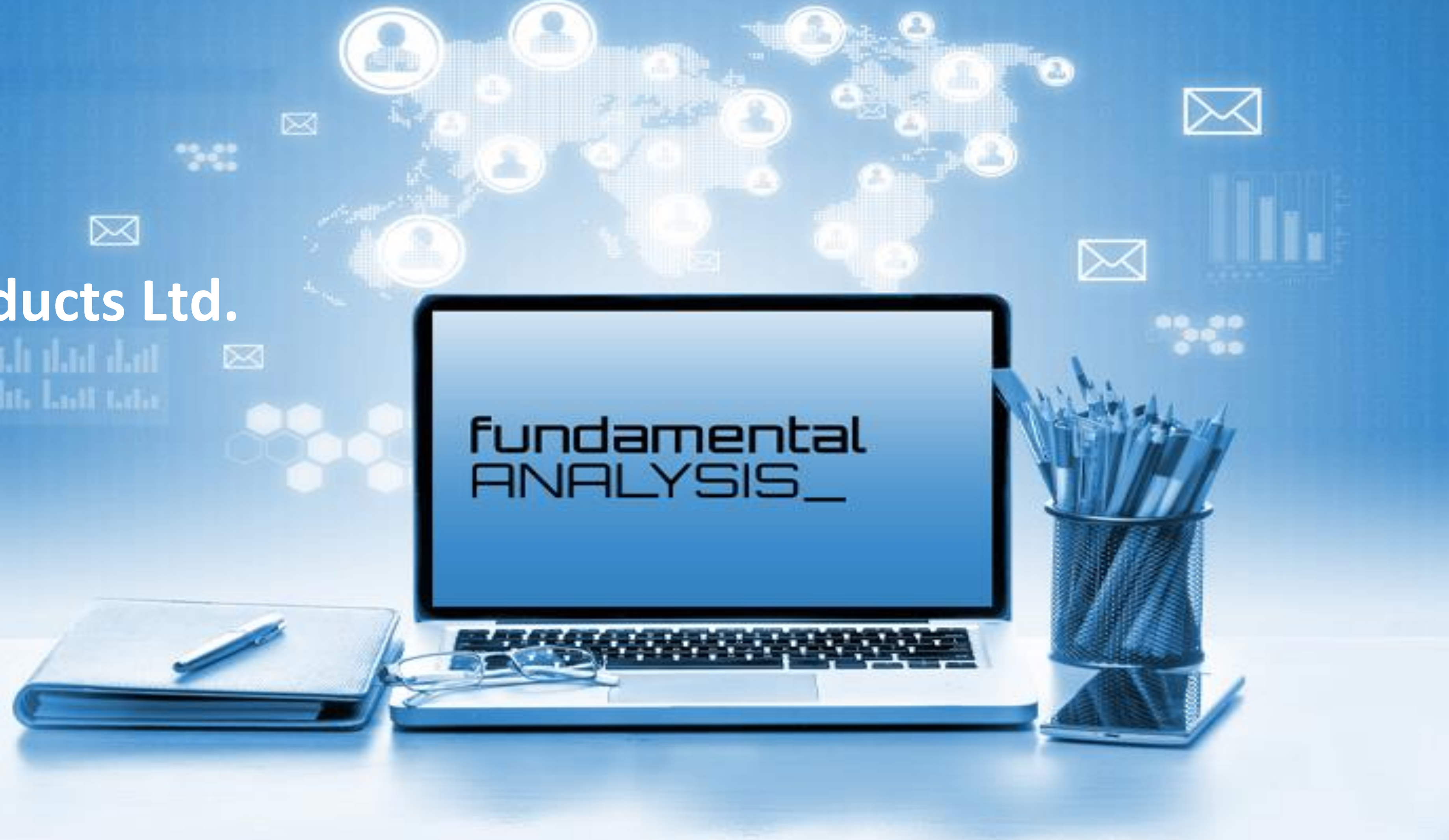
Stock Update

Godrej Consumer Products Ltd.

August 30, 2022



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Godrej Consumer Products Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
FMCG	Rs. 907.8	Buy in Rs 901-914 band and add more on dips in Rs 819-828 band	Rs. 985	Rs. 1065	2 quarters

HDFC Scrip Code	GODCON
BSE Code	532424
NSE Code	GODREJCP
Bloomberg	GCPL:IN
CMP – Aug 29, 2022	907.8
Equity Capital (Rs Cr)	102
Face Value (Rs)	1
Equity Share O/S (Cr)	102
Market Cap (Rs Cr)	92831
Book Value (Rs)	109
Avg. 52 Wk Volumes	1398169
52 Week High	1138.5
52 Week Low	660.2

Share holding Pattern % (Jun, 2022)	
Promoters	63.22
Institutions	30.08
Non Institutions	6.70
Total	100.0

* Refer at the end for explanation on Risk Ratings

Fundamental Research Analyst
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Our Take:

Godrej Consumer Products Ltd (GCPL) is a part of the 124-year-old Godrej Group; it was formed by the de-merger of the consumer products division of the erstwhile Godrej Soaps Ltd in April 2001. Although it was formed in its current form in 2001, it has been operating as Godrej Soaps for over 100 years, in the personal care segment. GCPL, today, has a strong presence in the FMCG industry—across three core categories - personal care, home care and hair care – with focus on three geographies - Asia, Africa and Latin America.

GCPL's inorganic expansion over the past decade plus in Asia, Africa, the US and Latin America has enabled it to enjoy a diversified revenue profile, with international operations driving ~44% of its consolidated revenue in FY22. This expansion has helped the company in extracting synergies in terms of product cross-pollination and stronger distribution network, besides being able to diversify its product portfolio and geographical reach. Also, at a consolidated level, in FY22, GCPL derived 41% of its revenue from the home care segment, 33% from hair care segment and 26% from personal care segment, reflective of a diversified segmental presence. Its brands such as Goodknight and Hit in home care, Godrej Expert in the hair colouring segment and Cinthol and Godrej No 1 in the personal care segment enjoy market leading positions in the domestic market. Similarly, in international markets, its brands Darling in the dry hair care segment in Africa and Mitu wet wipes and Stella air fresheners in Indonesia enjoy established market positions in their respective regions.

GCPL has a consistent track record of introducing new products to cater to shifting consumer preferences and we expect that, going forward, its revenue growth will be driven by stable demand growth and introduction of new products across geographies. Supported by its portfolio of strong brands, constant innovation, and brand repositioning, the company has managed to maintain its competitive position in these key product categories and geographies. It will continue to benefit from its established position in domestic and international FMCG markets.

Valuation & Recommendation:

After consecutive quarters of subdued performance with runaway RM inflation, demand slowdown and mounting troubles in Indonesia, turbulence seems to be stabilising. We believe, with the inflation pressure abating, a recovery in consumption and gross margin is expected. To our satisfaction, in terms of market shares, GCPL continues to gain share in most categories. Africa business is likely to improve on better growth prospects and strategic initiatives like simplifying business and improving governance while reducing pipeline inventory and media spends in Indonesia business to improve performance from Q3FY23 onwards. HI growth is likely to recover after the recent volatility with increasing penetration, marketing spends and category innovation; share gains should continue in soaps and other categories should see steady growth. New CEO, Mr. Sitapati has taken cognizance of strengths in its portfolio and revamped the company's strategy to undo mistakes made in the past. We believe the management's target of double-digit volume growth is achievable, given: a) increasing investments to drive penetration levels, b) rising marketing spends, and c) reduction in current complexity caused by a large portfolio. Palm oil and its derivatives prices, the key raw material in soaps (~25% of raw material costs) rose by 60% in FY22 and impacted the gross and operating margins. This was one of the main reasons for the 220 bps fall in OPM in FY22. Palm oil prices have fallen sharply between May 2022 and July 2022. This will lead to some recouping of margins from Q3FY23 onwards.

We think the base case fair value of the stock is Rs 985 (43x FY24E EPS) and the bull case fair value of is Rs 1065 (46.5x FY24E EPS). Investors can buy the stock in Rs 901-914 band (40x FY24E EPS) and add more on dips in Rs 819-828 (36 x FY24E EPS) band.

Financial Summary

Particulars (in Rs Cr)	Q1FY23	Q1FY22	YoY-%	Q4FY22	QoQ-%	FY20	FY21	FY22	FY23E	FY24E
Operating Income	3125	2895	8.0%	2916	7.2%	9,911	11,029	12,277	13,563	14,905
EBITDA	533	611	-12.8%	502	6.0%	2,143	2,388	2,395	2,660	3,144
APAT	364	415	-12.4%	307	18.3%	1,473	1,715	1,702	1,975	2,341
Diluted EPS (Rs)	3.6	4.1	-12.4%	3.0	18.3%	14.4	16.8	16.6	19.3	22.9
RoE-%						19.4	19.8	16.5	16.4	16.9
P/E (x)						63.0	54.1	54.6	47.9	40.4
EV/EBITDA						44.3	43.6	38.8	38.4	34.6

	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23
Revenue (in Rs Cr)													
India	1,315	1,521	1,524	1,114	1,381	1,679	1,695	1,500	1,661	1,838	1,817	1,635	1,849
Indonesia	372	426	448	449	406	446	447	471	411	445	447	402	377
Africa	562	591	679	484	437	652	779	630	694	749	884	723	779
Others	131	128	161	136	127	181	180	179	160	174	200	212	154
Revenue Mix													
India	56%	58%	55%	52%	59%	58%	55%	55%	57%	58%	55%	56%	59%
Indonesia	16%	16%	16%	21%	17%	15%	15%	17%	14%	14%	14%	14%	12%
Africa	24%	22%	24%	22%	19%	22%	25%	23%	24%	24%	27%	25%	25%
Others	6%	5%	6%	6%	5%	6%	6%	7%	6%	5%	6%	7%	5%
Segmental EBIT (in Rs Cr)													
India	307.3	401.6	442.6	306.1	378.2	465.3	462.9	327.7	427.1	448.5	454.3	382.2	410.1
Indonesia	87.7	105.7	112.4	154.4	98.4	110.1	108.4	164.1	93	114.8	91.9	85.4	57.6
Africa	46.6	50.4	60	12.2	-29.4	41.5	72.4	22	32.4	46.2	73.2	-46.1	24.6

Others	-1.7	3.7	0.7	6.2	12.8	33	21.1	4.7	21.4	27.7	21	19.1	2.5
Segmental EBIT - %													
India	23.40%	26.40%	29.00%	27.50%	27.40%	27.70%	27.30%	21.90%	25.70%	24.40%	25.00%	23.40%	22.20%
Indonesia	23.60%	24.80%	25.10%	34.40%	24.20%	24.70%	24.20%	34.80%	22.60%	25.80%	20.50%	21.30%	15.30%
Africa	8.30%	8.50%	8.80%	2.50%	-6.70%	6.40%	9.30%	3.50%	4.70%	6.20%	8.30%	-6.40%	3.20%
Others	-1.30%	2.90%	0.40%	4.50%	10.10%	18.20%	11.70%	2.60%	13.40%	15.90%	10.50%	9.00%	1.60%

(Source: Company, HDFC sec)

Q1FY23 Result Update

GCPL's revenue growth and EBITDA margin were broadly in line with expectations. Consolidated revenue grew 8% YoY, domestic/international clocked 12/3% YoY growth, with 12/7% three-year CAGR. India business continued to be led by a high share of price hike (18% YoY), with domestic volume declining 6%. Indonesia sales declined by 9% in INR and 12% in constant currency terms, year-on-year; 3-year CAGR -2% in constant currency. Africa, USA and Middle East sales grew by 12% in INR terms, year-on-year; 3-year CAGR 11% in constant currency. Latin America & SAARC sales declined by 5% in INR and grew 15% in constant currency terms, year-on-year; 3-year CAGR 28% in constant currency.

Gross margin contracted by 558bps YoY to 46.6%. Employee costs were down by 11% YoY (+11% in Q1FY22), A&P was up 37% YoY (+41% in Q1FY22), and other expenses were flat YoY (+9% in Q1FY22). EBITDA margin fell 407bps YoY (+80bps Q1FY22, -382bps Q4FY22) to 17%. EBITDA declined by 13% YoY. EBITDA margin for Indonesia/GUAM/Latin America & SAARC came in at 15.3/8.3/1.4% vs. 23.4/9.9/13.6% in Q1FY22.

Home Care: It declined by 4% with a 2-year CAGR of 8%. It delivered a soft performance in Household Insecticides, on the back of a high base and relatively muted season, however, it continued to deepen penetration and gain market share on MAT basis. It is seeding in category development initiatives to drive sustainable growth. GCPL launched a new campaign for Goodknight liquid vaporizer #NeendoKoNazarNaLage and for HIT.

The non-mosquito portfolio continues to deliver strong growth momentum. Air Fresheners witnessed strong performance, led by an uptick in the category. The category development initiative around driving relevance for Aer Power Pocket and premiumisation through Aer Matic ('If bathrooms/rooms could talk') is receiving encouraging consumer response, according to the management.

Personal Wash & Hygiene maintained its growth momentum as it grew by 25% with a 2-year CAGR of 21%. GCPL is strengthening its value-for-money and green proposition with the launch of the affordable and sustainable ready-to-mix Magic Bodywash priced at Rs 45.
Hair Colour witnessed strong growth driven by category uptick with a 2-year CAGR in double digits. Godrej Expert Rich Crème continues to perform well and gain market share, backed by strong marketing campaigns.

Indonesia business continues to bleed - Indonesia business delivered a weak performance with a sales decline of 12% in constant currency terms. Sales excluding Hygiene (Saniter) saw a decline of 4% in constant currency terms. GCPL continued to focus on reducing stocks with channel partners, resulting in nearly flattish growth on sell-outs. EBITDA margins, contracted by 810 bps year-on-year due to higher commodity inflation, upfront marketing investments, high hygiene comparator, and scale deleverage.

Africa's recovery is heartening - Africa, USA and Middle East cluster delivered double-digit sales growth of 12% in constant currency terms (3-year CAGR of 11%) with strong sales growth momentum in Southern Africa. Dry Hair category grew in mid-single digit, while the FMCG category grew in double digits. While EBITDA margins decreased by 160 bps year-on-year, GCPL continued to introduce marketing initiatives to drive sustainable growth and have increased investments across both Dry Hair and FMCG categories.

Key highlights from FY22 Annual Report

Extending leadership in its core categories and geographies

Particulars	India	Indonesia	Africa	LATAM
Household Insecticides	no. 1 in HI	no. 1 in HI		
Personal Wash	no. 2 in Soaps	no. 2 in Personal Wash		
Hair Care	no. 1 in Hair Colour		no. 1 in Ethnic Hair Colour no. 1 in Hair Extensions no. 3 in Caucasian Hair Colour	no. 1 in Hair Colour and Hair Styling Products (Argentina) no. 1 in Depilatory Products (Chile) no. 2 . in Har Colour (Chile)
Others	no. 2 in Air Fresheners no. 2 in Liquid Detergents	no. 1 in Air Fresheners no. 1 in Wet Wipes		

Renewed philosophy to drive the growth

Innovation has been a key strategy of growth for GCPL with new launches driving revenue growth over the past five years. After an intense period of innovation in FY21, characterised by the pandemic GCPL undertook a strategic reset of product innovation and new brand development activities. Leveraging its RIDE (R&D + Innovation + Design + Expertise) structure it intends to drive innovation by adopting following key principles:

- A 'less is more' approach: fewer, bigger, better innovations
- Even more consumer-centric: deeper insights, prioritising the voice of our consumers in decision-making
- 100% objectivity: rigorous stage-gate process, right governance
- Become truly global: efficiently delivering synergies

- Sustainability

While new brand development will continue to be an important capability and driver of value, GCPL aims to discontinue with smaller brands where it makes sense from a better parentage/value realisation perspective.

Likewise, GCPL has opted for the cross-pollination exercise to take products from one country to another and apply its learnings. Going forward, we expect both these strategies to drive value growth for the company.

Expanding penetration and reach

India: It aims to expand its total reach in India from 6 mn outlets in FY21 to 7 mn outlets in the next 2 years. It is particularly, focused on driving rural reach and penetration by launching lower priced stock-keeping units in our key categories. In the past year, it created a blueprint of the ideal rural coverage along with its external partner which helped to increase its rural sub-stockist network by 5%. Further, it experimented with moving the frontline salesforce to third-party payroll, which has resulted in improved productivity and reduced attrition. Tapping into the emerging opportunity of a growing chemist channel, it created a strong distributor network of pharma/over-the-counter drugs distributors.

Bangladesh: It is expanding its direct reach to 1,00,000 outlets and driving salesforce automation through handheld devices for salespeople.

In Indonesia, it has significantly accelerated its go-to-market transformation. Direct distribution, through active registered outlets, continued to grow strongly to reach nearly 1,75,000 outlets.

Africa: It is ramping up its go-to-market efforts across Africa. In Nigeria, where trade is largely unorganised and wholesale-led, it is scaling up last-mile distribution through van models, sub-distributor models, and salon advocacy. Its experiment of launching a D2C channel is faring well. It desires to continue the momentum in Nigeria and strengthen fundamentals at an accelerated pace in South Africa and Kenya to unlock the full potential over the next few years.

USA: Alongside Walmart, it has now expanded into other retail partnerships such as Target.

Ramping up e-commerce

In India, it is investing in ramping up capabilities in the e-commerce function with objective to improve margins in the e-commerce channel through a better mix and optimisation of operational efficiencies

Indonesia – It has significantly scaled up its efforts and investments with a focus on winning platforms backed by strong joint business partnering, new product launches, strong cataloguing and store management, and a step jump in leveraging analytic.

USA – Its efforts to strengthen e-commerce fundamentals paid off with the business growing strongly to become nearly 4% of overall US business this year.

Africa - E-commerce in Africa has significant headroom for growth, particularly in the fashion and beauty segments. Given limited resident traffic on the third-party platforms, in Africa (unlike in India, Indonesia, and the USA), GCPL has launched its own D2C platform in Nigeria.

Palm oil prices on a downtrend

Palm oil and its derivatives prices, the key raw material in soaps (~25% of raw material costs) rose by 60% in FY22 and impacted the gross and operating margins. This was one of the main reasons for the 220 bps fall in OPM in FY22. Palm oil prices have fallen sharply between May 2022 and July 2022. This will lead to some recouping of margins from Q3FY23 onwards. This will help GCPL to try to reach/surpass FY22 margins in FY23E and spend some of the savings into media investments for brand building.

Key risks

Competition risk can arise in the form of product pricing strategy, aggressive pricing by competitors, entry of new players, emergence of e-com/digital first brands and dependency on a few product categories to drive sales. The likely disruption in the grocery retail market and the growth of the hyper-local formats of Reliance Retail and the new e-commerce hypermarkets pose a risk to the industry dynamics in the medium term.

The company faces currency risk as it has over 40% of its revenue from foreign operations and has a presence in five continents. Currency fluctuations in its key international markets, including Africa and Indonesia, will affect its earnings performance.

Economic risk exists in the territories GCPL operates in. Extended lockdowns in geographies such as Indonesia and sub-Saharan Africa due to the COVID-19 spread also pose a risk. Also, if employment opportunities don’t improve soon, demand for some of GCPL’s products might be impacted negatively.

Commodity risk exists as volatility in commodity prices (like palm oil, crude oil derivatives etc.) can impact GCPL's revenue and margins.

Business slowdown risk exists. GCPL saw muted sales, EBITDA and PAT growth in FY18-20 due to a combination of factors (including consumer spending slowdown/downtrading in various geographies, volatility in raw material prices, geopolitical issues in some countries, nil growth/degrowth in insecticides business for some quarters, heightened competition in some categories, etc.) and, hence, its stock price underperformed. Any resurgence of such a slow-growth scenario could hurt its growth, going forward.

Foreign markets risk: The Africa business has been a big pain point for the past few years. GCPL has hired the ex-CEO of Nestle Nigeria as the new head of Africa business. The new regional CEO is well versed with the region for decades and the management expects him to lead a strong turnaround there. Recently, GCPL has seen a sequential improvement in performance.

Structural fall in demand for HI in India could be a risk for the company

About the Company

Godrej Consumer Products Ltd (GCPL) is a part of the 124-year-old Godrej Group. The group enjoys a patronage of 1.15 billion consumers globally. GCPL is present in emerging markets of Asia, Africa and Latin America and the company's product portfolio ranges from home care and personal care to hair care, household insecticides, hair colour, soaps, air fresheners, liquid detergents, hair extensions, personal wash, styling in mass and professional markets, skin care, sanitizers, sun care and female deodorants. GCPL is ranked among the largest household insecticide and hair care players in the emerging markets. In household insecticides, GCPL is the leader in India and Indonesia and is expanding its footprint in Africa. GCPL is also the leader in serving the hair care needs of women of African descent and is the number one player in hair colour products in India and sub-Saharan Africa, and among the leading players in Latin America. It ranks No. 2 in soap products in India, first in air freshener products in India and Indonesia, and is the leader in wet tissue products in Indonesia.

Financials

Income Statement

Particulars (in Rs Cr)	FY20	FY21	FY22	FY23E	FY24E
Net Revenues	**9911**	**11029**	**12277**	**13563**	**14905**
Growth (%)	***-3.9***	***11.3***	***11.3***	***10.5***	***9.9***
Operating Expenses	7768	8640	9881	10903	11761
EBITDA	**2143**	**2388**	**2395**	**2660**	**3144**
Growth (%)	***1.2***	***11.4***	***0.3***	***11.1***	***18.2***
EBITDA Margin (%)	***21.6***	***21.7***	***19.5***	***19.6***	***21.1***
Depreciation	197	204	210	227	245
Other Income	112	67	90	103	133
EBIT	**2058**	**2251**	**2275**	**2536**	**3032**
Interest expenses	217	127	110	108	69
PBT	**1760**	**2080**	**2155**	**2415**	**2963**
Tax	264	360	372	459	622
PAT	**1497**	**1721**	**1783**	**1956**	**2341**
Share of Asso./Minority Int.	0	0	0	0	0
Adj. PAT	**1473**	**1715**	**1702**	**1975**	**2341**
Growth (%)	***0.5***	***16.5***	***-0.8***	***16.0***	***18.6***
EPS	14.4	16.8	16.6	19.3	22.9

Balance Sheet

Particulars (in Rs Cr) - As at March	FY20	FY21	FY22	FY23E	FY24E
SOURCE OF FUNDS					
Share Capital	102	102	102	102	102
Reserves	7796	9337	11038	12809	14741
Shareholders' Funds	**7898**	**9439**	**11141**	**12911**	**14843**
Minority Interest	0	0	0	0	0
Total Debt	2664	1768	1608	958	378
Net Deferred Taxes	-570	-638	-680	-680	-680
Others	290	189	174	174	174
Total Sources of Funds	**10282**	**10759**	**12242**	**13363**	**14715**
APPLICATION OF FUNDS					
Net Block & Goodwill	3893	3779	3844	4117	4173
CWIP	213	171	380	430	480
Other Non-Curr. Assets	213	171	380	430	480
Total Non Current Assets	**5339**	**5130**	**5377**	**5377**	**5377**
Inventories	1703	1716	2130	2192	2409
Debtors	1157	1005	1116	1263	1388
Cash & Equivalents	1407	1329	1537	2361	3512
Other Current Assets	541	422	489	540	594
Total Current Assets	**4808**	**4472**	**5272**	**6357**	**7904**
Creditors	2480	2012	2163	2390	2626
Other Current Liab & Provisions	1547	835	582	643	706
Total Current Liabilities	**4028**	**2847**	**2745**	**3032**	**3333**
Net Current Assets	780	1625	2527	3324	4571
Total Application of Funds	**10282**	**10759**	**12242**	**13363**	**14715**

Godrej Consumer Products Ltd.

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Cash Flow Statement

Particulars (in Rs Cr)	FY20	FY21	FY22	FY23E	FY24E
Reported PBT	1,841	2,080	2,155	2,415	2,963
Non-operating & EO items	-50	61	-35	-38	-66
Interest Expenses	217	127	110	108	69
Depreciation	197	204	210	227	245
Working Capital Change	-261	-45	-695	27	-95
Tax Paid	-344	-397	-372	-459	-622
OPERATING CASH FLOW (a)	**1,601**	**2,030**	**1,373**	**2,280**	**2,493**
Capex	-152	-164	-564	-500	-300
Free Cash Flow	1,449	1,866	809	1,780	2,193
Investments	-438	-211	-313	-198	-184
Non-operating income	57	59	-111	0	0
INVESTING CASH FLOW (b)	**-533**	**-316**	**-989**	**-698**	**-484**
Debt Issuance / (Repaid)	-128	-1,619	-161	-650	-580
Interest Expenses	-152	-159	-110	-108	-69
FCFE	1,169	88	538	1,022	1,543
Share Capital Issuance	0	0	0	0	0
Dividend	-986	0	0	-205	-409
Others	-30	0	0	0	0
FINANCING CASH FLOW (c)	**-1,295**	**-1,778**	**-271**	**-963**	**-1,058**
NET CASH FLOW (a+b+c)	**-228**	**-64**	**114**	**619**	**951**

One-Year Share Price Chart

Key Ratios

Particulars	FY20	FY21	FY22	FY23E	FY24E
Profitability Ratios (%)					
EBITDA Margin	21.6	21.7	19.5	19.6	21.1
EBIT Margin	20.8	20.4	18.5	18.7	20.3
APAT Margin	14.9	15.6	13.9	14.6	15.7
RoE	19.4	19.8	16.5	16.4	16.9
RoCE	15.5	16.4	14.7	15.3	16.3
Solvency Ratio (x)					
Net Debt/EBITDA	0.0	0.0	0.0	0.0	0.0
Net D/E	0.2	0.0	0.0	-0.1	-0.2
PER SHARE DATA (Rs)					
EPS	14.4	16.8	16.6	19.3	22.9
CEPS	16.3	18.8	18.7	21.5	25.3
Dividend	6.0	0.0	0.0	2.0	4.0
Book Value	77.3	92.3	108.9	126.3	145.1
Turnover Ratios (days)					
Debtor days	43	33	33	34	34
Inventory days	60	57	57	59	59
Creditors days	91	67	64	64	64
VALUATION					
P/E	63.0	54.1	54.6	47.9	40.4
P/BV	11.7	9.8	8.3	7.3	6.4
EV/EBITDA	44.3	43.6	38.8	38.4	34.6
EV / Revenues	9.4	8.4	7.5	6.8	6.1
Dividend Yield (%)	0.7	0.0	0.0	0.2	0.4

Source: Company, HDFC sec

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HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

Disclosure:

I, **Harsh Sheth**, Research Analyst, **MCom**, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. SEBI conducted the inspection and based on their observations have issued advise/warning. The said observations have been complied with. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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