

Institutional Equities
 India Research

ITC
QUARTERLY REVIEW

 Bloomberg: ITC IN
 Reuters: ITC.BO

BUY

Robust Profitability Continues ...

Surpassing our as well as market expectation, ITC has reported strong set of numbers in Q2FY13. Its net sales grew 20% YoY owing to strong 26% & 40% growth in FMCG & Agri business, respectively. ITC's cigarette gross sales grew 17% YoY, while due to sharp 20% growth in excise duty, the Company's net sales registered slower 14% growth in Q2FY13. Its EBITDA margin rose by 73 bps YoY (192 bps QoQ) to ~37% (vs. our estimate of ~36%). Meanwhile, ITC's net profit rose 21% YoY to Rs. 18.36 bn (vs. our estimate of Rs. 17.27 bn). We maintain our "BUY" recommendation on the stock with the target price of Rs. 312 apiece.

Robust Sales Driven by 25% Growth in Non-cigarette Biz: Contributing significantly by ~20% to total net sales, ITC's non-cigarette business grew 25% in Q2FY13 vis-à-vis 14% growth in core cigarettes business. The non-cigarette sales mix has increased to 59.6% in Q2FY13 vs. 57.3% in Q1FY13 & 57.4% in Q2FY12. Beating the average growth of 22% in last 8 quarters, ITC's FMCG sales rose by 26% with all major FMCG categories recording significant growth during the quarter. The Company's growth in Agribusiness growth was supported by better wheat exports and reduction of leaf tobacco inventory level during the quarter.

Robust Profitability Led by All-time High Cigarette PBIT Margin: Cigarette PBIT margin rose 320 bps YoY to 61.4% in Q2FY13, which was all time margin. Periodic hike in consistent prices, change in cigarette mix and slower growth in input prices have resulted in robust profitability for the Company. Meanwhile, PBIT loss in FMCG business reduced to 1.8% in Q2FY13 vis-à-vis 4.2% & 2.6% loss in Q2FY12 and Q1FY13, respectively.

Outlook & Valuation

We expect 16.4%, 17.7% and 17.6% Sales, EBITDA & PAT CAGR in FY12-15E. ITC's cigarette business would maintain sales growth momentum and we expect 14.5% sales CAGR, while its non-cigarette business would exhibit 19% CAGR in FY12-15E. ITC's PBIT mix is also expected to improve from 20% Q2FY13 to 25% by FY15E. We value the stock based on DCF methodology assuming 18% & 16% FCF growth in 1st & 2nd 5 years post-FY15, and reiterate our "BUY" rating on ITC and with target price of Rs. 312 per share.

Key Financials

Y/E Mar (Rs mn)	FY11	FY12	FY13E	FY14E	FY15E
Revenue	222,737	261,795	302,334	355,033	413,141
EBITDA	74,208	88,376	105,234	124,721	144,659
Net Profits (Adj)	49,558	62,580	73,542	88,074	102,261
EPS (Rs)	6.3	8.0	9.4	11.3	13.1
PER (x)	45.3	35.9	30.5	25.5	21.9
P/BV (x)	13.6	11.5	10.0	8.6	7.4
EV/EBITDA (x)	29.3	24.5	20.6	17.1	14.5

Source: Company, Karvy Institutional Research

Recommendation

CMP:	Rs298
Target Price:	Rs312
Upside (%)	5%

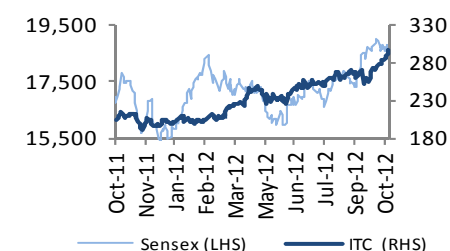
Stock Information

Market Cap. (Rs bn / US\$ mn)	2,337/43,331
52-week High/Low (Rs)	299/189
3m ADV (Rs mn /US\$ mn)	1,616/30.0
Beta	0.7
Sensex/ Nifty	18,682/5,684
Share outstanding (mn)	7,856

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	17.0	17.1	43.7	47.8
Rel. to Sensex	15.9	8.3	31.4	22.3

Performance



Source: Bloomberg

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Segmental Performance during Q2FY13

- ITC's cigarette gross sales grew 17% YoY, while due to sharp 20% growth in excise duty, the Company's net sales registered slower 14% growth in Q2FY13.
- Cigarette PBIT margin rose 320 bps YoY to 61.4% in Q2FY13, which was all time margin. Periodic hike in consistent prices, change in cigarette mix and slower growth in input prices have resulted in robust profitability for the Company.

Exhibit 1: Cigarette Business Performance

Particulars	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12
Gross Sales (Rs mn)	48,104	52,363	51,111	52,699	54,860	58,097	56,848	60,614	64,186
Gross Sales Growth (%)	15.0	18.4	13.2	12.9	14.0	11.0	11.2	15.0	17.0
Net Sales (Rs mn)	25,501	27,726	27,673	28,736	29,681	32,328	32,496	33,042	33,852
Net Sales Growth (%)_	15.9	18.9	12.8	15.7	16.4	16.6	17.4	15.0	14.0
Net Sales Mix (%)	42.6	45.4	43.4	41.2	42.6	46.2	43.1	42.7	40.4
PBIT Margin (%)	57.2	55.3	53.1	54.9	58.2	57.0	54.1	57.5	61.4
PBIT Mix (%)	77.6	81.5	81.9	81.4	77.0	81.4	82.7	81.8	79.8

Source: Company, Karvy Institutional Research

- FMCG sales were up by 26% and have beaten its past 8 quarters' average growth of 22%. All major FMCG categories recorded significant growth.
- FMCG business has also reduced PBIT loss to 1.8% as compared 4.2% & 2.6% loss in Q2FY12 and Q1FY13 respectively.

Exhibit 2: FMCG Business Performance

FMCG	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12
Net Sales (Rs mn)	10,556	11,021	13,125	11,978	13,407	13,707	16,165	14,731	16,908
Net Sales Growth (%)	22.3	23.9	16.9	19.6	27.0	24.4	23.2	23.0	26.1
Net Sales Mix (%)	17.6	18.1	20.6	17.2	19.3	19.6	21.4	19.0	20.2
PBIT Margin (%)	(6.3)	(6.7)	(5.2)	(6.4)	(4.2)	(3.4)	(1.0)	(2.6)	(1.8)
PBIT Mix (%)	(3.6)	(3.9)	(3.8)	(3.9)	(2.5)	(2.1)	(0.8)	(1.7)	(1.2)

Source: Company, Karvy Institutional Research

- Hotel business has been consistently showing sluggish performance in the past few quarters due to the weak economic condition in key international. Meanwhile, its PBIT margin has significantly reduced in the past two quarters.

Exhibit 3: Hotel Business Performance

Hotels	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12
Net Sales (Rs mn)	2,089	2,816	3,003	2,305	2,111	2,787	2,858	2,324	2,170
Net Sales Growth (%)	20.1	13.7	17.2	9.8	1.1	(1.0)	(4.8)	0.8	2.8
Net Sales Mix (%)	3.5	4.6	4.7	3.3	3.0	4.0	3.8	3.0	2.6
PBIT Margin (%)	19.1	31.5	33.2	22.3	20.6	36.5	29.0	11.3	7.1
PBIT Mix (%)	2.1	4.7	5.5	2.7	1.9	4.5	3.9	1.1	0.6

Source: Company, Karvy Institutional Research

- Agribusiness growth was supported by better wheat exports and reduction of leaf tobacco inventory level during the quarter.

Exhibit 4: Agribusiness Performance

Agribusiness	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12
Net Sales (Rs mn)	12,496	10,667	10,818	17,071	14,345	11,394	14,142	16,914	20,239
Net Sales Growth (%)	21.5	17.9	9.5	26.5	14.8	6.8	30.7	(0.9)	41.1
Net Sales Mix (%)	20.9	17.5	17.0	24.5	20.6	16.3	18.7	21.9	24.2
PBIT Margin (%)	16.2	13.2	9.2	9.2	16.6	12.4	7.5	10.1	12.8
PBIT Mix (%)	10.8	7.5	5.6	8.1	10.6	6.3	5.0	7.4	10.0

Source: Company, Karvy Institutional Research

- Paper business is maintaining the sales growth momentum however its sharp rise in PBIT margin in the past two quarters was remarkable.

Exhibit 5: Paper Business Performance

Paper & Packaging	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12
Net Sales (Rs mn)	9,192	8,773	9,170	9,596	10,054	9,764	9,799	10,361	10,590
Net Sales Growth (%)	16.3	8.1	14.2	20.9	9.4	11.3	6.9	8.0	5.3
Net Sales Mix (%)	15.4	14.4	14.4	13.8	14.4	14.0	13.0	13.4	12.6
PBIT Margin (%)	26.7	21.8	21.1	23.7	28.8	23.0	20.0	25.5	26.7
PBIT Mix (%)	13.1	10.2	10.8	11.7	12.9	9.9	9.2	11.4	10.8

Source: Company, Karvy Institutional Research

Strong Q2FY13 Performance

Exhibit 6: Quarterly Financial Performance

Year Ended Mar	Sep-11	Sep-12	YoY Gr%	Jun-12	QoQ Gr%	H1FY12	H1FY13	YoY Gr%
Net Sales	59,742	71,460	19.6	66,522	7.4	117,417	137,982	17.5
Other Operating Income	1,110	806	(27.4)	609	32.4	1,960	1,414	(27.8)
Total Income	60,852	72,266	18.8	67,131	7.6	119,377	139,397	16.8
Total RM cost	23,192	28,644	23.5	25,766	11.2	46,292	54,410	17.5
Gross profit	37,661	43,622	15.8	41,365	5.5	73,084	84,987	16.3
Gross margin %	61.9%	60.4%	-153bps	61.6%	-125bps	61.2%	61.0%	-25bps
Employee Expenses	2,650	2,892	9.1	4,125	(29.9)	6,535	7,017	7.4
Other Expenses	12,821	13,847	8.0	13,557	2.1	24,781	27,404	10.6
Total Expenditures	38,662	45,383	17.4	43,447	4.5	77,608	88,830	14.5
EBITDA	22,190	26,883	21.1	23,683	13.5	41,769	50,566	21.1
EBITDA Margin %	36.5%	37.2%	73bps	35.3%	192bps	35.0%	36.3%	129bps
Other Income	1,808	1,850	2.3	1,768	4.7	3,464	3,617	4.4
Interest	142	233	64.2	138	69.3	342	371	8.4
Depreciation	1,701	1,889	11.0	1,948	(3.0)	3,366	3,837	14.0
PBT	22,155	26,611	20.1	23,366	13.9	41,525	49,977	20.4
Total tax	7,012	8,247	17.6	7,344	12.3	13,055	15,591	19.4
Effective tax %	31.6%	31.0%	-66bps	31.4%	-44bps	31.4%	31.2%	-24bps
Reported PAT	15,143	18,364	21.3	16,021	14.6	28,471	34,386	20.8

Source: Company, Karvy Institutional Research

Financials

Exhibit 7: Profit & Loss Statement

Y/E Mar (Rs mn)	FY11	FY12	FY13E	FY14E	FY15E
Net Revenues	222,737	261,795	302,334	355,033	413,141
% Growth	16.4	17.5	15.5	17.4	16.4
Raw Material	81,184	96,453	106,207	123,619	143,951
Staff	17,319	19,443	22,844	26,499	30,739
Other Expenses	50,026	57,524	68,050	80,194	93,791
Total Expenditures	148,529	173,419	197,100	230,312	268,481
EBITDA	74,208	88,376	105,234	124,721	144,659
% Growth	18.3	19.1	19.1	18.5	16.0
EBITDA Margins (%)	33.3	33.8	34.8	35.1	35.0
Other Income	7,951	11,564	12,147	13,328	14,590
Interest	818	805	764	690	690
Depreciation	6,990	7,455	8,241	8,716	9,366
Profit Before Tax	74,351	91,680	108,377	128,644	149,194
Provision for tax	23,655	28,458	34,139	39,879	46,250
Effective tax rate (%)	31.8	31.0	31.5	31.0	31.0
Reported PAT	50,182	62,580	73,542	88,074	102,261
% Growth	22.3	24.7	17.5	19.8	16.1
Adjusted Net Profit	49,558	62,580	73,542	88,074	102,261
% Growth	20.5	26.3	17.5	19.8	16.1

Source: Company, Karvy Institutional Research

Exhibit 8: Balance Sheet

Y/E Mar	FY11	FY12	FY13E	FY14E	FY15E
Equity Share Capital	7,738	7,818	7,818	7,818	7,818
Reserves & surplus	157,161	186,767	217,104	253,434	295,617
Shareholders' funds	164,899	194,586	224,922	261,253	303,435
Minorities interests	1,408	1,571	2,385	3,199	4,013
Total Debt	1,439	1,587	1,305	1,305	1,305
Capital Employed	167,746	197,744	228,612	265,756	308,753
Net fixed assets	105,372	124,038	132,832	141,216	148,951
Cash & Cash Eq.	24,269	31,301	27,315	53,205	83,973
Net Other current assets	(2,597)	(1,009)	25,029	25,144	26,948
Investments	48,678	52,068	52,827	56,377	59,927
Net Deferred tax Assets	(7,958)	(8,658)	(9,394)	(10,190)	(11,049)
Total Assets	167,746	197,744	228,612	265,756	308,753

Source: Company, Karvy Institutional Research

Exhibit 9: Cash Flow Statement

Rs mn	FY11	FY12	FY13E	FY14E	FY15E
PBT	74,349	91,682	108,377	128,644	149,194
Depreciation	6,991	7,455	8,241	8,716	9,366
Tax	(22,784)	(24,153)	(33,402)	(39,084)	(45,391)
Change in Wkg Cap	807	(7,983)	(26,038)	(116)	(1,804)
CF from Operations	55,087	59,771	58,060	98,974	112,185
Capex	(14,894)	(24,090)	(17,035)	(17,100)	(17,100)
Investments	2,747	(1,044)	(758)	(3,550)	(3,550)
CF from Investing	(8,713)	(19,772)	(17,794)	(20,650)	(20,650)
Change in Equity	9,038	7,650	-	-	-
Change in Debt	(105)	48	(280)	-	-
Dividends & others	(44,564)	(40,671)	(43,206)	(51,744)	(60,078)
CF from Financing	(35,797)	(33,167)	(44,250)	(52,434)	(60,768)
Change in Cash	10,577	6,832	(3,984)	25,890	30,767

Source: Company, Karvy Institutional Research

Exhibit 10: Key Ratios

Y/E Mar	FY11	FY12	FY13E	FY14E	FY15E
Raw Material Cost/Sales (%)	36.4	36.8	35.1	34.8	34.8
Manpower Cost/Sales (%)	7.8	7.4	7.6	7.5	7.4
Operating & Other Cost/Sales (%)	22.5	22.0	22.5	22.6	22.7
Revenue Growth (%)	16.4	17.5	15.5	17.4	16.4
EBITDA Margins (%)	33.3	33.8	34.8	35.1	35.0
Net Income Margins (%)	22.2	23.9	24.3	24.8	24.8
ROCE (%)	44.2	44.7	46.0	46.9	46.9
ROE (%)	30.1	32.2	32.7	33.7	33.7

Source: Company, Karvy Institutional Research

Exhibit 11: Valuation Parameters

Y/E Mar	FY11	FY12	FY13E	FY14E	FY15E
EPS (Rs.)	6.3	8.0	9.4	11.3	13.1
P/E (x)	47.0	37.2	31.7	26.5	22.8
BV (Rs)	21.1	24.9	28.8	33.4	38.8
P/BV (x)	14.1	12.0	10.4	8.9	7.7
EV/EBITDA (x)	30.4	25.4	21.4	17.8	15.1
Fixed assets turnover ratio (x)	2.1	2.1	2.3	2.5	2.8
Net Debt/Equity (x)	(0.1)	(0.2)	(0.1)	(0.2)	(0.3)
EV/Sales	10.1	8.6	7.4	6.3	5.3

Source: Company, Karvy Institutional Research

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Stock Ratings		Absolute Returns
Buy	:	> 15%
Hold	:	5-15%
Sell	:	< 5%

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Disclosures Appendix

Analyst certification

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