FMCG

ICICI direct Research

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Volume growth still elusive; margins up sequentially

During the quarter, crude prices witnessed a sharp correction. This, along with a decline in palm oil prices earlier gave FMCG companies the opportunity to take price cuts & grammage restoration to pass on the benefit. FMCG companies are taking price cuts mainly to perk up volumes specifically in rural regions. We estimate 8.4% sales growth in our coverage universe still largely led by pricing growth. Though HUL has taken 5-10% price cuts in soaps & detergents in October-2022, we estimate 12.6% sales growth for the company still driven by 7% pricing growth and 5% volume growth. We estimate Nestlé will witness 12.3% revenue growth largely led by price hikes taken in last one year and volume growth contributed by improved supply of Maggi Noodles after capacity addition.

We also estimate strong growth for ITC's FMCG business led by price hikes, strong traction in discretionary categories (due to high mobility) & strong growth in education & stationary business. Dabur and Marico, in our coverage universe, are expected to see dismal sales growth with subdued demand in hair oils, health supplements (high base & late winters) & currency depreciation in international territories. This is despite edible oil brand Saffola (Marico) seeing strong recovery and double-digit volume growth after aggressive price cuts. Tea segment for HUL (F&B) & Tata Consumer is likely to see slower growth due to absence of pricing & high base quarter. Tata Consumer's foods business (salt & pulses) is expected to see strong growth largely led by prices. The 9% growth in Colgate is mainly due to slower growth in base quarter. Oral care category has been saturated with 90% penetration levels and the growth in the category is only contributed by naturals & premium segments. ITC is expected to witness strong growth in cigarettes volumes with moderation in growth rates to 7% during the quarter (~20% in H1). VST is also likely to see moderation in volume growth to 5% (9% in H1). With the stabilisation of commodity prices, volume growth has picked up in bits & pieces. However, FMCG companies are expected to increase their spends towards A&P to propel volumes, going forward.

Margins to improve sequentially

There is a mixed trend in RM prices for FMCG companies given imported RMs like palm, crude & related commodities have seen sharp decline but agri commodities like wheat, rice, coffee & milk prices continued to remain firm. Crude prices have come off 30% from peak in May 2022. However, it is only 10% below average prices in Q2FY23 and still 11% higher compared to average of Q3FY22. Moreover, the rupee depreciated ~10% in one year. We estimate sequential improvement in operating margins to the tune of 50-250 bps but on a YoY basis, it is expected to still contract by 50-150 bps for HUL, Colgate, Dabur, Nestlé & Zydus Wellness. We estimate net profit growth of 11.2% (adjusting for one-off factor for Nestlé PAT growth estimated at 8.8%).

Exhibit 1: Estimates for Q3FY23E: (FMCG) (₹ crore)

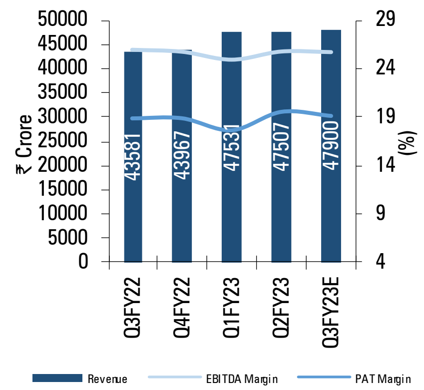
Company	Revenue	Change (%)		EBITDA	Change (%)		PAT	Change (%)	
	Q3FY23E	YoY	QoQ	Q3FY23E	YoY	QoQ	Q3FY23E	YoY	QoQ
Colgate Palmolive	1,394.2	8.9	0.5	412.1	8.3	1.0	277.2	9.9	-0.3
Dabur India Ltd	3,069.8	4.4	2.8	589.0	-6.1	-2.0	479.7	-4.9	-2.3
HUL	14,743.2	12.6	-0.1	3,567.6	8.8	5.6	2,519.2	12.3	-3.7
ITC	17,794.9	5.9	3.7	5,743.5	12.6	-2.1	4,503.7	8.4	0.8
Marico Ltd	2,480.2	3.0	-0.6	467.6	8.5	8.0	335.4	5.8	9.3
Nestle India	4,199.2	12.3	-8.5	911.4	5.3	-9.8	630.6	63.1	-5.6
Tata Consumer	3,445.7	7.4	2.5	472.3	2.3	8.9	321.3	10.8	-17.5
VST Industries	332.9	1.4	-3.0	112.4	3.0	20.9	89.2	7.8	-3.2
Zydus Wellness	439.7	13.3	2.4	31.6	-2.1	94.4	23.0	1.4	179.7
Total	**47,899.8**	**8.4**	**0.8**	**12,307.4**	**9.0**	**0.6**	**9,179.5**	**11.2**	**-1.5**

Source: Company, ICICI Direct Research

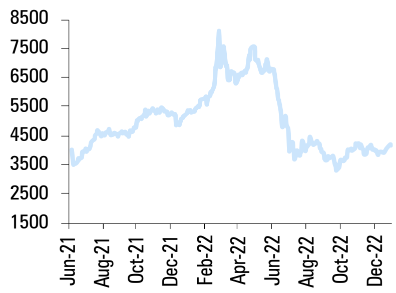
Result Preview

ICICI Securities – Retail Equity Research

Topline & Profitability (Coverage Universe)



Palm oil prices trend (MYR/tonne)



* MYR – Malaysian Ringgit

Operating margins FMCG Coverage (%)

Company	EBITDA Margin %				
	Q3'22	Q4'22	Q1'23	Q2'23	Q3'23E
Colagte	29.7	33.0	27.2	29.4	29.6
Dabur	26.9	18.0	19.3	20.1	19.2
HUL	25.0	24.1	22.8	22.9	24.2
ITC	30.4	31.8	30.8	34.2	32.3
Marico	17.9	16.0	20.6	17.3	18.9
Nestle	23.2	23.2	20.3	22.0	21.7
Tata Cons.	14.4	14.0	13.7	12.9	13.7
VST Ind.	33.2	35.1	37.5	27.1	33.8
Zydus Welln	13.0	22.1	21.3	3.8	7.2
FMCG Total	**25.9**	**25.7**	**24.9**	**25.8**	**25.7**

Top Picks

ITC
Tata Consumer Products
Dabur

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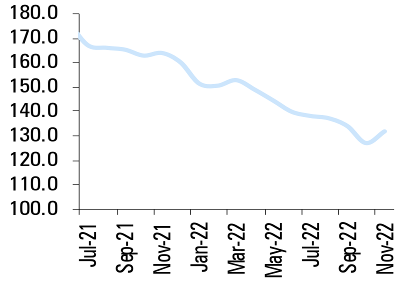
Exhibit 2: Company Specific Views (FMCG)

Company	Remarks
Colgate	Colgate is likely to post revenue growth of 8.9% largely led by price hikes taken in the last one year. We expect 3% volume growth & 6% pricing growth during the quarter. With softening of crude based packaging costs, gross margin is expected to improve sequentially by 120 bps but is still expected to contract by 160 bps YoY. Marketing spends are likely to remain at 12% to sales. We expect lower overhead spends, which would help in keeping operating margin stable at 29.6%. We estimate net profit growth of 9.9% to ₹ 277.2 crore
Dabur	Dabur is expected to report muted results with 4.4% revenue growth largely led by pricing growth. Weak rural demand conditions have continued to impact volume growth even in Q3. Though health supplements are expected to report positive growth numbers but it is impacted by high growth in base quarter. Foods & beverage segment continued to post strong sales with some moderation in growth. We expect 5.1% growth in international business adversely impacted by depreciation of Turkish lira. Gross margin is likely to improve sequentially by 50 bps but is expected to contract by 249 bps YoY. We expect 214 bps contraction in operating margins to 19.2%. We estimate 4.9% decline in net profit to ₹ 479.7
HUL	HUL is estimated to post sales growth of 12.6% largely led by pricing growth. We estimate 5% volume growth & 7% pricing growth during the quarter. Home care is expected to witness 23% sales growth given the company has taken price hikes in last one year. Further, detergent has continued to see strong volume growth. Beauty & personal care segment is estimated to post 5.3% sales growth as the company has passed on benefits of palm oil price decline in terms of price cuts in soaps in October 2022. Food & refreshment segment is expected to see growth of 2.3% mainly due to price deflation in the tea segment. We expect gross margin contraction of 392 bps YoY but 240 bps improvement sequentially. Operating margins are expected to contract by 82 bps during the quarter. We estimate net profit growth of 12.3% to ₹ 2519.2 crore
ITC	ITC is expected to witness 5.9% revenue growth on the back of strong growth in cigarettes, FMCG, paperboard & hotels business. Agri business is expected to see sales decline mainly due to restriction on wheat & rice exports during the quarter. We estimate 10.3% cigarettes sales growth led by 7% volume growth. FMCG business is expected to see strong 19.2% growth led by traction in discretionary categories, price hikes taken in the last one year and recovery in education & stationary business. Paperboard segment is expected to see strong pricing & volume growth. Hotels business is likely to see strongest occupancies and ARRs since Covid-19 outbreak. Agri business is likely to see 7.6% sales decline mainly on account of export restriction on many agri commodities. We estimate 12.6% growth in operating profit on account of operating leverage in cigarettes & softening of palm oil prices. We estimate 8.4% growth in net profit during the quarter
Marico	Marico is likely to witness revenue growth of 3.2% led by 6% volume growth. Parachute hair oil segment has seen low single digit volume growth. Given deflation in copra prices, we believe Parachute sales will see a decline. Further, a sharp decline in vegetable oil prices has resulted in mid-teen volume growth in Saffola Oil. The company has taken price cuts to pass on benefit of RM price decline. Value added hair oil (VAHO) segment has seen muted sales due to weak rural sales during the quarter. Foods, premium personal care & digital first brands likely to see strong growth during the quarter. International business is likely to see high single digit sales growth in constant currency. We estimate gross & operating margin improvement of 85 bps & 95 bps, respectively, in Q3FY23. Net profit is likely to grow 5.8% to ₹ 335.4 crore during the quarter
Nestlé India	We expect 12.3% revenue growth in Q4CY22 led by mix of volume & pricing growth. Though palm oil & crude based packaging raw materials has come down in last six months, milk & wheat prices have still remained high. We estimate 289 bps contraction in gross margins on YoY basis but 130 bps improvement sequentially. Operating margin is likely to witness 158 bps contraction during the quarter. Net profit is expected to grow 63.1% mainly on account of one-off expense in base quarter. Adjusting one-off, net profit is likely to grow 11.2% to ₹ 630.6 crore

Source: Company, ICICI Direct Research

Cochin Coconut Oil Price Trend (₹/kg)



Crude Price Trend (USD / barrel)

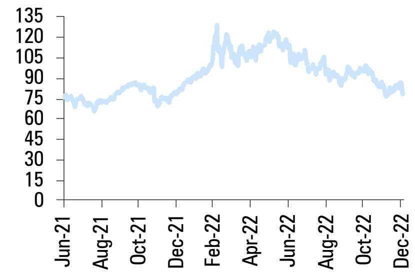


Exhibit 3: Company Specific Views (FMCG)

Company	Remarks
Tata Consumer (TCPL)	TCPL is expected to witness 7.4% revenue growth led by 26.6% growth in foods business. We estimate 1% growth in India beverage business & 3.4% decline in international beverage business. India tea business is expected to see low single digit volume growth with deflation in tea prices. The strong growth in foods business is likely to be led by pricing growth. We estimate 87 bps contraction in gross margins during the quarter. Marketing spends are likely to come down by 68 bps to 13.7%. Net profit growth is expected to grow 10.8% to ₹ 321.3 crore. We estimate ₹ 9.5 crore profit from associate compared to ₹ 2.4 crore is corresponding period mainly due to improved profitability of Starbucks
VST Industries	We expect VST Industries to witness revenue growth of 1.5% to ₹ 333.5 crore. We expect 4.6% growth in cigarette sales led by entirely volume growth. Tobacco sales are estimated to see a decline of 13.1% to ₹ 62.6 crore given the company sold large procured quantity in Q2FY23. We estimate gross & operating margin improvement of 90 bps & 51 bps, respectively. Net profit is likely to grow 7.8% to ₹ 89.2 crore
Zydus Wellness	We estimate Zydus Wellness to post sales growth of 13.3% to ₹ 439.7 crore on the back of mix of pricing & volume growth. Given, milk prices continue to remain firm, gross margins are continuing to remain weak with 525 bps contraction. We expect a cut in advertisement spends by 260 bps (as percentage to sales). Operating margins are likely to contract by 113 bps to 7.2% (its off season for major brands like Glucon-D, Nycil). Net profit is likely to grow 1.4% to ₹ 23 crore

Source: Company, ICICI Direct Research

Exhibit 4 : ICICI Direct coverage universe (FMCG)

	CMP	TP		M Cap	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)	Rating	(₹ Cr)	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Colgate (COLPAL)	1,535	1,610	Hold	43,606	39.6	38.6	42.3	38.7	39.7	36.3	8.6	8.2	7.5	77.8	82.6	92.7	62.2	62.9	70.8
Dabur India (DABIND)	550	700	Buy	97,076	9.9	10.9	12.7	55.8	50.5	43.4	8.9	8.2	7.2	24.9	24.6	26.5	20.8	21.4	22.6
Hindustan Unilever (HINLEV)	2,624	2,800	Hold	5,83,415	37.5	42.4	46.5	69.9	61.8	56.4	11.6	10.1	9.3	20.2	22.8	25.1	18.1	20.3	22.0
ITC Limited (ITC)	338	405	Buy	4,29,858	12.4	14.2	16.7	27.3	23.7	20.3	7.3	6.1	5.7	31.4	35.3	38.8	24.5	27.1	29.7
Jyothy Lab (JYOLAB)	203	205	Hold	7,076	4.3	6.2	7.8	47.7	32.5	26.2	3.3	2.9	2.6	18.7	26.2	31.3	16.6	23.0	26.8
Marico (MARLIM)	515	560	Hold	69,587	9.7	10.2	11.2	52.9	50.4	45.8	7.3	7.1	6.5	41.2	43.6	46.7	37.5	38.3	41.0
Nestle (NESIND)	20,086	22,400	Hold	1,90,912	222.4	255.8	301.1	90.3	78.5	66.7	13.0	11.4	10.3	58.7	57.1	63.0	111.3	103.6	110.3
Patanjali Foods (RUCSOY)	1,193	1,750	Buy	50,721	27.3	30.9	43.5	43.8	38.6	27.5	2.1	1.7	1.5	13.2	15.6	17.3	13.1	11.3	14.2
Tata Consumer Products (TAT	767	950	Buy	70,169	11.0	13.9	17.1	69.6	55.1	44.8	5.6	5.1	4.6	8.4	9.2	10.8	7.0	8.2	9.7
Varun Beverage (VARBEV)	1,309	1,235	Hold	71,889	17.2	23.2	26.8	76.0	56.3	48.9	8.1	5.6	5.0	17.1	30.3	33.5	18.3	29.0	29.4
VST Industries (VSTIND)	3,200	3,725	Hold	5,615	207.4	228.7	248.3	15.4	14.0	12.9	4.8	4.4	4.0	39.2	43.7	49.9	30.0	33.3	37.5
Zydus Wellness (ZYDWEL)	1,508	2,100	Buy	10,308	48.5	56.5	70.3	31.1	26.7	21.5	5.1	4.5	4.1	6.1	7.0	8.3	6.4	7.2	8.6

Source: Company, ICICI Direct Research

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