

Cigarette volumes rise; margins decline...

Net revenue (net of excise duty) increased by 13.3% YoY to ₹ 11,992.1 crore. Cigarette, FMCG, Agri, Paperboard & Hotels business witnessed a growth of 11.1%, 7.3%, 16.2%, 18.2% & 24.9% respectively. EBITDA grew by 10.3% to ₹ 4,571.7 crore supported by Cigarette, FMCG, Agri & Paperboard segments. FMCG EBIT increased from ₹ 91.2 crore to ₹ 201 crore (including ₹ 70.5 crore of loss making Lifestyle business sale) driven by strong growth in the branded packaged foods business, better product mix and cost rationalisation initiatives. The company declared dividend of ₹ 5.75/share.

Selective cigarettes price hikes to support margins

Cigarette business EBIT increased by 10% on the back of stable taxation regime during the year. ITC has taken price hike in 20% of its cigarette portfolio by increasing the prices of Flake Excel by 11%, Bristol by 6.7% and Capstan by 14.5%. This selective price hike would result in average price hike of 3%. The recent price hikes are undertaken in the lower end of the portfolio and brands such as Capstan, Bristol and Flake Excel have very limited preference in urban markets but are largely sold in tier-II and tier-III towns. However, price hikes in these brands were taken after a long gap as there was no significant tax increase on cigarettes in recent times. Hence, we expect price hikes to get absorbed in the market. We expect price hikes to provide some cushioning to EBIT margins of the cigarette business in the backdrop of revenue mix shifting towards low price cigarettes (64mm).

Strong distribution network to help build FMCG segment

In a bid to diversify away from the highly regulated cigarettes space, ITC has invested ₹ 4000 crore in FMCG business over the last 10 years. Strong agri value chain gives the company sourcing advantage for wheat, potato, fruits and other spices. ITC also has an extensive distribution network covering 6 million retail outlets, which has helped improve its visibility of its FMCG brands. FMCG business currently contributes to only 4% of its EBITDA and 25% of sales. With ITC looking to expand its core brands coupled with entry into new segments like dairy and rice, the company would be a formidable player in FMCG given its strong sourcing base and distribution muscle.

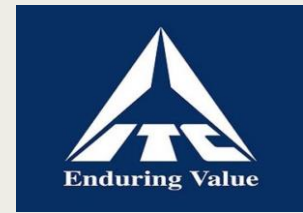
Valuation & Outlook

ITC has a strong margin profile with EBITDA & PAT margin of 38.5% & 27.7% respectively as on FY19. Led by superior margins, ITC has been able to generate operating cash flow of ₹ 11,000 crore in FY19. While overall RoCE is at 30.8%, cash cow cigarettes business enjoys RoCE of 200%+ due to superior pricing power and low capital intensity. High cash generation has enabled ITC to invest aggressively in other fast growing businesses and thereby diversify into non-stringent segments. We expect revenues and PAT to grow at a CAGR of 9.9% and 10.8% respectively in FY19-21E. We continue to maintain our **BUY** rating on the stock with a target price of ₹ 340/share.

Key Financial Summary

Key Financials	FY17	FY18	FY19	FY20E	FY21E	CAGR (FY19-21E)
Net Sales	39641.9	40254.7	44432.7	49069.1	53698.1	9.9%
EBITDA	14578.0	15541.0	17305.5	19366.3	21399.2	11.2%
EBITDA Margin %	36.8	38.6	38.9	39.5	39.9	
Net Profit	10200.9	11223.3	12464.3	13666.9	15294.7	10.8%
EPS (₹)	8.40	9.24	10.26	11.25	12.59	
P/E	34.5	31.4	28.3	25.8	23.0	
RoNW %	22.5	21.3	21.5	22.2	22.6	
RoCE (%)	32.9	30.9	30.8	32.7	33.3	

Source: Company, ICICI Direct Research



Particulars

Particulars (₹ crore)	Amount
Market Capitalization	352,274.6
Total Debt (FY19)	7.9
Cash and Investments (FY19)	16,275.3
EV	336,007.2
52 week H/L (₹)	322 / 259
Equity capital	1,225.9
Face value (₹)	1.0

Key Highlights

- Maintain BUY with a target price of ₹ 340/per share
- Cigarette volume growth was 8% led by higher growth of 64 mm segment, which now contributes ~40% of cigarette sales volumes
- Cigarette EBIT margins contracted by 73 bps due to higher salience of low priced 64 mm cigarettes
- FMCG EBITDA improved from 5.7% to 7% YoY; ITC has ended FY19 with EBITDA margin of 5.5%

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Exhibit 1: Variance Analysis

	Q4FY19	Q4FY19E	Q4FY18	YoY (%)	Q3FY19	QoQ (%)	Comments
Total Operating Income	11,992.1	11,463.3	10,586.7	13.3	11,227.7	6.8	Net revenue increased by 13.3% YoY. Cigarette, FMCG, agri business, paperboard segments and hotels grew by 11.1%, 7.3%, 16.2%, 18.2% and 24.9%, respectively. Cigarettes volumes increased by ~8%
Operating Income	141.9	100.9	107.5	32.0	91.1	55.7	
Raw Material Expenses	4,615.6	4,339.4	4,001.2	15.4	4,300.5	7.3	
Employee Expenses	760.0	625.3	611.3	24.3	629.2	20.8	Employee expenses increased by 24.3% on account of one-off incentives
Other operating Expenses	2,044.9	1,946.0	1,830.3	11.7	1,972.2	3.7	
EBITDA	4,571.7	4,552.7	4,144.0	10.3	4,325.8	5.7	Operating profit increased by 10.3%, well supported by profitable growth in all segments
EBITDA Margin (%)	38.1	39.7	39.1	-102 bps	38.5	-41 bps	EBITDA margins declined by 102 bps impacted by 73 bps drop in cigarettes EBIT (due to higher sales from low priced 64 mm cigarette segment)
Depreciation	350.2	328.9	304.0	15.2	335.4	4.4	
Interest	7.7	11.7	23.2	-66.6	5.6	38.0	
Other Income	740.2	701.1	516.5	43.3	836.4	-11.5	
PBT	4,953.9	4,913.2	4,333.3	14.3	4,821.2	2.8	
Tax Outgo	1,472.0	1,686.8	1,400.6	5.1	1,612.1	-8.7	
PAT	3,481.9	3,226.5	2,932.8	18.7	3,209.1	8.5	On the back of higher operating profit and other income, net profit grew by 18.7% YoY.
Key Metrics YoY growth (%)							
Cigarette Growth (%)	11.1		N.A.		9.6		Cigarette segment reported 11.1% increase in sales on the back of volume growth of ~8%
FMCG (Others) Growth (%)	7.3		5.8		11.5		FMCG segment reported 7.3% growth; barring restructuring of Lifestyle retailing segment, growth was 10%
Hotels Growth (%)	24.9		5.6		11.7		Hotels segment grew by 24.9% driven by 5% increase in ARR and higher F&B revenue from existing hotels and addition of new properties to the portfolio. Occupancy levels were at 68% during the quarter
Agri Business Growth (%)	16.2		-5.7		25.7		Agri business grew by 16.2% driven by trading opportunities in oilseeds, wheat and coffee
Paperboards Growth (%)	18.2		-5.2		20.5		Paperboards segment grew by 18.2% driven by product mix enrichment, higher realization, strategic investments in imported pulp substitution

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY20E			FY21E			Comments
	Old	New	Change	Old	New	Change	
Sales	48,962.1	49069.1	0.2	53,473.6	53,698.1	0.4	EBITDA margin revised downwards on moderation in cigarettes margins
EBITDA	19733.0	19366.3	-1.9	21724.4	21399.2	-1.5	
EBITDA Margin (%)	39.7	39.0	-72 bps	40.0	39.3	-67 bps	
PAT	13727.8	13666.9	-0.4	15108.1	15294.7	1.2	
EPS (₹)	11.37	11.32	-0.4	12.5	12.67	1.2	

Source: Company, ICICI Direct Research

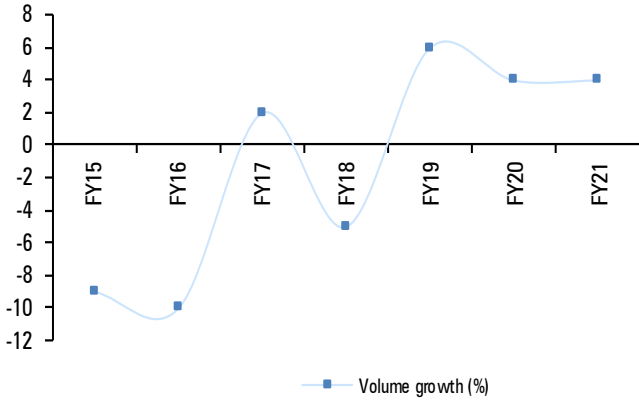
Exhibit 3: Assumptions

	Current				Earlier			
	FY17	FY18	FY19	FY20E	FY21E	FY20E	FY21E	
Cigarettes (₹ cr)	34,002.0	22,894.0	41,968.3	46,265.8	49,319.4	44,344.4	47,260.1	We have changed cigarettes revenue estimates on positive volume growth trajectory
Cigarette Vol. Growth (%)	2.0	-4.0	6.0	4.0	4.0	3.0	1.5	
Cigarette Price Growth (%)	3.0	12.0	9.5	6.0	2.5	7.0	5.0	
FMCG - Others (₹ cr)	10,498.6	11,314.4	12,600.6	14,211.0	16,224.8	14,681.5	16,759.8	
Hotels (₹ cr)	1,329.3	1,404.1	1,620.7	1,794.1	1,931.6	1,632.6	1,674.1	Changed hotel revenue estimates on higher ARR & higher occupancy levels
Agri Business (₹ cr)	5,352.9	4,552.0	9,084.3	9,879.3	10,689.6	9,738.3	10,538.1	
Paperboards (₹ cr)	3,819.0	3,792.4	5,855.9	6,240.4	6,650.9	6,157.2	6,562.3	

Source: Company, ICICI Direct Research

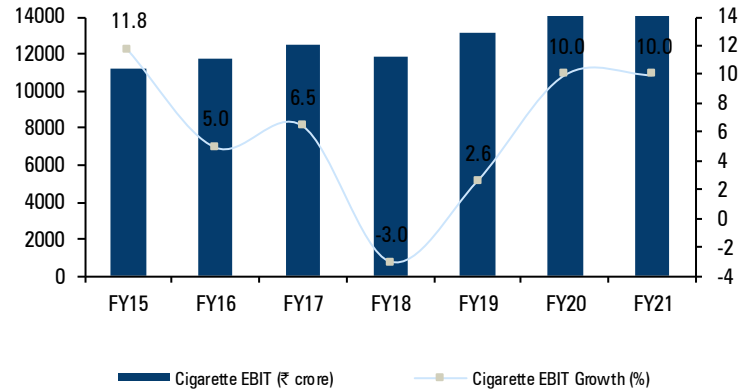
Key Metrics

Exhibit 4: Cigarette volume growth trend



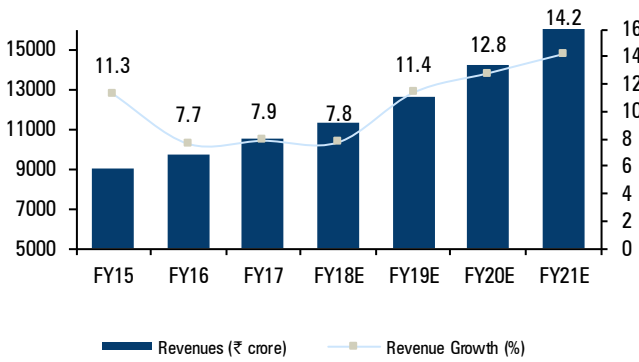
Source: Company, ICICI Direct Research

Exhibit 5: Cigarette EBIT growth trend



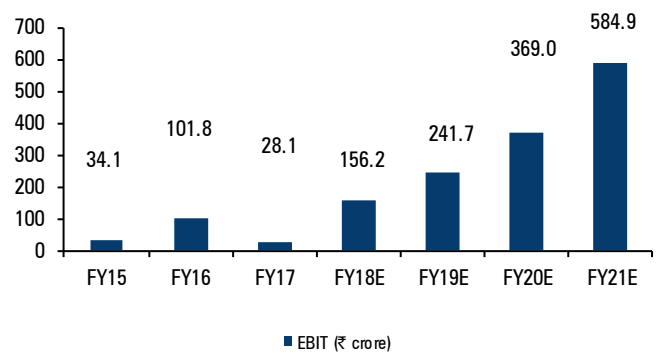
Source: Company, ICICI Direct Research

Exhibit 6: FMCG revenue (₹ crore) and growth (%)



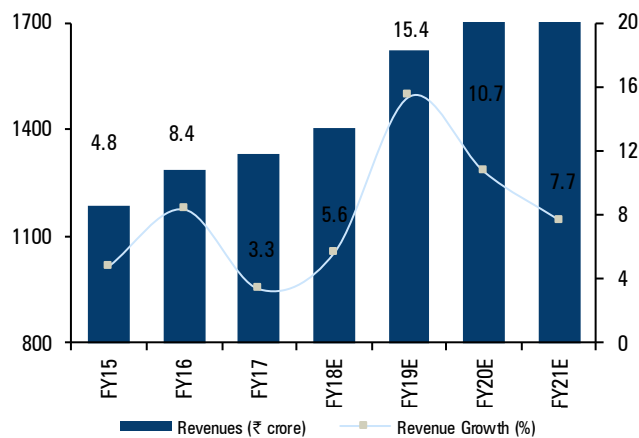
Source: Company, ICICI Direct Research

Exhibit 7: FMCG EBIT (₹ crore)



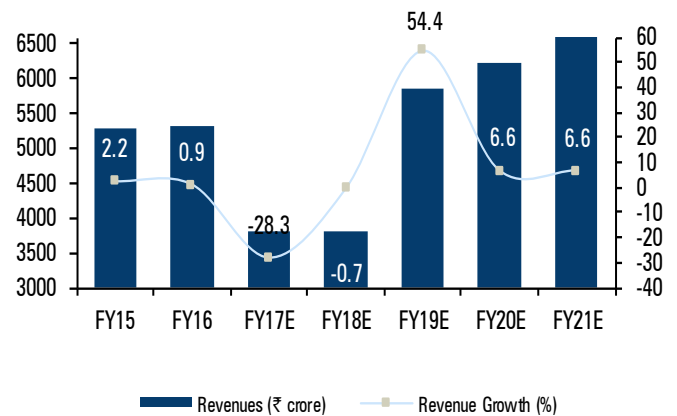
Source: Company, ICICI Direct Research

Exhibit 8: Hotel revenue (₹ crore) and growth (%)



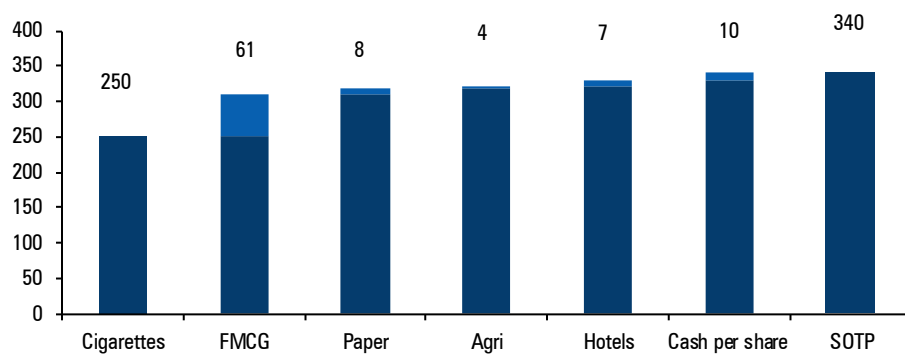
Source: Company, ICICI Direct Research

Exhibit 9: Paperboards revenue (₹ crore) and growth (%)



Source: Company, ICICI Direct Research

Exhibit 10: Sum of the parts valuation



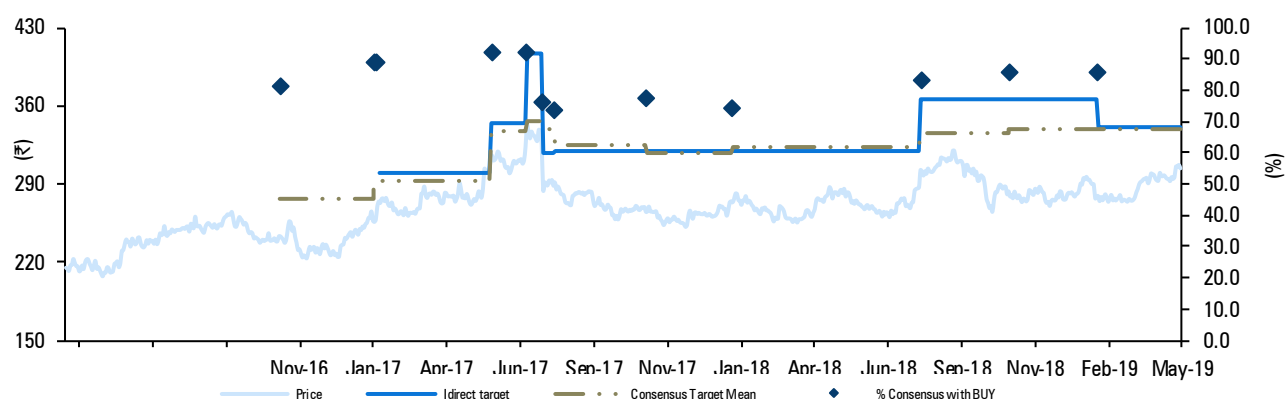
Source: Company, ICICI Direct Research

Exhibit 11: Valuations

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY18	40254.7	1.5	9.2	10.0	31.4	22.5	21.3	30.9
FY19E	44432.7	10.4	10.3	11.1	28.3	20.1	21.5	30.8
FY20E	49069.1	10.4	11.3	9.6	25.8	18.0	22.2	32.7
FY21E	53698.1	9.4	12.6	11.9	23.0	16.3	22.6	33.3

Source: Company, ICICI Direct Research

Exhibit 12: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 13: Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	British American Tobacco PLC	31-Dec-18	24.30	2,978.3	0.0
2	Life Insurance Corporation of India	31-Dec-18	16.11	1,975.1	0.0
3	UTI Asset Management Co. Ltd.	31-Dec-18	7.95	974.5	0.0
4	Myddleton Investments Co., Ltd.	31-Dec-18	3.97	486.3	0.0
5	ICICI Prudential Asset Management Co. Ltd.	31-Mar-19	1.87	229.8	-29.8
6	SBI Funds Management Pvt. Ltd.	31-Mar-19	1.84	225.7	4.8
7	General Insurance Corporation of India	31-Dec-18	1.69	206.8	0.0
8	The New India Assurance Co. Ltd.	31-Dec-18	1.54	188.3	-1.7
9	GIC Private Limited	31-Dec-18	1.51	184.7	-2.2
10	HDFC Asset Management Co., Ltd.	31-Mar-19	1.42	174.6	0.2

Source: Reuters, ICICI Direct Research

Exhibit 14: Recent Activity

Buys			Sells		
Investor name	Value	Shares	Investor name	Value	Shares
Aberdeen Asset Managers Ltd.	33.12m	8.50m	ICICI Prudential Asset Management Co. Ltd.	-128.07m	-29.81m
SBI Funds Management Pvt. Ltd.	20.50m	4.77m	Matthews International Capital Management, L.L.C.	-44.87m	-11.08m
Reliance Nippon Life Asset Management Limited	9.52m	2.22m	AllianceBernstein L.P.	-18.71m	-4.80m
Aditya Birla Sun Life AMC Limited	5.94m	1.38m	J O Hambro Capital Management Limited	-14.98m	-3.70m
Manulife Asset Management (Europe) Limited	5.45m	1.27m	Vontobel Asset Management, Inc.	-12.29m	-3.15m

Source: Reuters, ICICI Direct Research

Exhibit 15: Shareholding Pattern

(in %)	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Promoter	-	-	-	-	-
FII	18.0	17.5	17.3	17.1	17.0
DII	37.1	37.6	37.8	38.1	38.2
Others	44.9	44.9	44.9	44.9	44.8

Source: Company, ICICI Direct Research

Financial summary

Exhibit 16: Profit and loss statement				
	₹ crore			
	FY18	FY19	FY20E	FY21E
Total operating income	40,627.5	44,995.7	49,679.9	54,412.7
Growth (%)	1.3	10.8	10.4	9.5
Raw Material Expenses	15,790.0	17,305.2	19,201.6	20,873.7
Employee Expenses	2,487.5	2,728.4	3,089.4	3,367.6
Marketing Expenses	886.2	0.0	996.6	1,086.3
Administrative Expenses	4,154.5	0.0	1,694.2	1,873.9
Excise Duty	3702.2	788.7	788.7	788.7
Other expenses	1,768.3	7,656.6	5,331.8	5,811.9
Total Operating Expenditure	25,086.6	27,690.1	30,313.6	33,013.5
EBITDA	15,541.0	17,305.5	19,366.3	21,399.2
Growth (%)	6.6	11.4	11.9	10.5
Depreciation	1,145.4	1,311.7	1,426.4	1,510.4
Interest	86.7	34.2	60.7	66.5
Other Income	2,129.8	2,484.5	2,893.7	3,310.2
PBT	16,851.7	18,444.2	20,772.9	23,132.5
Total Tax	5,628.5	5,979.8	7,106.0	7,837.8
PAT	11,223.3	12,464.3	13,666.9	15,294.7
Growth (%)	10.0	11.1	9.6	11.9
EPS (₹)	9.2	10.3	11.3	12.6

Source: Company, ICICI Direct Research

Exhibit 17: Cash flow statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Profit After Tax	11,132.1	12,464.3	13,666.9	15,294.7
Add: Depreciation	1,145.4	1,311.7	1,426.4	1,510.4
(Inc)/dec in Current Assets	-157.3	-3,892.1	-1,764.7	-3,336.0
Inc/(dec) in CL and Provisions	2,077.4	765.0	1,161.2	1,017.2
CF from operating activities	12,650.9	10,648.9	14,489.8	14,486.4
(Inc)/dec in Investments	0.0	-577.7	-44.3	-3,538.4
(Inc)/dec in LT loans & advances	0.0	1.2	-50.0	0.0
(Inc)/dec in Fixed Assets	-2,547.8	-2,607.9	-4,749.2	-1,520.0
Others	0.0	94.4	0.0	0.0
CF from investing activities	-6,691.2	-3,567.9	-4,843.5	-5,058.4
Issue/(Buy back) of Equity	5.7	5.4	0.0	0.0
Inc/(dec) in loan funds	-7.8	-3.2	10.0	10.0
Dividend paid & dividend tax	-6,880.3	-7,510.8	-8,423.2	-9,265.5
Others	0.0	10.7	31.4	19.5
CF from financing activities	-6,019.9	-7,497.9	-8,381.8	-9,236.0
Net Cash flow	-60.2	-417.0	1,264.5	192.0
Opening Cash	156.2	95.9	-321.0	943.4
Cash with Bank	2,498.9	4,089.7	2,498.9	2,498.9
Closing Cash	2,594.9	3,768.7	3,442.3	3,634.3

*calculated, Source: Company, ICICI Direct Research

Exhibit 18: Balance sheet				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Liabilities				
Equity Capital	1,220.4	1,225.9	1,225.9	1,225.9
Reserve and Surplus	50,179.6	56,723.9	60,376.8	66,406.0
Total Shareholders funds	51,400.1	57,949.8	61,602.7	67,631.9
LT Borrowings & Provisions	11.1	7.9	17.9	27.9
Deferred Tax Liability	1,917.9	2,044.1	2,044.1	2,044.1
Others Non-current Liabilities	195.6	174.5	205.9	225.4
Total Liabilities	53,524.7	60,176.4	63,870.6	69,929.3
Assets				
Gross Block	27,233.7	32,259.3	35,660.7	37,760.7
Less: Acc Depreciation	10,372.7	11,684.4	13,110.9	14,621.3
Net Block	16,861.0	20,574.9	22,549.8	23,139.4
Capital WIP	5,025.6	3,401.4	2,100.0	1,500.0
Net Intangible Assets	446.0	540.8	560.8	580.8
Non-current Investments	13,493.8	14,071.5	14,115.8	17,654.2
LT loans & advances	7.4	6.2	56.2	56.2
Current Assets				
Inventory	7,237.2	7,587.2	7,394.0	8,091.5
Debtors	2,357.0	3,646.2	4,033.1	4,413.5
Loans and Advances	4.2	5.0	5.5	6.1
Other Current Assets	2,406.4	2,055.2	2,688.7	2,942.4
Cash	2,594.9	3,768.7	3,442.3	3,634.3
Current Investments	9903.5	12506.6	13443.6	15447.4
Current Liabilities	8,856.6	9,621.6	10,782.8	11,800.0
Creditors	3,382.3	3,368.3	4,033.1	4,413.5
Provisions	39.2	25.2	27.9	30.5
Short term debt & other CL	5,435.1	6,228.0	6,721.8	7,355.9
Application of Funds	53,524.7	60,176.4	63,870.6	69,929.3

Source: Company, ICICI Direct Research

Exhibit 19: Key ratios				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Per share data (₹)				
EPS	9.2	10.3	11.3	12.6
Cash EPS	10.2	11.3	12.4	13.8
BV	42.3	47.7	50.7	55.7
DPS	5.2	5.8	6.3	7.0
Cash Per Share	2.1	3.1	2.8	3.0
Operating Ratios (%)				
EBITDA Margin	38.3	38.5	39.0	39.3
PBT / Total Operating income	40.5	41.0	41.8	42.5
PAT Margin	27.6	27.7	27.5	28.1
Inventory days	65.6	62.3	55.0	55.0
Debtor days	21.4	30.0	30.0	30.0
Creditor days	30.7	27.7	30.0	30.0
Return Ratios (%)				
RoE	21.3	21.5	22.2	22.6
RoCE	30.9	30.8	32.7	33.3
RoIC	29.7	29.5	32.3	32.4
Valuation Ratios (x)				
P/E	31.4	28.3	25.8	23.0
EV / EBITDA	22.5	20.1	18.0	16.3
EV / Net Sales	8.7	7.8	7.1	6.5
Market Cap / Sales	8.8	7.9	7.2	6.6
Price to Book Value	6.9	6.1	5.7	5.2
Solvency Ratios				
Debt/EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	2.5	2.7	2.6	2.6
Quick Ratio	1.7	1.9	1.9	1.9

Source: Company, ICICI Direct Research

Exhibit 20: ICICI Direct coverage universe (FMCG)

Sector / Company	CMP		M Cap	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)			
	(₹)	TP(₹)		Rating	(₹ Cr)	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E
Colgate (COLPAL)	1,125	1,350	Hold	34,950	28.9	31.9	35.8	39.0	35.3	31.5	7.8	7.1	6.5	62.1	59.2	55.4	43.3	41.7	38.8
Dabur India (DABIND)	370	450	Buy	66,747	8.2	9.2	10.2	45.2	40.4	36.4	7.8	7.0	6.3	29.6	28.1	28.4	25.7	24.0	24.3
GSK CH (GLACON)	7,140	8,340	Buy	30,028	166.5	233.7	244.1	42.9	30.6	29.3	6.9	6.3	5.8	29.8	36.1	33.4	20.1	24.0	22.8
Hindustan Unilever (HINLEV)	1,700	1,900	Hold	378,000	28.5	32.9	37.9	59.6	51.7	44.9	9.9	8.7	7.6	100.8	123.7	162.3	87.2	106.9	141.3
ITC Limited (ITC)	290	340	Buy	352,275	10.3	11.3	12.6	28.3	25.8	23.0	7.9	7.2	6.6	30.8	32.7	33.3	21.5	22.2	22.6
Jyothy Lab (JYOLAB)	150	220	Buy	6,181	5.3	5.9	6.7	28.2	25.3	22.4	3.5	3.1	2.8	28.6	37.5	38.9	22.6	28.2	29.2
Marico (MARLIM)	350	425	Buy	46,963	8.8	8.7	9.8	39.8	40.4	35.9	6.4	5.5	4.9	38.0	42.6	41.7	31.6	35.8	34.6
Nestle (NESIND)	10,200	12,000	Buy	99,795	166.7	203.4	243.5	61.2	50.1	41.9	8.9	7.8	6.9	41.4	42.6	44.3	44.5	43.0	42.1
Tata Global Bev (TATGLO)	200	240	Buy	12,938	7.2	7.9	8.7	27.6	25.3	22.9	1.8	1.7	1.6	8.4	9.1	9.5	6.5	7.2	7.6
VST Industries (VSTIND)	3,500	3,900	Buy	5,348	146.9	164.4	178.8	23.8	21.3	19.6	4.9	4.4	4.0	51.4	51.1	50.3	34.2	34.4	33.9
Varun Beverage (VARBEV)	885	1,040	Hold	17,530	11.7	16.4	18.6	75.5	53.9	47.5	4.4	3.4	2.5	12.7	14.2	13.3	12.1	15.0	11.0

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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