



TM

Hindustan Unilever

19 January 2024

Marginal miss on estimates; soft near-term outlook given demand/competition headwinds

RESULT UPDATE

Sector: FMCG **Rating:** HOLD
CMP: Rs 2,565 **Target Price:** Rs 2,825

Stock Info

Sensex/Nifty	71,683/ 21,622
Bloomberg	HUVR IN
Equity shares (mn)	2350
52-wk High/Low	Rs 2,769/2,393
Face value	Rs 1
M-Cap	Rs 6,026bn/US\$ 73bn
3-m Avg value	US\$ 47mn

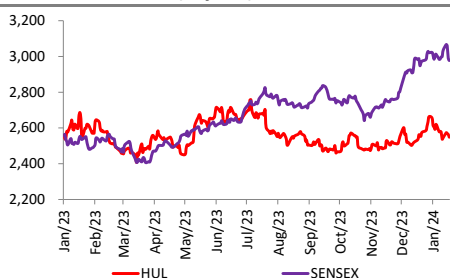
Financial Snapshot (Rs mn)

Y/E Mar	FY24E	FY25E	FY26E
Sales	624,805	674,504	735,426
PAT	105,865	119,193	132,763
EPS (Rs)	45.0	50.7	56.5
PE (x)	56.6	50.2	45.1
EV/EBITDA (x)	33.6	30.4	27.3
P/BV (x)	10.7	10.5	10.2
EV/Sales	7.9	7.3	6.7
RoE (%)	20.8	22.9	24.9
RoCE (%)	26.9	28.3	30.7
NWC (days)	-11	-11	-10
Net gearing (x)	(0.1)	(0.1)	(0.1)

Shareholding Pattern (%)

	Sep23	Jun23	Mar23
Promoter	61.9	61.9	61.9
-Pledged	-	-	-
FII	13.9	14.5	14.4
DII	11.9	11.5	11.5
Others	12.3	12.2	12.2

Stock Performance (1-year)



Hindustan Unilever (HUVR) delivered earnings marginally below our muted expectations with soft topline performance and gross margin improvement being ploughed back to increase A&P spends resulting in flattish earnings. Revenue growth fell short of expectations with a decline of 0.3% YoY while EBITDA/ Adj. PAT stood at +0.1%/-2.2% YoY respectively. Volume growth at 2% was lower than the market volume growth of 9% given decline in segments like tea, HFD and detergents indicating a combination of market share loss to regional players and consumer downgrading given cumulative inflation. But the company maintained its share gains on a 2-yr basis growing volumes at 4% vs 2% for industry. While home care and BPC grew volumes in mid-single digit, foods saw a low-single digit volume decline. A superior mix and continued cool-off in material inflation (esp. crude and palm-related) led to sharp gross margin expansion of 401bps to 51.5% albeit EBITDA margin remained flat at 23.3% given 270bps increase in ad spends and 149bps increase in other expenses given higher investments and royalty increase.

We expect gross margin recovery to continue, with commodity inflation continuing to moderate and premiumization/mix improvement playing out. But EBITDA margin improvement will be tempered by the 80bps phased increase in royalty and a continued uptick in ad spends. The impact of pricing cuts implemented in soaps and personal care have started to reflect in the numbers which should drive a gradual recovery in volume growth over next few quarters. But muted pricing should keep revenue growth muted over the next few quarters. Given the recent underperformance and initial signs of a volume recovery in few categories post pricing and marketing actions, we do not expect too much downside despite this weak growth delivery on both absolute and relative terms. Pricing should remain in the negative zone in near-term, translating to a soft revenue growth for FY24. We expect a rural recovery led by lower inflation, low base and better farm income expectations while urban demand especially in food categories should take some more time to see the benefits of innovation and market development. We expect volume growth to be the sole driver for revenue growth in near-term. Gross margin improvement is expected to be invested on higher A&P and innovation spends.

Valuation and View: We cut our FY24/25 EPS estimates by 5%/4% to build in a slower recovery in both topline and margins and now build a revenue/EBITDA/PAT growth of 8.5%/10.8%/12%, respectively, over FY24-26E. We introduce our FY26 estimates and roll over valuations to FY26, maintaining our HOLD rating with a target price of Rs 2,825 (Rs 2,760 earlier) based on 50x FY25E earnings, a 10% discount to its five-year average valuation multiple. While we like the potential for premiumization and marketing/innovation focus of the company, weak demand trends, high competitive intensity and absence of pricing lever remain near-term headwinds for the stock, which can drive continued underperformance for a couple more quarters. Higher royalty, A&P and GSK OTC business going away would limit margin improvement as well. Key monitorables would be the timing of industry demand recovery, commodity price trends and competitor actions.

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Management commentary: Management expects a gradual rural demand recovery, price growth is expected to be marginally negative moving ahead (in case commodity prices remain stable) while lower commodity prices are expected to keep competitive intensity high. They also highlighted the ~25% cumulative industry pricing over last 3 years having a protracted impact on demand, which might take a couple more quarters to normalize with pricing falling into negative territory at industry level. With competitive intensity rising, the company intends to maintain higher A&P spends and also take further price cuts and BTL spends if needed, which will moderate the EBITDA flow-through of expected gross margin expansion. Looking beyond a soft FY24, laundry category still retains strong premiumization and share gain potential while BPC segment should also recover with a pick-up in disposable income levels and company efforts on premiumization. Foods and HFD category, however, is also expected to witness a volume recovery with inflation cooling off in areas like tea and dairy.

3QFY24 Result highlights

- Revenue/EBITDA/Adj.PAT growth of -0.3%/0.1%/-2.2% YoY respectively led by 2% volume growth, 2% negative pricing and soft growth across categories given the high base as the company gained significant share last year.
- Overall revenue decline of 0.3% YoY was a result of 1.3% decline in home care, 0.2 % growth in BPC and 0.9% growth in foods.
- Overall gross margin grew 401bps to 51.5% driven by softening of RM inflation; EBITDA margin remained flat at 23.3% with rise (+270bps) in A&P spends, higher other expenses (+149bps) while employee costs remained flat (-17bps).
- EBIT margin fell 150bps for home care, grew 48bps for BPC while margin for foods grew 118bps.

Management presentation highlights

- **Margins** – Softening of RM inflation led to 440bps decline in COGS, coupled with price cuts in certain categories. There was a 270bps increase in A&P spends, 149bps rise in other expenses, while a decline of 17 bps in expenses.
- **Segment performance** - Home care was down 1.3%, BPC fell 0.2% and foods grew 0.9%; Margins in the home care segment stood at 17.7% (-150bps YoY), personal care stood at 25.6% (+48bps YoY) and Foods & Refreshments was 19% (+118bps YoY).
- **Home care** – Segment witnessed 1.3% revenue decline and mid-single digit volume growth. Fabric Wash volumes grew in mid-single digit YoY driven by outperformance in premium portfolio. Household care volumes grew in low-single digit led by Dishwash.
- **BPC** – Business delivered 0.2% sales decline with mid-single digit volumes. Skin Cleansing revenue declined due to the impact of price reductions taken to pass on the benefits of lower commodity costs to consumers. Market development actions in bodywash continue to yield good results. While delayed winter impacted Skin Care performance in the quarter, premium non-winter portfolio continued to do well. Hair Care delivered volume led double-digit growth with broad based performance across brands and future formats continuing to gain traction. Oral Care grew mid-single digit led by Closeup. Key launches in this quarter include Glow & Lovely Powder finish crème, New active skin barrier care

range by Simple, Sunsilk hair serums, Close-up naturals range and Lakme's range of make-up products.

- **Foods** – F&R revenue grew 0.9%, volume declined in low single digit. Tea further strengthened value and volume market leadership. Green Tea and flavoured tea performed well. Coffee grew in double-digits driven by pricing. Health Food Drinks delivered competitive modest price-led growth driven by Plus range. Foods Solutions, Mayonnaise and Peanut Butter continue to clock strong growths. Ice Cream grew in mid-single digit on a high base. During the quarter, Knorr Korean K-Pot noodles and Bru Gold in Vanilla, Caramel and Hazelnut flavours were launched.
- **Outlook** – Management expects gradual recovery, rural recovery to be determined by rural income growth and winter crop yields, price growth is expected to be marginally negative moving ahead (in case commodity prices remain stable), lower commodity prices to keep competitive intensity high.

Q&A takeaways

- **FMCG Industry** - FMCG demand trends have largely remained stable and similar to previous quarter. Market volumes grew in high single-digit YoY, this came on a base of volume decline in mid-single digit last year. Cumulatively, over two years, market volumes have grown marginally at 2% CAGR. Urban markets grew 3% on a two-year basis while rural at 1%. Modern trade is doing well and continues to outpace general trade. Volume growth of premium products is significantly ahead of mass products in the market. Price growth in the market continued to tail off as expected, this is reflected in a sequential reduction of market price growth from 8% in June quarter to marginally negative in current quarter.
- **Rural vs urban** - Due to lower agriculture yields and uncertainty over future crop outputs, rural consumer sentiment remains subdued. Consequently, the anticipated buoyancy from festive season did not materialize. Urban growth continued to outpace Rural. Premium segments performed better compared to mass. Premium portfolio in rural has grown well.
- **Penetration, market share and product superiority** - 60% of the business is winning value market share on an MSE basis. More than 75% of the business is getting penetration, both absolute and relative penetration. 80% of business is growing or maintaining brand power scores. Compared to 2021, company has improved corporate value market share by almost 200 bps. Company has 3x more superior products when compared to the 2019 base, and the rest of the products are at par with competition on functionality. Company has stepped up effective coverage, which now stands at 1.25x to 2019 levels. Company has a reach of 3 mn outlets directly, of which 2.3 mn outlets are covered through distributor network and the remaining by Shakti Entrepreneurs in the rural hinterlands. Company's market share and growth in MT is higher compared to GT.
- **Separation of beauty and personal care** - From 1st April 2024, the beauty and personal care business will transition into two independent business units, namely beauty and well-being and personal care. Beauty and well-being business unit will house skin care, premium beauty, hair care, color cosmetics, and health and well-being categories, while personal care will include skin cleansing, oral care, and deodorants. This separation will aid in scaling up the business, improve efficiency and develop a full portfolio of prestige brands.

- **Winter and non-winter portfolio** - Winter portfolio is 30% of skincare. Non-winter portfolio grew in mid-single digit volumes. Premium skin care grew in double digits.
- **Detergent bars** - Grammage fill backs, price correction, trade input corrections have got deployed in the marketplace. Due to commodity deflation mass players have entered the market. Company expects growth in detergents to stabilize from 4QFY24 onwards.
- **Tea** - Deflation of plain tea has continued. Consumers are downgrading the tea brands. However, company has maintained value and volume leadership and value and volume market share for tea.
- **HFD** - Category has long term growth potential. Penetration of Horlicks and Boost has increased by 600 bps. Company has built in a strong top tier value-added part of the portfolio with both the lite versions and the plus versions, which are more functional, nutrition-led, pharma-type offerings which it is further expanding. Horlicks and Boost had witnessed a drop in consumption due to milk inflation. However, company expects this consumption to improve with milk inflation reducing. Company is also focusing on driving HFD consumption in winter and monsoon. HFD is considered as a discretionary product. In South and East (40% penetration) HFDs are used a day to day products. However, penetration is low in North and west.
- **ATL & BTL** - In price sensitive categories which have witnessed commodity inflation such as skin cleansing and laundry, company has opted for aggressive spends both ATL and BTL.
- **Distributor incentives** - Company has changed the margin structure and incentivized distributors in big cities to essentially sell more, service more stores, service and deliver them quickly, sell more lines - especially more market development or premium lines or more assortment, or more weight which should help improve both volumes and distributor earnings.
- **Operating margin** - Company expects to maintain margins around current levels in the near-term. There is still a difference of 200 bps in gross margin compared to pre -covid level which will be recovered gradually.

Exhibit 1: Quarterly performance

YE March (Rs mn)	3QFY24	3QFY23	2QFY24	YoY (%)	QoQ (%)
Net Revenues	151,880	152,280	152,760	(0.3)	(0.6)
Cost of materials	44,230	51,050	43,780	(13.4)	1.0
(% of sales)	29.1	33.5	28.7		
Purchase of stock in trade	29,440	28,920	28,430	1.8	3.6
(% of sales)	19.4	19.0	18.6		
Gross Profit	78,210	72,310	80,550	8.2	(2.9)
Gross margin (%)	51.5%	47.5%	52.7%		
Employee cost	6,490	6,760	7,080	(4.0)	(8.3)
(% of sales)	4.3	4.4	4.6		
Selling & admin	15,930	12,000	17,200	32.8	(7.4)
(% of sales)	10.5	7.9	11.3		
Others	20,390	18,180	19,330	12.2	5.5
(% of sales)	13.4	11.9	12.7		
EBITDA	35,400	35,370	36,940	0.1	(4.2)
EBITDA margin (%)	23.3	23.2	24.2		
Other income	2,850	2,280	2,830	25.0	0.7
PBIDT	38,250	37,650	39,770	1.6	(3.8)
Depreciation	2,820	2,600	2,690	8.5	4.8
Finance cost	810	260	720	211.5	12.5
PBT	34,620	34,790	36,360	(0.5)	(4.8)
Tax	9,130	8,720	9,140	4.7	(0.1)
ETR (%)	26.4	25.1	25.1		
Adjusted PAT	25,490	26,070	27,220	(2.2)	(6.4)
PATAMI margin	16.8	17.1	17.8		
Exceptional item	(300)	(1,020)	(50)		
Reported PAT	25,190	25,050	27,170	0.6	(7.3)
No. of shares (mn)	2,350.0	2,350.0	2,350.0		
Adj EPS (Rs)	10.8	11.1	11.6		

Source: Company, Systematix Institutional Research

Exhibit 2: Segmental performance

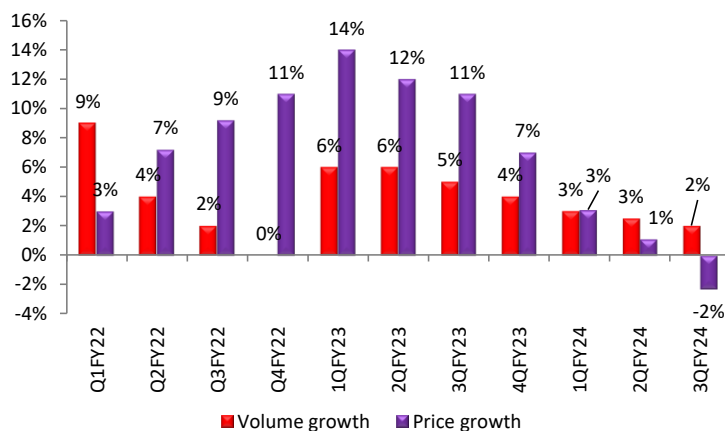
YE March (Rs mn)	3QFY24	3QFY23	2QFY24	YoY (%)	QoQ (%)
Segment revenue					
Home care	54,480	55,180	53,120	-1.3%	2.6%
Personal care	57,050	57,180	58,090	-0.2%	-1.8%
Foods & Refreshments	37,330	37,000	38,510	0.9%	-3.1%
Others	3,020	2,920	3,040	3.4%	-0.7%
Net Sales	151,880	152,280	152,760	-0.3%	-0.6%
Segment EBIT					
Home care	9,660	10,610	9,950	-9.0%	-2.9%
Personal care	14,610	14,370	15,810	1.7%	-7.6%
Foods & Refreshments	7,110	6,610	7,200	7.6%	-1.3%
Others	1,200	1,180	1,290	1.7%	-7.0%
Total EBIT	32,580	32,770	34,250	-0.6%	-4.9%

Source: Company, Systematix Institutional Research

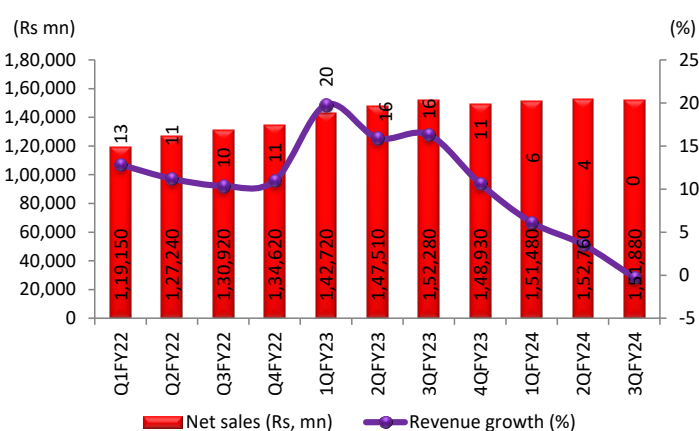
Exhibit 3: Change in Estimates

(Rs mn)	New estimates			Old estimates		Variance	
	FY24E	FY25E	FY26E	FY24E	FY25E	FY24E	FY25E
Revenue	624,805	674,504	735,426	639,802	697,513	-2%	-3%
EBITDA	147,454	162,555	180,915	154,192	170,891	-4%	-5%
EBITDA Margin	23.6%	24.1%	24.6%	24.1%	24.5%		
EPS	105,865	119,193	132,763	111,208	124,739	-5%	-4%

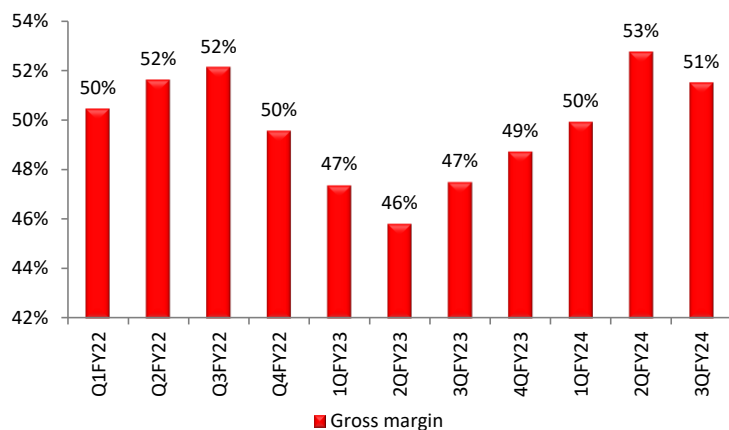
Source: Company, Systematix Institutional Research

Exhibit 4: Volume growth at 2%, pricing growth -2%

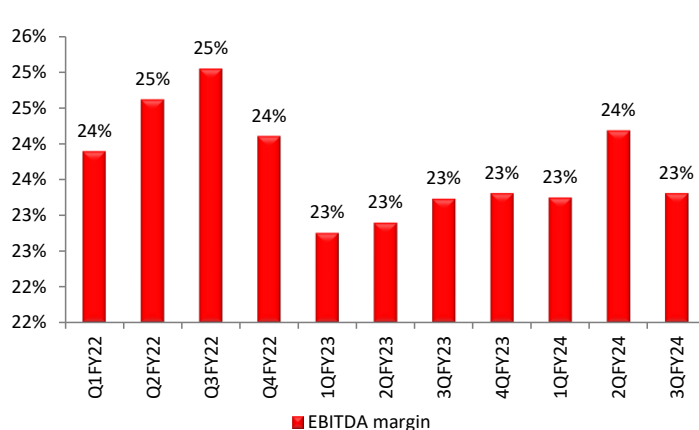
Source: Company, Systematix Institutional Research

Exhibit 5: Revenue declined 0.3% YoY and 0.6% QoQ

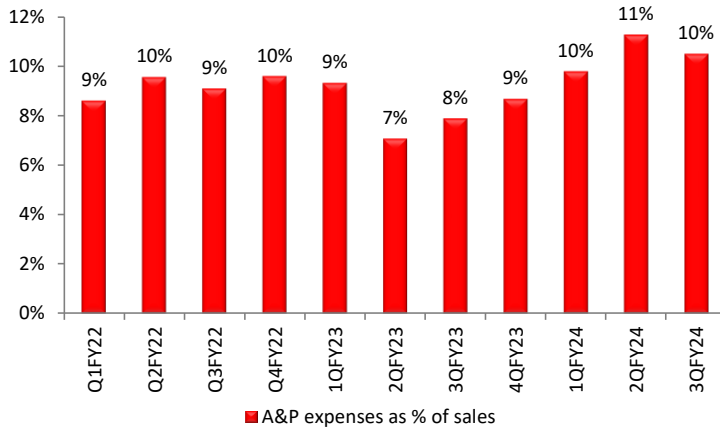
Source: Company, Systematix Institutional Research

Exhibit 6: Gross margin expanded 401 bps YoY

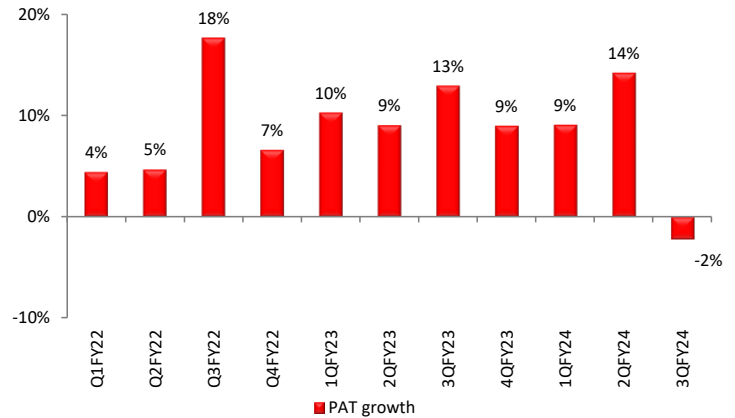
Source: Company, Systematix Institutional Research

Exhibit 7: EBITDA margin impact limited due to higher A&P/royalty

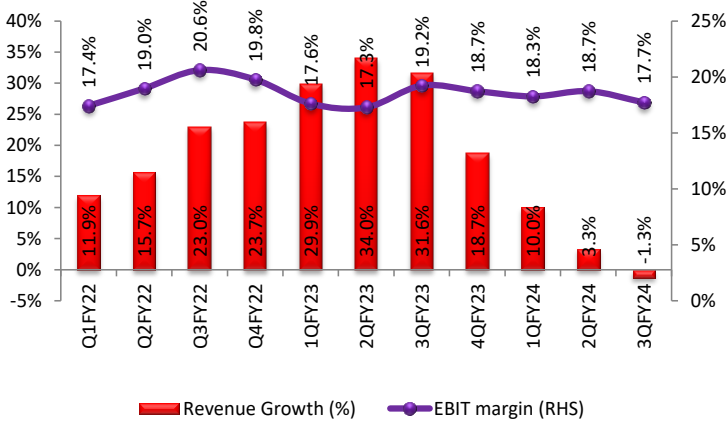
Source: Company, Systematix Institutional Research

Exhibit 8: A&P spends have picked up year on year

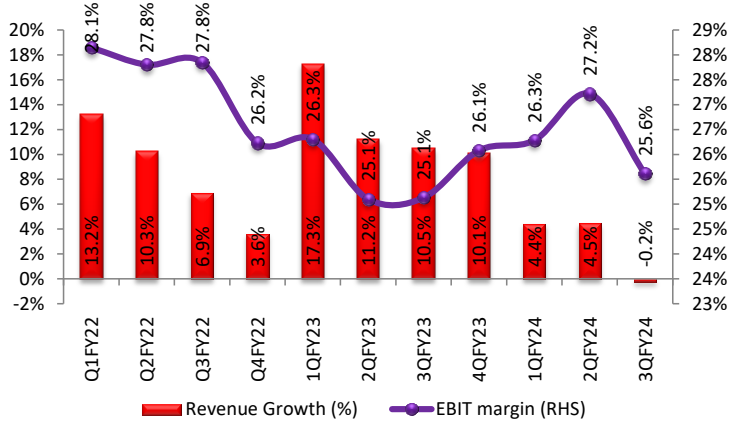
Source: Company, Systematix Institutional Research

Exhibit 9: PAT trajectory got into negative territory

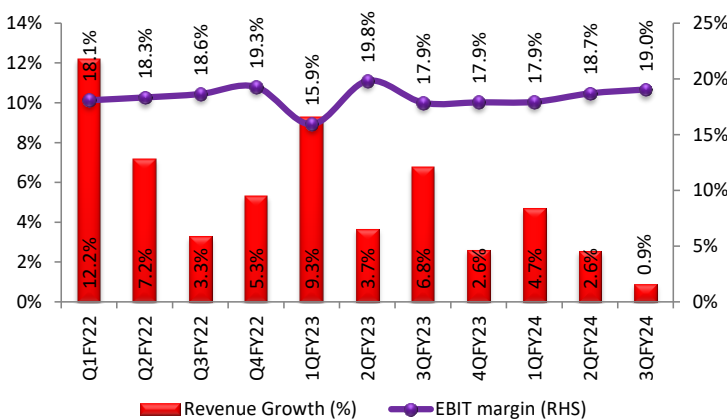
Source: Company, Systematix Institutional Research

Exhibit 10: Home care sees 1.3% decline, with volume uptick

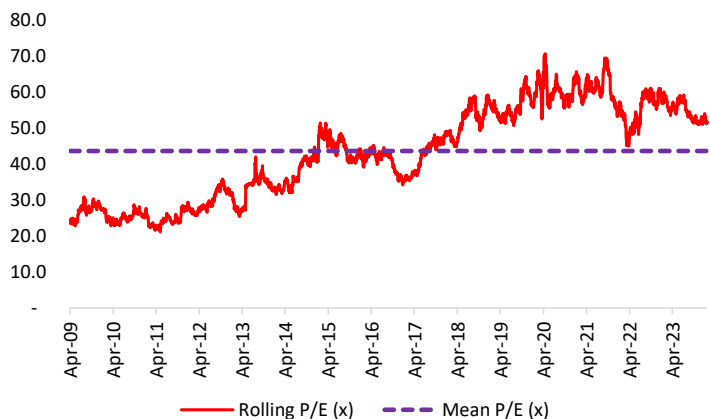
Source: Company, Systematix Institutional Research

Exhibit 11: BPC registered 0.2% decline, volumes remained positive

Source: Company, Systematix Institutional Research

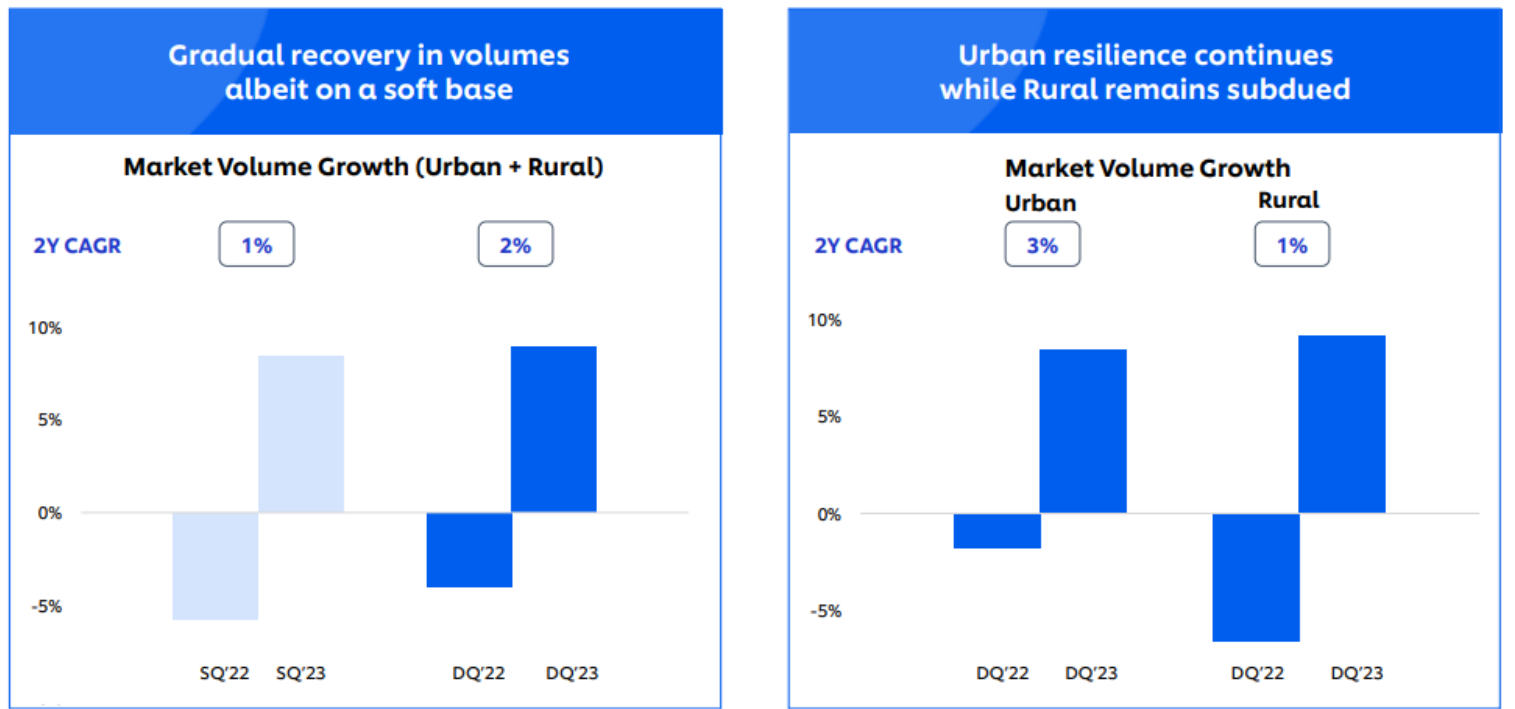
Exhibit 12: F&R growth at 0.9%, led by pricing in HFD

Source: Company, Systematix Institutional Research

Exhibit 13: Currently trades at 51.7x 1-yr fwd P/E

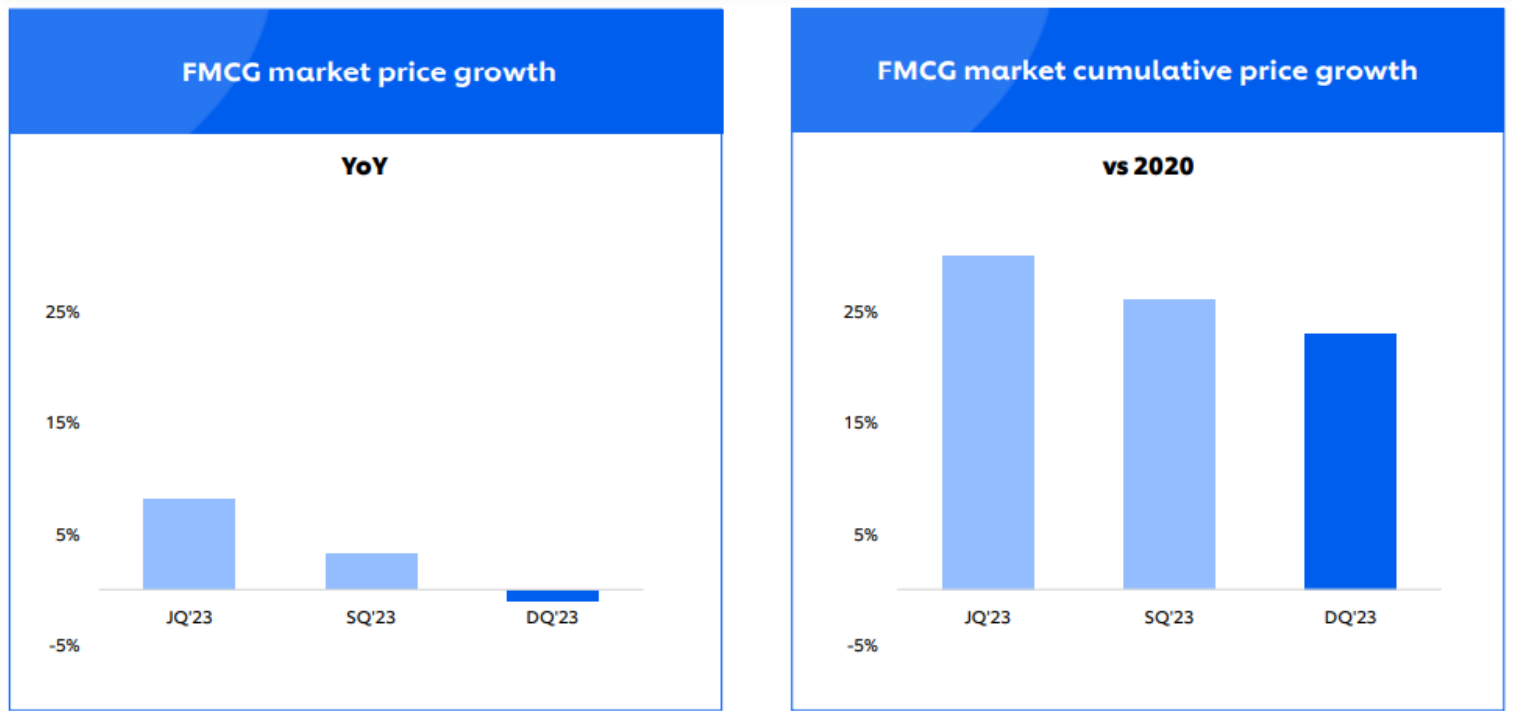
Source: Bloomberg, Systematix Institutional Research

Exhibit 14: FMCG industry volumes grew 9% with pick up in rural as well



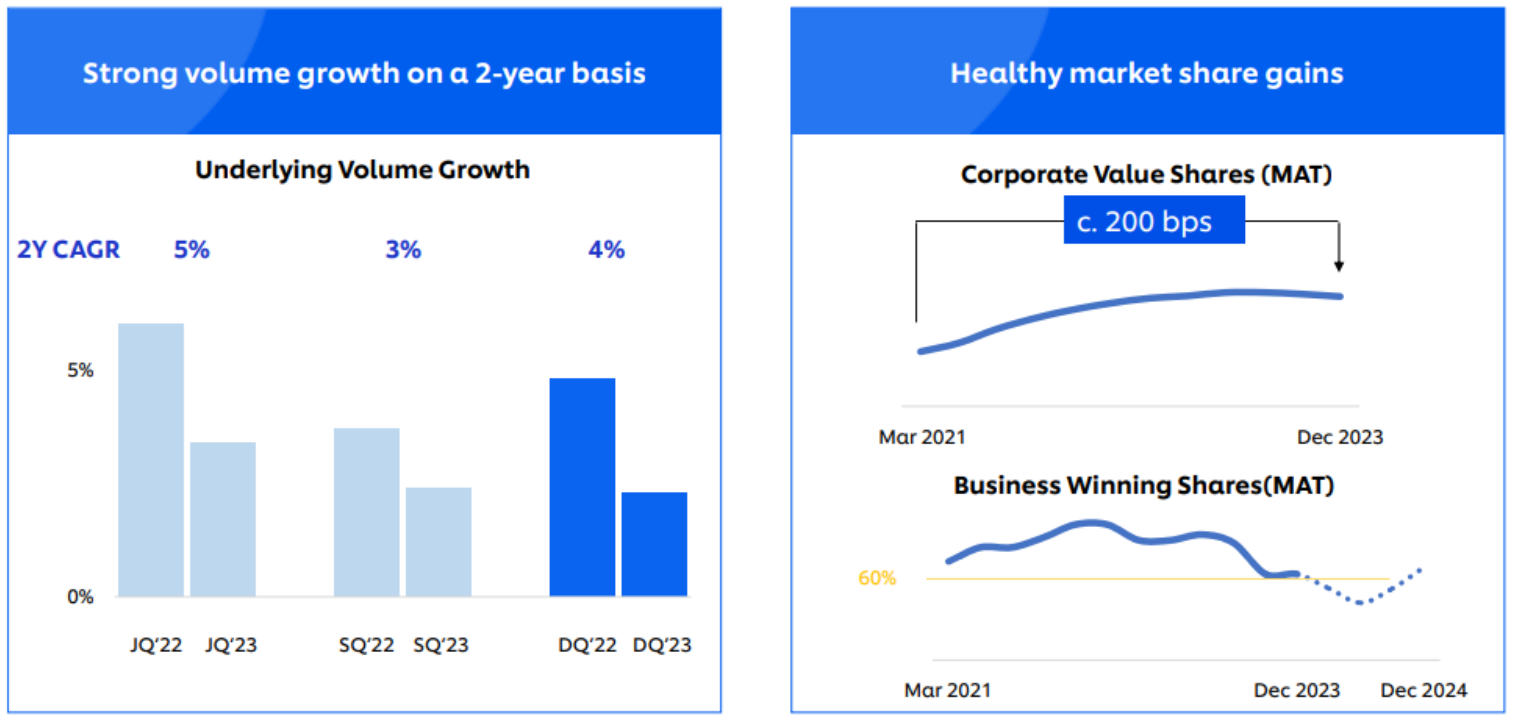
Source: Company, Systematix Institutional Research

Exhibit 15: Market price growth tailing off albeit remains high on 3 year basis at 20% plus



Source: Company, Systematix Institutional Research

Exhibit 16: HUL still outperforming industry with 4% 2-yr volume CAGR and 200bps higher share



Source: Company, Systematix Institutional Research

FINANCIALS

Profit & Loss Statement

YE: Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net Sales	5,24,460	6,05,800	6,24,805	6,74,504	7,35,426
RM Cost	1,64,240	2,01,370	1,92,440	2,09,096	2,27,982
Purchase of trad. Goods	93,110	1,15,790	1,07,466	1,09,944	1,19,874
Gross Profits	2,67,110	2,88,640	3,24,899	3,55,464	3,87,570
Employee costs	25,450	28,540	29,366	31,702	34,565
Selling & Admin costs	1,13,090	1,18,610	1,48,079	1,61,206	1,72,090
Total Expenses	3,95,890	4,64,310	4,77,351	5,11,948	5,54,511
EBITDA	1,28,570	1,41,490	1,47,454	1,62,555	1,80,915
Depreciation	10,910	11,370	11,043	12,279	13,371
Other income	2,580	5,120	9,500	6,656	7,322
EBIT	1,20,240	1,35,240	1,45,911	1,56,933	1,74,866
cost	1,060	1,140	2,850	3,135	3,449
PBT	1,19,180	1,34,100	1,43,061	1,53,798	1,71,417
Taxes	29,870	32,010	37,196	34,604	38,655
Adj. PAT	89,310	1,02,090	1,05,865	1,19,193	1,32,763
Extraordinaries/Exceptional	440	640	-	-	-
Reported PAT	88,870	1,01,450	1,05,865	1,19,193	1,32,763
No. of shares (mn)	2,350	2,350	2,350	2,350	2,350
Adj. EPS	38.0	43.4	45.0	50.7	56.5

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
PBT	1,18,740	1,33,460	1,43,061	1,53,798	1,71,417
Add: Depreciation	11,060	11,520	11,043	12,279	13,371
Add:	1,060	1,140	2,850	3,135	3,449
Less: taxes paid	(27,810)	(31,400)	(37,196)	(34,604)	(38,655)
Add: other adjustments	(2,570)	(5,230)	-	-	-
Less: WC changes	(10,000)	(9,580)	(4,587)	1,818	418
Total OCF	90,480	99,910	1,15,172	1,36,425	1,50,000
OCF w/o WC changes	1,00,480	1,09,490	1,19,758	1,34,607	1,49,582
Capital expenditure	(10,940)	(13,870)	(13,000)	(14,000)	(14,000)
Change in investments	(7,960)	(3,680)	-	-	-
/Dividend reced.	1,620	2,610	-	-	-
Total ICF	(17,280)	(14,940)	(13,000)	(14,000)	(14,000)
Free Cash Flows	79,540	86,040	1,02,172	1,22,425	1,36,000
Share issuances	-	-	-	-	-
Change in borrowings	-	-	-	-	-
Dividends	(75,260)	(84,740)	(95,278)	(1,07,274)	(1,19,486)
payment	(820)	(880)	(2,850)	(3,135)	(3,449)
Others	(4,070)	(3,910)	(61,649)	(61,649)	(61,649)
Total FCF	(80,150)	(89,530)	(1,59,777)	(1,72,058)	(1,84,584)
Net change in cash	(6,950)	(4,560)	(57,606)	(49,633)	(48,584)
Opening cash & CE	44,710	38,460	46,780	48,148	53,328
Closing cash & CE	38,460	46,780	48,148	53,328	58,564

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Equity capital	2,350	2,350	2,350	2,350	2,350
Reserves and surplus	4,88,260	5,00,690	5,11,276	5,23,194	5,36,469
Net worth	4,90,610	5,03,040	5,13,626	5,25,544	5,38,819
Minority	260.0	2,180.0	2,180.0	2,180.0	2,180.0
Total Debt	-	-	-	-	-
Other LT liabilities	26,780	30,300	32,421	34,690	37,119
Total sources	5,17,650	5,35,520	5,48,227	5,62,414	5,78,118
Net Block	61,690	69,490	79,490	89,490	99,490
Intangible assets	4,53,040	4,57,290	4,53,270	4,53,270	4,53,271
Net deferred tax	(63,030)	(63,330)	(63,330)	(63,330)	(63,330)
Other assets	10,380	11,030	11,802	12,628	13,512
CWIP	13,130	11,320	11,320	11,320	11,320
Investments	35,210	28,130	28,130	28,130	28,130
Cash	38,460	46,780	48,148	53,328	58,564
Inventories	40,960	42,510	46,218	49,895	56,416
Debtors	22,360	30,790	32,524	35,111	40,297
Other current assets	18,250	21,790	22,930	24,535	28,268
Current Assets	81,570	95,090	1,01,673	1,09,541	1,24,981
Creditors	90,680	95,740	97,572	1,05,333	1,16,862
Other CL	22,120	24,540	24,704	26,629	30,959
Current Liabilities	1,12,800	1,20,280	1,22,276	1,31,963	1,47,821
Net Working Capital	(31,230)	(25,190)	(20,603)	(22,421)	(22,840)
Total Uses	5,17,650	5,35,520	5,48,227	5,62,414	5,78,117

Source: Company, Systematix Institutional Research

Ratios

YE: Mar	FY22	FY23	FY24E	FY25E	FY26E
Yoy growth in Revenue	11.5	15.5	3.1	8.0	9.0
Yoy growth in EBITDA	10.6	10.0	4.2	10.2	11.3
Yoy growth in Net income	8.4	14.3	3.7	12.6	11.4
Effective tax rate	23.8	22.4	26.0	22.5	22.6
EBITDA margin	24.5	23.4	23.6	24.1	24.6
PAT margin	17.0	16.9	16.9	17.7	18.1
ROACE (pre-tax)	23.6	25.7	26.9	28.3	30.7
ROAE	18.5	20.5	20.8	22.9	24.9
Net debt to equity (x)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Inventory days	29	26	27	27	28
Debtors days	16	19	19	19	20
Payable days	63	58	57	57	58
NWC days	(19)	(14)	(11)	(11)	(10)
Per share numbers (Rs)					
Reported earnings	38.0	43.4	45.0	50.7	56.5
Dividend	34.0	39.0	40.5	45.6	50.8
Book Value	227.1	232.9	237.8	243.3	249.5
Valuations (x)					
Price to diluted earnings	67.0	58.7	56.6	50.2	45.1
EV / EBITDA	38.6	35.0	33.6	30.4	27.3
Price to sales	9.5	8.3	8.0	7.4	6.8

Source: Company, Systematix Institutional Research

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