



Colgate Palmolive

STOCK INFO.	BLOOMBERG
BSE SENSEX: 14,078	CLGT IN
	REUTERS CODE
S&P CNX: 4,151	COLG.BO

3 May 2007

Neutral

Previous Recommendation: Neutral

Rs352

Equity Shares (m)	136.0
52-Week Range (Rs)	464/273
1,6,12 Rel. Perf. (%)	-5/-24/-37
M.Cap. (Rs b)	47.8
M.Cap. (US\$ B)	1.2

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
03/07A	12,951	1,854	13.6	19.8	25.8	26.9	84.8	83.4	3.6	22.0
03/08E	14,833	2,073	15.2	11.8	23.1	25.0	112.2	109.9	3.1	19.2
03/09E	16,744	2,442	18.0	17.8	19.6	23.1	122.6	120.2	2.7	16.1

- Colgate's 4QFY07 results are in line with our estimates. Net sales were Rs3.43b (against our estimate of Rs3.37b) and PAT was Rs498m (against our estimate of Rs491m).
- Gross margins declined 40bp to 55.2% while EBITDA margins expanded 260bp to 15.6%, as advertising costs declined 100bp to 18.6% of sales. PBT grew 3.4% YoY to Rs670m due to 51% jump in other income. Service income for IT services accounted for most of the increase in other income.
- Toothpaste volumes grew by a strong 9-10% for FY07, while toothbrush volumes grew by 21.5%. Toothpowder volumes grew by 5% in FY07. Going forward, the company has given a cautious outlook, with expected volume growth at 10%. Long-term growth potential seems intact but short-term growth variations due to uncertain macroeconomic conditions cannot be ruled out.
- The company has announced capital restructuring, whereby the face value of each share would be reduced to Rs1 and Rs9 would be paid back to the shareholders as deemed dividend. This would reduce surplus cash and boost the return ratios. We expect the reduction in surplus cash to reduce financial other income. Colgate has proposed Rs2 as special dividend, which along with Rs9 as deemed dividend from capital restructuring would provide 3.1% yield in the short term.
- We are reducing our EPS estimates from Rs15.8 to Rs15.2 for FY08 and from Rs18.8 to Rs18 for FY09 primarily due to decline in other income due to capital restructuring. The stock is quoting at 23.1x FY08E and 19.6x FY09E earnings. We maintain **Neutral**.

QUARTERLY PERFORMANCE

(Rs Million)

Y/E MARCH	FY06				FY07				FY06	FY07
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q		
Net Sales	2,583	2,781	2,857	3,021	3,096	3,200	3,223	3,433	11,242	12,951
YoY Change (%)	6.4	13.2	21.2	25.8	19.9	15.1	12.8	13.6	16.6	15.2
Total Exp	-2,201	-2,396	-2,203	-2,629	-2,695	-2,642	-2,679	-2,897	-9,387	-10,846
EBITDA	382	385	654	392	401	558	544	536	1,855	2,106
Margins (%)	14.8	13.9	22.9	13.0	12.9	17.4	16.9	15.6	16.5	16.3
Depreciation	-26	-39	-47	-37	-37	-36	-44	-37	-260	-153
Interest	-2	-1	-1	-2	-2	-2	-3	-3	-6	-10
Other Income	140	98	109	115	148	122	166	174	461	525
PBT	494	443	715	467	509	643	664	670	2,050	2,468
Tax	-140	-134	-132	-97	-149	-137	-161	-172	-503	-614
Rate (%)	28.2	30.2	18.5	20.8	29.2	21.4	24.2	25.6	24.5	24.9
Adjusted PAT	355	309	583	370	361	505	503	498	1,548	1,854
YoY Change (%)	39.2	14.5	68.7	10.6	1.6	63.7	-13.6	34.6	28.5	19.8
Extraordinary Expenses	-75	0	-165	0	0	-274	0	8	-172	-252
Reported PAT	280	309	417	370	361	232	503	506	1,376	1,602
YoY Change (%)	9.8	14.5	46.2	14.4	28.9	-24.9	20.6	36.7	173.3	16.4

E: MOST Estimates

Steady volume growth in toothpastes, toothpowder reports poor volume growth

Colgate reported double-digit volume growth, with toothpaste volume growing by 10% in FY07. During 4QFY07, the company launched *Colgate Max Fresh Citrus Blast* in 40gm, 80gm and 140gm packs. New launches like *Max Fresh Gel*, *Whitening* and *Active Salt* contributed 10% of total volumes. Toothbrushes also reported strong volume growth of 21.5%. However, toothpowder reported a poor show with 5% volume growth for FY07. The outlook on toothpowder continues to be poor, as upgradation to toothpastes continues. We expect 14.5% growth in net revenues for FY08 to Rs14.8b and 12.9% growth for FY09 to Rs16.7b. Fiscal benefits will drive value growth, as the company has expanded the production facility at Baddi to 40,000 ton and full capacity utilization is expected in 4QFY08.

Market share gains

The toothpaste category reported broad-based growth, with all the major brands and past year launches like *Colgate Advanced Whitening*, *Colgate Active Salt* and *Colgate MaxFresh Gel* reporting steady growth. The company has not only been maintaining its dominance but gaining market share at the cost of its competitors.

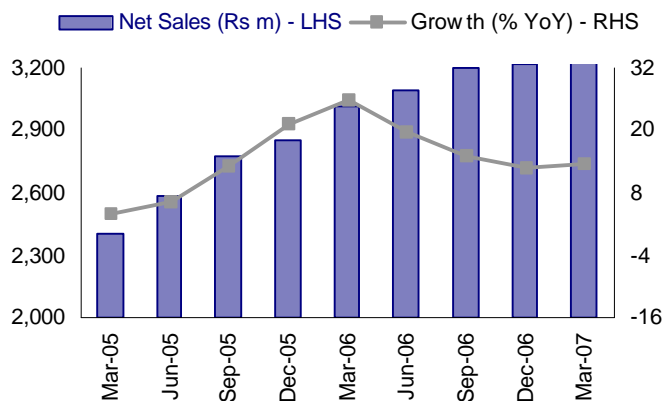
COLGATE: GAINING MARKET SHARE IN TOOTHPASTES (%)

	JAN-MARCH'06	JAN-MARCH '07
Colgate	47.0	48.2
HLL	30.4	30.0

Source: Company/Motilal Oswal Securities

For the industry, the popular segment grew by 20%, while the premium segment grew by 10%. Long-term demand potential remains intact, with product penetration being around 51%. The demand potential is huge as per capita usage in china and Malaysia is 2.5-3 times that of India. In addition, only 7% of the population in India has the habit of brushing teeth twice, indicating long-term demand growth potential.

TREND IN SALES GROWTH

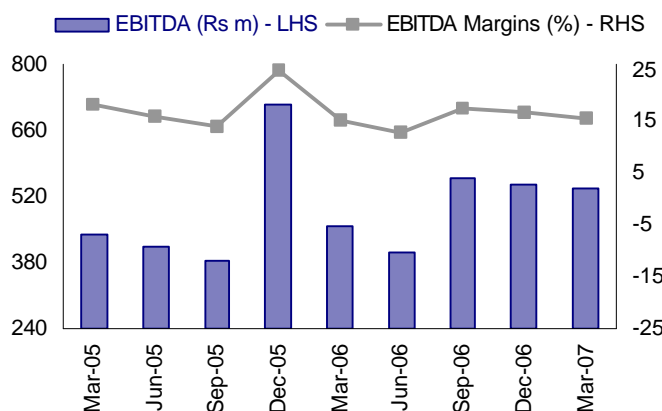


Source: Company/Motilal Oswal Securities

Decline in advertising cost boosts EBITDA margins

Colgate's gross margins were down 40bp at 55.2% in 4QFY07 due to increase in raw material and procurement costs. However, EBITDA margins increased by 260bp as advertising expenses declined from 19.7% to 18.6% in 4QFY07. For the full year, advertising expenses stood at 16% of sales. Advertising spend of Colgate has been lumpy in the past due to various launches and activation programs from time to time. Management expects medium-term advertising spend to stabilize at around 15%.

TREND IN EBITDA MARGINS



Source: Company/Motilal Oswal Securities

Other income to be lower, Sewri facility benefits not quantified

Colgate has announced capital restructuring, whereby the face value of each share would be reduced to Rs1 and Rs9 would be paid back to shareholders as deemed dividend. It will reduce surplus cash and boost return ratios. We expect the reduction in surplus cash to reduce financial other income. The management has indicated that the land of the Sewri unit is on lease from Bombay Port Trust and so cannot be sold off. Colgate has 80,000 sq ft of building space, which is likely to be put to alternate use or given on rent. Our estimates do not factor in any benefit of this

arrangement. The management has indicated very small overheads in maintaining the facility, which would not impact the reported profits.

Valuation and view

We expect overall volumes to grow at 10% due to mid-single-digit volume growth in the toothpowder segment. We are reducing our EPS estimates from Rs15.8 to Rs15.2 for FY08 and from Rs18.8 to Rs18 for FY09 primarily due to decline in other income due to capital restructuring. The stock is quoting at 23.1x FY08E and 19.6x FY09E earnings. We maintain **Neutral**.

Colgate Palmolive: an investment profile

Company description

Colgate is a market leader in the toothpaste segment with a market share of 50%. With the relaunch of Cibaca Top in early CY04 the company has captured 38% of low price segment. Oral care is one of the most underpenetrated segments of the FMCG market with a penetration of 32%. Colgate has invested Rs700m in a toothpaste facility at Baddi in Himachal Pradesh which will accrue fiscal benefits.

Key investment arguments

- ☞ Colgate has regained its leadership position in the oral care market. In FY05, it grew 14% in volumes compared to 9% industry growth.
- ☞ Pricing environment has improved as is evident by the latest price hikes. This would aid margin improvement.

Key investment risks

- ☞ P&G's entry in the oral care market with its Crest brand, at a lower price point than Colgate.
- ☞ Higher input cost prices could affect margins.

COMPARATIVE VALUATIONS

		COLGATE	HLL	NESTLE
P/E (x)	FY08E	23.1	25.5	25.4
	FY09E	19.6	22.5	20.7
EV/EBITDA (x)	FY08E	19.2	22.6	16.0
	FY09E	16.1	19.5	13.1
EV/Sales (x)	FY08E	3.1	2.9	3.0
	FY09E	2.7	2.7	2.6
P/BV (x)	FY08E	25.0	15.4	13.9
	FY09E	23.1	14.8	12.4

SHAREHOLDING PATTERN (%)

	MAR.07	DEC.06	MAR.06
Promoter	51.0	51.0	51.0
Domestic Inst	9.9	10.6	10.6
Foreign	12.1	11.7	10.3
Others	27.0	26.8	28.1

Recent developments

- ☞ Colgate has introduced *Colgate MaxFresh Citrus Blast* in three sizes – 40gm, 80gm and 140gm.
- ☞ The company has expanded the production facility at Baddi to 40,000 ton and full capacity utilization is expected by the end of 4QFY08.
- ☞ The company has announced capital reduction by paying off Rs9 from the face value as deemed dividend to the shareholders.

Valuation and view

- ☞ We have an EPS forecast of Rs15.2 for FY08 and Rs18 for FY09.
- ☞ The stock is trading at 23.1x FY08E EPS and 19.6x FY09E EPS. We maintain **Neutral** rating on the stock.

Sector view

- ☞ We have a cautious view on the sector, given the inflationary tendency in the economy, which could impact volumes as well as profit margins of companies.
- ☞ Companies with low competitive pressures and broad product portfolios will be able to better withstand any slowdown in a particular segment.
- ☞ Longer term prospects bright, given rising incomes and low penetration.

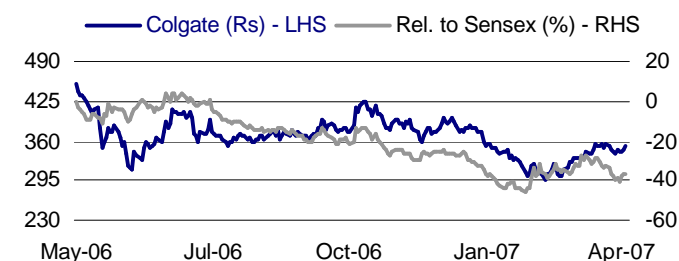
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY08	15.2	16.5	-7.7
FY09	18.0	19.5	-7.8

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
352	-	-	Neutral

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT		(RS MILLION)				
Y/E MARCH	2005	2006	2007E	2008E	2009E	
Net Sales	9,642	11,242	12,951	14,833	16,744	
Change (%)	2.7	16.6	15.2	14.5	12.9	
Total Expenditure	-7,968	-9,387	-10,846	-12,434	-13,901	
EBITDA	1,674	1,855	2,106	2,400	2,843	
Change (%)	14.4	10.8	13.5	14.0	18.5	
Margin (%)	17.4	16.5	16.3	16.2	17.0	
Depreciation	-224	-260	-153	-191	-205	
Int. and Fin. Charges	-12	-6	-10	-6	-6	
Other Income	342	290	525	610	681	
Profit before Taxes	1,781	1,879	2,468	2,813	3,314	
Change (%)	17.6	5.5	31.4	14.0	17.8	
Margin (%)	18.5	16.7	19.1	19.0	19.8	
Tax	-700	-529	-782	-777	-912	
Deferred Tax	52	26	167	37	44	
Tax Rate (%)	-36.4	-26.8	-24.9	-26.3	-26.2	
Adjusted PAT	1,124	1,548	1,854	2,073	2,442	
Change (%)	4.1	37.7	19.8	11.8	17.8	
Margin (%)	11.7	13.8	14.3	14.0	14.6	
Reported PAT	1,133	1,376	1,602	2,073	2,442	

BALANCE SHEET		(RS MILLION)				
Y/E MARCH	2005	2006	2007E	2008E	2009E	
Share Capital	1,360	1,360	136	136	136	
Reserves	1,138	1,351	1,646	1,778	1,935	
Net Worth	2,498	2,711	1,782	1,914	2,071	
Loans	40	44	44	44	44	
Deferred Liability	-86	-76	-106	-143	-187	
Capital Employed	2,452	2,678	1,719	1,815	1,928	
Gross Block	3,244	4,035	4,415	4,765	5,115	
Less: Accum. Depn.	-2,447	-2,435	-2,598	-2,789	-2,994	
Net Fixed Assets	797	1,600	1,817	1,976	2,122	
Capital WIP	675	91	91	91	91	
Investments	1,608	1,483	1,100	1,527	1,900	
Curr. Assets, L&A	2,493	3,014	2,781	2,831	2,903	
Inventory	745	744	876	968	1,026	
Account Receivables	174	74	110	125	141	
Cash and Bank Balance	561	879	445	352	312	
Others	1,014	1,317	1,351	1,386	1,423	
Curr. Liab. and Prov.	3,122	3,511	4,070	4,610	5,088	
Account Payables	2,024	2,425	3,176	3,666	4,092	
Other Liabilities	126	399	163	168	174	
Provisions	971	687	732	776	822	
Net Current Assets	-628	-497	-1,289	-1,779	-2,185	
Application of Funds	2,452	2,678	1,719	1,815	1,928	

E: MOST Estimates

RATIOS		2005	2006	2007E	2008E	2009E
Basic (Rs)						
EPS		8.3	11.4	13.6	15.2	18.0
Cash EPS		9.9	13.3	14.8	16.6	19.5
BV/Share		18.4	19.9	13.1	14.1	15.2
DPS		7.0	7.5	9.5	12.2	14.4
Payout %		84.7	65.9	70.0	80.0	80.0
Valuation (x)						
P/E			30.9	25.8	23.1	19.6
Cash P/E			26.5	23.8	21.1	18.1
EV/Sales			4.0	3.6	3.1	2.7
EV/EBITDA			24.5	22.0	19.2	16.1
P/BV			17.6	26.9	25.0	23.1
Dividend Yield (%)			2.1	2.7	3.5	4.1
Return Ratios (%)						
RoE		37.3	59.4	84.8	112.2	122.6
RoCE		45.2	58.6	83.4	109.9	120.2
Working Capital Ratios						
Debtor (Days)		6	2	3	3	3
Asset Turnover (x)		57.0	10.2	24.5	75.3	-265.2
Leverage Ratio						
Debt/Equity (x)		0.0	0.0	0.0	0.0	0.0

CASH FLOW STATEMENT		(RS MILLION)				
Y/E MARCH	2005	2006	2007E	2008E	2009E	
OP/(loss) before Tax	1,506	1,909	2,344	2,634	3,105	
Int./Div. Received	278	147	164	185	215	
Interest Paid	12	6	6	6	6	
Direct Taxes Paid	-700	-469	-568	-703	-828	
(Incr)/Decr in WC	-278	-186	-358	-397	-366	
CF from Operations	817	1,407	1,588	1,724	2,132	
(Incr)/Decr in FA	-751	-197	-410	-387	-394	
(Pur)/Sale of Investments	-449	124	383	-427	-373	
CF from Invest.	-1,200	-73	-27	-814	-766	
Issue of Shares	0	0	-1,224	0	0	
(Incr)/Decr in Debt	-17	-4	0	0	0	
Dividend Paid	-1,078	-1,163	-1,335	-1,940	-2,286	
Others	759	151	564	937	881	
CF from Fin. Activity	-336	-1,016	-1,995	-1,003	-1,405	
Incr/Decr of Cash	-719	318	-434	-93	-40	
Add: Opening Balance	1,280	561	879	445	352	
Closing Balance	561	880	446	352	312	



For more copies or other information, contact

Institutional: Navin Agarwal. **Retail:** Manish Shah

Phone: (91-22) 39825500 Fax: (91-22) 22885038. E-mail: inquire@motiloswal.com

Motilal Oswal Securities Ltd, 3rd Floor, Hoechst House, Nariman Point, Mumbai 400 021

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Colgate Palmolive

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|---|----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
| 4. Investment Banking relationship with company covered | No |

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