A Study on fundamental analysis of five selected companies in FMCG sector

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Abstract:

The study endeavours to analysis fundamental position of major listed FMCG companies using ratios. Fundamental analysis, the share price of a company is determined by all the fundamental factors. The purpose of study is HUL, ITC, NESTLE, DABUR, and P & G. were chosen, to analysis was done using past three year computed date of Net Profit Margin Ratio, Gross profit margin, Price to Earnings, Debt to equity ratio, Dividend payout ratio, Earnings per share starting April 2016 to March 2018.This study provides a precise presentation of data and guidelines that will help a fresh investor as well as a venture investor to know vital aspects of investing. This study helps to the investors to choose a safe investment and to identify the growth opportunities in the future.

Key words: Fundamental analysis, Investment, Ratio analysis.

Introduction:

Fundamental analysis is a method of evaluating a security in an attempt to measure its intrinsic value, by examining related economic, financial and other qualitative and quantitative factors.For stocks and equity instruments, this method uses revenues, earnings, future growth, return on equity, profit margins and other data to determine a company's underlying value and potential for future growth. In terms of stocks, fundamental analysis focuses on the financial statements of the company being evaluated. The Fundamental analyst works on the True worth or intrinsic value; then compares this intrinsic value with the current market price. If the current market price is higher than the intrinsic value, the share is said to be overpriced & vice versa.

This study provides a precise presentation of data and guidelines that will help a fresh investor as well as a venture investor to know vital aspects of investing. This study helps to the investors to choose a safe investment and to identify the growth opportunities in the future. FMCG industry is one of the major and important industries in the world. Large numbers of foreign investors are coming and investing in Indian FMCG sector due to its large potential growth in future. The scope of the study is limited to analyzing the financial statements and periodical reports published by the company and the information from the journals and websites.

Literature Review:

Boardman and Vinning(1989), Commander, Fan and Schaffer(1996) and La Porta and Lopez-de Silanes(1997). In the Historical approach, exante and ex post privatization performance of the same enterprise is compared.

Malik and Sur (1998) examined the working capital management of HUL, a well known FMCG company, during the period 1987-1996 using relevant statistical techniques and tests. The results reveal a very high degree of positive relationship between liquidity and profitability.

Nash and Randenborgh(1998) , Earle and Estrin(1999) and Dewenter and Malatesta(1999) beginning with Beaver's(1998) contended that standard financial ratios can predict the financial performance of firms, many subsequent studies have attempted to demonstrate the predictive value of various techniques for estimating actual business performance.

Lermack, (2003) the benifits of financial ratios analysis. Financial ratios are an important and well established technique of financial analysis.

Lasher, (2005) dept ratios show how effectively the organization uses other people's money and whether it is using a lot of borrowed money.

Sur et al.(2007) studied the case of Colgate- Palmolive(india) ltd. A leading FMCG company in the Indian health care industry for the period 1980-2004 using simple statically tools like arithmetic mean, techniques like ratio analysis, analysis of Kendall's coefficient of concordance, multiple regression analysis and multiple and statically tests like t- test, F-test and chi-square test at appropriate places to analyze the efficiency of the company's asset management.

Ross et.(2007) expressed most researchers divide the financial ratios into four group. Profitability, solvency, liquidity and activity ratios.

Brigham and Ehrhardt(2010) stated the financial ratios are designed to help evaluate financial statements. Financial ratios are used as a planning and control tool. Financial ratio analysis is used to evaluate the performance of an organization.

Bagchi and Khamrui(2012) evaluated the financial performance of the two leading FMCG companies, Britannia industries and Dabur India, over a period of 10 years(2000-2010) using various accounting ratios and statically tools.

R. Amsaveni and S. Gomathi(2013) found that through economic analysis the GNP, Interst rate, Exchange rate, FER, Agriculture production, Govt. Receipts and Expenses has a growth rate during the study period. The company analysis done with the help of ratio analysis indicates that Colgate and HUL Companies are financially in satisfactory position during the study period.

Ms. J. Hema and V. Ariram(2016) found that Indian FMCG industry has a high growth rate and its sales and net profit also shows increasing trend and the company analysis revealed that its financial performance through the financial ratio, which indicates that HUL is financially in satisfactory position during the study period.

Research Methodology:

Introduction of Topic:

According to Fundamental analysis, the share price of a company is determined by all the fundamental factors. The Fundamental analyst works on the True worth or intrinsic value; then compares this intrinsic value with the current market price. If the current market price is higher than the intrinsic value, the share is said to be overpriced & vice versa.

Objective of the Study:

Primary Objectives: To conduct Fundamental analysis for stock market listed FMCG companies and SWOT analysis for the FMCG industry.

Secondary Objectives:

1. To analyze the ratio, thereby to know the companies respective positions in the market.
2. To check whether fundamental analysis alone can evaluate investment opportunities in the share.
3. To forecast the future performance of the selected companies.
4. To recognize the suitability of the shares for investment in long term.
5. To select the best performing company among the selected five companies

Research Design: Descriptive research design which is based on secondary data.

Sample Size: Sample size used is five companies for analysis.

Collection of Data: Secondary data.

Research Tool: Analysis is done through Ratio analysis.

DATA ANALYSIS:

Intrinsic Value:

Intrinsic value = EPS * Price to earning value

Sr no.	Companies	EPS	Price to Earning	Intrinsic value	Market value
1	HUL	20.75	58.18	1207.235	1323
2	ITC	8.43	31.32	264.0276	267.45
3	Nestle	96.1	66.83	6422.363	7573
4	Dabur	5.67	46.51	263.7117	329.8
5	P & G	133.31	68.86	9179.7266	9448

Table 5.1.1 Intrinsic value

Finding: The market price of HUL is considered too high for its fundamentals. T he stock is trading above its intrinsic value. The market price of ITC is almost nearby to the intrinsic value of the stock. Which signifies that the stock price is correctly valued.The market price of NESTLE is considered too high for its fundamentals. The stock is trading above its intrinsic value.The market price of DABUR is considered too high for its fundamentals.The stock is trading above its intrinsic value. The stock of P & G is trading almost nearby to the current market value of the stock. The stock price is correctly valued.

Key financial ratio's:

1. Gross Profit Ratio = Gross Profit ÷ Net Sales

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	17.72	16.91	15.97
2	ITC	33.77	35.84	34.27
3	Nestle	14.72	14.77	17.19
4	Dabur	19.58	17.84	16.06
5	P & G	26.06	22.25	18.5

Table no.2.1 Gross Profit Ratio

Finding: Gross profit ratio shows the profitability of the company which signify higher the ratio is considered better. Gross profit ratio of P&G, Dabur, HUL is continuously increasing from the past three years and that of Nestle is facing downfall continuously and that of ITC's ratio increased from 2015 to 2016 and showed a bit of downfall from 2016 to 2017.

2. Return on Sales = Net Income ÷ Net Sales

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	69.18	110.73	115.87
2	ITC	22.49	29.94	31.31
3	Nestle	30.74	19.98	41.75
4	Dabur	27.29	32.71	33.66
5	P & G	82.24	28	28.17

Table 2.2 Return on sales

Finding: It measures how efficiently a company is at generating profits from its revenue.Return on sales is continuously decreasing of HUL, ITC and Dabur and that of Nestle has taken a change in the ratio from the year 2016 to 2017 and that of P&G is at a very good edge.

3. Return on Assets = Net Income ÷ Average Total Assets

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	29.99	17.04	17.22
2	ITC	37.33	40.92	38.35
3	Nestle	312.57	292.26	294.27
4	Dabur	20.77	16.32	13.3
5	P & G	26.06	22.25	18.5

Table 2.3 Return on Assets

Finding: Return on Assets shows how efficiently a company can use its assets to generate sales. Return on assets ratio higher is considered to better. The ratio that of HUL, P&G is very good than that of Dabur and Nestle the ratio is too increasing but they can take opportunity and increase the ratio by using assets. ITC has taken a downward slope from 2016 to 2017 .

4. Current Ratio = Current Assets ÷ Current Liabilities

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	0.82	0.75	0.75
2	ITC	1.94	1.2	1.45
3	Nestle	0.57	0.5	0.53
4	Dabur	0.83	0.83	0.89
5	P & G	1.31	2.77	2.23

Table 2.4Current Ratio

Finding:The current ratio is mainly used to give an idea of a company's ability to pay back its liabilities (debt and accounts payable) with its assets (cash, marketable securities, inventory, accounts receivable). The company P&G has performed very well in decreasing and bring the ratio to the ideal ratio followed by ITC; and that of Nestle, Dabur and HUL are focusing on maintaining the ratio between 0.5 to 0.8.

5. Acid Test Ratio = Quick Assets ÷ Current Liabilities

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	0.51	0.49	0.47
2	ITC	1.06	0.69	0.87
3	Nestle	0.32	0.25	0.25
4	Dabur	0.42	0.47	0.54
5	P & G	0.99	2.57	2.05

Table 2.5 Acid test ratio

Finding:The acid-test or quick ratio or liquidity ratio measures the ability of a company to use its near cash or quick assets to extinguish or retire its current liabilities immediately. While a quick ratio lower than 1 does not necessarily mean the company is going into default or bankruptcy, it could mean that the company is relying heavily on inventory or other assets to pay its short term liabilities. The higher the quick ratio, the better the company's liquidity position. Nestle and Dabur is too low and that of ITC, Dabur and HULis maintaining a good amount of quick ratio.

6. Net Working Capital = Current Assets - Current Liabilities

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	2209	247.82	480.73
2	ITC	17,707.32	9,546.88	1,273.12
3	Nestle	1646.29	1003.88	608.22
4	Dabur	577.44	478.72	313.29
5	P & G	973.3	983.73	641.44

Table 2.6 Net Working Capital

Finding:If a company has very high net working capital, it has more than enough current assets to meet all of its short-term financial obligations. ITC has the highest net working capital followed by Nestle and P&G; and that of HUL and Dabur is low.

7. Inventory Turnover = Cost of Sales ÷ Average Inventory

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	14.6	13.61	12.57
2	ITC	7.05	6.1	6.43
3	Nestle	10.13	10.33	12.06
4	Dabur	8.96	9.48	10
5	P & G	13.64	20.05	19.82

Table 2.8 Inventory Turnover

Finding: Inventory turnover measures how fast a company is selling inventory and is generally compared against industry averages. A low turnover implies weak sales and, therefore, excess inventory. A high ratio implies either strong sales and/or large discounts.The ratio of ITC, HUL and P&G is fair enough and that of Nestle is too high; Daburis low.

8. Total Asset Turnover = Net Sales ÷ Average Total Assets

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	5.39	9.73	8.32
2	ITC	0.97	1.23	1.2
3	Nestle	3.03	2.88	3.45
4	Dabur	1.36	1.97	2.22
5	P & G	4.41	1.68	1.9

Table 2.9 Total Asset Turnover

Finding: Higher total asset turnover ratios mean the company is using its assets more efficiently. Lower ratios mean that the company isn't using its assets efficiently and most likely have managementor production problems. For instance, a ratio of 1 means that the net sales of a company equals the average total assets for the year.. Ratio of ITC and Dabur is too low and that of HUL and P&G is good utilising the assets and that of Dabur is fair.

9. Equity Ratio = Total Equity ÷ Total Assets

Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	0.43	0.26	0.27
2	ITC	0.83	0.66	0.7
3	Nestle	0.44	0.46	0.49
4	Dabur	0.7	0.6	0.6
5	P & G	0.5	0.7	0.6

Table 2.10 Equity Ratio

Finding: The equity ratio throws light on a company's overall financial strength. A higher equity ratio or a higher contribution of shareholders to the capital indicates a company's better long-term solvency position.

A low equity ratio, on the contrary, includes higher risk to the creditors. The ratio of ITC, Dabur and P&G is fair and that of Nestle and HUL is comparatively low.

10 Debt-Equity Ratio = Total Liabilities ÷ Total Equity				
Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	0.16	0.36	0.3
2	ITC	1.2	1.5	1.44
3	Nestle	0.01	0.01	0.01
4	Dabur	0.08	0.03	0.06
5	P & G	1.2	0.43	0.58

Table 2.11 Debt-Equity Ratio

Finding: The high debt-to-equity ratio indicates that a company may not be able to generate enough cash to satisfy its debt obligations. However, low debt-to-equity ratios may also indicate that a company is not taking advantage of the increased profits that financial leverage may bring. ITC and P&G are maintaining are good amount of debt to equity ratio and that of Nestle, Dabur and HUL is too low.

11. Dividend Pay-out Ratio = Dividend per Share ÷ Earnings per Share				
Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	79.53	84.8	75.2
2	ITC	67.05	69.48	52.14
3	Nestle	65.55	83.01	51.27
4	Dabur	39.7	42.12	46.06
5	P & G	29.85	27.61	28.36

Table 5.4.13 Dividend Pay-out Ratio

Finding: The dividend payout ratio is the ratio of the total amount of dividends paid out to shareholders relative to the net income of the company. Payout ratios that are between 55% to 75% are considered high because the company is expected to distribute more than half of its earnings as dividends, which implies less retained earnings. A higher payout ratio viewed in isolation from the dividend investor's perspective is very good.HUL, Nestle, ITC have a very good payout ratio compare to Dabur and P&G.

12. Operating profit margin = EBIT ÷ Total revenue				
Sr no.	Companies	Mar-17	Mar-16	Mar-15
1	HUL	18.96	17.91	16.9
2	ITC	36.36	38.65	36.9
3	Nestle	18.55	19.01	20.61
4	Dabur	21	19.1	17.27
5	P & G	28.64	24.33	20.75

Table 5.4.14 Operating profit margin

Finding: A healthy operating margin is also required for a company to be able to pay for its fixed costs, such as interest on debt, so a high margin means that a company has less financial risk than a company with a low margin. It is same as EBITDA Margin . ITC and Nestle are facing downfall from 2016 to 2017 and HUL, Dabur and P&G are growing over the past three years.

RANKING:

Sr no.	Particulars	HUL	ITC	Nestle	Dabur	P&G
1	Gross Profit Ratio	3	4	5	2	1
2	Return on sales	5	4	2	3	1
3	Return on assets	1	5	4	3	2
4	Current Ratio	3	2	3	3	1
5	Acid test ratio	3	1	5	4	2
6	Net Working Capital	4	1	2	5	3
7	Inventory Turnover	2	5	3	4	1
8	Total Asset Turnover	1	5	3	4	2
9	Equity Ratio	5	1	4	2	3
10	Debt-Equity Ratio	3	1	5	4	2
11	Dividend Pay-out Ratio	1	2	3	4	5
12	Operating profit margin	4	1	5	3	2

Conclusion:

Fundamental analysis can be valuable, but it should be approached with caution. If you are reading research written by a sell- side analyst, it is important to be familiar with the analyst behind the report. We all have personal biases, and every analyst has some sort of bias.

As per analysis, we can say that FMCG sector has tremendous growth rate with relevant other growing sectors. The company analysis done with the help of ratio analysis, common size statement, comparative statement and intrinsic value method indicates that P&G, HUL and ITC are financially in satisfactory position during the study period. When analyzing profitability ratios of these companies P&G is earning more profits. However, HUL offering more return on investment to their shareholders.

‘Food Product’ is the leading segment, accounting for 43% of the overall market, personal care 22% and fabric care 12% are other large segments. Fundamental analysis aims at finding the true worth of a security by analyzing macroeconomic, industry scenario and company financial position and so on. An investor can make safest as well as lucrative investment by analyzing the related variables and ensure for optimum return. Fundamental analysis suggests that no investor should buy or sell a share on the basis of the advices of market intermediaries or tips given by the stock dealers, websites, etc., the fundamental analysis calls upon the investor to make his buy or sell decisions based on the detailed analysis of the information available.

This study focuses on fundamental analysis using various tools which help in trading strategies for risk reduction and maximization of return

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