

## MANAGEMENT DISCUSSION AND ANALYSIS

In line with international practice, Marico has been reporting consolidated results taking into account the results of its subsidiaries. This discussion therefore covers the financial results and other developments during April '04 - March '05 (FY05) in respect of Marico Consolidated - Marico Limited together with its subsidiaries Marico Bangladesh Limited (MBL), MBL Industries Limited (MBLIL), Kaya Skin Care Limited (KSCL) and its joint venture, Sundari LLC (Sundari). The consolidated entity has been, in this discussion, referred to as 'Marico' or 'The Company' or 'The Group'.

Some statements in this discussion describing the projections, estimates, expectations or outlook may be forward looking. Actual results may, however, differ materially from those stated on account of various factors such as changes in government regulations, tax regimes, economic developments within India and the countries within which your Company conducts its business, exchange rate and interest rate movements, impact of competing products and their pricing, product demand and supply constraints.

### INDUSTRY STRUCTURE AND DEVELOPMENT

Marico is committed, in accordance with its Business Direction, to improving the quality of people's lives through its offerings of branded products and services. The Company thus operates in two industries - Branded Products (the Fast Moving Consumer Goods (FMCG) industry) and Branded Services (Skin Care Services industry).

The FMCG industry comprises segments such as Personal Care, Soaps and Detergents, Skin Care, Oral Care, Health and Hygiene Products, Home Care, Hair Care, Coconut Oil,

Refined Edible Oils, Foods and Beverages, Dairy Products, etc. The FMCG industry is one of the largest in India, with an annual estimated turnover of Rs. 500 billion.

**WITH FY05 TURNOVER OF OVER RS. 1 BILLION, MARICO IS ONE OF THE LARGEST INDIAN FMCG COMPANIES IN TERMS OF OVERSEAS SIZE OF FRANCHISE.**

The FMCG industry typically is characterised by branding and product differentiation. However, over the last few years, differentiation has reduced due to lower innovation. This has led to emergence of smaller regional players who offer good quality products at reasonable price points. This has led to intensifying competition in the industry. Consumer insight into expressed and latent needs, innovation and cost control have assumed larger importance.

Another characteristic of this industry is the presence of a large unorganised sector, especially in rural India, offering products in loose unbranded form.

Of late, the FMCG industry has been witnessing the emergence of newer channels of distribution like Direct Marketing, large organised retail chains etc. Such developments are a fallout of the changing needs of Indian consumers. With the urban consumers becoming richer, younger and more aspirational, organized retailing is on the rise. With several malls and supermarkets springing up in cities across the country, organized retail penetration is likely to show a marked increase from its current estimated level of around 3%. Whilst on the one hand this puts pressure on margins as collective bargaining from retail chains increases, it also provides the opportunity to improve supply chain efficiencies and visibility of brands.

Marico has leveraged its core competitive advantages of Branding, Innovation, Distribution, Cost Management, and Research & Development in delivering higher value add to its consumers. It has deployed innovation to create product differentiation that enhances the brand equity.

Marico's portfolio of products, has, over the years created enduring value for its consumers. In the process, it has consolidated its presence in the market. In all its key categories of coconut oils, hair oils, anti-lice treatment, fabric care and premium refined edible oils, Marico has built significant market shares. During FY05, Marico has kept pace with the momentum of growth achieved in the past few years, with double-digit growth in topline and bottomline.

Marico's presence overseas (comprising exports from India and local operations in a foreign country) is entirely in branded FMCG products & services. The Company's products reach 24 countries, mainly in the SAARC and the Gulf. With FY05 turnover of over Rs.1 billion, Marico is one of the largest Indian FMCG companies in terms of overseas size of its franchise.

Holism, wellness and using natural products are now significant global trends. Skin care in the US is a large US\$ 7 billion market. Of this, US\$ 2 billion is attributable to the prestige skin care business, which is growing at the rate of 20% p.a. Spa is another segment that has grown very fast over the past few years. The market size of products used or sold in spas could be in the

region of US\$ 2 billion. Thus, there is a good potential for a skin care brand like Sundari, which focusses on selling Ayurvedic skin care products through spas and internet.

Over the years, especially

the past 5 years or so, owing to structural changes in the demographic profile of the Indian population, 'skin care' as a segment has gained importance. The modern-day consumer wants a healthy skin. She is looking for skin care offerings, both products and services that are safe and scientific. The current structure of the skin care services industry is fragmented, with local brands catering to local needs. There are very few corporate service providers. Marico's Kaya Skin Clinics attempt to fill this need gap with US FDA approved cosmetic dermatological procedures as also products that enhance the quality, look and feel of Indian skin.

## **OPPORTUNITIES AND THREATS**

Marico continuously seeks new opportunities in expanding its current portfolio of branded products and services, through constant gathering of new insights in consumer preferences.

On the macro economic front, India has been witnessing structural changes that open up new avenues for growth. The percentage of youth in the total population has grown significantly, with 55% of the total population being in the age group of 25-55. A new consuming class has emerged due to the rise of the service sector, and has unique needs. There is an increasing demand in the wellness categories (skin care and health care). All these have led to opportunities in various sectors of the Indian Economy. The Company is evolving strategies to exploit these opportunities and grow its businesses in the beauty and wellness segments.

With increasing popularity of beauty and wellness segments - skin care products and services, and healthy foods - Marico sees an opportunity to create new businesses in skin care and health care. It has already established itself in high-end skin care services through its Kaya Skin Clinics. The Company would leverage this



early mover advantage to garner a significant share of the overall skin care services and products pie.

Marico's refined edible oil brands - Saffola and Sweekar - already offer value-added healthy oils to health conscious consumers. Marico will aggressively pursue various prototypes in the category of health care products, and create brands with enduring value-generating apparatus.

Advancements in Information Technology will allow Marico's supply chain to reach even more consumers. In the process, it will also enhance the efficiency of the sales and marketing system.

Competition remains an ambient threat in any industry, especially in the FMCG sector, and has to be tackled on an ongoing basis. Product differentiation through genuine value add holds the key for survival and growth. Marico has been making continuous improvements, innovating in the fields of product formulation, packaging, distribution etc. It has introduced packs at various price points to address the different needs of consumers across income segments. In categories such as edible oils, where the market has witnessed crowding, Marico has been focussing on profitable growth, rather than chasing volumes.

## **THE HIGH MARGIN PORTFOLIO NOW CONSTITUTES 71% OF MARICO'S TURNOVER, UP FROM 66% LAST YEAR.**

Shifts in consumer habits may have an impact on the Company, and Marico has recognised the same. The Company has and will invest substantially in consumer education to ensure growth of its franchise, and has begun investing in newer categories in hair care and skin care.

Marico, like many other players in the branded FMCG segment, has been facing

the menace of unfair competition, manifesting itself in the form of duplicates, clones and pass-offs. The Company has initiated various measures to combat this menace by way of technology innovations and also field level action.

### **RISKS AND CONCERNS**

Macro-economic factors like recession, inadequate rainfall, subdued demand, political uncertainty, social upheavals and acts of God may affect the business of the Company as also the industry at large.

With increasing competitive pressures in all segments of the industry, increasing the market shares and the consumer base is a continuing challenge. Developments in technology - both 'hard' (product / packaging development) as also 'soft' (information, human resource management) - are other critical areas.

While a big rural franchise holds the key for many a FMCG player, changes in the purchasing power of the rural masses affect the overall business, as the rural incomes are closely linked to monsoons, although the linkage may be wearing off to some extent.

Adequate availability of key raw materials at the right prices is crucial for the Company. Any disruption in the supply or violent changes in the cost structure could affect the Company's ability to reach its consumers with the right value proposition.

Besides these, regulatory changes especially fiscal and those related to food and cosmetic laws, also have a bearing on the business performance, especially new opportunities.

The Company has, however, not been significantly impacted by these risk and concern factors due to the equity commanded by its

brands, product differentiation, proactive action towards anticipated hindrances, technological superiority and the strong distribution network.

Forays in new business areas and new product offerings would carry associated business risks. However, more astute management of financial and human resources, deployed in the new areas could help contain the attendant risks.

## **INTERNAL CONTROL SYSTEMS AND THEIR ADEQUACY**

Marico has a well-established and comprehensive internal control structure across the value chain to ensure that all assets are safeguarded and protected against loss from unauthorised use or disposition, that transactions are authorised, recorded and reported correctly and that operations are conducted in an efficient and cost effective manner. The key constituents of the internal control system are:

- Establishment and review of business plan.
- Identification of key risks and opportunities.
- Policies on operational and strategic risk management.
- Clear and well-defined organisation structure and limits of financial authority.
- Continuous identification of areas requiring strengthening of internal controls.
- Operating procedures to ensure effectiveness of business processes.
- System of monitoring compliance with statutory regulations.
- Well-defined principles and procedures for evaluation of new business proposals/capital expenditures.
- A robust management information system.
- A robust internal audit and review system, Aneja Associates, Mumbai, a firm of Chartered Accountants, being the Internal Auditors.

Internal Audits are undertaken on a continuous basis covering various areas across

the value chain like manufacturing, operations, sales and distribution, marketing, finance etc. Reports of the internal auditors are regularly reviewed by the Management and corrective action initiated to strengthen the controls and enhance the effectiveness of the existing systems. Summaries of the reports are presented to the Audit Committee of the Board.

During the year, the Company continued to track the effectiveness of controls across all operating centres, using a measure called Control Effectiveness Index (CEI). CEI is a proprietary methodology developed and deployed by the Internal Auditors in Marico. Under this system, a score on CEI is calculated based on status of control in each functional area. This system has helped strengthen controls in the Company through improved awareness among the role holders.

The SAP suite of ERP (SAP R/3, SCM, APO) provides a real time check on various transactions emanating from various business processes of the Company. Mi-Net, the web-enabled architecture that links Marico to its biggest business associates, namely its distributors also helps the Company exercise similar controls over its sales system.

## **HUMAN RESOURCES / INDUSTRIAL RELATIONS**

Marico is a professionally managed company that has built for itself a stimulating work culture that empowers people, promotes team building and encourages new ideas. This has, over the years, enabled Marico to grow its stature as one of the few successful Indian FMCG companies. Marico was awarded the National Award for outstanding work in HRD by National HRD Network in 1994 as also the award for Top Performing Global Growth Company from India at the World Economic Forum in 1997.

Human Resource programmes and initiatives

in Marico are aligned to meet the business needs. The Company believes in investing in people to develop and expand their capability. The Company has been able to create a favourable work environment that motivates performance, customer focus and innovation. Marico's strategies are based, inter alia, on processes of continuous learning and improvement.

Marico has a unique process of performance enhancement through deployment of MBR (Management By Results) to create an environment of challenge and provide opportunities for realisation of optimum performance.

The Company believes that engaging people leads to better performance as also proved by 'Gallup' - a research organisation of international repute, through research done over 20 years. It has therefore taken an active step in enhancing engagement in the organisation from its current levels, and the process is being partnered with Gallup India. The process involves measuring engagement levels, respective teams discussing the scores and action planning to improve the engagement in the teams. 2005 is the year where we have concluded the 4th Gallup Q12 engagement survey. Over the years, the overall engagement scores for the Company have increased year on year, which was a result of the actions taken based on the survey results. This is also reflected in the Company's performance over the years.

As on March 31, 2005, the employee strength of the Company was 1300.

Employee relations throughout the year were supportive of business performance.

#### **MARICO'S NEW IDENTITY**

##### **Solidity, freshness of thinking and vitality of spirit**

The most visible form of Marico's corporate



identity, its logo, was adopted during 1989. Since then, over the past 15 years, Marico has progressed from being a largely industrial enterprise to a more consumer-focussed FMCG, bringing value to the consumer across a wider range of products and services in the beauty and wellness space, through 12 brands.

Apart from its quintessential FMCG products, Marico offers consumers allied services in hair care (around brands such as Parachute Advanced, Silk-n-Shine) and health care (around brands such as Saffola). In skin care, Marico has invested in and promoted a new line of business under the brand 'Kaya Skin Clinic'. Overseas, it has acquired a holding in Sundari LLC, a skin care products business, catering to another service industry - the Spa business. All in all, there has been a significant increase in the range of offerings to the consumer - far beyond industrial products.

This establishment of a wider connect with the consumer beyond mere sale of industrial products has prompted Marico to drop the word 'Industries' from its name. The new name 'Marico Limited' reflects the extended range of its business better.

### **THE NEW IDENTITY REFLECTS THE NEW MARICO - SOLIDITY, FRESHNESS OF THINKING AND VITALITY OF SPIRIT.**

While Marico had moved with the times, its identity had not. The logo still reflected its industrial past, and not who Marico is today. The Company has therefore adopted a new logo to reflect its new identity, which is friendlier, more contemporary and more in keeping with the times.

The new identity is a natural progression for Marico, stylistically reflecting the nature of its

businesses and all that Marico stands for today: a consumer-friendly company that brings beauty and wellness to every home.

This is reflected in its lettering style, which is much softer. The trust mark (the symbol M) retains its basic strength - the pillars, symbolic of a company built on solidity and commitment, while the fresh green leaves bring to life Marico's focus on beauty and wellness.

The new identity thus reflects the new Marico - solidity, freshness of thinking and vitality of spirit.

## **TURNOVER GROWTH MOMENTUM TAKES MARICO BEYOND RS. 1000 CRORE**

### **A turnover landmark**

During Q4 FY05, Marico reached another milestone in its journey. The Marico Group turnover crossed the landmark of Rs. 1000 crore. The turnover for the full year, at Rs. 1013 crore, recorded a growth of 14% over the previous year. Profit before tax at Rs. 74.3 crore grew by 14% over FY04 and Profit after tax at Rs. 70.1 crore rose by 19%. We started 15 years ago in 1990 with 2 brands, a turnover of about Rs. 100 crore and a team of 200. Over a decade and a half, the Company has stayed focussed on building brands and gathering new insights in consumer preference. This has led it to grow its basket of brands to 12 through new launches and acquisitions, and move beyond products to solutions including services. Today a team of 1300 highly committed members manages its Rs. 1000 crore business. This journey has taken Marico beyond the shores of India to markets in Asia and other parts of the world, with manufacturing operations in Bangladesh; Kaya Skin Clinic offerings in Dubai, and the acquisition of a majority stake in a US based company - Sundari LLC.

All this has been managed along with consistent growth in profits and dividend, to reward

the shareholders. The Board of Marico Limited, at its meeting held on April 27, 2005, declared a fourth interim dividend of 17.5% on its equity share capital of Rs. 58 crore - a payout of 51% for the year. Q4 FY05 was the 17th consecutive quarter of dividend distribution.

## **CONSUMER PRODUCTS BUSINESS**

### **Sustained volume growth across categories**

Over the past few years, Marico has endeavoured to move up the value chain with consistent and derisked growth strategies. It has realigned its portfolio, enabling increased focus on high margin products and businesses. These now constitute 71% of Marico's total turnover, up from 66% last year. Sales of the low margin portfolio degrew 7% as resources and mind share were consciously focussed on high margin businesses. Brand building efforts too were directed towards the high margin portfolio - nearly 95% of the total advertising and sales promotion spends were allocated to this portfolio.

During FY05, volumes for Marico's Consumer Products business grew by 8% with the High Margin Portfolio growing by 16%.

### **Domestic FMCG Business**

On the back of its relaunch in FY04, the flagship brand Parachute grew by 8% in volume terms. Marico's Coconut Oil franchise now enjoys an all-India market share of over 50%. The Hair Care range (Parachute Jasmine, Shanti Amla, Mediker and Hair & Care being the key elements) grew by a strong 14% in volume and 19% in value terms. In the Premium Refined Oils market, the Saffola franchise clocked a record growth of 18% in volumes aided by healthy volumes in its blends, namely Saffola Tasty and Saffola Gold, which was launched in FY05. Sweekar, a non-focus brand, declined by 9% in volume. Revive, operating in the fabric care segment, held its volumes. In the

anti-lice market, Marico continued to be the only organized national player, with its offering of Mediker, in shampoo and oil formats. Parachute Sampoorna, Parachute Advansed, Silk-n-Shine and Saffola Gold were launched during the year and performed in line with expectations.

### **Stronger Flagships and growing portfolio of New Products and Prototypes**

Over the past few years, Marico has expanded its basket of new products and services across a broad range, while strengthening its flagships - Parachute and Saffola. This has been achieved while maintaining a record of several consecutive quarters of growth in financials, denoting a balance between caution and risk taking.

Marico's new product portfolio in the Consumer Products business - Silk-n-Shine, Parachute Sampoorna, Parachute Advansed and Saffola Gold in domestic and Parachute Cream, Parachute Gold and Beliphool in international - contributed a healthy 19% to the Consumer Products turnover.

A few 'brand stories' follow:

#### **Parachute**

Marico continues to hold its dominance in the Coconut Oil Category with Parachute, which was relaunched in Q4 FY04. The new packaging introduced in the second half of FY04 has been well received by consumers. During the year, the Company undertook micro-marketing initiatives in selected markets where there was a scope of increasing its market share. Despite strong competitive players both in the organized and unorganized sector, the overall volume market share



has moved above 50%. The total franchise (including flexi packs) marked a growth of 6% over the previous year.

#### **Saffola**

During the year, the Company launched Saffola Gold, a blend of refined kardi oil and refined ricebran oil. The brand franchise has successfully handled an important restructuring in recent times. From a single oil (safflower or kardi) that was offered under the Saffola brand till September 1999, it now has 3 variants: Saffola Refined Kardi (Safflower) Oil, Saffola Kardi Corn Tasty Blend and Saffola Gold. While launching the new variants and creating sub-brands, cannibalization within the Saffola franchise has been contained quite well. The franchise grew by a healthy 18% in volume terms during FY05. Saffola furthered its objective of creating awareness for health and heart care through a few specific initiatives - national roll out of Saffola, Dial-a-Dietician Service, and the launch of a new website [www.saffolalife.com](http://www.saffolalife.com)

Investments in the brand continued during the year. Saffola's brand building initiatives received a few accolades during FY05. Saffola advertising was rated amongst the best advertising for 2004-05 by ABBY. Saffola also won an award in the Food Category in the 1st FMCG Consumer Reaction Award 2005.

#### **Hair & Care**

Hair & Care was relaunched in Dec. '04 with a new formulation. It has been enriched with herbal proteins, extracted from neem and tulsi. This process has been developed and patented by Marico. The product has been repositioned as an expert on nonstickiness, with a claim of 'Upto 50% less sticky than other oils'. This relaunch is expected to strengthen Marico's hold over the Non-sticky Hair Oils segment.

### **Silk-n-Shine**

With Silk-n-Shine, Marico had entered yet another new segment in Hair Care - Hair Potion. It was successfully prototyped in Kolkatta last year and was nationally rolled out in Q2 FY05. Silk-n-Shine adopted an innovative strategy for branding



with its association with the popular programme 'Indian Idol' on Sony Entertainment Television. Through the programme, Silk-n-Shine achieved high visibility for the brand and innovatively showcased the effectiveness of the product. The brand has already captured significant market share (30%) of the post-wash hair conditioner market. In

February 2005, Marico introduced a small pack at a Rs. 25 price point. This pack is expected to break clutter at the retail level by making the category accessible to the mass market.

### **Parachute Sampoorna**

Parachute Sampoorna is a unique combination of Coconut Oil (for nourishment) with Almond Protein (for strength) and Hibiscus (for shine and lustre). After meeting the action standards of the prototype in Maharashtra, Sampoorna was scaled up nationally with strong above-the-line support. It has been



the pivot for driving growth for Hair Oils in the Value Added Coconut Oil category. The Parachute Sampoorna advertisement has been widely appreciated by consumers and media, as a refreshingly different campaign. At the Ad Review 2004

organised by Ad Club Mumbai, Sampoorna was chosen for the best evocative ad in the personal care / cosmetics category.

In the Value Added Coconut Oil (VACNO) category, Marico's brands comprising Parachute

Jasmine, Parachute Sampoorna and Parachute Advansed are now at the No.1 position, commanding 34% of the total market share.

### **Parachute Advansed**

Parachute Advansed, a 100% Coconut Hair Oil fortified with Coconut Milk Proteins, was launched nationally in June 2004. The brand seeks to leverage the goodness of coconut in nourishment of hair. The Company's extensive research shows that oiling hair with coconut oil before a wash with shampoo significantly lowers hair damage and loss of hair protein than when coconut oil is not applied. This is because coconut oil penetrates the hair shaft to a far greater extent than most other oils. This research has been leveraged by the Company to launch a campaign to make Parachute relevant to the young consumer by contexting it to shampoo. Apart from a television commercial campaign, the Company followed a 360 degree approach by addressing the consumer through radio, outdoor and on-ground activities such as the 'One-hour Chumpi Kiya Van Challenge', a programme called 'Hair Treats' to communicate the benefits of oiling through beauticians and sponsoring the Parachute Advansed Miss Kerala. These efforts are expected to lead to an increase in the market size.

### **Shanti Amla Badam**

Shanti Amla, Marico's offering in the Amla Hair Oil category, today enjoys a market share of 13%. It was initially launched on a platform of 'goodness of Amla at an amazingly affordable price'. In order to improve the value proposition, Marico has developed a variant of Shanti Amla - Amla Hair Oil reinforced with Badam. This value added product was prototyped in the state of Punjab and after meeting the action standards, has been rolled out nationally in April 2005.



### **Mediker Plus Anti Lice Oil**

In Q4 FY05, Marico expanded the Mediker product range with the introduction of Mediker Plus Anti-Lice Oil in the Southern Market. Mediker Plus has been launched with a strong benefit of One Hour - Lice Out, providing a perceptibly efficacious solution to the consumer.

The annualized turnover of the new products in the Consumer Products Business is now about Rs. 135 crore, contributing about 14% to the Consumer Products turnover.

### **New Prototypes**

To identify scalable marketing and product propositions, Marico follows the 'prototype' methodology, which allows the Company to test a few hypotheses on a low-cost, fail-fast model before any decision for scale up is taken. This approach has now stabilized. In addition to the prototypes of Parachute Sampoorna, Parachute Advanced and Silk-n-Shine, which were later launched during FY05, Marico is currently prototyping Parachute Advanced After Shower Cream and Saffola Daily Health Prototype in Mumbai.

### **International FMCG Business**

FY05 was yet another year of strong growth for Marico's international FMCG business. The sales turnover of international FMCG business grew by 29% to Rs. 96 crore over the FY04 base of Rs. 74 crore.

In Bangladesh, Parachute Coconut Oil consolidated its market leadership and crossed 50% market share in March '05. Parachute Cream continued to grow in the Gulf countries - volumes doubled during FY05. Parachute Sampoorna and Hair Tonic were two new products launched in the

Gulf markets. Marico has also achieved the One Star Export House Status.

The aggregate international business of Marico, comprising the FMCG business, Kaya in UAE and Sundari in the US now stands at Rs. 103 crore and thus contributes over 10% of the Group turnover.

### **ACQUISITION OF BRANDS BY MARICO BANGLADESH LTD.**

Marico Bangladesh Limited (MBL), the Bangladesh-based wholly owned subsidiary of Marico Limited, acquired the Toilet Soap brands 'Camelia' and 'Magnolia', from Marks and Allys Limited (MAL), another Bangladeshi Personal Care Products Company, in April 2005, for an undisclosed consideration. These brands have an aggregate turnover of about Taka 5.6 crore in toilet soaps in Bangladesh. They are also present in a minor manner, through extensions across talcum powder, petroleum jelly and amla hair oil. Camelia's brand equity owes its strength to the quality of the soap, primarily its fragrance, which has a strong recall amongst consumers.

The acquisition envisages Marico outsourcing the manufacture of the soaps to MAL, while continuing to draw on MAL's research and development. It also involves a suitable non-compete covenant by MAL.

Marico believes that this acquisition will help the Group to develop a broader Personal Care franchise amongst the Bangladeshi consumers, who have already made Parachute a market leader with 51% share in the Coconut Oil category. It will also help MBL to further strengthen its distribution network, which, at about 2.6 lac outlets, is already amongst the widest in Bangladesh.

## COST STRUCTURE FOR THE CONSUMER PRODUCTS BUSINESS

| % to Sales & Services (net of excise) | FY05 | FY04 |
|---------------------------------------|------|------|
| Material Cost (Raw + Packaging)       | 62.4 | 64.6 |
| Advertising & Sales Promotion (ASP)   | 9.7  | 8.2  |
| Personnel Costs                       | 4.3  | 4.8  |
| Depreciation                          | 1.2  | 1.3  |
| Other Expenses                        | 13.8 | 13.0 |
| Operating Costs                       | 91.4 | 91.9 |
| Net Operating Margin ( PBIT)          | 8.6  | 8.1  |
| PBDIT margins                         | 9.8  | 9.4  |
| Gross Margins ( PBDIT before ASP)     | 19.5 | 17.6 |
| Operating ROCE (%)                    | 42.5 | 40.9 |

### Notes:

1) Margins have been computed without including 'Other Income', major components of which are lease rental Rs. 0.56 cr. (previous year Rs. 0.5 cr.), exchange rate difference loss Rs. 0.23 cr. (previous year gain Rs. 0.1 cr), profit on sale of investment Rs. 0.35 cr. (previous year loss Rs. 0.1 cr.) and dividend income Rs. 0.44 cr. (previous year Rs. 1.3 cr.)

2) Advertising and Sales Promotion (ASP) has shown a significant increase of 32% in FY05 as compared to FY04, owing largely to increased spends on new products (65%) and increased investment in flagship brands. Also Marico continues to follow a contrarian strategy of focusing more on the advertisement (A) part of ASP (about 80% as compared to the industry number of only around 60%), as compared to the Sales Promotion (SP) part. We believe that focusing on demand creation in a consumer-centric manner is more important than 'buying sales' through consumer offers. Our ASP has therefore always comprised a judicious mix of both, A & SP.

3) Marico prices its products based on the value it provides to the consumer, targeting a certain margin per unit of volume. Therefore, Marico's operating margins are reasonably insulated from commodity price fluctuations, although commodity prices can influence turnover value for Marico. Therefore, instead of analyzing operating margins as a percentage of sales, it may be more logical to analyze operating ROCE.

4) The Consumer Products business comprises operations in India (Marico Ltd.) and Bangladesh (Marico Bangladesh Ltd, along with its subsidiary - MBL Industries Limited). Skin Care Services and Global Ayurvedics are still evolving; hence their cost structures have not been discussed here, as these may not yet be capable of meaningful analysis and projection.

### VALUE ADDED TAX (VAT)

VAT is finally being implemented in 21 states across the nation. This has been a major sales tax reform initiative since Independence and the trader community is still to come to terms with this new reality. As a result, VAT has evoked a mixed response, with traders in a few states going on day strikes. The matter is however expected to stabilise over the next couple of months as the benefits of VAT become clearer. Marico's turnover in the first quarter of FY06, like all other industry players, is likely to be impacted by the uncertainty caused by VAT. The Company expects the sales to be impacted to the tune of 10-15% in April. Marico is however watching the market responses closely to ensure that the demand is not affected and that the supplies to the market are smooth.

### CAPITAL UTILISATION

Over the years, Marico has been maintaining its Return on Capital Employed (ROCE) at levels above 30%. FY05 was no exception. Given below is a snapshot of various capital efficiency ratios for Marico:

| Ratio                                      | FY05 | FY04 |
|--|------|------|
| Return on Capital Employed                 |      |      |
| • Marico Group                             | 32%  | 33%  |
| • Consumer Products                        | 38%  | 38%  |
| Return on Net Worth (Group)                | 35%  | 34%  |
| Working Capital Ratios (Consumer Products) |      |      |
| • Debtors Turnover (Days)                  | 13   | 13   |
| • Inventory Turnover (Days)                | 39   | 39   |
| • Net Working Capital Turnover (Days)      | 38   | 33   |
| Economic Value Added (Group)               |      |      |
| • Rs. Crore                                | 48   | 38   |
| • % to Capital Employed                    | 21%  | 18%  |
| Debt: Equity (Group)                       | 0.16 | 0.06 |
| Finance Costs to Turnover (%) (Group)      | 0.2% | 0.1% |

**Balance Sheet for the Consumer Products Business Rs. Crore**

|                               | March 31,<br>2005 | March 31,<br>2004 |
|-------------------------------|-------------------|-------------------|
| <b>SOURCES OF FUNDS</b>       |                   |                   |
| Shareholders' Funds           | 236.1             | 191.9             |
| Borrowings                    | 43.7              | 9.4               |
| Deferred Income Tax Provision | 6.0               | 6.2               |
| <b>TOTAL</b>                  | <b>285.8</b>      | <b>207.5</b>      |
| <b>APPLICATION OF FUNDS</b>   |                   |                   |
| <b>Deployed in Business</b>   |                   |                   |
| Net Fixed Assets              | 93.6              | 91.1              |
| Investments                   | 28.2              | 13.0              |
| Current Assets                | 238.4             | 187.3             |
| Less: Current Liabilities     | 117.6             | 100.2             |
| Net Working Capital           | 120.8             | 87.1              |
| Operating Capital Employed    | 242.6             | 191.2             |
| <b>Financial Assets</b>       | <b>43.2</b>       | <b>16.3</b>       |
| <b>TOTAL</b>                  | <b>285.8</b>      | <b>207.5</b>      |

**NEW BUSINESSES - KAYA SKIN CARE**

The Indian Skin Care solutions business is growing fast with increased awareness and demand for cosmetic enhancement. With advancement in medical technology, safe and effective procedures are available that enhance the look and feel of the skin. Kaya Skin Clinic attempts to fill the existing need gap in the Skin Care solutions business in India. It offers scientific, unisex dermatological procedures using US FDA approved technology.

'Kaya' marked Marico's entry into the skin care solutions business. It attempted to leverage Marico's strengths in the Personal Care business and an in-depth understanding of the needs of the Indian consumer and her/his desire to enhance her/his natural beauty with the best cosmetic dermatology procedures available internationally.

The Kaya concept has been well received by the target consumers. In just over 2 years, Kaya has grown into a 34-clinic strong skin care chain - across 11 cities in India and UAE.

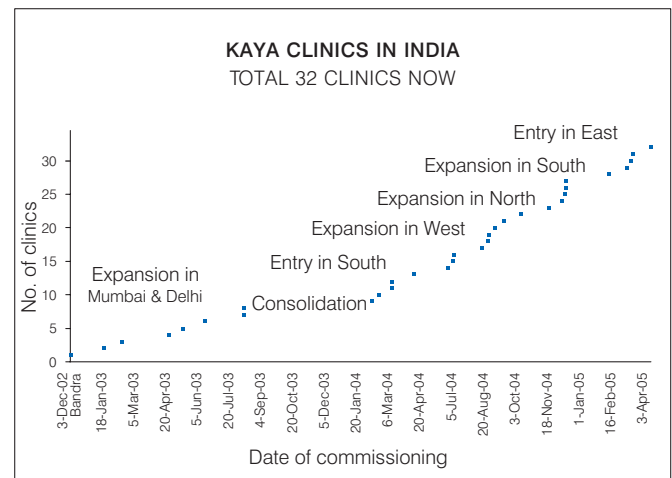
It seeks to create a differentiation as a

corporate service provider - offering a safe, efficacious and credible Skin Care Services range at multiple locations. This would be in contrast with the large number of small 'singular' clinics currently present in this segment.

Kaya targets high-end customers in SEC A1 and A2 with an age group of 16-60 years across metros and mini metros in the country. The objective is to provide result-oriented, personalized, non-surgical skin solutions in a serene Zen like environment.

All services at Kaya begin with a 'skinscription' - an in-depth analysis of a client's skin and a treatment plan customized to each skin type prescribed by a Kaya Skin Advisory (KSA) certified dermatologist. The treatments available include services segregated into three distinct categories - Enhancement services, Problem-Solution services and Anti-aging services.

All the services offered at Kaya Skin Clinic are designed and supervised by a distributed team of over 90 dermatologists, and carried out by certified skin practitioners, each with more than 300 hours of training.



As part of a complete solution set, Kaya has launched a range of skincare products, which are the result of extensive skin-care research in derma-cosmetic laboratories based in France, UK

& USA. These are not only used during the skin care services but are also available for post service usage as a follow up to the service undertaken at the clinic. All Kaya Skin Clinic Products are dermatologically tested and approved for Indian Skin by the Kaya Skin Advisory. The key products are Skin Lightening Complex, Lighten and Smooth Under-eye gel, Daily Moisturizing Sunscreen and Recharging Night Crème.

The base clientele at Kaya has now gone beyond 40,000 - 97% of Kaya's clientele rate Kaya's services between good and excellent. The financial model has also started showing results with the operational break even of each clinic being reached within 6 to 9 months of operation. The capital expenditure for a typical clinic ranges from Rs. 1 crore to Rs. 1.5 crore, the annual turnover potential being in a similar ballpark.

Marico's entry in the Skin Care Services business was also driven by the opportunity to be the first mover in yet another category, leveraging the access that Marico has to advancements in medical technology, which offer revolutionary products and deliver superior results. The Kaya Skin Clinics have filled the vacant space of providing high quality, credible and safe cosmetic dermatology based skin care and would gain from being the first mover. They also fit in with Marico's philosophy of aiming to provide solutions suitable to Indian consumers - we have taken additional care to ensure that the machines are suitable to Indian skin.

During FY05, the Kaya business reached a turnover of Rs. 20.9 crore, of which Rs. 8.4 crore was attained in the fourth quarter. On an annualised basis, Kaya's turnover based on current clinic build up would be about Rs. 30-35 crore. As the business continued to be in the investment phase, the loss for the year was Rs. 7.9 crore.

## **NEW BUSINESSES - SUNDARI**

For FY05, Sundari reached a turnover of Rs. 5.5 crore and the loss before tax was at Rs. 5.3 crore.

Marico acquired a controlling stake in Sundari LLC in Q4 FY03. Over the last two years, it has worked upon the model. Sundari has adopted the strategy of identifying big prospective spa clients in order to create an opportunity to convert a good proportion of these prospects into business. The spa products market is estimated to be about US\$ 2 billion in the USA. Sundari can find a niche in this market, positioning itself as an ayurvedic skincare brand. The Spa opportunity has a lag time of 6 to 9 months from the time a prospect is approached till the time an order is bagged. Sundari would thus continue to be in the investment phase. During the year, Sundari acquired some prestigious accounts such as Marriott (the spa at Camelback Inn, Star Pass and Desert Ridge), Canyon Ranch - Lennox, Ritz Carlton, Abhasa Spa - Waikiki in the USA and Four Seasons - Maldives & Langkawi, Westin - Bangkok, The Oberoi - Mauritius, Legian - Bali in Asia, among others.

There has also been a focussed effort in the area of cost management. This would help improve product margins and in the process bring down the pressure on the overall bottom line. Sundari has also been concentrating on new products development. In the recent past Sundari has been able to roll out 5 new products in the US market.

Some of the likely growth drivers for Sundari are:

- Entry into big accounts in the spa channel - especially destination spas.
- Quick scale up in the international business through full service distributors in the Asian markets.
- New product development so that Sundari

can address customer needs especially in destination spas.

- Enhancing the Sundari experience, through uniquely developed protocols for administration in spas.

Overall, the strategy for growth appears to be in place for the Sundari business.

## **SHAREHOLDER VALUE RELATED POLICIES & PRACTICES**

### **Payout - Distribution of profits to shareholders**

Marico's distribution policy, which aims at sharing Marico's prosperity with its shareholders, through a formal earmarking / disbursement of profits to shareholders, has, in the recent past, been characterized by the following:

- Payout increasing from year to year and, to the extent feasible, also from quarter to quarter in a year.
- Regular dividend - every quarter reflecting the confidence to sustain continuous distribution.
- Innovation through use of special instruments as and when feasible.
- Use of distribution to increase liquidity on the Stock Exchanges.

Marico's cash profits have continued to grow and provide a logical support to its practice of declaring a dividend every quarter. Marico will continue with its policy of declaring multiple dividends every year, while continuously identifying innovative means of rewarding its shareholders. The endeavor will be to keep a high payout - about 50%, subject to financial requirements of its business.

## **CHANGES IN THE BOARD OF DIRECTORS**

Mr. Kishore Mariwala, Director of the Company since its inception, has stepped down, upon completing 70 years of age earlier this year. In the vacancy caused by his resignation, the Board has appointed Mr. Rajen Mariwala, as a

Director. Rajen, 42, holds a degree in Masters in Chemical Engineering (M. Chem. Engg.) from Cornell University, USA, Ithaca, New York following a degree in Bachelor of Chemical Engineering (B.Tech Chem. Engg.) from A. C. College of Technology, Anna University, Chennai. He is the Managing Director of Hindustan Polyamides & Fibres Ltd. (HPFL), a leading exporter of speciality chemicals, primarily those used for fragrances and personal care products. With a turnover of about Rs. 80 crore, HPFL exports more than 90% of its products all over the globe - its client list covers most of the ten largest manufacturers of fragrance compounds globally. Rajen is a member of the Young Presidents Organization and an active member of The Indian Chemical Manufacturers Association.

## **OUTLOOK**

Sustainable profitable growth has been the pivot around which Marico's strategies have evolved. FY05 saw Marico reach two important milestones in this journey:

- Group Turnover reaching the Rs. 1000 crore mark and
- International Business Turnover reaching the Rs. 100 crore mark

The next phase of Marico's growth journey will build on this and will be centered on the following:

- Continued Investment in new products, creating a pipeline of new product ideas through prototypes in India and abroad.
- Realigning the portfolio towards higher value add.
- Accelerating, judiciously, the entrepreneurial foray into services through Kaya Skin Clinics.

## **On behalf of the Board of Directors**

### **Harsh Mariwala**

Chairman & Managing Director

Place: Mumbai

Date: April 27, 2005