

**RESULTS FIRST LOOK**

Colgate-Palmolive Q2FY12 results were marginally below our estimates. As expected advertising spends continue to move up, signaling heightened competitive activity in the HPC space. While topline growth was strong, pressure on margins was more than our expectations. We continue to believe A&P levels will continue to put pressure on margins near term. Maintain our cautious view on the stock at these levels.

Price target: 750.0 INR

Price (28 Oct 2011): 996.75 INR

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**Q2FY12 results hit by high A&P costs**

- Earnings vs. our Forecast: **BELOW**

**Likely Impact:**

- Earnings Estimates: **NO CHANGE**

- Dividend Estimates: **NO CHANGE**

- Price Target: **NO CHANGE**

- Long-term View: **CONFIRMED**

**Key highlights from Colgate Q2 FY12 results:**

- Net sales for the quarter were +18.7% to INR 6.75bn vs. our estimate of INR 6.5bn. Other operating income was at Rs. 183mn during the quarter vs. our estimate of Rs. 193mn.
  - Consolidated volume growth stood at 13% for the quarter.
  - Market share in toothpaste category stood at 52.6% for the quarter.
- As expected, material costs (primarily sorbitol) continue to remain at elevated levels and have not seen any declines on a q-q basis. The company attributes the flat gross margins to "prudent price increases and cost management". This is a trend which is expected to continue.
- A&P costs during the quarter were 16.9% of sales significantly higher than our estimate. As we have said in the past competitive intensity in the category is likely to remain strong, which means the high level of A&P spends may continue to hold back EBITDA growth in medium term. Company has also invested in brand support for new product launches such as Colgate Sensitive Pro Relief, which is likely to continue in the next couple of quarters.
- EBITDA came in at Rs. 1.39bn, 2% below our estimate of Rs. 1.42bn. EBITDA margins were 20.6% vs. our estimate of 21.8% mainly due to 45% rise in A&P expenses on y-y basis.
- PAT at INR997 was about 10% lower than our expectations but this was impacted by one off expense relating to the closing down of the toothpowder factory at Hyderabad. Company booked INR. 82.2mn in costs relating to employee severance during the quarter. Adjusted for this, PAT came in 3% below our expectations.

**Figure 1 – Colgate Q2FY11 results headline numbers**

| (Rs. mn)     | Quarter ended |        |       |        |        |
|--------------|---------------|--------|-------|--------|--------|
|              | Sep-11        | Sep-10 | % Chg | Jun-11 | % Chg  |
| Net Sales    | 6,755         | 5,693  | 18.7  | 6,294  | 7.3    |
| EBIDTA       | 1,390         | 1,297  | 7.2   | 1,356  | 2.5    |
| Other income | 95            | 81     | 16.8  | 120    | (21.0) |
| PBIDT        | 1,485         | 1,378  | 7.8   | 1,475  | 0.6    |
| Depreciation | 106           | 84     | 25.8  | 88     | 20.1   |

|                               |              |              |              |              |              |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| Interest                      | 8            | 6            | 23.0         | 6            | 23.0         |
| <b>PBT</b>                    | <b>1,372</b> | <b>1,288</b> | <b>6.5</b>   | <b>1,381</b> | <b>(0.7)</b> |
| Tax                           | 293          | 285          | 2.8          | 377          | (22.4)       |
| <b>Adjusted PAT</b>           | <b>1,079</b> | <b>1,003</b> | <b>7.6</b>   | <b>1,004</b> | <b>7.4</b>   |
| Extra ordinary income/ (exp.) | (82)         | 0            | N.A          | 0            | N.A          |
| <b>Reported PAT</b>           | <b>997</b>   | <b>1,003</b> | <b>(0.6)</b> | <b>1,004</b> | <b>(0.8)</b> |
| <b>No. of shares (mn)</b>     | <b>136</b>   | <b>136</b>   |              | <b>136</b>   |              |
| EBIDTA margins (%)            | 20.6         | 22.8         |              | 21.5         |              |
| PBIDT margins (%)             | 22.0         | 24.2         |              | 23.4         |              |
| <b>EPS(INR)</b>               | <b>7.9</b>   | <b>7.4</b>   |              | <b>7.4</b>   |              |

Source: Company, Nomura Research

Q2 results indicate continuing headwinds facing the company over the next few quarters. We do not see category dynamics changing in the near term which will mean margins will continue to remain under pressure.

With valuations close to 30x FY12, we continue to maintain our Reduce rating on the stock.

**Valuation Methodology and Investment Risks:** Colgate-Palmolive – We value Colgate-Palmolive at 22x one year forward earnings estimates of Rs. 33. Investment risks: Colgate, relative to its size, is the biggest spender on advertising and promotion in the Indian consumer sector. The company spends around 16% of sales on A&P, compared with the sector average of 12%. Any cuts in A&P expenses may pose an upside risk to our earnings estimates

Note: Ratings and Price Targets are as of the date of the most recently published report (<http://go.nomuranow.com/research/globalresearchportal>) rather than the date of this email.

Results First Look is the analyst's preliminary interpretation of the results announcement. Our recommendation and earnings estimates are not being changed in this report. Any formal changes to our recommendation or earnings estimates will be made in a subsequent report, which may differ from the preliminary views expressed in this report.

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| Issuer name               | Ticker  | Price      | Price date  | Stock rating | Disclosures |
|---------------------------|---------|------------|-------------|--------------|-------------|
| Colgate-Palmolive (India) | CLGT IN | 996.75 INR | 28 Oct 2011 | Reduce       | 123         |

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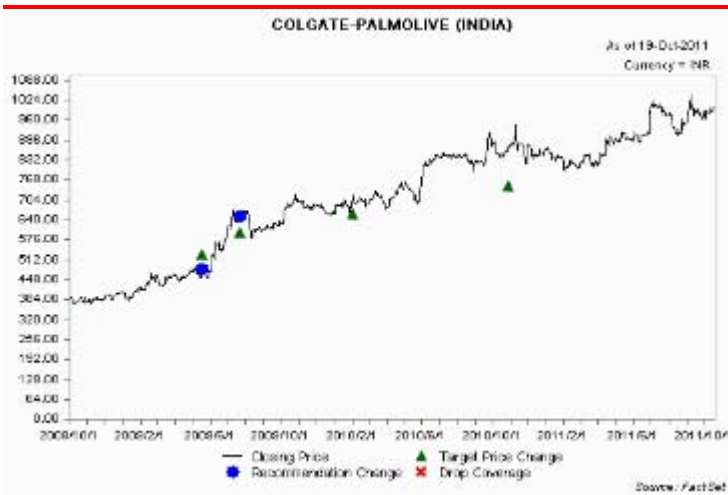
123 **Market Maker - NSI**  
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| Issuer name               | Previous Rating | Date of change |
|---------------------------|-----------------|----------------|
| Colgate-Palmolive (India) | Buy             | 23 Jul 2009    |

**Colgate-Palmolive (India) (CLGT IN)** 996.75 INR (28 Oct 2011) Reduce

Rating and target price chart (three year history)



For explanation of ratings refer to the stock rating keys located after chart(s)

**Valuation Methodology** We value Colgate-Palmolive at 22x one year forward earnings estimates of Rs. 33.5

**Risks that may impede the achievement of the target price** Colgate, relative to its size, is the biggest spender on advertising and promotion in the Indian consumer sector. The company spends around 16% of sales on A&P, compared with the sector average of 12%. Any cuts in A&P expenses may pose an upside risk to our earnings estimates

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### STOCKS

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