Godrej Consumer Products

STOCK INFO.	BLOOMBERG
BSE Sensex: 16,769	GCPL IN
	REUTERS CODE
S&P CNX: 5,018	GOCP.BO

Equity Shares (m)	308.2
52-Week Range (Rs)	336/140
1,6,12 Rel. Perf. (%)	16/5/74
M.Cap. (Rs b)	93.7
M.Cap. (US$ b)	2.1

7 May 2010

Buy

Previous Recommendation: Buy

Rs304

YEAR END	NET SALES (RS M)	PAT (RS M)	EPS (RS)	EPS GR. (%)	P/E (X)	P/BV (X)	ROE (%)	ROCE (%)	EV/ SALES	EV/ EBITDA
03/09A	13,957	1,824	5.9	-16.1	51.4	13.8	30.4	27.2	5.5	37.8
03/10A	20,412	3,396	11.0	86.2	27.6	13.1	50.4	48.3	4.5	21.7
03/11E	24,566	4,040	13.1	19.0	23.2	11.3	48.6	49.5	3.7	18.3
03/12E	28,207	4,624	15.0	14.4	20.3	9.7	47.7	49.7	3.2	15.7

** Estimates from FY10 factor in 49% consolidation for Godrej Saralee*

We attended an analysts' meeting, hosted by Godrej Consumer Products to get an overview on growth in the FMCG sector in the current inflationary environment and the acquisition-led growth strategy. We present the key takeaways:

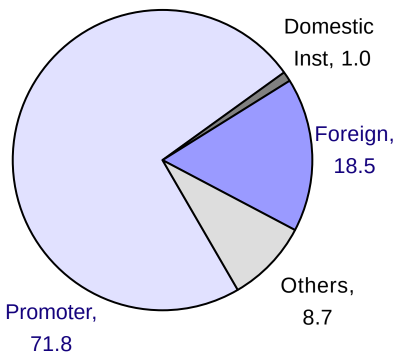
High food Inflation hurting urban poor; FMCG growth could be lower in 1HFY11

- The GCPL management indicated that a high inflation environment was being reflected in lower FMCG off-take. Growth rates for most categories decelerated in 4QFY10 and the trend continues in April.
- The impact of inflation is more pronounced on the urban poor, whose income has not increased in proportion to higher food prices. A normal monsoon (and agri growth) would be crucial to the revival of consumption sentiment, reducing food inflation and boosting rural income. The management signaled that FMCG growth could trend lower in 1HFY11 due to a lag effect of inflationary pressure.
- The management expects GST to be a significant growth driver of sales and profitability in the FMCG sector. While it reduces an unfair pricing advantage for unorganized players vis-à-vis organized players (due to tax evasion), supply chain costs (estimated at 1-2% of sales) could fall should there be fewer C&F agents. GCPL is likely to benefit from the large presence of unorganized players in the soaps and hair color segments.

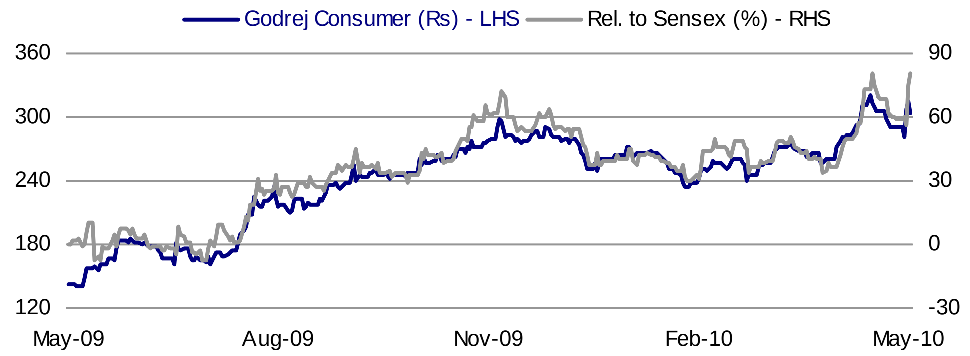
Domestic sales deceleration to be offset by improved performance of Godrej Sara Lee, subsidiaries

- Sales growth momentum for standalone operations will be muted in 1HFY11 due to sustained inflationary pressure and a high base effect. We are tweaking our estimates to factor in a slowdown in toilet soap sales and a price increase in hair color.
- Our consolidated estimates remain unchanged as the marginal hit in toilet soaps would be neutralized by higher realizations in hair color and toiletries. Besides GSL, *Kinky* and *Rapidol* are expected to post higher growth.
- We will factor in the impact of the Megasari acquisition after we receive financial details. Prima facie the deal looks EPS accretive by 13-18%. The acquisition of the balance stake in Godrej Sara Lee and the announcement of further acquisitions are crucial triggers to stock performance.
- The stock trades at 23.2x FY11E EPS of Rs13.1 and 20.3x FY12E EPS of Rs15. Incorporating the impact of the Megasari deal. The stock trades at 20.6x FY11E EPS of Rs14.8 and 17.2x FY12E EPS of Rs17.7. Maintain **Buy.**

SHAREHOLDING PATTERN (MAR.10 - %)



STOCK PERFORMANCE (1 YEAR)



Amnish Aggarwal (AmnishAggarwal@MotilalOswal.com); Tel:+9122 39825404 /**Nikhil Kumar** (Nikhil.N@MotilalOswal.com); Tel: +922 39825120

We attended an analysts' meeting, hosted by Godrej Consumer Products to get an overview on growth in the FMCG sector in the current inflationary environment and the impact of the company's acquisition-led growth strategy. We present the key takeaways:

High food Inflation hurting urban poor; FMCG growth could be lower in 1HFY11

- The management indicated that high inflation was being reflected in lower FMCG off-take. Growth rates for most categories decelerated in 4QFY10 and the trend continues in April.
- The impact of inflation is more pronounced on the urban poor, whose income has not increased in proportion to higher food prices. A normal monsoon (and agri growth) would be crucial to the revival in consumption sentiment, in terms of reducing food inflation and boosting rural income. The management signaled that FMCG growth could trend lower in 1HFY11 due to a lag effect of inflationary pressure.
- The management expects GST to be a significant growth driver of sales and profitability in the FMCG sector. While it will reduce the unfair pricing advantage for unorganized players vis-à-vis organized players (due to tax evasion), supply chain cost (estimated at 1-2% of sales) could fall should there be fewer C&F agents. GCPL is likely to benefit from a large presence of unorganized players in soaps and hair color.
- GCPL's 4QFY10 soap sales reflected a slowdown (we estimate a 5% decline). The management indicated that a high base effect of 4QFY09 and trade de-stocking (holding period down from 38 days to 30 days) led the decline. However, the slowdown was still higher than the industry growth as indicated by its market share gain of 110bp YoY.
- In the hair color segment, GCPL benefited from its market leadership in the powder category as it reported faster growth in 2HFY10 than premium hair creams. Increasing distribution reach and consumer activation at barber shops and salons also helped to boost sales. The company increased prices by 5-10% in the hair color portfolio in the past fortnight (weighted average of ~8%) which would boost sales growth in FY11.
- The management indicated that it held three months' inventory of PFAD (palm fatty acid distillate) at lower than market prices. The buying of material in domestic markets helped to cut its RM cost in the past six months.

Acquisitions to be EPS accretive; Megasari to add Rs500m to consolidated profit

- The management guided for profit accretion in the Megasari and Tura acquisitions. The Megasari deal, which is likely to be closed in the coming week, is likely to add Rs500m to consolidated profit in FY11 (~10 months).
- We believe Megasari will grow ~20% and margins expand ~50bp in FY11 resulting in 25% PAT growth. Our estimates factor in a valuation of ~Rs12b (2.2x EV/sales) and interest at 4% (pre-tax). We estimate the acquisition to be EPS accretive by 13-18%.
- The management also indicated that the Tura (a Nigerian acquisition) deal was likely to be closed in the coming months and would also be EPS accretive.
- The management reiterated its intention to acquire the balance 51% stake in Godrej Sara Lee over the coming months. In a recent release, the management revised upwards the likely price for the stake to Rs12b, citing Godrej Sara Lee's better performance.

- The company continues to scout for acquisition targets in Latin America, Kenya (East Africa) and other emerging markets as part of a "3x3 Strategy" (presence in three geographies, Asia, Africa and Latin America in three product categories, personal wash, hair care and household products).
- GCPL attained shareholder approval to raise Rs30b to fund acquisitions through a mix of debt and equity. While the management guided that the Megasari and Tura acquisitions would be debt financed, further acquisitions (including the Godrej Sara Lee stake) would be funded equally by equity and debt.
- GCPL may consider bridge loans for an interim period considering the time lag in raising equity funds.

ACQUISITION OF MEGASARI - IMPACT ON FINANCIALS

	FY10	FY11E	FY12E
Abridged P&L of Megasari (Expected)			
Expected Sales (Rs m)	5,500	6,600	7,788
Growth (%)		*20*	*18*
Expected EBITDA Margin (%)	*20*	*21*	*21*
Expected PAT Margin (%)	*14*	*15*	*15*
PAT (Rs m)	770	957	1,168
Deal Specifications and Funding			
Likely Acquisition Price (at ~2.2x EV/Sales)	12,100		
Internal Accruals (Rs m)	0	600	
Debt for Acquisition (Rs m)	12,100	11,500	
Impact on Consolidated EPS			
Interest on Debt of Rs12b (After tax)		339	339
Impact on Consolidated Profit for 10 months (Rsm)		515	829
Number of Equity Shares (m)		308	308
Impact on EPS (Rs)		1.7	2.7
Current EPS Estimates (Rs)		13.1	15.0
Revised EPS Estimates (Rs)		14.8	17.7
Change (%)		*13*	*18*

Source: Company/MOSL

4QFY10 results: Standalone operations disappoint; Godrej Sara Lee surprises

Standalone results are disappointing as 4QFY10 sales grew by just 2.1% to Rs2.8b. A 470bp margin expansion enabled EBITDA growth of 26% YoY. However, a 23% decline in other income and a 520bp increase in the tax rate reduced PAT growth to 13% YoY. GCPL's 4QFY10 results were above our estimates due to higher margins in standalone operations and better than expected profit contributions from Godrej Sara Lee. Net sales grew 48.1% to Rs5.1b (our estimate of Rs5b) led by sustained growth momentum in hair color and consolidation of 49% stake in Godrej Sara Lee. EBITDA margins expanded 150bp to 21.1% (our estimate of 18%) led by lower input costs and likely improvement in the sales mix. Adjusted PAT grew 54.5% to Rs918m (our estimate of Rs749m). Godrej Sara Lee's results surprised positively. GCPL's 4QFY10 share (49%) of sales and PAT were Rs1.47b and Rs228m respectively. For 10MFY10 (June 2009-March 2010, Godrej Sara Lee's net sales were Rs8.3b and PAT was Rs1.6b. GCPL's share was Rs4.1b (net sales) and Rs639m (PAT).

SEGMENTAL PERFORMANCE (RS M, STANDALONE)

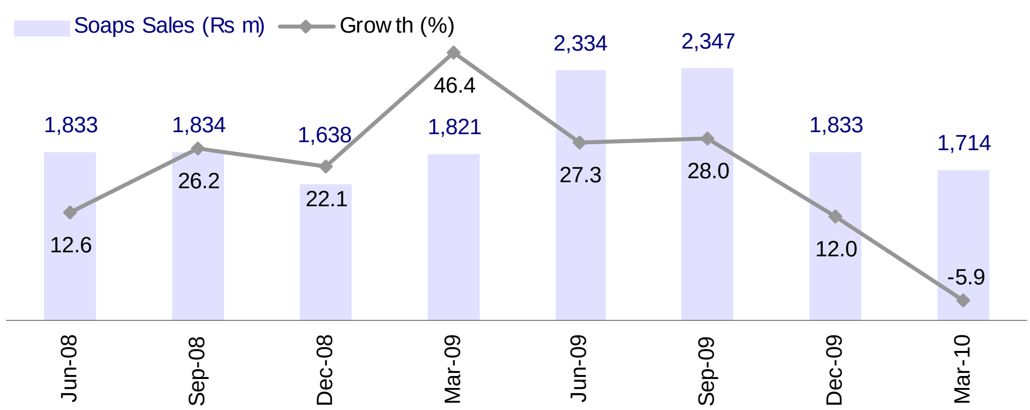
	4QFY10	4QFY09	CHG (%)	FY10	FY09	CHG (%)
Soaps	1,701	1,821	-6.6	8,241	7,138	15.5
Hair Colors	783	694	12.9	2,789	2,305	21.0
Toiletries	319	146	118.2	888	620	43.1
Liquid Detergents	76	55	38.3	507	429	18.2
By Products	40	50		254	358	-29.2
Exports	-95	0		0	0	
Total	**2,824**	**2,766**	**2.1**	**12,679**	**10,850**	**16.9**

Source: Company/MOSL

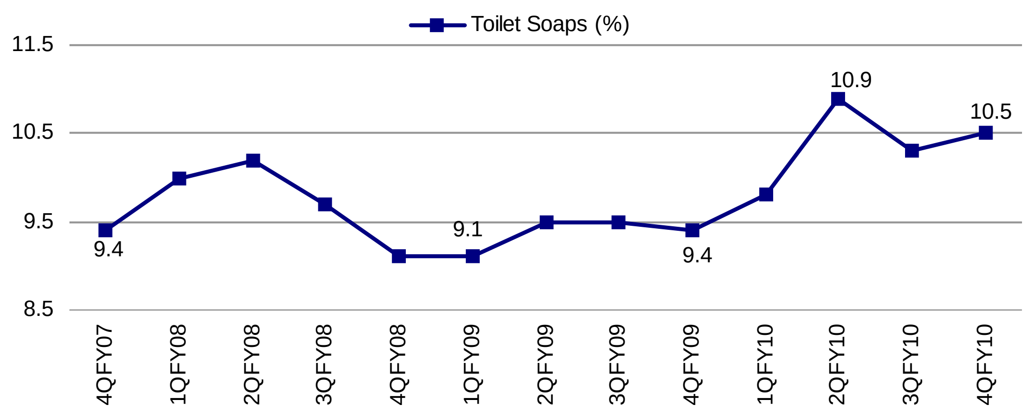
Toilet soap sales down 5%; market share up 110bp YoY

Standalone sales grew 2.1%. We estimated ~5% decline in toilet soap value sales (~65% of net sales), neutralizing sustained traction in hair color sales (up ~14% YoY). Toilet soap value growth has decelerated in recent months, led by multiple factors like: (1) a high base effect of 2HFY09 (product price hikes during that period), (2) lower volumes due to extended winters, (3) high food inflation and (4) trade de-stocking (from 38 days to 30 days). We estimate the pricing impact for the quarter to be negligible. We note that the category would have reported a higher de-growth as reflected by an increase of 110bp YoY (20bp QoQ) in market share by GCPL.

SOAP SALES DECLINE ~5% DUE TO CATEGORY DE-GROWTH



MARKET SHARE UP 110BP YOY



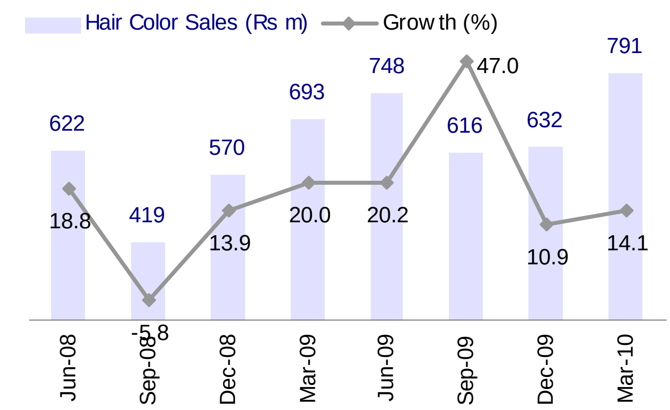
Source: Company/MOSL

Godrej No1 continued to maintain value leadership in North India and GCPL launched an activation campaign of *Cinthol* Original with the extension of the brand to small SKUs in its strong foothold, Tamil Nadu. GCPL also launched a moisturizing variant of *No1* soap in January 2010. GCPL relaunched *No1* in April 2010 with a new shape, packaging and natural oils. We believe the relaunch will boost sales in peak summer months.

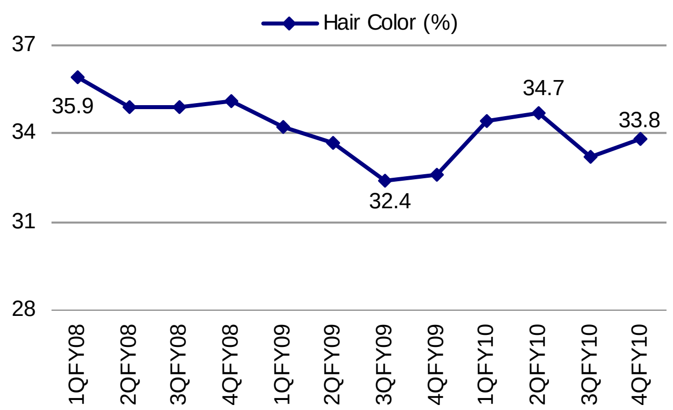
Hair color sales up 14%; market share up 120bp YoY

Hair color sales grew 14% (largely volume led). Sales growth slowed during the past couple of quarters due to the waning impact of the price increase (~7% in October 2009). GCPL's FY10 hair color sales grew 19% (category growth of 14%), its market share increased 120bp YoY to 33.8% (up 60bp QoQ). GCPL launched a new consumer offer (free shampoo) which evoked encouraging response. GCPL will continue to play its portfolio across price points to accelerate growth in this low penetration category. The company increased prices by 5-10% in the hair color portfolio in the past fortnight (weighted average of ~8%) which would boost sales growth in FY11.

HAIR COLOR SALES GROW 14%...



...ENABLING MARKET SHARE EXPANSION OF 120BP



Source: Company/MOSL

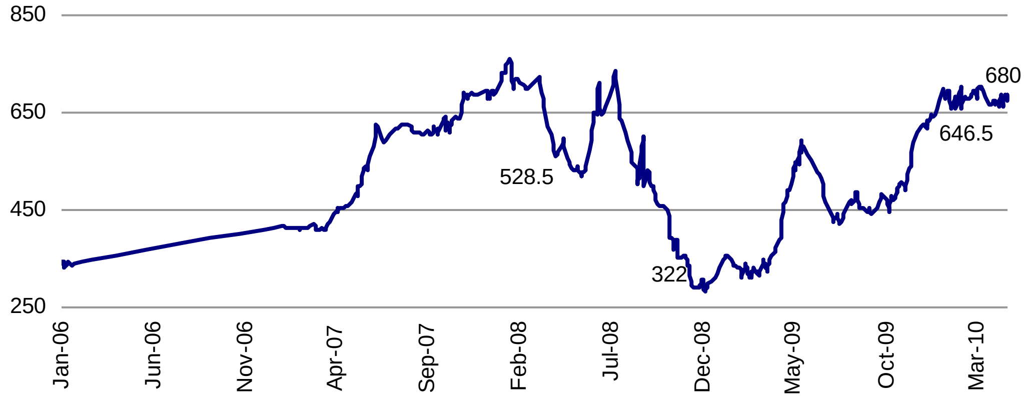
Lower input cost, better sales mix enables margin expansion of ~470bp (standalone)

Gross margins for the standalone business expanded by ~12% to 59.4% due to lower input costs and an improved sales mix (hair color grew faster). Palm oil fatty acid (PFAD) prices increased 35% since November 2009 to current levels of US$685/ton. GCPL started using a mix of imported PFAD and that sourced from domestic refiners (costing 15% less due to savings of import duty) which reduced input cost inflation. The company also benefited from the rupee appreciation during the last quarter, which partly negated the impact. The management indicated forward cover of up to three months of requirement.

EBITDA margins expanded 470bp to 24.8% as it invested part of the benefits on advertising (adspend up 580bp). Staff costs fell 250bp due to a higher base (higher performance linked incentive in 4QFY09).

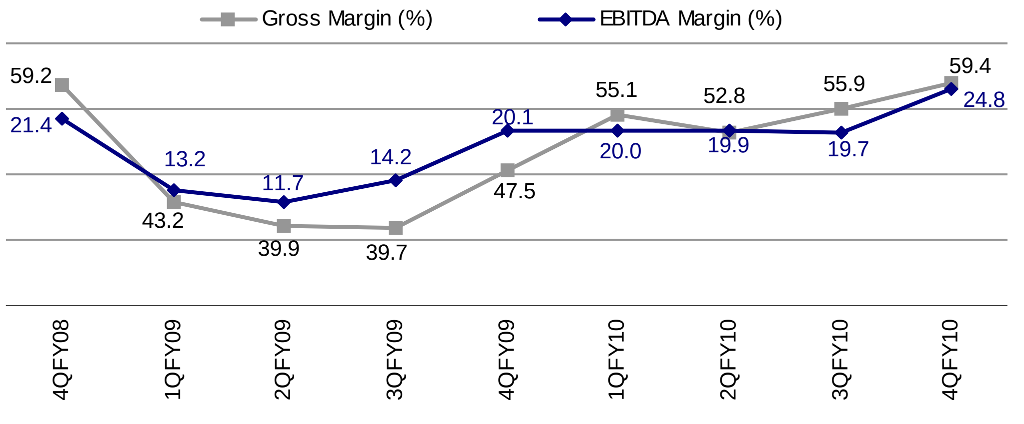
The company benefited from domestic procurement and the rupee appreciation during the last quarter

PALM FATTY ACID UP ~35% SINCE NOVEMBER 2009 (US$/MT)



Source: Company/MOSL

MARGINS MAY HAVE PEAKED



Source: Company/MOSL

Godrej Sara Lee 4QFY10 sales Rs3b; PAT Rs465m

The management in a recent release indicated that acquisition of the balance stake (51%) in GSL could cost up to Rs12b

Godrej Sara Lee results have been a positive surprise with GCPL's share (49%) of sales and PAT being Rs1.47b and Rs228m for 4QFY10, and Rs4.1b and Rs639m for 10MFY10 (June 2009 to March 2010) respectively. Between June 2009 and March 2010, Godrej Sara Lee posted net sales of Rs8.3b and PAT of Rs1.3b. However, since the June quarter is the weakest quarter for Godrej Sara Lee's household insecticide business, we estimate GSL's FY10 sales and PAT at Rs10b and Rs1.6b (12-month period) respectively. The management in a recent release indicated that acquisition of the balance stake (51%) in GSL could cost up to Rs12b. An increase in the cost of acquisition has been ascribed to Godrej Sara Lee's strong performance during FY10. We believe the acquisition of majority stake in Godrej Sara Lee is a positive for GCPL as it would expand its product portfolio and scale of operations significantly.

International business sales up 21%; *Rapidol*, Kinky integration boost South Africa sales

GCPL's international business sales grew 21% to ~Rs900m in 4QFY10 with a sharp increase in profits from Rs5m to Rs25m. We note that the rupee appreciated against the GBP, which might have impacted growth. FY10 sales increased 20% and PAT increased

81%. Keyline operations grew 9% in FY10. *Cuticura* emerged as a volume leader in the UK after strong growth in FY10 (consequent to the swine flu epidemic); the brand posted growth of 83%. Growth in Keyline would likely trend lower on account receding impact of H1N1 influenza. The operational integration of *Kinky* and *Rapidol* under a single management has been completed and the brands have begun to reap synergy benefits. *Rapidol* and *Kinky* reported FY10 sales growth of 42% and 40%, respectively. The management indicated that Kinky operates in a US$2b category and it expects strong growth rate to continue.

Valuation and view: Better GSL performance, subsidiaries to offset slow domestic sales

- Sales growth momentum for standalone operations will be muted in 1HFY11 due to sustained inflationary pressure and a high base effect. We are tweaking our estimates to factor in a slowdown in toilet soap sales and a price increase in hair color products.
- Our consolidated estimates remain unchanged as the marginal hit in toilet soaps would be neutralized by higher realizations in hair color products and toiletries. Besides Godrej Sara Lee, *Kinky* and *Rapidol* are expected to post higher growth.
- We will factor in the impact of the Megasari acquisition after we have detailed financials. Prima facie the deal looks EPS accretive by 13-18%.
- The acquisition of the balance stake in Godrej Sara Lee and announcement of more acquisitions remains crucial to the stock performance.
- The stock trades at 23.2x FY11E EPS of Rs13.1 and 20.3x FY12E EPS of Rs15. Incorporating the impact of the Megasari deal, the stock trades at 20.6x FY11E EPS of Rs14.8 and 17.2x FY12E EPS of Rs17.7. Maintain **Buy**.

Financials and Valuation

INCOME STATEMENT - CONSOLIDATED					(RS MILLION)
Y/E MARCH	2008	2009	2010E	2011E	2012E
Net Sales	**11,026**	**13,930**	**20,528**	**24,566**	**28,207**
Change (%)	*15.9*	*26.3*	*47.4*	*19.7*	*14.8*
Cost of Goods Sold	5,180	7,695	9,861	12,096	14,064
Gross Profit	**5,846**	**6,234**	**10,667**	**12,470**	**14,143**
Margin (%)	*53.0*	*44.8*	*52.0*	*50.8*	*50.1*
Other Expenditure	3,701	4,197	6,399	7,490	8,479
EBITDA	**2,145**	**2,037**	**4,269**	**4,980**	**5,664**
Change (%)	*19.4*	*-5.0*	*109.5*	*16.7*	*13.7*
Margin (%)	*19.5*	*14.6*	*20.8*	*20.3*	*20.1*
Depreciation	182	192	227	276	310
Int. and Fin. Charges	129	-172	-13	-130	-241
Other Income-rec.	40	75	338	289	301
PBT	**1,875**	**2,092**	**4,392**	**5,122**	**5,895**
Change (%)	*18.2*	*11.6*	*110.0*	*16.6*	*15.1*
Margin (%)	*17.0*	*15.0*	*21.4*	*20.8*	*20.9*
Tax	273	332	757	1,049	1,229
Deferred Tax	-9	-34	-28	-33	-42
Tax Rate (%)	*15.1*	*17.5*	*17.9*	*21.1*	*21.6*
PAT	**1,592**	**1,726**	**3,608**	**4,040**	**4,624**
Change (%)	*18.6*	*8.4*	*109.0*	*12.0*	*14.4*
Margin (%)	*14.4*	*12.4*	*17.6*	*16.4*	*16.4*
Non-rec. (Exp.)/Income	0	6	0	0	0
Reported PAT	**1,592**	**1,732**	**3,608**	**4,040**	**4,624**

BALANCE SHEET					(RS MILLION)
Y/E MARCH	2008	2009	2010E	2011E	2012E
Share Capital	226	257	308	308	308
Reserves	1,490	5,412	6,856	8,011	9,390
Networth	**1,716**	**5,668**	**7,164**	**8,319**	**9,698**
Loans	1,871	2,776	2,775	2,775	2,775
Deferred Liability	89	42	70	103	145
Capital Employed	**3,676**	**8,486**	**10,008**	**11,197**	**12,618**
Gross Block	2,937	3,370	4,399	4,708	4,921
Less: Accum. Depn.	-1,253	-1,098	-1,014	-1,291	-1,601
Net Fixed Assets	**1,683**	**2,272**	**3,385**	**3,417**	**3,320**
Capital WIP	716	25	150	150	150
Goodwill	956	2,086	2,086	2,086	2,086
Investments	1	3,291	3,239	4,394	5,813
Currents Assets	**3,519**	**4,111**	**5,439**	**6,297**	**7,065**
Inventory	1,916	1,675	2,566	2,890	3,134
Account Receivables	510	602	900	1,077	1,236
Cash and Bank Balance	426	567	643	867	1,457
Loans and Advances	668	1,268	1,330	1,463	1,237
Curr. Liab. & Prov.	**3,227**	**3,299**	**4,290**	**5,146**	**5,816**
Account Payables	1,491	1,145	1,485	1,822	2,118
Other Liabilities	1,464	1,834	2,151	2,446	2,702
Provisions	271	320	654	878	996
Net Current Assets	**292**	**812**	**1,149**	**1,151**	**1,249**
Miscellanous	29				
Net Assets	**3,676**	**8,486**	**10,009**	**11,197**	**12,618**

E: MOSL Estimates

RATIOS					
Y/E MARCH	2008	2009	2010E	2011E	2012E
Basic (Rs)					
EPS	**7.1**	**6.7**	**11.7**	**13.1**	**15.0**
Cash EPS	7.9	7.5	12.4	14.0	16.0
BV/Share	5.6	22.1	23.2	27.0	31.5
DPS	4.1	4.0	6.0	8.0	9.0
Payout (%)	58.2	59.7	51.3	61.0	60.0
Valuation (x)					
P/E	43.1	45.3	26.0	23.2	20.3
Cash P/E	38.7	40.7	24.4	21.7	19.0
EV/Sales	6.4	5.5	4.5	3.7	3.2
EV/EBITDA	32.7	37.8	21.7	18.3	15.7
P/BV	54.6	13.8	13.1	11.3	9.7
Dividend Yield	1.4	1.3	2.0	2.6	3.0
Return Ratios (%)					
RoE	92.8	30.4	50.4	48.6	47.7
RoCE	64.4	27.2	48.3	49.5	49.7
Working Capital Ratios					
Debtor (Days)	17	16	16	16	16
Asset Turnover (x)	4.6	6.1	5.8	6.9	8.1
Leverage Ratio					
Debt/Equity (x)	1.1	0.5	0.4	0.3	0.3

CASH FLOW STATEMENT					(RS MILLION)
Y/E March	2008	2009	2010E	2011E	2012E
OP/(Loss) before Tax	2,145	2,037	4,269	4,980	5,664
Int./Div. Received	40	75	338	289	301
Interest Paid	-129	172	13	130	241
Direct Taxes Paid	-273	-332	-757	-1,049	-1,229
(Inc)/Dec in WC	183	380	260	-222	-492
CF from Operations	**1,967**	**2,332**	**4,123**	**4,128**	**4,485**
Extraordinary Items	0	6	0	0	0
(Inc)/Dec in FA	-555	258	-1,155	-308	-213
(Pur.)/Sale of Investments	0	-3,291	52	-1,155	-1,420
Goodwill	-70	-1,130	0	0	0
CF from Investments	**-626**	**-4,156**	**-1,103**	**-1,463**	**-1,633**
Issue of Shares	0	3,601	51	0	0
Inc in Debt	135	905	-1	0	0
Dividend Paid	-1,085	-1,206	-2,164	-2,885	-3,245
Other Item	-439	-1,336	-819	366	929
CF from Fin. Activity	**-1,389**	**1,965**	**-2,932**	**-2,519**	**-2,316**
Inc/Dec of Cash	**-48**	**141**	**88**	**146**	**536**
Add: Beginning Balance	474	426	567	643	867
Closing Balance	**426**	**567**	**655**	**789**	**1,403**

NOTES

For more copies or other information, contact
Institutional: Navin Agarwal. **Retail:** Manish Shah
Phone: (91-22) 39825500 Fax: (91-22) 22885038. E-mail: reports@motilaloswal.com

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

Disclosure of Interest Statement	Godrej Consumer Products
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