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# FMCG Sector : Indian Companies Going Conglomerate

11th September 2008

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# Preamble

The FMCG sector seems to have finally joined India Inc's growth party by posting surprising double-digit growth in sales in the past couple of years. The Indian economy has maintained its growth momentum, with the GDP growth rate exceeding 8% every year since 2003-2004, and only now the effect is being seen in the largely defensive FMCG sector.

The Indian FMCG sector is the fourth largest sector in the economy with a total market size in excess of US$ 13.1 billion. The FMCG market is set to treble from US$ 11.6 billion in 2003 to US$ 33.4 billion in 2015. (source: IBEF). FMCG sector will witness more than 50 per cent growth in rural and semi-urban India by 2010, according to an analysis carried out by the Associated Chambers of Commerce and Industry of India (Assocham).

A major portion of the monthly budget of each household is reserved for FMCG products. An average Indian spends around 40 per cent of his income on grocery and 8 per cent on personal care products. However, the per capita income level in India is still very low compared to the developed world. Besides, the penetration level of many products is also relatively low and several categories remain fairly unbranded.

Burgeoning Indian population, particularly the middle class and the rural segments, presents an opportunity to makers of branded products to convert consumers to branded products. All these factors provide a huge untapped potential for the industry.

The industry's future prospects look bright, considering rising household incomes, higher penetration, increasing per capita consumption, a rising population base and the spread of modern retail. The announcements in the Budget 2008-09 also have an overall positive impact on all FMCG companies and benefit them in many ways:

- The debt relief scheme waiving off overdue agricultural loans will lead to an increase in disposable incomes in rural areas. Consumer companies with exposure to rural India will benefit.
- The increase in exemption limits of personal income tax can be expected to prop up consumption in a large section of the populace as there will will now be more disposable income in the hands of the consumers.
- The reduction in the CENVAT rate from 16% to 14% will be a competitive stimulus for domestic manufacturing activity. This will also benefit the consumers as goods will become cheaper.

Increases announced by the recent Pay Commission will also boost the spending power of Government employees.

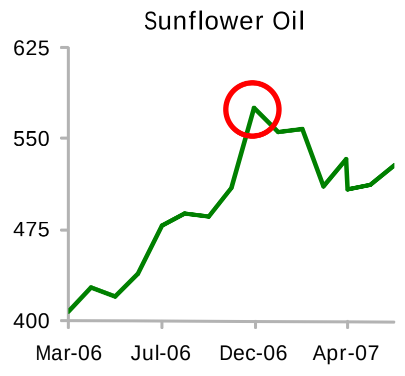
The FMCG industry is characterised by a well established distribution network, strong MNC presence, intense competition between the organised and unorganised segments and low operational cost. In contrast to other manufacturing sectors, FMCG is relatively less capital-intensive, but demands immense skills and expenditure on branding and distribution.

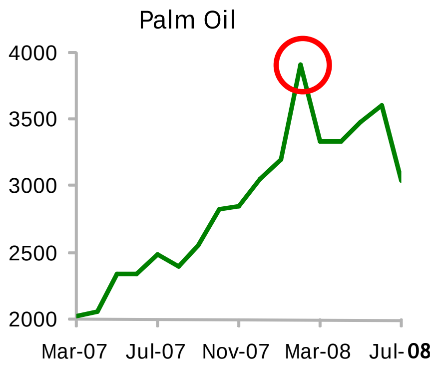
FMCG companies maintain intense distribution network. They spend a large portion of their budget on maintaining distribution networks and new entrants who wish to bring their products in the national level need to invest huge sums of money on promoting brands. But the market is more pressurized with presence of local players in rural areas and state brands.

The growth in the sector has so far been both volume and value driven. The growth has been substantially volume driven. Also the price hikes that have happened have not been across the board but only in a few categories and products.

The FMCG companise have also come into light on account of declining commodity prices. While inflation restricts the industry's growth, many companies in the sector thrive under inflationary pressures. Most companies pass on the cost inflation to consumers, via a judicious blend of price hikes, packaged size reduction and change in product mix. Few consumers react by down-trading to lower priced products, but most hang on to their preferred brands if price hikes are moderate.

In Q4 of FY07-08 FMCG companies had faced the challenge of sharp rise in commodity prices leading to increased input costs. The spiraling prices of essential commodities have impacted the companies' bottom line putting pressures on their volume growth. Last 2-3 yrs commodity price analysis shows abnormal high prices in Q408 period. This affected the margins but the companies resorted to gradual price increases thereby stabilizing the margins in the current quarter. The commodity prices are now on a downward move which is expected to impact profits like never before and lead to better margins.




FMCG companies are also expected to gain from the slowdown in media sector. The intense competition in FMCG sector makes advertising an important expense. They tend to spend nearly 10% of their revenues on an average on advertising and promoting their products, which is the highest ad spend figure for any industry. But the advertising spends are expected to decline as the media companies are expecting a deceleration in advertisement revenue growth on account of the current economic slowdown and increased competition.

Most companies in the sector create value through product differentiation, package innovation, differential pricing and highlighting the functional aspect. This adds to the brand value of the FMCG companies. In a market where products are similar, branding can have a large effect on the price that customers will pay. Traditionally price is determined on growth and brand value. Though these companies traditionally trade at around 20x on account of brand valuation. Today most of the companies are available at relatively lower valuation compared to the past valuations in spite of improved scenario and fundamentals. Thus the intrinsic values of these companies are understated categorizing them as "value picks".

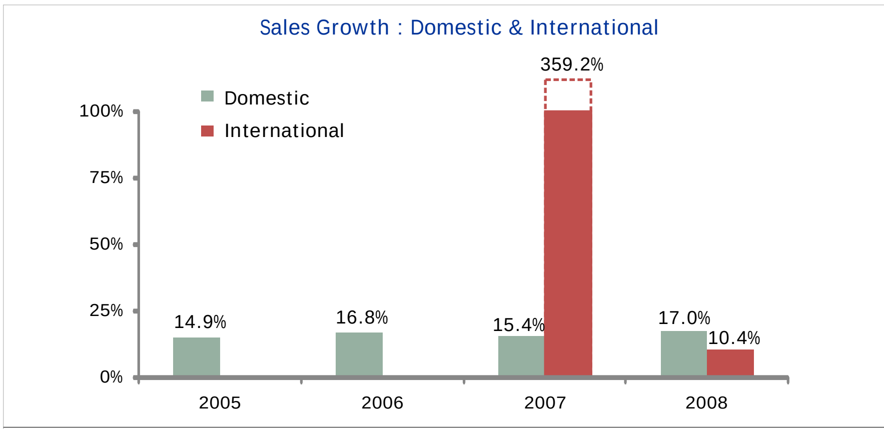
## Way forward: Indian companies going conglomerate through inorganic growth

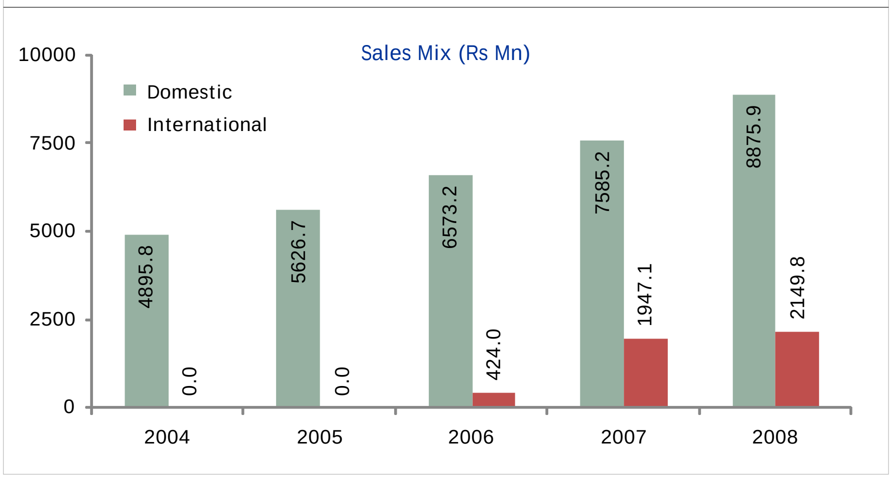
Multinational FMCG companies like Hindustan Unilever, ITC, Nestle, Procter & Gamble and GlaxoSmithKline Consumer Healthcare traditionally comprise the first category of FMCG companies. Another category is non-traditional FMCG companies, which is dominated by homegrown companies like Asian Paints, Dabur, Tata Tea, Marico and United Spirits. These companies have grown to become market leaders in their respective segments, giving strong competition to MNC brands. The third tier includes small, but strong regional players operating on a smaller scale. They are mostly price warriors, who expand by eating into the market share of national players. In this report we highlight on the three companies: Godrej Consumer Products Ltd., Marico Ltd. and Pidilite Industries, which are growing inorganically to become conglomerates.

Using a spider for an analogy in a story on FMCG business might be out of the ordinary. But in this case, its technique in building its habitat is simply the best way to illustrate the distinctive business model of these Indian FMCG going conglomerate companies. During the past few years, some companies in the sector have used the inorganic route to grow at a faster pace. Like the spider swinging from point to point, thread in tow, few FMCG companies are now rapidly diversifying, setting up more and more new businesses or extending existing product lines in diverse and uncommon business regions. The sector witnessed a spate of acquisitions and alliances with several companies aggressively exploring global markets especially those that had a substantial population of Indian origin.

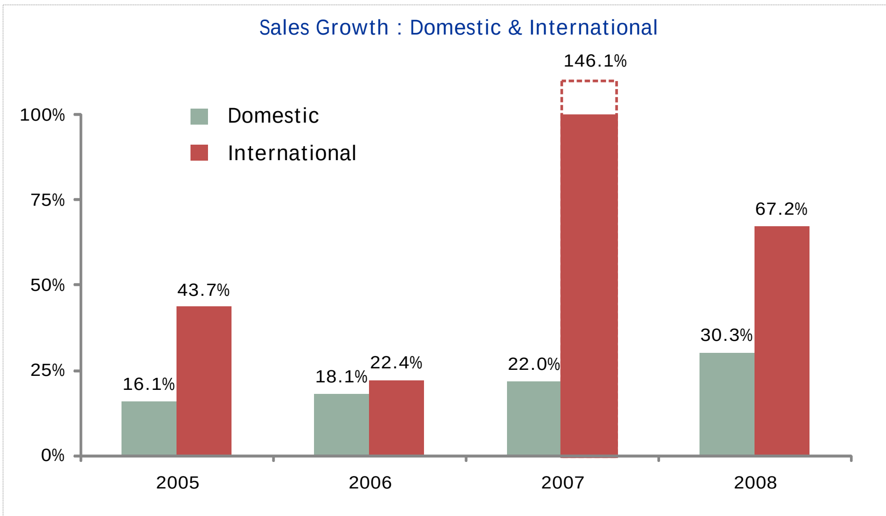
FMCG conglomerates expect to derive the key benefits of diversified portfolio, impressive growth rates, larger customer base, to mention a few, from transforming themselves from Indian majors to global conglomerates. To earn the right to be known as a conglomerate, a group has to demonstrate several domineering traits. It must be large. It must consistently demonstrate the ability to successfully diversify into new businesses, using cash from existing enterprises to fuel this insatiable desire for new opportunities. It must have the ability to distribute resources across a portfolio of businesses. It must de-risk itself from economic cycles and exert sizeable influence in its environment. Finally, the very mention of its name must send a shiver down the spines of competitors. Without doubt, all these traits are becoming evident in the three Indian FMCG conglomerates mentioned in the report.

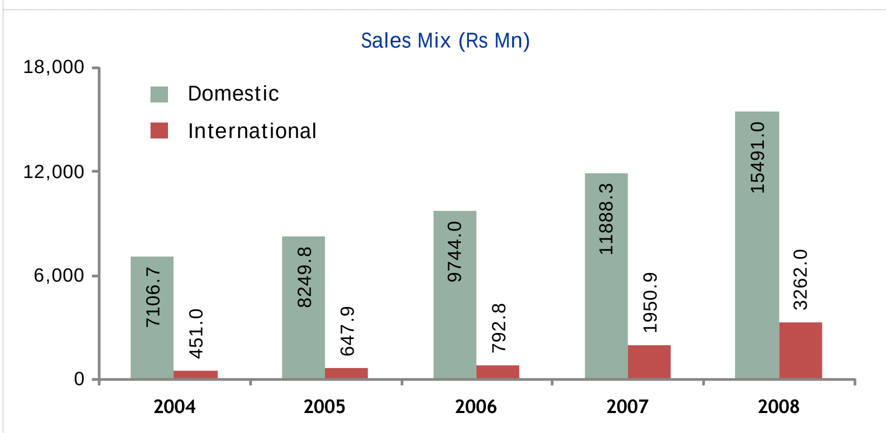
## Annexure I
## Godrej Consumer Products Ltd
## Geographical Breakup and Growth



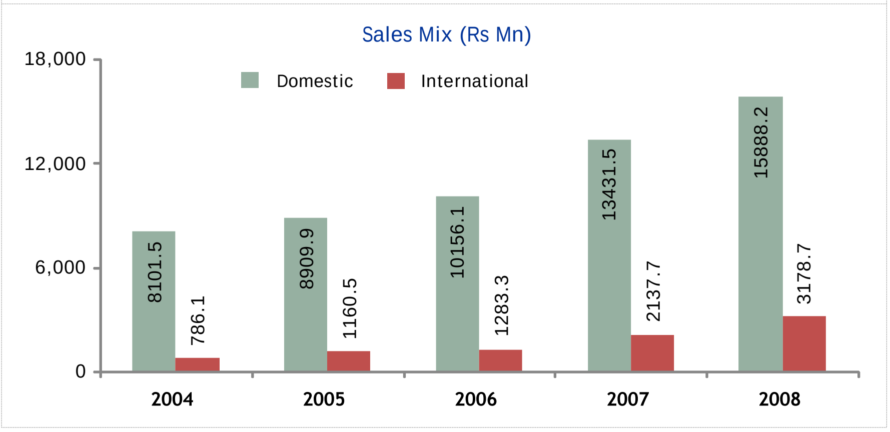




## Annexure II
## Pidilite Industries Limited
## Geographical Breakup and Growth



Annexure III
Marico Industries Ltd.
Sales Breakup
and Growth


Annexure No. 1, 2, and 3 depict the growth stories of the mentioned companies. The companies are growing at a delightful pace on account of inorganic ventures in the international markets. There is a change in the sales mix as the percentage contribution of international revenues to the total sales is on a rising trend. The growth in the international sales figures is also encouraging.

## On managing diversity

History has shown that conglomerates can become so diversified and complicated that they are too difficult to manage efficiently. Since the height of their popularity in the period between the1960s and the 1980s, many conglomerates have reduced the number of businesses under their management to a few choice subsidiaries through divestiture and spin offs.

Whether conglomerates are optimal organisation strategists is a debated question today. Research shows that premium conglomerates can create incredible value. One of the best performing companies in the last few years has been ITC, which is extremely diverse. "As many focused companies fail as conglomerates," Mr. Deveshwar, Chairman, ITC Ltd, notes with glee. "The conglomerates that failed, did so because they did not use their assets cleverly." And there is also a lot of research to suggest that diverse businesses are particularly appropriate to dynamic, emerging markets.

## Conclusion

FMCG companies are fighting to stand out amid the clutter of a massively vigorous and strengthening consumer market. To keep consumers interested India's brands are diversifying well-loved favourites by entering new FMCG territory. It is quite common for emerging market companies to want to sell their share of the business to their global partners. In case the global company is willing to acquire the local partner, the latter would improve its negotiating power and strengthen its position.

FMCG sector is long established and over the years, sustaining ups and downs of the Indian economy. Thus the Critical operating rules in Indian FMCG sector can be summarised as follows:

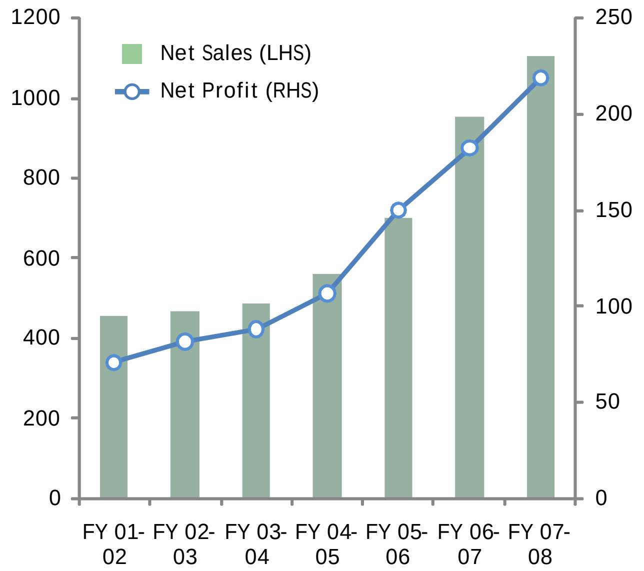
- Heavy launch costs on new products on launch advertisements, free samples and product promotions.
- Majority of the product classes require very low investment in fixed assets
- Existence of contract manufacturing
- Marketing assumes a significant place in the brand building process
- Extensive distribution networks and logistics are key to achieving a high level of penetration in both the urban and rural markets
- Factors like low entry barriers in terms of low capital investment, fiscal incentives from government and low brand awareness in rural areas have led to the mushrooming of the unorganised sector
- Providing good price points is the key to success.

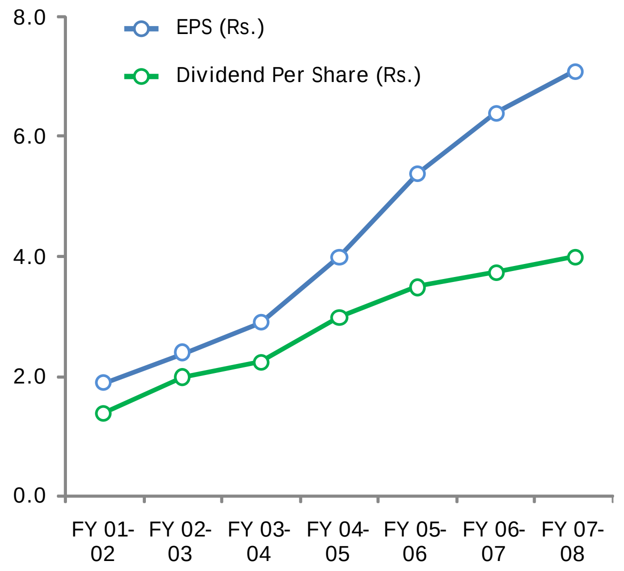
FMCG company stocks are relatively stable and are not affected by global variation. In most of the Stock exchanges, FMCG companies are the key players. With the market in a bearish phase, the FMCG sector has found flavour among investors. The sector's defensiveness is demonstrated by the stability in returns generated even during times of slow economic growth. While the Sensex is down by 29% since the beginning of this year, the ET FMCG index comprising the top 20 stocks in the sector, has fallen only by 12.5%.

Nevertheless, the FMCG growth story is here to stay. According to a survey on fast moving consumer goods (FMCG) industry undertaken by Federation of Indian Chambers of Commerce and Industry (Ficci), the growth momentum is likely to continue in the current fiscal as well, spurred by lifestyle category goods. It includes products categories like skin care, shampoos, deodorants, anti-aging solutions, fairness products and various men's products. Most are counting on two factors as driving forces :-

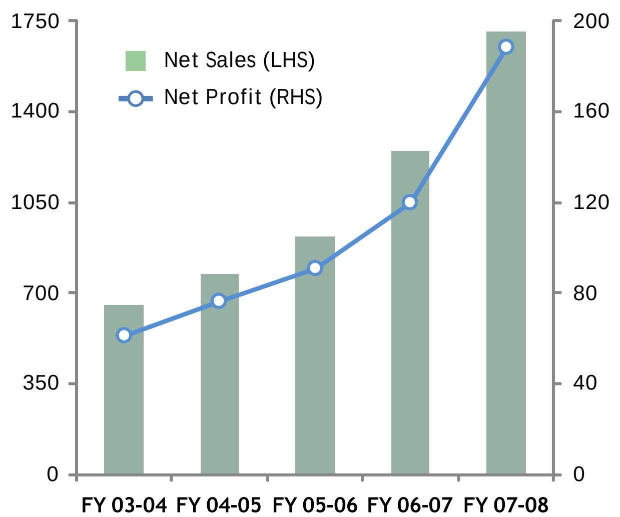
- Increased market penetration in rural areas and
- A shift in urban outlook regarding expenditure.

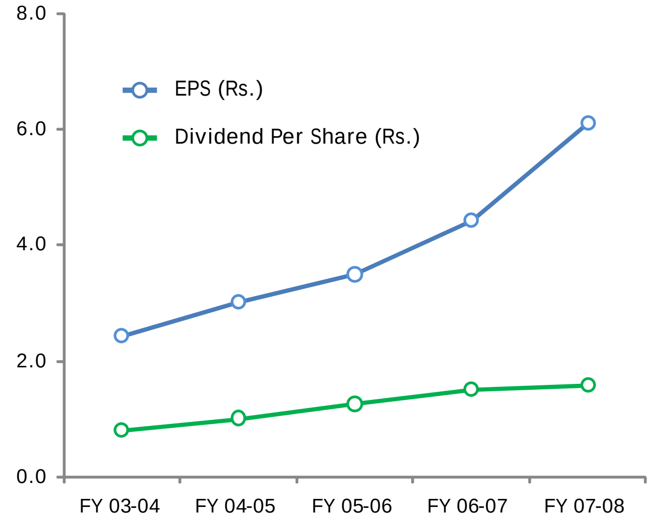
## Godrej Consumer Products Limited



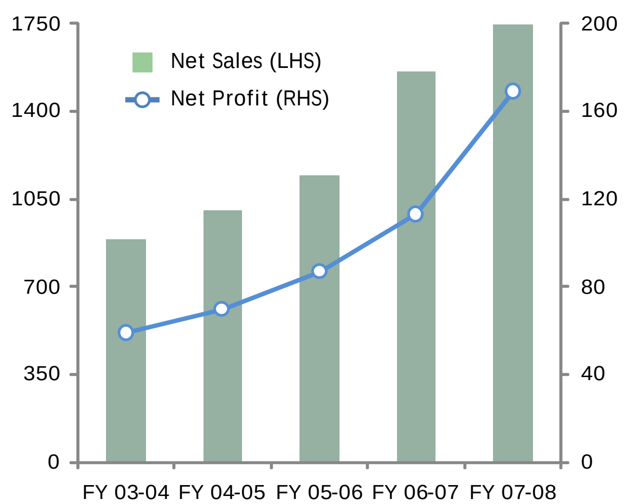



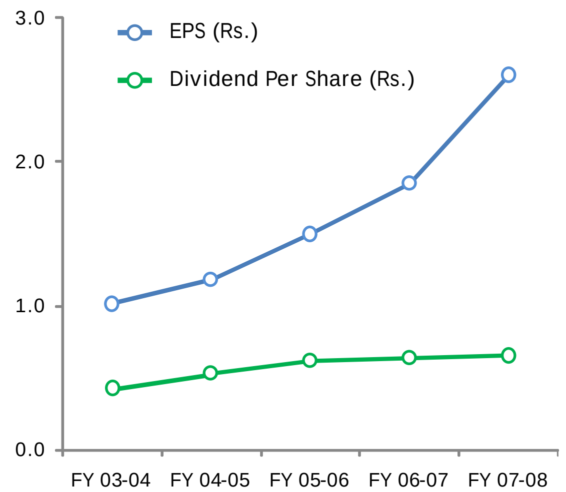

## Pidilite Industries Limited




## Marico Industries Limited




**EPS/DPS figures are ex-bonus*

# Godrej Consumer Products Ltd

CMP Rs. 124.1
Target Rs. 184.0

Initiating Coverage
BUY

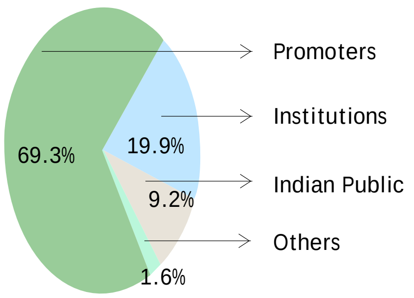
## Stock Data

| | |
|---|---|
| Bloomberg | : GCPL.IN |
| Reuters | : GOCP.BO |
| BSE Code | : 532424 |
| NSE Code | : GODREJCP |
| BSE Group | : B |

## Stock Codes

| | |
|---|---|
| Benchmark | : BSE FMCG |
| 52 W High/Low | : 160.1/95.0 |
| Float | : 30.7 Mn |
| Mkt Cap | : Rs. 28,027 Mn |
| Face Value | : Rs. 1.0 |

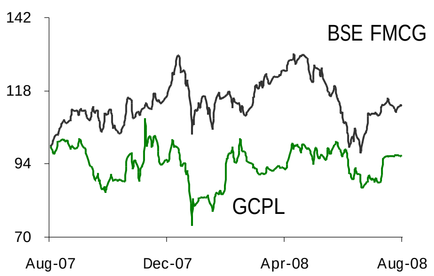
## Shareholding Pattern (as on June 08)




## Stock Returns

| | 1 Mth | 3 Mths | 6 Mths |
|---|---|---|---|
| GCPL | 8.24 | 0.76 | 1.12 |
| BSE 500 | 1.00 | -14.46 | -22.30 |

## Price Comparison




Deepti Singh - deepti@ppfas.com

Godrej Consumer Products Ltd. (GCPL) is a major player in the Indian FMCG market with leadership in personal, hair, household and fabric care segments. Their centre of attention is in providing customers with novel, value goods required for meeting their daily needs and improving the quality of their life. This is achieved through the brands the company markets.

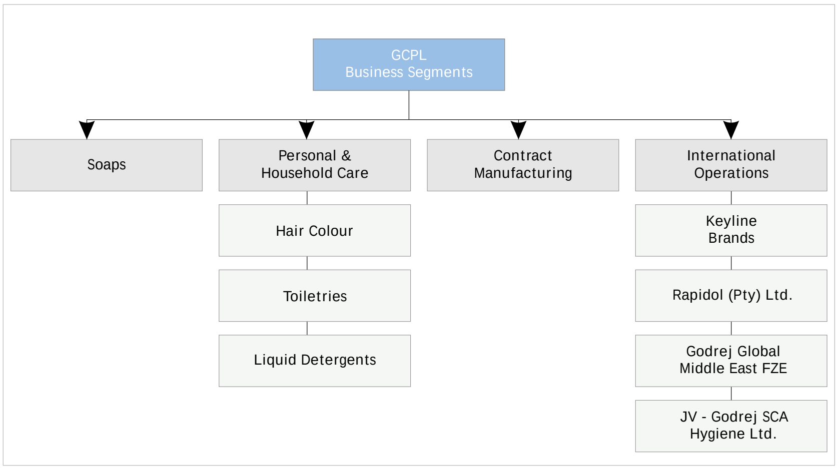
The company operates in two segments namely soaps and personal care.

They are among the largest marketer of toilet soaps in the country with leading brands such as Cinthol , Evita, Crowning Glory, Vigil, Shikakai, Fairglow , Godrej No.1.

They are the leader in the hair colour category in India and have a vast product range from Godrej Renew Coloursoft Liquid Hair Colours, Godrej Liquid & Powder Hair Dyes to Godrej Kesh Kala oil. Their personal care segment also includes shaving cream and gel, talcum powder and deodorant.

Their liquid detergent brand EZEE is the market leader in its category. They are also the preferred supplier for contract manufacturing of toilet soaps for some of the most well-known brands in the country. Their key strength is being part of the Godrej group of companies and the strong brand equity generated by the "Godrej" brand name. They believe that the Godrej brand commands a recall amongst the consumers in India due to its image and goodwill established over the years.

## Business Segmentation



## Strengthening the global marketing network

The company plans to leverage on its global marketing network by introducing its own established brands that would compliment the existing international product lines. There are also plans to unleash a slew of launches across new categories like Baby care, glycerine and healthcare across its global distribution network in a phased manner. It expects international sales to account for 50% of its revenues over time.

### KEYLINE Brand

GCPL acquired Keyline Brands Ltd, UK in October 2005. The acquisition gave the company access to established brands like CUTICURA, ERASMIC ,AAPRI etc and also entrance to the markets of Europe, Australia and Canada. Keyline has enabled them to manufacture, market, sell and distribute cosmetics, toiletries and men's grooming categories and developed a customer base in numerous supermarket chains and discount stores. Thus with the acqusition GCPL used Keyline's existing trade channels and strong customer base to take Godrej brands across the globe to reach newer heights. For the year ended March 31, 2008, Keyline reported revenues of Rs 1639.55 million and net profit of Rs 123.29 million. Keyline further acquired "Touch of Silver" and "Henara" hair care brands in 2008. This will further enhance its product portfolio and gain access to an already established consumer base of these products.

### RAPIDOL's Inecto Brand

Godrej Consumer Products Ltd. (GCPL) acquisition of the South African business of Rapidol, U.K. as well as its subsidiary Rapidol International gives the company ownership of strong ethnic hair colour brands like 'INECTO' and 'SOFLENE' in ten countries. INECTO has an 80% market share of the South African ethnic hair colour market. The company also gets access to Rapidol's strong marketing network spread across South Africa, Zambia, Mozambique, Tanzania, Swaziland, Ghana, Namibia, Zimbabwe, Mauritius, Seychelles and Madagascar. For the year ended March 31, 2008, Rapidol reported revenues of Rs 406.517 million and net profit of 46.122 million.

### Godrej Global Mideast FZE

GCPL acquired Godrej Global Mideast FZE on October 1, 2007, for Rs 58 million. Godrej Global Mideast FZE was a 100% subsidiary of Godrej International Limited and was established in Sharjah with the objective of distributing Godrej FMCG products in the Middle East. It has a strong distribution network in countries such as Oman, Saudi Arabia, Kuwait and Bahrain. It has reported revenues of Rs 49.1 million for the financial year 2007-08.

### Godrej SCA Hygiene Limited

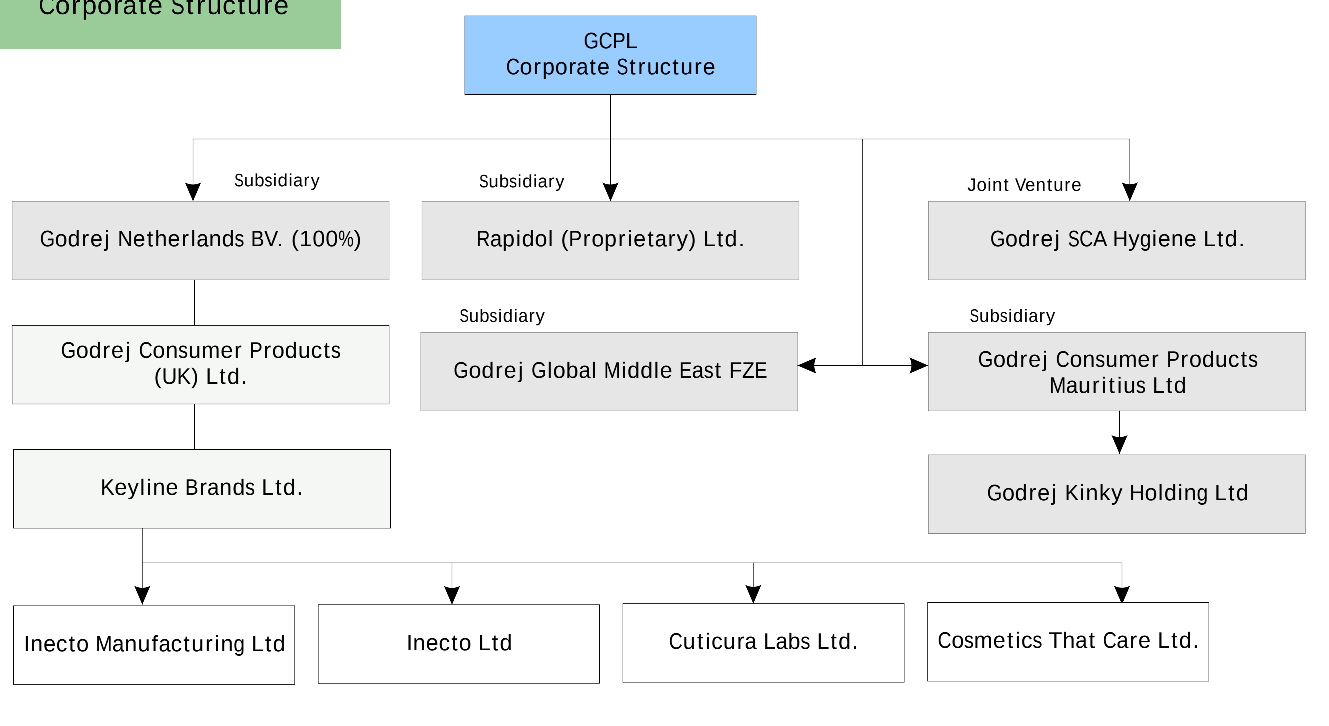
Godrej SCA Hygiene Limited is a Joint Venture Company between SCA Hygiene Products AB, Sweden, (SCA) and Godrej Consumer Products Limited

(GCPL). It manufactures and market's paper based absorbent hygiene products, specifically sanitary napkins and baby diapers, in India. SCA and Godrej Consumer Products Limited are equal partners in the Joint Venture.

### KINKY hair brand

In April 2008,GCPL acquired the KINKY hair business in South Africa. Kinky hair brand is one of the leading brands in the South African hair business, which is a 36 year old business set up by a family of entrepreneurs in South Africa. The Kinky brand is a self created premium brand South Africa and the trademark is registered in several countries of the world. Some of Kinky's products include dry hair, hair braids human hair extensions, hair pieces, wigs and wefted pieces. Kinky also offers hair accessories like styling gels, hair sprays, oil free shampoo, bonding glue and bonding glue removal. This acquisition enables the company to diversify into a new line of business and expand their hair product portfolio. The acquisition of a reputed brand like Kinky will enable them to strengthen their portfolio of product offerings in South Africa. This acquisition is their fourth and considerably enhances their scale and size as an Indian FMCG player in the International arena.

## Corporate Structure




Cosmetics That Care Limited has been wound up with effect from May 22, 2007. Cuticura Labs Limited has been wound up with effect from July 24, 2007.

## Soaps business on a high-growth trajectory

GCPL is the second largest toilet soaps player in India with a market share of 9.7% (FY08). The soap business is the single largest contributor accounting for almost 52% of the company's consolidated earnings at Rs 11025.7 Mn in FY08. The toilet soap category accounted for 63.8% of their standalone sales for FY 08. The company continues to maintain its market share in India. The following table indicates their market share in the toilet soaps category over the years:

| | Fiscal 2005 | Fiscal 2006 | Fiscal 2007 | Q2FY08 | Q3FY08 | Fiscal 2008 |
|---|---|---|---|---|---|---|
| Market Share | 8.00% | 8.50% | 9.10% | 10.20% | 9.70% | 9.70% |

*Source: AC Nielsen*

Their main brands in the toilet soap category include 'Cinthol', 'Godrej FairGlow', 'Godrej No.1', 'Evita', 'Godrej Shikakai',and 'Crowning Glory'. All the soaps marketed by GCPL are in 'Grade 1' category, and have edge over competition as all its major offerings are competitively priced. 'Cinthol', their flagship brand, is one of the oldest toilet soaps brands in India having been launched in 1952. 'Cinthol' has been recognised as a Superbrand by Superbrands Council (UK) in 2004 and 2006.

They launched 'Godrej FairGlow' brand of soaps in 1999. Fairglow brand, India's first Fairness soap, has created marketing history as one of the most successful innovations. 'Godrej No. 1' is the largest selling Grade 1 soap brand in the country. The brand provides a Grade 1 quality product at an affordable value for catering to the mass Indian populace. Their soaps 'Godrej Shikakai' and 'Crowning Glory' cater to the hair care markets.

## Maintaining market share in hair colourants

GCPL is a leader in this category in India, with a market share of 35.2% (FY08). The hair colourants category accounted for 23.1% and 22.8% of their standalone and consolidated sales for the FY 07-08 and is likely to grow at the industry rate of 20% in the coming years. Their hair colourant business grew by 20.4% during FY 07-08 as compared to FY 06-07.

Some of their main brands in the hair colourants category include Godrej Powder Hair Dye, Renew and ColourSoft. They have a variety of offerings ranging across powders, liquids and creams. They have priced their products at various price points to cater to a gamut of consumers. In the hair colour category value growth is lower in the last three quarters since it had not taken any price increases. The company expects the price hikes to help them in driving growth going forward.

## Widespread sales and distribution network and supply chain competencies in India

GCPL has a well penetrated and a widespread distribution network in India. They have built their presence in both the urban and rural markets. Thus enabling them to benefit from the opportunities in both segments. They have a sales team which comprise of over 250 staff spread across the country. They have a network of 33 Carrying and Forwarding agents and over

4,500 distributors, super stockists and sub stockists to support the sales force in India. This allows dissemination into the rural markets of the country. They have a distributor in almost every major town in India. Through their distributors and sub stockists cover they around 650,000 retailers in India.

### Sustained momentum in every business

GCPL has exhibited sustained growth momentum in every business segment over the years. GCPL continues to be the second largest toilet soaps player and a leader in the hair colour market with a market share of ~ 10% and 35% respectively. But the other business segments of the company are not lagging behind either. Their brand, 'Ezee' is one of the largest selling liquid detergents in India with leadership market share. The brand has been recognized as a Superbrand in FY07. They had launched Godrej Liquid Dishwash in January 2003 with a modern packaging and design. Toiletries contributed to 20% of GCPL's total consolidated sales in FY 07-08. 'Godrej Shaving Cream' is amongst the oldest brands in the toiletries category.

| Sales Comparison(consolidated) (Net of excise duty) | FY04 | FY05 | FY06 | FY07 | FY08 | % Growth | CAGR |
|---|---|---|---|---|---|---|---|
| Soaps | 2871.9 | 3341.3 | 3927.3 | 4750.9 | 5689.9 | 19.8% | 18.6% |
| Hair Colours | 1147.9 | 1335.5 | 1625.4 | 2091.3 | 2518.3 | 20.4% | 21.7% |
| Toiletries | 260.9 | 245.1 | 818.1 | 2148.9 | 2229.7 | 3.8% | 71.0% |
| Liquid Detergents | 355.9 | 365.2 | 397.2 | 388.4 | 384.7 | -1.0% | 2.0% |
| By – Products | 147 | 140 | 151 | 152.8 | 203.1 | 32.9% | 8.4% |
| Contract Manufacturing | 112.2 | 199.6 | 78.2 | 0 | 0 | | |
| Total | 4895.8 | 5626.7 | 6997.2 | 9532.3 | 11026.0 | | |

### Dividend Distribution Policy

The financials depict a healthy state of affairs. Topline has grown at a CAGR of 22.37% and bottomline at a CAGR of 25.19% over 04-08.(consolidation basis). Return on Capital Employed (ROCE) and Return on Net Worth (RONW) are high at 56% and 94.4% respectively on a consolidated basis. The company is quite shareholder friendly in its distribution policy. It has consistently paid out about 75 - 90 per cent of its earnings as dividends each year The Company has paid dividends in each of the last five years.

| Fiscal | EPS | Dividend per Equity Share of Re. 1 each | Dividend Payout (%) |
|---|---|---|---|
| 2004 | 2.90 | 2.25 | 79.20% |
| 2005 | 4.00 | 3.00 | 75.80% |
| 2006 | 5.40 | 3.50 | 65.20% |
| 2007 | 6.20 | 3.75 | 60.90% |
| 2008 | 7.10 | 4.00 | 60.00% |

(1) Excluding dividend tax where applicable
* The Equity Shares of the Company were sub divided from a face value of Rs 4 per share to a face value of Re 1 per share in the financial year 06-07.

The company is entering into strategic acquisitions and partnerships to accelerate growth and expand their international presence: The company has made its presence in the international markets of U.K, South Africa and U.A.E. While continuing to maintain growth momentum in the current territories, they intend to explore expansion into new markets as well.

Sales Analysis (in Mn)

| Sales Comparison ( Net of excise duty) | FY04 | FY05 | FY06 | FY07 | FY08 |
|---|---|---|---|---|---|
| Keyline B Ltd | | | 1,529.2 | 1,668.4 | 1,639.5 |
| Inecto Mfg Ltd | | | 221.1 | 171.9 | 186.8 |
| Rapidol (P)Ltd | | | - | 251.3 | 406.5 |
| Godrej Global Mideast FZE | | | - | - | 49.1 |
| Godrej Netherlands B.V., Amsterdam | | | - | - | - |
| Godrej Consumer Products (UK) Limited | | | - | - | - |
| Consolidation Adjustments | | | (1,326.3) | (144.5) | (132.2) |
| Total Internation Sales | - | - | 424.0 | 1,947.1 | 2,149.8 |
| % of total Sales | | | 6.1% | 20.4% | 19.5% |
| Total Consolidated Sales | 4,895.8 | 5,626.7 | 6,997.2 | 9,532.3 | 11,025.7 |

Profitability Analysis - Major Subsidiaries

| | | Sales | Sales Growth % | PAT | Pat Growth % |
|---|---|---|---|---|---|
| Keyline Brand | 2008 | 16,395.0 | -1.7% | 1,232.9 | -23.6% |
| | 2007 | 16,684.0 | 9.1% | 1,613.1 | 17.2% |
| | 2006 | 15,292.0 | | 1,375.8 | |
| Inecto Mfg | 2008 | 186.8 | 8.7% | 0.7 | 344.5% |
| | 2007 | 171.9 | -22.3% | 0.2 | -61.9% |
| | 2006 | 221.1 | | 0.4 | |
| Rapidol | 2008 | 406.5 | 61.8% | 46.1 | 58.3% |
| | 2007 | 251.3 | | 29.1 | |

The table below gives a brief synopsis of the standalone and consolidated numbers for the FY08.

| Particulars (Rs Mn) | Standalone | Consolidated |
|---|---|---|
| Revenue (Rs. Mn) | 8,875.9 | 11,025.7 |
| Reported PAT (Rs. Mn) | 1,481.1 | 1,592.4 |
| EPS (Rs.) | 6.6 | 7.1 |
| Operating Margin | 20.8% | 19.5% |
| PBIT Margin | 20.1% | 18.2% |
| PAT Margin | 16.7% | 14.4% |

From the tables above we can conclude that though the sales of the subsidiaries are growing at a good rate, the profits are unable to keep pace. The subsidiaries are able to contribute to the sales revenue of GCPL, but the subsidiaries are unable to contribute to the bottomline of the company.

Profit from subsidiaries to contribute exponentially

The new ventures contribute to the bottomline marginally (Consolidate EPS: 7.05 , Standalone EPS: 6.56). Thereby contributing to a meager 0.49 paise to the EPS. But these ventures are expected to contribute in a major way on gaining maturity.

# Competition

The following are the competitors in the various categories:

- In the soaps category, GCPL brands compete with 'Lux' and 'Lifebuoy'- Hindustan Unilever Limited, 'Nima' – Nirma.
- In the hair colours category, their products compete for market share with 'Black Rose' 'Super Vasmol' and 'L'Oreal'
- Their competitors in shaving cream category are 'Gillette', 'Palmolive', 'Indian Shaving', 'VI john' and 'Old Spice'
- Their talcum powder brands, compete with 'Ponds'- Hindustan Unilever and 'Denim'
- In the liquid detergent category their brand 'Ezee' competes with 'Genteel', 'Safewash- Wipro' and 'Surf Excel-Hindustan Unilever Limited'.

# Key Risks

The company's valuation is presently on a par with that of leading consumer goods companies such as Colgate Palmolive India and Dabur India. The valuation demands a 20 per cent-plus growth rate over the next few years. Whether the company can deliver these will depend mainly on two factors. One, with a much narrower product portfolio than companies such as Dabur or Marico, Godrej Consumer will depend heavily on just its soaps and hair colour business for growth. Both these segments are observers of intense competition with several new entrants.

Second, it will also have to build breadth within each category to widen its portfolio of brands by introducing products at various price points. The company seems reasonably equipped to do this, with expanding profit margins and healthy operational cash flows. However, investors will have to watch out for slowing growth rates or setbacks in market share, as these will be the key triggers to exit the stock.

Increase in cost of raw materials

Vegetable oil is a key ingredient for making soaps. In case of any rise in prices, cost of production would increase, thereby reducing the margins.

Weakening of the rupee

India is largely dependent on imports for vegetable oils. Weakening of the rupee against the US dollar or Euro could increase the company's cost of production.

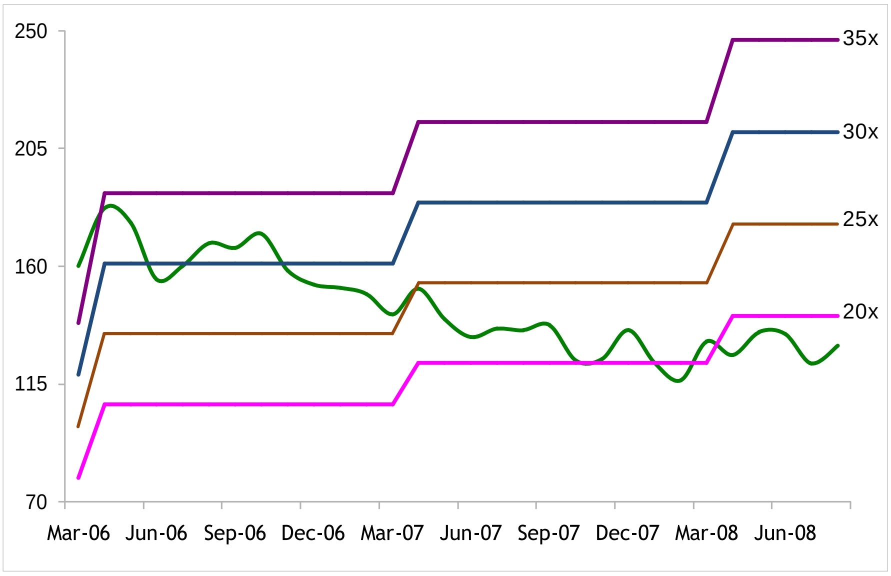
At the current market price of Rs. 124.10, the stock trades at 17.2x of FY09E earnings and 13.5x of FY10E earnings (on expanded equities post rights). We have valued the company at 20x its FY2010E consolidated earnings and recommend a BUY with a price target of Rs. 184, an upside of 48% from the current price.

Although GCPL is not directly comparable to other players (because of different product offerings), it has the highest margins among the peer groups in the FMCG industry. The growth in sales has been very impressive in the last two years and it is trading at a low PE ratio when compared to other players. Therefore we recommend a strong buy at current levels with a long term visibility, to participate into the expanding horizons of the Indian conglomerate.

| Description | P/E | CMP | EPS | Sales (Rs. Lakhs) | M Cap/Sales(x) |
|---|---|---|---|---|---|
| Asian Paints | 27.7 | 1202.8 | 43.4 | 440433.0 | 2.6 |
| Dabur | 24.2 | 92.6 | 3.8 | 236107.0 | 3.4 |
| Marico | 21.0 | 58.4 | 2.8 | 190669.0 | 0.2 |
| GCPL | 17.6 | 124.1 | 7.1 | 110257.0 | 2.5 |
| Pidilite | 20.4 | 138.3 | 6.8 | 170820.0 | 2.0 |

*Source: NSE*

Historic PE and trading Band



| Earnings Statement | | | | | | | |
|---|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY04 | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Total Revenues | 4,916.6 | 5,626.7 | 6,997.2 | 9,532.3 | 11,025.7 | 13,045.9 | 15,453.8 |
| - Growth (%) | | 14.4% | 24.4% | 36.2% | 15.7% | 18.3% | 18.5% |
| Total Expenditure | 4,053.8 | 4,622.1 | 5,570.0 | 7,735.4 | 8,880.7 | 10516.3 | 12302.8 |
| Operating Profit | 862.8 | 1,004.6 | 1,427.2 | 1,796.9 | 2,145.0 | 2,529.6 | 3,151.0 |
| Other Income | 21.3 | 64.1 | 73.1 | 26.5 | 40.3 | 54.4 | 64.4 |
| EBITDA | 884.2 | 1,068.7 | 1,500.3 | 1,823.4 | 2,185.3 | 2,584.0 | 3,215.5 |
| Depreciation | 94.0 | 106.6 | 114.7 | 142.1 | 181.7 | 307.0 | 389.7 |
| EBIT | 790.2 | 962.2 | 1,385.6 | 1,681.3 | 2,003.6 | 2,276.9 | 2,825.8 |
| Interest | 24.3 | 24.6 | 64.7 | 96.3 | 128.7 | 81.8 | 27.8 |
| PBT | 765.9 | 937.6 | 1,320.8 | 1,585.0 | 1,874.9 | 2,195.2 | 2,798.0 |
| Tax | 117.7 | 41.6 | 107.8 | 195.4 | 282.5 | 329.3 | 419.7 |
| PAT Before EI | 648.3 | 895.9 | 1,213.0 | 1,389.7 | 1,592.4 | 1,865.9 | 2,378.3 |
| - Growth (%) | | 38.2% | 35.4% | 14.6% | 14.6% | 17.2% | 27.5% |
| Extra-ordinary Items | 0.0 | 0.0 | 0.0 | 50.6 | 0.0 | 0.0 | 0.0 |
| Reported PAT | 648.3 | 895.9 | 1,213.0 | 1,440.3 | 1,592.4 | 1,865.9 | 2,378.3 |

| Ratio Analysis | | | | | | | |
|---|---|---|---|---|---|---|---|
| Particulars | FY04 | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| OPM (%) | 17.5% | 17.9% | 20.4% | 18.9% | 19.5% | 19.4% | 20.4% |
| EBITDA (%) | 18.0% | 19.0% | 21.4% | 19.1% | 19.8% | 19.8% | 20.8% |
| PBIT (%) | 16.1% | 17.1% | 19.8% | 17.6% | 18.2% | 17.5% | 18.3% |
| PAT (%) | 13.2% | 15.9% | 17.3% | 14.6% | 14.4% | 14.3% | 15.4% |
| Interest Cover (x) | 32.6 | 39.1 | 21.4 | 17.5 | 15.6 | 27.8 | 101.8 |
| EPS (Rs.) | 2.9 | 4.0 | 5.4 | 6.2 | 7.1 | 7.2 | 9.2 |
| P/E (x) | 43.5 | 31.4 | 23.1 | 20.2 | 17.6 | 17.2 | 13.5 |
| P/BV (x) | 66.6 | 56.4 | 35.6 | 23.0 | 16.6 | 10.0 | 6.2 |
| BVPS (Rs.) | 1.9 | 2.2 | 3.5 | 5.4 | 7.5 | 12.4 | 20.1 |
| Market Cap (Rs. Mn.) | 28,226.4 | 28,098.5 | 28,027.2 | 28,027.2 | 28,027.2 | 32,031.1 | 32,031.1 |
| M Cap/Sales (x) | 5.7 | 5.0 | 4.0 | 2.9 | 2.5 | 2.5 | 2.1 |
| EV (Rs. Mn.) | 28,329.0 | 28,070.1 | 28,441.0 | 29,288.3 | 29,472.3 | 31,609.8 | 29,808.4 |
| EV/EBITDA (x) | 32.0 | 26.3 | 19.0 | 16.1 | 13.5 | 12.2 | 9.3 |
| EV/Sales (x) | 5.8 | 5.0 | 4.1 | 3.1 | 2.7 | 2.4 | 1.9 |
| ROCE (%) | 118.7% | 171.8% | 94.0% | 56.9% | 56.3% | 53.8% | 51.0% |
| RONW (%) | 153.0% | 179.7% | 154.2% | 113.9% | 94.4% | 58.3% | 45.8% |
| Debt/Equity Ratio (x) | 0.6 | 0.1 | 0.9 | 1.4 | 1.1 | 0.3 | 0.1 |
| Inventory T/o Days | 36.5 | 47.9 | 52.4 | 51.8 | 63.4 | 63.0 | 63.0 |
| Debtors T/o Days | 9.8 | 3.4 | 15.8 | 18.5 | 16.9 | 17.0 | 17.0 |
| Advances T/o Days | 6.1 | 9.8 | 7.4 | 17.8 | 22.1 | 18.7 | 15.8 |
| Creditors T/o Days | 81.9 | 86.3 | 93.2 | 96.5 | 96.2 | 96.0 | 96.0 |
| Working Cap T/o Days | (22.1) | (24.3) | (8.9) | 6.1 | 9.7 | 15.6 | 37.1 |
| Fixed Assets T/o (Gross) | 2.9 | 3.1 | 4.0 | 3.5 | 3.8 | 3.5 | 4.2 |
| DPS (Rs.) | 2.3 | 3.0 | 3.5 | 3.8 | 4.2 | 4.3 | 5.5 |
| Dividend Payout (%) | 79.2% | 75.8% | 65.2% | 60.9% | 60.0% | 60.0% | 60.0% |
| Dividend Yield (%) | 1.8% | 2.4% | 2.8% | 3.0% | 3.4% | 3.5% | 4.5% |

| Balance Sheet | | | | | | | |
|---|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY04 | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Equity Capital | 227.4 | 226.4 | 225.8 | 225.8 | 225.8 | 258.1 | 258.1 |
| Reserves | 196.2 | 272.1 | 561.0 | 994.1 | 1,489.8 | 2,968.5 | 4,959.7 |
| Shareholders Funds | 423.6 | 498.6 | 786.8 | 1,220.0 | 1,715.6 | 3,226.6 | 5,217.8 |
| Borrowed Funds | 242.2 | 61.3 | 687.2 | 1,736.1 | 1,871.0 | 1,031.0 | 350.0 |
| Deferred Tax Liability | 76.0 | 79.4 | 65.7 | 79.8 | 89.1 | 89.1 | 89.1 |
| Total Liabilities | 741.8 | 639.3 | 1,539.7 | 3,035.9 | 3,675.7 | 4,346.7 | 5,656.9 |
| Fixed Assets | 1,040.0 | 1,014.1 | 849.6 | 1,992.1 | 2,399.1 | 2,136.3 | 2,431.6 |
| Goodwill | 0.0 | 0.0 | 851.4 | 885.7 | 956.0 | 956.0 | 956.0 |
| Investments | 0.0 | 0.0 | 10.1 | 0.1 | 0.1 | 669.1 | 669.1 |
| Current Assets | | | | | | | |
| Inventory | 491.7 | 738.1 | 1,004.7 | 1,352.3 | 1,915.6 | 2,251.8 | 2,667.4 |
| Sundry Debtors | 132.5 | 51.8 | 303.3 | 483.2 | 509.6 | 607.6 | 719.8 |
| Loans & Advances | 82.8 | 151.6 | 142.8 | 464.8 | 667.7 | 667.7 | 667.7 |
| Cash & Bank Balance | 139.6 | 89.7 | 263.4 | 474.9 | 425.9 | 783.2 | 1,903.6 |
| Other Current Assets | | | | | | | |
| Current Liabilities | | | | | | | |
| Sundry Creditors | 1,103.7 | 1,329.8 | 1,787.3 | 2,520.0 | 2,904.5 | 3,431.2 | 4,064.6 |
| Provisions | 41.2 | 76.1 | 98.1 | 97.3 | 322.4 | 322.4 | 322.4 |
| Net Current Assets | (298.2) | (374.8) | (171.3) | 158.1 | 291.8 | 556.6 | 1,571.5 |
| Miscellaneous Expenditure | 0.0 | 0.0 | 0.0 | 0.0 | 28.7 | 28.7 | 28.7 |
| Total Assets | 741.8 | 639.3 | 1,539.7 | 3,035.9 | 3,675.7 | 4,346.7 | 5,656.9 |

| Cash Flow | | | | | | | |
|---|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY04 | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Opening Cash & Bank | 71.5 | 139.6 | 89.7 | 263.4 | 474.9 | 425.9 | 783.2 |
| Profit After Tax | 648.3 | 895.9 | 1,213.0 | 1,389.7 | 1,592.4 | 1,865.9 | 2,378.3 |
| Invt Income | (21.3) | (64.1) | (73.1) | (26.5) | (40.3) | (54.4) | (64.4) |
| Interest Paid | 24.3 | 24.6 | 64.7 | 96.3 | 128.7 | 81.8 | 27.8 |
| Miscellaneous Exp W/Off | 0.0 | 0.0 | 0.0 | 0.0 | (28.7) | (0.0) | 0.0 |
| Depreciation | 94.0 | 106.6 | 114.7 | 142.1 | 181.7 | 307.0 | 389.7 |
| Deferred Taxation | 29.5 | 3.4 | (13.8) | 13.1 | 9.2 | 0.0 | 0.0 |
| Others | 37.8 | (7.1) | 110.2 | (10.1) | (67.4) | (6,698.3) | 4,300.0 |
| Change in Working Cap | 71.1 | 26.7 | (29.8) | (117.8) | (182.8) | 92.5 | 105.6 |
| CF - Operating Activities | 883.6 | 985.9 | 1,386.0 | 1,486.7 | 1,592.8 | (4,405.5) | 7,136.9 |
| Change in Fixed Assets | (239.5) | (75.6) | (36.0) | (1,255.9) | (555.4) | 3,652.6 | (3,696.8) |
| Change in Goodwill | 0.0 | 0.0 | (851.4) | (34.3) | (34.3) | (34.3) | (34.3) |
| Change in Investments | 40.0 | 0.0 | (10.1) | 10.0 | 0.0 | (669.0) | 0.0 |
| Investment Income | 21.3 | 64.1 | 73.1 | 26.5 | 40.3 | 54.4 | 64.4 |
| CF - Investing Activities | (178.2) | (11.5) | (824.4) | (1,253.7) | (549.4) | 3,003.7 | (3,666.7) |
| Increase in Equity | (97.7) | (48.4) | (47.7) | 0.0 | 0.0 | 3,968.4 | 0.0 |
| Changes in Borrowings | 63.7 | (180.8) | 625.9 | 1,048.9 | 134.9 | (840.0) | (681.0) |
| Interest Paid | (24.3) | (24.6) | (64.7) | (96.3) | (128.7) | (81.8) | (27.8) |
| Dividend Paid | (578.9) | (770.5) | (901.3) | (974.1) | (1,098.8) | (1,287.5) | (1,641.0) |
| CF - Financing Activities | (637.2) | (1,024.4) | (387.9) | (21.5) | (1,092.6) | 1,759.2 | (2,349.8) |
| Net Change in Cash | 68.2 | (49.9) | 173.8 | 211.5 | (49.1) | 357.3 | 1,120.4 |
| Closing Cash & Bank Bal | 139.6 | 89.7 | 263.4 | 474.9 | 425.9 | 783.2 | 1,903.6 |

# Pidilite Industries Ltd.

CMP Rs. 138.25
Target Rs. 176.00

Initiating Coverage
BUY

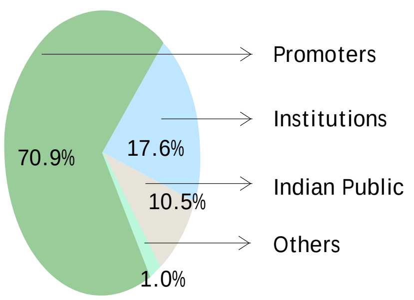
## Stock Data

| | |
|---|---|
| Bloomberg | : PIDI.IN |
| Reuters | : PIDI.BO |
| BSE Code | : 500331 |
| NSE Code | : PIDITIND |
| BSE Group | : B |

## Stock Codes

| | |
|---|---|
| Benchmark | : BSE 500 |
| 52 W High/Low | : 220.0/125.0 |
| Float | : 29.12 Mn |
| Mkt Cap | : Rs. 38,962 Mn |
| Face Value | : Rs. 1.0 |

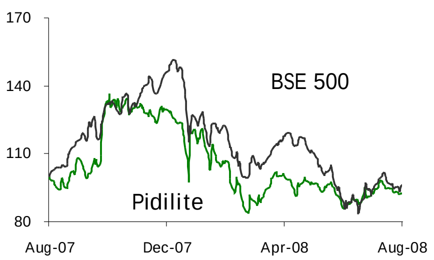
## Shareholding Pattern (as on June 08)




## Stock Returns

| | 1 Mth | 3 Mths | 6 Mths |
|---|---|---|---|
| Pidilite | -0.24 | -4.57 | -13.57 |
| BSE 500 | 1.91 | -13.03 | -20.77 |

## Price Comparison




Deepti Singh - deepti@ppfas.com

Pidilite is a leader in the field of consumer adhesives and sealants. Promoted by the Parekh family, Pidilite has several achievements to its credit. Its flagship brand – Fevicol – is a prime example of branding a commodity (adhesive), such that it is able to command a price premium over competition. Economic Times, (issue dated 11th June 2008), ranked Fevicol as 20th amongst the top trusted brands for the year which was ranked at 24th in year 2007.

### Business Segment

Company's Consumer & Bazaar segment (branded business) accounts for around 72% while the rest comes from Speciality Industrial chemicals & others (commodity business).

### R&D

Its strong R&D base has helped the company to develop new products and categories cost effectively and become a dominant player by introducing new products at regular intervals. This is evident from the fact that nearly 20% of its revenue comes from new products introduced by it in the last four years. As a part of its growth strategy, Pidilite has over the past few years acquired M-Seal, Mr. Fixit, Ranipal & Steelgrip and rejuvenated them. Going forward, we believe the new products and acquired brands to be the key growth driver for the company.

### Advertising Initiatives

Smart and effective advertising created by O&M over the years for Fevicol has engraved the brand firmly in the mind of the consumers. The efforts the management has put in buliding relations with the carpenters have also paid well and Fevicol has become their choice brand despite higher price. Adhesives and sealants continue to have major share in the products portfolio of the company but continuous introduction of new products coupled with related acquisitions have restricted the share of the flagship brand Fevicol and its variants to ~33%, though their share in profits is likely to be slightly higher.

### No major Competition

Another factor benefiting the company is that its main competitor in white adhesives (Jubiliant Organosys with Jivanjor brand) has reported loss of interest in the business and has reportedly put it on the block. With this Pidilite has gained status of near monopoly in the organized sector in its largest and most profitable product range. Also, there is no single company that competes with Pidilite in all its segments though some of its products compete with Jubiliant, Kores, Camlin, paint companies and a large number of small and unorganized players in single segments. Thus, there is no true peer comparison possible for Pidilite.

Consistent Growth

Pidilite has achieved consistent sales and earnings growth for the last 10 years, with ROCE in excess of 20%. In the last 4 years total income has grown at a CAGR of 30.29%, operating profit has grown at a CAGR of 25% and bottomline has grown at a CAGR of 32%.

This clearly shows a trend of gradually increasing margins and should continue in the foreseeable future as well. This has been possible due to their strong understanding of the Indian market, management wisdom and more importantly the customers. As a result, the products are suited not just for Indian environmental conditions, but also compare favourably to the international norms for performance and quality. The management has also stuck to their core business of adhesives, sealants and chemicals.

Pidilite has carved a niche for itself in direct consumer products. The company has built a strong franchise with carpenters, electricians and architects, which helps, as these people influence choice of products purchased, more than the consumers. The end user demands quality products in areas such as waterproofing and bonding. Most products in this segment are priced low but their performance is critical. Consumers are therefore willing to pay a premium over unheard brands. As a result of this, the margins in the consumer and bazaar segment are comparable to most leading FMCG categories.

**Global footprint through overseas investments**

Pidilite is expanding its global precence investing significantly in the international markets of Africa, Middle East, Indonesia, Malaysia and the US, viewing the rich market potential of the regions. It has recently begun greenfield projects in Bangladesh, UAE and Egypt. It gives Pidilite the opportunity to leverage its distribution network and widen the market for its products.

**New product development are strategies to de-risk the portfolio and innovating success**

Pidilite typically keeps up a steady stream of new product launches/product extensions. We believe the company is consistently working towards de-risking the portfolio through such new product launches. One of the company's key strength has been its comprehensive range of products (both in consumer and industrial segments) catering to a wide variety of consumers from retail & household consumers to industrial users. In order to increase its penetration, the company has introduced products even in the lower price segment.

Pidilite has a strong R&D division, which creates 4-5 new products each year and tailors industrial products to customer specifications. Thus constant product innovation has been the key to the company's phenomenal success. Moreover it has also helped the company in building up strong product portfolio & reducing its dependence on any single product or brand.

**Entry into food segment with “Chikkers”**

Pidilite has already entered the packaged food market with the launch of branded chikki known as 'Chikkers'. The company has launched this product in the North Indian markets. Though the foods segments contribution to revenues is negligible and the management admits to have diverted its attention to other areas, yet the in the event of strong success with the Chikkers venture, foods as a segment would become an exciting area to expand into.

**Industrial Chemicals Business is not as negative as perceived**

Pidlite generates more than 70% of its revenue from higher margin branded Consumer and Bazaar products and roughly 20% of its turnover from industrial chemicals such as organic pigments, industrial resins and industrial adhesives. As these products have lower margins and ROCE it is often perceived to be a negative for the company. The management has publicly committed to selling this business to buyers at a reasonable price.

However, the industrial chemicals business is profitable and though ROCE is far lower than that of the consumer products division, it is far higher than the cost of capital. The business continues to add to the bottomline and economic value of the company.

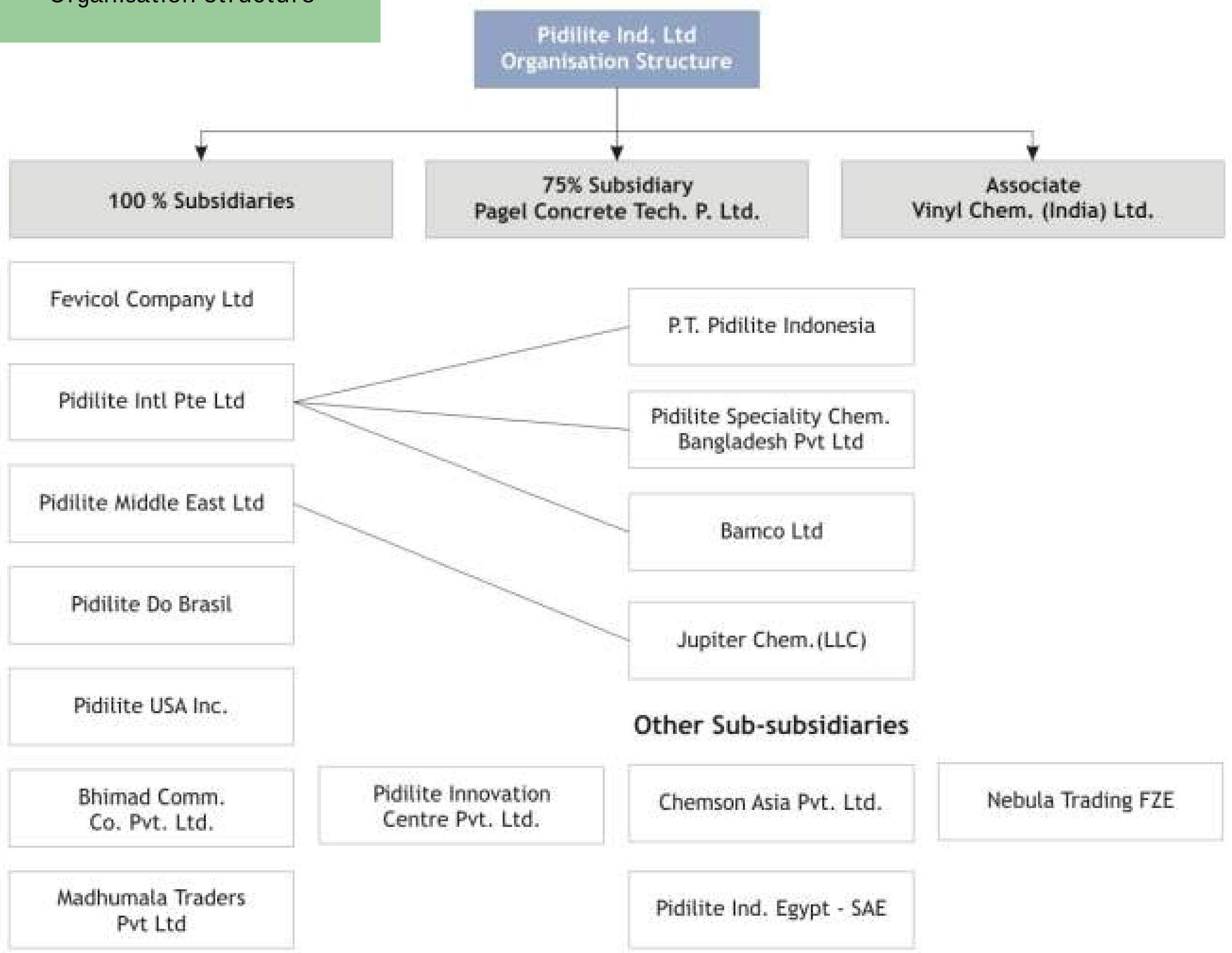
'Hobby Ideas'

Pidilite has entered the business of selling hobby and craft materials through its chain of branded stores, 'Hobby Ideas'. Pidilite currently operates six retail stores across Mumbai, Ahmedabad and Surat. It is positioned as a one-stop shop for all hobby products. There are over 1,500 products that support 30 hobbies. The shop educates the customers about the entire gamut of hobby and craft choices prevalent in the country and globally. In this scenario, Hobby Ideas gives Pidilite a vehicle to sell many of its products under one roof. Almost 50 per cent of the hobbies in the store require Pidilite products as basic raw materials and are sold as part of the kits. For example, the fabric painting hobby kit contains tubes of Fevicryl and other kits have Fevicol tubes.

Ability to sustain FMCG margins and ROCE

Pidilite is equipped with a diverse product range, of over 700 products, established brands and a strong distribution network spread throughout the country. The aspect that works in Pidilite's favour is that its portfolio is stacked with a formidable array of brands. The principal advantage of such a product basket is that when the company is confronted with a situation of rising input costs, it has the ability to pass on such rises — in the form of price hikes — to the end consumer without an adverse impact on both market share and margins.

## Organisation Structure




## Subsidiary Performance

Profit for the year as on Mar 08 is 188 crs on standalone basis whereas it is 172 crs on the consolidated basis. The subsidiaries are currently loss making but in future a turnaround is expected. On a standalone basis, sales as on Mar 08 is 1535.30 crs but 1708.237 crs on a consolidated basis. The PAT margin is 12.6 % on standalone basis versus 10.1% on consolidated basis. If the subsidiaries are able to perform like its parent then we are in position to expect positive surprises.

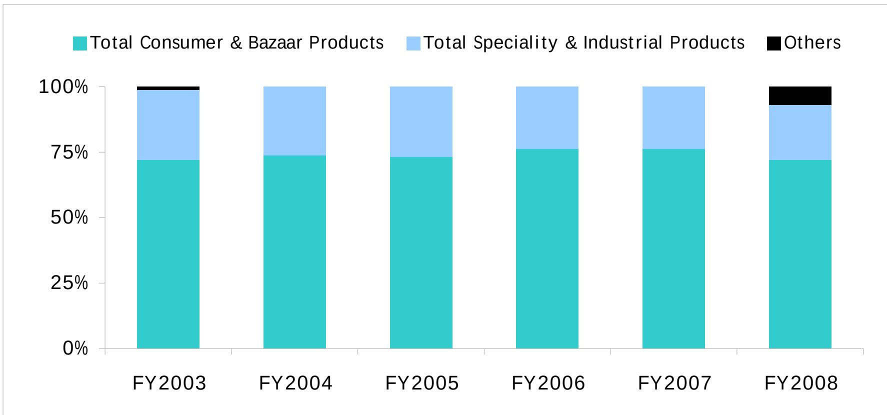
The table below gives a brief synopsis of the standalone and consolidated numbers for the FY08.

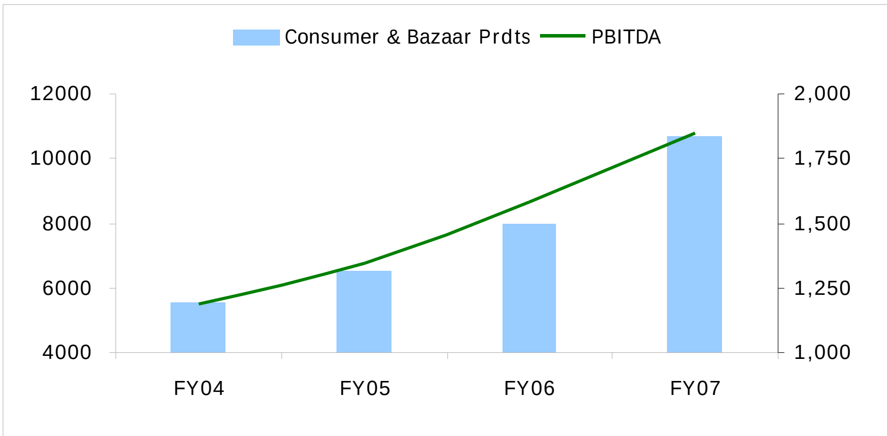
| Particulars (Rs Mn) | Standalone | Consolidated |
|---|---|---|
| Revenue (Rs. Mn) | 15,353.0 | 17,082.0 |
| Reported PAT (Rs. Mn) | 1,883.0 | 1,729.8 |
| EPS (Rs.) | 6.9 | 6.1 |
| Operating Margin | 16.9% | 14.1% |
| PBIT Margin | 16.0% | 13.3% |
| PAT Margin | 12.6% | 10.1% |

Strategy Revamp : Focus on bazaar segment

The following chart shows the changing business profile of the company over the past few years. Its two main operating segments include consumer and bazaar products, which account for about 75 per cent of sales, with the rest coming from industrial products. Pidilite may therefore now want to milk its consumer segment to the hilt, as both the profit margins and return on capital employed on its industrial business are dwindling. The impact of changing business profile of Pidilite is evident from the improvement in its earnings and margins expansion. Operating margins have slowly but steadily been moving up with increased contribution from the branded business. The following chart shows the impact of changing business profile on the operating margin.

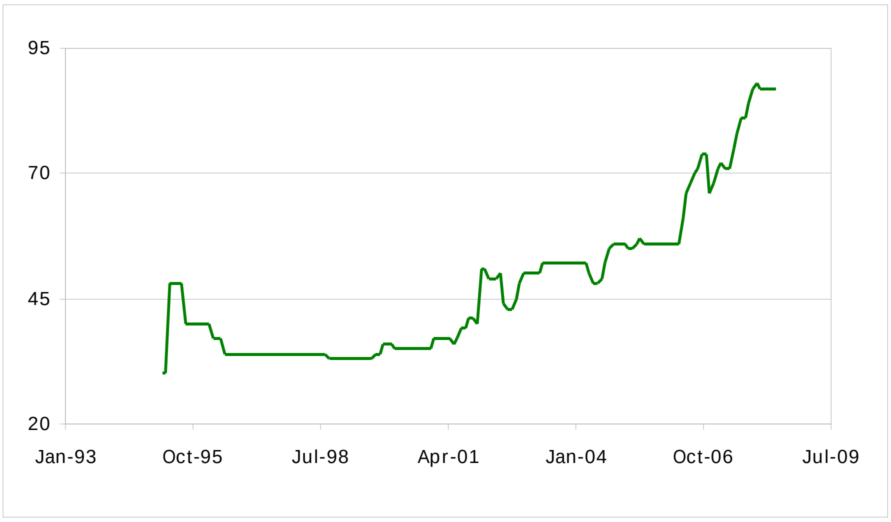
Sales Break up



Raw material costs play a crucial role in determining the health of margins, as they account for 51 per cent of gross sales on a consolidated basis in this case. A key input for Pidilite is vinyl acetate monomer (VAM), a derivative of crude oil. Rising prices of crude oil have a cascading effect on VAM, which, in turn, hurts margins. As the main raw material for the company is Vinyl Acetate Monomer (VAM), a petroproduct, it's pricing has been volatile and has from time to time resulted in margin pressures leading to the belief that the company is selling a commodity product. However, though volatile raw material prices cause short term swings in financial performance the long term pricing of the company's products is always adjusted for raw material prices.

Vam prices

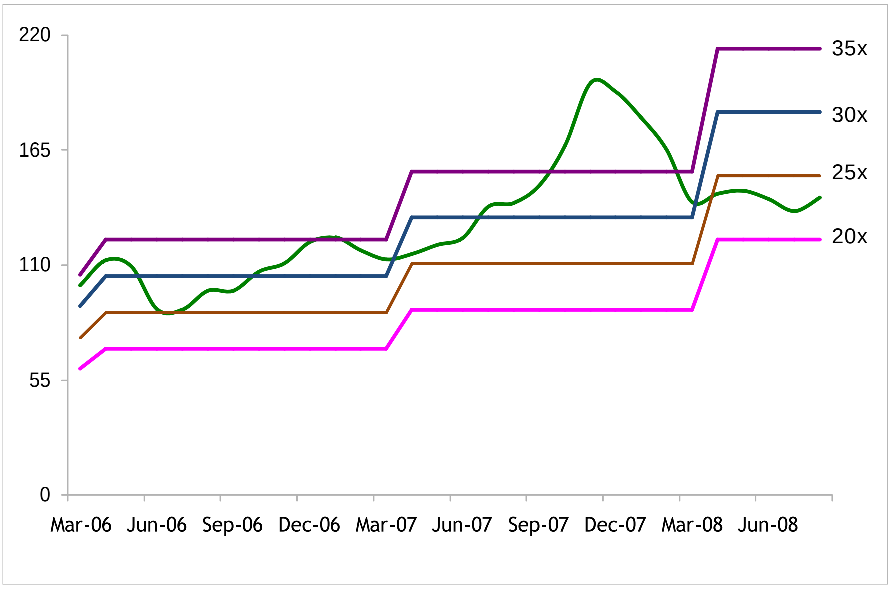



Debt would be the another area of concern that Pidilite has. However, it may be noted that its interest cover ratio has reduced dramatically in FY 07 and there was even further reduction in FY 08.

The Great Warren Buffet says it always pays off to invest in companies that have performed consistently well in the past. On the same grounds we have identified Pidilite industries which we feel would give a great value for shareholders money for years to come. Its dominance in the profitable and price-insensitive adhesive business, portfolio of branded products, early-bird entry into emerging segments and inorganic expansion make it a good growth stock for long-term investors. Moreover, the company is currently trading at attractive valuations. Thus given the current market situation, the stock is a good defensive bet, considering its price- and demand inelastic product portfolio.

For FY09E and FY10E, we expect Net Sales to grow by 26.57% & 26.35% to Rs.2161.99 crs & Rs.2731.622 crs respectively. Net profit for the period is expected to grow by 13.60% YoY & 27% YoY to Rs.196.5 Crs and Rs. 249.6 Crs respectively. At the current market price of Rs.138.25, the stock appears a very strong value pick at 15.7x FY10 earnings. We are initiating our coverage on the stock with a 'BUY' rating and a price target of Rs. 176.0, an upside of 27% from the current levels.

PE Band



| Earnings Statement | | | | | | |
|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Total Revenues | 7,723.3 | 9,170.0 | 12,481.7 | 17,082.0 | 21,619.9 | 27,316.2 |
| - Growth (%) | 18.1% | 18.7% | 36.1% | 36.9% | 26.6% | 26.3% |
| Total Expenditure | 6,480.7 | 7,766.1 | 10,820.2 | 14,670.8 | 18,549.8 | 23,437.3 |
| Operating Profit | 1,242.6 | 1,403.8 | 1,661.5 | 2,411.2 | 3,070.0 | 3,878.9 |
| Other Income | 100.8 | 176.2 | 188.7 | 314.6 | 398.1 | 503.0 |
| EBITDA | 1,343.4 | 1,580.1 | 1,850.2 | 2,725.8 | 3,468.2 | 4,381.9 |
| Depreciation | 270.1 | 277.8 | 327.7 | 459.0 | 674.8 | 884.8 |
| EBIT | 1,073.3 | 1,302.3 | 1,522.6 | 2,266.8 | 2,793.3 | 3,497.1 |
| Interest | 16.9 | 15.4 | 66.4 | 190.0 | 190.0 | 190.0 |
| PBT | 1,056.4 | 1,286.9 | 1,456.2 | 2,076.8 | 2,603.3 | 3,307.1 |
| Tax | 296.0 | 405.9 | 340.4 | 358.0 | 650.8 | 826.8 |
| PAT Before EI | 760.4 | 881.0 | 1,115.8 | 1,718.8 | 1,952.5 | 2,480.3 |
| - Growth (%) | 23.8% | 15.9% | 26.6% | 54.0% | 13.6% | 27.0% |
| Extra-ordinary Items: | | | | | | |
| Reported PAT before Assoc. and MI | 760.4 | 881.0 | 1,115.8 | 1,718.8 | 1,952.5 | 2,480.3 |
| Share of Profit/(Loss) | (9.4) | (6.3) | 1.0 | 9.0 | 10.2 | 13.0 |
| Profit before MI | 751.0 | 874.8 | 1,116.7 | 1,727.8 | 1,962.7 | 2,493.3 |
| Minority Interest | 3.3 | 2.8 | 0.7 | 2.0 | 2.3 | 2.9 |
| Profit after MI | 754.3 | 877.6 | 1,117.5 | 1,729.8 | 1,965.0 | 2,496.2 |
| - Growth (%) | 23.8% | 16.3% | 27.3% | 54.8% | 13.6% | 27.0% |

| Ratio Analysis | | | | | | |
|---|---|---|---|---|---|---|
| Particulars | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| OPM (%) | 16.1% | 15.3% | 13.3% | 14.1% | 14.2% | 14.2% |
| EBITDA (%) | 17.4% | 17.2% | 14.8% | 16.0% | 16.0% | 16.0% |
| PBIT (%) | 13.9% | 14.2% | 12.2% | 13.3% | 12.9% | 12.8% |
| PAT (%) | 9.8% | 9.6% | 8.9% | 10.1% | 9.0% | 9.1% |
| Interest Cover (x) | 63.4 | 84.5 | 22.9 | 11.9 | 14.7 | 18.4 |
| EPS (Rs.) | 3.0 | 3.5 | 4.4 | 6.1 | 6.9 | 8.8 |
| P/E (x) | 45.9 | 39.6 | 31.3 | 22.7 | 20.0 | 15.7 |
| P/BV (x) | 9.7 | 8.5 | 7.3 | 6.3 | 5.1 | 4.0 |
| BVPS (Rs.) | 14.3 | 16.4 | 19.0 | 22.0 | 26.9 | 34.2 |
| Market Cap (Rs. Mn.) | 34,894.3 | 34,894.3 | 34,894.3 | 38,961.6 | 38,960.0 | 38,960.0 |
| M Cap/Sales (x) | 4.5 | 3.8 | 2.8 | 2.3 | 1.8 | 1.4 |
| EV (Rs. Mn.) | 35,193.8 | 35,136.7 | 35,802.8 | 42,474.3 | 40,889.1 | 41,932.8 |
| EV/EBITDA (x) | 26.2 | 22.2 | 19.4 | 15.6 | 11.8 | 9.6 |
| EV/Sales (x) | 4.6 | 3.8 | 2.9 | 2.5 | 1.9 | 1.5 |
| ROCE (%) | 25.3% | 27.8% | 24.4% | 19.8% | 21.7% | 23.5% |
| RONW (%) | 21.1% | 21.3% | 23.2% | 27.7% | 25.7% | 25.8% |
| Debt/Equity Ratio (x) | 0.2 | 0.1 | 0.3 | 0.8 | 0.7 | 0.5 |
| Inventory T/o Days | 61.6 | 62.0 | 64.7 | 63.9 | 64.0 | 64.0 |
| Debtors T/o Days | 51.9 | 45.1 | 46.2 | 50.8 | 46.0 | 46.0 |
| Advances T/o Days | 15.7 | 6.4 | 14.9 | 19.8 | 15.7 | 12.4 |
| Creditors T/o Days | 39.5 | 41.0 | 47.9 | 47.3 | 48.0 | 48.0 |
| Working Cap T/o Days | 82.4 | 70.8 | 75.3 | 110.9 | 125.9 | 98.7 |
| Fixed Assets T/o (Gross) | 2.0 | 1.9 | 2.2 | 2.1 | 2.2 | 2.2 |
| DPS (Rs.) | 1.0 | 1.3 | 1.5 | 1.6 | 1.3 | 1.3 |
| Dividend Payout (%) | 33.2% | 35.8% | 33.9% | 25.8% | 19.4% | 15.3% |
| Dividend Yield (%) | 0.7% | 0.9% | 1.1% | 1.1% | 1.0% | 1.0% |

| Balance Sheet | | | | | | |
|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Equity Capital | 252.4 | 252.4 | 252.4 | 281.8 | 281.8 | 281.8 |
| Reserves | 3,362.2 | 3,880.5 | 4,553.5 | 5,915.8 | 7,312.1 | 9,348.3 |
| Shareholders Funds | 3,614.6 | 4,132.9 | 4,805.9 | 6,197.6 | 7,593.9 | 9,630.1 |
| Borrowed Funds | 627.2 | 563.2 | 1,449.1 | 5,263.6 | 5,263.6 | 5,263.6 |
| Deferred Tax Liability | 287.9 | 304.9 | 335.4 | 416.1 | 416.1 | 416.1 |
| Minority Interest | 5.5 | 14.7 | 15.2 | 12.7 | 15.0 | 17.9 |
| Total Liabilities | 4,535.2 | 5,015.6 | 6,605.6 | 11,890.0 | 13,288.5 | 15,327.6 |
| Fixed Assets | 2,598.3 | 3,072.4 | 3,868.8 | 6,668.1 | 5,795.8 | 7,911.0 |
| Investments | 186.2 | 159.6 | 159.2 | 32.4 | 32.4 | 32.4 |
| Current Assets | | | | | | |
| Inventory | 1,303.6 | 1,558.1 | 2,213.7 | 2,988.3 | 3,790.9 | 4,789.7 |
| Sundry Debtors | 1,097.6 | 1,133.4 | 1,579.9 | 2,377.4 | 2,724.7 | 3,442.6 |
| Loans & Advances | 332.5 | 330.0 | 509.5 | 928.0 | 930.0 | 930.0 |
| Cash & Bank Balance | 141.6 | 161.2 | 381.4 | 1,718.5 | 3,302.0 | 2,258.4 |
| Other Current Assets | 22.2 | 23.1 | 21.7 | 0.0 | 0.0 | 0.0 |
| Current Liabilities | | | | | | |
| Sundry Creditors | 835.7 | 1,028.8 | 1,637.9 | 2,212.1 | 2,843.2 | 3,592.3 |
| Provisions | 318.5 | 398.5 | 493.4 | 610.7 | 444.1 | 444.1 |
| Net Current Assets | 1,743.2 | 1,778.3 | 2,574.9 | 5,189.4 | 7,460.3 | 7,384.3 |
| Miscellaneous Expenditure | 7.6 | 5.2 | 2.7 | 0.3 | | |
| | | | | | | |
| Total Assets | 4,535.2 | 5,015.6 | 6,605.6 | 11,890.0 | 13,288.5 | 15,327.6 |

| Cash Flow | | | | | | |
|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Opening Cash & Bank | 75.1 | 141.6 | 161.2 | 381.4 | 1,718.5 | 3,302.0 |
| Profit After Tax | 760.4 | 881.0 | 1,115.8 | 1,718.8 | 1,952.5 | 2,480.3 |
| Invt Income | (100.8) | (176.2) | (188.7) | (314.6) | (398.1) | (503.0) |
| Interest Paid | 16.9 | 15.4 | 66.4 | 190.0 | 190.0 | 190.0 |
| Miscellaneous Exp W/Off | 2.4 | 2.3 | 2.5 | 2.4 | 0.3 | 0.0 |
| Depreciation | 270.1 | 277.8 | 327.7 | 459.0 | 674.8 | 884.8 |
| Deferred Taxation | (13.0) | 17.0 | 30.5 | 0.0 | 0.0 | 0.0 |
| Others | (25.4) | (145.0) | 143.9 | 846.1 | (110.2) | (2,369.1) |
| Change in Working Cap | (31.7) | 153.3 | (745.2) | (1,405.5) | (687.4) | 1,404.4 |
| CF - Operating Activities | 879.0 | 1,025.6 | 752.9 | 1,496.2 | 1,621.9 | 2,087.4 |
| Change in Fixed Assets | (678.3) | (769.6) | (1,098.4) | (3,735.6) | 197.6 | (3,000.0) |
| Change in Investments | 5.3 | 26.5 | 0.4 | 126.9 | 0.0 | 0.0 |
| Investment Income | 100.8 | 176.2 | 188.7 | 314.6 | 398.1 | 503.0 |
| CF - Investing Activities | (572.2) | (566.8) | (909.3) | (3,294.2) | 595.8 | (2,497.0) |
| Increase in Equity | 0.0 | 0.0 | 0.0 | 28.8 | 0.0 | 0.0 |
| Changes in Borrowings | 64.9 | (64.0) | 885.9 | 3,814.4 | 0.0 | 0.0 |
| Interest Paid | (16.9) | (15.4) | (66.4) | (190.0) | (190.0) | (190.0) |
| Dividend Paid | (288.3) | (359.8) | (442.9) | (518.1) | (444.1) | (444.1) |
| CF - Financing Activities | (240.3) | (439.2) | 376.6 | 3,135.1 | (634.1) | (634.1) |
| Net Change in Cash | 66.5 | 19.6 | 220.2 | 1,337.1 | 1,583.5 | (1,043.7) |
| Closing Cash & Bank Bal | 141.6 | 161.2 | 381.4 | 1,718.5 | 3,302.0 | 2,258.4 |

There's only one right way©

# Marico Industries Ltd.

CMP Rs. 58.2
Target Rs. 82.0

Initiating Coverage

BUY

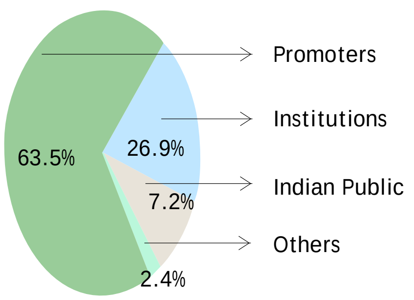
### Stock Data

| | |
|---|---|
| Bloomberg | : MRCO.IN |
| Reuters | : MRCO.BO |
| BSE Code | : 531642 |
| NSE Code | : MARICO |
| BSE Group | : A |

### Stock Codes

| | |
|---|---|
| Benchmark | : BSE FMCG |
| 52 W High/Low | : 83.3/47.0 |
| Float | : 36.55 Mn |
| Mkt Cap | : Rs. 35,535 Mn |
| Face Value | : Rs. 1.0 |

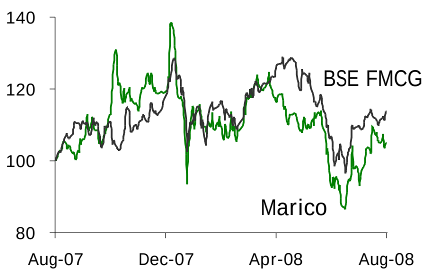
### Shareholding Pattern (as on June 08)




### Stock Returns

| | 1 Mth | 3 Mths | 6 Mths |
|---|---|---|---|
| Marico | 12.73 | -6.52 | -4.37 |
| BSEFMCG | 3.57 | -8.74 | -2.58 |

### Price Comparison




Deepti Singh - deepti@ppfas.com

Marico holds a leadership position in the Indian FMCG space. It has emerged as one of the fastest growing Indian business group operating in the beauty and wellness segments of the FMCG industry. The company is ranked amongst one of eight Indian companies in Standard & Poor's list of Global Challenger Companies in 2007. It offers products and services in hair care, health care and skin care to consumers in India and abroad.

Marico has come a long way in establishing itself as one of the leading consumer products and services company in India. They focus on branded products and their key brands and brand extensions include Parachute, Saffola, Kaya, Hair & Care and Mediker Sundari ,Fiancee etc which have significant market shares in their product categories. These products and Services reach out to more than 20 countries in the Middle East, Asian sub-continent, Australia and USA.

The company aims to be a leader in each of their business segments through heightened sensitivity to consumer needs, setting new standards in the delivery and quality of products and services and processes of continuous learning and improvement.

The company generated a turnover of Rs.19,133.7 million during 2007-08 derived principally from the sale of branded products and services. The company has demonstrated steady growth on both the topline and bottomline, over the last 5 years they grew to a CAGR of 21% and 30% respectively. Last years 22% growth comprised of 17% organic growth accompanied with 5% inorganic growth.

Brands

- Consumer Products Business: Parachute, Saffola, Medikar, Hair & Care, Revive, Sweekar, Shanti Badam Amla, Nihar, Starz, Manjal, Oil of Malabar
- International Business Group: Camelia, Aromatic, Fiancee, Hair Code, Caivil, Black Chic, Hercules, Sundari
- Kaya: Kaya Skin Clinic, Kaya Life.

Their business is segregated into

I) "Consumer Products" business including various branded products in coconut oil, premium refined edible oils, hair oils, other hair care products and functional foods which is further, divided into domestic business and international business; and
ii) "Others" which includes skin care services and products sold under the Kaya brand and Sundari spa skin care products.

## Strong set of core brands

Most of Marico's brands dominate their categories with significant marketshare. Its flagship brand, Parachute, is the leader in the branded coconut oil (CNO) category with a marketshare of 48% in volume terms as on March 08. Further, with the acquisition of Nihar, the company now enjoys 56% share in the branded CNO market.

Saffola pioneered blended oils to become one of the strongest food brands in India. Saffola enjoys substantial equity for its perceived health benefits, especially on the good for heart platform. The company also enjoys a dominant presence in niche categories like anti-lice oil *(Mediker)* and fabric starch *(Revive)*. Marico ventured into the Skin care solutions segment with Kaya Skin Clinics, the *Sundari* range of Spa skin care products and its soap franchise viz., *Camelia, Aromatic and Manjal*. The company acquired Fiancee and Haircode, both of which are Egypts leading haircare brands. They have a market share of 60% and cater to a customer base of 26 million.

Brands with Equity will find it easier to pass on price increases to their loyal customers. Given below is an overview of Marico's market standing as on 31st Mar 08.

| Brand | Category | Indicative Market Share (%)# | Rank |
|---|---|---|---|
| Parachute | Coconut Oil (India) | ~48% | 1 |
| Parachute | Coconut Oil (Bangladesh) | ~ 67% | 1 |
| Saffola | Refined Safflower Oil and its Blends | ~ 98% | 1 |
| Parachute<br>Jasmine<br>Shanti Amla<br>Hair & Care<br>Nihar | Hair Oil | ~ 23% | 2 |
| Parachute Cream | Hair Cream (GCC) | ~ 30% | 2 |
| Fiancee & Hair Code | Hair Cream & Gels (Egypt) | ~ 62% | 1 |
| Kaya | Cosmetological Skin Service | | 1 |
| Medikar | Anti Lice Treatment | ~90% | 1 |
| Revive | Instant Fabric Search | ~ 80% | 1 |

*Source: A.C.Neilsen Urban Retail Market Research and Company Sources*

**Parachute – Continues to provide firm platform**

Parachute is a Rs. 600 crore brand. The flagship brand continues to grow from year to year providing the firm platform for growth. Parachute has been successfully growing on account of innovations in the category. The company can leverage on the Parachute brand to create newer categories. Parachute Night Repair Cream and Parachute Cream with Aquashield are examples of value-added products that spawned new categories. The brand grew by 10% in volume over the previous financial year.

The loose oil market has a strong potential and the company has a consistent strategy of growing the coconut oil market by encouraging conversion from loose oil to branded oil. The company also takes various micro-marketing and distribution expansion initiatives.

**Concentration on the 'beauty and wellness' segment**

The company has transformed itself from a pure oil player to one focussed on beauty and wellness. Marico is a branded player in Beauty and Wellness solutions. The rising disposable income level in India has seen the emergence of lifestyle solutions offerings. Brands of Gymnasia, Spas and Health Clinics are establishing themselves in large cities.

**International business division performing impressively**

The company also has a strong international presence, through its branded products, in the markets of Bangladesh, Middle East and Egypt. During the year Marico's overall international business grew by 59%, while its organic growth over FY07 was 21%.

**Kaya skin care – holds huge potential for performance and growth**

Marico is present in the Skin Care Solutions segment through Kaya Skin Clinics (65 clinics in India and The Middle East) .Kaya has grown at 45% compounded annual growth over the last 3 years. Having established the clinics in select cities throughout India, they intend to consolidate their brand and position in this market.

**Widespread Distribution**

The company has developed a widespread distribution network of more than 2.5 Million outlets in India and overseas. Statistics indicate one in every eight Indians and six Egyptians is a Marico consumer. Also over 70 Million consumer packs from Marico reach approximately 130 million consumers in about 23 million households, every month. Marico's Overseas Sales franchise is one of the largest amongst Indian Companies and is entirely in branded products and services.

The company has identified the growth to be coming from the 3 strong pillars of parachute/coconut oil, Hair oils and Food - Saffola. Marico has adopted a four-pronged growth strategy viz., a) Strengthen its existing brands, b) develop new products, c) Expand international business, and, d) Grow its skin care business. Mentined herewith is a detailed note on each of the major business segments of the company.

- Consumer products business
- International Business
- Kaya

## Consumer Products Business

a) Coconut Oil

The branded coconut oil business in India is valued at about Rs. 10,700 million *(source: A.C. Nielsen)*. The company has indentified branded coconut oil to be their consistent maximum revenue generator. They market the coconut oil through the Parachute brand and it has been the flagship of their business. Parachute has over the years been the branded coconut oil market leader, with an approximately 48 national market share for the 12 months ended March 31, 2008 in the coconut oil category. *(source: A.C. Nielsen).*

| Year Ended March 31 | % market share of Parachute by sales volume |
|---|---|
| 2004 | 45.6% |
| 2005 | 50.5% |
| 2006 | 49.2% |
| 2008 | 48.0% |

*(Source: A.C. Nielsen)*

The company's coconut oil portfolio also comprises Nihar and Oil of Malabar. Marico Industries had acquired Nihar Brand from Hindustan Lever Limited. Nihar has strong equity in the Eastern region. This acquisition has enabled them to further strengthen their position in the coconut oil and perfumed coconut hair oils product category. Nihar coconut oil grew at a modest rate of 4% during the year. As on June 08, the market share of Nihar is ~7%. Marico commands 56% share of the coconut oil category in India with its 3 brands Parachute, Nihar and Oil of Malabar. The competition is largely from regional players. The company expects sustainable growth rates of around 6 to 8% in this segment.

During Q1FY09, Parachute coconut oil in rigid packs recorded a volume growth of 8% over Q1FY08. While Nihar is promoted in its bastion in the East, Parachute which commands better margins is prioritized in markets in the other regions.

b) Premium Refined Edible Oils

Marico offers the consumers refined edible oils in the premium segment through the two brands of Saffola and Sweekar. Sweekar is not a focus brand. Saffola has been actively promoting health consciousness and positioning itself on the "preventive" platform. Saffola is positioned strongly on a "good for the heart" equity. The Saffola refined edible oil franshise grew by 22% in volume terms in the current year. The brand continues to levearge on the growing awareness about heart health in India.

The company does not face any significant competition in the refined safflower oil product category or in the blends with refined safflower oil category. Since the potential for differentiation in the sunflower oil market is not high, brand building in the category is difficult.

The Saffola refined edible oils franchise grew by 28% in volume over Q1FY08, led by Saffola Gold. The volume growth was also boosted by the introduction of a new variant, Saffola Active. It is expected that input prices will remain firm during FY09. The company intends to pass on cost increases so as to maintain its margin per unit volume of sale.

c) Hair Oils

Marico has a range of hair oils that are positioned based on certain consumer benefits. The range comprises:

Parachute Advansed, Parachute Jasmine and Nihar perfumed hair oils, Hair & Care and Shanti Amla. Their portfolio caters to a relatively wide spectrum of consumers and each of these oils addresses a different consumer segment. The product porfolio grew at 16% in FY08.

The Hair Oils category has been experiencing healthy growth. As in the past, the company has focused on rigid pack sales of its portfolio. Marico has a lion's share in the perfumed coconut oils market. During the 12 months to May 2008 its share in rigid packs was at 77%.

d) Anti-Lice Treatment

They dominate the anti-lice treatment product market in India through their brand Mediker. They acquired the Mediker brand from Procter & Gamble Hygiene & Health Care Ltd. during Fiscal 2000 and entered into a noncompete agreement with Marico establishing that Procter & Gamble Limited and all its affiliates will not use an identical anti-lice formulation in India for a period of 10 years ending Fiscal 2010.

e) Others: Prototypes and New Launches

The company has over the years realized that in order to grow and generate additional sources of revenue it needs to maintain a healthy pipeline of new products. In December 2007, the company launched Parachute Advanced Starz range of hair care products for kids. During Q4FY08 Marico entered the the cooling oil market with Maha Thanda Ayurvedic Hair Oil. The idea was to plug the gap in its hair oil portfolio. Marico is also in the post-wash hair conditioner category. The business segment includes Hair & Care Silk-n-Shine, a hair conditioner. This was an introduction to the post-wash hair care market, though the market is small at 1 billion, it is currently one of the fastest growing hair care categories in India.

Marico is also in the process of building a portfolio of functional food products. The company wants to tap the current health and lifestyle trend in India. With this outlook it had introduced Saffola Cholestrol Management last year. During FY08 it introduced the Saffola Diabetics in Delhi and the National Capital Region.

The company also improved the breadth of South African ethnic hair care and health care market through the acquisition of the consumer division of Enaleni Pharmaceuticals Ltd. With these initiatives they aim at increasing the market share of their new products. The introduction of new products and brands acquired has reduced their dependence on established products.

## International Business

Geographic expansion forms part of Marico's growth strategy. Marico commenced their international operations in the early 1990s. The company has notched up a total of 7 acquisitions in the last 35 months. Last year their international consumer products business accounted for 16% of the groups turnover, totalling Rs.300 crore. International Business now comprises about 15% of the group's turnover. The international revenues are growing at 59%. The traditional markets of Middle East and Bangladesh continued to grow and record share gains during the year. With acquisitions in Egypt and South Africa the company is all set to tap the markets of Africa and West Asia.

The Egypytian brands, Fiancee and Hair Code recorded a turnover of about 88 crore during the year and thereby performed as per expectations. The company has also begun exports to the neighbouring countries of Africa. The international business now comprises about 16% of the groups turnover.

Marico's overall international business grew by 37% during Q1FY09. In its traditional markets, namely the Middle East and Bangladesh, Marico's International FMCG business continued to grow and record share gains.

During Q1FY09, Marico's international business without South Africa grew by 15%. The global input cost pressures, particularly for fuel and crude oil derivates, are having their impact on margins in the international business too.

### Inorganic Growth (Since 2005)

| Brands | Products | Primary Markets | Year o Acquisition |
|---|---|---|---|
| Cilvil and BlacK Chic | Hair Care and Health Care | South Africa | 2007 |
| Hercules | OTC Health Care | South Africa | 2007 |
| Fiancee and Hair Code | Hair Cream and Gels | Egypt | 2006 |
| Manjal | Soaps | Southern India | 2006 |
| Nihar | Coconut Oil and Perfumed Coconut Oil | India | 2006 |
| Camelia and Aromatic | Soaps | Bangladesh | 2005 |

## Kaya

Kaya Life :

Kaya Life offering holistic weight management solution which was launched in FY08 currently has 3 centers – all in the city of Mumbai. Customers are experiencing effective results on both weight loss and inch loss. The team is working on the model to increase the pace of customer acquisition and of expanding the menu of programmes and options. These modifications to the model will be tested before a full fledged roll out of Kaya Life is undertaken.

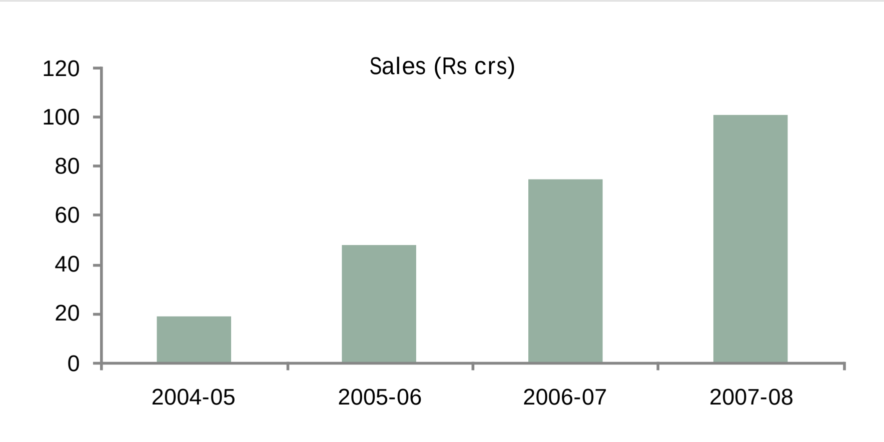
Kaya Skin Clinic:

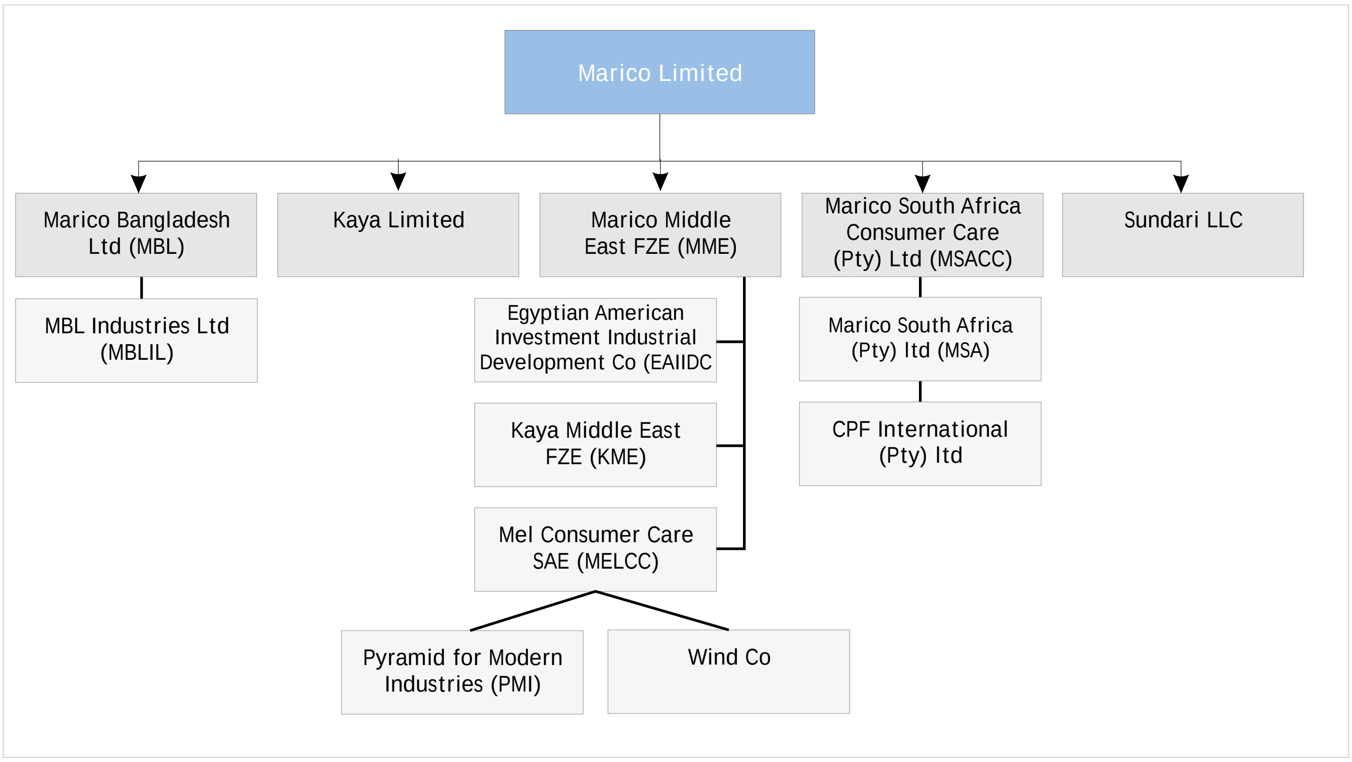
Kaya Skin Care Limited has been incorporated as a wholly-owned Subsidiary to operate skin care solution clinics and distribute Kaya-branded products. Kaya also markets a range of products to complement the services it offers. While initially the products were imported, in Fiscal 2006 they commenced manufacturing these products in India. Product sales constitute approximately 9.5% of total revenue of Kaya-Skin Care Limited. Kaya products are retailed only through Kaya Skin Clinics.

Kaya has expanded its operations in India from 11 clinics in 2 cities as at March 31, 2004 to 56 clinics as at March 31, 2008. In addition, they operate nine Kaya-branded clinics in the UAE. During the year it added 18 clinics . The product share of Kaya is around 15%. Marico plans to open about 15 clinics each year. Kaya's skin care solutions achieved revenue of Rs 100 crore during FY08.  During Q1FY09, Kaya recorded a turnover of Rs 36 crore, a growth of 62% over Q1FY08. Revenue growth in clinics in India in Q1FY09 that were operational in Q1FY08 too was 25%. Kaya Skin business is at breakeven but both Kaya Skin and Kaya Life put together are below break even.

| Particulars | Mar-08 | Mar-05 |
|---|---|---|
| Clinics (Total) | 65 | 33 |
| Cities (India) | 19 | 11 |
| Customer base | >350,000 | 40,000 |

Kaya derives 12% of its sales from product and 88 % sales from services. The ratio is 80: 20 for its sales in India : Abroad. Kaya growth performance over the years:






Marico's overseas market comprise primarily the Middle East, Egypt and SAARC countries.

The inorganic growth seems to aid the already expanding revenues and margins. The table below gives a brief synopsis of the standalone and consolidated numbers for the FY08.

| Particulars | Standalone | Consolidated |
|---|---|---|
| Revenue (Rs Mn) | 15687.80 | 19066.90 |
| Reported PAT (Rs Mn) | 1434.20 | 1690.70 |
| EPS (Rs) | 2.30 | 2.60 |
| Operating Margin | 12.50% | 12.90% |
| PBIT Margin | 11.90% | 11.70% |
| PAT Margin | 9.10% | 8.30% |

Revenues on standalone basis amount to Rs. 15687.8 million and 19066.9 million on consolidated basis as on Mar 08. Reported profit is 1434.2 Mn and 1690.7 Mn on standalone and consolidated basis. The operating margins are higher on consolidated basis but the PBIT and PAT margins drop marginally. The EPS improves to Rs. 2.6 marginally form 2.3 on standalone basis.

Consolidated revenues have grown at a CAGR of 21% whereas the standalone revenues have grown at a rate of 17% during the last 5 years. Even the reported PAT is growing at a lower CAGR rate of 25% (standalone basis)whereas the same is growing at almost 30% on consolidated basis.

Change in the classification of Parachute coconut oil for excise duty purposes will adversely impact earnings and financial performance:

Parachute coconut oil is currently taxed as edible oil (though it is functional for oiling hair). Edible oil attracts lower VAT rate of 4% compared to 12.5% VAT charged for other FMCG products. The manufacture of coconut oil contributes a significant proportion of the total income and profitability. Hence, a change in classification of Parachute coconut oil as hair oil would significantly increase amount of excise duty payable and will adversely impact profitability.

Raw Materials availability and seasonality :

Adequate availability of key raw materials at the right prices and throughout the year is crucial for any operations. Any disruption in the supply, or increase in the costs, of such materials could affect the ability to satisfy existing demand. Marico's key raw materials include copra, kardi oil, sunflower oil, corn oil and rice bran oil which are commodity crops whose availability may be seasonal . They also import some of their input materials into India in foreign currencies including US Dollars and Australian Dollars. Any unexpected jump in input prices could negatively impact the margins.

Risks from international markets:

Marico has acquired several international brands. Part of the revenues are earned in currencies such as US Dollars, Bangladeshi Taka ,UAE Dirhams and Egyptian Pounds which increases its risks to forex fluctuations. Any further expansion into new geographies and undertaking of new projects exposes them to additional foreign currency risks. Also, slower than expected growth in such markets would impact their consolidated financial performance.

Relatively high dependence on one product:

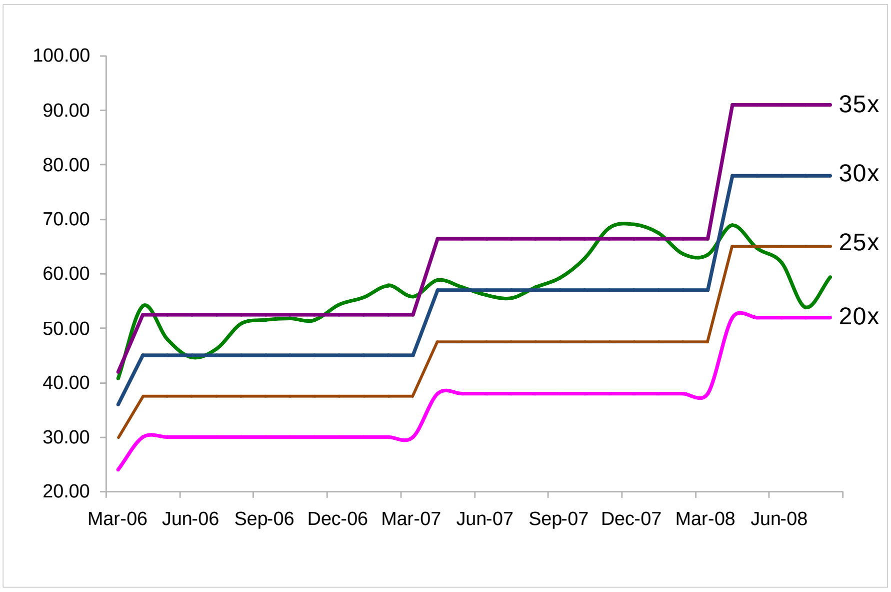
The company's revenue growth depends to a great extent on the performance of one brand, Parachute. The company has consciously tried to reduce this dependence, and has succeeded in bringing it down from 43% four years ago to approximately 33% in FY08. We expect it to further decrease by FY09. The reducing dependence on the sales of flagship Parachute coconut oil product in India is demonstrated in the table below:

| Period | Share of Group Turnover |
|---|---|
| FY 04 | 43.30% |
| FY 05 | 43.10% |
| FY 06 | 42.60% |
| FY 07 | 35.60% |
| FY 08 | 32.50% |

We identify with the company's philosophy of aiming consistent and sustainable growth. Marico identifies the current slowdown as an opportunity to enter new markets and maintain cost structures. The growth in profits has enabled them to target new markets and acquire new customers.

At the current market price of Rs. 58.25 , the stock trades as 16x of FY09 earnings and 14x of FY10 earnings. This seems grossly under priced and a value pick. PPFAS research expects the stock to reach a level of Rs. 82 within 18 months to trade at 20x on projected earnings of FY10E. Thereby we rate the stock as a BUY giving an upside of 40%.

PE Band



| Earnings Statement | | | | | | | |
|---|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY04 | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Total Revenues | 8,884.6 | 10,127.7 | 11,439.4 | 15,569.2 | 19,066.9 | 21,929.5 | 25,221.5 |
| - Growth (%) | | 14.0% | 13.0% | 36.1% | 22.5% | 15.0% | 15.0% |
| Total Expenditure | 8,140.5 | 9,245.8 | 9,997.6 | 13,443.3 | 16,603.4 | 19021.6 | 21877.1 |
| Operating Profit | 744.1 | 881.9 | 1,441.8 | 2,125.9 | 2,463.5 | 2,907.8 | 3,344.4 |
| Other Income | 29.0 | 16.1 | 35.4 | 101.6 | 66.8 | 232.0 | 266.8 |
| EBITDA | 773.1 | 898.0 | 1,477.2 | 2,227.5 | 2,530.3 | 3,139.8 | 3,611.2 |
| Depreciation | 128.2 | 147.8 | 446.7 | 520.6 | 308.6 | 288.7 | 399.8 |
| EBIT | 644.9 | 750.2 | 1,030.5 | 1,706.9 | 2,221.7 | 2,851.2 | 3,211.4 |
| Interest | 11.7 | 20.0 | 50.5 | 206.1 | 276.6 | 276.6 | 276.6 |
| PBT | 633.2 | 730.2 | 980.0 | 1,500.8 | 1,945.1 | 2,574.6 | 2,934.8 |
| Tax | 58.0 | 41.5 | 111.2 | 371.9 | 359.5 | 372.7 | 435.9 |
| PAT Before EI | 575.2 | 688.7 | 868.8 | 1,128.9 | 1,585.6 | 2,201.9 | 2,498.8 |
| - Growth (%) | | 19.7% | 26.2% | 29.9% | 40.5% | 38.9% | 13.5% |
| EI (Goodwill on consolidation) | 0.0 | (4.7) | 0.0 | 0.0 | 106.1 | 0.0 | 0.0 |
| Reported PAT before MI | 575.2 | 693.4 | 868.8 | 1,128.9 | 1,691.7 | 2,201.9 | 2,498.8 |
| Minority Interest | (17.6) | (8.0) | 0.0 | 0.0 | 1.0 | 1.3 | 1.5 |
| PAT after MI | 592.8 | 701.4 | 868.8 | 1,128.9 | 1,690.7 | 2,200.6 | 2,497.4 |

| Ratio Analysis | | | | | | | |
|---|---|---|---|---|---|---|---|
| Particulars | FY04 | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| OPM (%) | 8.4% | 8.7% | 12.6% | 13.7% | 12.9% | 13.3% | 13.3% |
| EBITDA (%) | 8.7% | 8.9% | 12.9% | 14.3% | 13.3% | 14.3% | 14.3% |
| PBIT (%) | 7.3% | 7.4% | 9.0% | 11.0% | 11.7% | 13.0% | 12.7% |
| PAT (%) | 6.5% | 6.8% | 7.6% | 7.3% | 8.3% | 10.0% | 9.9% |
| Interest Cover (x) | 55.1 | 37.5 | 20.4 | 8.3 | 8.0 | 10.3 | 11.6 |
| EPS (Rs.) | 2.0 | 1.2 | 1.5 | 1.9 | 2.6 | 3.6 | 4.1 |
| P/E (x) | 29.4 | 49.1 | 39.0 | 31.5 | 22.4 | 16.1 | 14.2 |
| P/BV (x) | 9.2 | 15.6 | 13.0 | 18.5 | 11.3 | 7.3 | 5.1 |
| BVPS (Rs.) | 6.3 | 3.7 | 4.5 | 3.2 | 5.2 | 8.0 | 11.4 |
| Market Cap (Rs. Mn.) | 16,921.5 | 33,843.0 | 33,843.0 | 35,535.2 | 35,535.2 | 35,535.2 | 35,535.2 |
| M Cap/Sales (x) | 1.9 | 3.3 | 3.0 | 2.3 | 1.9 | 1.6 | 1.4 |
| EV (Rs. Mn.) | 16,687.1 | 33,925.0 | 35,640.2 | 37,617.5 | 38,361.7 | 36,927.7 | 34,941.4 |
| EV/EBITDA (x) | 21.6 | 37.8 | 24.1 | 16.9 | 15.2 | 11.8 | 9.7 |
| EV/Sales (x) | 1.9 | 3.3 | 3.1 | 2.4 | 2.0 | 1.7 | 1.4 |
| ROCE (%) | 33.1% | 27.7% | 20.6% | 38.5% | 33.0% | 33.8% | 30.6% |
| RONW (%) | 31.3% | 31.8% | 33.3% | 58.7% | 50.4% | 45.3% | 36.1% |
| Debt/Equity Ratio (x) | 0.1 | 0.3 | 0.9 | 1.3 | 1.1 | 0.7 | 0.5 |
| Inventory T/o Days | 41.0 | 43.1 | 42.2 | 51.9 | 49.9 | 49.0 | 49.0 |
| Debtors T/o Days | 14.2 | 13.7 | 16.4 | 15.1 | 16.5 | 17.0 | 17.0 |
| Advances T/o Days | 9.1 | 16.9 | 16.9 | 16.8 | 20.3 | 17.7 | 15.4 |
| Creditors T/o Days | 36.2 | 38.2 | 47.8 | 62.8 | 49.0 | 49.0 | 49.0 |
| Working Cap T/o Days | 37.0 | 42.2 | 34.4 | 27.6 | 44.6 | 65.7 | 88.1 |
| Fixed Assets T/o (Gross) | 5.1 | 4.7 | 2.4 | 5.6 | 5.4 | 4.8 | 5.5 |
| DPS (Rs.) | 0.9 | 0.5 | 0.6 | 0.6 | 0.7 | 1.1 | 1.2 |
| Dividend Payout (%) | 42.9% | 45.1% | 41.4% | 34.6% | 25.2% | 30.0% | 30.0% |
| Dividend Yield (%) | 1.5% | 0.9% | 1.1% | 1.1% | 1.1% | 1.9% | 2.1% |

| Balance Sheet | | | | | | | |
|---|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY04 | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Equity Capital | 290.0 | 580.0 | 580.0 | 609.0 | 609.0 | 609.0 | 609.0 |
| Advance on Equity | 2.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Reserves | 1,552.4 | 1,589.2 | 2,034.8 | 1,314.7 | 2,537.2 | 4,247.0 | 6,315.4 |
| Shareholders Funds | 1,844.4 | 2,169.2 | 2,614.8 | 1,923.7 | 3,146.2 | 4,856.0 | 6,924.4 |
| Minority Interest | 18.7 | 0.0 | | | 1.2 | 2.5 | 4.0 |
| Borrowed Funds | 110.6 | 544.3 | 2,396.5 | 2,509.7 | 3,579.4 | 3,579.4 | 3,579.4 |
| Deferred Tax Liability | 62.4 | 60.5 | 82.8 | 0.0 | 0.0 | 0.0 | 0.0 |
| Total Liabilities | 2,036.1 | 2,774.0 | 5,094.1 | 4,433.4 | 6,726.8 | 8,437.9 | 10,507.7 |
| Fixed Assets | 1,124.5 | 1,459.1 | 3,813.0 | 1,654.4 | 2,573.1 | 2,667.1 | 2,597.3 |
| Goodwill | 0.0 | 16.7 | 16.7 | 449.5 | 842.4 | 842.4 | 842.4 |
| Investments | 4.8 | 124.2 | 184.7 | 0.1 | 0.1 | 0.1 | 0.1 |
| Deferred Tax Asset | | | 0.0 | 1,151.5 | 981.7 | 981.7 | 981.7 |
| Current Assets | | | | | | | |
| Inventory | 998.1 | 1,196.8 | 1,322.9 | 2,214.7 | 2,604.6 | 2,944.0 | 3,385.9 |
| Sundry Debtors | 345.3 | 379.0 | 515.3 | 642.6 | 862.7 | 1,021.4 | 1,174.7 |
| Loans & Advances | 221.0 | 468.2 | 528.8 | 716.6 | 1,060.9 | 1,060.9 | 1,060.9 |
| Cash & Bank Balance | 340.2 | 338.1 | 414.6 | 427.3 | 752.8 | 2,186.8 | 4,173.0 |
| Other Current Assets | | | | | | | |
| Current Liabilities | | | | | | | |
| Sundry Creditors | 880.7 | 1,061.3 | 1,498.3 | 2,677.2 | 2,559.6 | 2,944.0 | 3,385.9 |
| Provisions | 122.2 | 150.6 | 206.1 | 147.2 | 391.9 | 322.4 | 322.4 |
| Net Current Assets | 901.7 | 1,170.2 | 1,077.2 | 1,176.8 | 2,329.5 | 3,946.6 | 6,086.2 |
| Miscellaneous Expenditure | 5.1 | 3.8 | 2.5 | 1.2 | 0.0 | 0.0 | 0.0 |
| Total Assets | 2,036.1 | 2,774.0 | 5,094.1 | 4,433.5 | 6,726.8 | 8,437.9 | 10,507.7 |

| Cash Flow | | | | | | | |
|---|---|---|---|---|---|---|---|
| Particulars (Rs Mn) | FY04 | FY05 | FY06 | FY07 | FY08 | FY09E | FY10E |
| Opening Cash & Bank | 253.3 | 340.2 | 338.1 | 414.6 | 427.3 | 752.8 | 2,186.8 |
| Profit After Tax | 575.2 | 688.7 | 868.8 | 1,128.9 | 1,585.6 | 2,201.9 | 2,498.8 |
| Invt Income | (29.0) | (16.1) | (35.4) | (101.6) | (66.8) | (232.0) | (266.8) |
| Interest Paid | 11.7 | 20.0 | 50.5 | 206.1 | 276.6 | 276.6 | 276.6 |
| Miscellaneous Exp W/Off | 1.8 | 1.3 | 1.3 | 1.3 | 1.2 | 0.0 | 0.0 |
| Depreciation | 128.2 | 147.8 | 446.7 | 520.6 | 308.6 | 288.7 | 399.8 |
| Deferred Taxation | (1.6) | (1.9) | 31.9 | 158.1 | 202.1 | 0.0 | 0.0 |
| Others | (79.8) | (34.1) | (45.0) | (4,715.7) | 42.7 | 269.0 | 433.0 |
| Change in Working Cap | 123.7 | (270.6) | 169.5 | (86.9) | (827.2) | (183.2) | (153.3) |
| CF - Operating Activities | 730.2 | 535.1 | 1,488.3 | (2,889.2) | 1,522.8 | 2,621.0 | 3,188.2 |
| Change in Fixed Assets | (214.7) | (475.0) | (2,778.4) | 2,091.7 | (1,197.6) | (382.8) | (330.0) |
| Change in Goodwill | 0.0 | (16.7) | 0.0 | (432.8) | (392.9) | 0.0 | 0.0 |
| Change in Investments | 133.1 | (119.4) | (60.5) | 184.6 | 0.0 | 0.0 | 0.0 |
| Investment Income | 29.0 | 16.1 | 35.4 | 101.6 | 66.8 | 232.0 | 266.8 |
| CF - Investing Activities | (52.6) | (595.0) | (2,803.5) | 1,945.1 | (1,523.7) | (150.8) | (63.2) |
| Increase in Equity | (290.0) | | | 1,513.9 | | | |
| Changes in Borrowings | (9.3) | 433.7 | 1,852.2 | 113.2 | 1,069.7 | 0.0 | 0.0 |
| Interest Paid | (11.7) | (20.0) | (50.5) | (206.1) | (276.6) | (276.6) | (276.6) |
| Dividend Paid | (279.7) | (355.9) | (410.0) | (464.2) | (466.7) | (759.6) | (862.1) |
| CF - Financing Activities | (590.7) | 57.8 | 1,391.7 | 956.8 | 326.4 | (1,036.2) | (1,138.7) |
| Net Change in Cash | 86.9 | (2.1) | 76.5 | 12.7 | 325.5 | 1,434.0 | 1,986.3 |
| Closing Cash & Bank Bal | 340.2 | 338.1 | 414.6 | 427.3 | 752.8 | 2,186.8 | 4,173.0 |

# Disclaimer

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|---|---|
| Disclosure of Interest Statement | - |
| 1. Analyst Ownership of the scrip | NO |
| 2. PPFAS ownership of the scrip | NO |
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## Contact

| | | | |
|---|---|---|---|
| Hiten Sampat | President - Institutional Sales | hiten@ppfas.com | 91 22 2284 6555 Extn 302 |
| Ridhim Thapar | Institutional Sales | ridhim@ppfas.com | 91 22 2284 6555 Extn 312 |
| Deepti Singh | Analyst - Investment Research | deepti@ppfas.com | 91 22 2284 6555 Extn 202 |

**Parag Parikh Financial Advisory Services Limited**

130/132,Great Western Building,1st Floor, S. B. Marg, Near Lion Gate, Fort, Mumbai - 400 023.

Tel : 91-22-2284 6555  Fax : 91-22-2284 6553,e-mail : researchcall@ppfas.com

Investment Boutique: Shiv Shakti, Gr. Floor, N. S. Rd. No.10, Opp. Haveli, Juhu Scheme, Mumbai - 400 049

Tel :91-22- 2623 6555 Fax : 91-22-2623 6553,e-mail : ib@ppfas.com

www.ppfas.com