

Consumer Goods

Price stability to aid demand

Even as FMCG players strategize for demand recovery and enhancing volume growth on a low base/expected improvement in demand, price growth has largely dried up, given easing raw-material prices for most categories (in our coverage, HUL, GCPL, Britannia have negative pricing). Inflationary trends have sustained in select categories like coffee, tea, milk, and chocolate which has led to steady price hikes. Oral care remains divergent, with players continuing to effect price hikes with enhanced formulation. We see the raw-material basket benefitting from expected easing of prices of crude/palm oil in producing countries, in 2HFY25. FMCG companies are eyeing low single-digit price growth which, along with high single-digit volume growth, would aid double-digit revenue growth in FY25. Sector valuations factor-in an improved demand milieu and healthy earnings ahead. Given the pricy valuations, we remain selective and continue to favor HUL, Dabur, Honasa Consumer, and Emami.

Home and Personal care prices stable; competitive intensity on the rise

Amid a relatively better raw-material (RM) setting, most product prices in the home and personal care segment have been stable. For large product-categories like Soap and Household insecticide, the companies are done with technological upgrades which is likely to aid growth. In laundry, we see faster shift toward liquids, where increased competition is resulting in price wars. In oral care, product superiority has been a key enabler for the consistent price hikes. Discretionary segments like Shampoo/Hair color are likely to see demand recovery with onset of the festival season and higher number of weddings. Hair oil, though, would remain stressed, with consumers moving to lower priced brands (ie brand downgrade). Easing in crude prices will positively impact the RM basket. Palm oil price trajectory is crucial for price hikes, as increase in custom duty rate would drive inflation, but cut in export duty in Indonesia and surplus inventory in Malaysia would offset the inflationary impact, in our view.

Inflationary raw material prices in Foods segment, a concern for demand

Prices of RMs in the Foods segment have been inflationary, particularly of milk, cocoa, coffee, and tea. FMCG players have gradually effected price hikes in respective categories to pass on the inflation impact. In Edible oil, prices have been steady for the last three months, with easing of RM prices in the base. In Biscuits, price actions have been limited, and players have used trade promotions to pass on deflation in RM prices. Incrementally, surge in wheat/palm oil prices would limit price-cuts and a surge in competition would limit price hikes. The milk, baby foods, and functional nutrition segments continue to be impacted by inflationary prices of milk. Inflation in prices of tea continues to compel consumers to move downgrade to lower-priced brands, with prices likely to further rise in the coming procurement season in 2HFY25. Coffee and Chocolate prices are still high, causing steady price hikes. Juices and Honey have seen stable prices.

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Consumer Goods Price hikes on the rise

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Our monthly price checks across FMCG segments revealed select price hikes across most categories, except soap and edible oil. The impact of easing raw-material prices on demand recovery and enhancing volume growth on a low base/expected improvement in demand, price growth has largely dried up, given easing raw-material prices for most categories (in our coverage, HUL, GCPL, Britannia have negative pricing). Inflationary trends have sustained in select categories like coffee, tea, milk, and chocolate which has led to steady price hikes. Oral care remains divergent, with players continuing to effect price hikes with enhanced formulation. We see the raw-material basket benefitting from expected easing of prices of crude/palm oil in producing countries, in 2HFY25. FMCG companies are eyeing low single-digit price growth which, along with high single-digit volume growth, would aid double-digit revenue growth in FY25. Sector valuations factor-in an improved demand milieu and healthy earnings ahead. Given the pricy valuations, we remain selective and continue to favor HUL, Dabur, Honasa Consumer, and Emami.

Categories with price hikes on the rise, footprints continue to lead. Our monthly product IMP tracking of 14 FMCG categories suggests incremental price hikes. Soap, edible oil, and biscuits were the three categories where we saw negative pricing. However, for the rest of the categories, we have started seeing incremental price hikes. With inflation-driven price hikes over in the base, FMCG companies are looking to drive inflation-linked price hikes for FY25. The category heat map suggests incremental price hikes in toothpastes, hair oil, cereals, chocolates, milk products, health and drinks, tea, and coffee. Product prices for soaps and edible oil continue to see downward revisions. Prices of baby food and winter offerings have been stable in two months.

Muted demand outlook to keep the top-line in a slow lane. FMCG companies have been hopeful of demand recovery ahead, with no material tailwind. In the long term, getting the top-line through pricing also gives relevance. Contrary to the common perception of FMCG companies affecting price cuts to pass raw-material benefits, players are revisiting the case for price growth in line with inflation ahead, as highlighted in our sector review note (Sept 2023), margin recap is largely in place for most FMCG companies, except for HUL and Dabur. We see the emergence of a scenario where further price hikes should help companies drive margin, which will support double-digit earnings momentum. Here, relevant competition is going to be heavy, which, so far, has been in place amid national players. Regional competitive pressure is likely to sustain, as large players are now operating with cost and material advantages.

Demand pressure hurting valuations; preference for Dabur and ITC. The FMCG sector has gone through time correction, where most leading companies have recorded a three-10 year historical P/E, except for Colgate and GCPL, which have sustained their premium valuations. The FMCG sector forward P/E valuation at 5x is now trading at a discount to 5x by average forward P/E for the last five years and is at a premium to 4.5x to 10-year historical P/E average. Valuation premium to the broader market seems to be gradually eroding to <10%. Going ahead, muted demand setting, as we see valuation holding on as companies will try to further expand margins, which will help in earnings delivery. We continue to prefer opens, with execution and better valuations like ITC and Dabur India. We like GCPL, but the valuation caps the upside. We remain bullish on Colgate.



Eyes on the market Emkay Connect: Assessing demand setting in East India

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We hosted a group of investors for Emkay Connect – our East India trip covering major listed consumer companies (across segments), selected players, sector experts, and supply chain partners. Consumption picking in FMCG segments is clearly visible with large incumbents focusing on growth. We continue to see sector valuations factoring in the improved demand setting in East India and better execution aiding faster earnings. We remain selective and continue to favor HUL, Dabur, Honasa, and Emami.

Top-10 takeaways from our corporate connect and ground checks are: (1) ahead of time winter trade leading to help Dabur report better growth in Q2; (2) quick formalization of active smoke category is leading to better growth for not only large players, but also for fast-scaling regional players like Amrapur Bhandari; (3) sustained healthy in beauty care for Himalaya and others for The Derma Co.; (4) in beverages, Campa would look to disrupt the market as four-pack agreement comes up for renewal in late 2024; (5) competition has been a fast growing channel, where adoption has been healthy in urban centers; accordingly, 40% of media budget is now digital; (6) in pesticides, Dhan has not made many inroads given limited offering and lack of brand appeal; (7) Alcohol continues to see premiumization; price hikes (offset by demand) in brand (Bengal) will in cigarettes; Marubeni does have visible volume uplift in urban centers, where a massive offer of 8-leaf playing field and south side has been good; (8) leaf tobacco inflation to have a bearing on margins for cigarette; supply chain sees price hikes undertaken to only product margin being absorbed, but any excess pricing should have a bearing on volume; and (9) renewed thrust on hygiene seen across companies where players are upbeat on festive demand recovery.

Consumer adoption of convenience fast paced; premium segment doing well. Consumption of revenue in East for most consumer companies has been low, given slower consumer evolution and a price sensitive consumer base. Unlike other parts of the country, unorganized segmentation has been high, which we see as a factor of relatively limited suburbanization. The setting post-Covid seems to be shifting quickly toward formalization, where consumer is seeking convenience and concentration of organized players has been high.

Rural threat phosessed, urban thrust enhanced; focus on execution. Rural is poised for growth recovery when FMCG companies have taken action. Enhanced focus is on urban, where select channels continue to see consumer adoption, leading to faster growth. Thrust on product superiority in selling premiumization. Trade expects innovation intensity to expand with players focusing on brand innovation. Our contact with media player suggest 40% of industry spend is now on the digital medium.



Rating, Target Price and Valuation

	Rating	CMP (Rs)	TP (Rs)	Upside (%)	P/E (x)		EV/EBITDA (x)	
					FY25E	FY26E	FY25E	FY26E
Britannia Industries	ADD	6,191	6,250	1	61.3	53.1	42.4	37.4
Colgate-Palmolive	REDUCE	3,682	2,850	(23)	65.0	59.5	45.2	41.3
Dabur India	BUY	656	750	14	55.1	46.6	40.6	34.2
Emami	BUY	761	950	25	40.2	36.4	29.7	26.7
Godrej Consumer Products	ADD	1,446	1,450	-	64.8	53.4	43.0	37.4
Hindustan Unilever	BUY	2,951	3,200	8	63.4	56.7	44.4	39.9
Honasa Consumer	BUY	474	600	26	102.2	63.7	82.2	45.8
ITC	ADD	515	520	1	29.1	26.7	22.5	20.7
Marico	REDUCE	705	700	(1)	56.8	49.4	40.8	35.8
Nestlé India	ADD	2,696	2,650	(2)	77.2	68.2	52.1	45.6

Source: Company, Emkay Research