

# ITC Ltd

BUY

CMP Rs215

Target Rs266

Upside 23.4%

## Mixed quarter; agribusiness bump-up offsets soft cigarettes performance

### Result Highlights

- ✓ **Result summary** – Gross and net revenue growth of 24.1% and 21.3% yoy led by strong growth in agribusiness and sequential recovery in other segments, EBITDA growth of only 7.4% with margin decline of 480bps to 33.6% given lower EBIT margins in cigarettes and agribusiness and losses in hotels, PBT growth 7.6% and PAT decline of 1.3%.
- ✓ **Segmental performance** – Cigarettes saw 14.2% revenue and 7.7% EBIT growth, FMCG saw 15.8% revenue and 28.5% EBIT growth, hotels saw 38% revenue decline and loss of Rs 400mn at EBIT level, agribusiness saw 78.5% revenue and 54.2% EBIT growth and paper saw 13.1% revenue growth with 8% EBIT decline.
- ✓ **Other highlights** – Cigarette volume growth of around 8% with pricing/mix constituent deteriorating to 6% driving a 370bps dip in EBIT margins, FMCG saw recovery on discretionary segments with 23% growth and normalization in staples/foods/hygiene segment with 13% growth while margins expand by 50bps to 5.1%, hotel losses reduce, agribusiness margin lower due to inferior mix while paper margins flat.

**Valuation and view** – We would rate ITC's 4Q performance as mixed with revenues delivering a positive surprise while margin performance was disappointing. Cigarette volumes were up ~8%, a continuation of sequential improvement but still below pre-COVID levels, coupled with some deterioration in mix as well. While May has been impacted by the lockdowns but should still be relatively better than last year given restricted store operations. FMCG growth was in-line given that the momentum of staple/foods/hygiene categories is now normalizing and discretionary categories are recovering. The bump-up seen in agri business led by wheat exports should normalize and hotels and paper business should steadily keep improving. Hotels getting into positive EBITDA and FMCG business keeping up the margin growth trajectory were other positives. ITC's FY21 dividend payout ratio reached 100%, which has kept dividend yield for the stock ~5%. We build in 9% revenue and 14% EBITDA and PAT CAGR for the company over FY21-23E led by 11% volume growth in cigarettes from a favorable base and normalized growth rates in agribusiness and FMCG, in addition to margin improvement especially in cigarettes with positive operating leverage and a better mix.

We assume coverage on the stock with a BUY rating and a TP of Rs 266 based on 20x FY23E earnings, a significant discount of 50-60% to sector peers and a 15% discount to its long-term average multiple. We also believe concerns on ESG and FMCG business growth/margin trajectory look overdone. While valuation remains cheap for the stock, the stock can continue to remain range bound for now given lack of positive triggers either on growth or corporate action. But cheap valuations, strong volume growth outlook for cigarettes in FY22 given low base and benign taxation and strong cash flow yield of 6% provide strong downside support.

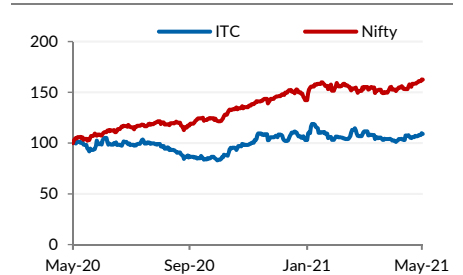
### Exhibit 1: Result table

(Rs mn)	Q4FY21	Q4FY20	% yoy	Q3FY21	% qoq
Net revenue	1,32,947	1,08,423	22.6	1,19,690	11.1
EBITDA	44,730	41,635	7.0	43,147	4.0
EBITDAM (%)	34	38		36	
Depreciation	3,880	3,925	(1.2)	3,923	(1.1)
Interest	31	147	(78.7)	138	(77.2)
Other income	7,720	7,555	2.0	9,718	(20.6)
PBT	48,539	45,118	7.6	48,804	(0.5)
Tax	11,055	7,148	55	11,926	(7.3)
Adjusted PAT	37,484	37,971	(1.3)	36,879	1.6
PATM (%)	28	35		31	
EPS (Rs)	3.0	3.1		3.0	

### Stock data (as on June 01, 2021)

Nifty:	15,575
52 Week h/l (Rs)	239 / 163
Market cap (Rs/USD mn)	2649479 / 36345
Outstanding Shares	12,309
6m Avg t/o (Rs mn):	7,310
Div yield (%):	2.3
Bloomberg code:	ITC IN
NSE code:	ITC

### Stock performance



	1M	3M	1Y
Absolute return	6.2%	4.0%	15.5%

### Shareholding pattern (As of Mar'21 end)

Promoter	0.0%
FII+DII	56.3%
Others	43.8%

### Financial Summary

(Rs mn)	FY21	FY22e	FY23e
Net Revenue	4,92,728	5,42,341	5,82,225
YoY Growth	(0.3)	10.1	7.4
EBIDTA	1,61,754	1,90,172	2,10,271
Margins (%)	32.8	35.1	36.1
PAT	1,25,625	1,48,609	1,63,553
YoY Growth	(20.1)	18.3	10.1
ROE	20.0	24.4	26.3
ROCE	27.2	32.5	35.0
EPS	10.2	12.1	13.3
P/E	21.1	17.8	16.2
EV/EBITDA	16.1	13.7	12.3

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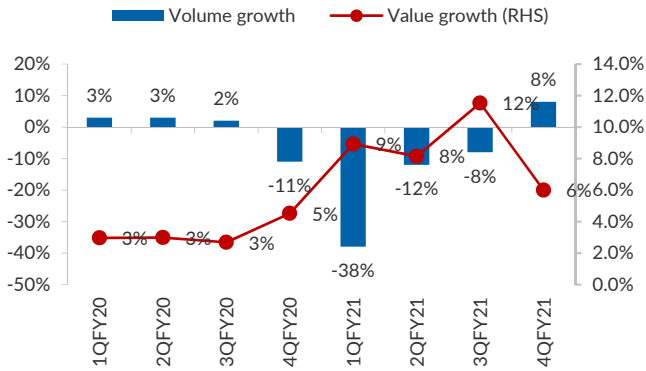
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## PRESENTATION HIGHLIGHTS

- ✓ **Quarter summary** - Gross revenue up 24.1%, PBT up 7.6% and adjusted PAT up 8.4%; final dividend of Rs 5.75 per share which takes total dividend for the year to Rs 10.75 per share vs Rs 10.15 per share last year despite lower profits.
- ✓ **FMCG business** - Comparable revenue up 16% yoy with staples/food/hygiene segment sales up 13% (78% of business) displaying normalization trends and discretionary segment sales up 23% (22% of business) displaying a good recovery. Education and stationary business was impacted due to closure of educational institutions. Comparable EBITDA up 36% with margin expansion of 115bps led by enhanced operational efficiencies, increased scale, better product mix and value chain interventions. FY21 revenue up 16% and EBITDA margins up 180bps to 8.9%. Market and outlet coverage has been expanded to 1.3x and 1.1x compared to pre-COVID levels. Over 120 new innovative products were launched in FY21. Sunrise business was amalgamated in February 2021.
- ✓ **Key trends in FMCG** - Demand for health & hygiene, immunity and Ayurveda products remains elevated albeit at lower levels than 1HFY21, staples demand normalized with broadening of consumer purchase assortment, snacks and beverages post double digit growth, rural markets continue to outpace urban growth, sharp inflation in crude and vegetable oil prices, ITC e-commerce sales grew 2x now at 5% of sales.
- ✓ **Cigarettes business** - Sequential recovery continued with gross revenue up 14% and net revenue up 7% along with margin expansion of 70bps led by progressive easing of restrictions and improved mobility which brought volumes back to pre COVID levels towards year-end. Smart recovery was witnessed in metros and large towns, company enhanced market share via innovative and competitive offerings, convenient packs and portfolio fortification, augmented the number of stockists, grocery outlets, and rural/semi-urban markets, legal industry volumes still bearing the brunt of 13% tax hike in Feb 2020.
- ✓ **Agribusiness** - Segment revenue and EBIT up 78.5% and 54.2% respectively led by higher sales of wheat, rice and oilseeds, growth in value added spice exports and higher supplies given enhanced scale in packaged foods segment, margins impacted by adverse mix and subdued demand for leaf tobacco in international markets.
- ✓ **Paper business** - Segment revenue and EBIT up 13.5% and 13.1% respectively led by strong volume recovery in paperboards, robust growth in carton packaging exports and flexible packing in domestic markets.
- ✓ **Hotels business** - Sequential improvement continued aided by higher occupancy and F&B business. EBITDA improved to Rs 25crs after breaking even in 3Q led by cost interventions (cash fixed costs down 41% in FY21) and revenue augmentation measures like introduction of special packages and launch of curated food delivery/takeaway menus. Wedding business and staycations remain key growth drivers while leisure locations witnessed strong demand.
- ✓ **Current situation** - While supply chain has not been impacted, company is facing challenges at front-end due to constraints in number of operating outlets and limited operational hours, company is sharply focused on cost reduction, management confident of responding with agility leveraging recent learnings across the value chain.

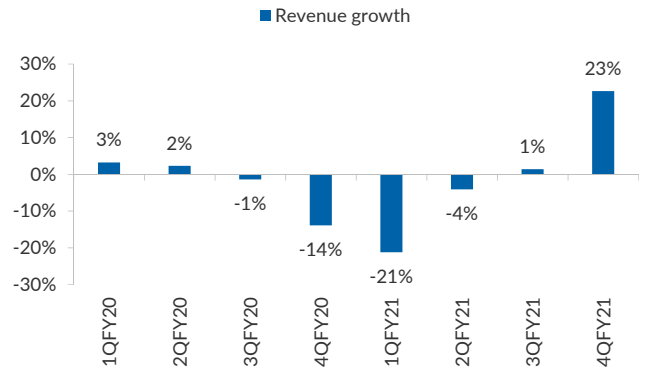
**CHARTS**

**Exhibit 2: Cigarette volume recovered close to pre-Covid levels in March**



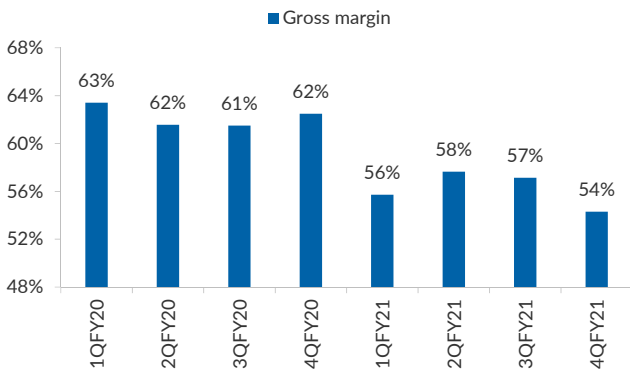
Source: Company, YES Sec - Research

**Exhibit 3: Revenue growth led by FMCG - Other and Agri business**



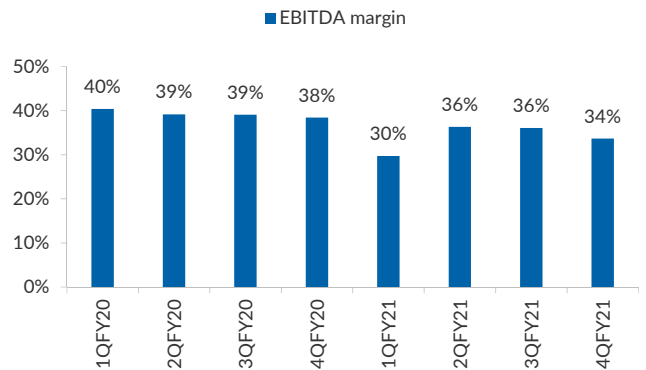
Source: Company, YES Sec - Research

**Exhibit 4: Gross margin impacted by inferior category, product mix and change in NCCD accounting**



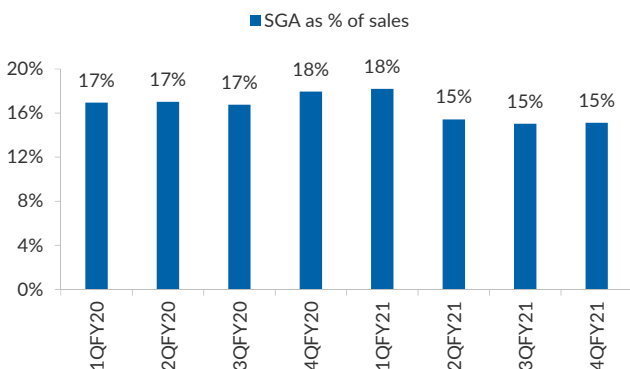
Source: Company, YES Sec - Research

**Exhibit 5: EBITDA margin also declined albeit to a lesser extent**



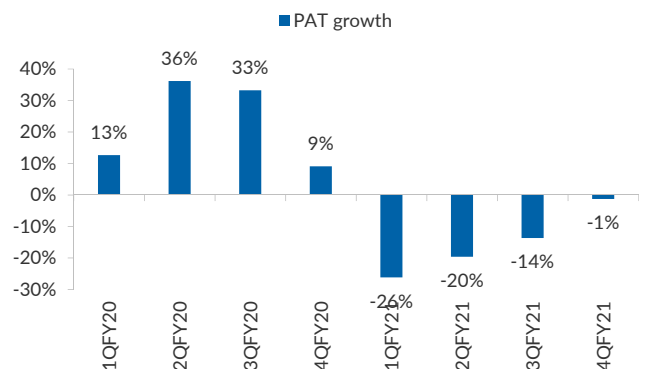
Source: Company, YES Sec - Research

**Exhibit 6: Tight cost control help offset margin contraction**



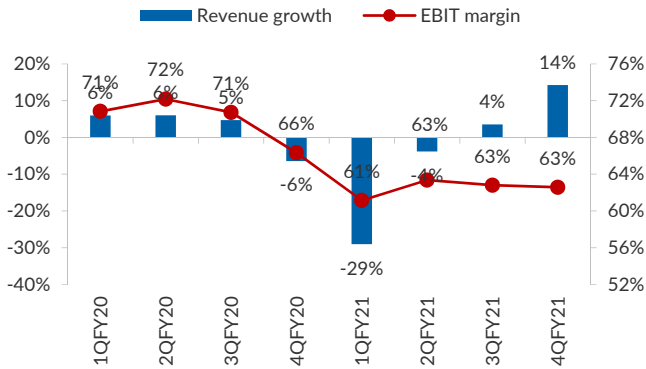
Source: Company, YES Sec - Research

**Exhibit 7: Earnings growth gradually recovering to positive territory**



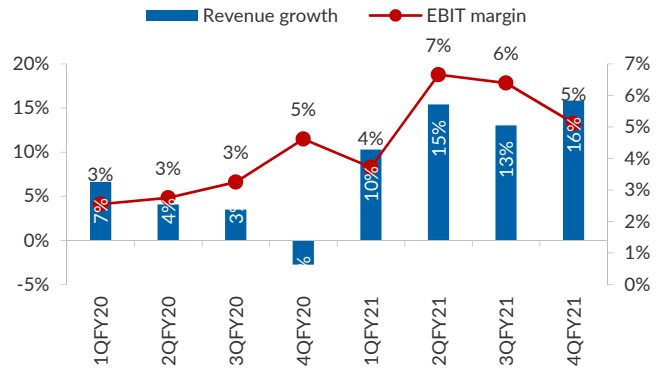
Source: Company, YES Sec - Research

**Exhibit 8: Cigarette revenues continue sequential recovery**



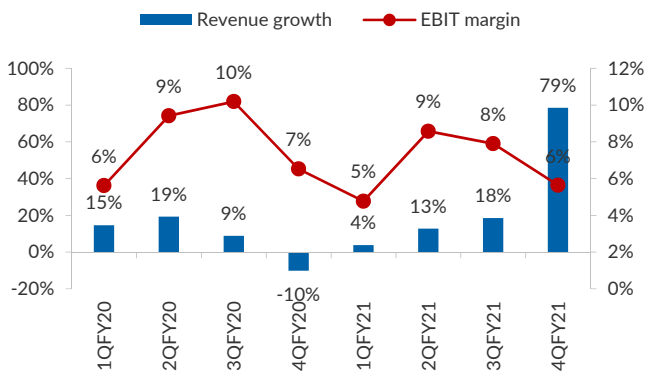
Source: Company, YES Sec - Research

**Exhibit 9: Strong FMCG - Other revenue growth with margin expansion**



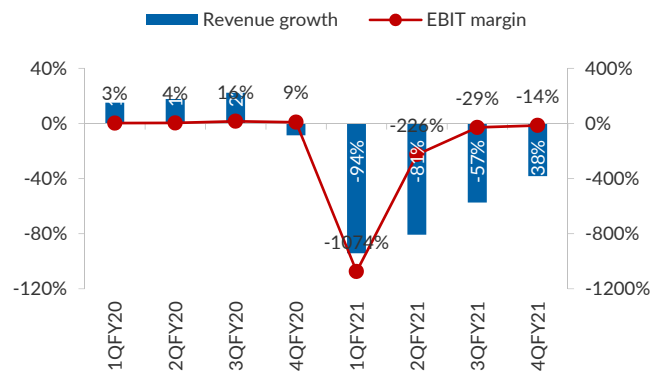
Source: Company, YES Sec - Research

**Exhibit 10: Robust revenue growth in Agri business across categories but inferior mix impacted margin**



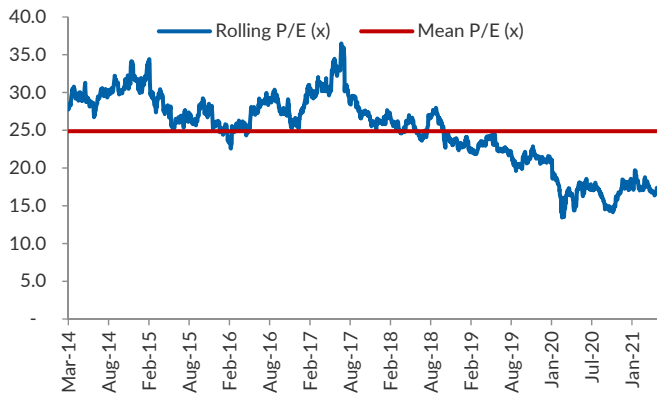
Source: Company, YES Sec - Research

**Exhibit 11: Sequential improvement in Hotel business led by higher occupancy and F&B business**



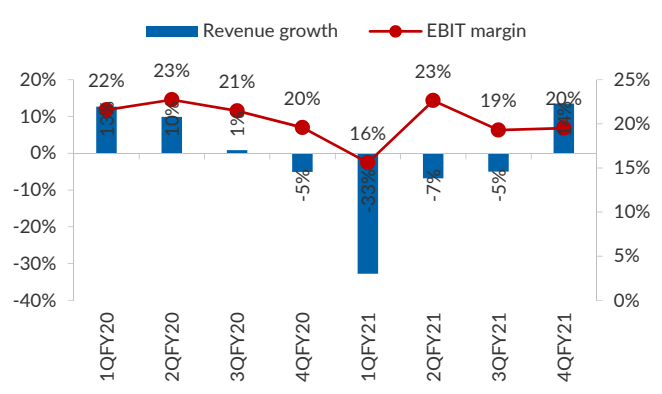
Source: Company, YES Sec - Research

**Exhibit 12: Currently trading at 17.5x one-yr fwd earnings**



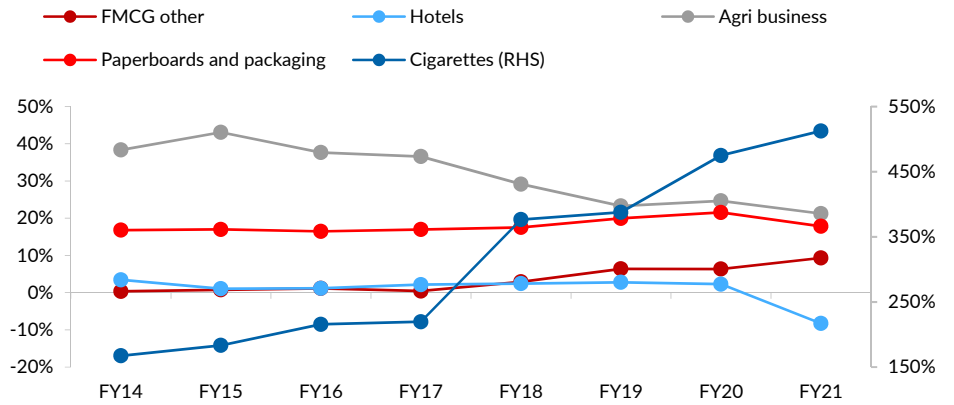
Source: Company, YES Sec - Research

**Exhibit 13: Recovery continued with stable margins in Paperboards, paper and packaging**



Source: Company, YES Sec - Research

**Exhibit 14: FMCG – Other and Paper business continue to improve ROCEs**



Source: Company, YES Sec – Research

## FINANCIALS

### Exhibit 15: Balance sheet

Y/e 31 Mar (Rs mn)	FY19	FY20	FY21	FY22E	FY23E
Equity capital	12,259	12,292	12,309	12,309	12,309
Reserves	5,79,150	6,40,440	5,91,165	6,00,838	6,18,508
Net worth	5,94,843	6,56,507	6,06,942	6,16,615	6,34,285
Debt	100	73	95	95	95
Deferred tax liab (net)	20,521	16,272	17,364	17,364	17,364
Other non current liabilities	2,419	5,234	6,935	7,282	7,646
Total liabilities	6,17,883	6,78,087	6,31,335	6,41,355	6,59,389
Fixed Asset	2,35,106	2,36,173	2,59,560	2,65,677	2,70,294
Investments	2,50,434	2,90,487	2,52,474	2,52,474	2,52,474
Other Non-current Assets	48,445	31,440	24,702	25,908	27,174
Net Working Capital	42,376	47,213	48,008	50,506	50,440
Inventories	78,596	88,793	1,03,972	1,04,011	1,03,684
Sundry debtors	40,353	25,625	25,017	29,717	31,903
Loans and Advances	68	63	35	149	160
Sundry creditors	35,096	36,298	43,187	41,604	39,878
Other current liabilities	64,492	57,803	61,731	66,864	71,781
Cash & equivalents	41,521	72,773	46,590	46,789	59,008
Total Assets	6,17,883	6,78,087	6,31,335	6,41,355	6,59,389

### Exhibit 16: Income statement

Y/e 31 Mar (Rs mn)	FY19	FY20	FY21	FY22E	FY23E
Revenue	4,83,527	4,94,041	4,92,728	5,42,341	5,82,225
Operating profit	1,84,064	1,92,602	1,70,027	1,90,172	2,10,271
Depreciation	13,966	16,449	16,456	18,883	20,383
Interest expense	454	547	446	468	491
Other income	21,738	25,979	26,326	27,642	29,024
Profit before tax	1,91,381	2,01,585	1,79,451	1,98,463	2,18,420
Taxes	63,139	44,418	45,553	49,854	54,867
Minorities and other	-	-	-	-	-
Adj. profit	1,28,242	1,57,167	1,33,898	1,48,609	1,63,553
Exceptional items	(117)	1,239	69	-	-
Net profit	1,28,359	1,55,928	1,33,829	1,48,609	1,63,553

## Exhibit 17: Cash flow statement

Y/e 31 Mar (Rs mn)	FY19	FY20	FY21	FY22E	FY23E
PBIT	1,91,835	2,02,131	1,79,897	1,98,931	2,18,911
Depreciation	13,966	16,449	16,456	18,883	20,383
Tax paid	(63,139)	(44,418)	(45,553)	(49,854)	(54,867)
Working capital Δ	(33,239)	(50,845)	30,225	(2,498)	67
Other operating items					
Operating cashflow	1,09,423	1,23,317	1,81,025	1,65,462	1,84,494
Capital expenditure	(28,749)	(17,516)	(39,843)	(25,000)	(25,000)
Free cash flow	80,674	1,05,801	1,41,181	1,40,462	1,59,494
Equity raised	22,925	30,162	(50,768)	-	0
Investments	(2,121)	5,955	6,993	-	-
Debt financing/disposal	(188)	(27)	21	-	-
Interest Paid	(454)	(547)	(446)	(468)	(491)
Dividends paid	(84,976)	(1,24,766)	(1,32,320)	(1,38,936)	(1,45,882)
Other items	(3,334)	14,673	9,155	(859)	(902)
Net Δ in cash	12,525	31,252	(26,183)	199	12,219

## Exhibit 18: Du-pont analysis

Y/e 31 Mar (Rs mn)	FY19	FY20	FY21	FY22E	FY23E
Tax burden (x)	0.7	0.8	0.7	0.7	0.7
Interest burden (x)	1.0	1.0	1.0	1.0	1.0
EBIT margin (x)	0.4	0.4	0.4	0.4	0.4
Asset turnover (x)	0.7	0.7	0.7	0.7	0.8
Financial leverage (x)	1.2	1.2	1.2	1.2	1.2
RoE (%)	23.0	25.3	21.3	24.4	26.3

## Exhibit 19: Ratio analysis

Y/e 31 Mar	FY19	FY20	FY21	FY22E	FY23E
<b>Growth matrix (%)</b>					
Revenue growth	11.3	2.2	(0.3)	10.1	7.4
Op profit growth	11.7	4.6	(11.7)	11.8	10.6
EBIT growth	12.3	5.4	(11.0)	10.6	10.0
Net profit growth	15.7	22.6	(14.8)	11.0	10.1
<b>Profitability ratios (%)</b>					
OPM	38.1	39.0	34.5	35.1	36.1
EBIT margin	39.7	40.9	36.5	36.7	37.6
Net profit margin	26.5	31.8	27.2	27.4	28.1
RoCE	34.1	32.3	28.5	32.5	35.0
RoNW	23.0	25.3	21.3	24.4	26.3
RoA	18.8	21.1	17.7	19.9	21.4
<b>Per share ratios</b>					
EPS	10.5	12.8	10.9	12.1	13.3
Dividend per share	6.9	10.2	10.8	11.3	11.9
Cash EPS	11.6	14.1	12.2	13.6	14.9
Book value per share	48.5	53.4	49.3	50.1	51.5
<b>Valuation ratios</b>					
P/E	20.6	16.8	19.8	17.8	16.2
P/CEPS	18.6	15.2	17.6	15.8	14.4
P/B	4.4	4.0	4.4	4.3	4.2
EV/EBIDTA	14.1	13.4	15.3	13.7	12.3

Y/e 31 Mar	FY19	FY20	FY21	FY22E	FY23E
<b>Payout (%)</b>					
Dividend payout	66.3	79.4	98.8	93.5	89.2
Tax payout	33.0	22.0	25.4	25.1	25.1
<b>Liquidity ratios</b>					
Debtor days	30	19	19	20	20
Inventory days	59	66	77	70	65
Creditor days	26	27	32	28	25



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10	Research Analyst or YSL has been engaged in market making activity for the subject company(ies)	No

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**BUY:** Potential return >15% over 12 months

**ADD:** Potential return +5% to +15% over 12 months

**REDUCE:** Potential return -10% to +5% over 12 months

**SELL:** Potential return <-10% over 12 months

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