The Resource Centre

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Emami 2.0: to the big league?

Firm in a life-cycle stage similar to Dabur's; stock could re-rate

EMAMI

RATING: OUTPERFORM

EMAMI entering into a bigger league; transition similar to Dabur's ten years ago. We see Emami entering a high-growth phase over the next five-ten years as the company moves beyond its core strengths in niche segments and supplements them with high-growth personal care and health care products. We see Emami at roughly the same life stage as Dabur was ten years back, when the company moved beyond its core strengths in hair oils and health supplements into high-growth but competitive categories and intentional markets.

Emami is undergoing major positive changes: Emami is undergoing a major transition in its product mix, geographical footprint, organisational structure, and systems and processes. We are very positive on these changes as they have helped Emami move into the league of the large Indian FMCG (fast-moving consumer goods) companies such as Dabur, GCPL (Godrej Consumer Products) and Marico over the next three-four years. These changes are very similar to what Dabur had undergone ten years ago; they have helped the company move into an accelerated growth phase in the past ten years. We see Emami in a similar stage of its life cycle as Dabur was ten years back.

What has Dabur achieved in the past ten years: Dabur over the past ten years has delivered very strong and consistent growth in revenues and profits, which have translated into strong performance of the stock as well. Sales have witnessed at a CAGR of 20% and earnings a CAGR of 24% over the past ten years for Dabur. Also, the contribution of categories such as juices, toothpaste, home care and parts of skin care have become as high as 40% of the India business. Its international business has grown to become 31% of overall sales from about 10% ten years ago. As we have highlighted above, Dabur had gone through a similar transition as Emami ten years ago. Dabur's revenue ten years back was at ₹11 bn, which increased to ₹71 bn in FY14. Emami's sales in FY14 were slightly below ₹20 bn, which could witness an 18-20% CAGR (compound annual growth rate) over the next five-ten years.

Aggressive entry into new categories and Zandu HCD should drive the next growth phase. Emami has entered high-growth categories, such as face wash, deodorants, sanitary napkins and light hair oils, where the cumulative category size is about ₹60 bn. One material success or two moderate successes in these could be a major trigger for the stock. Emami is also looking to scale up Zandu HCD (healthcare division) to several times of its current size in four-five years. We feel confident about Emami, given its innovation track record, and the initial response to some of the launches it has done in the past six months.

Organisation ready for the larger scale: influx of senior professional talent and next generation distribution system. Emami has hired a number of senior marketing professionals from larger FMCG companies to help drive the transition. Distribution systems are also being upgraded, e.g., IT-enabling all distributors and handheld terminals for salesmen. Its international business is also seeing localisation of manufacturing and marketing activities.

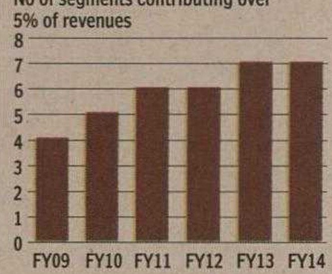
Emami's valuation discount to mid-cap FMCG peers unwarranted; we expect a rerating. The larger Indian FMCG mid-caps trade at a 13% premium to Emami, despite the company having higher ROE (return on equity) and lower share of international business. Our estimates are 8-11% higher than consensus. We raise our target price to ₹700 (from ₹630), and target multiple to 27x, as we expect the stock to re-rate relative to other FMCG mid-caps.

—Credit Suisse

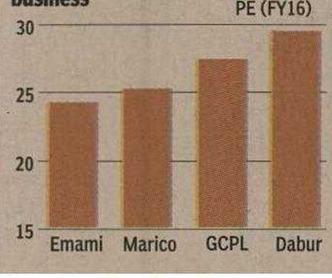
Emami has entered high-growth personal care and health care segments

Source: Company data, Credit Suisse estimates

Emami's track record of innovation is strong, as it successfully scaled up new segments



Indian mid-cap FMCG stocks are trading at a 13% premium to Emami, although Emami has higher ROE & lower share of international business



Stock performance