**Note: This score measures the amount of ESG data a company reports publicly and does not measure the company's performance on any data point. All scores are based on 2022 disclosures

Relative performance



Source: Ace Equity, Axis Securities

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Other Key takeaways

- **FMCG –** The FMCG business continued to witness robust growth in both urban and rural markets where segment revenue stood at Rs 5292 cr, up by 8.3%, amidst a high base. Margins were up by 150 bps YoY at 11% mainly driven by multi-prolonged interventions – supply channel, premiumisation, new launches, digital intervention, strategic cost management and judicious price actions.
  - **Stationery Products-** In the stationery business, both Classmate Notebooks and pens continued their Number 1 positions and witnessed strong growth backed by an increase in exports.
  - **Sun Feast Biscuits and Cakes-** Recorded a resilience performance on the back of stability in core brands and new launches. However, this category also faced competition from the local/regional players in the backdrop of commodity price deflationary conditions barring a few mainly wheat, maida, sugar, and potato.
  - **D2C Platform-** The Company's trade marketing and distribution channel has transformed into a smart omni-channel network via the D2C platform. Currently, the company's D2c platform is operating in 24,000+ cities and delivers an excellent customer response.
  - **Unnati-** The Unnati app now covers over 6.3 outlets, facilitating sharp and direct engagement with retailers, superior analytics, personalized recommendations of hyperlocal baskets based on consumer purchase insights and deeper brand engagement.
  - **Packaged food business-** Aashirvaad Atta posted robust growth reinforcing its leadership position in the Branded Atta industry. Further, in line with the new innovations, the company has augmented with the launch of several new variants in this category.

- **Hotels –** Revenue grew 21% YoY, amidst a high base, led by strong growth in ARR. However, occupancy was flattishly impacted owing to a high base and fewer wedding dates, and pre-planned innovation undertaken. Despite this, EBIT grew 50% YoY (EBIT margins 19.4.9%, up 370bps YoY on account of higher realisation per room and operating leverage.

- **Paperboards –** Revenue declined 10% YoY, and EBIT declined 50% YoY owing to subdued demand conditions, increased competitive intensity from cheap Chinese players, and a steep decline in global pulp prices.

- **Agri –** Agri business de-grew 2% YoY, on account of the ban on exports of wheat. However, adjusting for wheat exports, the Agri business grew 26% YoY.

- **ITC Infotech –** Revenue stood at Rs 930 Cr (up 13% YoY)

Key Risks to our Estimates and TP

- Increase in competitive intensity in Cigarettes, RM inflation, and the slowdown in the economy impacting Hotels and other cyclical businesses.

Change in Estimates

	Old		New		% change	
	FY25E	**FY26E**	**FY25E**	**FY26E**	**FY25E**	**FY26E**
Rev	79,127	86,860	79,127	86,860	0%	0%
EBITDA	30,475	33,452	30,475	33,452	0%	0%
PAT	23,919	26,304	23,919	26,304	0%	0%
EPS	19.2	21.2	19.2	21.2	0%	0%

Source: Company, Axis Securities

Results Review

(Rs cr)	Q2FY23	Q1FY24	Axis Sec Est.	Q2FY24	YoY growth %	QoQ growth %	Axis Sec Est. Var (%)
Volume growth est. (% yoy)	20.0	8.0	5.0	5.0	-1500 bps	-300 bps	
Net sales	**15,942**	**15,676**	**16,495**	**16,394**	**2.84**	**4.58**	**(0.6)**
Other operating Income	188	153	190	156	(17.01)	2.47	(17.8)
Gross Profits	**9,004**	**9,260**	**9,732**	**9,330**	**3.62**	**0.75**	**(4.1)**
Gross Margin (%)	**56.5**	**59.1**	**59.0**	**56.9**	**43 bps**	**-216 bps**	**-209 bps**
Staff costs	936	904	1,030	909	(2.90)	0.60	(11.7)
Other operating expenses	2,391	2,259	2,750	2,535	6.01	12.23	(7.8)
EBITDA	**5,864**	**6,250**	**6,142**	**6,042**	**3.02**	**(3.34)**	**(1.6)**
EBITDA margin (%)	**36.8**	**39.9**	**37.2**	**36.9**	**7 bps**	**-302 bps**	**-38 bps**
Other Income	507	709	558	896	76.68	26.37	60.6
Interest	11	11	11	11	(1.50)	(1.96)	(2.9)
Depreciation	422	402	407	413	(2.09)	2.67	1.6
PBT	5,939	6,546	6,283	6,514	9.68	(0.49)	3.7
Tax	1,472	1,643	1,633	1,587	7.75	(3.43)	(2.9)
Tax rate (%)	24.8	25.1	26.0	24.4	-44 bps	-74 bps	
Reported PAT	**4,466**	**4,903**	**4,649**	**4,927**	**10.32**	**0.49**	**6.0**
Reported EPS	**3.6**	**3.9**	**3.7**	**4.0**	**10.20**	**0.49**	**6.0**

Segmental Performance

Segment Revenue	Q2FY23	Q1FY24	Q2FY24	YoY%	QoQ (%)
Cigarette	6,954	7,465	7,658	10.1%	2.6%
Other FMCG	4,885	5,166	5,292	8.3%	2.4%
Hotel	536	600	649	21.2%	8.2%
AgriBusiness	3,997	5,705	3,931	-1.7%	-31.1%
Paper Board	2,288	2,121	2,070	-9.5%	-2.4%
Total	**18,659**	**21,058**	**19,600**	**5.0%**	**-6.9%**

% Revenue Contribution	Q2FY23	Q1FY24	Q2FY24	YoY%	QoQ (%)
Cigarette	37.3%	35.5%	39.1%	180bps	362bps
Other FMCG	26.2%	24.5%	27.0%	82bps	247bps
Hotel	2.9%	2.9%	3.3%	44bps	46bps
AgriBusiness	21.4%	27.1%	20.1%	-136bps	-704bps
Paper Board	12.3%	10.1%	10.6%	-170bps	49bps

Segment EBIT	Q2FY23	Q1FY24	Q2FY24	YoY%	QoQ (%)
Cigarette	4,429	4,656	4,782	8.0%	2.7%
Other FMCG	321	431	439	36.8%	1.8%
Hotel	84	131	126	49.8%	-4.1%
AgriBusiness	345	356	357	3.3%	0.2%
Paper Board	630	472	316	-49.9%	-33.2%
Segment EBIT Margin %	**Q2FY23**	**Q1FY24**	**Q2FY24**	**YoY%**	**QoQ (%)**
Cigarette	63.7%	62.4%	62.4%	-125bps	7bps
Other FMCG	6.6%	8.3%	8.3%	173bps	-5bps
Hotel	15.7%	21.9%	19.4%	370bps	-249bps
AgriBusiness	8.6%	6.2%	9.1%	44bps	283bps
Paper Board	27.5%	22.3%	15.3%	-1227bps	-702bps

Source: Company, Axis Securities

Financials (Standalone)

Profit & Loss

(Rs Cr)

Y/E Mar	FY23	FY24E	FY25E	FY26E
Net sales	**65,273**	**72,161**	**79,127**	**86,860**
Growth, %	17	11	10	10
Other operating income	770	847	932	1,025
Total income	66,043	73,009	80,059	87,886
Raw material expenses	-28,880	-31,191	-33,686	-36,886
Employee expenses	-3,569	-3,926	-4,319	-4,751
Other Operating expenses	-9,649	-10,478	-11,579	-12,797
EBITDA (Core)	**23,944**	**27,413**	**30,475**	**33,452**
Growth, %	26.5	14.5	11.2	9.8
Margin, %	36.7	38.0	38.5	38.5
Depreciation	-1,663	-1,788	-1,918	-2,051
EBIT	**22,282**	**25,626**	**28,557**	**31,400**
Growth, %	28.9	15.0	11.4	10.0
Margin, %	34.1	35.5	36.1	36.2
Interest paid	-42	-42	-43	-43
Other Income	2,438	2,803	3,084	3,392
Non-recurring Items	73	0	0	0
Pre-tax profit	**24,750**	**28,387**	**31,598**	**34,749**
Tax provided	-5,997	-6,898	-7,679	-8,445
Profit after tax	**18,753**	**21,488**	**23,919**	**26,304**
Others (Minorities, Associates)	0	0	0	0
Unadj. shares (Cr)	1,243	1,243	1,243	1,243
Wtd avg shares (Cr)	1,243	1,243	1,243	1,243

Source: Company, Axis Securities

Balance Sheet

(Rs Cr)

As at 31st Mar,	FY23	FY24E	FY25E	FY26E
Cash & bank	3,831	4,577	9,300	16,419
Marketable securities at cost	16,357	16,357	16,357	16,357
Debtors	2,321	4,943	5,420	5,949
Inventory	10,594	11,712	12,842	14,098
Loans & advances	6	6	6	6
Other current assets	2,094	2,094	2,094	2,094
Total current assets	35,203	39,689	46,019	54,923
Investments	16,364	16,364	16,364	16,364
Gross fixed assets	34,261	36,761	39,361	41,961
Less: Depreciation	-10,087	-11,875	-13,793	-15,844
Add: Capital WIP	1,697	1,697	1,697	1,697
Net fixed assets	25,871	26,583	27,265	27,813
Non-current assets	4,824	4,824	4,824	4,824
Total assets	**82,262**	**87,459**	**94,472**	**1,03,924**
Current liabilities	11,639	12,105	12,577	13,100
Provisions	978	999	1,021	1,045
Total current liabilities	12,617	13,105	13,597	14,144
Non-current liabilities	2,050	2,050	2,050	2,050
Total liabilities	14,668	15,155	15,648	16,195
Paid-up capital	1,243	1,243	1,243	1,243
Reserves & surplus	66,351	71,061	77,581	86,486
Shareholders' equity	67,594	72,304	78,824	87,729
Total equity & liabilities	**82,262**	**87,459**	**94,472**	**1,03,924**

Source: Company, Axis Securities

Cash Flow (Rs Cr)

Y/E Mar	FY23	FY24E	FY25E	FY26E
Pre-tax profit	24,750	28,387	31,598	34,749
Depreciation	1,663	1,788	1,918	2,051
Chg in working capital	-796	-3,252	-1,115	-1,238
Total tax paid	-5,818	-6,898	-7,679	-8,445
Other operating activities	0	0	0	0
Cash flow from operating activities	**19,799**	**20,024**	**24,722**	**27,118**
Capital expenditure	-1,847	-2,500	-2,600	-2,600
Chg in investments	-706	0	0	0
Chg in marketable securities	-4,732	0	0	0
Other investing activities	0	0	0	0
Cash flow from investing activities	**-7,285**	**-2,500**	**-2,600**	**-2,600**
Free cash flow	12,514	17,524	22,122	24,518
Equity raised/(repaid)	2,567	0	0	0
Debt raised/(repaid)	-1	0	0	0
Dividend (incl. tax)	-19,255	-16,778	-17,399	-17,399
Cash flow from financing activities	**-16,689**	**-16,778**	**-17,399**	**-17,399**
Net chg in cash	-4,176	746	4,723	7,119
Opening cash balance	3,878	3,831	4,577	9,300
Closing cash balance	3,831	4,577	9,300	16,419

Source: Company, Axis Securities

Ratio Analysis (%)

	FY23	FY24E	FY25E	FY26E
Per Share data				
EPS (INR)	15.0	17.3	19.2	21.2
Growth, %	23.0	15.0	11.3	10.0
Book NAV/share (INR)	54.4	58.2	63.4	70.6
FDEPS (INR)	15.0	17.3	19.2	21.2
CEPS (INR)	16.3	18.7	20.8	22.8
CFPS (INR)	15.6	13.9	17.4	19.1
DPS (INR)	15.5	13.5	14.0	14.0
Return ratios				
Return on assets (%)	23.9	25.4	26.3	26.6
Return on equity (%)	27.6	29.7	30.3	30.0
Return on capital employed (%)	28.2	29.8	30.8	30.8
Turnover ratios				
Asset turnover (x)	2.2	2.3	2.3	2.4
Sales/Total assets (x)	0.8	0.9	0.9	0.9
Sales/Net FA (x)	2.5	2.8	2.9	3.2
Working capital/Sales (x)	0.0	0.1	0.1	0.1
Receivable days	13.0	25.0	25.0	25.0
Inventory days	59.2	59.2	59.2	59.2
Payable days	37.7	38.5	38.8	38.8
Working capital days	14.5	29.7	32.3	34.8
Liquidity ratios				
Current ratio (x)	2.8	3.1	3.4	4.0
Quick ratio (x)	2.0	2.2	2.5	2.9
Interest cover (x)	532.9	606.8	669.6	728.9
Net debt/Equity (%)	(5.7)	(6.3)	(11.8)	(18.7)
Valuation				
PER (x)	29.9	26.0	23.3	21.2
PEG (x) - y-o-y growth	1.3	1.7	2.1	2.1
Price/Book (x)	8.3	7.7	7.1	6.4
EV/Net sales (x)	8.2	7.4	6.7	6.0
EV/EBITDA (x)	22.5	19.6	17.5	15.7
EV/EBIT (x)	24.1	21.0	18.6	16.7

Source: Company, Axis Securities

ITC Ltd Price Chart and Recommendation History

Date	Reco	TP	Research
04-Feb-22	BUY	280	Result Update
19-May-22	BUY	295	Result Update
02-Aug-22	BUY	340	Result Update
29-Sep-22	BUY	380	AAA
21-Oct-22	BUY	385	Result Update
02-Feb-23	BUY	410	Company Update
06-Feb-23	BUY	460	Result Update
01-Mar-23	BUY	460	Top Picks
01-Apr-23	BUY	460	Top Picks
02-May-23	BUY	470	Top Picks
19-May-23	BUY	480	Result Update
01-Jun-23	BUY	490	Top Picks
01-Jul-23	BUY	495	Top Picks
20-Jul-23	BUY	550	AAA
01-Aug-23	BUY	540	Top Picks
16-Aug-23	BUY	540	Result Update
01-Sep-23	BUY	540	Top Picks
03-Oct-23	BUY	540	Top Picks
20-Oct-23	BUY	540	Result Update

Source: Axis Securities

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