

Godrej Consumer Products

Rising comfort on growth sustainability

We met the management of GCPL. Key takeaways:

3 growth pillars: Innovation, brand building, and distribution: GCPL's initiative to innovate home insecticide (HI) portfolio is fructifying into market share gains and improving margin profile of the category. New variants in soaps were supported by increase in above-the-line brand spend. While distribution reach has increased to 4.7 mn outlets in FY12 (vs. 4 mn outlets in FY11), the continued benefit of GHPL* and GCPL distribution merger (only 50% completed) is playing through. We expect the domestic portfolio to grow by 24% in FY13 (vs. 22% in FY12) led by 28% growth in Soaps and 25% growth in HI.

Stepping up international initiatives: We believe GCPL has now entered its next phase of international growth with integration issues largely dealt with (70% of international business has no involvement from local promoter). The company is now focused on geographical distribution expansion, new innovations (e.g. Hit Magic paper in HI, extension of Mitu Baby brand into shower gels, talc and oil segment in Indonesia) and cross selling of its products (launch of HI in Africa and LATAM) to scale up international business. We expect 35% international business CAGR (including Cosmetica Nacional and Darling consolidation) over FY12-14.

Softer Palm oil price and operating leverage to aid margin: Palm oil (~20% of RM) price has corrected by 23% (rupee term) from its peak over last 6 months and expected to remain weak in FY13 due to high global inventory. Growth in international business and mix improvement is further expected to aid margin expansion.

Raise multiple, target price; upgrade to BUY: Our conviction level on growth out performance has increased on the back of strong innovation funnel and unexplored distribution synergy with GHPL. Hence we raise our target PE multiple to 25x from 23x. Our TP stands revised to Rs 740 (Rs 660 earlier). **Upgrade to BUY.**

Financial summary (Consolidated)

Y/E	Net Sales	Adj. PAT	Consensus	EPS	Change	P/E	RoE	RoCE	EV/EBITDA	DPS
Mar	(Rs mn)	(Rs mn)	EPS* (Rs)	(Rs)	YoY (%)	(x)	(%)	(%)	(x)	(Rs)
2011	36,936	4,665	-	14.4	31	-	34.8	32.2	-	4.5
2012	48,662	6,033	-	17.7	23	-	26.6	23.3	-	4.9
2013E	63,305	8,183	22.1	24.0	36	29.3	26.4	25.6	20.2	6.0
2014E	76,674	10,033	26.9	29.5	23	23.8	26.7	28.7	16.1	7.0

Source: *Consensus broker estimates, Company, ENAM estimates

CMP (Rs)	703
Target price (Rs)	740
Potential upside	5%

Stock data

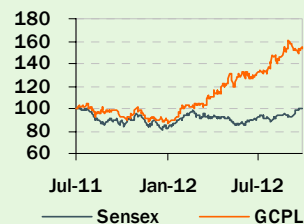
No. of shares (mn)	340
FV (Rs)	1/-
Market cap (Rs bn)	239
52 week high/low (Rs)	702/370
Avg. daily vol.* (shares)	381,600
BSE Code	532424
NSE Code	GODREJCP
Bloomberg code	GCPL IB
Reuters Code	GOCP.BO

* BSE & NSE 6 monthly

Shareholding (%)

	Jun-12	QoQ Chg
Promoter	64.0	0.0
FIIs	27.2	1.9
MFs / UTI	0.7	(0.7)
Banks / FIs	0.3	0.0
Others	7.8	(1.2)

Price performance



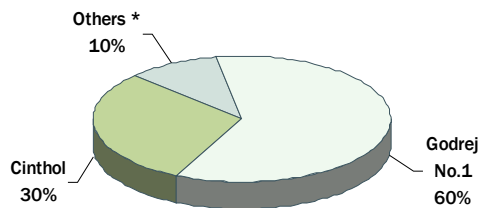
Source: Cline, ENAM Research

* GHPL : Godrej Household Products Limited (erstwhile Godrej Sara Lee JV)

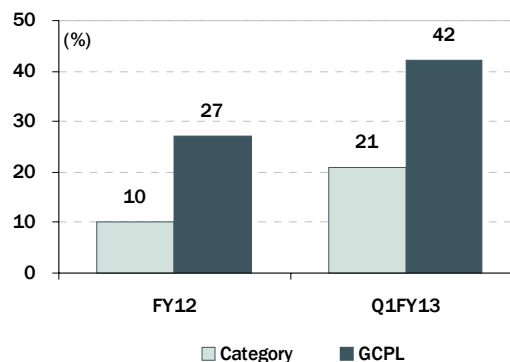
Personal wash (33% of standalone revenue):

- **FY12 growth:** As per AC Nielsen, growth in soaps category has been 10-12% (volume growth of 2-3%) in FY12. However, GCPL believes the category growth was higher by 200-300 bps at 12-15% (volume growth of 3-5%). For GCPL, a mix of price-led growth (~12% in FY12) and volume growth (16-18% in FY12) led to 27% revenue growth in FY12.
- **Price-based competition unlikely:** GCPL doesn't expect price-based competition in soaps due to lower palm oil prices but expects higher regional competition, higher freebies and increased promotions. No increase in regional competition seen thus far.
- **Cost pressure to ease in short term, but trend upwards in Long Term:** Palm oil constitutes almost ~20% of GCPL's RM cost. Price of Palm oil (i.e. PFAD - Palm Fatty Acid Distillate) has corrected 23% from its peak over last 6 months in rupee terms due to inventory build up in Malaysia and Indonesia. GCPL has already contracted its Palm oil supplies for next few months at prevailing prices. Since it takes about 2 quarter for lower input price to reflect in financial performance, we expect gross margin for standalone business to gradually improve during the year. We expect no price hikes in soap portfolio this year. However, the base effect of price hikes in FY12 will aid realization improvement of ~10% in FY13.
- **Variants strategy plays out:** Growth in Godrej No. 1 (~60% of soaps revenue) and Cinthol (~30% of soaps revenue) was been driven by constant improvement in variants. Godrej No. 1 soap currently has 7 regular variants. In fact, 5 non-performing variants were weeded out last year as company's consumer research insight indicates more preference towards natural ingredients as against fruits and flower variants. Apart from the regular variant of Cinthol, the premium offering of Cinthol Deo (in Aqua, Classic, Cologne, Musk and Sport) has done well. Godrej No.1 brand has grown 200 bps faster than Cinthol.
- **Under invested in the past, but stepped up in the last 2 years:** Increase in brand investment for Godrej No. 1 has aided growth. According to the management, GCPL has grabbed market share from both regional and national players in soaps. HUL grew 9% vs. 27% for GCPL in FY12.

GCPL's domestic soaps sales mix



Soaps ahead of category growth

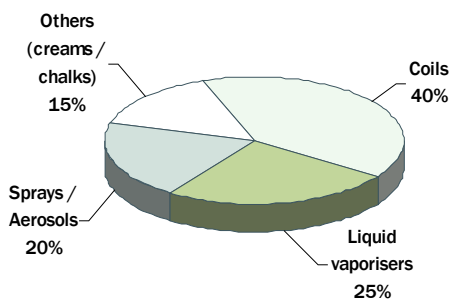


Source: Company, ENAM Research, * Fairglow / Evita / Vigil

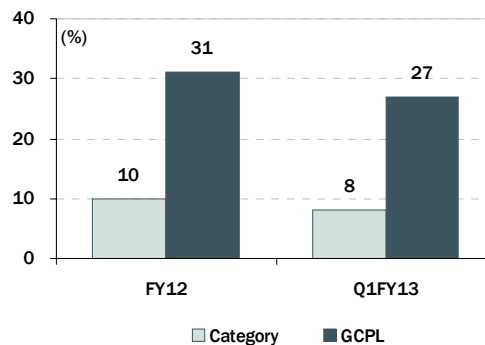
Household insecticide (~45% of standalone revenue):

- **Penetration levels in coils are flattening out and growth will mainly come from electric, spray and aerosols.** Innovation, branding and distribution have helped GCPL’s HI portfolio to grow 31% YoY (vs. category growth of 10%) in FY12. GCPL has recently taken average 3-4% price increase in its domestic household insecticide portfolio.
- **GCPL has been the leader in HI innovations:** GCPL had introduced Goodknight Advanced low smoke coil about 4-5 years back and Goodknight Advanced Active Plus liquid vapourizer about 3 years back. Both the products have changed the market landscape and helped GCPL gain share. While low smoke coils have lower trade margin and priced 15% higher than regular Goodknight coils, demand pull from consumers was led by perceived health and low irritation benefit. Low smoke coils now contribute 45-50% of GCPL’s coil portfolio. Similarly, Advance Active Plus liquid vapourizer value proposition (higher intensity) has also gained consumer acceptance. It now dominates the liquid vaporizer segment with over 60% revenue share.
- **Reckitt launches me-too low smoke coil:** Reckitt Benckiser recently launched the low smoke coil under Mortein Naturgard brand. However, GCPL has first mover advantage and 5-year lead in the segment over the competition.
- **Changing terms of trade and category margin profile:** The low smoke coil has significantly lower trade discounts at ~6% vs. regular coils at ~24%. Thus, growth in low smoke coils will improve margin profile and increase capability to invest behind brands.

GCPL domestic HI sales mix



HI growth ahead of category growth

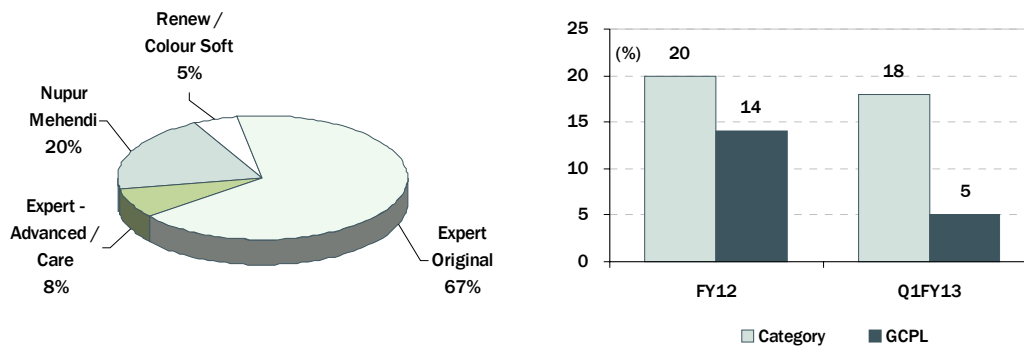


Source: Company, ENAM Research

Hair Color (~11% of standalone revenue):

- Underperforming category growth: Hair color has about 50% penetration in India. Growth has been driven by crème-based hair color (40% of the value market). GCPL is largely present in the economy segment with its powder hair color (~90% of portfolio). Consequently, growth in hair color has been muted at 14% in FY12 (vs. 20% growth in the category), below company expectation.
- To launch crème sachets to premiumize portfolio: According to the management, there exists a gap in the current market offering i.e. powder hair color at Rs 15 per use and crème-based products like L’Oreal starting at Rs 60 per use (4x the price difference). GCPL is looking at introducing new crème sachets (based on technology of its Argentinean subsidiary) between this price gaps. Initial R&D into the same has been already conducted with encouraging results. The company may soon launch the product under one of its existing hair color brand or launch a completely new brand. The management expects high margin similar to its current hair colour portfolio in its new crème sachets offering.

GCPL Domestic hair color sales mix Hair color growth below category growth

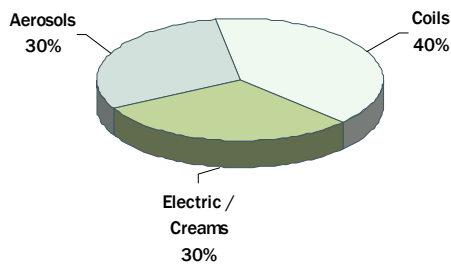


Source: Company, ENAM Research

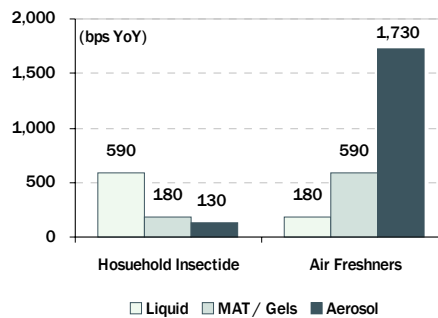
International markets (~40% of consolidated revenue):

- **Phase II of Darling consolidation completed:** GCPL recently completed phase II of Darling acquisition that will result in 65-70% revenue consolidation of Darling group vs. 45% consolidation earlier. Kenya hair extension business along with exports to certain East African geographies (such as Ethiopia, Rwanda, Tanzania, Uganda, and Ghana) will be merged during the phase.
- **Megasari growth led by innovation and distribution expansion:**
- Megasari has grown 20% in constant currency in FY12. The strong growth has been driven by initiatives such as: (a) increasing depth in distribution reach in the main Java & Sumatra Island and expanding into new areas of other Indonesian islands as well, (b) innovations such as Hit Magic Paper and one push aerosol, and (c) extending into adjacencies – extension of Mitu brand into Baby oils, Talcum powder and shower gels. Competitive dynamics is stable for Megasari with share gains in household insecticide (130-590 bps gain across format in FY12) and air freshners (180-1730 bps gain across format in FY12).
- **African opportunity set to get larger with HI launch by end of FY13:** GCPL plans to launch its household insecticide portfolio in Africa by end of FY13 and in LATAM in FY14. The HI market in Africa and LATAM is estimated to be about USD ~700 mn each in CY11/FY12. The enhanced geographical footprints and larger product basket shall help drive revenue growth from Africa.
- **International margin profile to improve on operating leverage:** Benefit of scale in Megasari and better margin profile in Darling group and recently acquired Cosmetica Nacional is expected to drive improvement in international EBITDA margin for GCPL.

Indonesian HI category split



Market share gain in Indonesia (FY12)



Source: Company, ENAM Research

International business revenue trend

(Rs mn)	Q1FY12	Q2FY12	Q3FY12	Q4FY12	Q1FY13	Q2FY13E	Q3FY13E	Q4FY13E
Total Int'l Revenue	3,600	4,190	5,660	5,190	6,030	6,712	7,842	7,228
YoY%	94	24	69	50	68	60	39	39
Asia -Megasari	1,940	2,300	2,500	2,550	2,710	2,944	3,050	3,060
YoY%	134	26	35	31	40	28	22	20
Asian - Middle East	50	60	50	60	70	72	60	72
YoY%	25	50	25	50	40	20	20	20
Africa	430	650	1,860	1,280	1,440	1,780	2,732	2,036
YoY%	26	48	251	184	235	314	47	59
Latam	560	650	820	820	1,080	1,280	1,484	1,484
YoY%	367	10	30	28	93	129	81	81
UK	620	530	430	480	730	636	516	576
YoY%	17	10	43	23	18	20	20	20

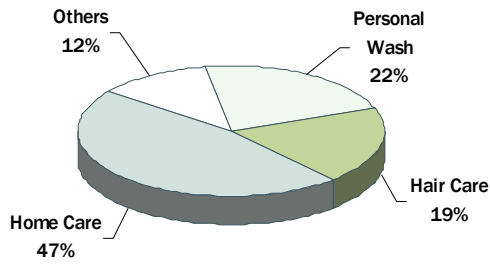
Source: Company, ENAM Research

International business EBITDA trend

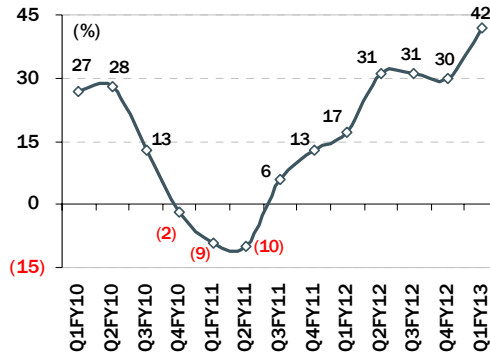
(Rs mn)	Q1FY12	Q2FY12	Q3FY12	Q4FY12	Q1FY13	Q2FY13E	Q3FY13E	Q4FY13E
EBITDA	462	722	1191	959	829	1,177	1,516	1,359
% of sales	13	17	21	18	14	18	19	19
Megasari	322	446	515	528	488	565	641	655
% of sales	17	19	21	21	18	19	21	21
Africa	40	169	577	247	274	409	683	387
% of sales	9	26	31	19	19	23	25	19
Latam	10	48	74	134	(28)	128	163	252
% of sales	2	7	9	16	(3)	10	11	17
Other Geographies	90	58	26	50	95	74	29	65
% of sales	13	10	5	9	12	11	5	10

Source: Company, ENAM Research

Consol. revenue mix - FY12

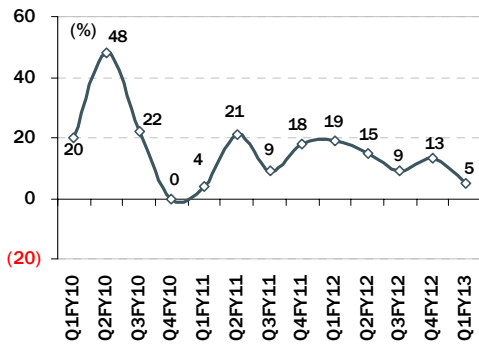


Soaps: Domestic sales growth

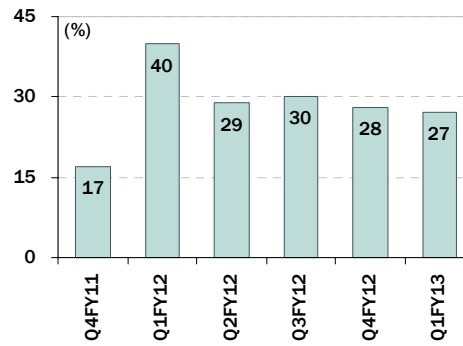


Source: Company

Hair Color: Domestic sales growth

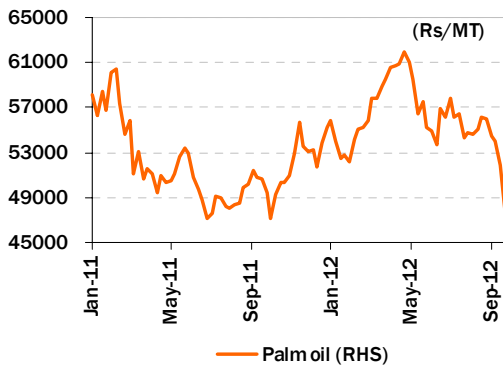


Insecticides: Domestic sales growth

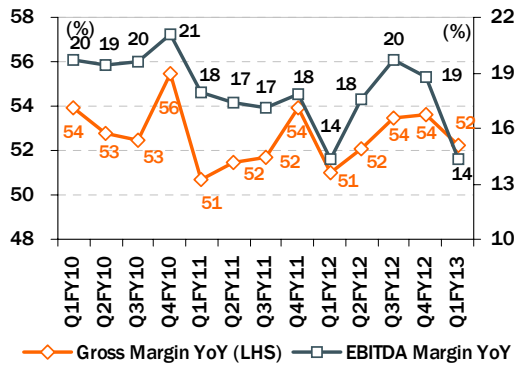


Source: Company, ENAM Research

Palm oil prices corrects sharply

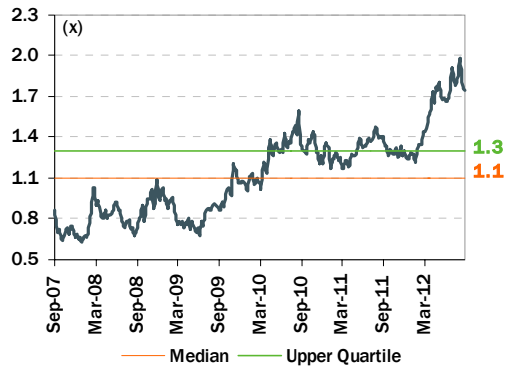


Margin trend (consolidated)

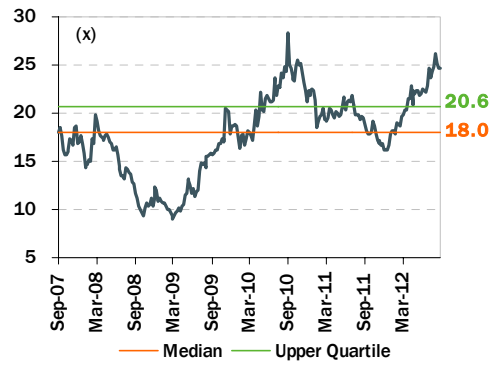


Source: Company, ENAM Research

GCPL P/E relative to Sensx P/E



GCPL - 1-yr rolling forward P/E



Source: ENAM Research, Bloomberg

ENAM Securities Direct Pvt. Ltd.

201, Laxmi Towers, 'A' Wing, Bandra-Kurla Complex, Bandra East, Mumbai - 400 051.

Board: 6680 3600 **Helpline:** 6680 ENAM **Fax :** 6680 3700

Website: www.enam.com / www.enamdirect.in **Email:** directresearch@enam.com

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Main/Dealing office:

Solaris,"C" Bldg., 6th floor, Opp. L&T Gate No. 6, Saki Vihar Road, Powai, Mumbai-400072, Tel No.-18001030808,

Compliance Officer Details:

Name: AnandShaha, E-Mail ID: compliance.officer@axisdirect.in, Tel No: 022-40754152.

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