



# Colgate Palmolive

BSE SENSEX 17,481	S&P CNX 5,258	<b>CMP: INR1,041</b>	<b>TP: INR827</b>	<b>Sell</b>								
Bloomberg Equity Shares (m)	CLGT IN 136.0	<b>YEAR</b>	<b>NET SALES</b>	<b>PAT</b>	<b>EPS</b>	<b>EPS</b>	<b>P/E</b>	<b>P/BY</b>	<b>ROE</b>	<b>ROCE</b>	<b>EV/</b>	<b>EV/</b>
52-Week Range (INR)	1,069/783	<b>END</b>	<b>(INR M)</b>	<b>(INR M)</b>	<b>(INR)</b>	<b>GR. (%)</b>	<b>(X)</b>	<b>(X)</b>	<b>(%)</b>	<b>(%)</b>	<b>SALES</b>	<b>EBITDA</b>
1,6,12 Rel. Perf. (%)	0/24/32	03/10A	19,625	4,038	29.7	39.1	-	-	156.1	154.0	-	-
M.Cap. (INR b)	141.6	03/11A	22,206	4,026	29.6	-0.3	35.2	36.9	114.1	114.3	6.2	26.0
M.Cap. (USD b)	2.9	03/12E	25,893	4,446	32.7	10.4	31.8	30.4	104.6	105.3	5.3	23.1
		03/13E	29,929	5,128	37.7	15.4	27.6	25.3	100.0	100.4	4.5	19.5

Colgate Palmolive's (CLGT) 2QFY12 results were in line with our estimates as PAT increased 7% to INR1,076m (against our estimate of INR1,085m). Strong volume growth of 15% in toothpastes drove overall 13% volume growth, but increased investment in new launches and aggressive promotion resulted in a 45% increase in ad-spends (up 310bp), which impacted profitability.

■ **2QFY12 results in line with estimates as adjusted PAT increases 7.2%:** Net sales grew 19.1% to INR6.6b (against our estimate of INR6.3b) due to overall volume growth of 13% and 15% volume growth in toothpaste. Gross margin declined 20bp YoY to 59.9% (against our estimate of 59.8%) due to higher input costs (up 30bp QoQ). Ad-spends increased 44% YoY to 17.4% of sales (up 310bp) led by new launches and aggressive sales promotion schemes. EBITDA margins thus declined 190bp to 20.9%. EBITDA increased 9% YoY to INR1.4b (against our estimate of INR1.4b). Adjusted PAT increased 7.2% to INR1,076m (against our estimate of INR1,085m). The tax rate was higher by 80bp at 22.9%. Reported PAT declined by 1% to INR997m due to one-time VRS and exceptional costs related to closure of its Hyderabad toothpowder factory.

■ **Valuations at a high, factor in structural positives; Maintain Sell with a target price of INR827, 21% downside:** We believe CLGT's strong positioning and single-segment focus make it a formidable competitor in the oral-care market and CLGT is likely to continue posting healthy double-digit growth over the medium term. We expect P&G to launch Oral B toothpaste in India. This will trigger fresh competition in the toothpaste market in India, which would have growth and margin implications for the entire oral-care segment. We increase our estimates for toothpaste volume growth from 12.5% to 14% but continued input cost pressures and higher ad-spends keep our estimates largely unchanged. We believe the stock, at 31.8x FY12E EPS of INR32.7 and 27.6x FY13E EPS of INR37.7, factors in all structural positives and it trades at a 25% premium to its five-year average P/E multiple. Maintain **Sell**.

Quarterly Performance									(INR Million)	
Y/E March	FY11				FY12				FY11	FY12E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
<b>Toothpaste Volume Gr %</b>	<b>14.0</b>	<b>12.0</b>	<b>13.0</b>	<b>13.0</b>	<b>14.0</b>	<b>15.0</b>	<b>14.0</b>	<b>13.0</b>	<b>13.0</b>	<b>14.0</b>
<b>Net Sales</b>	<b>5,288</b>	<b>5,518</b>	<b>5,582</b>	<b>5,818</b>	<b>6,111</b>	<b>6,572</b>	<b>6,497</b>	<b>6,712</b>	<b>22,206</b>	<b>25,893</b>
YoY Change (%)	13.0	13.2	13.8	12.6	15.6	19.1	16.4	15.4	13.2	16.6
COGS	1,967	2,201	2,160	2,393	2,467	2,637	2,573	2,584	8,720	10,260
<b>Gross Profit</b>	<b>3,321</b>	<b>3,316</b>	<b>3,422</b>	<b>3,425</b>	<b>3,644</b>	<b>3,936</b>	<b>3,924</b>	<b>4,128</b>	<b>13,486</b>	<b>15,633</b>
Gross Margin (%)	62.8	60.1	61.3	58.9	59.6	59.9	60.4	61.5	60.7	60.4
Other operating Expenses	1,932	2,195	2,675	2,176	2,471	2,706	2,738	2,640	8,979	10,555
% to sales	36.5	39.8	47.9	37.4	40.4	41.2	42.1	39.3	40.4	40.8
Other operating Income	209	175	184	195	183	183	210	223	767	799
<b>EBITDA</b>	<b>1,598</b>	<b>1,297</b>	<b>931</b>	<b>1,444</b>	<b>1,356</b>	<b>1,413</b>	<b>1,397</b>	<b>1,711</b>	<b>5,273</b>	<b>5,876</b>
Margins (%)	29.1	22.8	16.1	24.8	21.5	20.9	21.5	25.5	23.0	22.0
Depreciation	79	84	91	88	88	106	97	78	342	369
Interest	3	6	19	4	6	8	13	3	33	30
Financial other Income	54	81	92	78	120	95	120	115	301	450
<b>PBT</b>	<b>1,569</b>	<b>1,288</b>	<b>913</b>	<b>1,429</b>	<b>1,381</b>	<b>1,395</b>	<b>1,407</b>	<b>1,745</b>	<b>5,199</b>	<b>5,927</b>
Tax	350	285	250	288	377	319	394	392	1,174	1,482
Rate (%)	22.3	22.1	27.4	20.2	27.3	22.9	28.0	22.5	22.6	25.0
<b>Adj PAT</b>	<b>1,219</b>	<b>1,003</b>	<b>663</b>	<b>1,141</b>	<b>1,004</b>	<b>1,076</b>	<b>1,013</b>	<b>1,352</b>	<b>4,026</b>	<b>4,446</b>
YoY Change (%)	18.6	11.8	-37.4	8.1	-17.6	7.2	52.8	18.6	-0.3	10.4

E: MOSL Estimates

Colgate Palmolive's (CLGT) 2QFY12 results were in line with our estimates as PAT increased 7% to INR1,076m (against our estimate of INR1,085m). Strong volume growth of 15% in toothpastes drove 13% overall volume growth but increased investment in new launches and aggressive promotions resulted in a 45% increase in ad-spends (up 310bp) and impacted profitability.

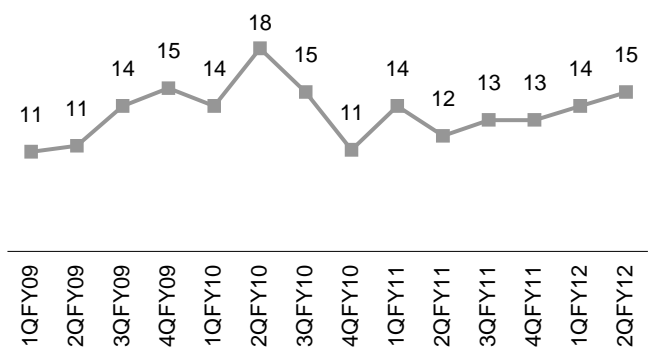
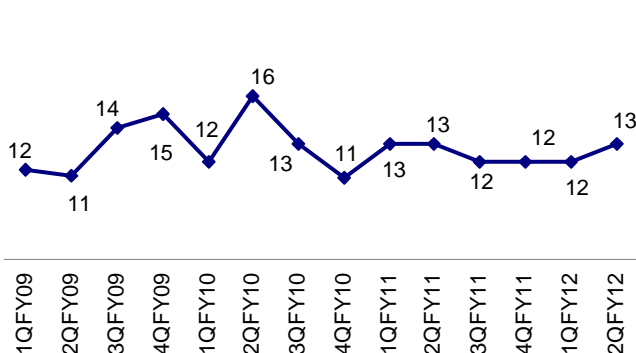
- We believe CLGT's strong positioning and single-segment focus make it a formidable competitor in the oral-care market and CLGT is likely to continue to post healthy double-digit growth over the medium term.
- The first half however reflects the impact of stiffer competition with CLGT having increased ad-spends by 310bp. We note that Colgate Sensitive Pro Relief and Sensodyne are competing aggressively in the nascent sensitive-toothpaste market. Besides, CLGT is aggressively promoting brands like CDC and Total, which would keep margins in check.
- We note that P&G has been aggressively expanding its Oral-B franchise across markets. Recent launches include Nigeria, Ghana and the UK. The Columbia launch is likely next year. It has achieved 5% share in Brazil (10% in channels it competes in). We believe that some of these markets are potentially much smaller than the Indian oral care market (USD1b) and we expect P&G to launch Oral B toothpaste in India. This will trigger fresh competition in the toothpaste market in India, which would have growth and margin implications for the oral-care segment.
- We increase our estimates for CLGT's toothpaste volume growth from 12.5% to 14% but continued input cost pressures (RM index at an all-time high) and higher ad-spends keep our estimates largely unchanged. We estimate CLGT's PAT CAGR at 13% over FY11-13, led largely by volume growth in the oral-care segment. We believe the stock, at 30.7x FY12E EPS of INR32.7 and 26.6x FY13E EPS of INR37.7, factors in all structural positives and trades at a 25% premium to its five-year average P/E multiple. **Maintain Sell.**

**2QFY12 results in line with estimates as adjusted PAT increases 7.2%**

- Net sales grew 19.1% to INR 6.6b (against our estimate of INR6.3b) due to overall volume growth of 13% and 15% volume growth in toothpastes. The oral-care category grew 20% in value terms in 2QFY12.
- CLGT's volume market share in toothpastes was 52.6% and it was 36.3% in toothbrushes over October 2010-September 2011. CLGT's mouthwash market share was 26.4%.

Overall volume growth 13%...

...led by 15% toothpaste volume growth



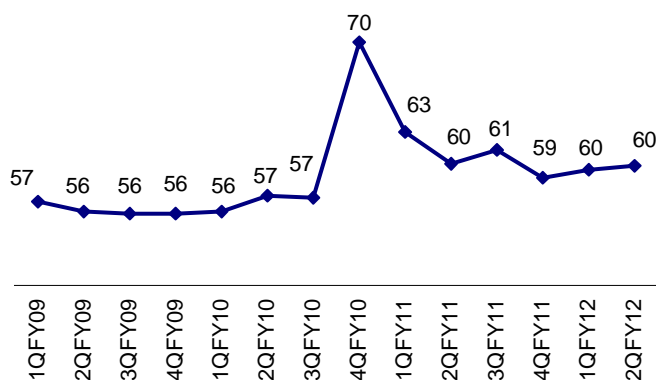
Source: Company/MOSL

- CLGT's gross margin declined 20bp YoY to 59.9% (against our estimate of 59.8%) due to higher input costs (up 30bp QoQ). Gross margin management has been good, aided by cost control, price increases and premiumisation. Ad-spends increased 44% YoY to 17.4% of sales (up 310bp) led by new launches and aggressive sales promotion schemes. EBITDA margins thus declined 190bp to 20.9%.
- EBITDA increased 9% YoY to INR1.4b (against our estimate of INR1.4b). Adjusted PAT increased 7.2% to INR1,076m (against our estimate of INR1,085m). The tax rate was higher by 80bp at 22.9%.
- Reported PAT declined by 1% to INR997m due to one-time VRS and exceptional costs related to closure of the Hyderabad toothpowder factory.

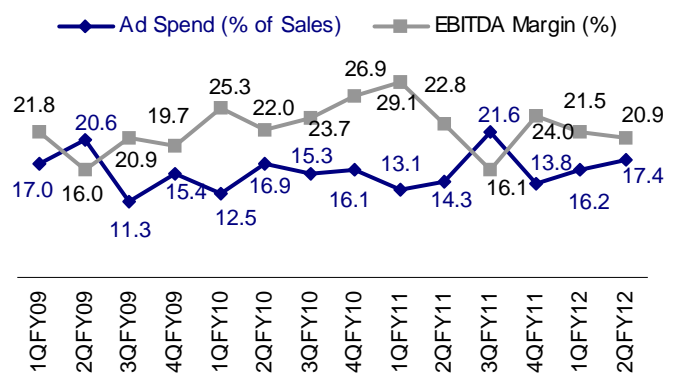
**Toothpaste volume growth strong at 15%; Investments in new oral-care launches impact profitability**

- 2QFY12 toothpaste volume growth remained strong at 15% led by aggressive investments across brands and the new launch of Colgate Sensitive Pro Relief. CLGT's growth was above industry volume growth, which has been 12-13%, and CLGT's 12-month average market share was 52.6% in volume terms. For toothbrushes CLGT's market share was sequentially lower by 370bp at 36.3%. However CLGT's market share by volume in the nascent mouthwash category rose 240bp QoQ to 26.4%.
- Price increases of ~4% YTD resulted in gradual improvement in gross margins. However, the full impact of this is likely to come through in 3QFY12. CLGT's input cost index has not softened and any improvement in gross margins is likely to be very gradual.
- We are increasing volume growth estimates to 14% for toothpastes (12.5% earlier) taking cognizance of CLGT's above-industry growth trajectory.
- The launch of sensitive oral-care products across its categories (Sensitive Pro-Relief in toothpastes, 360 Sensitive Pro-Relief toothbrush, Plax Sensitive mouthwash, 360 Surround) over the past two quarters resulted in A&P spends increasing by 310bp to 16.8% of sales in 1HFY12. Although we expect spends to fall marginally in 2HFY12, we increase our A&P spend assumption from 16% to 16.5% of sales, factoring in new launch expenses.

**Gross margins up 30bp QoQ (%)**



**EBITDA margins down 190bp as ad-spends expand (%)**



Source: Company/MOSL

**Valuations at a high, factor in structural positives; Maintain Sell with a target price of INR827, 21% downside**

- We believe CLGT's strong positioning and single-segment focus makes it a formidable competitor in the oral-care market and CLGT is likely to continue posting healthy double-digit growth over the medium term.
- We expect P&G to launch Oral B toothpaste in India. This will trigger fresh competition in the toothpaste market in India, which will have growth and margin implications for the entire oral-care segment.
- We increase our estimates for toothpaste volume growth from 12.5% to 14% but continued input cost pressures and higher ad-spends keep our estimates largely unchanged.
- We believe the stock, 31.8x FY12E EPS of INR32.7 and 27.6x FY13E EPS of INR37.7, factors in all structural positives and the stock trades at a 25% premium to its five-year average P/E multiple. Maintain **Sell**.

## Colgate Palmolive: an investment profile

### Company description

Colgate Palmolive (CLGT) is a market leader in the toothpaste segment with a market share of ~50% in India. Oral care is one of the most under-penetrated segments of the FMCG market with penetration of ~31% in toothpowder and ~57% in toothpaste. CLGT invested INR700m in a toothpaste facility in Baddi, Himachal Pradesh, which will accrue fiscal benefits until FY15.

### Key investment arguments

- CLGT maintains its leadership position in the oral-care market. It has maintained its market share over its main competitors.
- Volume growth continues to be strong with toothpaste growing in strong double digits, led by increasing conversions from toothpowder and improved penetration.

### Key investment risks

- P&G's entry in the oral-care market with its Crest/Oral B brands will intensify competition.
- A slowdown in toothpaste volume growth could affect CLGT as it is still a single-segment company.

### Recent developments

- CLGT affected a price increase of 1.5-2% on select brands/SKUs.
- CLGT amalgamated its subsidiary Professional Oral Care Products Private Ltd and CC Healthcare, another subsidiary, has filed a petition for amalgamation with the company with effect from 1 April 2009.

### Valuation and view

- Our EPS estimates remain largely unchanged at INR32.7 in FY12 and INR37.7 in FY13.
- The stock trades at 31.8x FY12E EPS of INR32.7 and 27.6x FY13E EPS of INR37.7. Maintain **Sell**.

### Sector view

- We have a cautious view on the sector due to pressure on consumer wallets.
- Companies with low competitive pressures and broad product portfolios will be able to better withstand a slowdown in a segment.
- Long-term prospects are bright, given rising income levels and low penetration.

### Comparative valuations

		Colgate	HLL	Nestle
P/E (x)	FY12E	31.8	33.6	41.1
	FY13E	27.6	29.7	34.5
EV/EBITDA (x)	FY12E	23.1	25.0	26.8
	FY13E	19.5	21.8	21.9
EV/Sales (x)	FY12E	5.3	3.5	5.4
	FY13E	4.5	3.1	4.4
P/BV (x)	FY12E	30.4	25.7	32.9
	FY13E	25.3	21.7	24.4

### Shareholding Pattern (%)

	Sep-11	Jun-11	Sep-10
Promoter	51.0	51.0	51.0
Domestic Inst	7.3	7.5	7.8
Foreign	19.6	19.2	16.5
Others	22.1	22.4	24.7

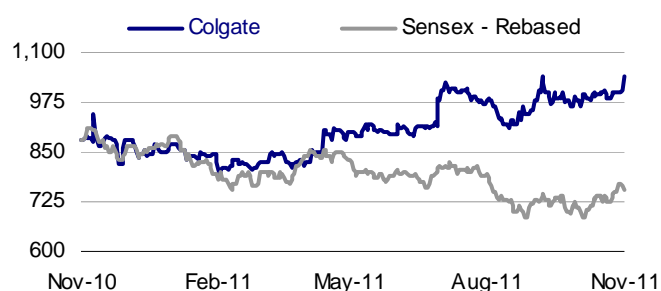
### EPS: MOSL forecast v/s Consensus (INR)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY12	32.7	31.9	2.6
FY13	37.7	36.8	2.5

### Target Price and Recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
1,041	827	-20.6	Sell

### Stock performance (1 year)



## Financials and Valuation

Income Statement						Ratios					
(INR Million)											
Y/E March	2009	2010	2011	2012E	2013E	Y/E March	2009	2010	2011	2012E	2013E
<b>Net Sales</b>	<b>16,948</b>	<b>19,625</b>	<b>22,206</b>	<b>25,893</b>	<b>29,929</b>	<b>Basic (INR)</b>					
Change (%)	15.0	15.8	13.2	16.6	15.6	<b>EPS</b>	<b>21.3</b>	<b>29.7</b>	<b>29.6</b>	<b>32.7</b>	<b>37.7</b>
COGS	7,413	7,768	8,720	10,260	11,801	Cash EPS	23.0	32.5	32.1	35.4	40.6
<b>Gross Profit</b>	<b>9,535</b>	<b>11,856</b>	<b>13,486</b>	<b>15,633</b>	<b>18,128</b>	BV/Share	15.9	24.0	28.2	34.2	41.2
Gross Margin (%)	56.3	60.4	60.7	60.4	60.6	DPS	15.0	20.0	22.0	22.9	26.4
Operating expenses	6,919	7,602	8,979	10,555	12,064	Payout %	70.3	64.3	73.8	70.0	70.0
Other Operating Income	760	758	767	799	855	<b>Valuation (x)</b>					
<b>EBITDA</b>	<b>3,376</b>	<b>5,012</b>	<b>5,273</b>	<b>5,876</b>	<b>6,919</b>	P/E			35.2	31.8	27.6
Change (%)	15.6	48.5	5.2	11.4	17.7	Cash P/E			32.4	29.4	25.6
Margin (%)	19.1	24.6	23.0	22.0	22.5	EV/Sales			6.2	5.3	4.5
Depreciation	229	376	342	369	394	EV/EBITDA			26.0	23.1	19.5
Int. and Fin. Charges	11	15	33	30	20	P/BV			36.9	30.4	25.3
Financial Other Income	318	227	301	450	520	Dividend Yield (%)			2.1	2.2	2.5
<b>Profit before Taxes</b>	<b>3,453</b>	<b>4,848</b>	<b>5,199</b>	<b>5,927</b>	<b>7,025</b>	<b>Return Ratios (%)</b>					
Change (%)	18.2	40.4	7.3	14.0	18.5	RoE	153.4	156.1	114.1	104.6	100.0
Margin (%)	20.4	24.7	23.4	22.9	23.5	RoCE	150.2	154.0	114.3	105.3	100.4
Tax	448	837	1,166	1,556	1,991	<b>Working Capital Ratios</b>					
Deferred Tax	103	-28	8	-74	-95	Debtor (Days)	2	2	7	6	6
Tax Rate (%)	16.0	16.7	22.6	25.0	27.0	Asset Turnover (x)	10.6	6.9	7.0	7.1	7.1
<b>Adjusted PAT</b>	<b>2,902</b>	<b>4,038</b>	<b>4,026</b>	<b>4,446</b>	<b>5,128</b>	<b>Leverage Ratio</b>					
Change (%)	25.2	39.1	-0.3	10.4	15.4	Debt/Equity (x)	0.0	0.0	0.0	0.0	0.0
Margin (%)	17.1	20.6	18.1	17.2	17.1						
Non-rec. (Exp)/Income	0	194	26	0	0						
<b>Reported PAT</b>	<b>2,902</b>	<b>4,233</b>	<b>4,052</b>	<b>4,446</b>	<b>5,128</b>						
<b>Balance Sheet</b>						<b>Cash Flow Statement</b>					
(INR Million)						(INR Million)					
Y/E March	2009	2010	2011	2012E	2013E	Y/E March	2009	2010	2011	2012E	2013E
Share Capital	136	136	136	136	136	OP/(loss) before Tax	3,376	5,012	5,273	5,876	6,919
Reserves	2,027	3,125	3,705	4,522	5,464	Int./Div. Received	318	227	301	450	520
<b>Net Worth</b>	<b>2,163</b>	<b>3,261</b>	<b>3,841</b>	<b>4,658</b>	<b>5,600</b>	Interest Paid	-11	-15	-33	-30	-20
Loans	47	46	1	1	1	Direct Taxes Paid	-448	-837	-1,166	-1,556	-1,991
Deferred Liability	-177	-179	-168	-175	-200	(Incr)/Decr in WC	-106	441	255	332	527
<b>Capital Employed</b>	<b>2,033</b>	<b>3,128</b>	<b>3,673</b>	<b>4,484</b>	<b>5,401</b>	<b>CF from Operation:</b>	<b>3,128</b>	<b>4,828</b>	<b>4,631</b>	<b>5,072</b>	<b>5,953</b>
Gross Block	4,253	5,345	5,798	6,098	6,598	(Incr)/Decr in FA	273	-1,108	-514	-322	-535
Less: Accum. Depn.	-2,513	-2,875	-3,248	-3,617	-4,010	(Pur)/Sale of Investmen	343	173	-177	-313	-300
<b>Net Fixed Assets</b>	<b>1,739</b>	<b>2,470</b>	<b>2,550</b>	<b>2,482</b>	<b>2,588</b>	<b>CF from Invest.</b>	<b>615</b>	<b>-935</b>	<b>-691</b>	<b>-635</b>	<b>-835</b>
Capital WIP	47	62	123	145	180	Change in Equity	20	44	16	0	0
Investments	383	210	387	700	1,000	(Incr)/Decr in Debt	0	-1	-45	1	0
<b>Curr. Assets, L&amp;A</b>	<b>5,377</b>	<b>5,907</b>	<b>7,044</b>	<b>8,293</b>	<b>9,698</b>	Dividend Paid	-2,381	-3,178	-3,489	-3,628	-4,185
Inventory	824	1,106	1,537	1,853	2,126	Others	-300	206	58	67	70
Account Receivables	111	98	430	426	492	<b>CF from Fin. Activi</b>	<b>-2,661</b>	<b>-2,929</b>	<b>-3,460</b>	<b>-3,561</b>	<b>-4,115</b>
Cash and Bank Balance	2,511	3,476	3,956	4,833	5,836	<b>Incr/Decr of Cash</b>	<b>1,082</b>	<b>964</b>	<b>480</b>	<b>876</b>	<b>1,003</b>
Others	1,930	1,228	1,122	1,181	1,245	Add: Opening Balance	1,430	2,511	3,476	3,956	4,833
<b>Curr. Liab. and Provi</b>	<b>5,513</b>	<b>5,521</b>	<b>6,432</b>	<b>7,136</b>	<b>8,065</b>	<b>Closing Balance</b>	<b>2,512</b>	<b>3,475</b>	<b>3,956</b>	<b>4,833</b>	<b>5,836</b>
Account Payables	3,417	3,740	4,213	4,738	5,319						
Other Liabilities	528	527	526	552	587						
Provisions	1,568	1,254	1,693	1,846	2,158						
<b>Net Current Assets</b>	<b>-136</b>	<b>387</b>	<b>612</b>	<b>1,157</b>	<b>1,633</b>						
<b>Application of Func</b>	<b>2,033</b>	<b>3,128</b>	<b>3,673</b>	<b>4,484</b>	<b>5,401</b>						

E: MOSL Estimates

**N O T E S**

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