

## Marico Industries

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Rs160

### Key takeaways of the Analysts' Meet held by the company on 14 May 2003.

In Q4FY03, Marico's sales grew by 6% YoY to Rs1.90bn. OPM (ex. Other Income) during the same period declined by 310bps from 11.30% to 8.20%. Net profit declined 2% to Rs150mn in the same period.

For the full year (FY03), the company's sales grew by 10% to Rs7.38bn. OPM (ex. Other Income) declined by 120bps from 10.80% to 9.60%. Net profit grew by 6% to Rs520mn (adjusted for extraordinary income of Rs10mn, net of tax) during FY03.

### Major reasons for the lackluster performance in Q4FY03

- Relatively high cost of safflower oil during H2 FY03. Safflower oil is the main ingredient of Marico's *Saffola* brand cooking medium offering that is primarily promoted on the "Health Platform" (April-June is the main harvest time for safflower seeds in India).
- VAT related issues and the resultant uncertainties.
- Levy of excise duty at 8% ad valorem on branded oils in Budget 2003.

### Financials

Financials	Rs Million					
	Q4FY02	Q4FY03	Growth	FY02	FY03	Growth
Net Sales	1802.7	1904.6	6%	6710.1	7382.7	10%
Net Profit	153.5	150.8	- 2%	493.2	521.1*	6%
OPM (ex. O.I)	11.30%	8.20%		10.80%	9.60%	
Equity	145.0	290.0		145.0	290.0**	
EPS (Rs)				34.00	18.00	

Note: \* - Adjusted for Extraordinary Income of Rs10mn, net of tax; \*\* - After 1:1 Bonus Issue

### Key Highlights

- *Parachute Jasmine, Shanti Amla, Mediker oil and Mediker anti-lice oil*, etc., some of the high-margin value-added products in the hair care segment, grew at a relatively faster rate of 16% in FY03. The company focused less on low-margin products such as *Sweekar* sunflower oil. In sum, the management took the right steps towards moving away from low margins products to higher ones.
- Marico's YoY market share in hair oil improved from 13.5% to 16% in FY03 driven by *Parachute Jasmine* and *Shanti Amla*. Major player Dabur's share in this category too declined.
- International business in the hair care business continued to grow especially in the Gulf and Bangladesh (CAGR of 40% between FY98 and FY03) at Rs700mn in FY03, i.e., 9% of sales (around 3% of sales in FY98). This was on the back of effectively meeting regional tastes and offering new products such as *Parachute* hair cream in the Gulf.
- YoY market share in coconut oil (CNO) improved from 54.8% to 55.6% in FY03 driven by *Parachute* rigids/minis. Share of HLL declined by 1.5%.
- Conversion of "loose" CNO consumers to the *Parachute* brand in mini packs (Rs1 per price point) continued to deliver growth. Recently, Marico also came out with a different small pack *Parachute* CNO which is quite different from the usual sachets.
- Share of new products in overall sales rose from Rs800mn in FY02 to Rs1.32bn in FY03. As a percentage of sales, new products contributed to 17% of sales -- around 4% three years ago.

- The company acquired the *Meal Maker* brand for Rs18mn. *Meal Maker* is a soya-based food ingredient positioned on the “Health Platform” in conjunction with Marico’s philosophy of entering high-end foods segment in line with the present offering of *Saffola* low salt.
- Advertisement and sales promotion spend continued in a narrow range of around 12.5% of sales without affecting brand equity, brand building efforts especially for new products and profitability. The company continued to pursue less of freebies distribution strategy unlike many other FMCG players. It also pursued the strategy of prototyping new launches for a higher success rate.

### **New Businesses’ roundup**

Recently, Marico ventured into two new businesses - *Kaya* skin care clinics (through *Kaya Aesthetics Limited* in which Marico has a 76% stake; the balance is held by *Adil & Associates*) and *Sundari* brand ayurvedic skin care products in the US (through *Sundari Inc.*, in the US in which Marico has a 63% stake).

#### *Leveraging on new businesses*

Per se these two businesses don’t find place in Marico’s core business. However, the contention has been that they would help Marico leverage its expertise in understanding and meeting the retail consumer needs and thereby evolve the businesses that have excellent growth potential. In addition, *Sundari* acquisition would provide Marico with good learning curve and capitalise on its distribution channel for entering the lucrative US market even in respect of its traditional hair care products that need to be suitably modified.

*Kaya* skin care clinics are scientifically managed and well-equipped clinics run under the supervision of professional dermatologists providing comprehensive remedies for skin related problems and maintenance. Presently, there are 8 such clinics (including 2 in Dubai) with an investment of Rs80-100mn. Marico’s investment in *Sundari* is to the tune of US \$1.15mn.

The management refused to divulge as to how the two new businesses would perform in FY04 since it is still at the nascent phase. However, the initial response to the skin care clinics has been positive. The company targets setting up 100 clinics in India in the next 4-5 years covering the metros and large cities (presently the clinics only are only there in Mumbai and Delhi). The opportunity being looked at is Rs10mn per clinic per annum – Rs1bn in all. The *Sundari* range of products has some downside having incurred losses last year. Nonetheless, the management expects to break-even this year. Going by present sales in the USA and UK, there exists potential to be leveraged globally.

### **Future Outlook**

FY04 has started with moderate consumer confidence in a somewhat uncertain business climate. Though no specific topline and bottomline growth numbers were disclosed, in FY04 Marico expects growth to be in double digits. The company would be looking at bettering its FY03 performance in the domestic market by laying emphasis on maintaining consistency (it could be assumed at 12-13%).

This would be aided by:

- Continued thrust on present value added hair care products and leveraging *Saffola* variants.
- Plans to take *Mediker* anti-lice oil in hair care category national.
- Launch of *Shanti Thanda* (cool) hair oil to complement the range. The market for cool oil is approximately Rs1.75bn growing at 15% p.a.
- Share of new products aimed at 25% in FY04.
- Conversion from loose to branded CNO (present market size for loose CNO being 1.5x that of branded packed CNO) to continue to drive growth. This would be further accentuated by the recent launch of the new handy sachet variant in blister packs (Rs1per price point).

*Targeting double digits FY04 bottomline*

The company expects its bottomline to grow at double digits in the domestic market in FY04. However, this would mainly be dependent on the company's operating margins, which in turn would depend on prices of safflower oil and other raw materials. Safflower oil (key raw material for the company) prices after having spiked have now stabilised.

*RoCE of 30% on high distribution*

The company looks at maintaining a 30% RoCE in FY04 with high distribution policy continuing. Marico's dividend payout in FY03 was 26.50% on enhanced equity share capital of Rs290mn (1:1 bonus issue). In addition, during FY03, Marico issued bonus 8% preference shares in 1:1 ratio to its equity shareholders. The past trend of low effective tax rate of 9-13% should continue for another 2-3 years. In the long run though, the effective tax rate could go up unless helped by tax planning, in which direction the management has started working.

VAT uncertainties still persist. But, overall it should be positive for the industry. Respite has come with the withdrawal of ad valorem excise duty on branded oils with the levy now coming on refining.

**View and Valuation**

Marico is on a major investment – cum – transition phase. Growth in the core business is expected amidst competitive pressures. The two new businesses have a long way to go before witnessing upsides. However, in the short term they are likely to experience pressures. Quarterly profits would vary depending on contribution from the new businesses. The management is open to acquiring brands or businesses. Similarly, it is also open to getting out of low margins products/brands, which destroys the company's value.

At current levels of Rs160, Marico trades at 9x its FY03 fully diluted EPS of Rs18. We believe that at this level, Marico is evenly balanced out with no major cause for upside in the near to short term. We believe the company will grow in its core business but concerns about the new ventures would keep the sentiment low towards the stock.



19 May 2003  
Analyst Meet

**Stock Ratings Absolute Returns**

Buy : > 25%  
Out Performer : 16 - 25%  
Market Performer : 0 - 15%  
Under Performer : < 0%

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