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Growth aided by price hikes; margins still under check

Q2FY22 has seen normalisation of the consumption trend after a recovery from the second wave of pandemic. We believe FMCG companies would continue to witness structural mid to high single digit volume growth. Most companies have taken 5-15% price hikes in previous quarters to withstand commodity price inflation. Our coverage universe is expected to witness 13.7% revenue growth led by equal mix of volumes & pricing growth. Dabur, Marico would continue to witness strong volume growth led by foray into newer categories, higher traction of immunity products & healthier consumption trend. Marico sales would also be driven by higher pricing growth. HUL is likely to witness a strong recovery in both home care & BPC categories from low base quarter. Moreover, acquired nutrition brands would continue to grow at a healthier pace for the company driven by smaller SKUs & distribution expansion.

Colgate & Nestlé will continue to grow at a moderate pace driven largely by volumes. Tata Consumer is expected to continue to witness strong sales growth led by sharp price hikes taken in the last one year to pass on a steep rise in procurement prices. Tea procurement prices have witnessed more than 30% decline in the last two months, which would ease pressure on prices. Zydus Wellness is expected to see a recovery from low base quarter with 12% growth in a non-peak quarter. Cigarettes companies are expected to see a strong recovery in cigarettes segment on YoY as well as QoQ basis. We believe cigarette companies would see 5-7% volume growth in Q2. We believe structural trend in FMCG sector i.e. direct distribution expansion, e-commerce channel sales growth, consumption shift towards packaged foods & new products launches would continue to drive growth in the medium term for the industry. With expected moderation in commodity price inflation in next two quarters, the industry would increase its advertisement spends to drive growth from newer products.

Commodity inflation to pressurise margins in near term

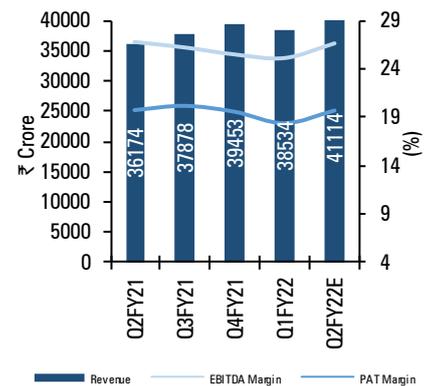
Our coverage universe is likely to witness a 15 bps contraction in operating margins but ex-ITC it is likely to contract by 80 bps. Most commodities have remained elevated in the last three months pressurising FMCG companies to take prices hike & reduce advertisement spends. Average palm oil prices are up 60% YoY and 6% QoQ. Similarly, average crude prices have increased by 68% YoY and 6% QoQ. Copra prices have been flat YoY but cooled off by 22% from the peak in March 2021. Tea prices have also declined ~30% in last two months. Despite price hikes, we believe operating margins of HUL, Dabur, Marico, Nestlé would be under pressure. We believe FMCG companies would be able to pass on this inflation with staggered price hikes or dip in commodity prices in next few quarters. We estimate net profit growth of 13.4% in Q2FY22.

Exhibit 1: Estimates for Q2FY22E: (FMCG)

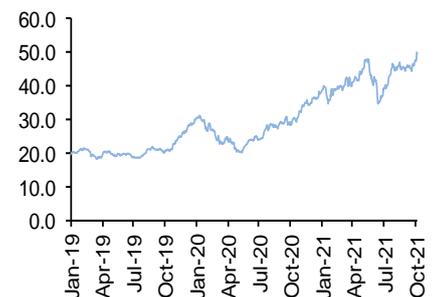
Company	Revenue			EBITDA			PAT		
	Q2FY22E	YoY	QoQ	Q2FY22E	YoY	QoQ	Q2FY22E	YoY	QoQ
Colgate Palmolive	1,379.4	7.3	18.3	444.1	8.5	25.0	297.6	8.5	27.6
Dabur India Ltd	2,823.3	12.2	8.1	630.8	10.8	14.3	509.3	5.5	16.4
HUL	13,132.2	14.8	10.2	3,129.9	9.1	9.9	2,210.2	10.0	7.2
ITC	13,585.9	13.4	4.8	4,766.6	17.4	19.4	3,619.1	12.0	20.1
Marico Ltd	2,399.3	20.6	-5.0	453.3	16.6	-5.8	337.9	23.8	-7.4
Nestle India	3,928.8	10.9	13.0	965.5	9.3	13.9	653.8	11.4	21.4
Tata Consumer	3,151.3	13.3	4.7	433.8	8.6	8.6	318.7	16.7	53.2
VST Industries	328.0	9.3	19.3	130.5	15.5	42.0	99.3	12.1	41.0
Zydus Wellness	386.1	12.9	-35.4	34.5	27.1	-75.5	23.3	LP	-82.2
Total	41,114.3	13.7	9.4	10,988.9	13.0	11.4	8,069.2	13.4	14.8

Source: Company, ICICI Direct Research

Topline & Profitability (Coverage Universe)



Surge in palm oil prices (₹/kg)



Operating margins FMCG Coverage (%)

Company	EBITDA margin %				
	Q2'21	Q3'21	Q4'21	Q1'22	Q2'22
Colagte	31.8	30.1	32.9	30.5	32.2
Dabur	22.6	21.0	18.9	21.1	22.3
HUL	25.1	24.1	24.4	23.9	23.8
ITC	33.9	35.0	31.6	30.8	35.1
Marico	19.6	19.4	15.9	19.0	18.9
Nestle	24.9	22.6	25.8	24.4	24.6
Tata Cons.	14.4	11.8	9.9	13.3	13.8
VST Ind.	37.7	34.8	35.3	33.4	39.8
Zydus Wellness	7.9	13.0	24.0	23.5	8.9
FMCG Total	26.9	26.3	25.6	25.2	26.7

Top Picks

Dabur
Marico
Zydus Wellness

Research Analysts

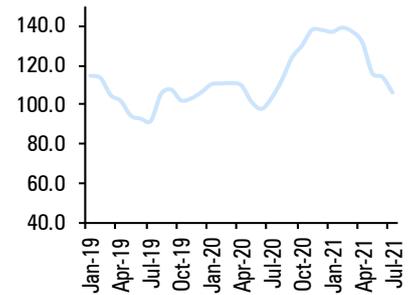
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Exhibit 2: Company Specific Views (FMCG)

Company	Remarks
Colgate	Colgate is expected to report 7.3% revenue growth largely led by volumes. The expected growth is on the back of a normalised quarter. Oral care category has been least impacted by pandemic. Moreover, key raw materials like sorbitol & calcium carbonates were favourable for most of the last 12 months. Crude based packaging cost have been steadily moving upwards. We expect flattish gross margins in Q2FY22. Operating margins have moved up by 600 bps in the last six quarters. We believe the company would be able to maintain the elevated operating margins above 32%. PAT is expected to grow 8.5% to ₹ 297.6 crore
Dabur	Dabur India is likely to witness 12.2% revenue growth led by mix of volumes & prices on the back of strong growth of 13.7% in base quarter. The company has been a major beneficiary of increasing consumer awareness about health & immunity. It is foraying into several newer categories like edible oil, household Insecticides. We believe aggressive product launches & foraying into multiple newer categories is driving growth for the company. With increasing cost inflation, gross margins are likely to contract 240 bps in Q2. However, we expect smaller contraction of 30 bps in operating margins. Net profit is expected to grow 5.5% to ₹ 509.3 crore
HUL	HUL is likely to witness revenue growth of 14.8% to ₹ 13132 crore on back of a recovery in home care & beauty & personal care segment. The base quarter revenue growth was flattish for these segments. The acquired nutrition business is part of the foods & refreshment segment. We expect 10.5%, 15.7% & 11.3% sales growth in home care, beauty & personal care and foods segment, respectively. We estimate 100 bps gross margins contraction with a steep increase in commodity costs. Operating margins are likely to see a 124 bps contraction in Q2FY22. Net profit is likely to grow 10% to ₹ 2210.2 crore
ITC	ITC is expected to see a swift recovery in cigarette volumes & other discretionary business with normalisation of out of home activity. Consolidated revenues are likely to grow at 13.4% with the expected 9.4% growth in cigarettes sales. We expect cigarettes volumes growth of 7%. Hotels business sales is estimated to grow 2x from the low base quarter. FMCG & paper business is likely to grow 13.4% & 12.2%, respectively. We estimate agri business growth of 6.5% on a relatively high base. We estimate 118 bps improvement in operating margins at 35.1%. Net profit is likely to grow 12.0% to ₹ 3619.1 crore
Marico	We expect consolidated sales growth of 20.6% to ₹ 2399.3 crore led by domestic growth of 22.6% & international business growth of 13.5%. VAHO segment volume has grown in double digits whereas Saffola brand saw muted growth on high base & volatility in commodity prices. Foods & digital brands are continuing the high growth momentum in Q2 as well. We believe the high growth is also driven by high pricing growth taken in previous quarter to pass on steep commodity price inflation. We estimate 300 bps gross margin contraction & subsequently 70 bps operating margins dip. We estimate PAT growth of 23.8% to ₹ 337.9 crore
Nestlé India	Nestlé India is expected to see sales growth of 10.9% to ₹ 3928.8 crore with the normalised base. The demand for milk based products & noodles has remained strong. Moreover, price hikes are likely to partially contribute to growth. Further, the company is aiming to expand its rural distribution channel to benefit from the rising consumption levels in smaller cities & villages. E-commerce channel is also growing at a faster pace for the company. With the increase in milk prices, gross margins are expected to contract 180 bps but lower overhead spends would help in curbing operating margins contraction by 37 bps. Net profit is likely to grow 11.4% to ₹ 653.8 crore

Source: Company, ICICI Direct Research

Copra Price Trend (₹/kg)



Crude Price Trend (USD / barrel)

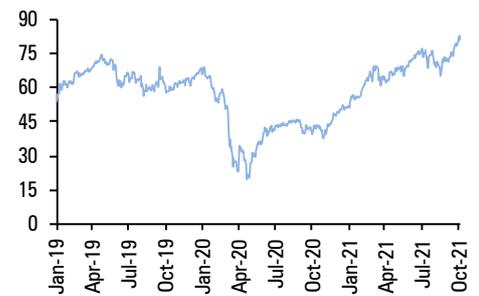


Exhibit 3: Company Specific Views (FMCG)

Company	Remarks
Tata Consumer (TCPL)	Tata Consumer is likely to witness sales growth of 13.3%, largely led by price hikes taken in previous quarters. Indian beverage segment is expected to witness growth of 18.3% whereas international beverage business is likely to see flat sales in Q2. We expect strong 26.9% sales growth in Indian food segment led by volumes as well as price hikes in salt & pulses segment. Tea procurement prices have cooled off significantly in the last two months. Though we believe full impact of this dip would be seen in Q3FY22, gross margins would be largely protected during the quarter. We estimate 60 bps contraction in operating margins. Net profit is expected to grow 16.7% to ₹ 318.7 crore
VST Industries	VST Industries is expected to see 9.3% revenue growth on the back of a sharp recovery in cigarettes volumes. We believe normalised activity after the second wave of pandemic would have resulted in strong volume recovery in cigarettes segment. Cigarettes & tobacco business sales are likely to grow 6.9% & 20.3%, respectively. We estimate 15.5% growth in operating profit to ₹ 130.5 crore. We estimate net profit growth of 12.1% to ₹ 99.3 crore
Zydus Wellness	September quarter is not a peak sales quarter for Zydus & contributes 18-20% of the annual sales. The company was adversely impacted by the pandemic given peak summer months were impacted the most. We expect 12.9% sales growth during the quarter with normalisation of Everyuth sales. We estimate operating profit growth of 27.1% to ₹ 34.5 crore. Operating margin is likely to see uptick of 100 bps during the quarter on the back of adverse base quarter. The 68% dip in interest cost on the back of debt reduction is expected to boost profitability. We estimate net profit of ₹ 23.3 crore against adjusted loss of ₹ 7.4 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)	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E
Colgate (COLPAL)	1,688	2,000	Buy	46,485	38.1	39.2	42.6	44.3	43.1	39.6	9.7	9.0	8.3	106.4	110.9	111.9	88.8	85.1	85.8
Dabur India (DABIND)	607	740	Buy	108,544	9.6	10.6	12.0	63.3	57.4	50.7	11.4	10.0	9.1	24.5	25.8	27.1	22.1	22.3	23.1
Hindustan Unilever (HINLEV)	2,640	2,750	Buy	558,687	33.9	40.5	45.0	78.0	65.2	58.6	12.3	10.6	9.9	18.9	25.6	27.7	17.1	20.0	21.6
ITC Limited (ITC)	232	240	Hold	261,086	10.7	12.0	13.5	21.6	19.3	17.2	5.4	5.0	4.6	28.2	31.3	33.6	22.1	24.2	25.9
Jyothy Lab (JYOLAB)	165	180	Hold	6,389	5.2	5.7	6.5	31.8	28.9	25.4	3.4	3.1	2.8	26.0	27.1	31.1	20.4	22.7	26.2
Marico (MARLIM)	564	630	Buy	70,503	9.3	10.4	11.5	60.7	54.4	48.9	8.8	7.6	7.0	39.6	42.8	46.6	36.3	38.4	40.4
Nestle (NESIND)	18,986	20,450	Hold	173,556	216.0	249.9	279.6	87.9	76.0	67.9	13.1	11.8	10.7	50.9	54.9	56.4	86.5	87.8	86.3
Tata Consumer Products (TAT)	819	900	Buy	69,943	10.1	12.4	14.3	81.1	66.0	57.3	6.0	5.3	4.9	8.0	9.1	9.9	6.4	7.6	8.4
VST Industries (VSTIND)	3,475	3,850	Hold	5,384	201.3	214.6	231.1	17.3	16.2	15.0	4.9	4.4	4.1	43.4	45.0	48.2	33.0	33.4	36.0
Varun Beverage (VARBEV)	901	950	Buy	34,166	8.4	14.2	19.3	107.7	63.3	46.7	5.3	4.3	3.8	10.9	17.5	22.9	10.3	15.5	17.9
Zydus Wellness (ZYDWEL)	2,367	2,800	Buy	13,537	18.7	57.8	68.3	126.8	40.9	34.7	7.3	6.4	5.8	6.2	7.5	8.7	5.5	7.7	9.0

Source: Company, ICICI Direct Research

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