

ITC

BUY

On a steady path

### Summary

We attended ITC Limited (ITC) analyst meet. Company aims to achieve double digit revenue and operating profit growth in near term. Cigarette business is witnessing improvement in revenue mix driven by new launches (new products contribute 11% to volume, while assortment increased 2x during last 8 years). Rich revenue mix should help in offsetting impact on cigarette volume growth due to tax driven price hikes taken earlier/if-any-in-future. On FMCG business; ITC expects to maintain EBITDA margin despite raw material cost inflation. In hotel business; company expects leisure segment to outperform in near term while business travel continues to face growth headwinds due to rise in virtual reality. ITC expects inbound tourism to do well in near term. On the IT business; ITC sounded positive on separate listing. Capex is expected to be c. 30bn p.a. for next 3 years. We maintain our estimates. At current price; we have a BUY rating on the stock.

### Key Highlights and Investment Rationale

#### ■ Premium products to drive revenue growth in cigarette business

Cigarette business is likely to do well if tax rates are stable at current levels driven by higher contribution from premium products. In Classic brand; 4 new variants launched during last 5 years now contributes c. 25% to portfolio while under Gold Flake brand; new launches over last 5 year account for 10% of the portfolio. ITC has doubled overall assortment of cigarette business over last 8 years.

#### ■ FMCG business is stable; hotel to be divested; IT could be listed separately

FMCG business will continue to benefit from growth in power brands driven by increase in distribution reach and penetration. ITC expects to maintain EBITDA margin at 9% despite inflation in raw material cost. ITC remains committed to divest the Hotel business only after industry is back to normalcy. On Infotech business; ITC is open to the possibility of separate listing.

TP **Rs299**CMP **Rs228**Potential upside/downside **+31%**Previous Rating **BUY**

### Price Performance (%)

	-1m	-3m	-12m
Absolute	(2.1)	5.7	5.7
Rel to Sensex	2.2	5.9	(19.9)

### V/s Consensus

EPS (Rs)	FY22E	FY23E	FY24E
IDBI Capital	11.7	13.5	14.9
Consensus	12.3	13.8	15.0
% difference	(5.2)	(2.2)	(0.4)

### Key Stock Data

Bloomberg / Reuters	ITC IN / ITC.BO
Sector	FMCG
Shares o/s (mn)	12,322
Market cap. (Rs mn)	2,813,199
Market cap. (US\$ mn)	36,741
3-m daily average value (Rs mn)	--
52-week high / low	Rs 265 / 197
Sensex / Nifty	58,117 / 17,325

### Shareholding Pattern (%)

Promoters	0.0
FII	13.6
DII	39.9
Public	46.6

### Financial snapshot

(Rs mn)

Year	FY20	FY21	FY22E	FY23E	FY24E
Revenue	4,56,197	4,51,764	5,24,146	5,76,234	6,33,902
EBITDA	1,79,044	1,54,616	1,77,942	2,07,744	2,30,294
EBITDA(%)	39.2	34.2	33.9	36.1	36.3
Adj.PAT	1,51,362	1,29,864	1,44,159	1,66,532	1,83,427
EPS(Rs)	12.3	10.6	11.7	13.5	14.9
EPSGrowth(%)	21.1	(14.3)	10.9	15.5	10.1
PE(x)	18.5	21.6	19.5	16.9	15.3
DividendYield(%)	2.5	6.6	4.2	4.9	5.3
EV/EBITDA(x)	15.3	17.9	15.5	13.2	11.8
RoE(%)	24.8	21.1	23.9	26.4	27.7
RoCE(%)	25.9	21.8	25.6	28.8	30.5

Source: IDBI Capital Research;

## Analyst meet key takeaways

### On Cigarette business;

- In cigarette business ITC expects better revenue mix to offset impact on volume due to higher prices.
- Compensation Cess is not likely to be extended beyond 2022.
- During 2011-16 tax was bigger concern for cigarette business. GST was intended to be revenue neutral but it ended-up being on the higher side.
- On electronic nicotine; India has put a ban as it was a gateway product. As per WHO; there is no adequate evidence of harm reduction from usage of electronic nicotine.
- 4 new variants of Classic brand launched over last 5 years contribute to ~25 % of the portfolio.
- Under Gold Flake brand; new launches in the last 5 years account for 10% of the Portfolio. Also, 10+ new product launched during last 18 months – thus aiming for rapid diversification into new segments.
- 11% of volume is from new products.
- Assortment more than doubled in last 8 years.

### On FMCG business;

- ITC expects to be able to maintain 9% EBITDA margin despite cost inflation .
- The company expects general trade to remain dominant despite rise in modern trade. ITC would be helping kirana stores to digitize, provide access to credit, and develop lean inventory models.
- ITC has a dedicated team to drive growth in the e-commerce channel (owned and operated by the company). Overall business from ecommerce rose 3x in 1HFY22 compared to 1HFY20.
- Aashirvaad brand will only get into value added products (and not in commodity like; lentils, sugar etc).
- ITC has to stock higher inventory of wheat during 1H as per processing requirement for the Atta business. Classmate business is more credit heavy and hence generates higher receivables unlike other business segments.
- Company expects more M&A in D2C brands going forward.

**On Hotel business;**

- Business travel has reached 40-50% of pre-covid while occupancy recovered 100%.
- ARR stands at 70% of pre-covid.
- Leisure destination is doing well. While business travel is still a laggard.
- Due to COVID, there is natural preference towards safe brands. Hence, branded hotels like ITC are likely to do well.
- ITC expects WFH and virtual reality to last for long period of time. Hence, leisure segment in hotels are likely to outperform.
- Outbound tourism has higher market share compared to inbound tourism. ITC expects rise in inbound tourism going forward.

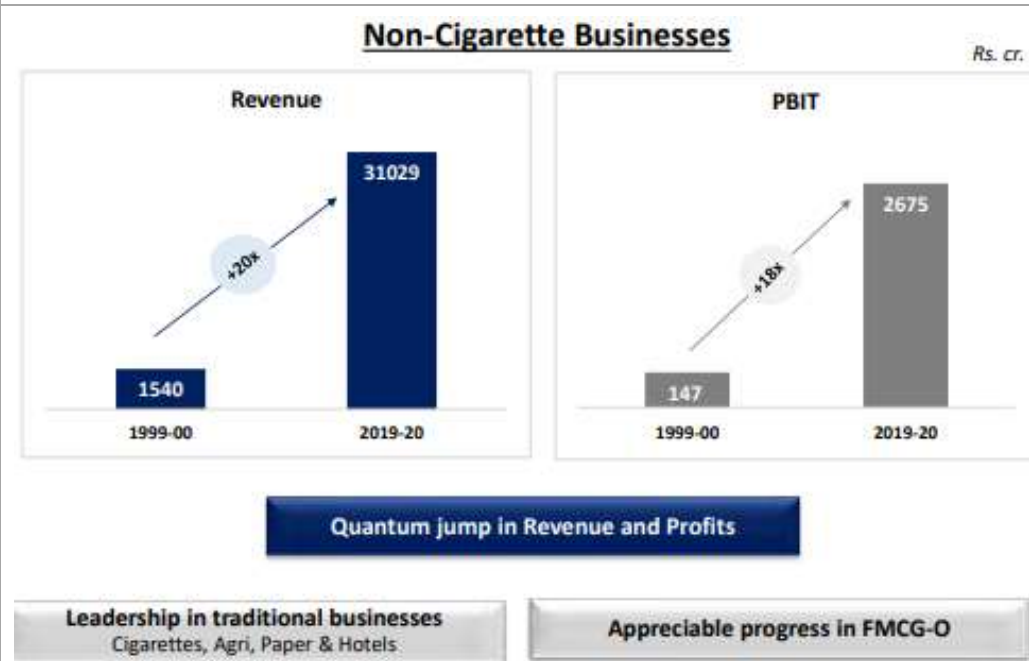
**On Infotech business;**

- ITC is open for merger and acquisition opportunities.
- The company also sounded positive on chances of the Infotech business getting listed separately.

**Capex plans;**

- Over next 3 years; ITC expect to spend c. Rs 90-100 bn, which is c. Rs 30bn p.a. (80% higher than depreciation).
- ITC expects to spend; 35-40% of the capex on FMCG, 25-30% on paperboard and packaging business, 10% in hotel business and rest in Agri business, digital and ESG.
- Hotel business is likely to consume lower capex going forward as the company is using asset-right model for expansion.

Exhibit 1: ITC revenue performance of non-cigarette business over last 2 decades



Source: Company; IDBI Capital Research

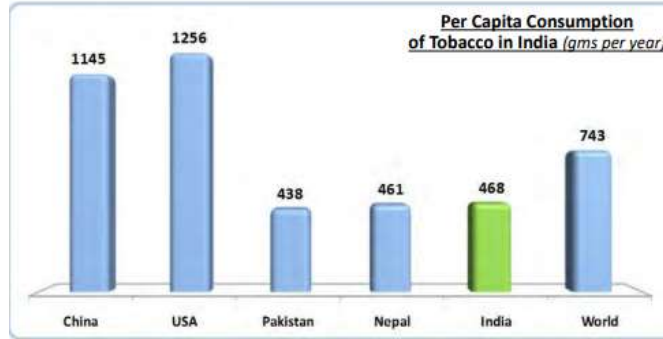
Exhibit 2: Market position of power brands



Source: Company; IDBI Capital Research

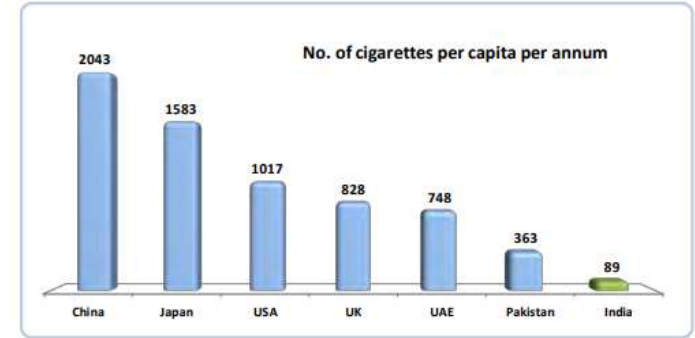
**Exhibit 3: Unique pattern of tobacco consumption in India**

**Per Capita Tobacco consumption @ ~60% of World Average**



Source: World Cigarettes – ERC Statistics, Tob Board & Industry Estimates – gms/Yr

**Per Capita Cigarette Consumption @ 11% of World average**



Source: Tobacco Atlas, 6<sup>th</sup> Edition, ACS 2018

**India accounts for over 18% of world population; share of world cigarette consumption is less than 2%**

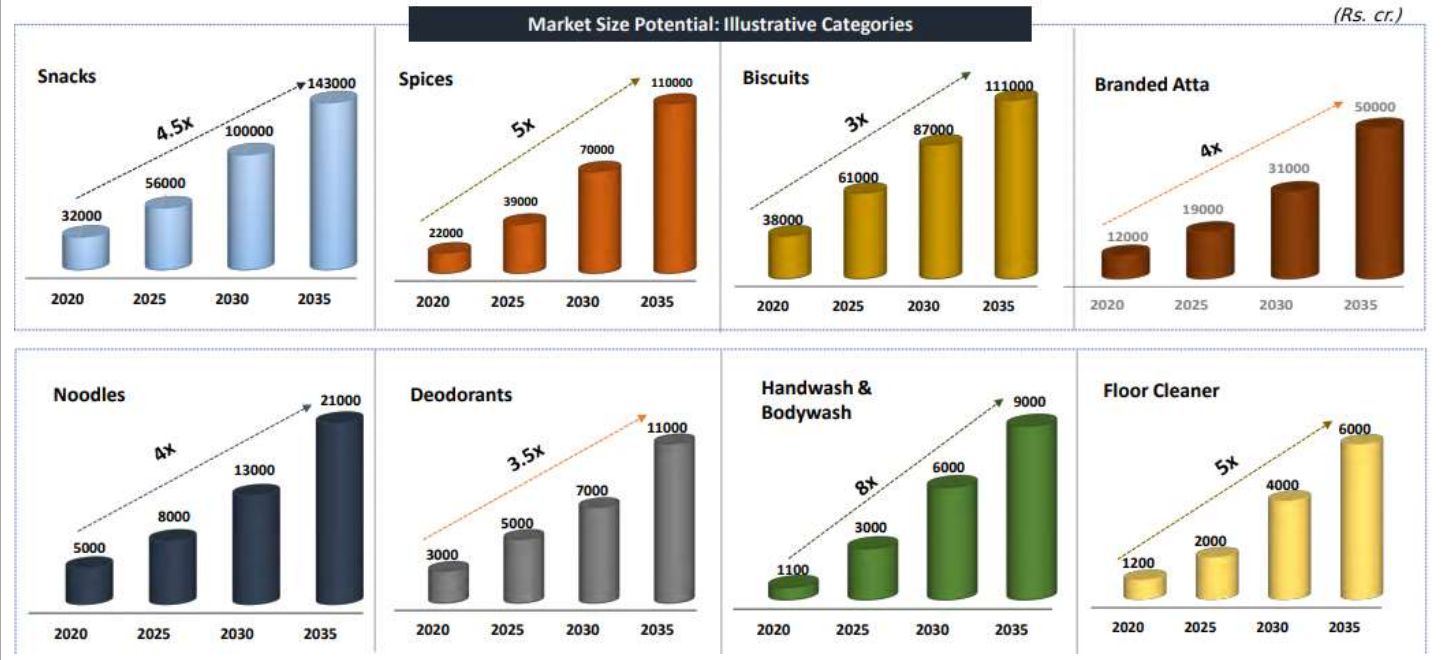
Source: Company; IDBI Capital Research

**Exhibit 4: Cigarette business; leading brand in every market segment**

		Insignia   Classic Blue Leaf				
	<small>MRP / Pack of 10s</small> <b>Rs.150 &amp; Above</b>	<b>Classic</b> (9 Offers)	<b>Gold Flake</b> (8 offers)	<b>India Kings</b> (2 Offers)	<b>B&amp;H   555</b> (3 Offers)	
	<b>Rs.110 – Rs.140</b>	<b>Gold Flake</b> (3 Offers)	<b>Classic</b> (2 Offers)	<b>American Club</b> (5 Offers)	<b>Wills   Flake</b> (3 Offers)	
	<b>Rs.70 – Rs.100</b>	<b>Gold Flake</b> (10 Offers)	<b>Wills</b> (3 Offers)	<b>Flake   Scissors</b> (5 Offers)	<b>Player's</b> (2 Offers)	<b>Capstan   Bristol</b> (4 Offers)
	<b>Rs.40 - Rs. 60</b>	<b>Gold Flake</b> (11 Offers)	<b>Flake</b> (11 Offers)	<b>Capstan</b> (4 Offers)	<b>Wave</b> (5 Offers)	
		<b>Berkeley</b> (2 Offers)	<b>Royal</b> (4 Offers)	<b>Duke</b> (2 Offers)	<b>Navy Cut</b> (5 Offers)	<b>Silk Cut</b> (4 Offers)

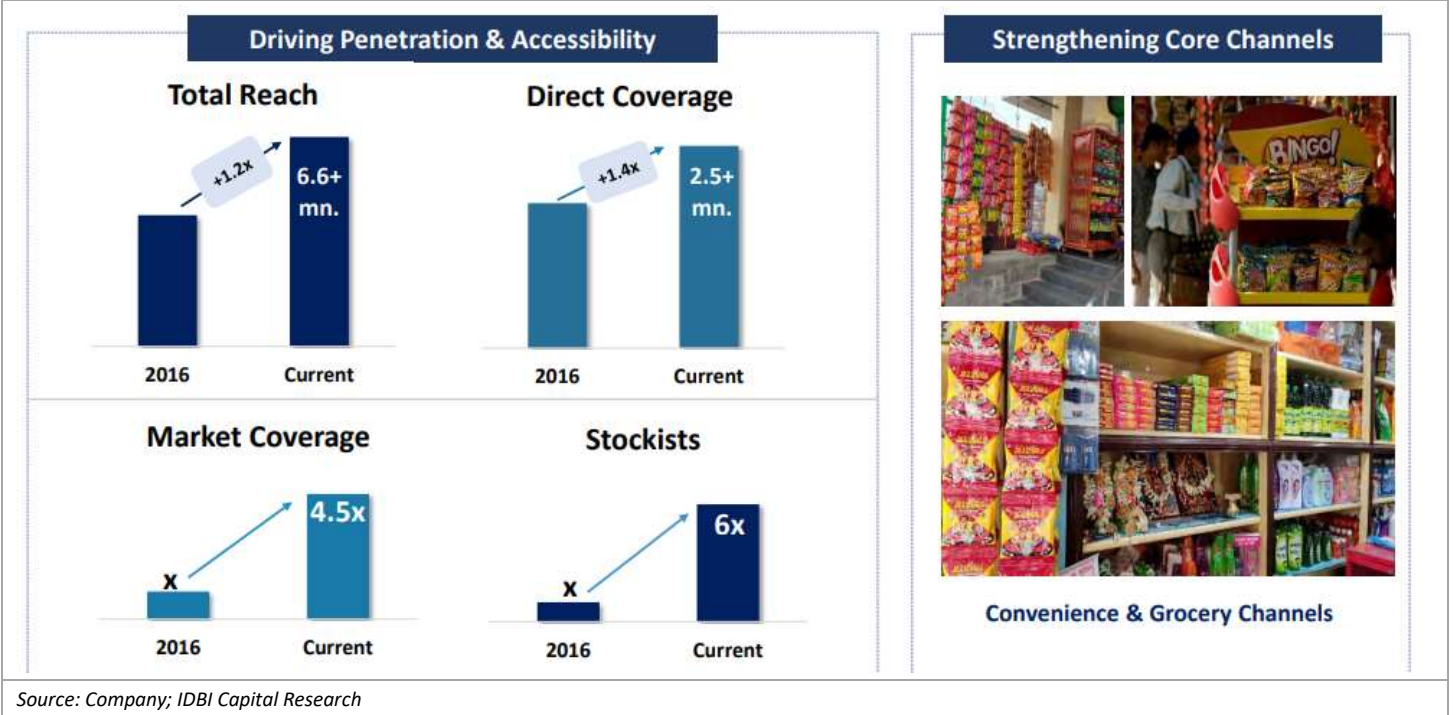
Source: Company; IDBI Capital Research

**Exhibit 5: Addressable market expansion potential**

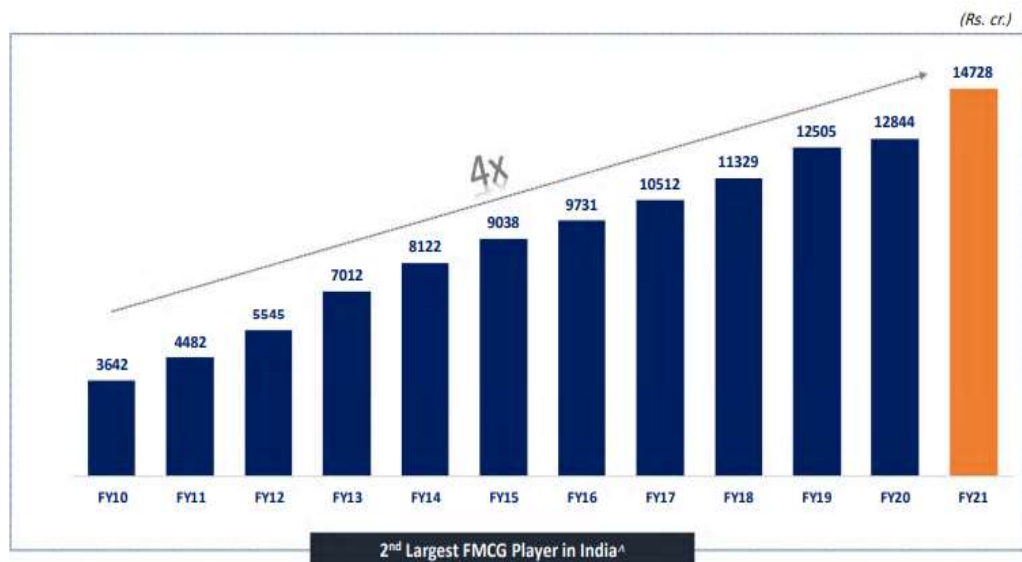


Source: Company; IDBI Capital Research

Exhibit 6: Evolution of distribution strength

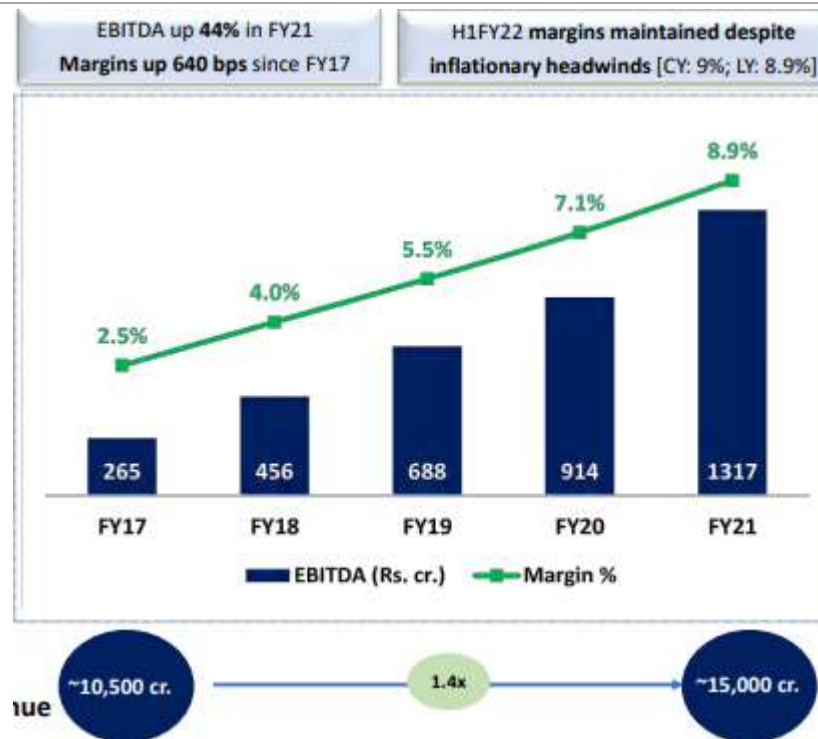


**Exhibit 7: ITC's FMCG business grew at 13% CAGR (vs 10% by FMCG peers) during last 10 years**



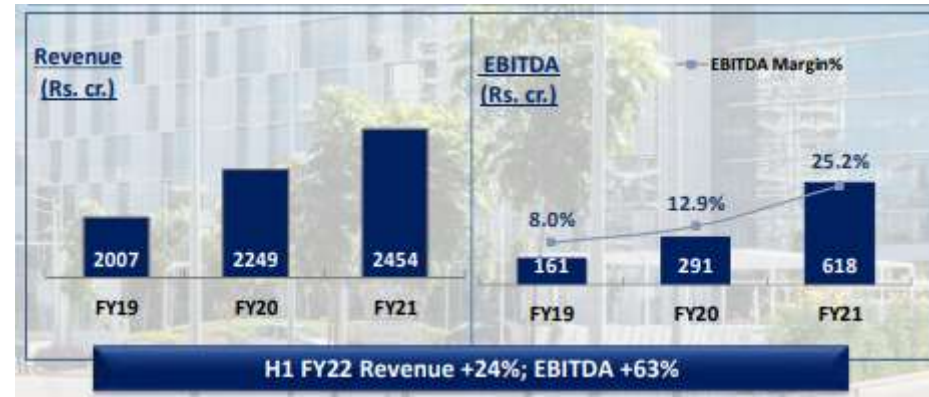
Source: Company; IDBI Capital Research

**Exhibit 8: On track to sustain improvement in profitability**



Source: Company; IDBI Capital Research

Exhibit 9: ITC Infotech; addressing clients across 29 countries including 60+ fortune listed companies



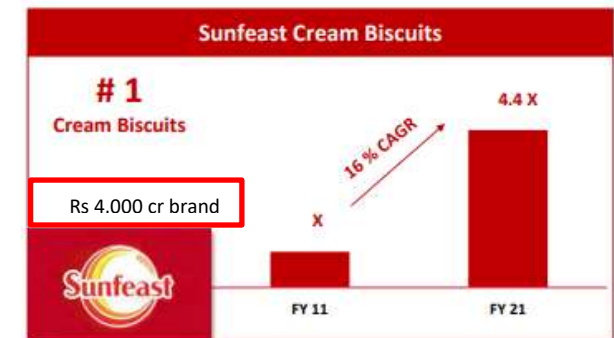
Source: Company; IDBI Capital Research

Exhibit 10: India's no. 1 brand in <4 years of launch



Source: Company; IDBI Capital Research

Exhibit 11: Bounce; India's no. 1 cream biscuit brand



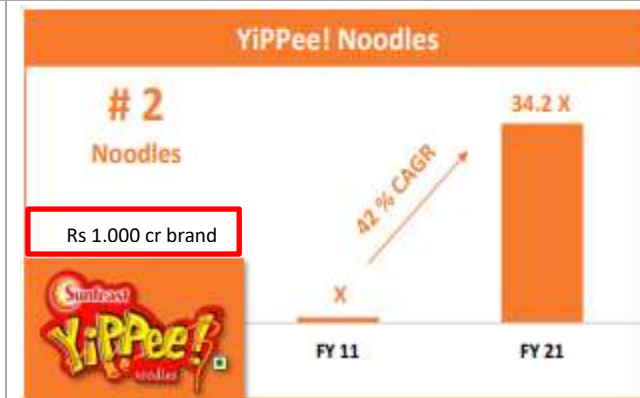
Source: Company; IDBI Capital Research

**Exhibit 12: Bingo; no. 1 finger snacks brand in India**



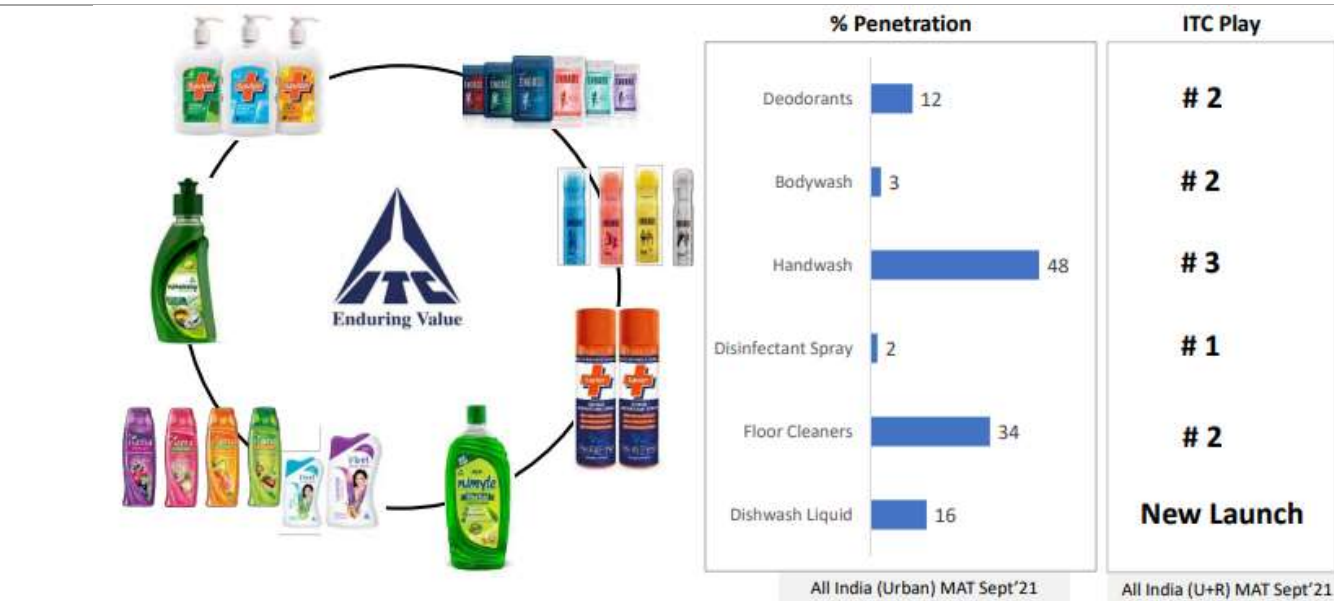
Source: Company; IDBI Capital Research

**Exhibit 13: Yippee; no. 2 noodles brand in India**



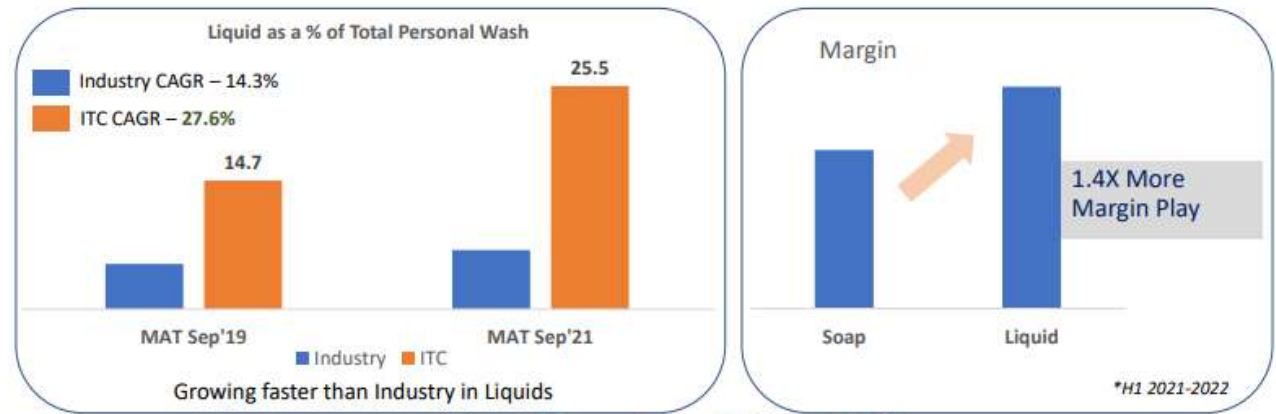
Source: Company; IDBI Capital Research

**Exhibit 14: Detail of penetration and ITC's positioning in fast growing categories**



Source: Company; IDBI Capital Research

**Exhibit 15: ITC's market share in liquids (personal wash)**



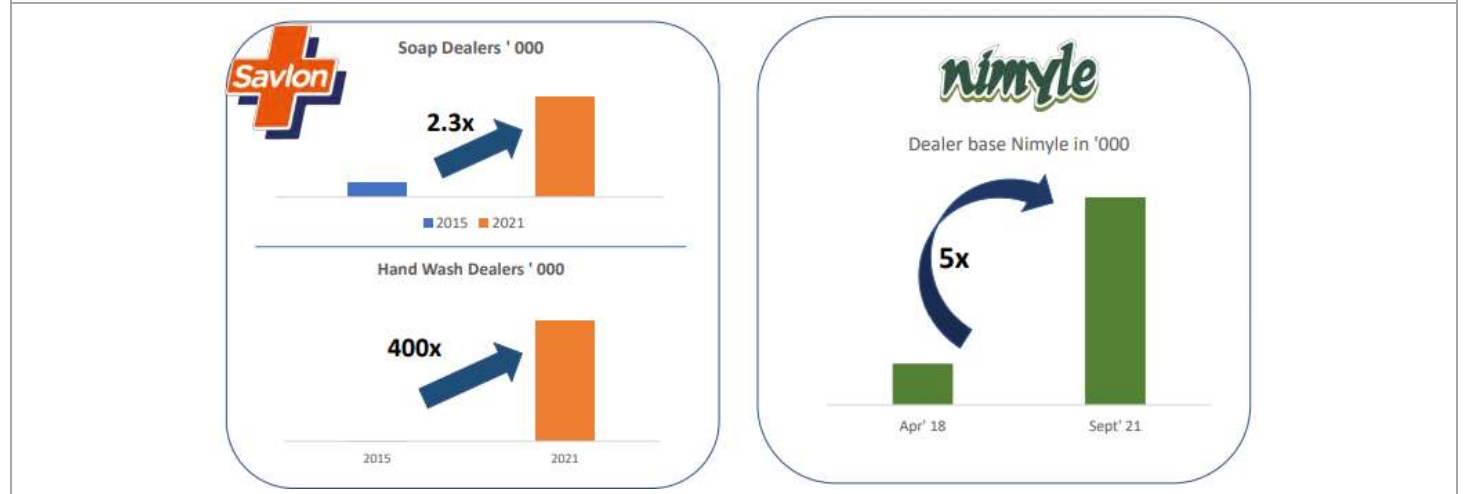
Source: Company; IDBI Capital Research

Exhibit 16: Value growth in brand which has been acquired historically



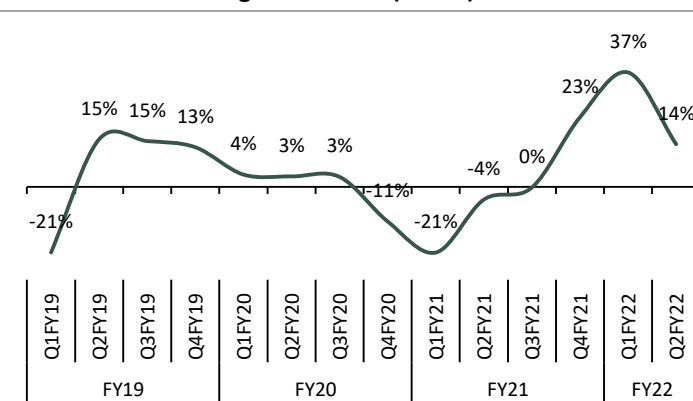
Source: Company; IDBI Capital Research

Exhibit 17: Distribution strength of ITC helped scaling up of Savlon and Nimyle brands



Source: Company; IDBI Capital Research

**Exhibit 18: Revenue growth trend (% YoY)**



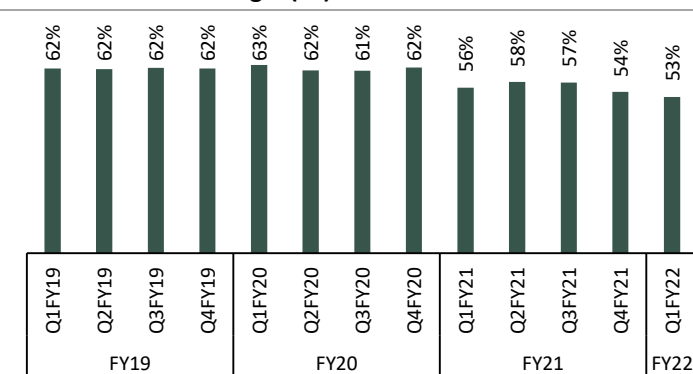
Source: Company; IDBI Capital Research

**Exhibit 19: Segmental revenue growth trend**

Revenue (%YoY)	FMCG: Cigarette	FMCG: Others	Hotel	Agri-business	Paperboard, paper and packaging
Q2FY20	6%	4%	18%	19%	10%
Q3FY20	5%	3%	22%	9%	1%
Q4FY20	-6%	-3%	-9%	-10%	-5%
Q1FY21	-29%	10%	-94%	4%	-33%
Q2FY21	-4%	15%	-81%	13%	-7%
Q3FY21	4%	8%	-57%	18%	-5%
Q4FY21	14%	16%	-38%	79%	14%
Q1FY22	33%	10%	464%	9%	54%
Q2FY22	10%	6%	260%	-7%	25%

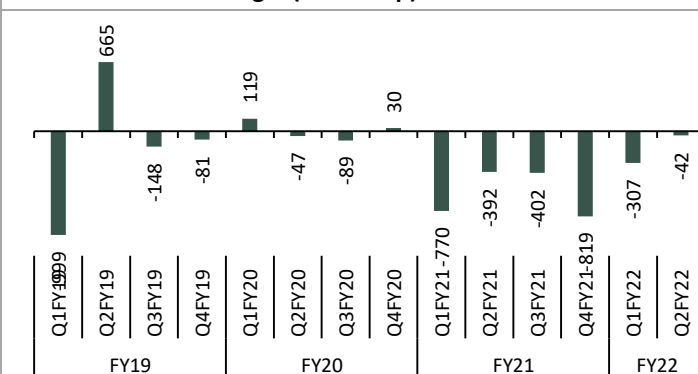
Source: Company; IDBI Capital Research

**Exhibit 20: Gross Margin (%)**

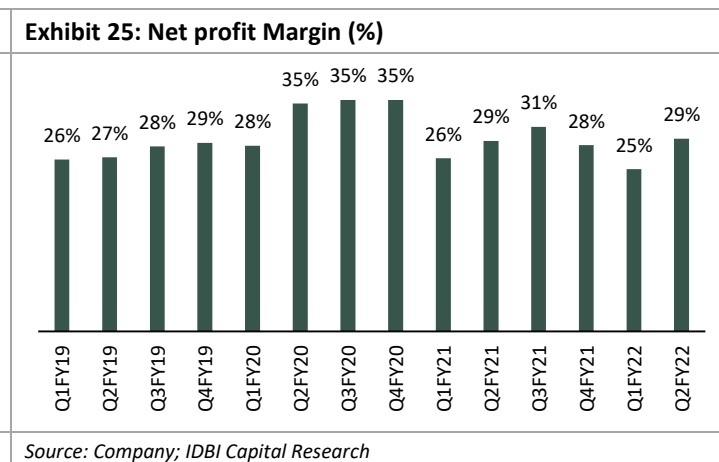
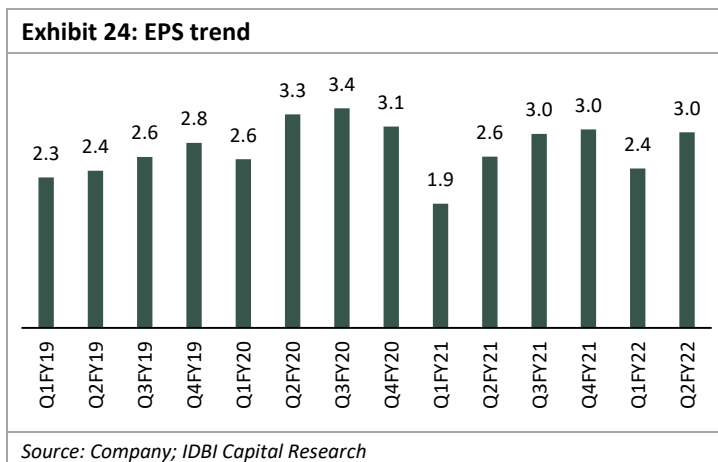
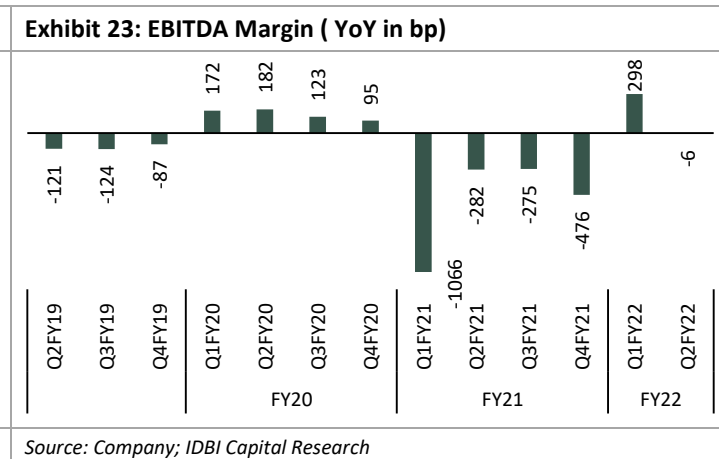
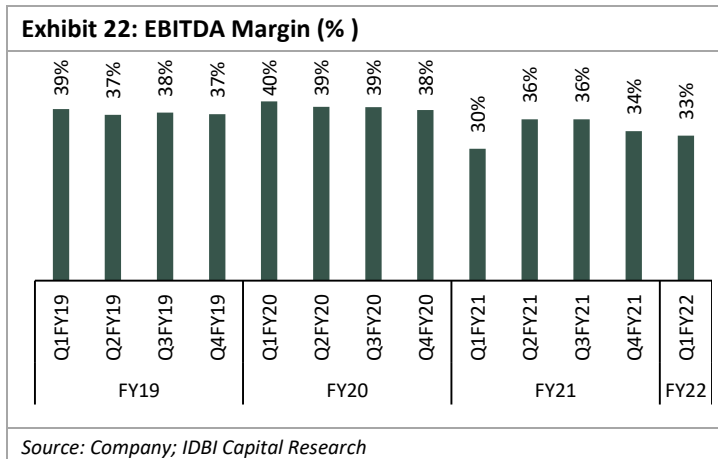


Source: Company; IDBI Capital Research

**Exhibit 21: Gross Margin (YoY in bp)**



Source: Company; IDBI Capital Research



## Financial Summary

### Profit & Loss Account

(Rs mn)

Year-end: March	FY21	FY22E	FY23E	FY24E
<b>Net sales</b>	<b>4,51,764</b>	<b>5,24,146</b>	<b>5,76,234</b>	<b>6,33,902</b>
<i>Growth (%)</i>	<i>(1.0)</i>	<i>16.0</i>	<i>9.9</i>	<i>10.0</i>
Operating expenses	(2,97,148)	(3,46,204)	(3,68,490)	(4,03,608)
<b>EBITDA</b>	<b>1,54,616</b>	<b>1,77,942</b>	<b>2,07,744</b>	<b>2,30,294</b>
<i>Growth (%)</i>	<i>(13.6)</i>	<i>15.1</i>	<i>16.7</i>	<i>10.9</i>
Depreciation	(15,596)	(17,943)	(19,471)	(21,153)
<b>EBIT</b>	<b>1,39,020</b>	<b>1,59,999</b>	<b>1,88,273</b>	<b>2,09,141</b>
Interest paid	(475)	(498)	(523)	(550)
Other income	32,497	33,226	34,887	36,631
<b>Pre-tax profit</b>	<b>1,71,043</b>	<b>1,92,726</b>	<b>2,22,636</b>	<b>2,45,223</b>
Tax	(41,179)	(48,567)	(56,104)	(61,796)
<i>Effective tax rate (%)</i>	<i>24.1</i>	<i>25.2</i>	<i>25.2</i>	<i>25.2</i>
Minority Interest	-	-	-	-
<b>Net profit</b>	<b>1,29,864</b>	<b>1,44,159</b>	<b>1,66,532</b>	<b>1,83,427</b>
Exceptional items	-	-	-	-
<b>Adjusted net profit</b>	<b>1,29,864</b>	<b>1,44,159</b>	<b>1,66,532</b>	<b>1,83,427</b>
<i>Growth (%)</i>	<i>(14.2)</i>	<i>11.0</i>	<i>15.5</i>	<i>10.1</i>
<i>Shares o/s (mn nos)</i>	<i>12,309</i>	<i>12,320</i>	<i>12,320</i>	<i>12,320</i>

### Cash Flow Statement

(Rs mn)

Year-end: March	FY21	FY22E	FY23E	FY24E
Pre-tax profit	1,71,043	1,92,726	2,22,636	2,45,223
Depreciation	15,558	17,943	19,471	21,153
Tax paid	(39,566)	(48,567)	(56,104)	(61,796)
Chg in working capital	(3,948)	175	(7,378)	(8,168)
Other operating activities	(28,147)	498	523	550
<b>Cash flow from operations (a)</b>	<b>1,14,940</b>	<b>1,62,775</b>	<b>1,79,149</b>	<b>1,96,961</b>
Capital expenditure	(15,821)	(28,697)	(24,263)	(26,693)
Chg in investments	88,039	-	-	-
Other investing activities	(7,239)	-	-	-
<b>Cash flow from investing (b)</b>	<b>64,979</b>	<b>(28,697)</b>	<b>(24,263)</b>	<b>(26,693)</b>
Equity raised/(repaid)	2,907	-	-	-
Debt raised/(repaid)	(4)	4	-	-
Dividend (incl. tax)	(1,86,293)	(1,18,211)	(1,36,556)	(1,50,410)
Chg in minorities	-	-	-	-
Other financing activities	(399)	(2,251)	(523)	(550)
<b>Cash flow from financing (c)</b>	<b>(1,83,789)</b>	<b>(1,20,458)</b>	<b>(1,37,080)</b>	<b>(1,50,959)</b>
<b>Net chg in cash (a+b+c)</b>	<b>(3,871)</b>	<b>13,620</b>	<b>17,806</b>	<b>19,309</b>

## Balance Sheet

(Rs mn)

Year-end: March	FY21	FY22E	FY23E	FY24E
Net fixed assets	2,44,049	2,54,803	2,59,595	2,65,134
Investments	1,33,269	1,33,269	1,33,269	1,33,269
Other non-curr assets	20,333	20,333	20,333	20,333
<b>Current assets</b>	<b>3,18,154</b>	<b>3,27,246</b>	<b>3,55,772</b>	<b>3,87,515</b>
Inventories	94,709	90,038	98,986	1,08,892
Sundry Debtors	20,904	22,976	25,260	27,787
Cash and Bank	40,015	51,704	68,999	88,308
<b>Total assets</b>	<b>7,15,805</b>	<b>7,35,651</b>	<b>7,68,969</b>	<b>8,06,251</b>
<b>Shareholders' funds</b>	<b>5,90,046</b>	<b>6,15,994</b>	<b>6,45,970</b>	<b>6,78,987</b>
Share capital	12,309	12,309	12,309	12,309
Reserves & surplus	5,77,737	6,03,686	6,33,661	6,66,678
<b>Total Debt</b>	<b>53</b>	<b>56</b>	<b>56</b>	<b>56</b>
Secured loans	53	56	56	56
Other liabilities	23,965	22,212	22,212	22,212
<b>Curr Liab &amp; prov</b>	<b>1,01,742</b>	<b>97,388</b>	<b>1,00,730</b>	<b>1,04,996</b>
Current liabilities	1,00,051	95,697	99,551	1,03,816
Provisions	1,691	1,691	1,179	1,179
<b>Total liabilities</b>	<b>1,25,760</b>	<b>1,19,657</b>	<b>1,22,999</b>	<b>1,27,264</b>
<b>Total equity &amp; liabilities</b>	<b>7,15,805</b>	<b>7,35,651</b>	<b>7,68,969</b>	<b>8,06,251</b>
<b>Book Value (Rs)</b>	<b>48</b>	<b>50</b>	<b>52</b>	<b>55</b>

Source: Company; IDBI Capital Research

## Financial Ratios

Year-end: March	FY21	FY22E	FY23E	FY24E
Adj. EPS (Rs)	10.6	11.7	13.5	14.9
Adj. EPS growth (%)	(14.3)	10.9	15.5	10.1
EBITDA margin (%)	34.2	33.9	36.1	36.3
Pre-tax margin (%)	37.9	36.8	38.6	38.7
ROE (%)	21.1	23.9	26.4	27.7
ROCE (%)	21.8	25.6	28.8	30.5
<b>Turnover &amp; Leverage ratios (x)</b>				
Asset turnover (x)	0.6	0.7	0.8	0.8
Leverage factor (x)	1.2	1.2	1.2	1.2
Net margin (%)	28.7	27.5	28.9	28.9
Net Debt/Equity (x)	(0.1)	(0.1)	(0.1)	(0.1)
<b>Working Capital &amp; Liquidity ratio</b>				
Inventory days	77	63	63	63
Receivable days	17	16	16	16
Payable days	51	41	42	42

## Valuation

Year-end: March	FY21	FY22E	FY23E	FY24E
P/E (x)	21.6	19.5	16.9	15.3
Price / Book value (x)	4.8	4.6	4.4	4.1
PCE (x)	19.3	17.4	15.1	13.7
EV / Net sales (x)	6.1	5.3	4.8	4.3
EV / EBITDA (x)	17.9	15.5	13.2	11.8
Dividend Yield (%)	6.6	4.2	4.9	5.3



# Notes

Dealing

(91-22) 6836 1111

dealing@idbicapital.com

**Key to Ratings Stocks:****BUY:** 15%+; **HOLD:** -5% to 15%; **SELL:** -5% and below.**IDBI Capital Markets & Securities Ltd.****Equity Research Desk**

6th Floor, IDBI Tower, WTC Complex, Cuffe Parade, Colaba, Mumbai – 400 005. Phones: (91-22) 2217 1700; Fax: (91-22) 2215 1787; Email: info@idbicapital.com

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