



# 14th Annual Wealth Creation Study 2004-2009

**By Raamdeo Agrawal**

December 17, 2009

# Discussion Points

- **14<sup>th</sup> Wealth Creation Study Findings**
- **Theme 2010:  
Winner Categories + Category Winners**
- **Conclusions**



# | 14<sup>th</sup> Annual Wealth Creation Study

## Concept of Wealth Creation:

The process by which a company enhances market value of the capital entrusted to it by its shareholders

## Net Wealth Created:

Change in Market Cap over the study period adjusted for corporate actions



# Wealth Creation Study - Methodology

## Wealth Creators:

Though Rs 100 crores of net wealth created is the qualifying criteria, the top 100<sup>th</sup> wealth creating company managed Rs 1,000 crores



# 10 Biggest Wealth Creators



Rank, Company	NWC (Rs cr)	Price CAGR
1. Reliance Inds.	151,386	28%
2. Bharti Airtel	89,091	32%
3. B H E L	58,845	38%
4. NMDC	57,826	71%
5. O N G C	47,081	7%

Rank, Company	NWC (Rs cr)	Price CAGR
6. ITC	43,556	22%
7. Infosys	40,461	16%
8. L&T	29,110	36%
9. SAIL	26,497	24%
10. HDFC	19,313	17%

**Last 6 years, Wealth Creation dominated by Oil & Gas:  
ONGC for first 3 years, Reliance in the next 3 years**



# 10 Fastest Wealth Creators

Rank, Company	Price Appn. (x)	Price CAGR %
1. Unitech	54	122
2. Areva T&D	29	97
3. BF Utilities	21	84
4. Opto Circuits	21	84
5. NMDC	14	71

Rank, Company	Price Appn. (x)	Price CAGR %
6. Shriram City	14	70
7. United Spirits	12	64
8. Jindal Steel	12	64
9. Sterling Intl	11	62
10. Chettinad	10	58

**Unitech – Fastest Wealth Creator for the 2<sup>nd</sup> time in a row**



# Most Consistent Wealth Creators



Rank, Company	Appeared in WC Study (x)	10-Year Price CAGR %
1. H D F C	10	25
2. Sun Pharma	10	24
3. Reliance	10	22
4. Hero Honda	10	21
5. Infosys	10	2

Rank, Company	Appeared in WC Study (x)	10-Year Price CAGR %
6. Asian Paints	9	18
7. Nestle India	9	17
8. HDFC Bank	9	16
9. ITC	9	16
10. Ambuja Cem	9	11

**Non-cyclicity of business is key for consistent wealth creation**



# Wealthex v/s Sensex (2004-2009)



	Mar-04	Mar-05	Mar-06	Mar-07	Mar-08	Mar-09	5 Year CAGR %
BSE SENSEX	5,591	6,493	11,280	13,072	15,644	9,709	<b>12</b>
YoY (%)		16	74	16	20	-38	
Wealthex	5,591	7,050	12,600	14,759	20,877	14,206	<b>21</b>
YoY (%)		26	79	17	41	-32	
Sensex EPS (Rs)	348	450	523	718	833	820	<b>19</b>
YoY (%)		29	16	37	16	-2	
Sensex PE (x)	16	14	22	18	19	12	
Wealthex EPS	381	533	616	840	1085	1126	<b>24</b>
YoY (%)		40	16	36	29	4	
Wealthex PE (x)	15	13	21	18	19	13	

**Wealth Creators – higher EPS growth, lower P/E, higher appreciation**



# Wealth Creation by Industry



Industry (No of Cos.)	WC (Rs cr)	2009 (%)	2004 (%)
Oil & Gas (4)	212,589	22	43
Metals (10)	145,755	15	7
Engg. (13)	116,709	12	5
FMCG (16)	104,424	11	1
Telecom (4)	101,211	11	0
Banking (12)	88,857	9	15
IT (5)	49,240	5	7
Pharma (9)	42,749	4	6

Industry (No of Cos.)	WC (Rs cr)	2009 (%)	2004 (%)
Auto (8)	35,680	4	6
Others (7)	19,812	2	4
Cement (6)	18,566	2	2
Utility (3)	14,320	1	4
Constn / RE (1)	5,584	1	0
Media (1)	5,277	1	0
Retail (1)	2,930	0	0
<b>Total</b>	<b>963,702</b>	<b>100</b>	<b>100</b>

**Telecom and FMCG have gained share at the cost of Oil & Gas and Banking**

**Categories like Retail which are small now can grow big**



# Wealth Creation by base year P/E

2004 P/E (x)	No. of Cos.	Price CAGR %
<5	9	30
5-10	22	25
10-15	21	18
15-20	19	18
20-25	13	28
>25	16	20
<b>Total</b>	<b>100</b>	<b>21</b>

**High margin of safety in single digit P/Es**



# Wealth Creation & Payback ratio



Payback in 2004	No. of Cos.	Price CAGR %
<b>&lt; 0.25</b>	<b>9</b>	<b>74</b>
<b>0.25-0.5</b>	<b>13</b>	<b>39</b>
<b>0.5-1</b>	<b>19</b>	<b>25</b>
1-1.5	18	19
1.5-2	25	21
>2	16	11
<b>Total</b>	<b>100</b>	<b>21</b>

**Payback of less than 1x creates fastest wealth**



# Wealth Creation & Purchase Price



“There is absolutely no substitute for paying right price.

In the Bible, it says that love covers a multitude of sins.

Well, in the investing field, price covers a multitude of mistakes.

For human beings, there is no substitute for love.

For investing there is no substitute for paying right price – absolutely none.”

— *Van Den Berg, OID, April 2004*



# Wealth Creation & Entry Barriers



Companies	No. of cos.	Wealth Created (Rs crores)	% of total
<b>With Entry Barriers</b>	<b>66</b>	<b>8,31,400</b>	<b>86</b>
Others	34	1,32,302	14
<b>TOTAL</b>	<b>100</b>	<b>9,63,702</b>	<b>100</b>

**Companies with Entry Barriers will continue to enjoy disproportionate share of wealth in future as well**



# Theme 2010



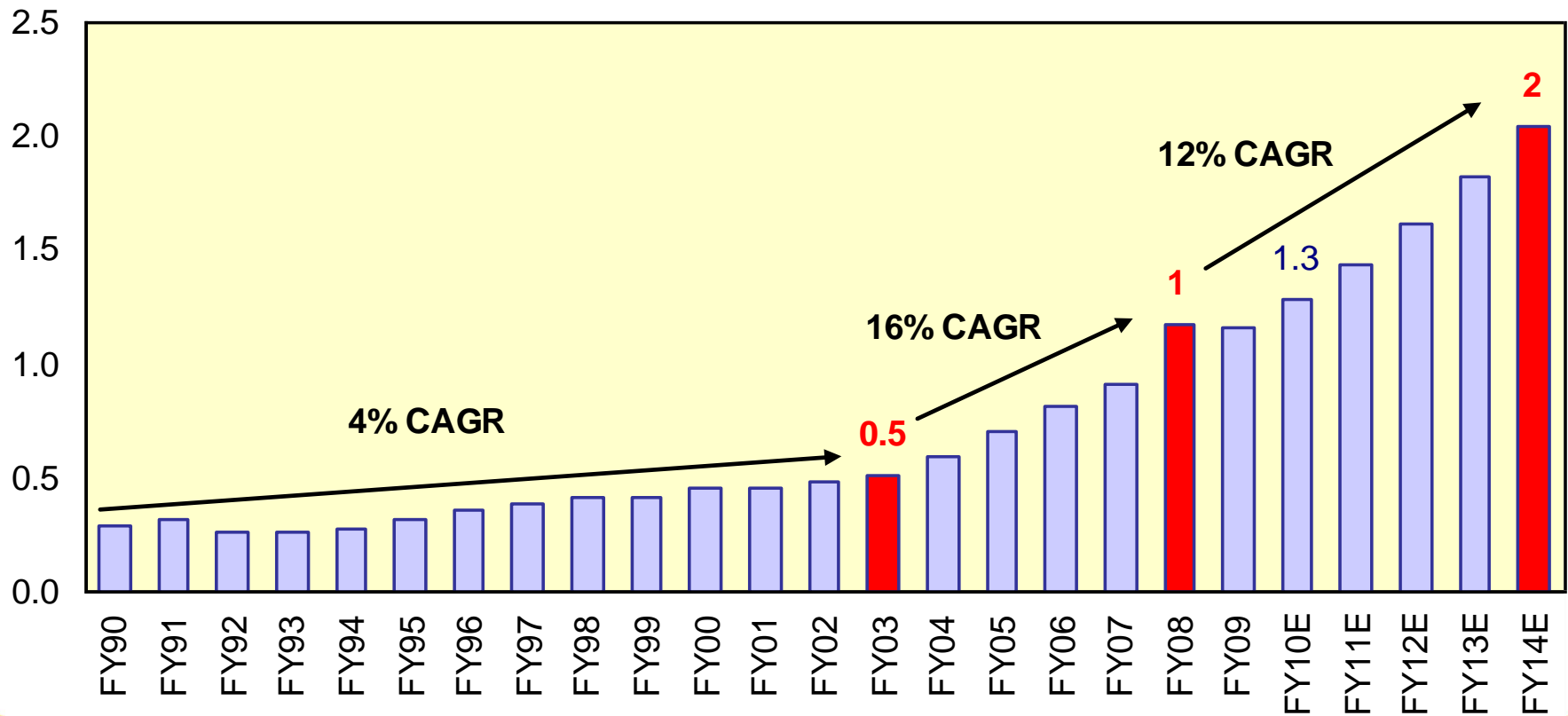
# Theme Outline

- **Winner Categories = India's NTD Era + Scalability**
- **Category Winners = Winning Categories  
+ Entry Barriers  
+ Great Management**
- **Great Investments = Category Winners  
+ Reasonable Valuation**



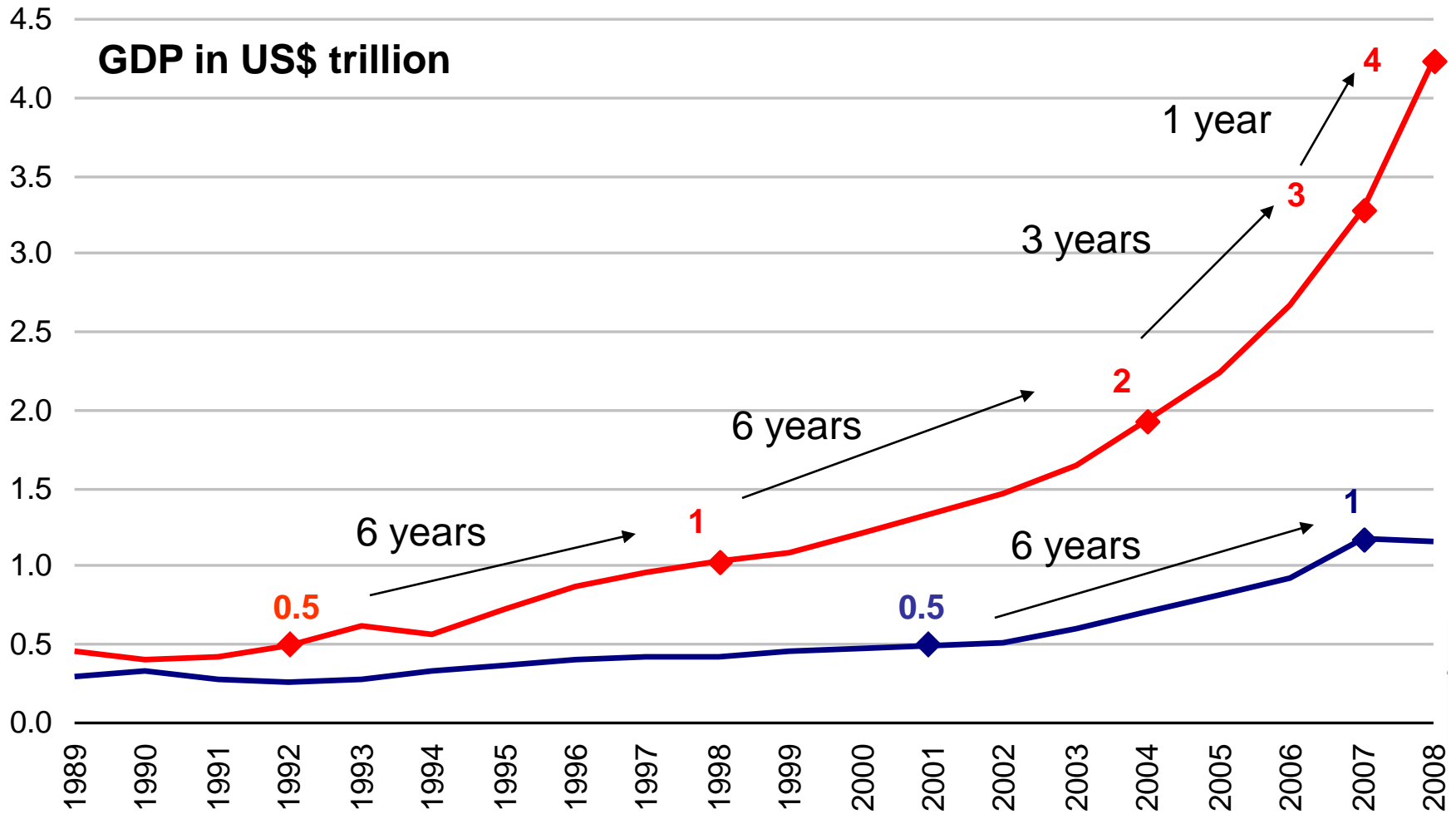
# Recap of India's NTD Era

- 60 years for first US\$ 1 trillion of GDP
- 6 years for the NTD





# The Chinese Experience



## India's NTD Era

- **Consumption Boom**
- **Savings & Investment Boom**



# Consumption boom in NTD Era

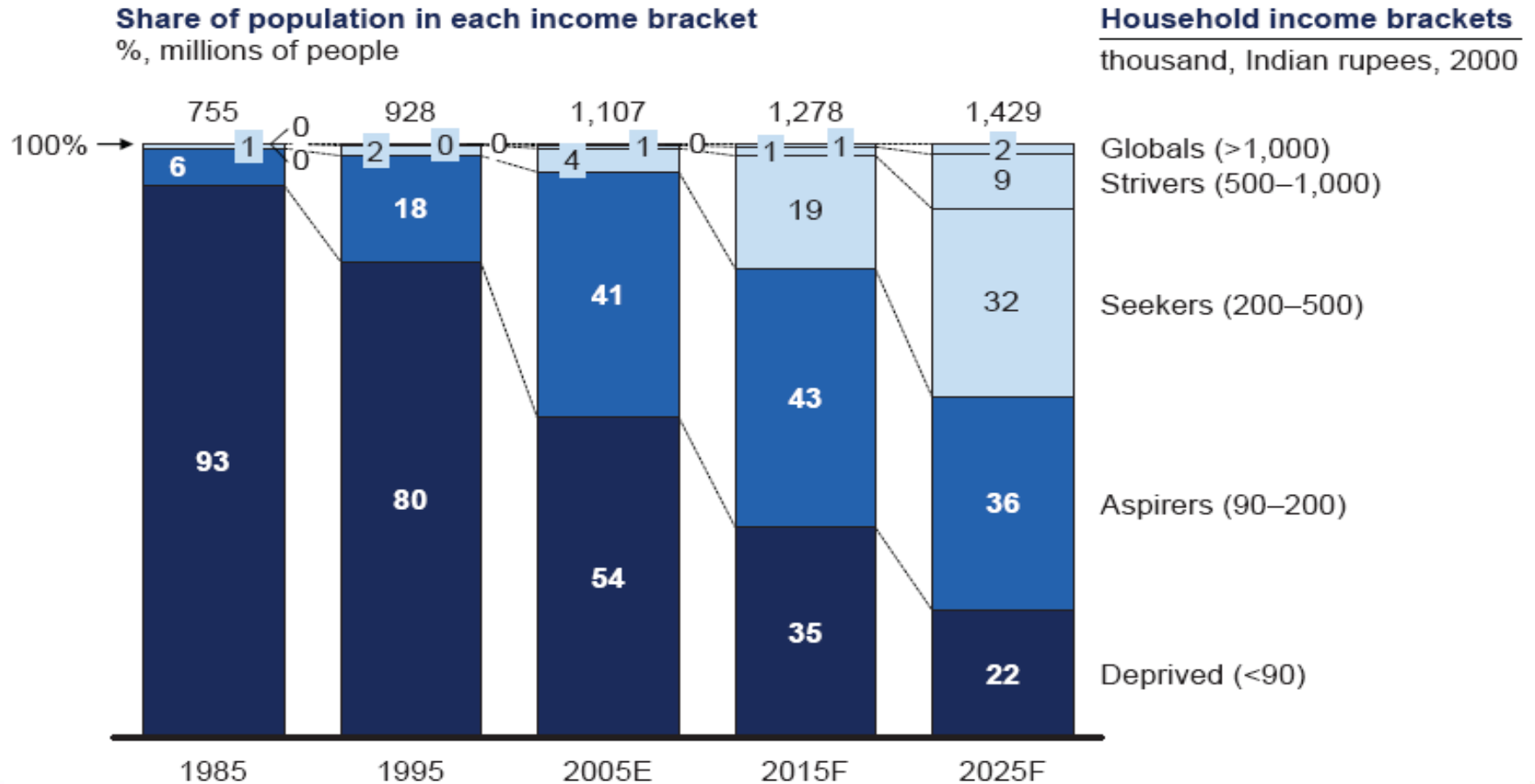


We have drawn heavily on McKinsey Global Institute's Report –  
“The Bird of Gold: The Rise of India's Consumer Market”



# Consumption boom in NTD Era

Poverty will fall from 93% in 1985, 54% in 2005 to 22% by 2025



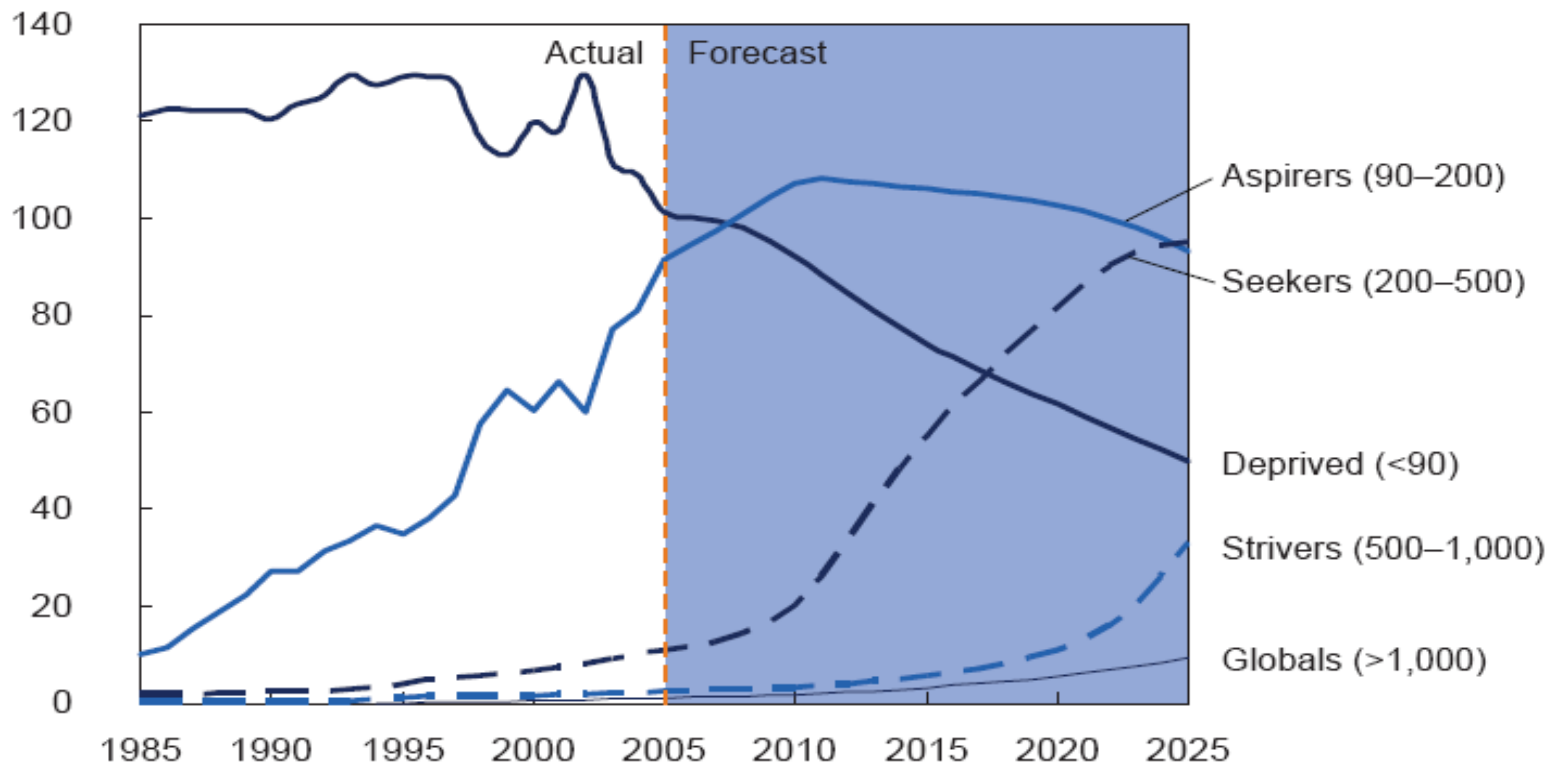
# Consumption boom in NTD Era



Middle class will swell 12x from 50m in 2005 to 583m in 2025

Number of households in each income bracket  
millions of people

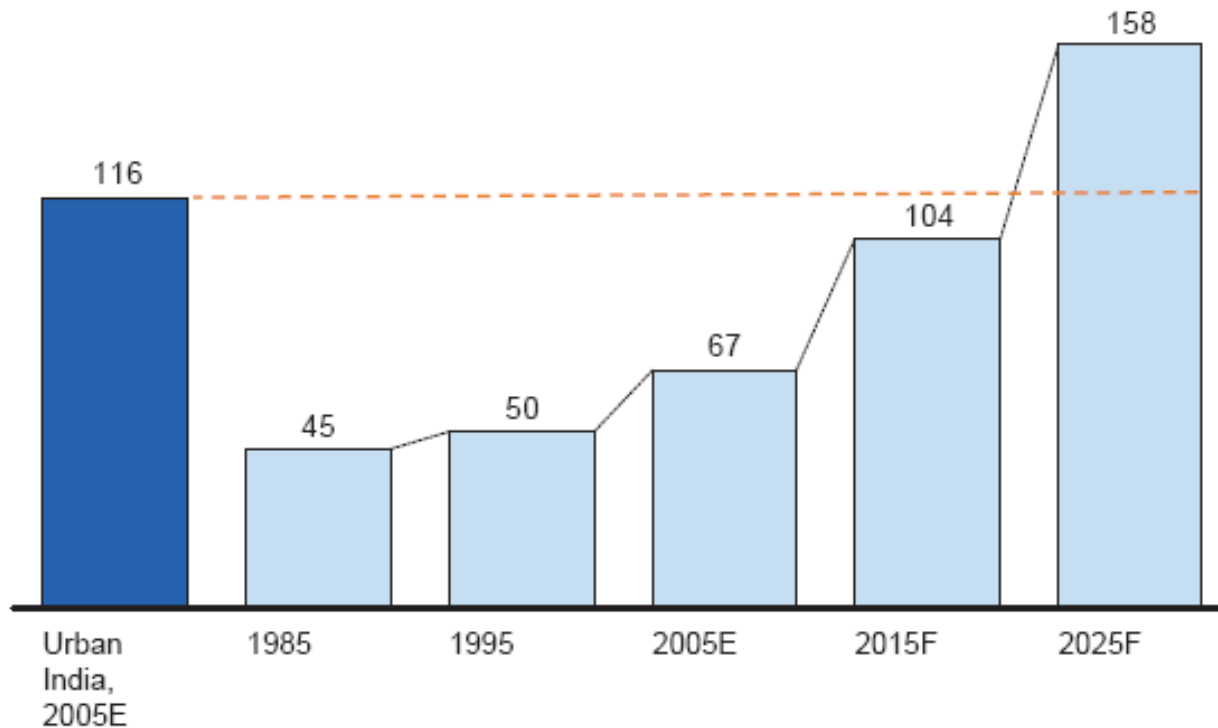
Household income brackets  
thousand, Indian rupees, 2000



## Consumption boom in NTD Era

Per household consumption in rural India will reach present urban levels by 2017

Average rural consumption per household  
thousand, Indian rupees, 2000

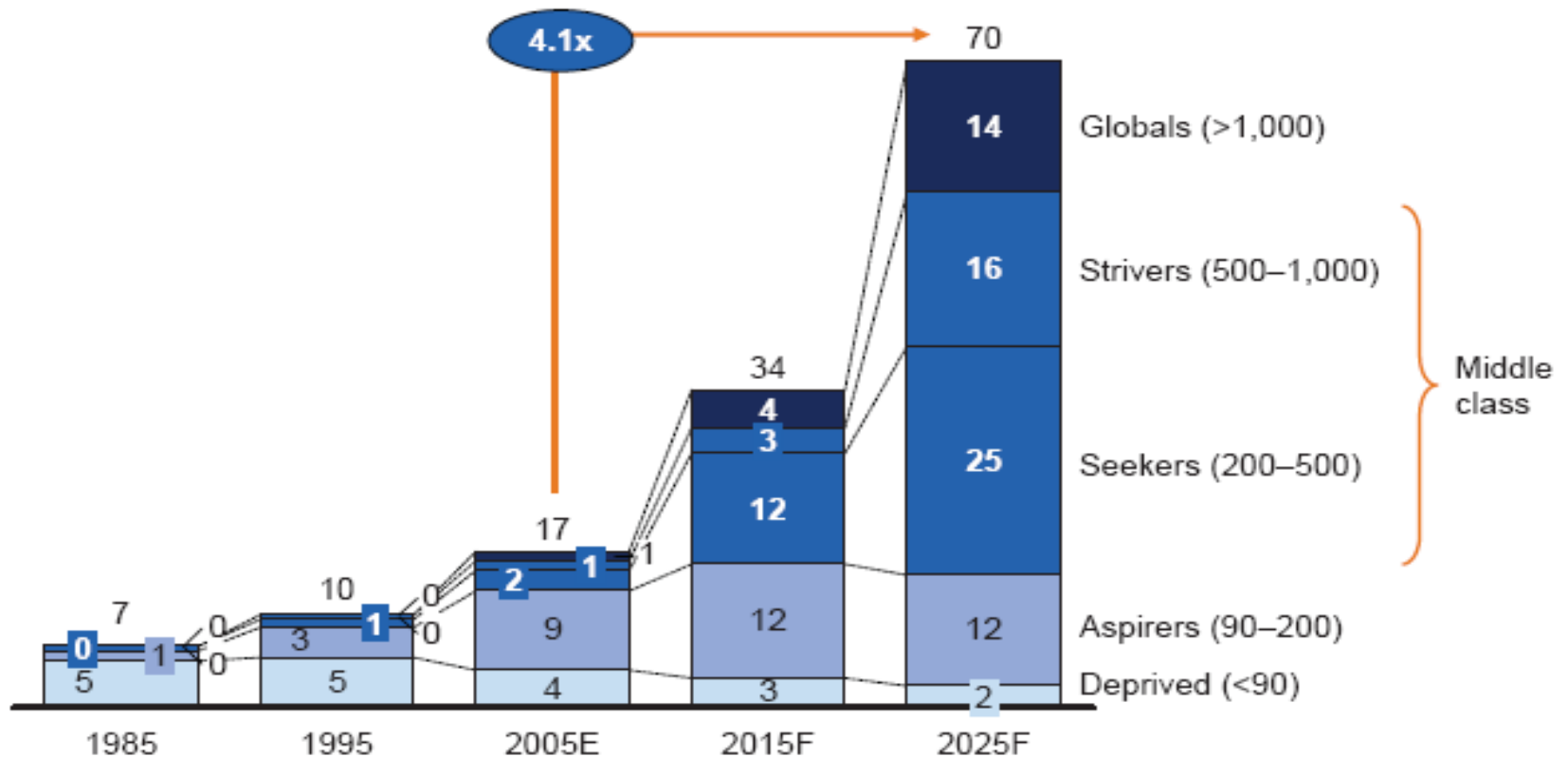


# Consumption boom in NTD Era

## Aggregate consumption will quadruple in 2025 over 2005

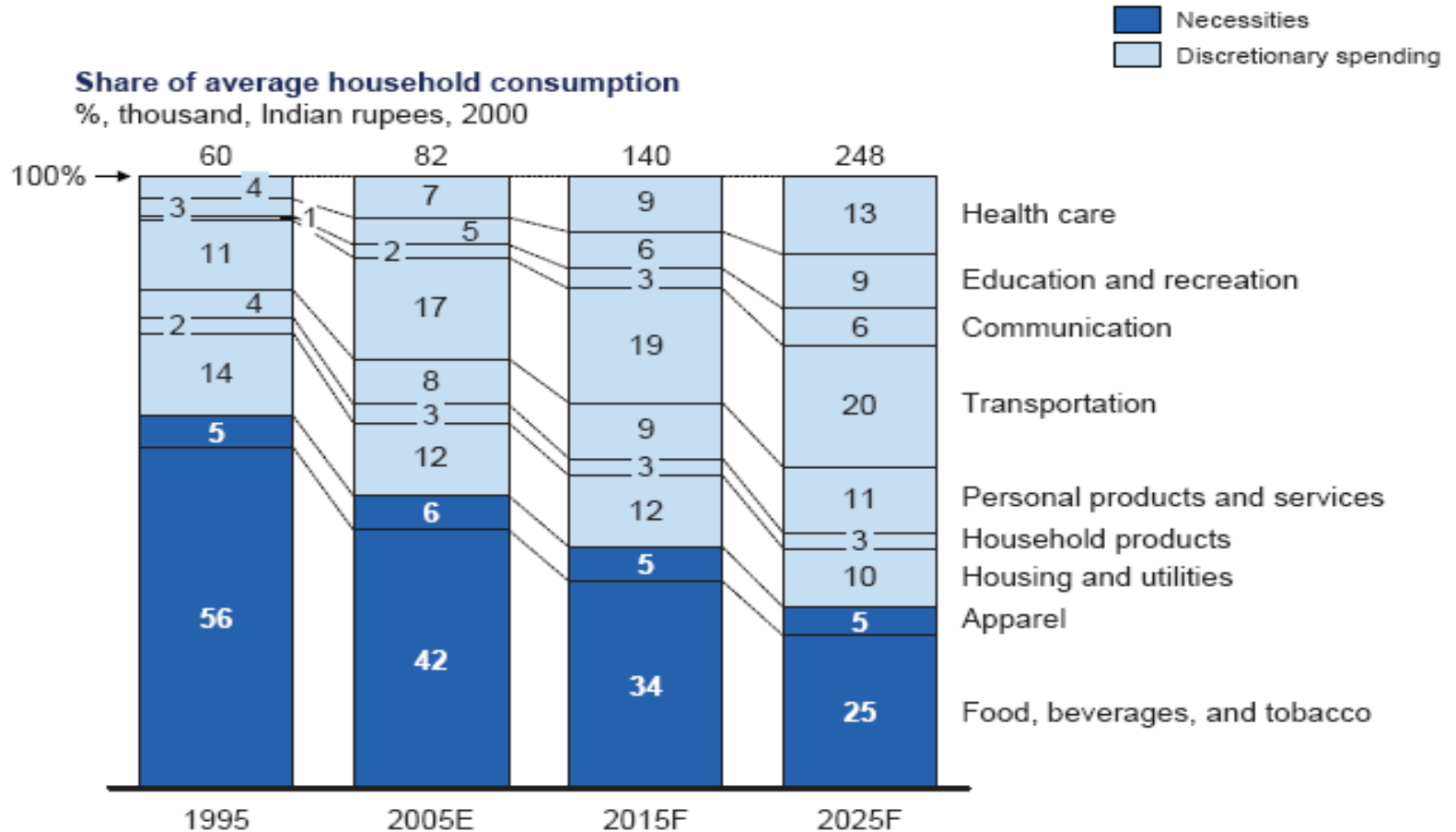
**Aggregate consumption across income brackets**  
trillion, Indian rupees, 2000

**Household income brackets**  
thousand, Indian rupees, 2000



# Consumption boom in NTD Era

Discretionary spend will rise from 52% in 2005 to 70% in 2025





## Consumption boom in NTD Era



### Food will remain the biggest category

(Rs B)

CATEGORY	2005	% SHARE	2015	% SHARE	CAGR (%)
Food, beverages, tobacco	7,147	22	11,547	18	4.9
Transportation	2,788	8	6,395	10	8.7
Housing, Utilities, etc	2,019	6	4,032	6	7.2
Education and recreation	1,198	4	3,195	5	10.3
Healthcare	1,148	3	3,076	5	10.4
Personal Products & Services	1,273	4	3,044	5	9.1
Apparel and footwear	931	3	1,847	3	7.1
Communication	344	1	1,090	2	12.2
Household products	484	1	959	1	7.1
<b>TOTAL</b>	<b>32,892</b>	<b>100</b>	<b>64,456</b>	<b>100</b>	<b>7.0</b>

## Consumption boom in NTD Era



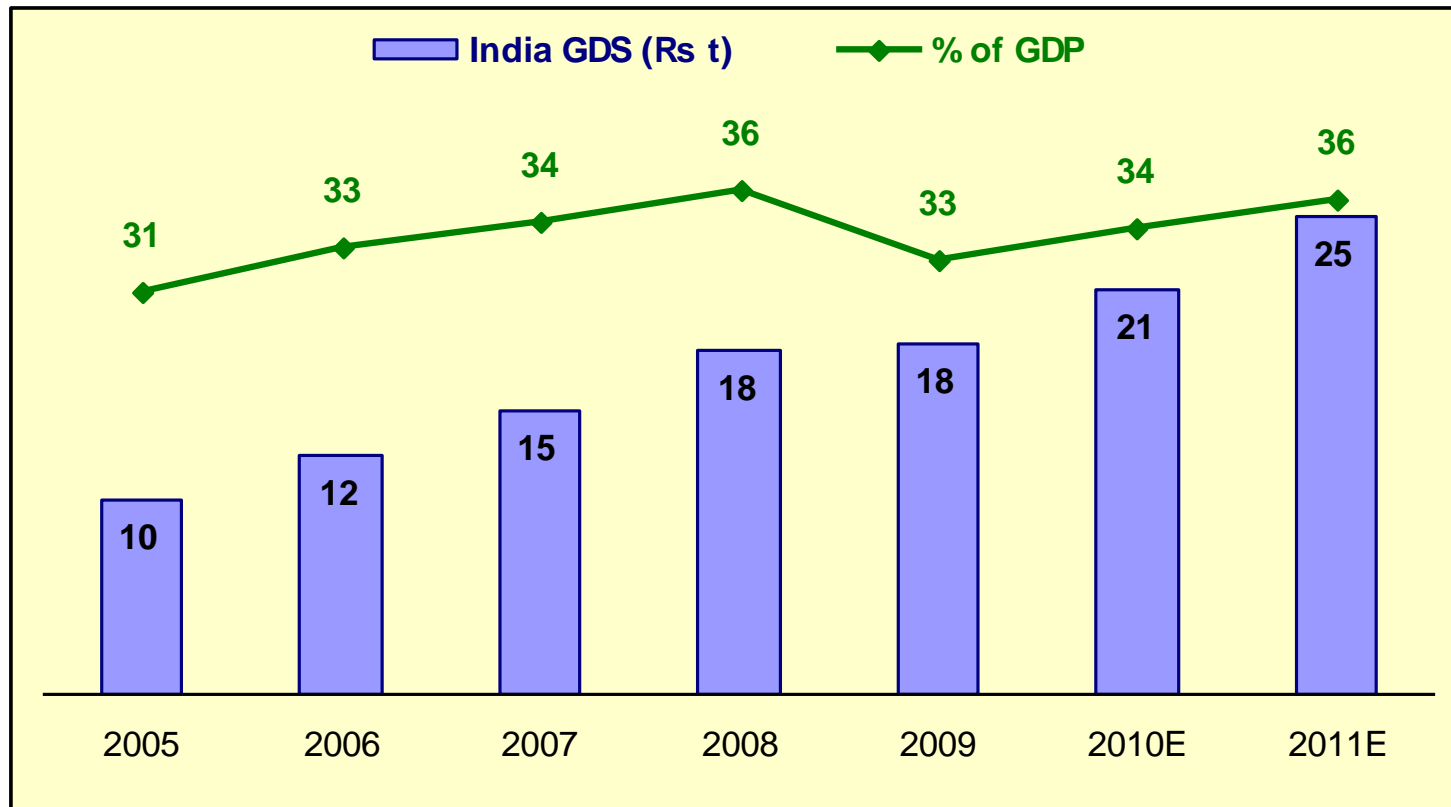
### Communication will grow the fastest

(Rs B)

CATEGORY	2005	% SHARE	2015	% SHARE	CAGR (%)
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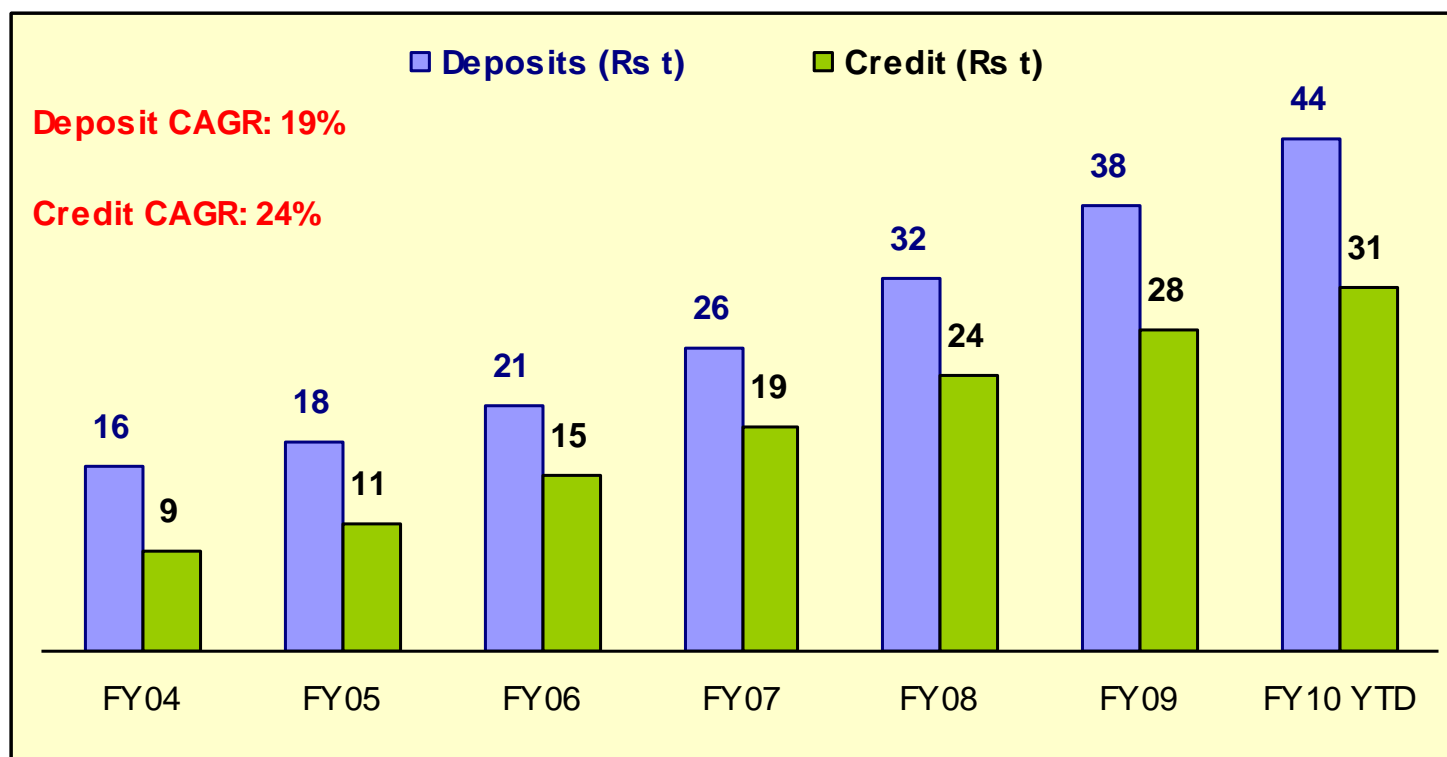
# Savings boom in NTD Era

At 35% of GDP, India's savings could hit US\$1 tn in 7-8 years



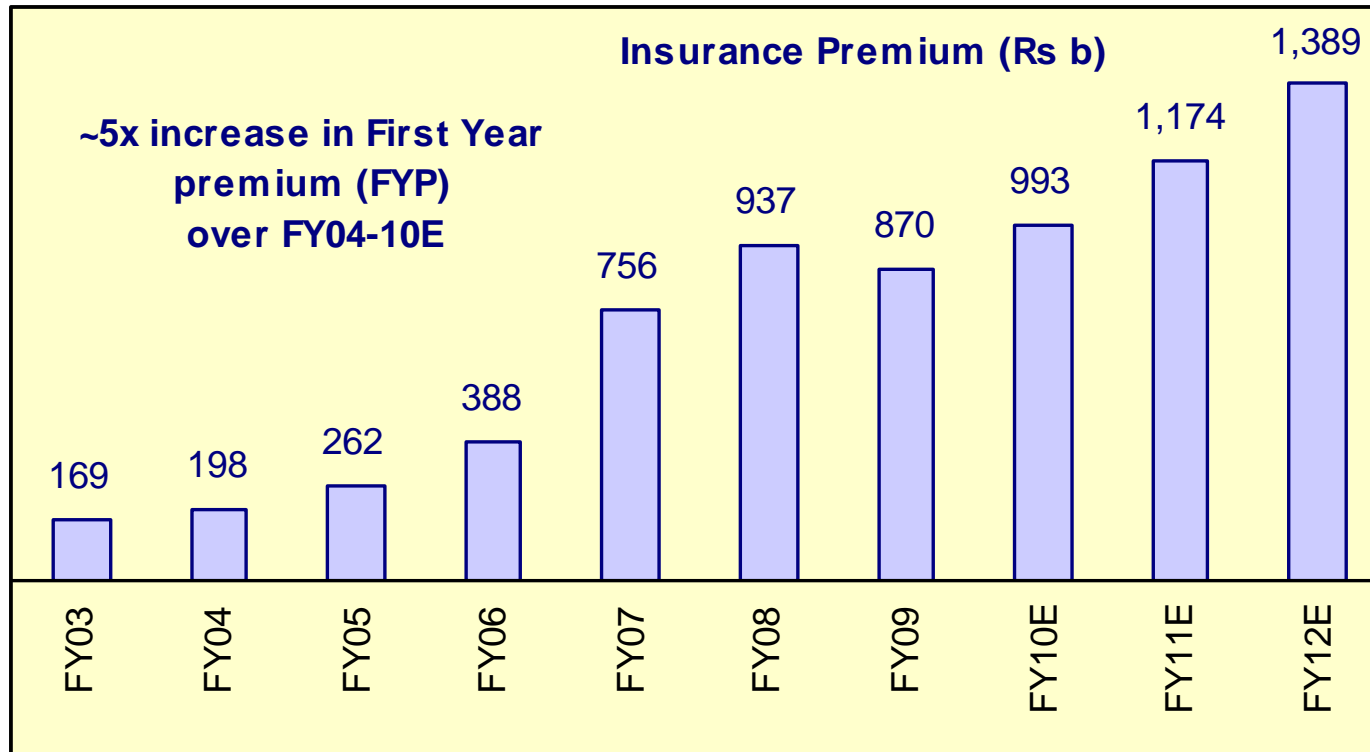
## Savings boom in NTD Era

Huge financial intermediation opportunity for banks



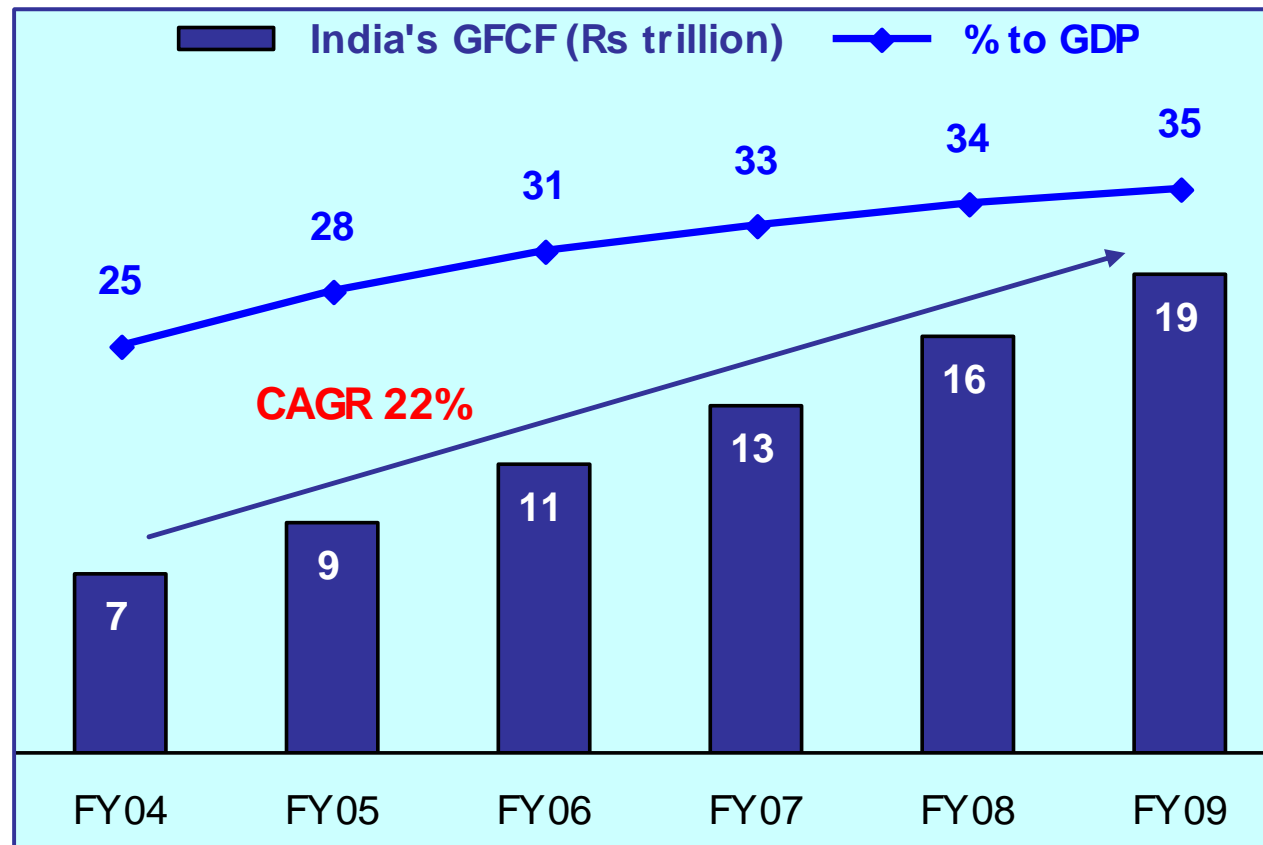
## Savings boom in NTD Era

### Huge opportunity for insurance



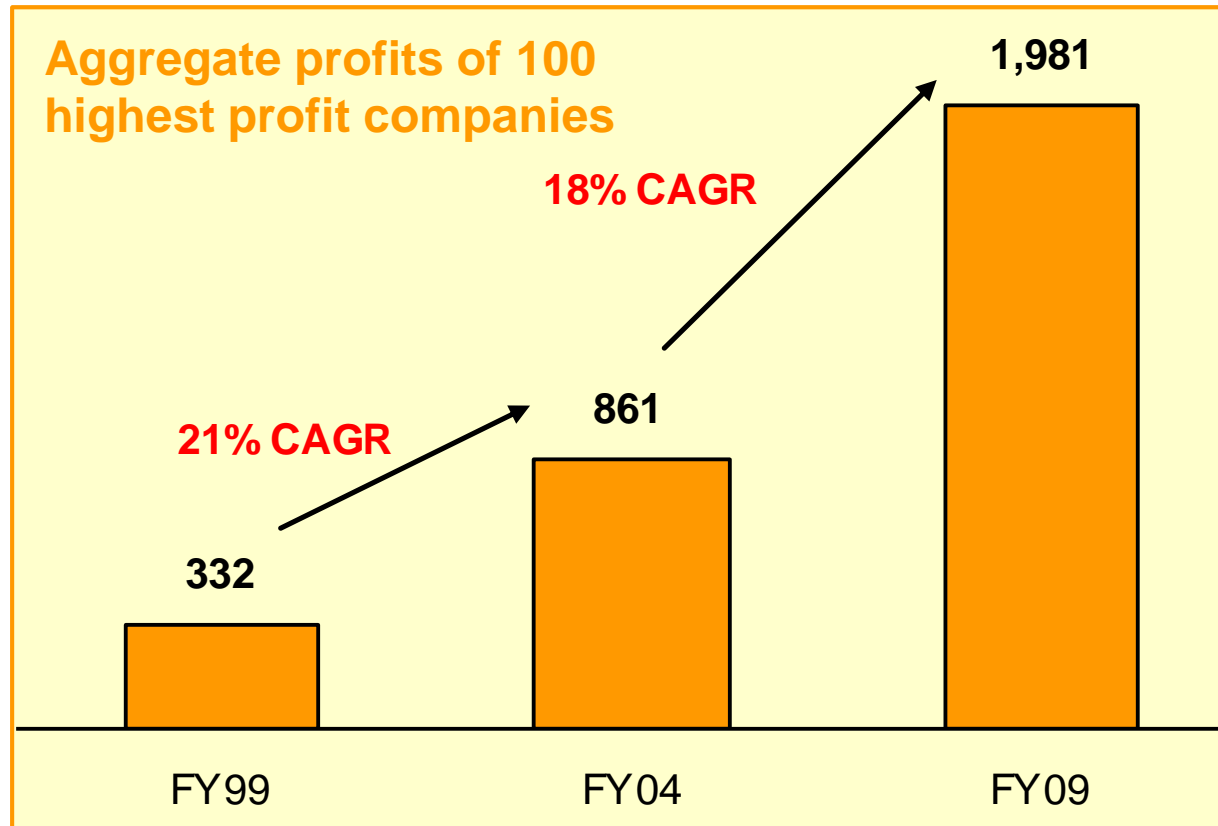
# Investment boom in NTD Era

Huge opportunity for Engg, Construction, Real Estate, Infrastructure, Cement, Steel, Electricals, etc



# Corporate profit boom in NTD Era

Future corporate profitability should be better than past



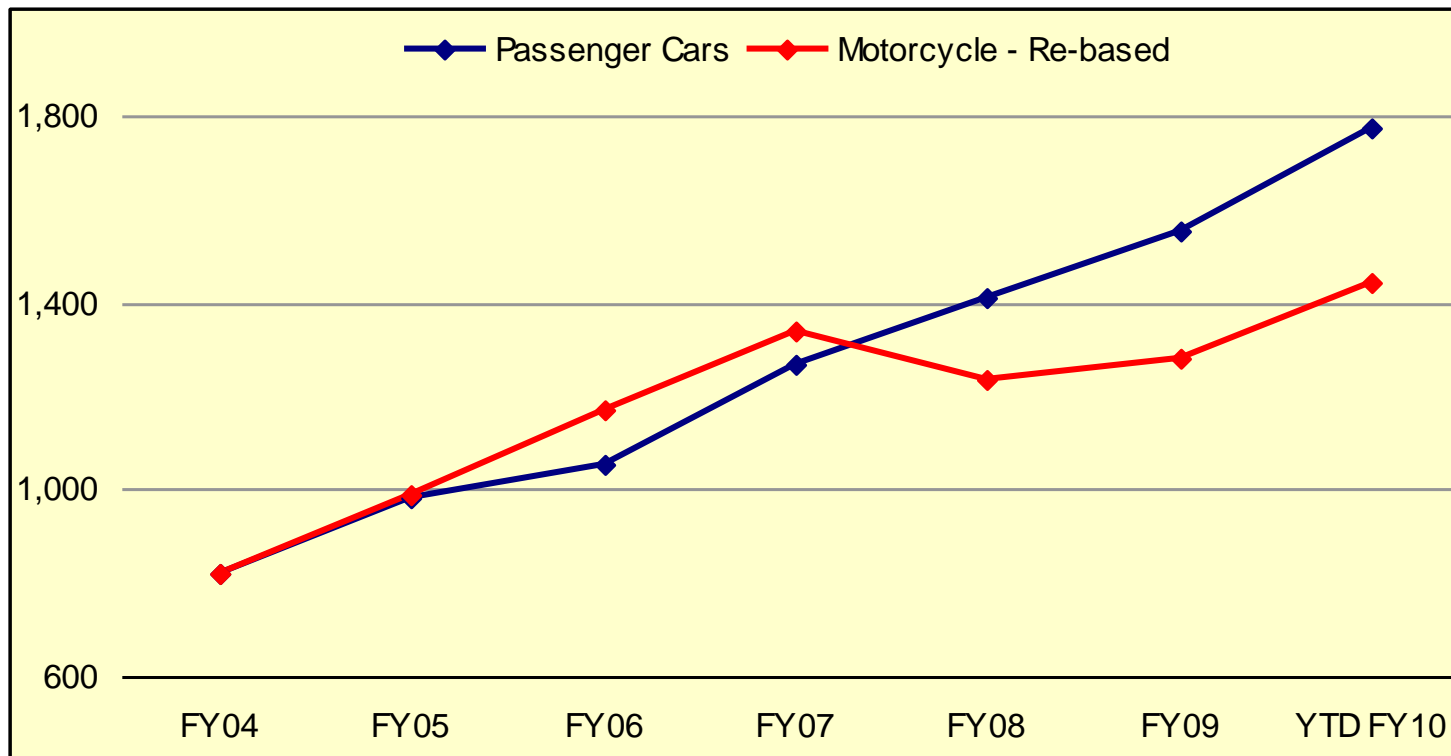
## Finding Winner Categories





# Winner Categories - Insights

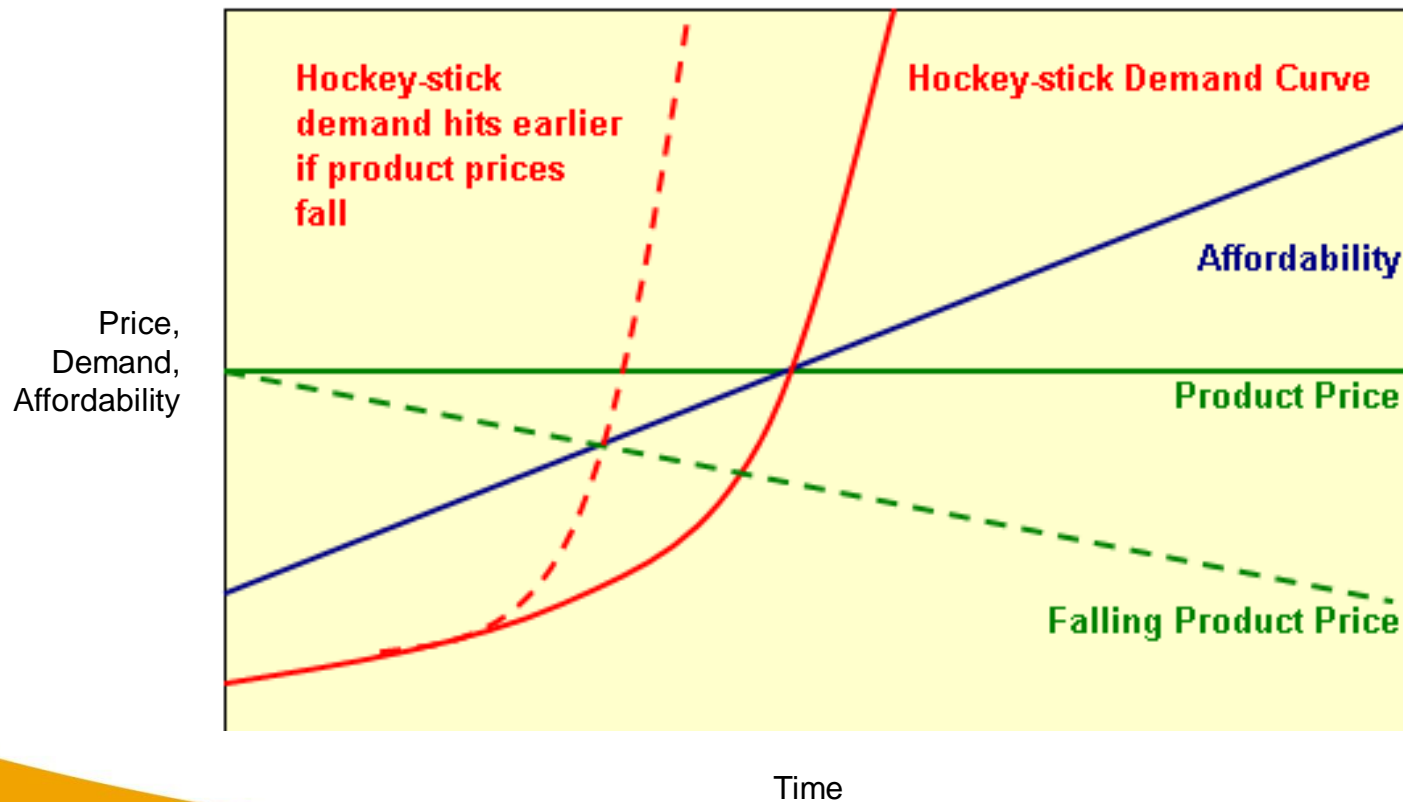
Value migrates from basic spend to discretionary spend categories



# Winner Categories - Insights

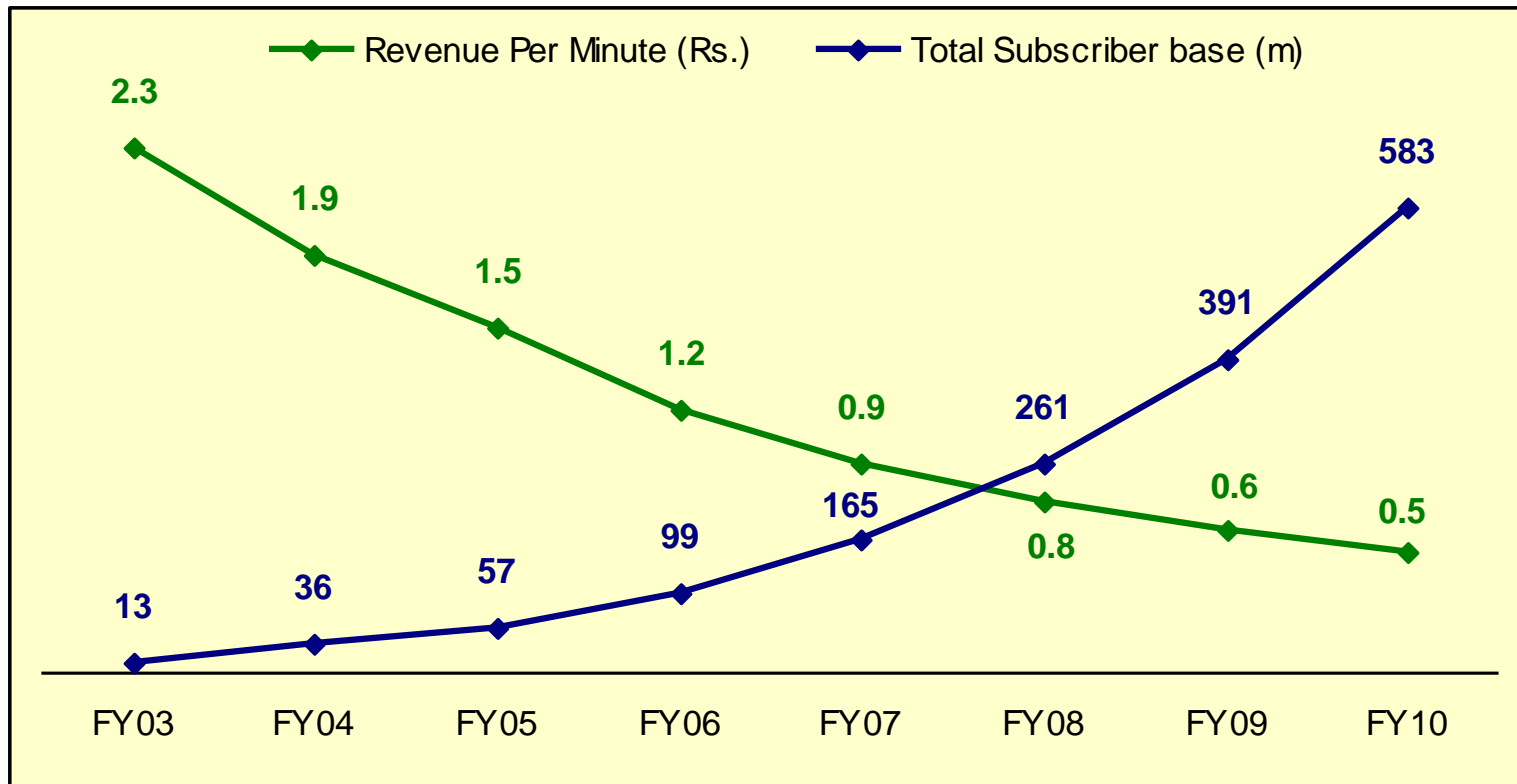
## Winner Categories see hockey-stick demand curves

Hockey-stick demand curve occurs when product price meets affordability for a large section of customers



# Winner Categories - Insights

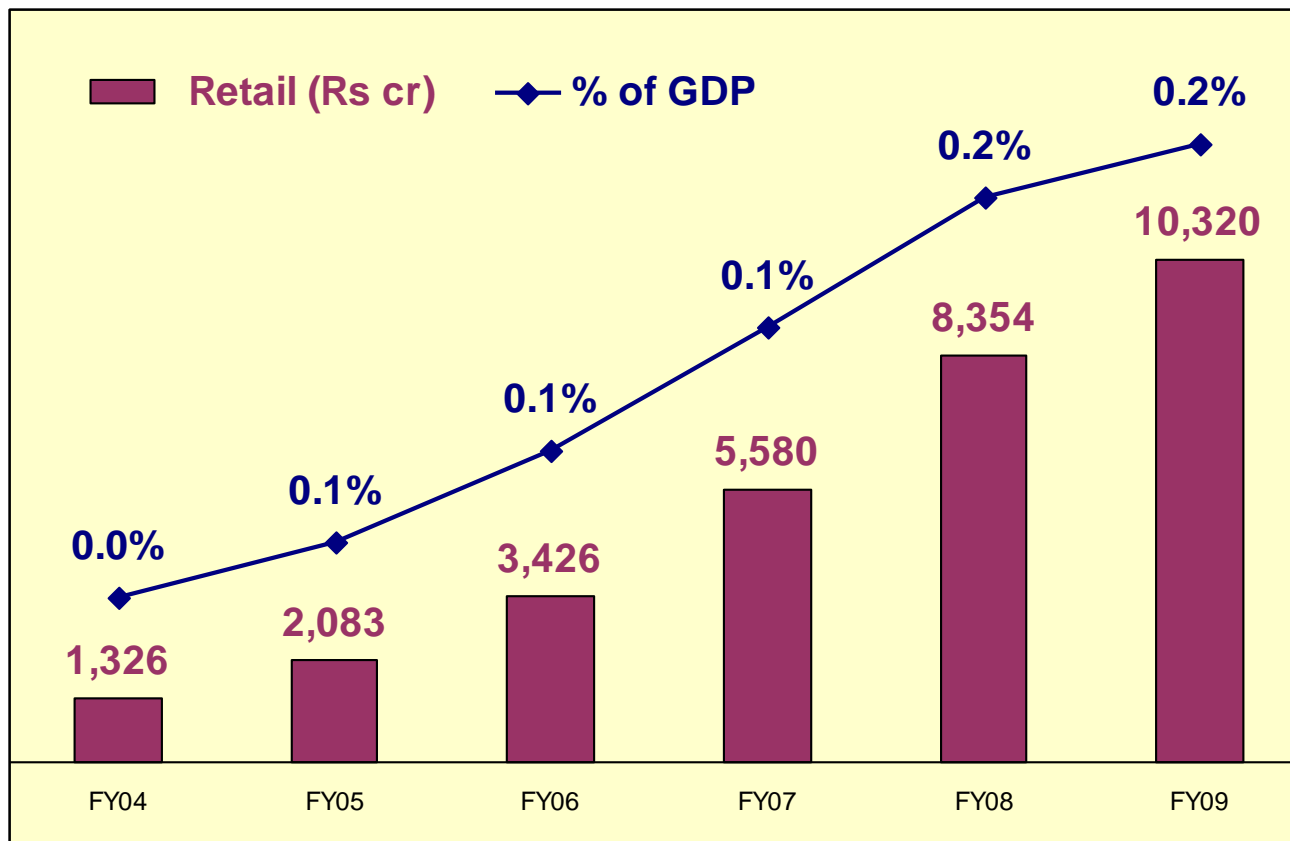
Falling product price accelerates demand in wireless telecom



# Winner Categories - Insights

Categories with size and scalability are potential winners

Retail sales of major listed players



# Winner Categories - Insights



Categories with growth and consolidation are winners

<b>Category Growth</b> High  Medium  Low	Education Gems & Jewelry IT - Hardware IT - Software Healthcare Services Household Appliances Real Estate	Auto - Cars Finance - Banks, Public sector Finance - Banks, Private sector Finance - Brokerages Media - Entertainment	Alcoholic Beverages Auto - Tractors Auto - 2-wheelers Aviation Cap. Goods - Power Engg/Constn - Turnkey Finance - Housing Finance - Insurance	Finance - Credit Rating FMCG - Proc. Food Infrastructure Oil & Gas - Gas Distbn. Telecom	
	Cement Hotels Pharmaceuticals	Utilities - Power Generation	Auto - CVs Auto Ancillaries FMCG - Personal Care Metals - Non-ferrous/Mining Metals - Steel, Primary Oil & Gas - Refining	Paints Tyres	
	Chemicals Fertilizers Sugar Tea Textiles	Shipping	FMCG - Cigarettes		
	Low	Medium	High		
	<b>Consolidation</b>				

# Winner Categories – Final list



1. Alcoholic beverages	12. Finance - Housing
2. Auto - 2-wheelers	13. FMCG - Personal Care
3. Auto - Cars & UVs	14. FMCG - Processed Food
4. Auto - Tractors	15. Gas distribution
5. Capital Goods - Power equipment	16. Infrastructure
6. Construction	17. Insurance
7. Engineering - Turnkey	18. Media - Entertainment
8. Finance - Banks, Private sector	19. Real Estate
9. Finance - Banks, Public sector	20. Retailing
10. Finance - Brokerages	21. Telecom
11. Finance - Credit rating	

All our Winner Categories will grow at least 1.5x GDP growth rate



## Finding Category Winners



# Category Winners



## Characteristics to find Category Winners -

- **Entry Barriers**
- **Great Management**





# What are Entry Barriers?

- **Entry Barriers is a simpler term for sustainable competitive advantage**

“The existence of barriers to entry means that incumbent firms are able to do what potential rivals cannot. Being able to do what rivals cannot is the definition of competitive advantage. Thus, barriers to entry and incumbent competitive advantage are simply two ways of describing the same thing.” – Bruce Greenwald and Judd Kahn in their book ***Competition Demystified***

- **Horlicks v/s Milo**



# Analyzing Entry Barriers



## Kinds of Entry Barriers

- **Demand side**
  - Customer Captivity, Differentiated Brands, Strong distribution network, High switching costs
- **Supply side**
  - Patent protection for products and/or processes
  - Privileged access to critical inputs e.g. captive ore mines
- **Economies of scale**

**Category Winners tend to enjoy all  
3 kinds of Entry Barriers**



# Analyzing Entry Barriers

**Demand side Entry Barriers are intangible and generate huge returns on capital**

COMPANY	ADJUSTED ROCE (%)	
	LATEST	10-YR AVG
Hero Honda Motor	50	80
Nestle India	171	71
Godrej Consumer	34	70
Colgate Palmolive	179	67
Hindustan Unilever	105	67
Castrol India	91	58
GlaxoSmithKline Pharma	57	52
Abbott India	45	48
Astrazeneca Pharma	72	47
P & G Hygiene	54	44



# Great Management



For the purposes of this discussion, great management is one which -

- Successfully defends or even increases Entry Barriers and
- Manages growth at least in line with category



## Finding Winning Investments



## Category Winners at Reasonable Valuation

**Don't buy into Bubble Valuation**



# Winning Investments

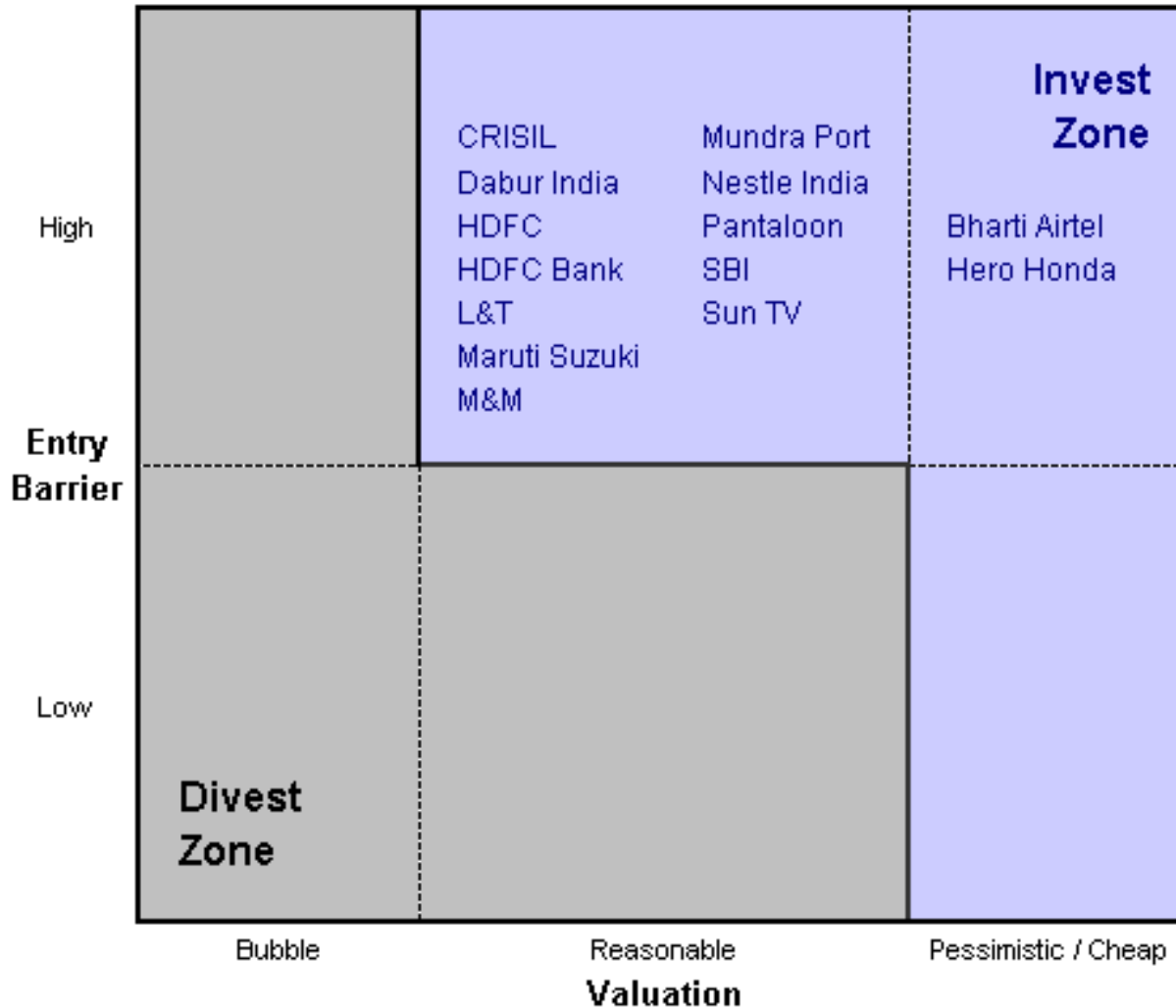


“We are partial to putting out large amounts of money where we won’t have to make another decision. If you buy something because it’s undervalued, then you have to think about selling it when it approaches your calculation of its intrinsic value. That’s hard. But, if you can buy a few great companies, then you can sit on your ass. That’s a good thing.”

- **Charlie Munger**, co-owner of Berkshire Hathaway,  
*in his book **Poor Charlie’s Almanack***



# Winning Investments Evaluation



Category Winners in the Invest Zone are winning investments



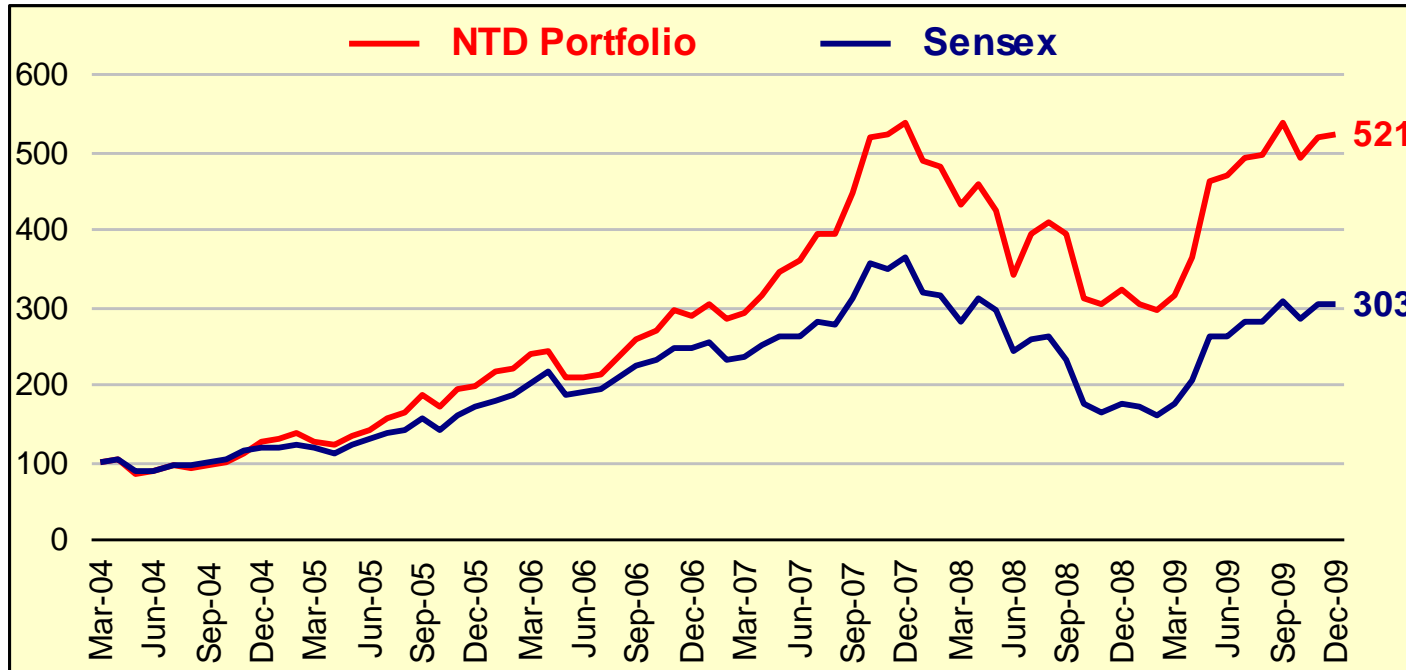


# Model Portfolio for NTD Era

WINNER CATEGORY	CATEGORY WINNER
Auto - 2-wheelers	Hero Honda Motor
Auto - Cars & UVs	Maruti Suzuki
Auto - Cars & UVs / Tractors	Mahindra & Mahindra
Capital Goods - Power equipment	B H E L
Engineering - Turnkey	Larsen & Toubro
Finance - Banks, Private sector	HDFC Bank
Finance - Banks, Public sector	State Bank of India
Finance - Credit Rating	CRISIL
Finance - Housing	H D F C
FMCG - Personal Care	Dabur India
FMCG - Processed Food	Nestle India
Infrastructure	Mundra Port
Media - Entertainment	Sun TV
Retailing	Pantaloon Retail
Telecom	Bharti Airtel



# NTD Era Portfolio Performance



The NTD Era portfolio would have outperformed if purchased any time in the last five years

## NTD Portfolio Performance

## Return to date if purchased in

	Mar-09	Mar-08	Mar-07	Mar-06	Mar-04
Average Return	89%	41%	85%	104%	521%
BSE Sensex Return	77%	10%	31%	52%	303%
<b>Outperformance</b>	<b>12%</b>	<b>31%</b>	<b>53%</b>	<b>51%</b>	<b>218%</b>
Stocks outperforming Sensex	7	11	11	12	13
<b>% of 13-stock portfolio *</b>	<b>54%</b>	<b>85%</b>	<b>85%</b>	<b>92%</b>	<b>100%</b>

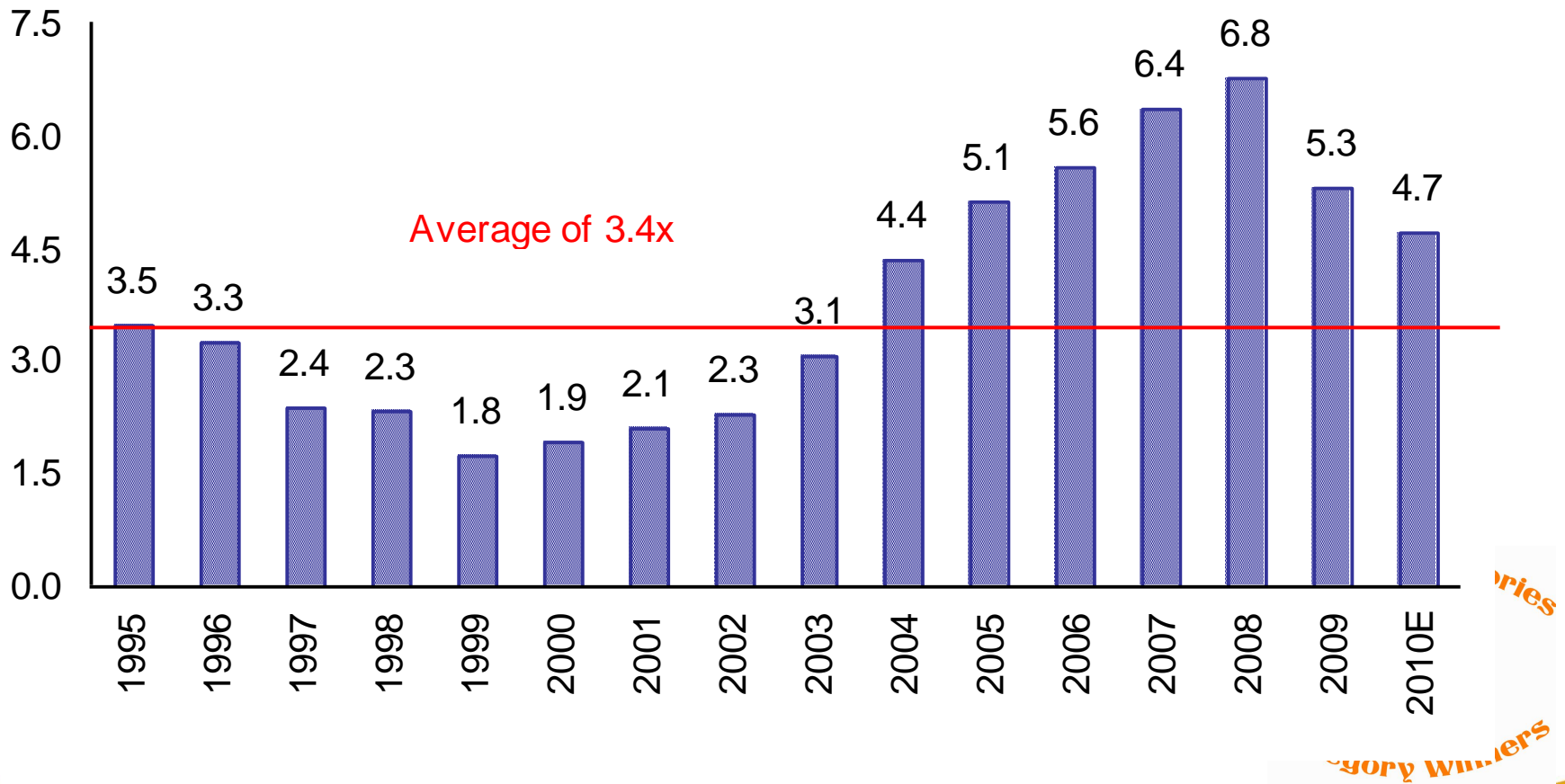
\* Sun TV and Mundra Port not included due to short listing history



# Market Outlook



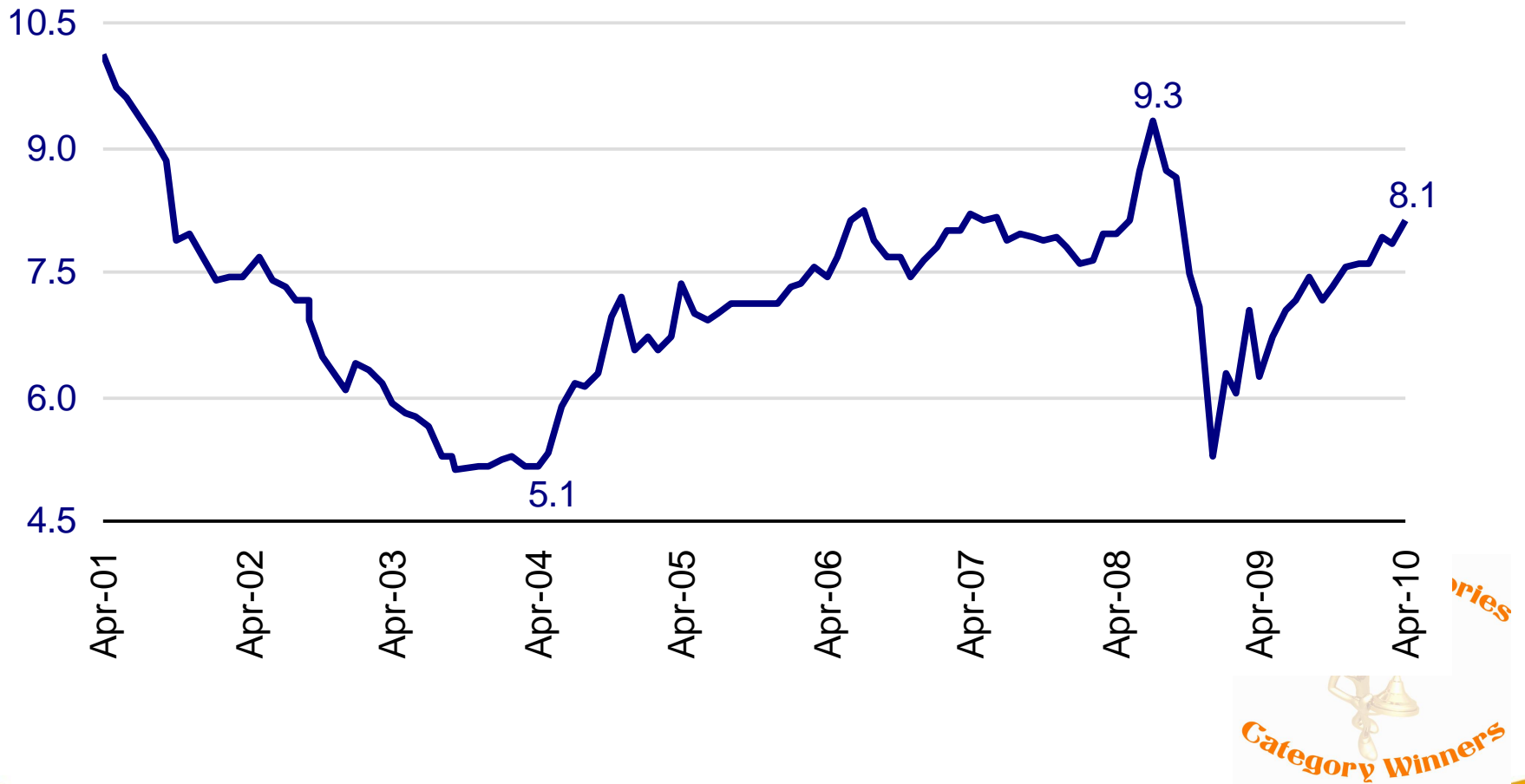
# Corporate Profit / GDP to bottom out



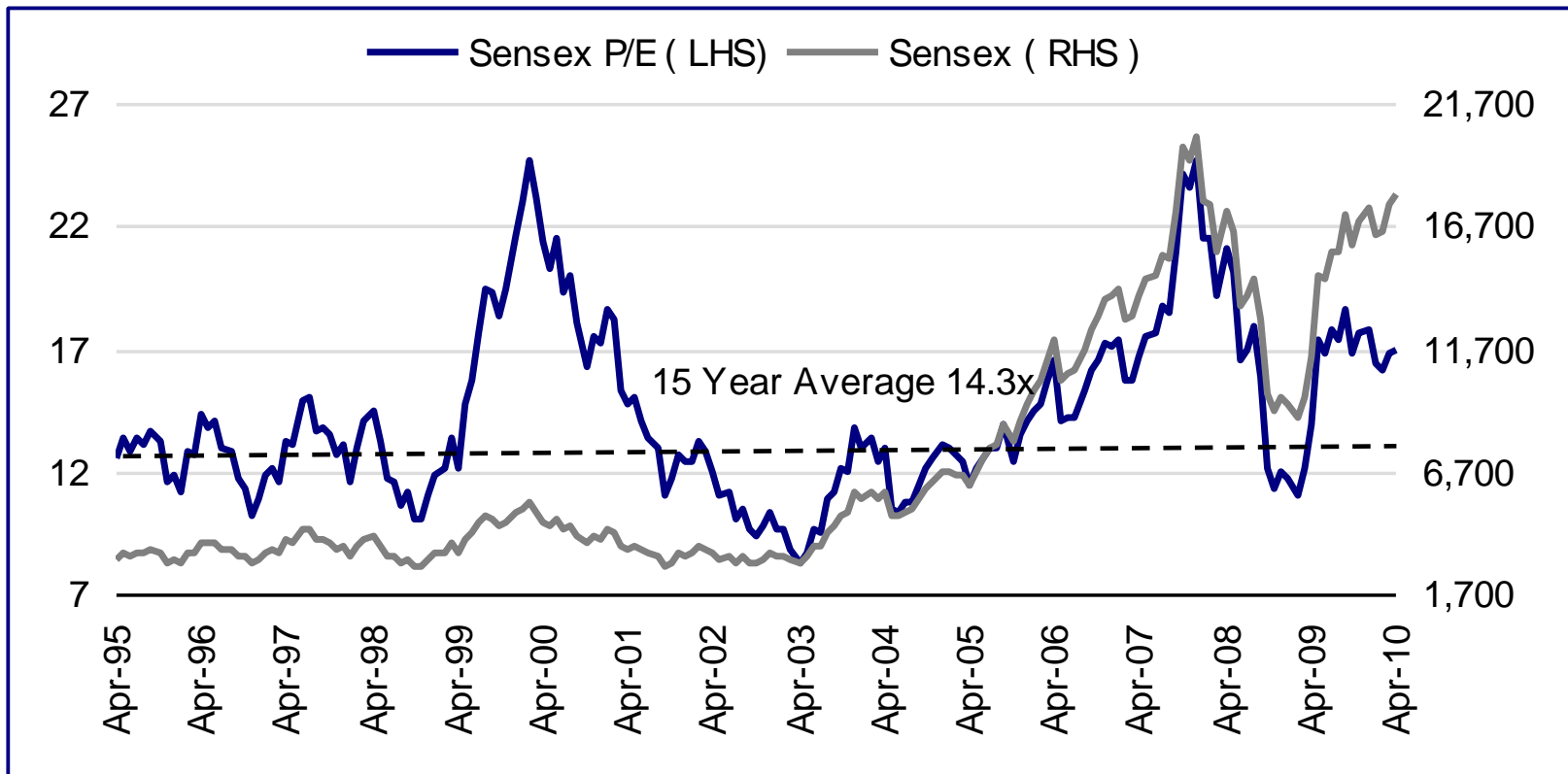
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Category Winners

# Interest rates likely to stabilize



# Sensex P/E at 12% premium to LTA

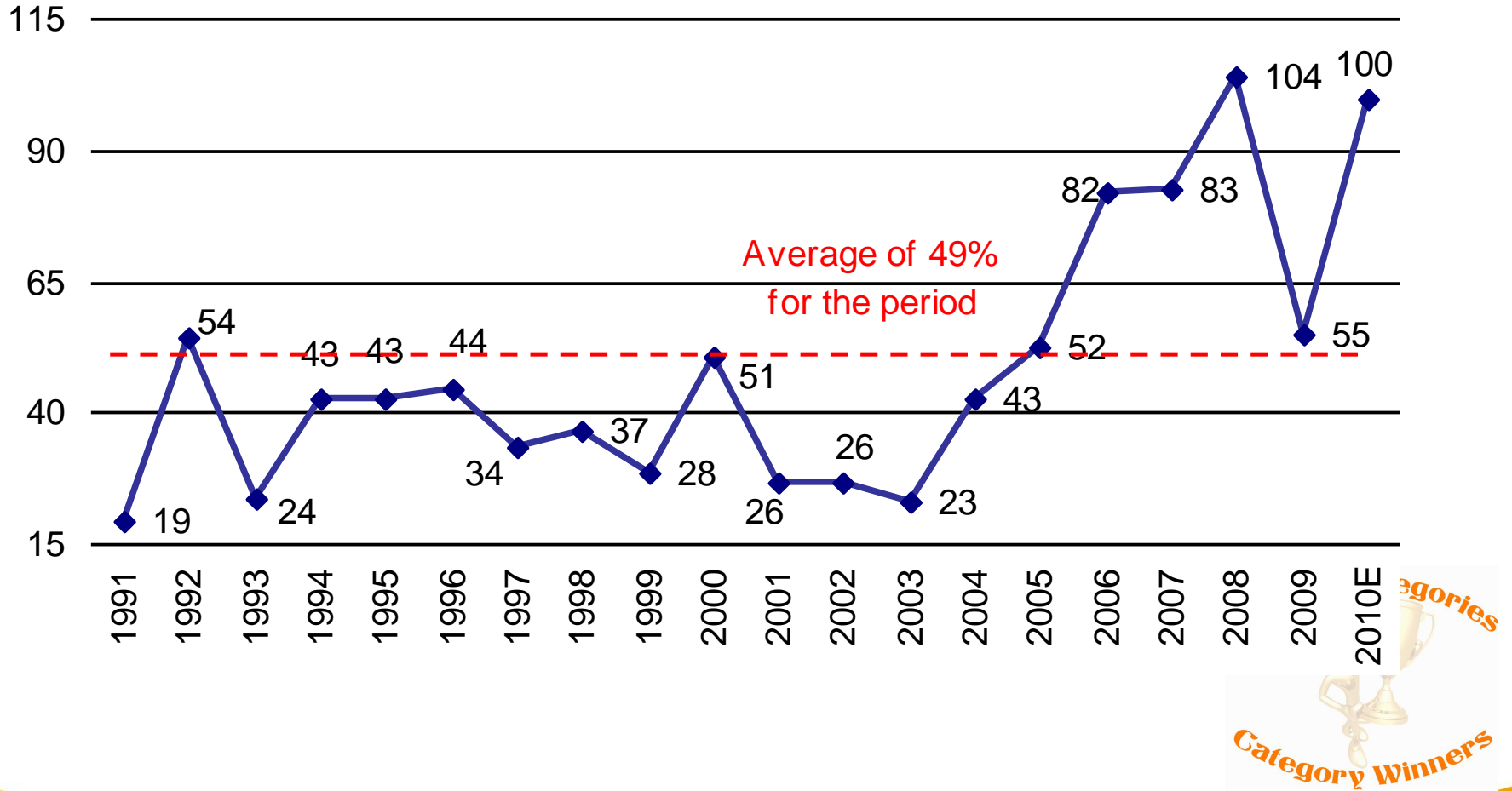


Categories

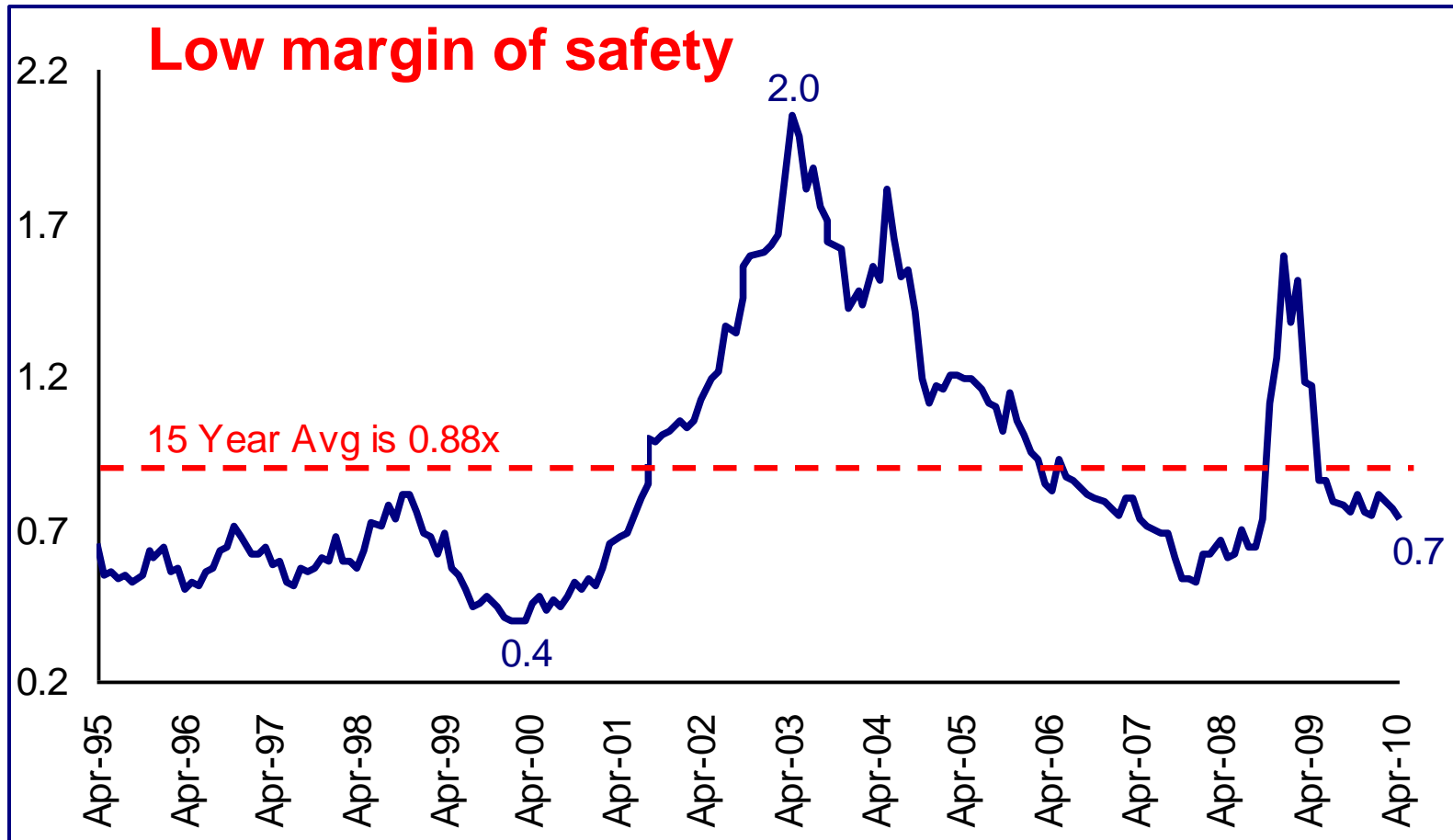
Category Winners



# MCap/GDP – close to all-time high



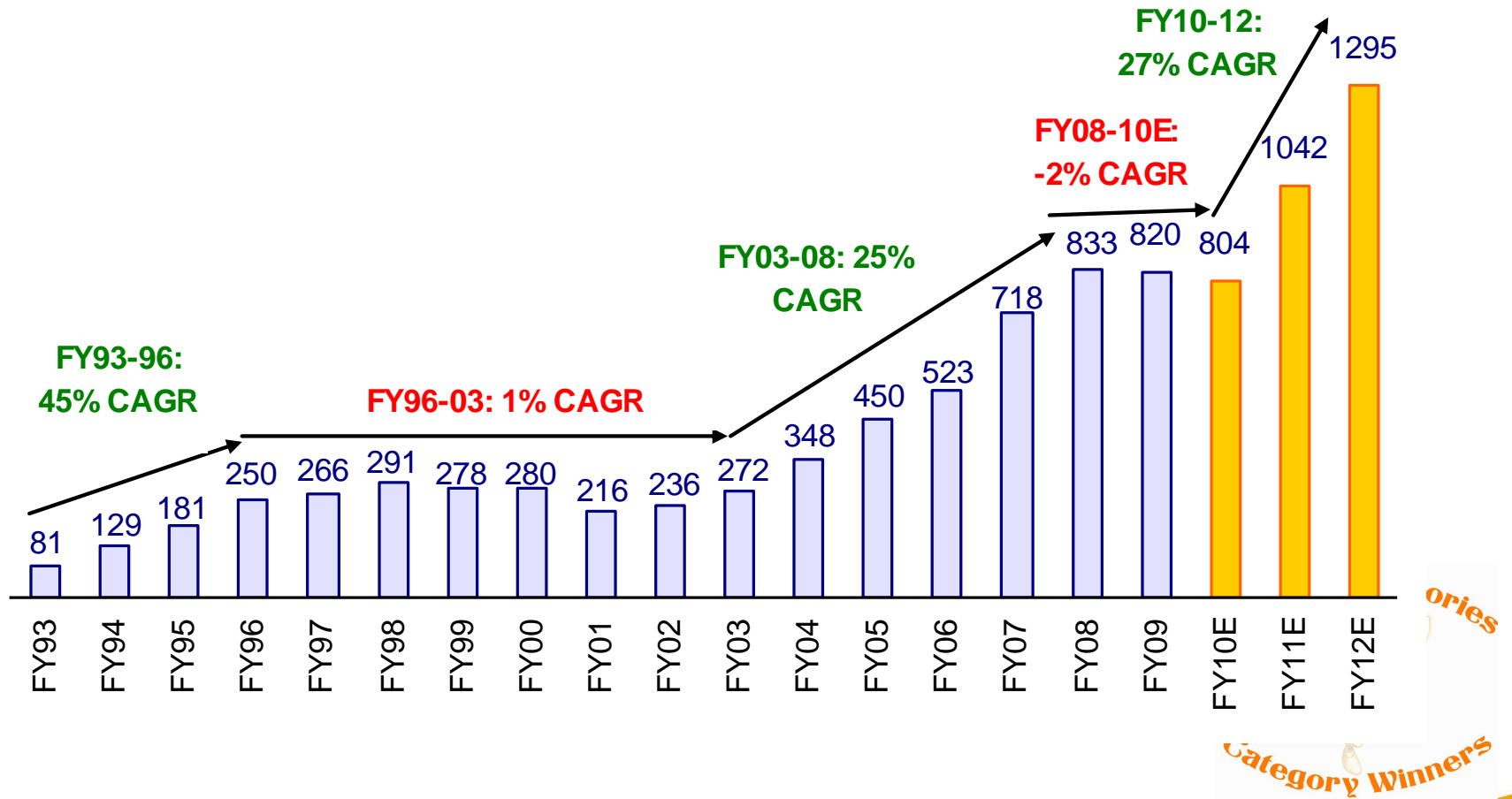
# Earnings Yield / Bond Yield



Categories  
Category Winners



# Earnings growth to see a new cycle



# In Conclusion



- **NTD Era** will be marked by sustained boom in discretionary spend, savings and investment.
- **Winner Categories** and **Category Winners** will enjoy exponential growth in profits.
- Category Winners bought at **reasonable valuation** create significant wealth over the long term.
- Markets are likely to reward growth in earnings



**Wishing you exponential returns in  
exponential times !**

**Thank You & Happy Wealth Creating !!**

