

12 June 2024

India | Equity Research | Sector Update

Consumer Staples & Discretionary

Rising tide lifts all – prefer companies which are in self-help mode

Recent optimism of acceleration in consumption, driven by expectations of the government implementing social welfare schemes, may improve the demand conditions for all consumer companies, though conversion of these expectations into better volume growth might span 12–24 months. For FY25, we continue to envisage headwinds petering out (negative pricing, competitive intensity) while a few tailwinds (populist measures, above normal monsoons, rural recovery) shall help lift the sector. Though, valuation multiples provide a shallow margin of safety – trading similar to or higher than their 5-year/10-year average of their one-year forward P/E multiples. That said, we continue to prefer companies executing well with a self-help approach while consumption recovery is another tailwind too for these companies. Our top picks in consumer staples remain Marico, Godrej Consumer (GCPL), Tata Consumer, Jyothy Labs and Honasa Consumer.

Populist measures may drive higher consumption growth

Consensus expects higher spending on welfare schemes (direct benefit transfers, MNREGA etc.) and it is somewhat priced in too. Higher welfare schemes are likely to drive faster private consumption growth as compared to the last few years. Higher real rural wage growth has high correlation with HUL's volume growth (**Exhibit 1**). Historically, India has been a consumption-led economy, but consumption growth has been lagging overall GDP growth in FY24 (**Exhibit 2**).

Above-normal monsoons augur well for consumer sentiment

India Metrological Department has reiterated that the country is likely to receive above-normal monsoons through Jun–Sep'24. Though, historically we have not seen a very high correlation between monsoons and volume growth (correlation of HUL's revenue growth with monsoons/agri-GDP growth is 0.2/0.6 – see our earlier [report](#)). That said, our conversations with various managements historically, suggest that normal monsoons do lead to improved consumer demand sentiment, which in turn enables better offtakes. Further, discretionary demand has higher linkage with better monsoons and agri-GDP.

Early signs of rural recovery

During Q4FY24 earnings calls, certain companies highlighted early signs of rural recovery in their recent performance. Dabur noted that their rural has outperformed (by ~120–130bps) urban for the first time in the last three years. Emami too witnessed improved performance in their rural markets. Colgate India also highlighted positive macros in rural with rural outperforming urban by ~200bps. Jyothy Labs saw its rural markets picking up and the slowdown seems to be bottoming out. Marico recorded a visible uptick in rural growth towards the end of the quarter. Zydus Wellness mentioned that it witnessed a gradual pick-up in demand and growth in rural, which has started converging with that of urban demand. That said, sustainability of recovery in rural demand is key for improvement in performance of consumer staples.

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Pricing growth lever likely to lie between neutral and positive in FY25

Most of the consumer staples companies have been weathering negative (low-single digit to mid-single digit) pricing due to significant correction in raw material (RM) prices while also passing on benefits to consumers. Therefore, price decline headwinds for most of the companies are likely behind us now, except for a few companies in H1FY25. Management of most companies have highlighted that they expect low-single-digit pricing growth in FY25 led by moderate inflation in input cost prices in H2FY25. Therefore, overall pricing growth needle will likely point between neutral to low-single-digits for FY25, in our view.

Regional/smaller players' relative competitive intensity to slacken

Another headwind for large consumer staples in FY24 was the increased competitive intensity from regional/smaller players. Historically, smaller players exit the market at times of significant input cost inflation, which leads to extensive market share gains for large players (occurred in FY22 and FY23); they re-enter the market when input cost prices abate or become favourable and recoup some of lost ground from the larger players (occurred in FY24). That said, we do not expect any incremental headwinds of increased competition from smaller/regional players. Further, most of the consumer staples companies have beefed up their ad-spends (~24% YoY increase in ad-spends in FY24 vs ~1-6% YoY increase in FY20-23), which is likely to blunt the impact of increased competitive pressure.

Numeric distribution expansion – a key growth driver

Over the last few years, Nestle and Jyothy Labs delivered volume outperformance thanks to the companies activating their sales growth vectors effectively (numeric distribution expansion and improved line selling). It is comprehensible that distribution expansion as a growth lever may not be as potent for all the large companies as it was a decade ago; that said, a few companies (Marico, Dabur, GCPL, Jyothy Labs, Mrs. Bector's) have highlighted plans in this avenue over the next two–three years, which consequently may drive outperformance. Further, assuming that the government's welfare schemes will be rural markets-focused, which is also on the radars of most of the companies, this exercise of distribution expansion may yield better results.

Valuation multiples likely to have downside risks

Most of the large consumer staples companies are currently trading either similar to or higher than their last 10-year/5-year average one-year forward P/E multiples (**Exhibit 6**). With that as context, we see shallow margin of safety. Further, even if welfare schemes are implemented to drive consumption, it will likely take 12–24 months for these initiatives to translate into actual volume growth improvement. Therefore, there are downside risks to these valuation multiples, in our view.

Prefer companies executing well (with self-help approach)

We continue to prefer companies that are executing well and have self-help approach to drive growth despite the above headwinds through multiple vectors such as: 1) Distribution – expand direct distribution, or focus on improve line-selling. 2) Disrupting existing or new categories with right to win. 3) Growing via acquisitions by utilising their strong balance sheets (likely getting into fast-growing new demand spaces).

Our top picks in consumer staples are: Marico, Godrej Consumer, Tata Consumer Jyothy Labs and Honasa Consumer.

Welfare schemes may lift small ticket-size discretionary companies

As discussed earlier, if more welfare schemes are implemented, it may lead to higher disposable incomes; discretionary consumption will also likely improve (which has been under stress over last few quarters), as footfalls have been impacted with consumers shying away from discretionary consumption [except services] over the last few quarters. In our view, small ticket-size discretionary consumption is likely to benefit. However, we would still prefer companies executing well.

Alcobeve: Popular segment has been witnessing significant demand headwinds, which may see a recovery. Further, consensus is watching any potential policy changes in Andhra Pradesh (AP). Over the last few years, some alcobeve companies had downsized operations in AP. There may be an opportunity to ramp up presence incrementally.

Apparel retail: The sector is facing growth challenges at premium price points while the value segment's performance has been superior. Consequently, we believe that the welfare schemes are unlikely to have any meaningful impact for branded (>INR 3,000 ASP) players. However, in the value segment, we expect retailers/brands that are over indexed to tier-3-and-beyond cities (VMART) to be primary beneficiaries of such welfare schemes. However, companies that operate in the value segment (<INR 1,000 ASP) are over-indexed to tier-1/2 cities (TRENT, GO Fashion) may benefit marginally.

Footwear retail: Demand pressure in the value segment (<INR 3,000 price point) may witness potential improvement while premium segments continue to maintain growth momentum. Hence, retailers with superior brand (for given value) appeal (like Metro brands) may stand to benefit. However, we remain cautious on players that are facing revenue growth challenges due to underlying changes in the business/distribution structures (like BATA).

Grocery retail is likely to benefit. For DMart, general merchandise (GM) and apparels segment, which has been witnessing moderation in growth rates over the last few years, will likely be a significant beneficiary. Interestingly, consumers were still shopping in the foods and FMCG segments, though they were cutting down on discretionary consumption in GM and apparel segment. The GM and apparel segment already appears to have bottomed out in Q4FY24.

Jewellery retail is unlikely to benefit due to its higher ticket-size, in our view. That said, the segment has been outperforming within the discretionary segment driven by its market share gains from the unorganised segment, which will likely continue. That said, Titan, in our view, is navigating through medium-term challenges of higher competitive intensity – leading to its cautious approach on both growth and margin guidance. Further, other jewellery retail companies provide very low margin of safety given their valuation multiples, in our view. We remain positive on Kalyan Jewellers given its continued outperformance (highlighted double-digit SSSG growth till Akshaya Tritiya in Q1FY25).

Paints: Generally, consumers take painting decision twice in a decade. Hence, the decision to paint the house is from balance sheet funding (i.e., accumulated savings/loans) and not necessarily from additional savings in any one year. While we do not model any material benefit to paint companies, we believe there will be small stimulus in rural markets (which are already under stress). Also, the additional savings may help drive premiumisation. Additional savings in the hands of labour (painters) may also help pause labour inflation. It may result in reducing overall spends on paints.

QSRs are also witnessing pressure on SSSG over the last few quarters. This is largely owing to the possible reason that the marginal consumer is either reducing frequency or ticket size to manage his/her budget, in our view. Therefore, higher incomes may ease the pressure on the marginal consumer's wallet, there could be improvement in ticket size/frequency. JUBI's delivery fee waiver can be a significant driver for SSSG, in our view. We remain constructive on JUBI and Sapphire Foods in QSRs.

Valuation and risks

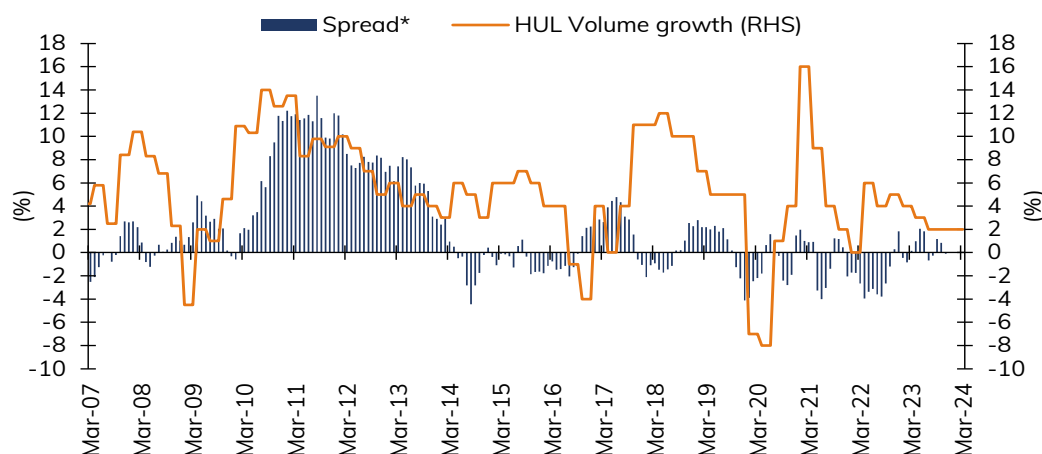
We value the stocks as per DCF methodology (WACC and TG ranging from 10–13%, 3–6%, respectively), except for Adani Wilmar, Burger King India, Godrej Consumer and Tata Consumer, which we value on a SoTP-basis. Please refer to **Exhibits 7-8** for updated TP and ratings.

Upgrades – ADD to BUY – Jyothy Labs

Downgrades – ADD to HOLD – Britannia, Restaurant Brands

Key upside risk is better-than-expected gross margin due to correction in input prices. Key downside risk is unexpected irrational competition due to deceleration in general consumption demand.

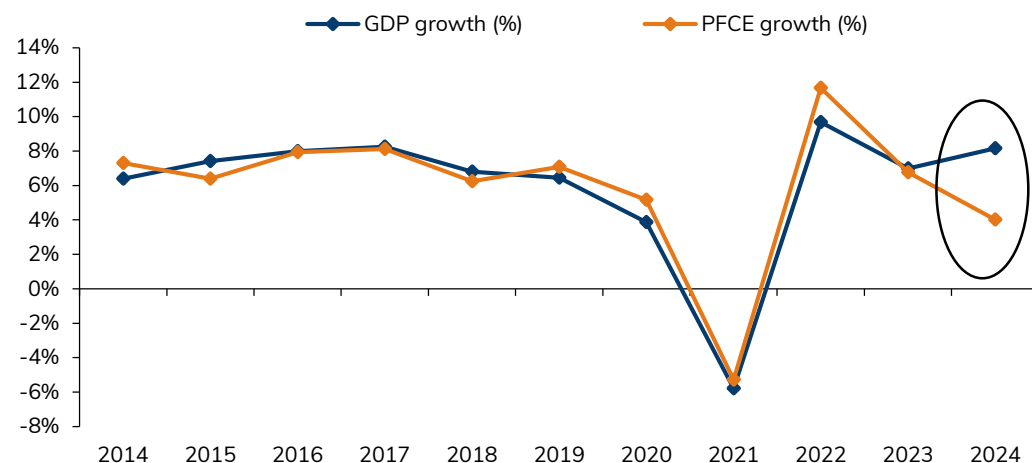
Exhibit 1: Rural real wage growth versus HUL's volume growth



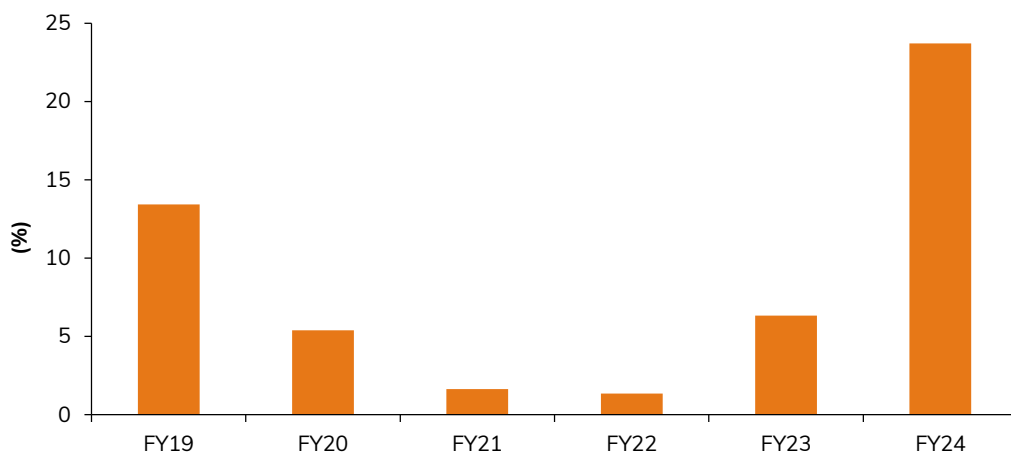
Source: I-Sec research, Company data, Bloomberg, MOSPI

* Spread = Rural CPI – Rural Wage Growth

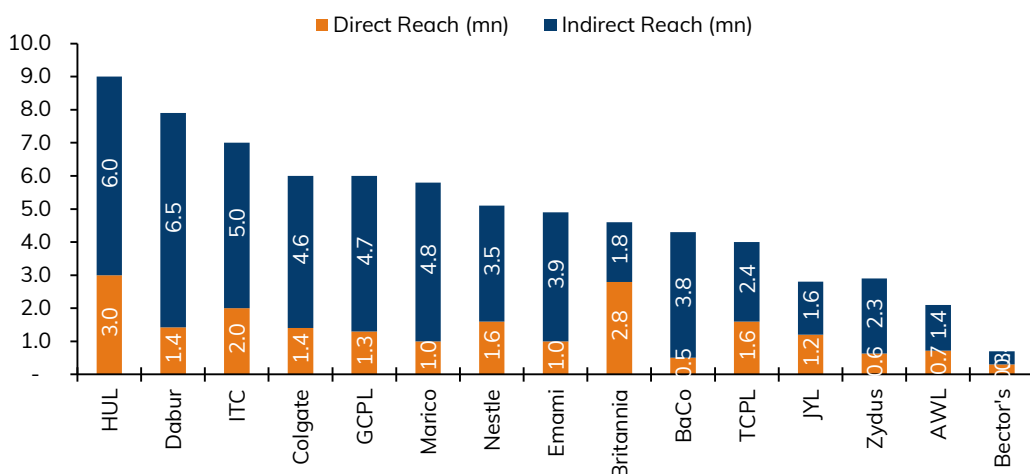
Exhibit 2: Private Final Consumption Expenditure (PFCE) growth lagged GDP growth in FY24



Source: I-Sec research, Company data

Exhibit 3: Ad-spends growth over last few years

Source: I-Sec research, Company data

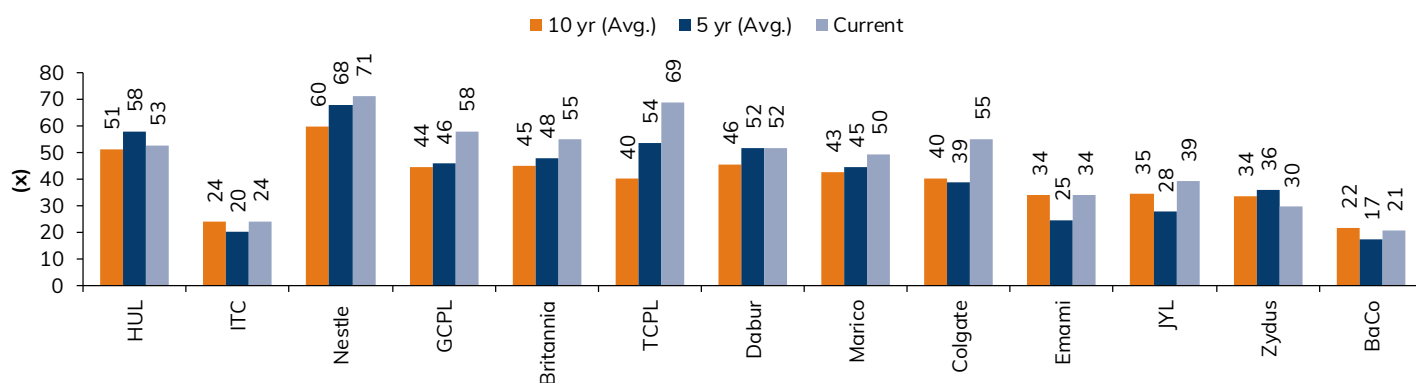
Exhibit 4: Distribution reach of consumer staple companies

Source: I-Sec research, Company data

Exhibit 5: Low correlation between HUL's revenue growth with both agri-GDP and monsoon rainfall deviation

	Average agri-GDP growth (%)	Monsoon rainfall deviation from LT average (%)	Average HUL revenue growth (%)	Correlation (HUL with Agri-GDP)	Correlation (HUL with rainfall deviation)
1980-1989	11.60	-3.00	10.90	-0.10	-0.10
1990-1999	13.30	-1.10	21.00	-0.20	0.10
2000-2009	8.60	-4.20	5.70	0.70	0.10
2010-2019	12.67	-5.63	8.88	0.25	0.26
2014-2023	10.56	0.39	7.73	0.10	0.28
Overall (1990-2023)	11.43	-2.13	11.27	0.56	0.17

Source: I-Sec research, Company data, Ministry of Agri Research, IMD

Exhibit 6: One-year forward P/E multiple

Source: I-Sec research, Bloomberg

Exhibit 7: Updated target prices and rating changes

	Target Price (INR)		Rating	
	Old	New	Old	New
Staples				
Adani Wilmar	360	360	HOLD	HOLD
Bajaj Consumer	300	300	BUY	BUY
Britannia	5,000	5,250	ADD	HOLD
Colgate	2,900	2,900	HOLD	HOLD
Dabur	560	650	ADD	ADD
Emami	650	780	ADD	ADD
GCPL	1,525	1,650	BUY	BUY
HUL	2,350	2,600	HOLD	HOLD
Honasa Consumer	550	550	BUY	BUY
ITC	480	480	ADD	ADD
Jyothy Labs	480	520	ADD	BUY
Marico	650	750	BUY	BUY
Mrs. Bector's Foods	1,450	1,620	BUY	BUY
Nestle	2,600	2,600	HOLD	HOLD
Tata Consumer	1,360	1,360	BUY	BUY
Zyklus Wellness	1,850	2,100	ADD	ADD
Discretionary				
Avenue Supermarts	5,000	5,000	ADD	ADD
Bata	1,350	1,400	HOLD	HOLD
Cello	1,060	1,060	BUY	BUY
FSN E-Commerce Ventures	175	175	HOLD	HOLD
Go Fashion (India)	1,200	1,200	BUY	BUY
Jubilant FoodWorks	580	620	BUY	BUY
Kalyan Jewellers	460	460	ADD	ADD
Metro Brands	1,210	1,210	ADD	ADD
Page Industries	34,000	38,000	HOLD	HOLD
Restaurant Brands Asia	115	115	ADD	HOLD
Sapphire Foods	1,550	1,650	ADD	ADD
Titan	3,400	3,400	HOLD	HOLD
United Spirits	1,220	1,400	ADD	ADD
Vedant Fashion	1,000	1,200	ADD	ADD
Westlife Development	800	880	ADD	ADD
Paints				
Akzo Nobel	2,520	2,600	HOLD	HOLD
Asian Paints	2,450	2,600	REDUCE	REDUCE
Berger Paints	450	450	REDUCE	REDUCE
Indigo Paints	1,380	1,380	HOLD	HOLD
Kansai Nerolac	290	300	ADD	ADD

Source: I-Sec research

Exhibit 8: Valuation summary

Company	TP* (INR)	Rating	PE (x)		EV/EBITDA (x)		ADTV	Market Cap	
			FY25E	FY26E	FY25E	FY26E	(USD mn)	(INR bn)	(US\$ bn)
Staples									
Adani Wilmar	360	HOLD	48	38	23	20	9.8	447	5.3
Bajaj Consumer	300	BUY	21	18	17	15	1.9	37	0.4
Britannia	5,250	HOLD	55	49	38	34	25.7	1,329	15.9
Colgate	2,900	HOLD	55	50	39	36	15.1	803	9.6
Dabur	650	ADD	52	46	41	37	25.7	1,087	13.0
Emami	780	ADD	34	30	29	26	10.5	314	3.8
GCPL	1,650	BUY	58	50	43	37	19.0	1,462	17.5
HUL	2,600	HOLD	53	47	38	33	74.2	6,006	71.9
Honasa Consumer	550	BUY	86	56	65	44	3.4	141	1.7
ITC	480	ADD	24	22	19	18	137.2	5,406	64.7
Jyothy Labs	520	BUY	39	33	31	27	6.5	166	2.0
Marico	750	BUY	50	43	36	32	20.4	838	10.0
Mrs. Bector's Foods	1,620	BUY	50	38	28	23	2.9	83	1.0
Nestle	2,600	HOLD	71	63	48	43	34.0	2,451	29.3
Tata Consumer	1,360	BUY	69	58	39	34	31.3	1,082	12.9
Zyduz Wellness	2,100	ADD	30	30	29	25	1.0	122	1.5
Discretionary									
Avenue Supermarts	5,000	ADD	88	70	60	48	29.1	3,059	36.6
Bata	1,400	HOLD	45	35	31	25	9.0	190	2.3
Cello	1,060	BUY	49	39	31	27	3.3	186	2.2
FSN E-Commerce Ventures	175	HOLD	202	123	82	53	11.4	492	5.9
Go Fashion (India)	1,200	BUY	51	38	36	27	1.0	56	0.7
Jubilant FoodWorks	620	BUY	84	60	40	31	22.4	349	4.2
Kalyan Jewellers	460	ADD	50	37	27	23	9.3	421	5.0
Metro Brands	1,210	ADD	66	51	34	27	3.9	308	3.7
Page Industries	38,000	HOLD	67	53	45	36	14.1	435	5.2
Restaurant Brands Asia	115	HOLD	NM	NM	193	43	2.8	56	0.7
Sapphire Foods	1,650	ADD	85	55	16	13	3.5	96	1.1
Titan	3,400	HOLD	72	57	48	40	55.5	3,028	36.2
United Spirits	1,400	ADD	66	55	48	41	15.6	958	11.5
Vedant Fashion	1,200	ADD	55	45	36	29	3.9	271	3.2
Westlife Development	880	ADD	106	81	47	36	1.6	129	1.5
Paints									
Akzo Nobel	2,600	HOLD	29	27	19	17	0.5	124	1.5
Asian Paints	2,600	REDUCE	55	55	37	36	46.7	2,784	33.3
Berger Paints	450	REDUCE	48	44	31	29	12.4	575	6.9
Indigo Paints	1,380	HOLD	41	35	25	22	1.0	65	0.8
Kansai Nerolac	300	ADD	36	33	22	21	1.5	228	2.7

Company	EV/ sales (x)		P/B (x)		P/CEPS (x)		RoE (%)		RoCE (%)	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Staples										
Adani Wilmar	0.8	0.7	5	4	33	28	10	11	10	10
Bajaj Consumer	3.0	2.7	4	3	19	17	19	20	17	18
Britannia	7.3	6.6	29	25	48	43	53	51	39	38
Colgate	13.1	12.1	43	42	49	45	78	84	99	106
Dabur	7.8	7.1	10	9	43	38	20	21	13	14
Emami	8.0	7.3	11	9	34	30	35	33	43	41
GCPL	9.5	8.6	10	9	53	45	19	20	15	16
HUL	9.2	8.3	12	11	48	43	22	25	16	18
Honasa Consumer	5.5	4.5	11	9	68	47	13	17	11	15
ITC	7.2	6.6	7	7	22	20	30	32	32	34
Jyothy Labs	5.4	4.9	8	7	35	29	22	22	23	23
Marico	7.6	6.8	21	20	45	39	43	48	30	33
Mrs. Bector's Foods	4.4	3.7	10	8	32	26	22	22	19	19
Nestle	11.4	10.3	63	55	62	55	95	94	46	49
Tata Consumer	5.9	5.3	7	6	54	46	10	11	10	11
Zydus Wellness	4.8	4.3	2	2	28	28	7	7	7	8
Discretionary										
Avenue Supermarts	5.0	4.1	14	12	72	57	17	18	21	23
Bata	4.7	4.1	10	8	23	19	23	25	34	34
Cello	8.1	6.9	12	9	22	27	28	27	28	28
FSN E-Commerce Ventures	5.8	4.5	30	24	97	68	15	19	16	23
Go Fashion (India)	5.9	4.8	8	7	23	18	16	17	24	26
Jubilant FoodWorks	4.5	3.8	11	10	30	24	16	17	14	16
Kalyan Jewellers	1.9	1.5	8	7	36	29	17	19	14	16
Metro Brands	10.4	8.6	14	12	42	34	21	24	28	31
Page Industries	8.2	7.0	25	22	58	47	39	44	31	34
Restaurant Brands Asia	1.7	1.5	12	15	26	18	(30)	(25)	(2)	2
Sapphire Foods	3.0	2.5	7	6	20	16	8	11	15	19
Titan	5.4	4.5	24	18	62	51	38	36	27	28
United Spirits	8.0	7.1	12	10	55	48	19	20	23	24
Vedant Fashion	17.4	14.3	15	12	44	36	28	29	49	50
Westlife Development	4.7	4.0	19	16	41	32	19	21	30	33
Paints										
Akzo Nobel	2.8	2.5	9	8	24	22	31	31	31	32
Asian Paints	7.3	6.8	13	12	46	44	25	23	22	20
Berger Paints	4.8	4.3	8	7	39	35	20	19	18	18
Indigo Paints	4.1	3.5	6	5	28	25	15	16	16	16
Kansai Nerolac	2.7	2.4	4	4	27	25	11	11	11	11

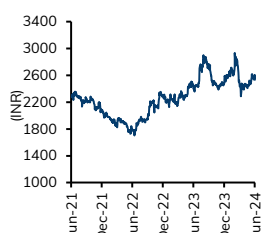
Source: I-Sec research; ADTV, Market Cap – Bloomberg; *Latest TP / Rating as of 11 June'24

Price charts

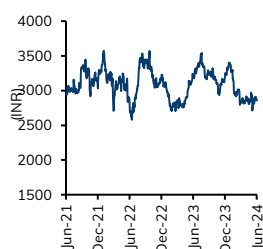
Adani Willmar



Akzo Nobel



Asian Paints



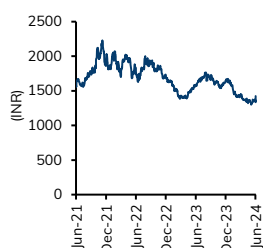
Avenue Supermarts



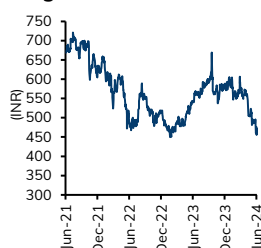
Bajaj Consumer



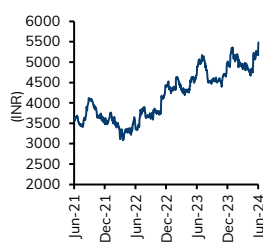
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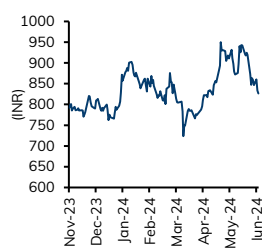
Berger Paints



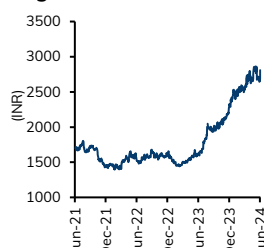
Britannia



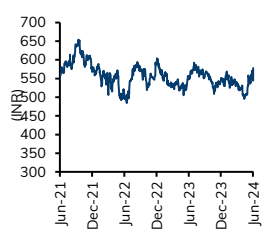
Cello



Colgate



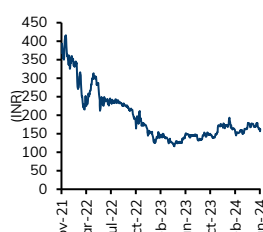
Dabur



Emami



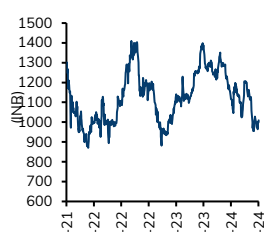
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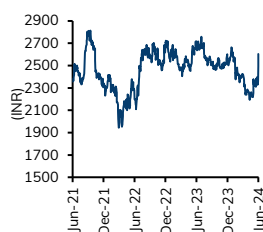
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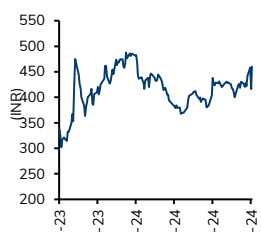
Go Fashion India



HUL



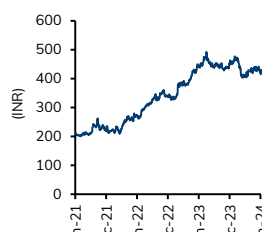
Honasa Consumer



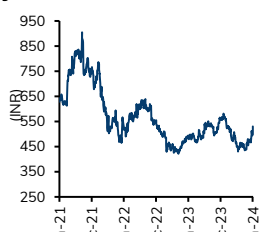
Indigo Paints



ITC



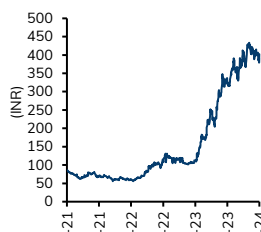
Jubilant FoodWorks



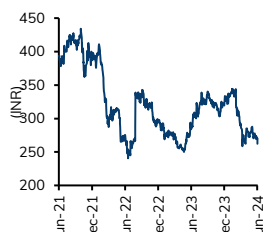
Jyothy Labs



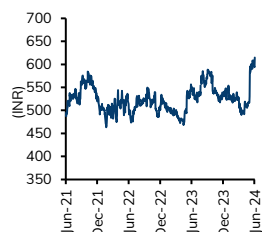
Kalyan Jewellers



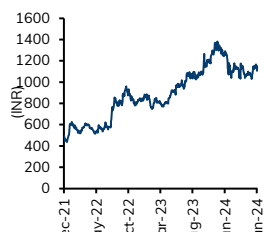
Kansai Nerolac



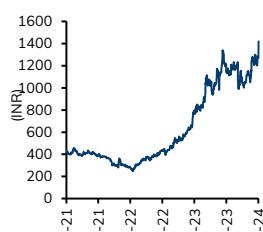
Marico



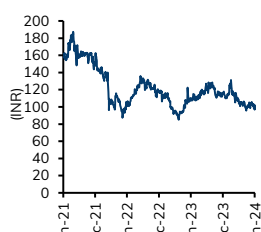
Metro Brands



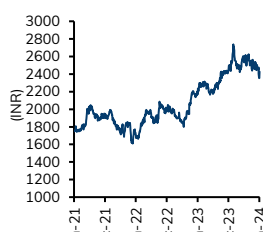
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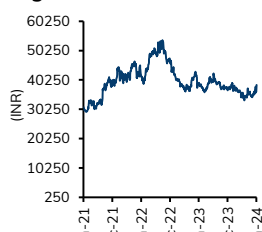
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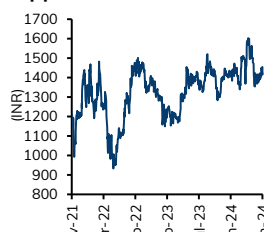
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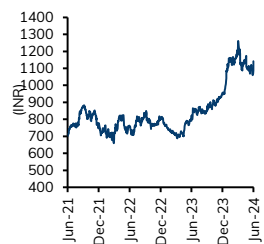
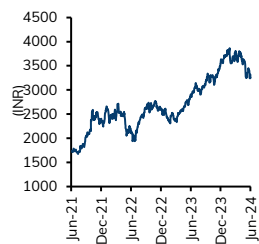
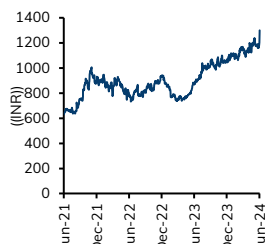
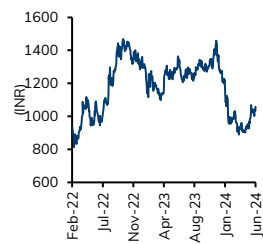
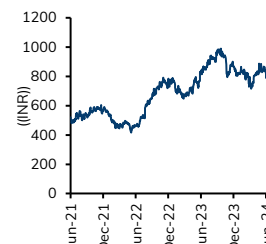
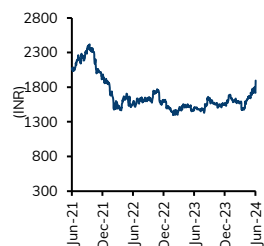


Page Industries



Sapphire India



Tata Consumer**Titan****United Spirits****Vedant Fashion****Westlife Foodworld****Zydus Wellness**

Source: Bloomberg

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