

Colgate-Palmolive (India)

NEUTRAL

Re-rating is unwarranted

Colgate's 2Q performance was weaker than anticipated. Company has arrested market share decline but that is only half the job. Oral care category growth lags sector growth and hence Colgate needs to gain share to justify re-rating in the stock. We cut EPS by 1-3% and value the co. at 35x on Sep-21 EPS, arriving at a TP of Rs 1,400. Maintain NEUTRAL.

HIGHLIGHTS OF THE QUARTER

- Revenue grew by 4.5% (vs. exp. of 5.5%) driven entirely by volume growth. Volume growth was sluggish given (a) Slowdown in rural (now trailing urban), (b) Absence of share gains despite 27% growth in A&P and (c) Slow-moving category growth (trails FMCG sector by 2-3%). Competitive intensity remains high particularly in LUPs (Rs 10/pack).
- Naturals growth has now tapered to mid-teens from 25-30% range as it has attained a meaningful share (>25% mix in oral care category). Within naturals, Colgate has gained market share (8.1% in CY18 vs. 6.5-7% in CY17) led by Swarna Vedshakti and re-launch of Colgate Salt. Colgate has recently launched Colgate Charcoal to capitalize on naturals fad.
- Premium segment (4% mix vs. 8% mix earlier) has now returned to growth but is not enough to compensate for

Financial Summary

YE March (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	FY18	FY19	FY20E	FY21E	FY22E
Net Revenues	12,218	11,680	4.6	10,849	12.6	41,880	44,646	47,655	51,978	56,929
EBITDA	3,230	3,296	(2.0)	2,998	7.7	11,125	12,361	13,223	14,992	16,991
APAT	2,441	1,964	24.3	1,691	44.3	6,816	7,502	8,784	10,138	11,643
Diluted EPS (Rs)	9.0	7.2	24.3	6.2	44.3	25.0	27.6	32.3	37.2	42.8
P/E (x)						62.5	56.8	48.5	42.0	36.6
EV / EBITDA (x)						37.9	34.1	31.7	27.7	24.2
Core RoCE (%)						64.4	67.2	74.4	83.3	96.5

Source: Company, HDFC sec Inst Research

moderation in growth in other segments. Co. has re-launched Colgate Total to capitalize on this trend.

- GM were flat as co reinvested benefits from benign commodity inflation into higher promotions. A&P/Other expenses grew by 27/-1% which resulted in 2% de-growth in EBITDA (vs. exp of 7%). New management's focus is on spending aggressively on A&P (~14% of sales) at the cost of margins to drive market share gains. Lower corp. taxes resulted in 24% growth in APAT to Rs 2.44bn (exp Rs 2.65bn).

STANCE

Colgate's market share has largely stabilized but we still don't see signs of gaining meaningful share anytime soon. As a category leader, Colgate needs to drive category growth at a time when natural's fad is moderating. New management (Ram Raghavan - MD and Mukul Deoras - India chairman) keeps us interested in the story. Ram began his career as a management trainee with Colgate India in 1997. His recent experience as the head of innovation center at Colgate-Palmolive LATAM is exactly what Colgate India needs i.e. product excitement and diversification. Thereby, we model revenue/EBITDA CAGR of ~9/13% over FY20-22E. We don't expect a re-rating in the stock owing to modest earnings expectation. We maintain NEUTRAL.

INDUSTRY	FMCG
CMP (as on 24 Oct 2019)	Rs 1,565
Target Price	Rs 1,400
Nifty	11,583
Sensex	39,020
KEY STOCK DATA	
Bloomberg	CLGT IN
No. of Shares (mn)	272
MCap (Rs bn) / (\$ mn)	426/5,988
6m avg traded value (Rs mn)	652
STOCK PERFORMANCE (%)	
52 Week high / low	Rs 1,590/1,075
	3M 6M 12M
Absolute (%)	35.4 29.6 41.2
Relative (%)	32.3 29.7 26.5
SHAREHOLDING PATTERN (%)	
	Jun-19 Sep-19
Promoters	51.00 51.00
FIs & Local MFs	10.26 11.37
FPIs	15.14 15.46
Public & Others	23.60 22.17
Pledged Shares (% of total shares)	- -
Source : BSE	

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Revenue growth of 4.5% (exp 5.5%) was driven by 4% volume growth (4% exp.)

Colgate's market share has begun to stabilize

Oral care category is growing at ~4% volume growth

Gross margins were flat owing higher promotions

Co is aggressively investing in A&P spend to drive market share gains

APAT growth was driven by lower corp tax rates

Quarterly Financials

Particulars (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	FY19	FY18	YoY (%)
Net Revenue	12,218	11,680	4.6	10,849	12.6	44,624	41,880	6.6
Material Expenses	4,308	4,115	4.7	3,704	16.3	15,586	14,899	4.6
Employee Expenses	819	764	7.2	835	(1.9)	2,959	3,059	(3.3)
ASP Expenses	1,758	1,389	26.5	1,513	16.2	5,647	5,268	7.2
Other Operating Expenses	2,104	2,116	(0.6)	1,799	16.9	8,072	7,528	7.2
EBITDA	3,230	3,296	(2.0)	2,998	7.7	12,361	11,125	11.1
Depreciation	504	398	26.6	499	1.1	1,592	1,565	1.7
EBIT	2,726	2,897	(5.9)	2,500	9.0	10,769	9,560	12.6
Other Income	86	86	(0.1)	152	(43.1)	377	387	(2.6)
PBT	2,812	2,984	(5.8)	2,651	6.1	11,146	9,947	12.1
Exceptional	-	-	na	-	na	305	(117)	
PBT after exceptional	2,812	2,984	(5.8)	2,651	6.1	11,451	9,830	16.5
Tax	347	1,020	(66.0)	937	(63.0)	3,670	3,097	18.5
RPAT	2,441	1,964	24.3	1,691	44.3	7,756	6,734	15.2
Adjustments	-	-	na	-	na	(254)	83	na
APAT	2,441	1,964	24.3	1,691	44.3	7,502	6,816	10.1
EPS (adjusted)	9.0	7.2	24.3	6.2	44.3	27.6	25.1	10.1

Source: Company, HDFC sec Inst Research

Margin Analysis

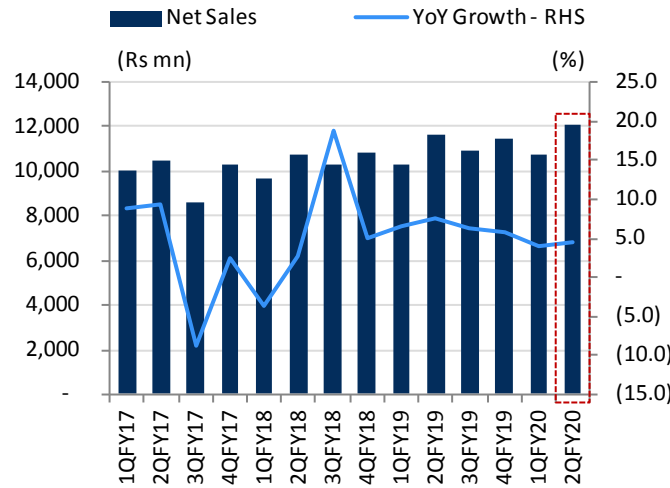
Particulars	2QFY20	2QFY19	YoY (bps)	1QFY20	QoQ (bps)	FY19	FY18	YoY (bps)
Material Expenses % Net Sales	35.3	35.2	2	34.1	112	34.9	35.6	(65)
Employee Expenses % Net Sales	6.7	6.5	16	7.7	(99)	6.6	7.3	(67)
ASP Expenses % Net Sales	14.4	11.9	250	13.9	44	12.7	12.6	8
Other Operating Expenses % Net Sales	17.2	18.1	(90)	16.6	63	18.1	18.0	11
EBITDA Margin (%)	26.4	28.2	(178)	27.6	(120)	27.7	26.6	113
Tax Rate (%)	12.3	34.2	(2,186)	35.3	(2,302)	32.0	31.5	55
APAT Margin (%)	20.0	16.8	317	15.6	439	17.4	16.1	130

Source: Company, HDFC sec Inst Research

Volume growth was sluggish given (a) Slowdown in rural (now trailing urban), (b) Absence of share gains despite 27% growth in A&P and (c) Slow-moving category growth (trails FMCG sector by 2-3%).

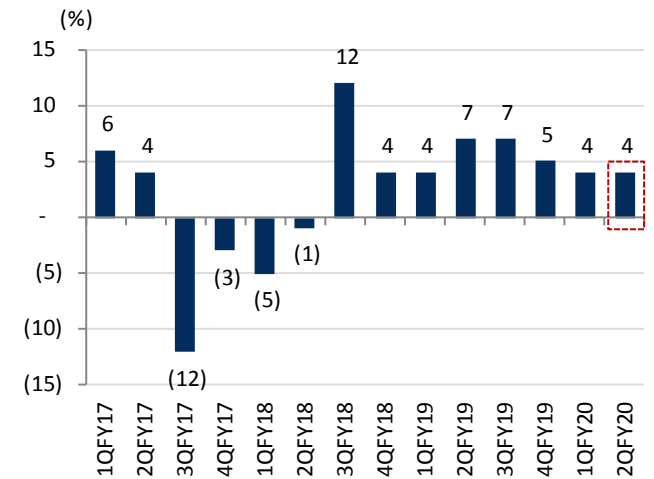
Gross margins remain under pressure as promotion intensity remains high

Net Revenue



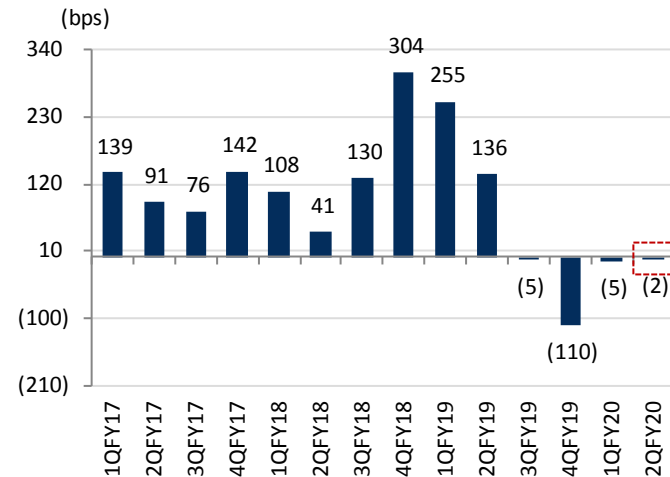
Source: Company, HDFC sec Inst Research
Note: 1QFY16-4QFY16 growth is based on old AS

Volume Growth



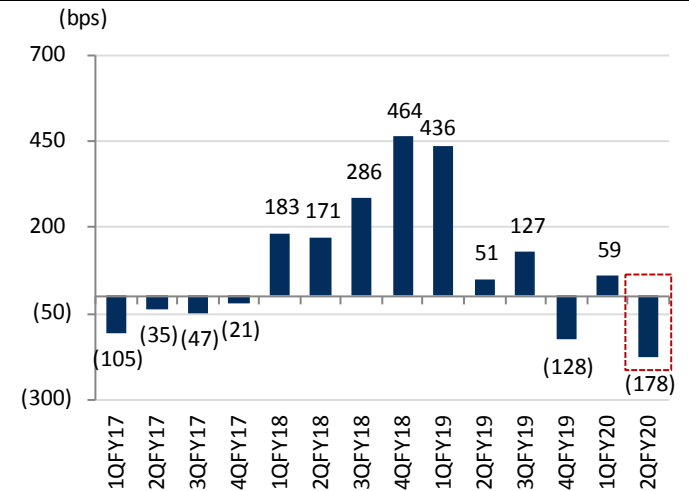
Source: Company, HDFC sec Inst Research

Gross Margin Change



Source: Company, HDFC sec Inst Research
Note: 1QFY16-4QFY16 change is based on old AS

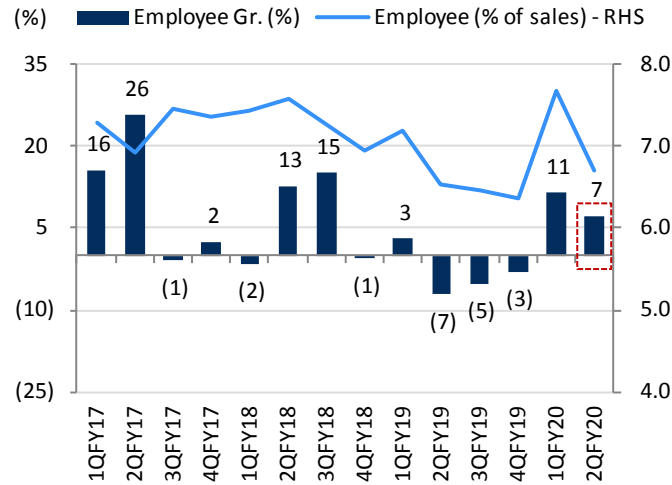
EBITDA Margin Change



Source: Company, HDFC sec Inst Research
Note: 1QFY16-4QFY16 change is based on old AS

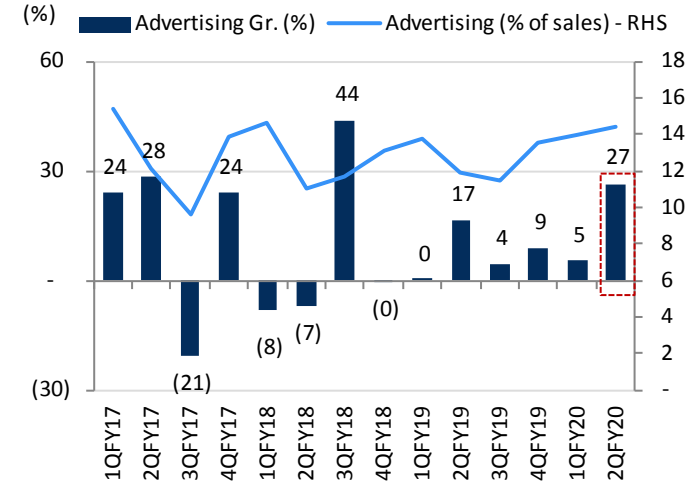
Colgate has rationalised its other expenses and is investing aggressively in A&P

Employee Expense



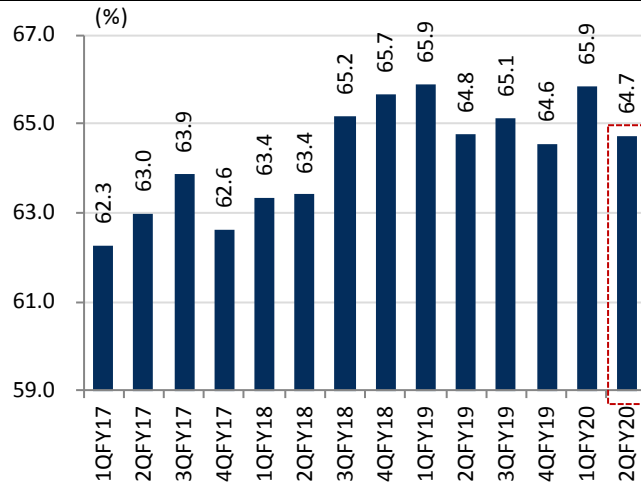
Source: Company, HDFC sec Inst Research
 Note: 1QFY16-4QFY16 growth is based on old AS

Advertising Expense



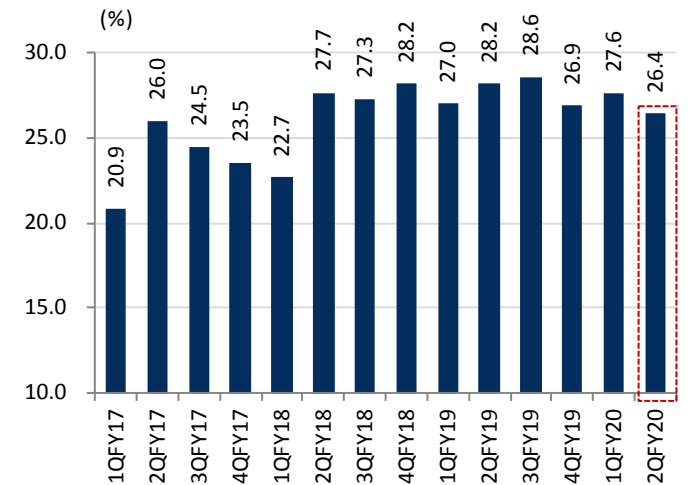
Source: Company, HDFC sec Inst Research
 Note: 1QFY16-4QFY16 growth is based on old AS

Gross Margin



Source: Company, HDFC sec Inst Research

EBITDA Margin



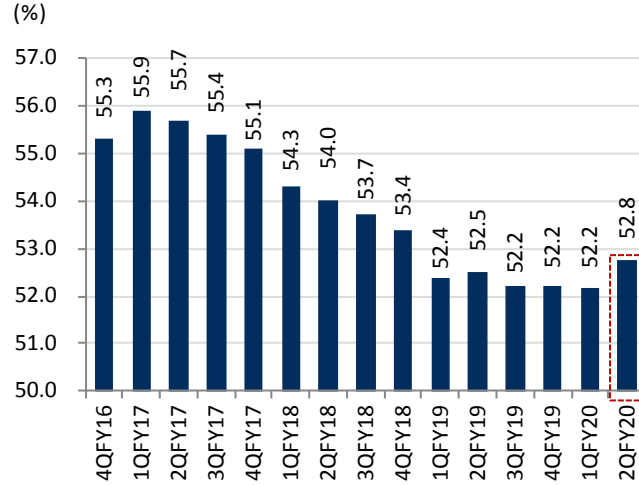
Source: Company, HDFC sec Inst Research

Market share declines in the last 2 years for Colgate in toothpaste have come from its premium segment (Colgate Sensitive and Colgate Total). The premium segment revenue contribution is at ~4% vs. ~8% earlier

Market share has now largely stabilized at ~52%

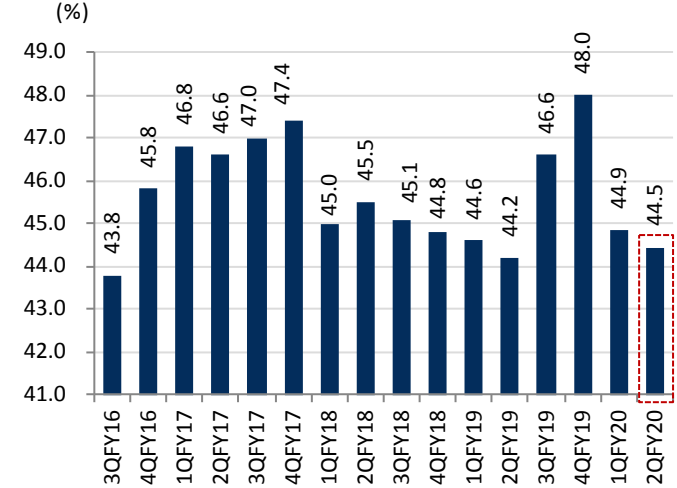
Colgate continued to face intense competition in the naturals segment (25% mix for industry) which is dominated by Dabur and Patanjali (80% combined share)

Colgate's Toothpaste Market Share



Source: Company, HDFC sec Inst Research

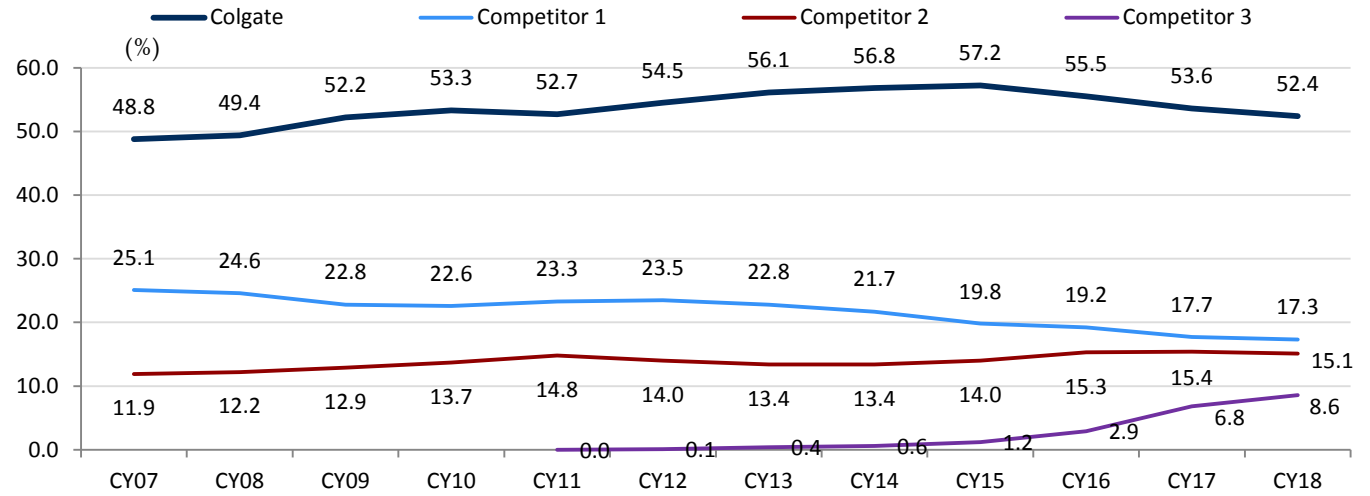
Colgate's Toothbrush Market Share



Source: Company, HDFC sec Inst Research

Sharp decline in toothpaste market share during CY15-18 has started stabilizing

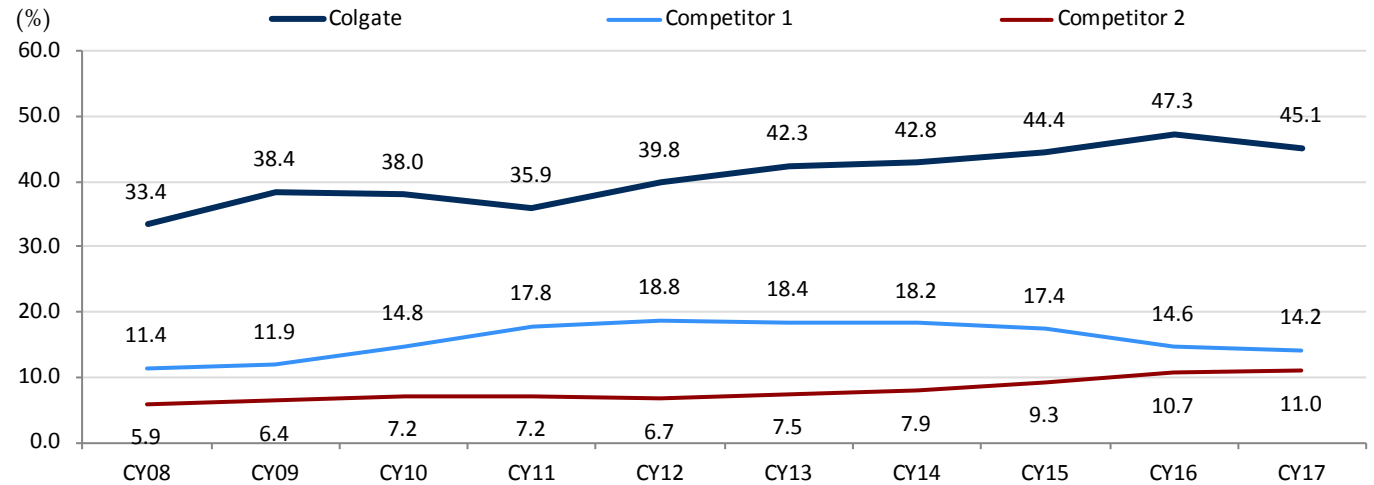
Toothpaste Market Share



Source: Company, HDFC sec Inst Research

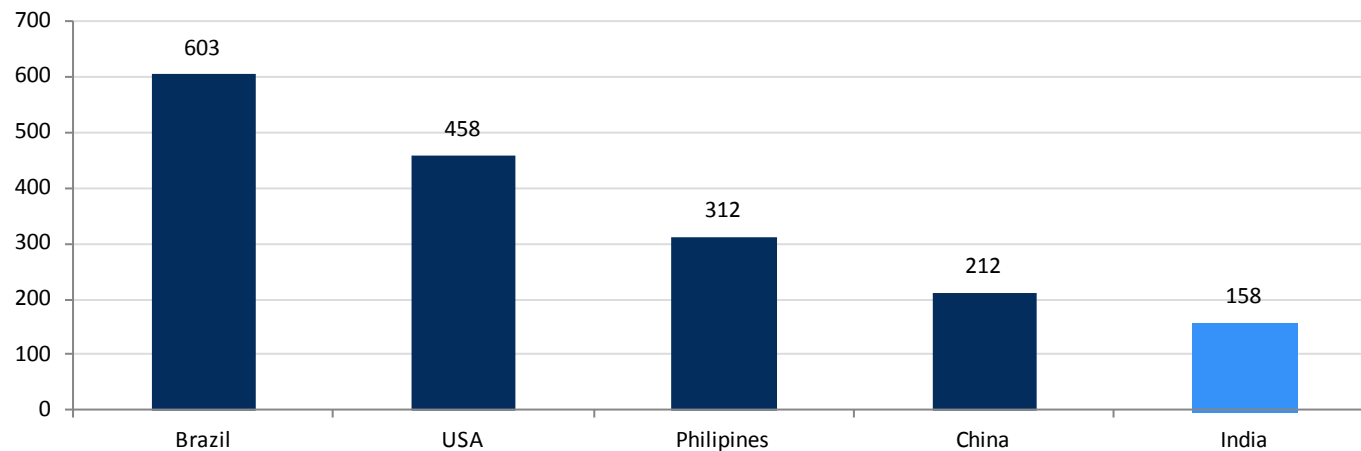
Toothbrush exit volume market share in Mar'19 was at ~48%

Toothbrush Market Share



Source: Company, HDFC sec Inst Research

Per Capita Consumption



Source: Company, HDFC sec Inst Research

Assumptions

	FY18	FY19	FY20E	FY21E	FY22E
Toothpaste revenue growth	7.4	6.8	6.3	8.6	9.1
Toothpaste volume growth	2.5	5.8	5.3	7.0	7.0
GM (%)	64.4	65.1	65.4	66.0	66.5
Employee (% of sales)	7.3	6.6	6.8	6.6	6.5
ASP (% of sales)	12.6	12.7	13.8	13.7	13.6
Distribution (% of sales)	3.1	3.0	3.0	3.0	3.0
Royalty (% of sales)	4.9	4.9	4.9	4.9	4.9
Other expenses (% of sales)	9.9	10.2	9.1	8.9	8.6
EBITDA Margin (%)	26.6	27.7	27.7	28.8	29.8
Tax Rate (%)	31.5	32.1	25.2	25.2	25.2

Source: Company, HDFC sec Inst Research

We cut EPS by ~1-3% to factor slower than expected recovery in FY20.

Change In Estimates

	NEW			OLD			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Net Sales	47,655	51,978	56,929	47,655	51,978	56,929	0.0%	0.0%	0.0%
EBITDA	13,223	14,992	16,991	13,453	14,957	16,767	-1.7%	0.2%	1.3%
PAT	8,784	10,138	11,643	9,045	10,205	11,541	-2.9%	-0.7%	0.9%
EPS	32.3	37.2	42.8	33.2	37.5	42.4	-2.9%	-0.7%	0.9%

Source: HDFC sec Inst Research

Peer Set Comparison

Company	MCap (Rs bn)	CMP (Rs)	Reco.	TP (Rs)	EPS (Rs)			P/E (x)			EV/EBITDA (x)			Core RoCE (%)		
					FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
HUL	4,544	2,133	NEU	2,017	28.1	34.3	42.2	75.8	62.2	50.6	51.2	46.3	35.7	248.6	38.7	28.0
ITC	2,790	249	BUY	368	10.4	12.9	14.0	23.9	19.2	17.8	15.1	13.7	12.2	39.2	46.3	49.1
Nestle	1,448	15,020	NR	13,640	167.1	233.6	278.1	89.9	64.3	54.0	52.1	44.7	38.3	82.1	114.7	137.3
Dabur	828	470	BUY	490	8.2	9.5	11.4	57.3	49.3	41.2	46.1	39.6	34.2	50.1	52.9	58.3
Britannia	788	3,283	BUY	3,594	48.1	58.6	71.9	68.3	56.0	45.7	44.7	40.5	33.1	39.2	43.1	49.8
Marico	510	395	NEU	400	7.2	8.7	10.4	54.8	45.4	38.0	39.7	31.9	27.7	48.8	47.4	53.4
Colgate	426	1,565	NEU	1,400	27.6	32.3	37.2	56.8	48.5	42.0	34.1	31.7	27.7	67.2	74.4	83.3
Emami	156	336	BUY	468	11.0	13.0	14.7	30.5	25.9	22.9	20.6	18.2	15.9	21.5	26.5	32.0
Jub. Food	203	1,540	BUY	2,134	24.1	33.2	42.1	63.9	46.4	36.5	32.8	28.8	22.4	45.8	35.5	25.8
United Spirits	442	609	BUY	754	10.2	11.8	16.9	59.5	51.6	36.0	34.4	28.7	23.1	15.8	18.2	22.8
Radico Khaitan	42	312	BUY	496	14.1	17.8	21.5	22.1	17.5	14.5	12.8	11.3	9.5	11.5	13.8	15.3

Source: HDFC sec Inst Research

Income Statement

(Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
Net Revenues	41,880	44,646	47,655	51,978	56,929
Growth (%)	5.2	6.6	6.7	9.1	9.5
Material Expenses	14,901	15,586	16,054	17,405	18,838
Employee Expense	3,059	2,959	3,214	3,505	3,839
ASP Expense	5,268	5,647	6,576	7,121	7,742
Distribution Expense	1,315	1,339	1,430	1,559	1,708
Other Expenses	6,211	6,755	7,158	7,395	7,811
EBITDA	11,125	12,361	13,223	14,992	16,991
EBITDA Growth (%)	17.8	11.1	7.0	13.4	13.3
EBITDA Margin (%)	26.6	27.7	27.7	28.8	29.8
Depreciation	1,565	1,592	1,880	2,080	2,280
EBIT	9,560	10,769	11,343	12,912	14,711
Other Income (Inc. EO Items)	270	682	492	736	953
Interest	-	25	96	101	105
PBT	9,830	11,426	11,739	13,547	15,559
Total Tax	3,097	3,670	2,955	3,410	3,916
RPAT	6,734	7,756	8,784	10,138	11,643
Adjustments	(83)	254	-	-	-
Adjusted PAT	6,816	7,502	8,784	10,138	11,643
APAT Growth (%)	18.0	10.1	17.1	15.4	14.9
Adjusted EPS (Rs)	25.0	27.6	32.3	37.2	42.8
EPS Growth (%)	18.0	10.1	17.1	15.4	14.9

Source: Company, HDFC sec Inst Research

Balance Sheet

(Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
SOURCES OF FUNDS					
Share Capital - Equity	272	272	272	272	272
Reserves	14,974	14,614	18,157	21,422	25,135
Total Shareholders' Funds	15,246	14,886	18,429	21,695	25,408
Long Term Debt	-	777	777	777	777
Short Term Debt	-	-	-	-	-
Total Debt	-	777	777	777	777
Net Deferred Taxes	355	309	309	309	309
Other Non-current Liabilities & Provns	209	201	201	201	201
TOTAL SOURCES OF FUNDS	15,811	16,172	19,715	22,981	26,694
APPLICATION OF FUNDS					
Net Block	11,460	11,909	12,029	11,949	11,670
CWIP	1,586	1,987	1,987	1,987	1,987
Other Non-current Assets	1,978	1,903	2,491	2,721	2,982
Total Non-current Assets	15,024	15,798	16,507	16,657	16,639
Inventories	2,267	2,486	2,657	2,900	3,177
Debtors	2,010	2,098	2,239	2,442	2,675
Other Current Assets	1,465	1,611	1,772	1,950	2,145
Cash & Equivalent	4,873	4,689	7,769	11,113	15,120
Total Current Assets	10,615	10,884	14,438	18,405	23,116
Creditors	6,145	6,132	6,539	7,024	7,585
Other Current Liabilities & Provns	3,683	4,378	4,691	5,057	5,476
Total Current Liabilities	9,828	10,510	11,230	12,081	13,061
Net Current Assets	788	374	3,208	6,324	10,055
TOTAL APPLICATION OF FUNDS	15,811	16,172	19,715	22,981	26,694

Source: Company, HDFC sec Inst Research

Cash Flow Statement

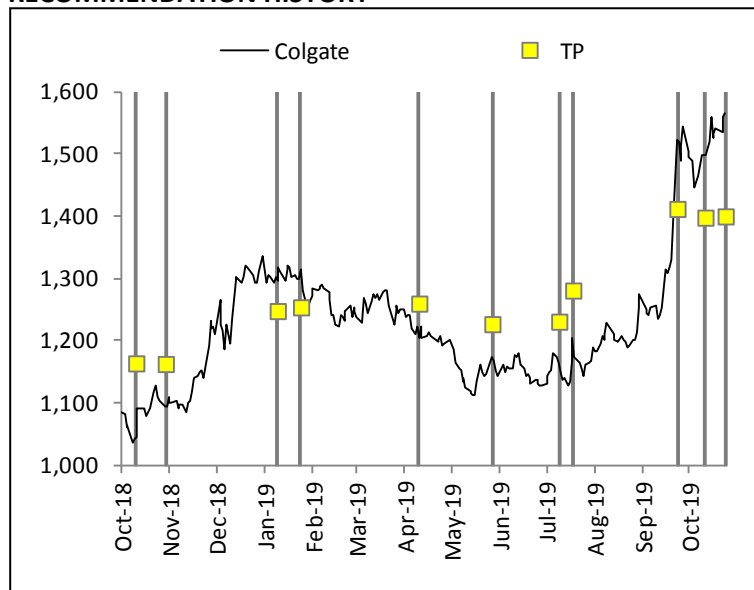
(Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
Reported PBT	9,947	11,426	11,739	13,547	15,559
Non-operating & EO Items	81	-	-	-	-
Interest Expenses	(290)	25	96	101	105
Depreciation	1,565	1,592	1,880	2,080	2,280
Working Capital Change	(889)	620	(207)	192	235
Tax Paid	(3,474)	(3,670)	(2,955)	(3,410)	(3,916)
OPERATING CASH FLOW (a)	6,939	9,992	10,553	12,510	14,263
Capex	(2,087)	(2,442)	(2,000)	(2,000)	(2,000)
Free Cash Flow (FCF)	4,852	7,550	8,553	10,510	12,263
Investments	(273)	-	-	-	-
Non-operating Income	287	(312)	(132)	(189)	(217)
INVESTING CASH FLOW (b)	(2,073)	(2,754)	(2,132)	(2,189)	(2,217)
Debt Issuance/(Repaid)	-	777	-	-	-
FCFE	4,866	8,016	8,421	10,320	12,046
Share Capital Issuance	-	-	-	-	-
Dividend	(3,705)	(7,862)	(5,241)	(6,872)	(7,930)
Others	(92)	(298)	(100)	(104)	(108)
FINANCING CASH FLOW (c)	(3,798)	(7,382)	(5,341)	(6,976)	(8,039)
NET CASH FLOW (a+b+c)	1,068	(144)	3,080	3,344	4,007
EO Items, Others	(550)	41	-	-	-
Closing Cash & Equivalents	4,562	4,377	7,457	10,801	14,808

Source: Company, HDFC sec Inst Research

Key Ratios

	FY18	FY19	FY20E	FY21E	FY22E
PROFITABILITY (%)					
GPM	64.4	65.1	66.3	66.5	66.9
EBITDA Margin	26.6	27.7	27.7	28.8	29.8
EBIT Margin	22.8	24.1	23.8	24.8	25.8
APAT Margin	16.3	16.8	18.4	19.5	20.5
RoE	48.7	49.8	52.7	50.5	49.4
RoIC (or Core RoCE)	64.4	67.2	74.4	83.3	96.5
RoCE	47.9	47.9	49.8	48.2	47.5
EFFICIENCY					
Tax Rate (%)	31.5	32.1	25.2	25.2	25.2
Fixed Asset Turnover (x)	2.1	2.0	2.0	2.0	2.0
Inventory (days)	19.8	20.3	20.4	20.4	20.4
Debtors (days)	17.5	17.2	17.2	17.2	17.2
Other Current Assets (days)	12.8	13.2	13.6	13.7	13.8
Payables (days)	53.6	50.1	50.1	49.3	48.6
Other Current Liab & Provns (days)	32.1	35.8	35.9	35.5	35.1
Cash Conversion Cycle (days)	(35.6)	(35.3)	(34.9)	(33.6)	(32.5)
Net D/E (x)	(0.3)	(0.3)	(0.4)	(0.5)	(0.6)
Interest Coverage (x)	na	na	na	na	na
PER SHARE DATA (Rs)					
EPS	25.0	27.6	32.3	37.2	42.8
CEPS	30.8	33.4	39.2	44.9	51.1
Dividend	24.0	16.0	21.0	24.2	27.8
Book Value	56.0	54.7	67.7	79.7	93.3
VALUATION					
P/E (x)	62.5	56.8	48.5	42.0	36.6
P/BV (x)	27.9	28.6	23.1	19.6	16.8
EV/EBITDA (x)	37.9	34.1	31.7	27.7	24.2
EV/Revenues (x)	10.1	9.5	8.8	8.0	7.2
OCF/EV (%)	1.6	2.4	2.5	3.0	3.5
FCF/EV (%)	1.2	1.7	2.0	2.5	2.9
FCFE/Mkt Cap (%)	1.1	1.9	2.0	2.4	2.8
Dividend Yield (%)	1.5	1.0	1.3	1.5	1.8

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY


Date	CMP	Reco	Target
10-Oct-18	1,050	NEU	1,164
29-Oct-18	1,102	NEU	1,163
9-Jan-19	1,311	NEU	1,248
24-Jan-19	1,322	NEU	1,254
10-Apr-19	1,231	NEU	1,260
28-May-19	1,180	NEU	1,227
9-Jul-19	1,164	NEU	1,231
18-Jul-19	1,203	NEU	1,281
22-Sep-19	1,397	NEU	1,412
11-Oct-19	1,497	NEU	1,398
25-Oct-19	1,565	NEU	1,400

Rating Definitions

- BUY** : Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

INSTITUTIONAL RESEARCH
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