Contraire

BONANZA WEALTH MANAGEMENT RESEARCH

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8th Nov. 2021

ITC - Buy

CMP : 228
Target Price : 278
Upside : 22%
Stop Loss : 210 (closing basis)

Investment Thesis

Revenue was up 12% YoY at ~Rs 135.5 bn, EBITDA grew 13% YoY to Rs 46.2 bn and recurring PAT was up 14% YoY at Rs 37 bn. EBITDA margin expanded ~30 bps YoY to 34.1%, as ~35bps YoY decline in gross margin was more than offset primarily by 70 bps YoY decline in other expenses as % of sales. PAT beat was led by higher-than-expected other income.EBITDA margin expanded 142ps to 10% owing to operating leverage, sustained premiumization trends and integrated manufacturing facilities despite scaling up of new categories (Dairy, hygiene range, frozen foods etc). Interestingly, management stated Savlon is expected to achieve consumer spend of Rs 10 bn in FY21 (vs Rs 2.5 bn in FY20). We believe healthy revenue trends to sustain for FMCG in FY22 as well given consumer preference for essentials.Agri revenue was driven by higher wheat supplies for Aashirvaad atta and trading opportunities in rice, soya and wheat exports. While revenue grew 18.5% YoY, EBIT declined by 8% due to 230 bps dip in margin due to weaker mix. During the quarter, leaf exports were impacted by lower volumes and adverse crop/ grade mix. Paperboard, paper and packaging posted 5%/ 15 YoY decline in revenue/ EBIT. Robust growth in exports was partly offset by weak domestic demand. Company witnessed QoQ recovery across segments. Speciality papers – pharma and decorative saw strong growth while liquor, publications, notebooks, and wedding card segments remain subdued. expect hotels business to see gradual demand revival in FY22 as travel related restrictions are lifted.Moreover, management highlighted hotel business had become Ebitda positive in Dec,2020 owing to improved occupancy levels and strong response to F&B Initiatives. business. During Q2FY22 Cigarette recovery has been healthy, and stable taxation remains key to sustaining category growth ahead. The Paper business delivered a strong performance, with Sales/EBIT up 25%/24%. Hotels business continued to witness strong recovery trends with easing travel restrictions leading to higher occupancy levels. FMCG sequential trends indicate a likely pick-up in growth in H2FY22 as the base normalizes.Increasing cost pressure may, however, limit margin gains in the immediate term. Other divisions (Hotels/Agri/Paper) saw strong growth (EBIT up 64%), led by Paper/Hotels.

Stock Details	
Market Cap (RsCr)	287580
BSE Code	500875
NSE Code	ITC
Sector/Index	Tabacco / S&P BSE
Year End	March
52 w.High/Low	183/265
Outstanding shares	1230(cr)
BSE Sensex	60008
NSE Nifty	17898

Shareholding Pattern	
Promoters	00.00%
DIIs	39.60%
FIIs	13.00%
Others	47.40%

Price Performance (%)

	1M	3M	12M
Absolute	2.4	-11.0	-33.4
Rel To Sensex	-3.5	-21.1	-36.9

During the past 5 years,Revenue of grew at a CAGR of 5% while Net Profit grew at a CAGR of 8% in the same period.

Particulars(RsCr)	FY19	FY20	FY21	FY22E	FY23E
Revenue	44433	45136	43568	49275	53710
Net Profit	12464	14401	12733	15575	17295
EPS(Rs)	10.2	11.7	10.6	12.5	13.7
PE(x)	16.7	14.5	16.4	13.9	12.7
Dividend yield (%)	3.4	6.0	5.3	6.3	6.9
FCF yeild (%)	4.1	5.5	4.9	5.4	5.9
PB(x)	3.6	3.3	3.2	3.0	2.8
ROE(%)	22.8	23.6	19.7	23.1	23.5

Key Business Highlights

ITC has used a small portion of its core business operating cashflow to incubate and scale up its FMCG business, which in terms of revenue is now the second largest in India. The FMCG business has built a strong brand portfolio, largely organically, and revenue contribution from FMCG expanded from 20% in FY10 to 28% in FY20. Similarly, its Ebitda contribution expanded from -6% in FY10 to +7% in FY20. ITC's cigarettes business remains a cash cow and is providing capital to support FMCG's big drives. ITC has helped to generate steady free cash flow generates US$1.5bn, a clear path towards the profitable scaling-up of the FMCG business, and improving capital allocation provide a much-needed supportive narrative for ITC against a backdrop of subdued valuations including 5.4% free cashflow yield, 6.3% dividend yield in FY22E.

Risk & Concern

Increase in cigarette taxes higher than inflation or implementation of plain packaging.

Stricter norms to curb tobacco consumption.

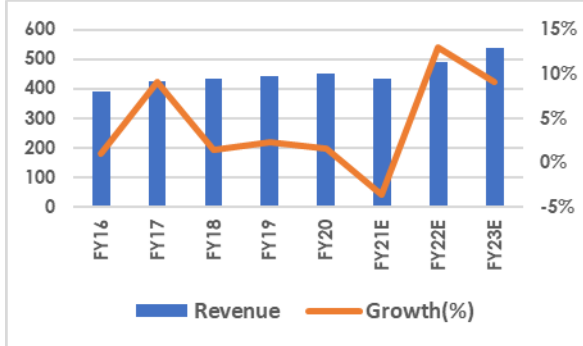
Stock overhang from the possible sale of the government's 7.9% stake in ITC (that it owns through the Specified Undertaking of Unit Trust of India -SUUTI)

Valuation

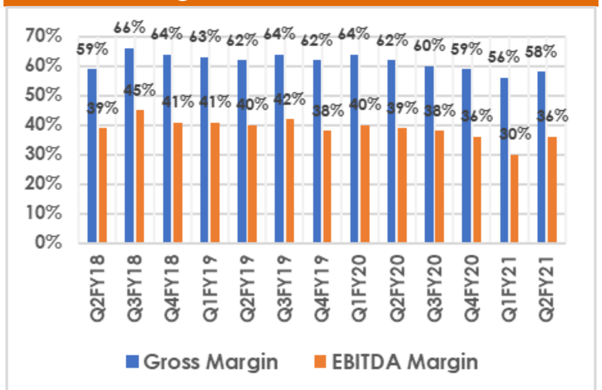
it is witnessing smart recovery in metros/ large towns after a soft H1,metro markets remain relatively more impacted vs pre-Covid levels,focused portfolio/ market interventions, small packs, innovative and competitive offerings aided market share gains; (revenue at 9x compared to nearest competition). ITC can comfortably pass any tax-hikes to customers by raising prices. Business recovery in Cigarette business has been better than expected while Hotel segment recovery is likely to be on time. ITC's cigarette business allows the company to have a consistent strong cash flow (FY17-20 FCF CAGR 18%, FY20 FCF Rs.11600Cr) which should continue to help FMCG business, good management, High Free cash flow yield (5.4%), high dividend yield (6.3%) and strong business moat, that gives confidence to call it a high conviction buy at inexpensive valuation 20x its FY23E EPS. we expect ITC stock to see decent performance.

Graphs & Charts

Revenue CAGR of 5% between FY19 -FY23E

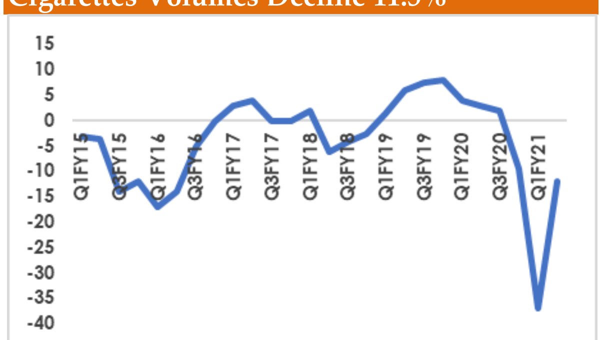


EBITDA margin contracted in 2QFY21



Contribution of cigarettes to revenue decline

Cigarettes Volumes Decline 11.5%



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Disclosure:

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