

12 December 2008

India Consumer Sector

Defensive appeal, at a premium

Overweight

Nifty/Sensex: 2784/9163



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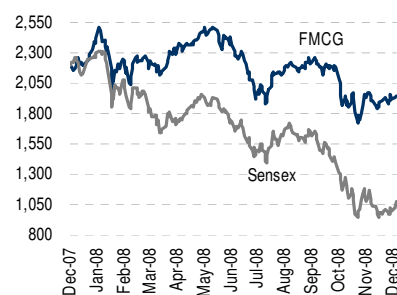
- **Initiating sector coverage.** Despite the sector's recent out-performance vs the Sensex, we expect robust earnings (15% FY08-10e CAGR vs 6% CAGR for the Sensex) and the sector's defensive appeal to hold valuations at premium levels. Declining bond yields, too, render these dividend stories attractive.
- **Defensive appeal.** With the macro outlook challenging, the consumer sector will retain its safe haven status. Consumer companies offer debt-free balance sheets, enjoy strong pricing power and relatively inelastic demand. Risk aversion should sustain interest in consumer companies.
- **Sub-segmentation strategy to help.** We expect companies' sub-segmentation strategy to help pass on raw material costs through price hikes where competition is low. This strategy also helps arrest down-trading.
- **Volume growth, margins under pressure.** Though some raw material prices have fallen, many are still firm – up 15% yoy. As some companies have hiked prices by around 10%, lower pricing power is expected to result in margin contraction. Slowing income growth should impact volume growth.
- **Stock calls.** We prefer stocks that have lower premium valuations and well above market average earnings growth. We assign Buy ratings to Colgate, Britannia and GSK Consumer, Hold to Nestlé and Marico and Sell to HUL and Dabur.

India consumer sector – Valuation matrix

	HUL	Nestle	Dabur	Colgate	Marico	Britannia	GSK
Rating	Sell	Hold	Sell	Buy	Hold	Buy	Buy
Price (Rs) (5 th Dec 2008)	235	1,390	82	401	51	1,165	519
Target Price (Rs)	207	1,495	88	513	61	1,516	850
Market cap (US\$m)	10,234	2,680	1,417	1,091	621	557	437
Upside (%)	(12)	8	7	28	20	30	64
Target PE (x) (FY10e)	20.9	23.0	18.2	19.0	18.0	14.0	17.0
FY08-11e EPS CAGR (%)	11.4	18.7	14.0	21.9	12.3	18.8	14.1
FY10e RoE (%)	166.0	102.9	45.6	221.1	47.2	28.4	25.2
FY10e RoCE (%)	192.8	150.0	52.0	261.3	39.7	33.3	38.4
FY10e PE (x)	23.8	21.6	17.0	14.8	15.1	10.8	10.3

Source: Anand Rathi Research

BSE FMCG vs Sensex



Source: Capitaline, Anand Rathi Research

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