

**ITC Ltd.**

₹ 346

*The Branded Scrip!***Accumulate**

May 09, 2014

**Company Background**

ITC was incorporated on August 24, 1910 under the name Imperial Tobacco Company of India Ltd. As its ownership progressively Indianised, the name was changed to India Tobacco Company Limited in 1970 and then to I.T.C. Limited in 1974. The Company's multi-business portfolio encompasses a wide range of businesses - Fast Moving Consumer Goods comprising Foods, Personal Care, Cigarettes and Cigars, Branded Apparel, Education and Stationery Products, Incense Sticks, Hotels, Paperboards & Specialty Papers, Packaging, Agri-Business and Information Technology. ITC is an associate of BAT (British American Tobacco) controls more than 2/3rd of the cigarette market in India. ITC has emerged as a diversified conglomerate with leading presence in Paperboards, Hotels and processed foods. E-Choupal, its agri rural initiative has been widely appreciated for its foresight in harnessing the potential in the rural market.

**Key Highlights**

- ➔ Cigarette volumes and profit growth is expected to further accelerate as higher prices and demand recovery has set in. Sustained FMCG sales growth with continued share gains in Biscuits and Noodles, is positive. One can expect a full turnaround in FY15 backed by a strong performance in Foods portfolio and rising benefits of scale.
- ➔ The pattern of tobacco consumption in India is unique with over 17% of the world's population, India has a miniscule share of Global Cigarette consumption this keeps in a large growth prospect for a company whose primary revenue business is from cigarettes.
- ➔ In a view to counter the dependence on Revenues from Cigarettes ITC has very aggressively pursuing the Other Segments of FMCG and has established many brands in Food Products, Processed foods, Confectionaries, Personal Care, Stationery, etc in a very short span.
- ➔ ITC's Hotels business continues to be the fastest growing hospitality chains in India operating under 4 brands – the luxury 'ITC Hotel', the 5 star 'Welcome Hotel', the mid market to upscale 'Fortune' and 'WelcomHeritage' in heritage leisure segment. In addition, the business has licensed 2 international brands.

**Key Financials**

Year Ended 31 <sup>st</sup>	Mar 11	Mar 12	Mar 13
Revenue (INR mn)	268,013.5	300,702.6	366,646.7
Rev. growth (%)	18.85	12.20	21.93
EBITDA (INR mn)	80,250.8	97,531.7	116,071.2
Net profit (INR mn)	49,882.1	61,629.6	74,190.0
Shares outstanding (mn)	7,738.1	7,818.4	7,901.8
EPS (INR)	6.4	7.9	9.4
EPS growth (%)	(39.40)	22.28	19.11
P/E (x)	28.1	28.8	32.9
RONW (%)	33.5	35.6	36.3
ROCE (%)	33.2	35.4	36.1

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**Info Codes**

Reuters	: ITC.BO
Bloomberg	: ITC@IN
NSE	: ITC
BSE	: 500875

**Market Data**

52 Wk Range (₹)	: 285 / 380
Shares in Issue (mn)	: 7901.8
Mkt. Cap (₹ bn)	: 2743.9
BSE 2 Wk Avg Vol	: 309000

**Share Holding Pattern (%)**

Promoters	: 0.00
FII's	: 19.26
DII's	: 34.68
Others	: 46.06

**Investment Theme**

Continuing with ITC's chosen strategy of creating multiple drivers of growth, it is today, the leading FMCG marketer in India, the second largest Hotel chain, the clear leader in the Indian Paperboard and Packaging industry & India's foremost Agri business player. Its wholly owned subsidiary, ITC Infotech India Limited, is one of India's fast growing InfoTech company in mid-tier segment. Further, over last 18 years, ITC's Gross Revenues and Net Profits have recorded impressive and consistent growth. ITC today is one of India's most admired and valuable corporations with a market capitalisation of nearly INR 2700 bn & has consistently featured, over the last 20 years, amongst the top 10 private Co's in terms of market cap and profits. Its variety of brands touch lives of every Indian every day. The best part, its a professionally managed company without promoters.

**Trying to Quit Tobacco**

## Financial Statements

### Income Statement

(₹ mn)

Year end	Mar 11	Mar 12	% Chg	Mar 13	% Chg
Total Sales + Excise	308192.8	352208.9	14.28	421055.1	19.55
Other Income	5821.9	8322.2	42.95	9774.0	17.44
Change in Stocks	3464.8	1493.0	(56.91)	9358.3	526.81
Raw Material Con.	71852.2	78951.2	9.88	91574.0	15.99
Employee Exp.	11751.9	13001.8	10.64	14300.7	9.99
Indirect Taxes	97532.9	104686.2	7.33	133109.4	27.15
Other Exp.	56994.1	68789.0	20.69	86224.3	25.35
Operating Exp.	234666.3	263935.2	12.47	315850.1	19.67
Operating Profit	73526.5	88273.7	20.06	105205.0	19.18
Total Interest	879.8	1367.9	55.48	1059.1	(22.57)
Gross Profit	78468.6	95228.0	21.36	113919.9	19.63
Net Dep.	5709.6	6227.6	9.07	6941.3	11.46
Total Taxation	22876.9	27370.8	19.64	32788.6	19.79
Net Profit/Loss	49882.1	61629.6	23.55	74190.0	20.38

### 4 Years Balance Sheet

(₹ mn)

Balance Sheet as on 31 <sup>st</sup>	Mar 10	Mar 11	Mar 12	Mar 13
<b>SOURCES OF FUNDS</b>	<b>141,177.0</b>	<b>159,991.3</b>	<b>188,279.6</b>	<b>223,127.7</b>
Equity Share capital	3,818.2	7,738.1	7,818.4	7,901.8
Share Application Money	0.0	0.0	0.0	0.0
Preference Share Capital	0.0	0.0	0.0	0.0
Reserves & Surplus	136,281.7	151,261.2	179,570.0	214,449.2
Long Term Loans	1,077.1	972.6	873.5	776.7
Short Term Loans	0.0	19.4	17.7	0.0
<b>USES OF FUNDS</b>	<b>141,177.0</b>	<b>159,991.3</b>	<b>188,279.6</b>	<b>223,127.7</b>
Gross Block	119,678.6	127,658.6	141,443.5	169,443.8
Less : Revaluation Reserves	543.9	533.4	530.5	527.5
Less : Accumulated Depreciation	38,254.6	44,207.5	50,451.6	57,350.4
Net Block	80,880.1	82,917.7	90,461.4	111,565.9
Capital Work in Progress	12,736.8	13,334.0	22,767.5	14,877.9
Investments	57,268.7	55,546.2	63,165.9	70,602.9
Current Assets	82,474.8	106,382.7	117,443.0	147,913.0
Less : Current Liabilities	92,183.4	98,189.3	105,558.2	121,832.0
Total Net Current Assets	(9,708.6)	8,193.4	11,884.8	26,081.0
Misc. Expenses not written	0.0	0.0	0.0	0.0
<b>NOTE</b>				
Bk Val Unquoted Investments	17,163.3	19,238.9	22,699.1	26,861.7
Mkt Val. Quoted Investments	46,862.1	9,448.9	40,799.2	34,760.5
Contingent Liabilities	12,769.4	22,581.9	25,600.1	21,492.3
Dividend (%)	450	995	450	525

## Quarterly Income Sheets

(₹ mn)

Quarter Ended	Mar 13	Jun 13	Sep 13	Dec 13
Net Sales	82,574.00	74,107.00	78,625.30	87,268.50
Cost Of Sales	55,510.80	46,193.90	46,866.90	54,425.50
Operating Profit	27,063.20	27,913.10	31,758.40	32,843.00
Recurring Income	2,539.80	2,031.80	2,788.60	3,910.60
Adjusted PBDIT	29,603.00	29,944.90	34,547.00	36,753.60
Financial Expenses	242.70	169.50	0.00	91.40
Depreciation	2,066.90	2,153.00	2,208.70	2,259.20
Other Write Offs	0.00	0.00	0.00	0.00
Adjusted PBT	27,293.40	27,622.40	32,338.30	34,403.00
Tax Charges	8,013.60	8,709.10	10,033.00	10,549.60
Adjusted PAT	19,279.80	18,913.30	22,305.30	23,853.40
Non Recurring Items	0.00	0.00	0.00	0.00
Other Non Cash Adjust	0.00	0.00	0.00	0.00
Net Profit	19,279.80	18,913.30	22,305.30	23,853.40

## 52 Week Index Relative Percentage Appreciation



## ITC vs SENSEX

## Risks Associated

Policy directives from the union government form the biggest risk to ITC. The tobacco sector is highly levered to policy decision from the central and state governments. Any changes in the tax structure could prove to be a negative for the company. Stricter laws against smoking and potential changes to include plain packaging could also have a negative impact on ITC's earnings and thus market price. ITC has a dominant 70% market share by volume in India's cigarette sector, with the cigarette business accounting for over 80% of ITC's profits. Any potential opening up of the sector to foreign companies would increase competition, which could hurt ITC's dominant position in the market. Additionally, continuing losses in the FMCG business is a risk.

Indians are known for their dual consumption of tobacco, which means a tobacco consumer would consume tobacco in more than one form. While Cigarettes are considered the premium segment, so is the government tax burden always on their anvil, rather the government has lower taxes for all other forms of tobacco and some are even tax free industries. The rising tax burden on cigarettes may force the consumers to shift to other cheaper modes of tobacco in the long run thus harming revenues for the company. This fact is further quantified by the fact that the total tobacco consumption in India increased from 406 mn kg to 475 mn kg in a span of last 30 years however the consumption in the form of cigarettes declined from 86 mn kg to 72 mn kg.

**In a Nutshell**

Cigarette consumption still accounts for only 15% of overall tobacco consumption in the country. Over the long term, as consumers migrate to cigarettes from other forms of tobacco, ITC will be the biggest beneficiary. Consumers have been trading up from the regular-size sticks to King size across markets, and this has helped the margins as has been evident over the last couple of years. This is the biggest positive for ITC as the mix improvement part is likely to be a sustainable form of revenue and profitability driver. The King-size sticks are growing at a double-digit percentage, much faster than the regular-sized ones. This is a key long term driver of cigarette business profitability. The competitive landscape remains a positive for ITC as foreign investment in expanding capacities is banned by the government. This is unlikely to change in the medium term as the government has been reluctant to allow foreign participation in tobacco, which means ITC will continue to have a dominant share of the market in the medium to long term. Some of the states have banned use of Pan Masala as well as other forms of tobacco recently. This move is likely to help migrate consumers to cigarettes over the long term, where ITC will likely be the biggest beneficiary, in our view. While we do not expect any short-term benefits from this move, in the longer term, it is a positive for ITC. Within a relatively short span of time, the Company has established several strong consumer brands in the Indian FMCG market. Company's Branded Packaged Foods business grew significantly during the year, recording growth in market shares and enhanced market standing across segments.

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**Rating Interpretation**

<b>Buy</b>	: Expected to appreciate 20% or more over 12-months	<b>Reduce</b>	: Expected to depreciate up to 10% over 12-months
<b>Accumulate</b>	: Expected to appreciate 10% to 20% over 12-months	<b>Sell</b>	: Expected to depreciate 10% or more over 12-months
<b>Trade Buy</b>	: Expected to appreciate more than 10% over 45-days	<b>Trade Sell</b>	: Expected to depreciate more than 10% over 45-days

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