



Tax headwinds to weigh on near-term performance

Consumer Goods

Sharekhan code: ITC

Reco/View: Buy



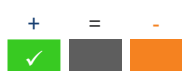
CMP: Rs. 350

Price Target: Rs. 420



3R MATRIX

Right Sector (RS)



Right Quality (RQ)



Right Valuation (RV)



+ Positive

= Neutral

- Negative

What has changed in 3R MATRIX

	Old		New
RS	Positive	↔	Positive
RQ	Positive	↔	Positive
RV	Positive	↔	Positive

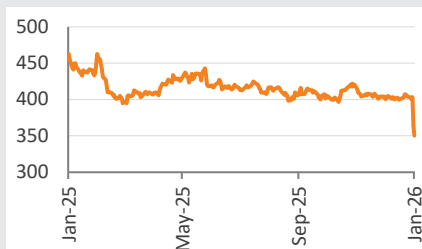
Company details

Market cap:	Rs. 4,38,637 cr
52-week high/low:	Rs. 471 / 345
NSE volume: (No of shares)	139.6 lakh
BSE code:	500875
NSE code:	ITC
Free float: (No of shares)	1252.7 cr

Shareholding (%)

Promoters	0.0
FII	38.3
DII	47.4
Others	13.4

Price chart



Source: NSE India, Mirae Asset Sharekhan Research

Price performance

(%)	1m	3m	6m	12m
Absolute	-12.7	-13.7	-15.2	-24.3
Relative to Sensex	-13.4	-19.6	-18.0	-31.6

Source: Mirae Asset Sharekhan Research, Bloomberg

Summary

- The recent hike in taxes on cigarettes expected to the tune of 20-55%, effective February 1, 2026 looks unusually steep.
- This hike is likely to hit volumes and margins, and spur illicit trade in the near term. Margin pressure is also expected, as the company may not be able to pass on the tax burden fully to consumers.
- ITC's long-term prospects are intact as it will soften the impact through calibrated price hikes, product mix optimisation, cost efficiencies and scale benefits. Rising contribution from other businesses also provides earnings diversification.
- Stock trades at 21x/20x/19x its FY26E/FY27E/FY28E EPS, respectively. We maintain a Buy with a revised PT of Rs. 420.

As per a recent government notification, effective February 01, 2026, specific excise duties will be levied depending on length of the cigarette, replacing the existing compensation cess structure. Moreover, earlier in GST 2.0, the government had revised the rate on cigarettes from 28% to 40% which will also be implemented from the same date. Accordingly, taxes on cigarettes are expected to rise 20-55%. While a revision in taxation was expected, the quantum has negatively surprised the street. This unusually steep hike is expected to hit near-term volumes and potentially spur illicit trade. We expect EBIT to shrink, as the company may struggle to fully pass on the tax burden to consumers given the magnitude of the hike. However, ITC's long-term growth prospects remain intact; the company is likely to offset these headwinds through calibrated pricing, cost efficiencies, and an optimized product mix, while growing non-cigarette business segments provide essential earnings diversification.

- Adverse shift in tax regime:** As per the government notification, excise duty on the cigarette has been imposed in the range of Rs. 2,100 to Rs. 8,500 per 1,000 sticks depending on the length of the cigarettes, leading to a 20-55% increase in the tax rate on the cigarettes. This will be over and above the 40% GST rate and both will be implemented from February 01, 2026. Clarity on whether the NCCD (National Calamity Contingent Duty) will be included in this excise duty is awaited. The tax hike is higher for longer cigarettes, while the hike is relatively modest for those under 65mm in length.
- Volumes and margins to be stressed:** ITC will have to hike prices by 10-30% in its cigarette portfolio to pass on tax hike to the consumers. Accordingly, cigarette volumes are likely to see a mid-single digit y-o-y decline in FY27. Further, this might also lead to proliferation of illicit/counterfeit cigarettes. Margin is also likely to be under pressure, as the company may not be able to fully pass on the tax burden to consumers and would take calibrated price increase.
- Long term outlook intact:** Despite immediate headwinds, ITC's long-term prospects remain strong. The company is likely to mitigate these impacts through 1) Calibrated price hikes, 2) An optimized product mix, 3) Operational excellence by leveraging cost efficiencies and scale benefits and 4) Diversification (rising contribution from non-cigarette business segments provides a buffer and ensures resilient earnings growth). Further, tailwinds in the form of 1) Tobacco RM likely to turn favourable in FY27 after challenging past few quarters, 2) Benefit in foods portfolio due to recent GST cuts and 3) Recovery in paper business will support growth in the coming years.

Our Call

View - Retain Buy with a revised PT of Rs. 420: Increased taxation on cigarettes has raised concerns on the company's near-term growth and is likely to impact volumes and margins in the coming quarters. ITC has undertaken relevant strategic actions to revive growth in the non-cigarette FMCG business. Long-term growth trajectory remains intact, with most business segments maintaining steady progress. We have reduced FY27-FY28 estimates by 9-12% to factor in the near-term pressure. The stock has corrected ~13% in the past two days since the announcement and trades at 21x/20x/19x its FY26E/FY27E/FY28E EPS, respectively. We maintain a Buy on the stock with a revised SOTP-based PT of Rs. 420.

Key Risks

Any further hike in taxes on cigarettes, slow recovery in consumer demand or sustained volatility in raw-material prices would act as key risks.

Valuation (Standalone)

Particulars	Rs cr				
	FY24	FY25	FY26E	FY27E	FY28E
Net revenues	62,628	69,324	73,911	78,794	84,503
OPM (%)	37.5	34.7	33.0	33.5	34.0
Adjusted PAT	19,910	19,669	20,045	21,536	23,114
Adjusted EPS (Rs.)	15.9	16.1	16.0	17.2	18.5
P/E (x)	21.5	21.3	21.3	19.8	18.5
P/B (x)	6.0	6.5	6.3	6.4	6.6
EV/EBIDTA (x)	17.7	17.4	17.2	15.9	14.6
RoNW (%)	28.5	28.7	29.2	31.4	34.4
RoCE (%)	30.0	30.4	31.8	34.3	38.0

Source: Company; Mirae Asset Sharekhan estimates

Outlook and Valuation

■ Sector Outlook – Tax biz unfavourable; other businesses steady

The domestic cigarettes industry in the past was affected by a sustained rise in taxes and regulatory regime along with a sharp hike in illegal trade in the past few years, especially at the premium end, which continues to pose significant challenges to the legal cigarettes industry. However, in recent times, the government has undertaken stringent actions to curb illicit cigarette sales. This along with lower price hikes in the cigarette portfolio will help cigarette companies post better volume growth. On the FMCG front, consumer demand is expected to improve from H2FY26 with reduction in tax on consumer goods, further supported by the festive season. We expect margins to have bottomed out in Q1 and see margins rise from H2FY26 aided by easing raw material price inflation, new inventory coming in and better operating leverage through higher volumes.

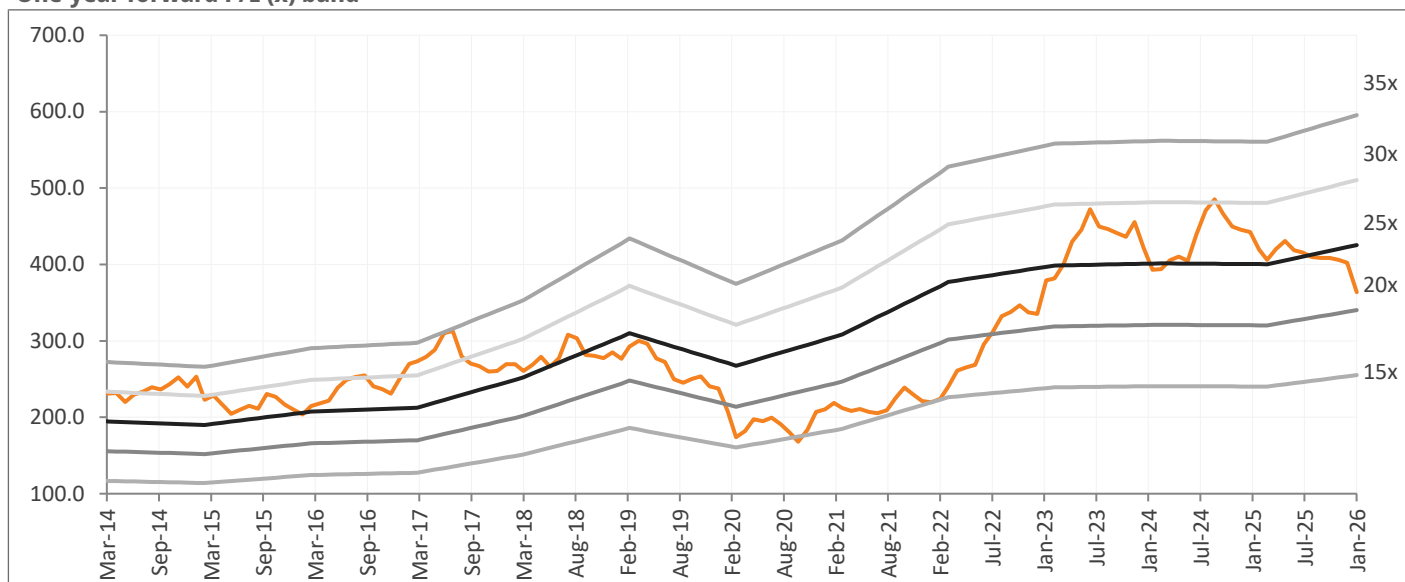
■ Company Outlook – Higher cigarette taxes to dent performance

Cigarette volumes and margins are likely to be impacted in the near term due to a sharp increase in taxes on cigarettes. Market coverage for FMCG products was stepped up to 2x pre-pandemic levels. Direct reach enhancement was around 1.4x over pre-pandemic levels. Strong traction to product launches and increased digital and modern trade salience will help the non-cigarette FMCG business's revenue to consistently grow in mid-teens to high teens in the coming years. PBIT margins will improve, led by efficiencies and scale-up in the contribution of new businesses. We expect ITC's revenue and PAT to report a 7% and 6% CAGR, respectively over FY25-FY28E.

■ View – Retain Buy with a revised PT of Rs. 420

Increased taxation on cigarettes has raised concerns on the company's near-term growth and is likely to impact volumes and margins in the coming quarters. ITC has undertaken relevant strategic actions to revive growth in the non-cigarette FMCG business. Long-term growth trajectory remains intact, with most business segments maintaining steady progress. We have reduced FY27-FY28 estimates by 9-12% to factor in the near-term pressure. The stock has corrected ~13% in the past two days since the announcement and trades at 21x/20x/19x its FY26E/FY27E/FY28E EPS, respectively. We maintain a Buy on the stock with a revised SOTP-based PT of Rs. 420.

One-year forward P/E (x) band



Source: Company; Mirae Asset Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY25	FY26E	FY27E	FY25	FY26E	FY27E	FY25	FY26E	FY27E
Hindustan Unilever	53.8	52.2	47.2	38.0	36.4	33.0	26.9	28.6	32.9
ITC	21.3	21.3	19.8	17.4	17.2	15.9	30.4	31.8	34.3

Source: Company; Mirae Asset Sharekhan Research

About company

ITC is one of the largest diversified players in India present in businesses such as cigarettes, FMCG, agri, and paper. The company is the market leader in the domestic cigarette and PPP segments. The company has a robust distribution reach of more than 2 million, which it is utilising to scale up its consumer goods business and de-risk its business model. ITC's revenue and PAT grew by 3.0x and 3.8x, respectively, over FY09-FY20.

Investment theme

ITC is focusing on de-risking its business model by reducing dependence on its core cigarette business (affected by regulatory and tax hurdles for the past few years) by scaling up the fast-growing consumer goods, PPP, and agri businesses. Post the demerger of the asset-heavy hotels business, the return profile of ITC will substantially improve in the coming years, with RoE/RoCE expected to rise to ~34%/~38% in FY28 from ~29%/~30% in FY25, respectively.

Key Risks

- ◆ A significant rise in taxes on cigarettes or government actions to curb tobacco and tobacco consumption would act as a key risk to the cigarette business.
- ◆ Sustained consumption slowdown would affect the growth rate of categories such as consumer goods and hotels in the near term.

Additional Data

Key management personnel

Name	Designation
Sanjiv Puri	Chairman and Managing Director
Supratim Dutta	Chief Financial Officer
Rajendra Kumar Singhi	Executive Vice President & Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	British American Tobacco PLC	22.91
2	Life Insurance Corp of India	15.85
3	Unit Trust of India	7.78
4	SBI Funds Management Ltd.	3.30
5	ICICI Prudential AMC Ltd.	2.70
6	GQG Partners LLC	2.18
7	General Insurance Corp of India	1.73
8	Goldman Sachs Group Inc.	1.69
9	Goldman Sachs Trust II GQG Intl.	1.65
10	NPS Trust A/c Util retirement solutions Ltd.	1.58

Source: Bloomberg

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Understanding the Mirae Asset Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/ weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Mirae Asset Sharekhan Research

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SEBI Regn. Nos.: BSE / NSE (CASH / F&O / CD) / MCX - Commodity: INZ000171337; BSE - 748, NSE - 10733, MCX - 56125, DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669 (date of initial registration: 03/07/2004, and valid till 02/07/2026); IRDAI Registered Corporate Agent (Composite) License No. CA0950, valid till June 13, 2027.

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