

Godrej Consumer Products Ltd

Building a global footprint; upgrade to Buy

We attended the analyst meet of Godrej Consumer Products (GCPL) wherein the management remained upbeat on the company's growth prospects in both domestic and international markets. Although the financial details for its recent acquisitions in Indonesia and Nigeria were not disclosed, we expect these deals to be earnings accretive for GCPL from FY11 onwards. Strong growth in the Godrej Sara Lee (GSL) portfolio will provide a further fillip to the domestic business. Given GCPL's robust growth outlook, we upgrade the stock from Hold to Buy and revise our March '11 price target from Rs 282 to Rs 350, valuing it at 23x March '12 earnings.

Indonesia to be the next growth driver: GCPL announced the acquisition of the PT Megasari group in April '10 – a company that has a dominant presence in the household care market in Indonesia. Megasari had net sales of US\$ 120mn (Rs 5.5bn) in CY09 and the management expects the deal to add Rs 500mn to GCPL at the net profit level. The detailed financials and deal size have not been disclosed as yet.

Africa presence gets a flavour added through Tura: GCPL also entered the Nigerian markets through the acquisition of Tura – a market leader in the personal care category that manufactures and distributes products like soaps, moisturising lotions and skin-toning creams. The company will cross-promote its products between Nigeria and South Africa, which will further augment growth. Financials of Tura are not available though the company is smaller than Megasari.

GSL portfolio to generate domestic growth: GSL reported revenues of Rs 4bn and PAT of Rs 640mn for the period from 1 June 2009 to 31 March 2010. It will contribute ~25% to GCPL's sales in FY11 (financials without consolidation of Megasari and Tura acquisitions).

Upgrade to Buy: GCPL has graduated from a two-product domestic company to a conglomerate with a strong domestic presence in the home & personal care and household insecticide categories in India. It will also have a strong and dominant position in the fast growing economies of Africa and South East Asian countries like Indonesia. The company is expected to make an acquisition in Latin America to complete its 3x3 strategy entailing a presence across Asia, Africa and Latin America. We believe GCPL is successfully transforming itself into a well-diversified global conglomerate in the home & personal care segment; we therefore upgrade the stock from Hold to Buy and raise our target price from Rs 282 to Rs 350. We have not incorporated the financials of Megasari and Tura in our financials and valuation.

Financial highlights

(Rs mn)	FY09	FY10	FY11E	FY12E
Revenue	13,930	20,412	24,798	28,352
Growth (%)	26.3	46.5	21.5	14.3
Adj net income	1,733	3,396	4,137	4,771
Growth (%)	8.8	95.9	21.8	15.3
FDEPS (Rs)	6.7	11.3	13.3	15.4
Growth (%)	(4.8)	68.7	17.8	15.3

Profitability and return ratios

(%)	FY09	FY10	FY11E	FY12E
EBITDA margin	14.6	20.0	19.8	19.9
EBIT margin	13.2	18.8	18.4	18.4
Adj PAT margin	12.4	16.6	16.7	16.8
ROE	46.9	50.3	48.1	43.4
ROIC	36.2	52.8	54.0	54.9
ROCE	31.5	37.0	38.4	36.4

What's New?	Target	Rating	Estimates
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CMP	TARGET	RATING	RISK
Rs 303	Rs 350	BUY	LOW

BSE	NSE	BLOOMBERG
532424	GODREJCP	GCPL IN

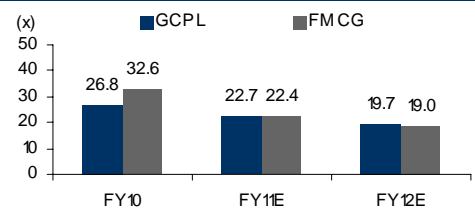
Company data

Market cap (Rs mn / US\$ mn)	94,484 / 2,077
Outstanding equity shares (mn)	309.8
Free float (%)	28.2
Dividend yield (%)	1.4
52-week high/low (Rs)	340 / 139
2-month average daily volume	360,936

Stock performance

Returns (%)	CMP	1-mth	3-mth	6-mth
GCPL	303	8.4	21.7	9.4
BSE FMCG	2,818	(1.4)	4.2	(0.0)
Sensex	16,769	(6.5)	5.3	2.0

P/E comparison



Valuation matrix

(x)	FY09	FY10	FY11E	FY12E
P/E @ CMP	45.2	26.8	22.7	19.7
P/E @ Target	52.1	30.9	26.2	22.7
EV/EBITDA @ CMP	45.4	22.7	18.9	16.4





Analyst meet highlights

International business – The next growth driver

Five overseas acquisitions since 2005 to fulfil GCPL's 3x3 market strategy

Under the 3x3 strategy for its international operations, GCPL is focusing on the emerging markets of Africa, Latin America and Asia (ex-Japan) and targeting the categories of personal wash, hair care and home care. Since mid-2005, GCPL has made five overseas acquisitions – in October '05, it acquired Keyline in the UK for ~£ 13mn; in September '05 and April '08, Rapidol and Kinky in South Africa, and now in March and April '10, Nigeria-based Tura and Indonesian group Megasari respectively.

Tura – An entry point into under-penetrated North Africa

We peg the acquisition price of Tura – a subsidiary of UK-based personal care company Lornamead – at 2x its estimated CY09 sales of US\$ 50mn and assume that the deal will be funded with the help of low-cost debt. Tura has been operating for over two decades in Africa's skincare market with a range of products like soaps, moisturising lotions and toners, and an efficient sales network that has a 70%+ distribution reach in the West African region. Its medicated soap is among the top three in its category in Nigeria.

Tura to strengthen GCPL's presence in Africa and allow for cross-selling of Kinky and Rapidol products

We believe Tura will further fortify GCPL's presence in the African continent and also provide a platform for introducing GCPL's own products and those of its South African brands Kinky and Rapidol into the market. Lower product penetration in Africa and an entry into an important personal product market like Nigeria (population of 140mn+; economic growth rate of 6%) would prove to be strong growth drivers for the company.

Megasari – A strategic fit

GCPL has acquired Indonesia-based Megasari along with its distributor PT Intrajari Raya. Although the management has not disclosed the acquisition price, we estimate it at 2.2x Megasari's CY09 sales of US\$ 120mn. Here too, the deal is likely to be funded with the help of low-cost overseas debt.

Megasari a leading player in Indonesia's household insecticide category

Megasari is a household care company that manufactures products such as household insecticides, air fresheners, wet tissues, baby care, car and motorcycle products, food wrappings, drain openers, bleach, metal polishers and fly & rat glue. Several of the company's brands like *Hit*, *Stella*, *Mitu* and *Simba* are well known in Indonesia and are among the top 3 in their respective product segments. The company markets its insecticide products (liquid and aerosol-based) under the brand name *Hit*, which is ranked No. 2 in the US\$ 150mn Indonesian household insecticides market. It has six factories across Indonesia and a widespread distribution network.

Fig 1 - Megasari's market share across categories

Category	Market size in 2009 (US\$ mn)	Category market share (%)	Rank
Household insecticides	150	35	2
Air care	68	45	1
Wipes	21	80	1
Breakfast cereals	17	15	N/A

Source: Company, RCML Research

Megasari has gained market share in all major segments over the past couple of years and a majority of its brands are profit making. Its products have a high penetration of ~75% in the Indonesian market. The household insecticides segment contributes 45–48% to the topline. Air care and wipes are its two other major business segments. Megasari has clocked a revenue CAGR of 25% over the last three years, growing by 20% in CY09 to US\$ 120mn. The company has also posted a strong EBITDA CAGR of 53% over the past three years with EBITDA margins of over 20%.



Indonesia's market profile suggests strong growth potential

We believe the Megasari acquisition augurs well for GCPL's strategy to inorganically expand its overseas personal care and home care business in emerging markets. Lower penetration of liquid and aerosol-based insecticides in Indonesia (as compared to coils) provides a high growth opportunity for the company. Also, Indonesia's tropical climate and rainforests create a high demand environment for insecticides, while its similarities to the Indian market (large population, stable GDP growth and comparable consumer profile) indicate strong growth potential. In the domestic market, GCPL is present in the home care segment through its joint venture, GSLL. GCPL plans to cross-sell GSLL and Megasari products in the Indonesian and Indian markets respectively.

Tura and Megasari to add 10.3% and 17.7% to earnings in FY11 and FY12

Tura, Megasari to be earnings accretive from Year 1 itself

We expect the Tura and Megasari acquisitions to be earnings accretive to the tune of 10.3% and 17.7% in FY11 and FY12 respectively. We estimate that GCPL will raise debt of ~Rs 14bn to fund these acquisitions.

Fig 2 - Proforma financials considering the merger impact of Tura and Megasari

Company (Rs mn)	FY11E	FY11E*	FY12E	Comments
Tura				
Sales	2,700	2,025	3,240	Tura had estimated sales of US\$ 50mn in CY09. We estimate a 20% YoY growth for FY11 and FY12
EBITDA	432	324	518	
EBITDA Margin(%)	16.00	16.00	16.00	We expect Tura's EBITDA margin to be in the range of 15-17%
Interest	230	173	230	We estimate the acquisition price for Tura to be 2x CY09 sales and assume that the acquisition will be fully funded by low-cost debt (interest rate @5%)
PAT	40	30	94	We estimate Tura's PAT margin to be in the range of 9-11% (interest cost deducted to arrive at PAT)
Megasari				
Sales	6624	4,968	7,949	As per the management, Megasari had sales of US\$ 120mn in CY09. We estimate a 20% YoY growth for FY11 and FY12, assuming a US\$ exchange rate of Rs 46
EBITDA	1,325	994	1,590	
EBITDA Margin(%)	20.0	20.0	20.0	We estimate Megasari's EBITDA Margin to be in the range similar to that of GCPL
Interest	600	450	600	We peg the acquisition price for Megasari at 2.2x CY09 sales and assume that the acquisition will be fully funded by low-cost debt (interest rate @5%)
PAT	526	395	751	We estimate Megasari's PAT margin to be in the range of 16-17%, similar to that of GCPL (interest cost deducted to arrive at PAT)
GCPL-Ex Acquisitions				
		FY11E	FY12E	
Sales		24,798	28,352	
EBITDA		4,910	5,646	
EBITDA Margin(%)		19.8	19.9	
PAT		4,137	4,771	
PAT Margin(%)		16.7	16.8	
Shares Outstanding(mn)		309.9	309.9	
EPS (Rs)		13.3	15.4	
GCPL- Post Acquisitions				
		FY11E	FY12E	
Sales		31,791	39,541	
EBITDA		6,228	7,755	
EBITDA Margin(%)		19.6	19.6	
PAT		4,561	5,617	
PAT Margin (%)		14.3	14.2	
Shares Outstanding(mn)		309.9	309.9	
EPS (Rs)		14.7	18.1	
EPS accretion (%)		10.3	17.7	EPS accretive by 10.3% in FY11E and 17.7% in FY12E

Source: RCML Research

*FY11E financials considering 9 months of consolidation of Tura and Megasari with GCPL



Domestic business on a strong footing

May raise funds via equity dilution to fund GSLL buyout; D/E not to exceed 1x

GSLL likely to become 100% owned soon

GCPL, which holds 49% in GSLL, is looking forward to acquiring the balance 51% stake whenever it comes up for sale. The company may raise funds via equity dilution to fund the GSLL stake buy such that its D/E ratio remains ~1x. GCPL has already received board and shareholder approval to raise up to Rs 30bn through debt and equity for mergers and acquisitions.

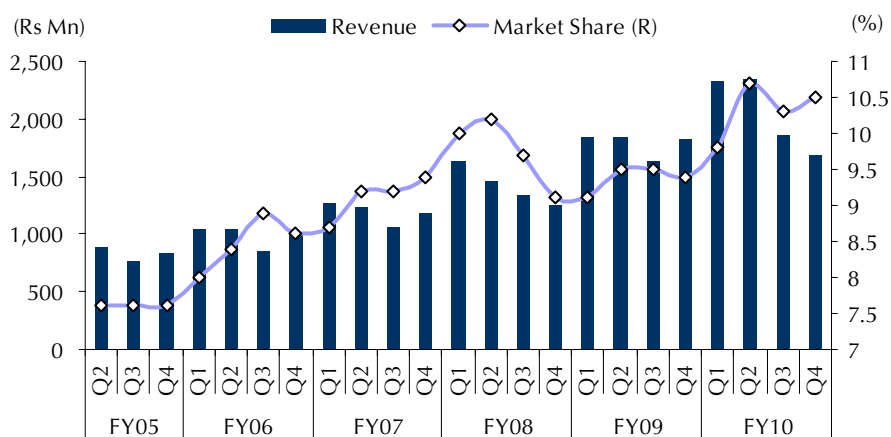
GSLL remains the market leader in household insecticides, air care and hair cream segments in the Indian market. The company sells its products under leading brands such as *GoodKnight*, *JET*, *HIT*, *Ambipur*, *Brylcreem* and *Kiwi*.

Holds a value market share of 10.3% in toilet soaps and volume share of 12.3%

Domestic soaps business gains market share...

The soap market size is currently estimated at Rs 85.8bn, with GCPL holding a value market share of 10.3% and volume share of 12.3%. The company continues to be the second largest toilet soap player in the country with a dominant position in North India. GCPL has relaunched its *Godrej No. 1* soap in April '10 in a new shape and packaging and with natural oil ingredients. It had earlier launched a couple of variants of Godrej No. 1 in FY10. The company intends to maintain the price points of Rs 5 and 10 for this product.

Fig 3 - GCPL: Soaps market share trend



Source: Company, RCML Research

...but competitive intensity remains high

The toilet soaps industry in India remains highly competitive with Hindustan Unilever involved in heavy brand promotions to regain its lost market share. Pricing power is unlikely to return in the near future and competitive intensity will remain high. However, growth rates for the industry are likely to improve on expectations of a normal monsoon, as the easing of food inflation will ease the pressure on consumers.

Fig 4 - Soaps market share among players

Company	Q4FY09	Q4FY10	Change	FY09	FY10	Change
HUL	48.2	44.6	(360 bps)	49.9	45	(490 bps)
GCPL	9.4	10.5	110 bps	9.4	10.3	90 bps
Wipro	8.5	9	50 bps	8.3	8.8	50 bps
Reckitt	6.1	6.8	70 bps	6.5	7.3	80 bps
Nirma	4.6	4.3	(30 bps)	4.7	4.4	(30 bps)
ITC	2.4	3.7	130 bps	1.8	3	120 bps

Source: Company

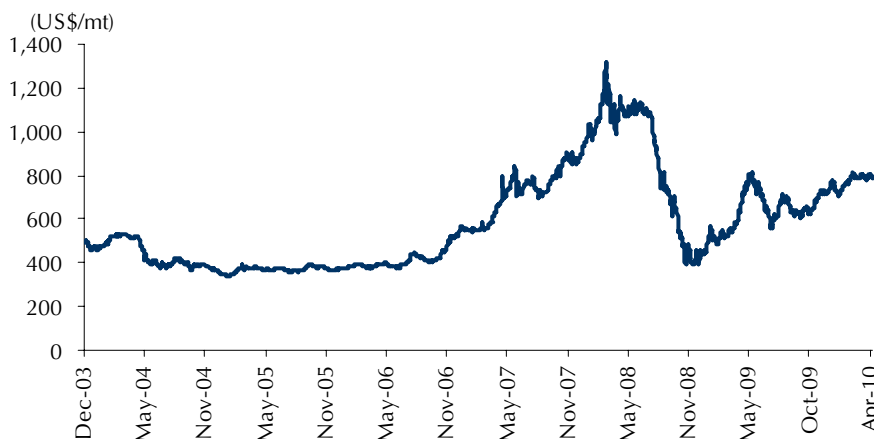


Palm oil costs have moved on account of local buying

Local buying pushes down raw material costs

GCPL has benefited from the lower palm oil prices in FY10 (a key ingredient for soaps), although prices have started inching up towards the year end. The company has now started to buy palm oil locally which proves cheaper than overseas buying now that large palm oil players like Wilmar have set up refineries in India. These companies are processing crude palm oil which can be imported duty-free into the country. Rupee appreciation is also likely to partly offset the increase in palm oil prices over the last quarter.

Fig 5 - Malaysian palm oil prices



Source: Bloomberg, RCML Research

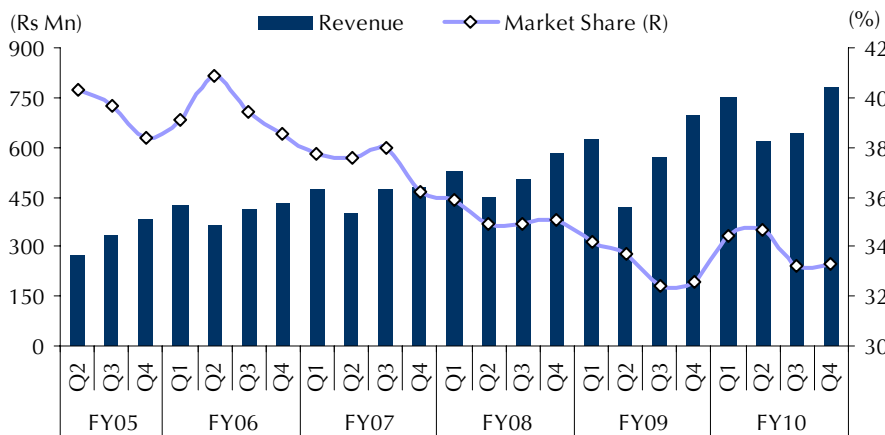
Strong presence in lower end hair colour market but faces hurdles in crossing over to the premium segment

Hair colour business has strong mass market brand equity

The hair colour industry in India is estimated at Rs 11.3bn with a growth rate of 14% in FY10. GCPL held a market share of 33.9% in FY10 with the category continuing to have penetration levels of just 30%. The company has a strong presence in the lower end of the market through its flagship brand *Godrej Expert Hair Colour*. Around 80–85% of GCPL’s hair colour sales are through this brand. The company is targeting salons for the distribution of its products in non-metro and rural markets. It currently has a base of 45,000–50,000 salons from an estimated half a million in the country.

GCPL, however, continues to face a tough challenge at the top end of the market where MNC players like Garnier have a strong presence. The company has its brand *Renew* positioned in this segment, which is available in six colours; however this has not proved to be a successful venture.

Fig 6 - GCPL: Hair colour market share trend



Source: Company, RCML Research



Valuation

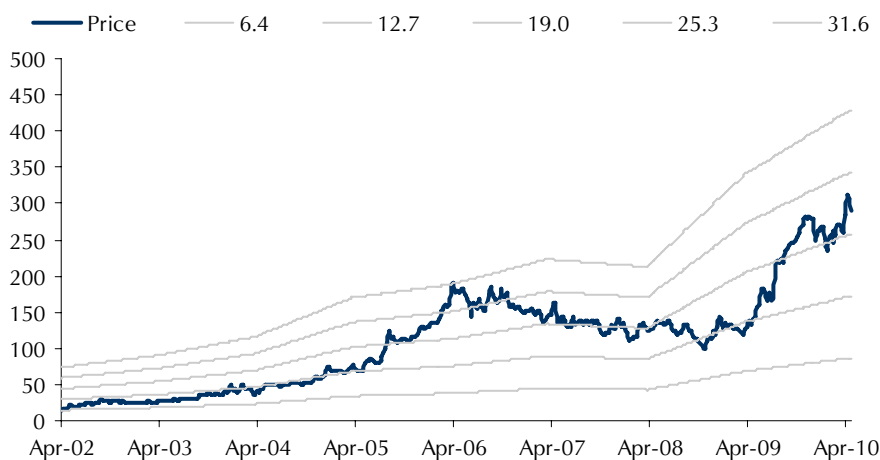
Scope for re-rating – upgrade to Buy

Diversification in the domestic market, and a growing presence in Asia and Africa to drive re-rating

GCPL is currently trading at a P/E of 22.7x and 19.7x its FY11E and FY12E earnings. The stock has historically traded in a band of 12–30x in the last five years. However, it witnessed a significant re-rating post the merger of GSLL which widened its product basket and enabled it to finally graduate from being a two-product company.

We see scope for re-rating once again on account of diversification in the domestic market through the GSLL portfolio, and strong growth in the international arena by virtue of its presence in the faster growing economies of Asia and Africa. We value GCPL at 23x FY12E earnings to arrive at a March '11 target price of Rs 350. Our target price provides an appreciation of 18% from current levels; we upgrade the stock from Hold to Buy.

Fig 7 - 1-year forward P/E band



Source: RCML Research



Consolidated financials

Profit and Loss statement

Y/E March (Rs mn)	FY09	FY10	FY11E	FY12E
Revenues	13,930	20,412	24,798	28,352
<i>Growth (%)</i>	26.3	46.5	21.5	14.3
EBITDA	2,038	4,073	4,910	5,646
<i>Growth (%)</i>	(5.0)	99.9	20.5	15.0
Depreciation & amortisation	192	236	353	417
EBIT	1,845	3,837	4,557	5,230
<i>Growth (%)</i>	(6.0)	107.9	18.8	14.8
Interest	189	111	150	175
Other income	436	473	589	708
EBT	2,093	4,199	4,996	5,763
Income taxes	360	803	859	991
Effective tax rate (%)	17.2	19.1	17.2	17.2
Extraordinary items	-	-	-	-
Min into / inc from associates	-	-	-	-
Reported net income	1,733	3,396	4,137	4,771
Adjustments	-	-	-	-
Adjusted net income	1,733	3,396	4,137	4,771
<i>Growth (%)</i>	8.8	95.9	21.8	15.3
Shares outstanding (mn)	258.1	308.2	309.9	309.9
FDEPS (Rs) (adj)	6.7	11.3	13.3	15.4
<i>Growth (%)</i>	(4.8)	68.7	17.8	15.3
DPS (Rs)	3.9	4.2	5.3	6.1

Cash flow statement

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Net income + Depreciation	1,897	3,576	4,490	5,188
Non-cash adjustments	(27)	121	81	93
Changes in working capital	(353)	574	(492)	(150)
Cash flow from operations	1,517	4,272	4,078	5,131
Capital expenditure	(483)	(1,698)	(994)	(697)
Change in investments	(1,203)	-	-	-
Other investing cash flow	-	-	-	-
Cash flow from investing	(1,686)	(1,698)	(994)	(697)
Issue of equity	3,816	51	2	-
Issue/repay debt	86	(271)	-	-
Dividends paid	(1,173)	(1,532)	(1,915)	(2,209)
Other financing cash flow	798	-	-	-
Change in cash & cash eq	3,357	823	1,170	2,225
Closing cash & cash eq	3,784	4,607	5,775	8,000

Economic Value Added (EVA) analysis

Y/E March	FY09	FY10E	FY11E	FY12E
WACC (%)	11.0	10.5	10.5	10.5
ROIC (%)	36.2	52.8	54.0	54.9
Invested capital (Rs mn)	4,962	6,360	7,625	8,156
EVA (Rs mn)	1,249	2,692	3,314	3,619
EVA spread (%)	25.2	42.3	43.5	44.4

Balance sheet

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Cash and cash eq	3,784	4,607	5,775	8,000
Accounts receivable	602	1,386	1,902	2,330
Inventories	1,675	2,617	3,207	3,651
Other current assets	1,267	1,417	1,736	1,985
Investments	75	75	75	75
Gross fixed assets	2,745	3,968	4,862	5,559
Net fixed assets	1,807	2,761	3,302	3,582
CWIP	25	500	600	600
Intangible assets	2,551	2,551	2,551	2,551
Deferred tax assets, net	(88)	(167)	(248)	(341)
Other assets	42	-	-	-
Total assets	11,737	15,746	18,900	22,433
Accounts payable	1,145	2,420	2,791	3,191
Other current liabilities	1,773	2,293	2,644	3,023
Provisions	380	1,038	1,249	1,441
Debt funds	2,771	2,500	2,500	2,500
Other liabilities	-	-	-	-
Equity capital	257	308	310	310
Reserves & surplus	5,411	7,187	9,409	11,971
Shareholder's funds	5,668	7,496	9,718	12,280
Total liabilities	11,737	15,746	18,900	22,433
BVPS (Rs)	22.0	24.3	31.4	39.6

Financial ratios

Y/E March	FY09	FY10E	FY11E	FY12E
Profitability & Return ratios (%)				
EBITDA margin	14.6	20.0	19.8	19.9
EBIT margin	13.2	18.8	18.4	18.4
Net profit margin	12.4	16.6	16.7	16.8
ROE	46.9	50.3	48.1	43.4
ROCE	31.5	37.0	38.4	36.4
Working Capital & Liquidity ratios				
Receivables (days)	15	18	24	27
Inventory (days)	85	82	91	94
Payables (days)	63	68	81	82
Current ratio (x)	2.5	2.1	2.3	2.6
Quick ratio (x)	0.4	0.3	0.4	0.4
Turnover & Leverage ratios (x)				
Gross asset turnover	5.9	6.0	5.6	5.4
Total asset turnover	1.5	1.5	1.4	1.4
Interest coverage ratio	9.8	29.4	30.4	29.9
Adjusted debt/equity	0.5	0.3	0.3	0.2
Valuation ratios (x)				
EV/Sales	6.6	4.5	3.7	3.3
EV/EBITDA	45.4	22.7	18.9	16.4
P/E	45.2	26.8	22.7	19.7
P/BV	13.8	12.5	9.7	7.7



Quarterly trend

Particulars	Q4FY09	Q1FY10	Q2FY10	Q3FY10	Q4FY10
Revenue (Rs mn)	3,439	4,389	5,756	5,176	5,092
YoY growth (%)	26.5	21.4	66.1	53.1	48.1
QoQ growth (%)	1.7	27.6	31.2	(10.1)	(1.6)
EBITDA (Rs mn)	673	864	1,119	1,014	1,075
EBITDA margin (%)	1,957.3	1,969.2	1,944.6	1,959.5	2,111.6
Adj net income (Rs mn)	587	697	930	851	918
YoY growth (%)	43.9	78.2	167.8	112.5	56.3
QoQ growth (%)	46.6	18.7	33.5	(8.5)	7.8

DuPont analysis

(%)	FY08	FY09	FY10E	FY11E	FY12E
Tax burden (Net income/PBT)	84.9	82.8	79.6	82.8	82.8
Interest burden (PBT/EBIT)	95.5	113.4	111.1	109.6	110.2
EBIT margin (EBIT/Revenues)	17.8	13.2	18.5	18.4	18.4
Asset turnover (Revenues/Avg TA)	178.0	150.2	147.3	143.2	137.2
Leverage (Avg TA/Avg equity)	421.9	251.2	208.8	201.3	187.9
Return on equity	108.5	46.9	50.3	48.1	43.4

Company profile

GCPL, a part of the Godrej group, is one of the mid-sized players in the Indian FMCG market. The group has been in the consumer goods business for the last 78 years, primarily engaged in soap and hair colour products. GCPL is a major player in the toilet soap and hair colour categories in the Indian FMCG market. It has a vast product range in its categories spread across various price points. Its brands include Godrej Liquid, powder hair dyes, Godrej Kesh Kala oil, Nupur hair dyes at the lower end and Renew and Coloursoft at the high end.

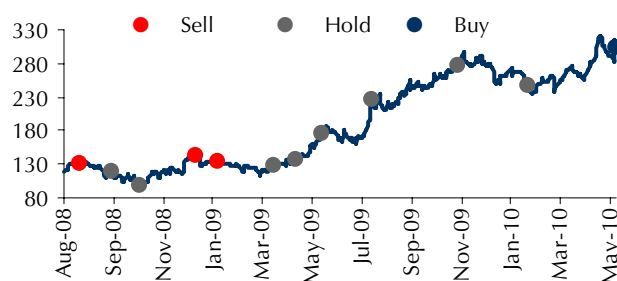
Shareholding pattern

(%)	Sep-09	Dec-09	Mar-10
Promoters	69.0	73.5	71.8
FII's	18.8	16.6	18.5
Banks & FI's	1.3	1.1	1.0
Public	10.9	8.8	8.7

Recommendation history

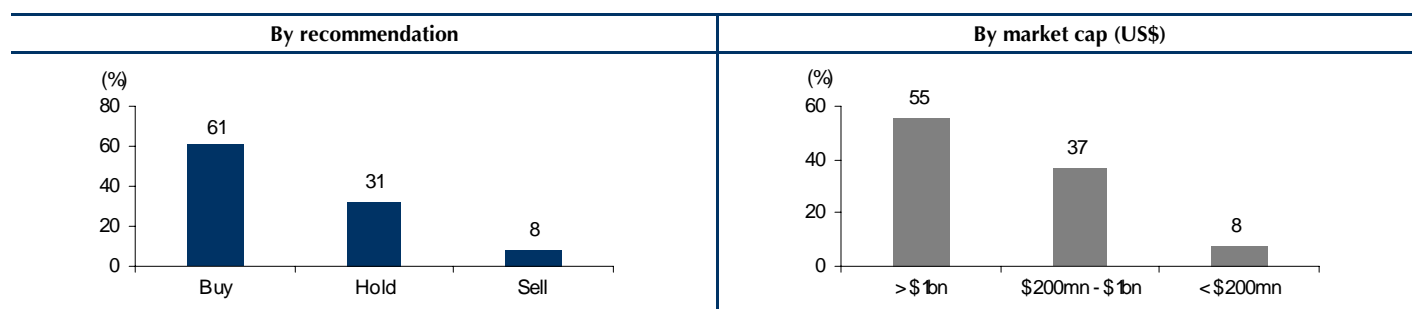
Date	Event	Reco price	Tgt price	Reco
21-Aug-08	RHH Compendium	132	137	Sell
26-Sep-08	Company Update	119	137	Hold
3-Nov-08	Results Review	99	118	Hold
2-Jan-09	Quarterly Preview	142	118	Sell
27-Jan-09	Results Review	135	130	Sell
6-Apr-09	Quarterly Preview	126	130	Hold
4-May-09	Results Review	137	139	Hold
28-May-09	Results Review	175	163	Hold
27-Jul-09	Results Review	225	228	Hold
3-Nov-09	Results Review	275	272	Hold
25-Jan-10	Results Review	247	282	Hold
10-May	Company Update	303	350	Buy

Stock performance





Coverage Profile



Recommendation interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and -5%
Sell	Less than -5%

Recommendation structure changed with effect from March 1, 2009

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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